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ENHANCED CONSUMER FINANCIAL PROTECTION AFTER THE FINANCIAL CRISIS

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED TWELFTH CONGRESS

FIRST SESSION

ON

EXAMINING THE IMPACT OF THE FINANCIAL CRISIS ON CONSUMERS AND HOW THE DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT OF 2010 WILL ENHANCE CONSUMER FINANCIAL PROTECTION

JULY 19, 2011

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C O N T E N T S

TUESDAY, JULY 19, 2011

	Page
Opening statement of Chairman Johnson	1
Opening statements, comments, or prepared statements of:	
Senator Shelby	2
Senator Moran	3

WITNESSES

Michael D. Calhoun, President, Center for Responsible Lending	4
Prepared statement	38
Response to written question of:	
Senator Reed	
Marcus Schaefer, President and Chief Executive Officer, Truliant Federal Credit Union	6
Prepared statement	61
Albert C. Kelly, Jr., Chairman and Chief Executive Officer, SpiritBank, on behalf of the American Bankers Association	8
Prepared statement	62
Lynn Drysdale, Managing Attorney, Consumer Unit, Jacksonville Area Legal Aid, Inc.	9
Prepared statement	67
Andrew J. Pincus, on behalf of the U.S. Chamber of Commerce	11
Prepared statement	73
Adam J. Levitin, Professor of Law, Georgetown University Law Center	13
Prepared statement	102

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

AARP statement for the record	120

ENHANCED CONSUMER FINANCIAL PROTECTION AFTER THE FINANCIAL CRISIS

TUESDAY, JULY 19, 2011

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10:03 a.m. in room SD–538, Dirksen Senate Office Building, Hon. Tim Johnson, Chairman of the Committee, presiding.

OPENING STATEMENT OF CHAIRMAN TIM JOHNSON

Chairman JOHNSON. Good morning. I would like to call this hearing to order. Today the Committee will examine enhanced consumer financial protection after the Financial crisis.

As we approach the 1-year anniversary of the Wall Street Reform and Consumer Protection Act, we should all be reminded of a basic lesson we learned from the Great Recession: failing to protect consumers has consequences not only for individuals and families, but also for the health of America's economy.

The failure by regulators to hold Wall Street banks and unscrupulous mortgage lenders accountable for complying with consumer protection laws was detrimental to American families and brought the global financial system to near collapse.

The cost of that failed oversight and accountability has been the loss of millions of American jobs, millions of homes, and trillions of dollars in retirement, college, and other savings.

In numerous hearings in recent years, the Committee documented these failures by big banks and predatory subprime lenders to comply with consumer protection laws and the failure of banking regulators to hold them accountable.

Passed in the wake of that thorough review with a bipartisan vote, the Wall Street Reform and Consumer Protection Act created a robust, independent consumer financial protection regulator.

Congress established the Consumer Financial Protection Bureau to be the first financial regulator solely focused on consumer protection, but with more checks on its authority than the regulatory agencies that fell asleep at the switch.

It is important to remember that most of the checks and balances imposed on this new regulator come from bipartisan ideas that were incorporated into the reform law during the months it was considered, and that the CFPB is modeled on the structure of existing financial services regulators.

Putting partisanship aside, all of us here have a deep concern for American consumers, and we all believe that the small-community institutions that had no hand in the abusive practices that led to our financial crisis should not pay a price for being honest brokers.

The CFPB will help by promoting an equitable and transparent marketplace and leveling the playing field between those responsible actors and the unregulated companies that preyed unchecked on consumers.

That is why undermining this cornerstone of the Wall Street Reform law would be irresponsible. It would also ignore our responsibility to America's consumers and risk taking us back to the same unstable financial system that ushered in the Great Recession.

Thank you, and I look forward to working with all of you on these important issues.

Now I turn to Ranking Member Shelby.

STATEMENT OF SENATOR RICHARD C. SHELBY

Senator SHELBY. Thank you, Mr. Chairman.

Today's hearing provides the Committee a timely opportunity to examine one of the most serious flaws in the Dodd-Frank Act, namely, the governance structure of the new Bureau of Consumer Financial Protection. The issue is whether the Bureau is sufficiently accountable to the American people. I and 43 of my colleagues believe that it is not.

There is a broad, bipartisan support for improving consumer protection. There has never been any disagreement on that point that I know of. There is a disagreement, however, over the appropriate means by which we should make those improvements.

The approach taken by the Dodd-Frank Act was to create a huge new and entirely unaccountable bureaucracy. This is a typical response by Washington to any crisis. What is new, however, is the unprecedented amount of autonomy the bureaucracy will have. We will hear testimony today on what can only be described as the unfettered power of the Director. Unlike every other financial regulator, the Director of the Bureau essentially answers to no one. This concentration of power violates our Nation's basic democratic principles.

Our National Government was carefully crafted to defuse authority and prevent one person from exercising power arbitrarily. In contrast, the Dodd-Frank Act builds a wall around the Bureau with the express purpose of eliminating any real checks on the Director's authority.

Supporters of Dodd-Frank said that they wanted to make the Bureau independent. What they did was make the Bureau unaccountable. They argued that the Bureau needed to be protected from political pressures, yet by making the Bureau completely autonomous, they removed any avenues for meaning congressional oversight.

What makes the lack of accountability of the Bureau so troubling is that Congress, for all intents and purposes, delegated its own legislative power by giving the Bureau an enormous amount of policymaking and rule-writing authority. At the same time it also insulated it from the very body that created it and gave it its mandate. This was a mistake, I believe, and it needs to be corrected.

After nearly 1 year, the President has finally nominated someone to be the Director of the new bureaucracy. The Chairman has announced his intent to move quickly on this nomination. But given the fundamental flaws with the existing structure of the Bureau, the Senate, I believe, should not confirm any person to lead the Bureau until some responsible reforms are adopted.

Those who are advocating for more accountability have been accused of trying to gut, cripple, or de-fang the Bureau. I believe it is important to note, however, that we have not and are not proposing—this is very important—not proposing any changes to the Bureau's authority. We are proposing changes to the Bureau's structure so that it will be more accountable to the American people.

The creation of the Bureau was largely a partisan effort. We now have an opportunity to make some changes with strong bipartisan support. We all agree that consumer protection, as the Chairman mentioned, needs to be improved. We should also be able to agree that the structure of our financial regulators should comport with our democratic values.

I see no reason why we cannot work together to make the Bureau a strong consumer advocate as well as a fully accountable governmental agency itself.

Thank you, Mr. Chairman.

Chairman JOHNSON. Are there any other Members who would like to give opening statements? Senator Moran.

STATEMENT OF SENATOR JERRY MORAN

Senator MORAN. Mr. Chairman, thank you very much.

Almost a year to the day after the President signed the Dodd-Frank bill into law, the President has finally nominated an individual, Richard Cordray, to head the Consumer Financial Protection Bureau. It is unclear to me why the centerpiece of the President's financial reform package has taken so long to materialize, but what is clear is that the nomination is dead on arrival because it does nothing to increase accountability or shed light on the operations of the CFPB.

Two months ago, as Senator Shelby indicated, I, along with 43 of my Senate colleagues, called for the Bureau's leadership structure to be strengthened prior to consideration of any nominee. We asked for three specific changes in our May 5th letter to the President: a board or commission to replace the single director, the Bureau to be funded through the appropriations process, and additional input by prudential regulators into the rulemaking and operation of the CFPB.

I have introduced legislation to implement these three reforms. President Obama himself agreed with each of these three principles when he sent his original proposal to Congress back in 2009. Yet our request to return to these same principles is now being categorized as an attempt to kill the Bureau in its infancy.

The rhetoric may grab headlines, but it ignores the basic fact. What we are asking for is not radical. Transparency and accountability are our goals—goals that should be shared by every policymaker interested in protecting consumers from abuses of the past. Ask Chairman Schapiro of the SEC if a Commission has weakened her agency, or ask Chairman Gensler of the CFTC the same question. While seeking consensus among fellow regulators may not always be easy, that consensus will lead to a better public policy.

Even with these basic reforms to the structure of the agency, the CFPB will remain an incredibly powerful Government bureaucracy. Nothing I have proposed would undermine those authorities or responsibilities. But without additional accountability, the result of a poorly drafted rule could lead to less credit and less opportunity for consumers and small business alike.

I look forward today to answers from these witnesses about how consumer protection and small business access to credit will intersect, and I welcome the testimony of our witnesses here today. And thank you, Mr. Chairman.

Chairman JOHNSON. Before we begin, I would like to briefly introduce the witnesses that are here with us today.

Our first witness is Mr. Michael Calhoun. Mr. Calhoun is President of the Center for Responsible Lending, a nonprofit, nonpartisan consumer research and product organization.

Mr. Marcus Schaefer is the President and CEO of Truliant Federal Credit Union, a $1.1 billion credit union located in North Carolina, with the mission of improving the financial lives of its members.

Mr. Albert C. Kelly, Jr., is the Chairman and CEO of SpiritBank based out of Oklahoma. Mr. Kelly is also the chairman-elect of the American Bankers Association.

Ms. Lynn Drysdale is an attorney with Jacksonville Area Legal Aid in Florida, representing consumers, including servicemembers who have been harmed by financial institutions.

Mr. Andrew Pincus is a partner at the law firm of Mayer Brown LLP in Washington, D.C., representing the U.S. Chamber of Commerce.

And Professor Adam Levitin is from the Georgetown University Law Center. Professor Levitin specializes in bankruptcy, commercial law, and financial regulation.

We welcome all of you here today and thank you for your time. Mr. Calhoun, you may proceed.

STATEMENT OF MICHAEL D. CALHOUN, PRESIDENT, CENTER FOR RESPONSIBLE LENDING

Mr. CALHOUN. Thank you, Chairman Johnson, Ranking Member Shelby, and Members of the Committee.

The Center for Responsible Lending works to help families achieve and maintain financial success. We are an affiliate of Self-Help, the Nation's largest community development lender, which has provided home financing to more than 64,000 families along with charter school financing, small business loans, and other community development financing.

As we approach this anniversary of the Wall Street Reform Act, it is important to remember how we came to this point. Borrowers were placed in loans they had no reasonable chance to repay. One of those borrowers came to us, a retiree on Social Security benefits. He was placed in a loan with a deep teaser rate. After the loan readjusted, the required payments exceeded his entire take-home income. Notably, the mortgage broker and the lender received large bonuses for originating this loan. Unfortunately, that loan was all too typical.

Wall Street in turn stoked the demand for these loans and created so much demand for the loans that they had to create synthetic securities because there were not enough loans to satisfy the demand for securities backed directly by these loans. This further leveraging of the loans plunged the country into crisis when the securities collapsed due to the weakness of the underlying loans.

Importantly, when you compare the experience of the U.S. to other countries, no other country had such poor-quality mortgages. Other countries experienced similar reductions in home values, but because their loans were more sustainable, they incurred much less harm than the U.S. economy.

Another lesson from the crisis was that a single company or group of companies cannot stop predatory practices. Indeed, some tried in the mortgage boom by not offering unsustainable products and by refusing to pay these bonuses that brokers were demanding for putting people into these risky loans. The result was those companies found their market share quickly evaporated, as the loans were steered to other companies who played by different rules. Ultimately, most of the companies joined in these unsustainable practices.

The need for the Consumer Bureau remains critical as we approach the transfer date. Mortgage-servicing abuses have been permitted to become epidemic as financial regulators failed to exercise the necessary oversight. In addition, CRL is releasing a study this week showing that banking consultants have been peddling 350 percent interest loans for programs to be offered out of our biggest banks out of their own offices. The regulators, instead of keeping our flagship institutions out of this modern-day loan sharking, have let it spread to some of the largest national banks in our country, leaving struggling families trapped in a cycle of high-cost debt.

There are proposals to restructure the CFPB before it opens its doors. As set out in detail in our testimony, there are many safeguards already in place. Certainly there must be care, certainly with small businesses and small financial institutions to consider the impact and burdens on those companies. However, already hard-wired into existing law is the requirement that the CFPB consult with and give notice to small companies before they can even issue a proposed rule, a requirement unique among financial regulators.

Finally, the American people know how badly the CFPB is needed. CRL, along with AARP and Americans for Financial Reform, commissioned a poll this month asking about opinions regarding the consumer agency. The poll showed that members of all parties overwhelmingly support a strong consumer agency and oppose efforts to repeal it. They also reject the argument that fair lending is bad for the economy.

In summary, America is still recovering from the devastation caused by the flood of unsustainable lending. Yet, to date, basic financial transactions for the average family remain unfathomable. Anyone who tries to read a mortgage loan agreement or even a credit card agreement has had that experience. And there is an absence of basic ground rules. Those deficiencies hamper the operation of our free markets and put our economy at risk. The CFPB is needed now to both help American families individually achieve and maintain financial stability, but also to restore our overall economic health. It should be allowed to begin this overdue work.

Thank you, and I look forward to answering your questions.

Chairman JOHNSON. Thank you, Mr. Calhoun.

Mr. Schaefer, you may proceed.

STATEMENT OF MARCUS SCHAEFER, PRESIDENT AND CHIEF EXECUTIVE OFFICER, TRULIANT FEDERAL CREDIT UNION

Mr. SCHAEFER. Truliant Federal Credit Union appreciates the opportunity to provide input into the public policy dialog regarding the enhancement of consumer protection. We would like to thank Chairman Johnson, Ranking Member Shelby, Senator Hagan, and Members of the Committee for having us here today.

Our mission is to enhance the quality of life of our members and to become their preferred financial institution. Truliant offers a full range of financial services, including savings, checking, certificates, money markets, IRAs, and rainy-day savings. Loan services include first mortgage and home equity, new and used auto, personal lines, and Visa credit cards. We offer small business services including member business and SBA loans. We provide state-of-the-art home banking and electronic bill payment programs, mobile access, and remote deposit capture. Through our Credit Union Service Organization, we offer financial planning and a very popular auto-buying service.

As a member-owned financial institution, we can offer lower loan rates, higher savings rates, low (and often no) fees as we help members execute financial plans for their future. Central to all our services is our emphasis on financial literacy education and counseling to our members and for our communities. Over 55 percent of our member households earn less than $45,000 per annum. Affordable, well-informed financial service access and delivery is key to our mission.

Truliant maintains an overarching commitment to improve our members' lives by understanding and meeting their financial needs. This focus translates into our TruService culture. Our staff engages our members to bring about real change and help them meet their long-term objectives rather than the traditional product-pushing sales approach so prevalent in modern banking. For example, a benefit of low interest rates has allowed us to reposition hundreds of members into lower-cost mortgages and car loans.

Our operating principle is, "Consumer, Be Aware," not "Consumer Beware." Well before the financial crisis, we instituted our Points of Differentiation that embody the spirit and practice of improving member financial lives. We have not sold our credit card accounts to the large credit card issuers. We never offered an opt-out courtesy pay overdraft protection program. We do not advertise a car loan rate to members unless the majority has the credit quality to qualify. We do not allow indirect auto loan car dealers to mark up our rate. We help our member-owners become debt free on their primary home by the time of retirement. We support public policy that informs and educates the consumer on financial decisions while improving personal balance sheets.

Our experience is that consumers have been needlessly financially disadvantaged by a history of questionable practices and procedures by both mainstream and non-bank providers. Examples include opt-out overdraft protection, the sequence of clearing checking debits, extending credit to borrowers with terms they could not reasonably meet, overly complex disclosure materials, and punitive credit card practices.

These seem to be acceptable "gotchas" rather than consumer-focused services and argue for some balance toward better information sharing. Congress has addressed some of these more egregious practices, and heightened consumer awareness post-financial crisis may have driven providers to become more consumer-friendly in the near term.

Even with reforms like the CARD Act, Regulation E rule changes, and the consumer protection initiatives of individual regulators, it make sense to have a regulator focused on consumer protection.

Clearly, controlling practices of non-bank providers, such as unregulated mortgage brokers, who in some cases were able to lure our members into products that did not improve their financial lives, is needed. We noted 13 finance companies operating in the small manufacturing town of Asheboro, North Carolina, leading to our extending services there.

As we offered volunteer income tax assistance this spring, I observed that many national tax preparers continued to offer high-priced, tax-refund anticipation loans. A consumer protection regulator could address these practices directly or through a national initiative to improve financial literacy for consumers of varying degrees of education and experience. We all want our children to make better decisions for themselves.

Even for traditional financial service providers, we support clear language and visual presentations like the "Federal box" required of credit card disclosures. However, regulators should be mindful of the impact of mass implementation of regulation on smaller financial institutions, particularly credit unions, where the cooperative structure has historically resulted in pro-consumer practices.

Seemingly small regulatory dictates can have a large impact on these institutions and ignore their "local knowledge" of how to best communicate with members. Larger institutions will benefit from economies of scale on a per account cost basis, further tipping the scale toward too-big-to-fail institutions.

There may be unintended consequences to consumer-friendly financial institutions as the bad actors are reined in by one-size-fits-all regulations. Implementation of the CARD Act requiring that specific credit card statement language for late payments be used resulted in hundreds of panicked calls by Truliant members who were not delinquent. The staff time required to explain the language mandated by the Fed could have gone to advising our members on how to better build their financial foundation.

We support streamlining and simplifying existing overlapping regulation to improve consumer understanding while reducing cost to the financial institution that can be passed on to the member-owner. We welcome combining TILA and RESPA to improve usability by the consumer and financial institutions. Streamlining ECOA and the Fair Credit Reporting Act could have similar benefits. We support regulation that allows and promotes innovation in financial services that is also helpful to the consumer. The consumer protection regulator will need to carefully balance these two deliverables. Consumer protection is not a one-time fix, but an ongoing effort that will span different political landscapes. We support a balanced governance structure that would not make the regulator ineffectual nor one that allows for public policy to become overly politicized.

Thank you again for the invitation to speak on behalf of Truliant, and I welcome your questions and discussion on this matter.

Chairman JOHNSON. Thank you, Mr. Schaefer.

Mr. Kelly, you may proceed.

STATEMENT OF ALBERT C. KELLY, JR., CHAIRMAN AND CHIEF EXECUTIVE OFFICER, SPIRITBANK, ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION

Mr. KELLY. Thank you, Chairman Johnson, Ranking Member Shelby, and Members of the Committee, for the opportunity to testify today on ways to improve the accountability of the new Bureau of Consumer Financial Protection. My name is Albert Kelly. I am from SpiritBank in northeastern Oklahoma, and we run a bank that has offices in 10 cities and towns in the northeast part of the State.

The banking industry fully supports effective consumer protection. At SpiritBank we are proud of our 95 years of service to our customers built on fair treatment of those customers. No bank can be successful without a long-term perspective like ours and without treating customers fairly.

The new Bureau will certainly impose new obligations on banks large and small that had nothing to do with the financial crisis and already have a long history of serving consumers fairly in a competitive environment. Therefore, there are several features of the Bureau that make improved accountability imperative. These include the problems brought about by: the extensive new powers of the agency, the unfettered authority of the Director to impose new rules, the separation of consumer protection from bank safety and soundness, the gaps in regulating non-banks, and the expanded and unaccountable enforcement authority of prudential regulators and State Attorneys General.

For all these reasons, and others, it is ABA's first priority to improve the accountability of the Bureau. Establishing accountability supersedes other important priorities regarding the Bureau, including ensuring appropriate bank-like supervision of non-banks for consumer protection.

ABA supports the creation of a board or commission that would be responsible for the Bureau's actions rather than giving the head of the Bureau sole authority to make decisions that could fundamentally alter the financial choices available for customers. It also provides the needed balance and appropriate checks in the exercise of the Bureau's significant authority. We urge the Congress to pass statutory provisions that ensure such accountability before the Bureau is established with a single Director.

The Dodd-Frank Act also gives license to pile on additional State law requirements and enables State Attorneys General and prudential regulators to second-guess Bureau standards as they see fit. If we are to hold the Bureau accountable, we must also hold accountable all those who derive authority from its existence.

ABA also supports a simple majority vote of the Financial Stability Oversight Council to set aside a Bureau rule instead of the two-thirds vote. If a majority of the Nation's top regulators believe a Bureau rule will have an adverse impact on the banking system, the rule should not go forward.

Moreover, ABA also believes that a finding of systemic risk is too narrow a review standard. The review standard should be recalibrated to account for adverse consequences of Bureau actions that do not rise to the level of systemic risk. For example, Bureau actions that end up driving some community banks out of business would not rise to the level of systemic risk but have enormous implications for the communities they serve.

Once the goal of accountability is achieved, we believe the Bureau should direct its resources to the gap in regulatory oversight: a failure to supervise and impose enforcement actions on non-bank lenders committing consumer protection violations. We welcome current efforts to define the Bureau's non-bank supervisory scope as it prepares for the future exercise of that supervisory authority.

As we have since our beginnings, banks across the country will continue to do whatever we can to make sure our customers understand the terms of the loans they are taking on. Our task is made more difficult by the many new hurdles that we have to jump over to serve our customers' most basic needs. Already, there are 2,700 pages of proposed regulations, and this is before the Bureau undertakes any new changes or rulemakings. All these changes have consequences for our communities: high costs, restrictions on sources of income, limits on new sources of capital, and excessive regulatory pressure. All make it harder to meet the needs of our communities. These impediments inevitably reduce the credit that can be provided and the cost of credit that is supplied. Fewer loans mean fewer jobs. Since banks and communities grow together, the restrictions that limit one necessarily limit the other. It is critically important that Congress establish accountability of the Bureau and ensure that the rules from the Bureau do not restrict access to financial products by responsible American families.

Thank you.

Chairman JOHNSON. Thank you, Mr. Kelly.

Ms. Drysdale, you may proceed.

STATEMENT OF LYNN DRYSDALE, MANAGING ATTORNEY, CONSUMER UNIT, JACKSONVILLE AREA LEGAL AID, INC.

Ms. DRYSDALE. Chairman Johnson, Ranking Member Shelby and Members of the Committee, I appreciate the opportunity to speak today. I have been a legal services attorney representing low-income consumers for the last 23 years in Jacksonville, Florida. As some of you may know, we are proud to be the home of two major military bases, so I have had the honor of serving military clients in my tenure there.

The group of low-income individuals has grown exponentially during the financial crisis. As this demographic grows, so also has grown the amount of aggressive and harmful lending which is going unregulated, or at least underregulated, throughout the United States.

One of the most vulnerable populations are the servicemembers who are serving our country. Many years ago, Congress passed the Military Lending Act. This Committee also was in favor of that Act. This Act was meant to curb illegal and harmful products that were hijacking servicemembers' bank accounts and taking their automobiles while they were serving our country overseas, leaving them with low morale, harming military readiness, and certainly harming their families at home.

Despite the passage of the Military Lending Act, which, among other things, reduced the interest rates which could be charged for military members and their families, and also prohibits mandatory unilateral arbitration, one of the individuals I spoke of when I spoke at the hearing in 2006 was an air traffic controller. He was having to monitor the airways at the same time he was being called and being threatened with court-martial and imprisonment for not paying back payday loans even though he had already paid back $10,000. Despite the protections of the Military Lending Act and despite the prohibitions of the Federal Fair Debt Collection Practices Act, he was still getting these threats. He was in danger of losing his security clearance as well as his job.

The Military Lending Act capped interest rates and prohibited unlawful terms, but we are still seeing these loans with triple- or four-digit interest rates being provided to servicemembers as well as many American citizens. This is happening because these lenders are operating under the guise of the Internet. They are able to charge interest rates that are in excess of those allowed by the Military Lending Act and State laws and engage in other illegal practices such as requiring the assignment of wages as a condition of obtaining the loan. This is also in violation of Federal Trade Commission regulations.

One may wonder why someone would take out a loan with triple-digit or four-digit interest rates. Well, that is because these loan products are packaged in a manner that is deceptive. The interest rates are not provided up front or either they are understated. For example, another client of mine took out a $2,200 automobile title loan secured by his free and clear title to his automobile. He also was required to pay $900 to purchase insurance which was required and provided no benefit to him and went straight to the pocket of the lender. The stated interest rate was 24 percent, which sounded high but reasonable to him, but the real interest rate was well above triple digits. He ended up losing his car.

Another very disturbing trend in providing unregulated loans are loans provided to military veterans who are not covered by the Military Lending Act. These veterans are being enticed with ads with flags flying, with military names in the name of the loan company, and they are led to believe that these companies are sanctioned by the military, when instead they are taking their pensions with loans of interest rates of triple digits. These types of loans are completely unregulated.

Just as I have—I know you have heard many hours of testimony relating to the problems with the mortgage industry, but I did want to bring up just a couple of instances where I have had clients who were fighting insurgents in Afghanistan at the same time they were fighting Wells Fargo on the mainland because Wells Fargo would refuse to accept their allotment payments even though they were current. I have received email messages from near Singapore from a gentleman with top secret clearance who was current in his mortgage and who was still being turned over to an attorney to proceed with mortgage foreclosure proceedings. This gentleman eventually was going to lose his home because he could not handle the stress of being on the job near Singapore as well as having his home lost for his family and his children. This automatically is going to affect the morale of military servicemembers. The Military Lending Act does not at all protect our veterans, and it also does not protect other citizens who should be protected by these unregulated or underregulated, aggressively marketed, high-interest loan products.

Thank you.

Chairman JOHNSON. Thank you, Ms. Drysdale.

Mr. Pincus, you may proceed.

STATEMENT OF ANDREW J. PINCUS, ON BEHALF OF THE U.S. CHAMBER OF COMMERCE

Mr. PINCUS. Thank you, Mr. Chairman, Ranking Member Shelby, and Members of the Committee. It is an honor to testify before the Committee today on behalf of the U.S. Chamber of Commerce and the hundreds of thousands of businesses that the Chamber represents.

The Chamber strongly supports sound consumer protection regulation that deters and punishes financial fraud and predation and requires that consumers receive clear, concise, and accurate disclosures about financial products. Businesses as well as consumers benefit from a marketplace free of fraud and other deceptive and exploitative practices.

At the same time, consumer protection regulation must further these goals while avoiding duplicative and unjustified regulatory burdens. Those burdens harm all Americans by diverting resources essential to fueling economic growth and by preventing small businesses from obtaining the credit they need to expand and create the new jobs that our economy so desperately needs.

The ability of a regulatory agency to carry out its mission successfully is influenced by its regulatory structure. The Bureau's unique and unprecedented structure deviates radically from the fundamental principles of accountability and checks and balances that have been a basic feature of our Federal Government for the past 224 years.

The Bureau's current structure confers on its Director unprecedented unchecked power of extraordinary breadth, far beyond that wielded by any other Federal regulator of individuals and businesses. Indeed, the Bureau lacks each of the ordinary checks designed to ensure accountability that are present in these other agencies. All other agencies are subject to at least one of these checks, but there are none here.

First of all, in contrast to the very familiar commission structure that is the norm for the FTC, the SEC, and other agencies, the Director exercises sole decisionmaking authority with respect to rulemaking, enforcement, and supervision actions, and every other matter.

Number two, most Government officials, of course, serve at the pleasure of the President. The Director has policy independence from the President such that he or she may be removed from office only for, and I am quoting the statute, "inefficiency, neglect of duty, or malfeasance in office."

Number three, in other agencies the power to appoint deputies and other officials is reserved to officials subject either to the President or to officials subject to the President's authority. Here the Director has plenary power to appoint every one of the agency's employees.

And, number four, of course, appropriation of funds by Congress is the norm for virtually every Government entity. Here the Director has the ability to spend more than half a billion dollars without congressional approval. There is no other regulation of private sector activities that enjoys both sole authority over an agency and tenure protection. Here the Director's additional authority to appoint all subordinates and freedom from the congressional appropriations process renders the position even more anomalous.

I know that there have been analogies attempted to the Comptroller, and I think it is important to say at the outset that the Comptroller is subject to the President's plenary power of removal and that the Secretary of the Treasury has oversight authority, general oversight authority, over the OCC as well as the power to appoint the Comptroller's deputy. So this is a very, very different situation.

Some cite other constraints that are claimed to substitute for the ones that are present in every other agency and not present here. But, again, those contentions are just wrong.

A budget cap, while it is true there is a budget cap in that Dodd-Frank sets a cap of $550 billion, escalating in the future, here every agency has a budget cap set by its authorization legislation and its appropriations legislation. So that is no difference.

The fact that there is a GAO audit, every agency is subject to an audit either by the GAO or by its Inspector General. Again, no difference.

The fact that there is a review by the Financial Stability Oversight Council, again, if the Bureau were a private entity and it cited FSOC review as a check on its power, that statement could well be the subject of an enforcement action for a deceptive practice. First of all, FSOC review applies only to rules. Second of all, the process itself is illusory and seems to have been designed never to be triggered. It has a high standard. There has to be a threat to the entire U.S. financial system, not just a part of it. And then seven of nine votes have to be in favor of overturning the rule, and even if every prudential regulator opposes the rule, it still cannot be overturned.

Finally, also false is the contention that a multi-member commission would somehow impose radical constraints on consumer protection. The Commission model, as I said, is the norm for a Federal agency, and I do not think anyone would say that the Federal Trade Commission is not a vigorous regulator.

In addition, the commission model was proposed by the President for this very agency and approved by the House of Representatives for this very agency in the course of its consideration of Dodd-Frank. Again, I do not think anyone would say that either the President or the House of Representatives in the last Congress was somehow interested in gutting the power of consumer protection.

The Chamber believes strongly that unless the Bureau's flaws are remedied now, problems in execution that are already being shown will worsen and spread, harming consumers, legitimate businesses, and our entire economy.

Thank you again and I look forward to answering your questions.

Chairman JOHNSON. Thank you, Mr. Pincus.

Professor Levitin, you may proceed.

STATEMENT OF ADAM J. LEVITIN, PROFESSOR OF LAW, GEORGETOWN UNIVERSITY LAW CENTER

Mr. LEVITIN. Good morning, Chairman Johnson, Ranking Member Shelby, and Members of the Committee. My name is Adam Levitin. I am a Professor of Law at the Georgetown University where my research focuses on consumer finance and financial regulation.

Three bills have been proposed in the Senate and the House to reform the structure of the CFPB. Let us be clear about what these bills are about. They are not about reforming the CFPB. They are simply attempts to hobble the agency under the banner of accountability and oversight. It is, frankly, puzzling that there are concerns about CFPB oversight before the CFPB is even operational. Nothing the CFPB transition team has done has raised any concerns about the existing oversight structure. Instead, it has only received accolades from financial institutions and consumer advocates.

I would suggest that concerns about oversight would be better directed at other bank regulators, like the OCC and the Federal Reserve, which failed epochally in their safety and soundness and systemic stability missions preceding the financial crisis. Curiously, those who demand better oversight of the CFPB have shown no interest in also pursuing better oversight of the agencies on whose watch the financial crisis occurred.

Looking at the design of the CFPB, it is apparent that the CFPB is, contrary to what Mr. Pincus claims, actually more accountable than any other Federal financial regulator. On page 6 of my testimony, you can see a chart comparing the CFPB's oversight with other Federal agencies.

As you might notice, it does differ somewhat from Mr. Pincus' chart, especially in its characterization of OCC and OTS oversight. In particular, I would note that it is not clear whether the President has the ability to remove the Comptroller at will or if it is only for cause. Mr. Pincus cites an OTS general counsel memorandum on post-employment retirement as his authority on this.

As far as I know, that is not the law. That is simply the opinion of the general counsel in one part of the Treasury Department. It is not the United States Code.

I think that when you look at the chart as a whole, it shows that there is extensive and unprecedented oversight for the CFPB. This accountability does sometimes differ from that of other Federal bank regulators, but given these other bank regulators' abysmal performance in allowing the financial crisis, it is not clear why we would want to replicate them. Their oversight structures have not worked.

So to review the key CFPB oversight provisions, the CFPB is subject to the Administrative Procedures Act notice and comment, rulemaking, and hearing and adjudication provisions. The CFPB is one of only three Federal agencies that is subject to OIRA's Small Business Flexibility Review. No other Federal bank regulator is subject to that kind of review.

The CFPB has numerous statutory limitations on its rulemaking powers. For example, the CFPB must make detailed findings if it wishes to exercise its power to declare certain acts or practices unfair, deceptive, or abusive. And it is prohibited from imposing usury caps or from regulating non-financial businesses.

The CFPB is also the only Federal bank regulator subject to a budgetary cap. While some think that this cap is too high because it will enable the CFPB to be too effective, I have never heard similar complaints about the lack of budgetary controls on the Fed, the OCC, the OTS, or the FDIC. There seems to be concern about budgetary independence only when it involves an agency tasked with prioritizing American families, not banks.

The CFPB is the only Federal bank regulator whose actions are subject to a veto by the Financial Stability Oversight Council. I have not heard many calls to subject the Fed or the OCC to similar vetoes.

The CFPB is, of course, subject to moral suasion by the Administration and, perhaps most crucially, the CFPB is subject to oversight by Congress. There have been no less than six hearings on the CFPB in the last 4 months, and the CFPB is not even open for business. I think that is impressive oversight. There is no escaping the fact that no other Federal regulator is subject to comparable oversight and limitations on its actions.

Turning to the specific bills, one would subject the CFPB to the appropriations process. Doing so would be a serious mistake. The financial crisis should have taught us that consumer financial protection is too important systemically to politicize it through the appropriations process. Do we want the level of consumer protection that we get in a given year to be the results of political horse trades? If it is a tight year in the budget, are we going to say exploding ARMs are OK this year? That would be the result. No other Federal bank regulator is subject to this appropriations process, and there is no reason the CFPB should be.

OFHEO, the former regulator of Fannie Mae and Freddie Mac, was subject to appropriations, and it was an impotent regulator as a result. Whenever OFHEO showed some teeth, the GSEs' allies in Congress yanked on its funding leash. Congress recognized this problem when it freed OFHEO's successor, FIFA, from the appropriations process. The only reason to subject the CFPB to the appropriations process is to create the possibility of de-funding the agency and rendering it ineffective.

Other provisions in the reform bills would replace the single Director with a five-member commission. Put differently, this proposes paying five people to do one person's job. This is classic Big Government bloat and waste, and it is going to diminish accountability. Instead of having the buck stopping with one person, authority will be diffused over five people. If a single Director is good enough for the OCC, it should be good enough for the CFPB.

Finally, the reform bills would lower the threshold for the Financial Stability Oversight Council to veto CFPB rulemakings. They would require a veto if the rulemaking were inconsistent with bank safety and soundness. Now, "bank safety and soundness" is a technical term. It means profitability. It is axiomatic that a bank can only be safe and sound if it is profitable. But consumer protection is sometimes at loggerheads with bank profits. The only reason to engage in predatory lending, for example, is because it is profitable. It is not done out of spite. What this means is that any CFPB rulemaking that affected bank profitability would, therefore, be inconsistent with safety and soundness and be subject to a veto under this reform bill standard. Accordingly, the Credit Card Act of 2009 and Title 14 of the Dodd-Frank Act, which reforms the mortgage lending industry, could not be implemented because they would affect bank profitability and, thus, be inconsistent with safety and soundness.

Congress established the CFPB to protect American families, not maximize bank profits. Let us let the CFPB have a chance to do its job.

Thank you.

Chairman JOHNSON. Thank you, Professor, and thank you all for your testimony.

We will now begin asking questions of our witnesses. Will the clerk please set 5 minutes on the clock for each Member for their questions?

Ms. Drysdale, in your testimony you talk about the scams servicemembers and their families are tricked into. As you know, the CFPB has an office headed by Holly Petraeus dedicated to servicemembers and designed to help them. What are the benefits your clients will get from Mrs. Petraeus' office?

Ms. DRYSDALE. I think her office will be extremely effective in providing servicemembers with an avenue of redress when they have a problem. Now they are not sure where to go. It will be one agency that will be tasked with taking on consumer complaints, with trying to address consumer complaints, and by recognizing systemic problems that need to be addressed.

I think one of the clear examples of her effectiveness that has already taken place was her actions in ensuring that three of the main mortgage servicers were providing the foreclosure notice required to be given to active-duty military. Active-duty military individuals were losing their homes without proper notice and without the protections of the Servicemembers Civil Relief Act. She took notice of this. There were hearings and enforcement actions have been taken against three of the servicers that were the most at fault in the failure to provide notice. I am sure there are others out there who also need to be addressed, and I feel comfortable that the Office of Service Member Affairs will be the most effective vehicle to do this.

Chairman JOHNSON. Mr. Schaefer, without a Director in place, the CFPB will not be able to exercise its examination and enforcement powers over non-bank financial institutions such as payday lenders. Do you agree that this authority is essential to level the playing field between responsible small community banks and credit unions that will not be examined by the CFPB and their non-bank competitors that will?

Mr. SCHAEFER. Senator, we agree that the sooner the CFPB can get to the task of monitoring and regulating the non-bank participants, the better. We recognize that it is a somewhat arduous and political process now. We would love to see a CFPB that is not subject to political whipsaw in terms of not knowing—like any business, we like it to be predictable what we are going to be subject to, but certainly the sooner the better in terms of being able to regulate payday lenders, the folks that do tax anticipation refund loans. We would like to see some leveling of the playing field, so the sooner the better.

Chairman JOHNSON. Professor Levitin, there seems to be much misinformation about the accountability of the CFPB and the checks and balances imposed on that new agency. Professor Levitin, would you please set the record straight about this issue?

Mr. LEVITIN. The CFPB has a unique set of oversight and accountability provisions. It does not look like any other Federal bank regulator in this regard, and I think that is actually a very good thing because we have seen that the oversight has not worked well for the other Federal bank regulators.

The CFPB has not opened its doors yet. The other Federal bank regulators allowed the financial crisis to occur.

If you look at the oversight provisions, I think they can be fairly characterized as much more exacting. The CFPB is subject to a budget cap. No other Federal bank regulator is subject to that budget cap. The CFPB is subject to a veto. There is no other Federal bank regulator that can be vetoed by the other regulators. Only the CFPB is subject to that veto.

The CFPB also is subject to a very standard set of oversight provisions in addition. It is subject to the Administrative Procedures Act which governs rulemaking and enforcement actions and adjudication. The CFPB is subject to the Small Business Review by OIRA within the Office of Management and Budget. No other Federal bank regulator is subject to that.

There is a mandatory GAO audit of the CFPB annually. That does not occur for any other Federal bank regulator. The Federal Reserve received a one-time partial audit as part of the Dodd-Frank Act, and that occurred only over the Fed's kicking and screaming. Mr. Pincus' characterization that GAO audits of financial regulators are routine is not correct.

And, last, it is important to note that as part of the Federal Reserve, the CFPB is subject to the Federal Reserve's Inspector General, that there may not be a dedicated CFPB Inspector General, but the Federal Reserve does have a very capable IG's office, and its mission includes the CFPB.

Chairman JOHNSON. Professor Levitin, would you please explain all of the ways that the actions of the CFPB will be tempered by the prudential regulators and their safety and soundness mission?

Mr. LEVITIN. Well, most importantly, we have the Financial Stability Oversight Council. The Financial Stability Oversight Council has the ability to veto CFPB rulemakings if they endanger the systemic stability of the U.S. economy. That is a critical oversight, and it is unique. If the OCC were to take an action that endangered systemic stability, no other regulator would have a say on that.

The CFPB is also instructed to coordinate with the prudential regulators regarding rulemakings, and the CFPB has already shown an extreme willingness to listen to other regulators, to listen to consumer advocates, and to listen to financial institutions. This is not an agency that is looking to be one-sided only for consumers. It is an agency that has really shown already that it is trying to find the right balance between consumer protection and ensuring that we do not have too many restrictions on business.

Chairman JOHNSON. Senator Shelby.

Senator SHELBY. Thank you, Mr. Chairman.

Mr. Kelly, Professor Levitin notes that if the Bureau opens without a Director, the Bureau will not have all of its powers, including the authority to regulate non-banks. Some have said that the Director should be installed immediately in order to ensure that banks and non-banks are regulated similarly.

What is the American Bankers Association's position on the need to immediately confirm a Director?

Mr. KELLY. Thank you, Senator. The American Bankers Association's position has been consistent since the beginning of Dodd-Frank and the introduction of the CFPB, and that is, it is a matter of governance. Just as I report to a board and most other businesses do, we believe that this should have an oversight board or a commission that allows that Director to report to it. That has been our position. We believe that is a sound way to roll this out. No one ever will stand in favor of having any consumer damage or having the egregious nature that certainly Ms. Drysdale discussed. We believe this needs to be gotten right the first time. We have done without this particular position for 150 years in the banking industry, and we ought to get it right this time if we are going to do it.

So it is not a matter of the ABA not saying go ahead. It is a matter of the ABA saying from the beginning, which we said, we believe this structure is the proper structure for this agency.

Senator SHELBY. And it is all about accountability, is it not?

Mr. KELLY. Yes, it is.

Senator SHELBY. Mr. Pincus, in your testimony you state, and I will quote, that "The Bureau's unique and unprecedented structure"—unique and unprecedented—"deviates radically from the fundamental principles of accountability and checks and balances that have been a basic feature of our Federal Government for the past 224 years."

In the testimony by Professor Levitin, he states that the Bureau "is more accountable than any other Federal financial regulator."

On what specific points do you disagree with Professor Levitin's analysis here?

Mr. PINCUS. I think I disagree on all of them, Senator, and I think what is critical in looking at accountability before we get into the specifics is what is the purpose of these checks and balances.

Senator SHELBY. That is right.

Mr. PINCUS. And I think the critical thing about the four checks and balances that I mentioned and that have been present, at least one of them, in every other agency that has been created—a commission structure, plenary removal authority in the President, subject to the appropriations process, Presidential power, either oversight or appointment of subordinates—is that they ensure oversight and some control by the political branches, because what is critical here is not just checks and balances for the sense of checks and balances. It is checks and balances so that this exercise of Government power by this entity in the end answers to the elected officials who are elected by the people. And I think the absence of any of those means that there is a critical defect here, that the Director has power but really is not in any way checked by a representative of the people because it lacks each of those four things. And I think turning to the things that the professor mentioned, they are either common to all agencies, or they do not really tie back to the people's elected representatives.

For example, it is true that like every other agency of the Federal Government the Bureau's regulations will be subject to the Administrative Procedures Act, but that Act merely codifies probably much of what the Constitution's Due Process Clause requires. So, again, it ties back to some important guarantees, but it does not tie back to the people's elected representatives.

He mentioned the FSOC review. As I said, I think it is the most illusory system ever constructed. First of all, it does not even apply to enforcement actions. The Director has total authority over enforcement actions. And the people setting up the Bureau have already said that they plan to proceed principally through enforcement actions rather than regulations, as the SEC and FTC have. But even if there were a regulation, the standard, as Mr. Kelly mentioned, threatening the stability of the entire financial system is a standard that cannot be met, shouldn't we be concerned about a regulation that would threaten the stability of a sector of the financial system? And the voting is such that there will never be an instance—this is a review system set up never to be used.

Congressional oversight, it is true there can be hearings, although I think it is interesting to take a look at the report of a House Appropriations Committee on the financial services budget, which talks about the problems that that Committee has had getting information about how the Bureau intends to spend the money that it has under this line of credit from the Fed.

The SBREFA, the Small Business Review Authority, it is true it is in the statute, but, A, it again only applies to rulemaking, not to enforcement or supervision; and, B, it is advisory. You have to go through the process, but at the end of the day, there is no check on the Director's decision. The Director gets to decide and reject whatever the SBREFA panel has decided. That is very different from the Office of Management and Budget OIRA review process where OMB, representing the President, can instruct agencies to change their views because what they plan to do does not comport with what the President believes is what is proper in his role as the people's representative.

Senator SHELBY. Thank you.

Mr. KELLY. Senator, may I add a comment to that?

Senator SHELBY. Sure, go ahead.

Mr. KELLY. I just want to say that, as well as what Mr. Pincus says, when we talk about the FSOC review, I guess the reality is when these rules were promulgated and put forth, we have 7,500-plus, 7,750-plus community banks out there scattered on Main Street across this country. And sometimes I think when we testify and when we are up here, we talk about things that—what is this review standard and what is that review standard. None of those banks are ever going to rise to systemic risk. As a matter of fact, the collection of those banks is not going to rise to systemic risk. Those banks get up every day—they are in your communities and mine, and they get up every day with the intent of trying to serve their customers, support their schools, and do the things that they have done for years and years. And all we are saying is this needs to have a board because it can become very unwieldy. Today the only growth areas of most of these small banks is compliance, and it is very, very difficult for them to take on the burdens of Dodd-Frank and CFPB in the manner that it is going to be promulgated just because of the massive amount of regulations. We will comply. We will do that, and we as always will welcome that to the extent that it is required. But the fact of the matter is if we look at this review as being a systemic risk review, it is far too broad.

Senator SHELBY. Do you believe that Dodd-Frank is going to help us create jobs in this country?

Mr. KELLY. Senator, I would say that from a standpoint of the banking industry, it is doing quite the opposite.

Senator SHELBY. Thank you.

Mr. KELLY. I can cite example after example. I was sitting literally thinking the other day that today I can think of a thousand jobs that we have funded that are working today, that if that loan came in I promise you we would not even take it down the road to the committee, because it requires there to be imagination and creativity and hope, that you think about that, think about that community, the jobs that that will create, and what it is going to build in the economy. And today, quite frankly, most community banks are running their banks in order to comply with regulation, which they always have, but not to really develop business or to try and create jobs for the economy because they are absolutely overwhelmed by the regulations they are getting.

Senator SHELBY. Thank you.

Thank you, Mr. Chairman.

Mr. LEVITIN. Senator, may I add a word to that, please?

Senator SHELBY. Sure, go ahead.

Mr. LEVITIN. I cannot say whether the Dodd-Frank Act is going to create jobs or not, but I think it is important that we all remember that hundreds of thousands of jobs were lost in this economy before Dodd-Frank, that were lost before we had this regulatory scheme in place, and, arguably, because we did not have it in place.

Chairman JOHNSON. Senator Reed.

Senator REED. Well, thank you very much, Mr. Chairman.

Mr. Levitin, as I understand it—and you could elucidate for me—the agency becomes effective in a few days. It has the authority to promulgate regulations. Those regulations will be enforced by the existing regulatory entities. Is that accurate?

Mr. LEVITIN. No, not quite. On July 21st, the CFPB stands up, it becomes effective. At that point, unless there is a Director that has been appointed by the President and who has either been a recess appointment or confirmed by the Senate, the Treasury Secretary becomes the Acting Director. The Treasury Secretary, however, will have limited powers as Acting Director. The Treasury Secretary will only be able to exercise the powers given the Bureau by subtitle (f) of Title X. Those powers include enforcing existing Federal consumer protection laws, but they do not include the power to create—to do new rulemakings other than under those laws, and it does not include the ability to examine non-banks.

Senator REED. Thank you very much, because I think that is an important clarification of what happens, effectively, on the day that the agency stands up.

One of the consistent themes here is that we should be applying these standard provisions to all financial agencies. Mr. Pincus, would you and the Chamber support subjecting the Federal Reserve's budget to the congressional appropriations process.

Mr. PINCUS. I think the Chamber's position, Senator, is that at least one of these checks needs to apply.

Senator REED. So which check——

Mr. PINCUS. Well, the Federal Reserve has one check already, which is that it is a multi-member commission. It is not a single person who exercises the power, and, of course, Congress did that because the power that the Fed has is vast, and it did not want to put that into the hands of one person.

Senator REED. So the Fed is a multi-member commission, but what is your position with respect to the budget as well as the FDIC budget? Should it be subject to Congress?

Mr. PINCUS. No.

Senator REED. No?

Mr. PINCUS. No, we think that history has shown that that check has proved effective with respect to the Federal Reserve. Of course, that is not a check that is present with respect to the Bureau.

Senator REED. Well, how effective has it been since I believe Congress in the 1990s—in 1993, 1994—passed HOEPA, which was designed to address the issue of predatory lending? The Federal Reserve refused to enforce the regulation despite their commission status. In fact, it was not until, I believe, March of 2009 that they did enforce some regulations with respect to predatory lending, but not under HOEPA, under the Truth in Lending Act, which they had authority for a long time before HOEPA. So as far as consumers are concerned, do you feel that commission structure was effective?

Mr. PINCUS. I think there certainly—and the Chamber said this during the Dodd-Frank debate, that there were failures with respect to the entities that had consumer protection authority, and the Chamber supported congressional action to remedy those failures. So the Chamber certainly recognized that during the run-up to the financial crisis, there were failures of enforcement, there were failures of regulators to exercise their existing regulatory authority. One question was what was the best way to remedy that. Congress decided the best way to do that was to consolidate that authority in a new regulator. But the problem is that it is a new regulator that is not—really has none of the checks and balances designed to ensure accountability, first of all, that the President proposed when he first proposed the agency, but that are the features generally of our Government structure.

Senator REED. How about the commission structure of the SEC with respect to the regulation of Lehman Brothers, Bear Stearns, and others? Was that an effective—and, by the way, their budget is subject to congressional authorization also. Do you think they were effective regulators with that structure in place, two of the elements?

Mr. PINCUS. I think the SEC has had some regulatory failures, and in fact, the Chamber issued a report before the financial crisis saying that changes were needed. On the other hand, I think if you look at the Federal Trade Commission, many people would say that the Federal Trade Commission has, A, been an extremely successful and effective consumer regulator, and also if you compare the Federal Trade Commission to the Antitrust Division, I think a lot of people would say that it has been a more effective antitrust regulator than the Antitrust Division has been.

Mr. CALHOUN. Senator, may I add a comment?

Senator REED. I would like to go to Mr. Levitin and then, if I may, get a comment.

Mr. CALHOUN. Thank you.

Senator REED. Mr. Levitin, you have heard this dialog. What is your impression?

Mr. LEVITIN. I think that Mr. Pincus is being rather kind in his characterization of the FTC as a consumer protection agency. The FTC has tried at times, but it has been held on a very tight leash by Congress, not least through the appropriations process. And if you think back a ways to 1980, the FTC tried to ban certain advertising targeting children as unfair. And what happened? Congress stepped in and choked off the FTC's budget. Then a few years later, we see Congress itself acting on cigarette advertising targeting children. I do not know that that is the way we really want to do our regulation, having a whipsaw effect.

I think maybe the most instructive comparison is with the Office of the Comptroller of the Currency. No commission structure, single Comptroller. The U.S. Code expressly prohibits the Treasury Secretary from delaying or preventing the Comptroller from undertaking rulemakings, so, you know, really a very independent regulator with an independent budget, and that is really the analog for the CFPB. The Comptroller has been an incredibly effective advocate on behalf of banks. And part of creating the CFPB is to create a counterweight to that, recognizing that consumer protection and safety and soundness need to be balanced, that it cannot simply be one subordinated to the other but they need to be balanced with parallel agencies.

Senator REED. A quick comment, Mr. Calhoun.

Mr. CALHOUN. Yes. I think in this discussion, following up on Professor Levitin's comments, we have overlooked the most fundamental checks and balances there, and that is the constitutional authority of the Congress through the normal legislative process. There have been repeated instances where agencies have taken actions that the Congress thought were inappropriate, and Congress has then through the normal legislative process revised the structure or rules and authority of that agency.

What concerns us so much about doing this in advance, by changing the structure of the agency, is the history that we have had. In one of the most recent ones, when the Federal Reserve proposed modest credit card reforms, far less comprehensive than what the Senate and the Congress enacted, the OCC declared those mild reforms as a threat to the safety and soundness of the banking system. And it is that viewpoint that it affected short-term profits, we are going to oppose it, that makes us concerned about putting it in a place where it can veto readily the actions of the Consumer Bureau.

Senator REED. Thank you, Mr. Chairman.

Chairman JOHNSON. Senator Corker.

Senator CORKER. Thank you, Mr. Chairman, and I thank all of you for your testimony. I know that my friend from Rhode Island was not suggesting that because people have failed—and many have—that we should not have any checks and balances in any of these organizations. I know that could not be possible. But let me go to you, Mr. Calhoun.

I know that you know that a lot of us tried to figure out a way to cause this thing to have some checks and balances, and I guess I ask this question: I do not understand why—I mean, there has been a major victory in having a consumer protection organization. It is obviously going to be well funded. I do not understand why people have tried to press into sort of an ideological divide to say that this one entity is one that should have absolutely no checks and balances. I mean, I would not confirm me as head of this agency, OK, because it is just not an appropriate thing. And I guess I would just ask you: Why is it that we have taken this one issue? There have been some modest requests. I know you have been very involved in the creation of this. There have been some modest requests regarding checks and balances.

One of the things you all are forgetting is, you know, there is going to be a Democratic appointee to this. There could be some ideological Republican appointed at some point on the opposite side that just repeals everything. I mean, I do not understand why you all have done this and why you have not been willing—I know that your input has had a big effect on this—why you all have not been willing to just sit down and say, OK, you know, they are right, maybe we ought to have just a few appropriate checks and balances where everybody will be united behind this instead of this continuing to be a political football as it has been because of the lack of any kind of checks and balances?

Mr. CALHOUN. Well, first of all, Senator, thank you and all the Members of this Committee for your work on this. This really is where the rubber meets the road of how do we avoid another financial crisis. I think our perspective and experience, again, has been that you have had—and we think the checks and balances are appropriate, that you have an OCC that is set up whose primary responsibility is safety and soundness——

Senator CORKER. Let me just make one point——

Mr. CALHOUN.——parallel structure for the Consumer Bureau, and that has been the guiding philosophy, again, based on the experience we have had.

Senator CORKER. You know, the one thing about the OCC that you all continue to leave out, though, is that the OCC, the way it is set up, a banking institution can choose not to be regulated by the OCC. So that is really not appropriate. I mean, you can end up being a State-chartered entity and not deal with the OCC. So that is not apples to apples.

Mr. CALHOUN. We think, though, that that cuts the other way because the history has clearly shown that because of that feature that the banks can choose their charter, that has tilted the OCC's perspective to be even more pro-bank and, quite frankly, anti-consumer. We saw that. Countrywide objected to very mild restrictions put on it by the OCC and they flipped——

Senator CORKER. So why are you using the OCC as an example?

Mr. CALHOUN. And they flipped to the OTS.

Senator CORKER. So that is my point. So why are you using the OCC as an example? It is not a good example.

Mr. CALHOUN. But it will be the continuing regulator, primary regulator of the national banks in this country, which control a huge share of consumer financial transactions, and the Consumer Protection Bureau and its Director need to be on par so that you do have the two of these working together with comparable structures, comparable powers to move us—and we agree, in a very balanced way—forward. But I would tell you again, everyone in the agencies, and in particular the Consumer Bureau, is very aware that at the end of the day for them to be sustainable they have to stay in line with where the Congress, where the Administration, and where the political process is, because we saw that with the FTC in the 1970s. It stepped further than the Administration or the Congress thought it should, and they promptly came in and revised and substantially cut back its authority.

Senator CORKER. I think you all have needlessly created an issue that actually created a divide over financial regulation in general, which then meant that the only way it could pass is with all Democrats, which then meant that the bill ended up being lopsided in a way, which then meant that we ended up with a tremendous lack of clarity now and will have for several years. And I just want to say to you, I think this was a gross misstep. I think you had the opportunity at one point to actually—Senator Shelby worked on it. We have all worked on it. You had a point in time when you could have created just some checks and balances and brought people together, and we have ended up with a financial reform bill that is not what it could have been really over this issue. And to me, this is a great example of people taking an ideological viewpoint and causing really, really bad legislation—not just on this issue, but really bad legislation on numbers of fronts to come forth.

Let me ask a final question, and I will stop. If you knew that the person appointed to this position was going to use this position to then run for Statewide public office in a few years and had told people that, would you believe that would be the right person for this job? Do you think it ought to be a politicized job?

Mr. CALHOUN. I think that the person should have qualifications, and you look at the qualifications, and, again, you would look at the accountability that the person has to do a good job.

Senator CORKER. There is no accountability. There is no accountability. So I just want to ask you this question. If someone stated that they wanted to run for Governor of a State in 2014 but they were going to do this in the interim—and I would assume make a name for themself—would you consider them to be an appropriate nominee for this position?

Mr. CALHOUN. I do not think that that has disqualified people from other positions, that there are a lot of folks who have been in administrations and then moved to electorate offices, including recent history.

Senator CORKER. Thank you, Mr. Chairman.

Chairman JOHNSON. Senator Akaka.

Senator AKAKA. Thank you very much, Mr. Chairman, for this hearing. I want to welcome the witnesses and say, Mr. Chairman, that history has shown that our country has been great because whenever we have been challenged, we have been able to come forth with legislation that has turned our country around. And I think the Dodd-Frank bill has done that because of a crisis that we faced. We can talk about many of the failures that have happened already, and as we know, it has been documented there has been failure of the Federal banking regulators to address consumer protection issues. And for me this is what it is all about, and here is one.

Ms. Drysdale, a 2006 DOD report found that payday lending had a negative effect on military readiness and our troop morale, as you did mention. The report was further evidence that junior enlisted servicemembers are particularly vulnerable to predatory lending practices.

Do you see any existing gaps in consumer protection for members of the Armed Forces to ensure that our servicemembers maintain a high level of readiness in the defense of our Nation? What role can the CFPB and its Office of Service Member Affairs play in addressing these gaps?

Mr. DRYSDALE. I see very large gaps, and I think my testimony—in my testimony I attempted to highlight the loopholes that have been created by the Federal regulations adopted after the Military Lending Act was enacted, which allows payday lenders, title lenders, refund anticipation lenders to create products that put themselves outside of the coverage of the Military Lending Act, so that takes them outside the 36 percent interest rate cap. It allows them to include mandatory unilateral arbitration in their contracts which prohibit military members from being able to have access to courts if they do have problems with these very aggressively and deceptively marketed products.

I think that the loopholes that have been created have watered down the Military Lending Act to make it almost ineffectual to protect the younger servicemembers.

Also, one of the big gaps in the Military Lending Act is it does not apply to automobile financing, and I think one of the first things that many of the young enlisted do when they get their first paycheck, one of the first things they are going to do is try to purchase an automobile.

I think also the protections provided by the Military Lending Act should be expanded. Veterans are not covered by the Military Lending Act, as watered down as it is. Older Americans are not covered by the protections of the Military Lending Act. And talking about checks and balances, we have businesses that are putting mandatory unilateral arbitration clauses in their contracts which provide consumers no redress if they are harmed by these very high cost, unfair products that are bleeding them of their bank accounts, robbing them of their vehicles, and, more importantly, I think, taking their homes away, leaving them and their families without a place to live.

Senator AKAKA. Mr. Levitin, Professor, in your testimony you identified a tradeoff that sometimes arises between consumer protection and bank profitability. Can you talk more about that tradeoff and what implications it should have on the focus of the CFPB?

Mr. LEVITIN. Of course. There is a balance that the regulatory structure is trying to strike between bank safety and soundness and consumer protection. Bank safety and soundness sounds like it is a very technical term, but it simply means bank profitability. A bank that not profitable is not safe and sound. You do not want to put your money in a bank that is losing money. And, unfortunately, the way the regulatory architecture worked prior to the creation of the CFPB was that consumer protection and safety and soundness were entrusted to the same agencies, and those agencies consistently put bank safety and soundness—that is, bank profitability—ahead of consumer protection.

By creating the CFPB and not giving it safety and soundness responsibility, this now means that consumer protection has a fighting chance against concerns over bank profitability. We need to have profitable banks in our country, but I do not think that we have any public policy concern over the exact level of bank profits. As long as they are profitable, there is no public interest in whether they are probably making X number of billion dollars or 2X. It is simply that they be profitable. And the banks, though, as self-interested actors, want to increase their profits, and they are very concerned that the CFPB will reduce their profitability. As long as the CFPB does not create a systemic risk by rendering banks insolvent, I do not think there is really any concern there. There is no reason that Congress should be concerned about the exact level of bank profitability, simply that banks are profitable. And that is what the FSOC veto does. It ensures that the CFPB does not create a systemic risk, and instead it allows the CFPB to find the right level of consumer protection.

Senator AKAKA. Thank you very much.

Mr. KELLY. Senator, may I comment on that?

Chairman JOHNSON. Yes.

Mr. KELLY. Well, just very briefly, I think that with respect to the professor, I can assure you that the regulators that come into our bank and banks like us look very closely at compliance with every consumer law and are severe beyond all means if you are not in compliance. We spend an enormous amount of money trying to comply every day, and I think it is wrong to suggest that any of us would rise to the level of a systemic risk under any system. So anything that is done or imposed on us would never be something that would rise to that level. So I just take respectful exception to that.

Chairman JOHNSON. Thank you.

Senator Merkley.

Senator MERKLEY. Thank you, Mr. Chair.

Mr. Calhoun, we have heard about the Federal Trade Commission being a very effective regulator. It is my impression that they are a regulator of mortgage brokers, and we had a period in which brokers engaged in both receiving steering payments or bonuses for steering families into predatory loans when they qualified for prime loans. The liar loans developed in which the loans were not underwritten and the numbers were often fictionalized. We had the teaser rates with families being locked in by the prepayment penalties. So where was the FTC through all this? Why didn't the FTC end these practices?

Mr. CALHOUN. I think you saw a variety of influences, and they are ones that have been proposed today for the CFPB that, in fact, handcuff the FTC and would in turn handcuff the Consumer Bureau. For one, there was repeated deadlock on the Commission, on the FTC Commission. As has been, I think, widely acknowledged, there has been a general challenge with the confirmation process, not just of the CFPB but across the board, and this body has been looking at ways to improve that. But that raises concerns with five members. But the CFPB had authority but was unable to use it because of that deadlock. They also——

Senator MERKLEY. The Trade Commission?

Mr. CALHOUN. The Trade Commission, excuse me. And, in fact, we saw this appropriations process again, and this is a concern we have. HUD also had authority over mortgage brokers and in the 1990s moved to try to limit these kickbacks that brokers got for putting people in the 2/28 loans that blew up the economy. There were appropriation riders put on HUD's budget to dissuade them from moving in that direction, and they backed off, and that was a direct contributing cause to our ultimate crisis.

So those are the concerns we have. Those agencies were not effective. You look at—the absence of rulemaking or enforcement actions are really stark at the FTC and with HUD during the crisis as well.

Senator MERKLEY. Thank you, Mr. Calhoun.

Mr. Levitin, we heard that the OCC objected to the Fed's mild credit card reforms. You might recall that we had issues like companies creating remote post offices so that payments were late, changing the number of days each month so that the consumer, when they did their regular payment, it turned out that they were late—a whole series of clever actions designed to run up fees.

Why did the OCC object to such mild considerations?

Mr. LEVITIN. Because the OCC was concerned that it would affect the short-term profitability of banks.

Senator MERKLEY. So here is kind of an interesting puzzle, and that is, it appears that under the argument to protect short-term profitability, long-term structural problems were allowed to emerge and that families' personal finances were undermined, making them weaker, and ultimately we ended up with mortgage practices that were turning to securities that carried the flaws of the mortgages into the securities and blew up our entire system. Why was the short-term profitability put over the long-term soundness of our system under the argument of soundness?

Mr. LEVITIN. I think a lot of that has to do with the competition for charters among bank regulators, that banks can shop for the regulator and that has some real serious consequences. Mr. Calhoun spoke about it earlier in his dialog with, I think, Senator Corker about how the ability to shop for charters has created a race to the bottom in bank regulation, and that the OCC, for example, gets its budget from appropriations—not from the appropriations process but, rather, from fees that it charges to the banks that it charters. And if it wants to have a larger budget, it has to charter more banks. And how is it going to get more banks? Well, it is going to offer more favorable regulation—not necessarily better regulation, just regulation that the banks like more. That means less regulation.

Senator MERKLEY. Thank you very much.

Ms. Drysdale, you mentioned the Military Lending Act and the fact that there are loopholes in it or that a lot of the pieces are not being effectively regulated. Who is the regulator for that? And how do we fix these loopholes? Is it a regulator issue?

Ms. DRYSDALE. It is a regulator issue, I believe. Thank you. I believe it is a regulator issue, and the regulations that were provided narrowed the products that were covered and the businesses that were covered so greatly that there are very, very few products that are actually covered, and it is very easy for any type of lender, institutional or otherwise, to create a loan product that is 92 days as opposed to 90 days to completely allow it to avoid regulation altogether.

The Department of Defense is the actual entity that regulates the Military Lending Act, and as you can well imagine, the Department of Defense has an awful lot of other matters on its mind rather than regulating financial industries.

Senator MERKLEY. Thank you. My time has expired, Mr. Chair, but I just want to note that as we look into the details, we find that HUD's efforts were stymied, the FTC efforts were stymied, the Fed's efforts never materialized because of their pursuit of the safety and soundness side, DOD is limited in their enforcement. So many of these issues that started with fairness to consumers ended up to be huge systemic risks, and I think it helps us to understand why the CFPB is such an important institution.

Thank you.

Chairman JOHNSON. Senator Schumer.

Senator SCHUMER. Thank you, Mr. Chairman, and I thank the witnesses and you, Senator Shelby.

First, I want to echo the comments from Senator Reed and many other of my colleagues about the need to preserve independent funding for the CFPB. As one of the original sponsors of the bill, before we put it into Dodd-Frank, I believe in it strongly.

We have seen in debates over funding for the SEC and CFTC some Members of Congress use the power of the purse, not just to hold agencies accountable—that is a good thing—but to undermine their mission and achieve deregulation through the back door. That is a bad thing.

Now, we know most Republicans oppose the creation of the CFPB and that fights about funding and accountability are just efforts to take away the Bureau's teeth before it is up and running.

I should also point out the Bureau is not funded by taxpayer dollars, and it is an irony that many of the same Members of Congress who express so much concern over the debt and deficit now want to add the CFPB to the taxpayers' tab.

Look, I went through this. For 10 years I tried to get the Fed to do a "Schumer Box," credit card disclosure. It took 10 years because that was not the Fed's mission. Their mission was safety and soundness. And even when they looked at this issue, they looked through the lens of safety and soundness, not through protecting consumers. And that is why we need an independent board.

My question is related to that. As you know, a recent study by the Pew Charitable Trust found nearly half of all checking account disclosure statements provided to new customers from the 10 largest banks run over 111 pages. The report found that half of all banks have more than 49 different hidden fees in these disclosure statements, and Americans are expected to pay, for instance, $38 billion in overdraft fees in 2011 alone.

Following this study, I proposed an easy-to-read checking fee disclosure statement on all checking account applications similar to the "Schumer Box" disclosure that I championed when I was a Congressman in the House and is still found on credit card applications, and it has been very successful. Remember, we are not talking Government regulation. We are talking Adam Smith here. Disclosure is how the economy is supposed to work.

The new box would show in an easy-to-read chart the key terms of any checking account, including minimum deposit, interest rate, amount of ATM fees, account closing fees, and other important fees like the terms of overdraft fees, *et cetera*.

So I want to ask each of the witnesses: Would you support a new "Schumer Box" disclosure requirement for checking accounts? Mr. Calhoun.

Mr. CALHOUN. Yes. The box that was used with credit cards was an important advance in consumer protection for credit cards. This would also be so for checking accounts and is particularly needed right now as many banks are adjusting the fees that they are charging on checking accounts, and they change them frequently, and it is very hard for consumers to move their accounts from one bank to another, and so they really need to know what they are getting into.

Senator SCHUMER. Before they get into it.

Mr. CALHOUN. Yes.

Senator SCHUMER. That is correct.

How about you, Mr. Schaefer?

Mr. SCHAEFER. Enthusiastically.

Senator SCHUMER. Great. How about you, Mr. Kelly?

Mr. KELLY. Senator, we support simplification and disclosure so that the customer understands it clearly. The simpler that could be, if that is what the "Schumer Box" would be on a checking account, that is fine as long as it does not violate the other things that we are mandated to do. I think the same should be true on mortgages and other things.

Senator SCHUMER. Good. So you are basically supportive of the concept of a simplified——

Mr. KELLY. I am not speaking on behalf of the ABA because I have not talked with them about it, but I am saying from my standpoint, the simpler that we could do it, the much better.

Senator SCHUMER. And 111 pages is not very simple. I understand you need legal requirements and all that, but it is not——

Mr. KELLY. Well, Senator, we do not have 111 pages, and I respect the Pew report, but ours is not 111 pages, but it still could be simplified.

Senator SCHUMER. Great.

Mr. KELLY. I will tell you that I believe that the mortgage—all of the mortgages—and we do quite a few of them. I think that there is too much paperwork that is mandated by the various laws, regulations, and this sort of the thing, and the simplification of that as well would be very, very welcome.

Senator SCHUMER. Great. I like simplification myself, and thank you for being supportive, and I would ask you to go back and bring your views to the ABA.

Ms. Drysdale?

Ms. DRYSDALE. Yes, sir, we would be supportive because a lot of the problems caused by products today are because they are being crafted as non-loan products, and the Truth in Lending disclosures are not being provided at all.

Senator SCHUMER. Thank you.

Mr. Pincus?

Mr. PINCUS. Senator, I do not know the Chamber's views on your legislation, but I do know we are very supportive of simplification, shorter, clearer disclosures. For example, the process underway now in the mortgage disclosure process, the Chamber is very supportive of that process and certainly would be supportive of a similar simplification process with respect to accounts.

Senator SCHUMER. Good. If you could show my proposal to the Chamber, I would be interested in a written answer from the Chamber and the ABA on whether they support it or not, and I hope they would.

Mr. Levitin?

Mr. LEVITIN. Yes, I think standardized disclosures are a very important step for checking accounts. It would allow consumers to do an apples-to-apples comparison between accounts, and that would enable consumers to get the best deals.

Senator SCHUMER. Thank you. I would say to all the witnesses that when the "Schumer Box" actually went into effect, it did bring credit card interest rates down because there was real competition. And many people propose a cap on credit card interest rates. I am sure Mr. Kelly and Mr. Pincus would not be for it. The ideal way to go is have disclosure, and if it can work in a simplified good form, that is the best way to go, and that is what we are trying to do here. So I thank all the witnesses for their virtually unanimous support of this proposal, and we will try to move it forward.

Chairman JOHNSON. Senator Hagan.

Senator HAGAN. Thank you, Mr. Chairman. Thanks for holding this hearing. And I do want to take one quick opportunity to welcome two of our panelists from North Carolina, Mike Calhoun and Mark Schaefer.

Mike Calhoun is the President of the Center for Responsible Lending, which has its roots in Durham, and your organization has truly been a forceful advocate for consumer protections in my State and at the national level.

Then I have had many dealings with Mr. Schaefer as the President and CEO of Truliant, which has 22-member financial centers and approximately $1.4 billion in assets.

Both of these individuals are exceptionally knowledgeable voices on consumer protection issues and were deeply engaged on these issues during the Dodd-Frank Act. So I do want to thank you both for being here.

Mr. Calhoun, I wanted to ask you one question having to do with for-profit education. Title X of the Dodd-Frank Act requires the study and monitoring of the private education student loan market, and it is my understanding from hearings in the Health, Education, Labor, and Pensions Committee that it is common for the for-profit educational institutions to make student loans directly to their students as a way to fill the gap between Federal loans and the price of tuition.

Do you know if these loans would be covered by the Bureau's new authorities under Dodd-Frank Act? And if not, do you believe they should be?

Mr. CALHOUN. They are covered, and they should be because this is, if you will, a mini version of some of the subprime lending and other mortgage problems that we saw, because these loans are provided to people who are trying to do the right thing—get an education, advance themselves, which helps the economy. Importantly, many of these loans are Government guaranteed, and so ultimately taxpayers are at risk on these loans.

Also, for the consumers they are typically non-dischargeable in bankruptcy except in the most extraordinary circumstances, so that student debt follows them essentially to the grave. And there have been repeated studies showing overreaching with these loans, providing loans that people really do not have the ability to repay. The loans are made, the for-profit educator gets paid, taxpayers are then left with the bill, along with the family. So it is a very serious problem, and it is one example where there has been a regulatory gap that needs to be carefully looked at.

Senator HAGAN. Thank you.

Mr. Schaefer, I understand from your testimony that Truliant has been particularly forward-thinking in its approach to handling overdraft fees. In April of this year, the Pew released a study titled "The Case for Safe and Transparent Checking Accounts" that highlighted several of the overdraft procedures that may be harmful to customers.

Can you tell me just a little bit about the overdraft policies that Truliant has implemented and what the results have been for your institution and your customers?

Mr. SCHAEFER. Well, as you know, with the Reg. E reform, the bad practice, in our opinion, of opt-out overdraft protection was eliminated. Truliant never had opt-out. We always had opt-in, so our members were always aware of their options other than paying a high overdraft fee, such as advancing a line of credit or taking a draft from savings.

I think relative to the CFPB, you know, they have indicated a willingness to allow innovation, and I think in the area of overdraft protection, there is lots of room for innovation. I hate to kind of give a feather to my own competitors, but Coastal Credit Union in North Carolina and the State Employees Credit Union both have an early warning notification on NSF charges. I have been trying to get my staff to implement it for a couple years now. We intend to implement it as well. You would get a notice, obviously, on your PDA, and you would have until 10 o'clock in the morning to cure it.

So that type of innovation, we just want to make sure the CFPB—and I know they backed away from plain vanilla. I think that is good that they backed away from that because innovation comes from the shops that are actually trying to help their members, and so I think we will have some ways to redress what we consider overpayment of overdraft fees.

Senator HAGAN. Thank you.

Mr. Calhoun, as you know, when I was in the State Senate in North Carolina, I worked aggressively to oppose the payday lenders that preyed on the families throughout the State, and we were successful in effectively ending that practice in North Carolina. Under Dodd-Frank it granted the CFPB certain supervisory and enforcement authorities over the payday lenders.

Do you feel that these authorities are sufficient to curtail the practice? And what might be the hurdles that the CFPB is facing or may face in the future as it attempts to regulate these predatory practices?

Mr. CALHOUN. Well, first, it does have explicit authority there, and it is badly needed. We urge the CFPB—and I think it is moving forward carefully with a lot of research, looking at the markets, understanding them, reaching out to businesses. There is, as I indicated in my testimony, an immediate crisis, though, in that the national banking regulators are allowing our biggest banks to come in and offer payday loans out of the national banks, even in States that expressly prohibit those loans. And we just think that is the wrong direction for lending in general, but particularly for flagship institutions.

Senator HAGAN. Thank you, Mr. Chairman.

Chairman JOHNSON. Senator Menendez.

Senator MENENDEZ. Thank you, Mr. Chairman. I thank all the witnesses.

You know, I would like to ask Professor Levitin, have you seen the CFPB's "Know Before You Owe" effort? Have you had a chance to look at that?

Mr. LEVITIN. I have read about it. I have not actually seen it.

Senator MENENDEZ. Mr. Calhoun, have you seen that at all?

Mr. CALHOUN. Yes, I have.

Senator MENENDEZ. You know, my understanding is it is an effort to simplify the mortgage disclosure form. As someone who practiced quite a bit at one time in that field, I am happy to see the mortgage disclosure forms simplified.

In your view, is the new form being proposed by the CFPB and going through consumer testing right now better than the two existing forms under RESPA and TILA?

Mr. CALHOUN. Yes, and my understanding is it has received accolades from both consumer advocates as well as mortgage lenders, and we look at it through the lens of both, being affiliated with a substantial mortgage lender. And it is a place where, again, consolidating the authority is—what you had for literally more than a decade you had HUD and the Federal Reserve with both having authority in that area and being unable to agree on even a simple disclosure form. And it is a place where I think we see the value of the Consumer Bureau being demonstrated. And, also, we see the care with which the Consumer Bureau has moved forward with that proposal.

Senator MENENDEZ. You mean this horrible agency has actually done something that, prior to its existence, no one could create, so to simplify and yet create a clear opportunity for the consumer to understand what they are entering into, and to get the mortgage lenders and the private sector to actually have a simpler, more modified, more efficient process? Is that actually what happened here?

Mr. CALHOUN. That is what is happening certainly in the context of this form.

Senator MENENDEZ. Well, that is interesting.

Ms. Drysdale, what do you think about the Bureau's new consumer complaint process that routes complaints to financial service providers for resolution and gathers information about those complaints?

Ms. DRYSDALE. I think that that is going to be a very effective mechanism. Now consumers do not know who to turn to, and often when they turn to Federal regulatory agencies, they do not receive relief from those agencies. Also, many of the products I have talked about, the State regulatory agencies just do not have any control over. Either they are acting under the auspices of a national bank, or they are importing interest rates from other States, or, quite frankly, the State regulatory authorities just do not have the funding to address some of the significant needs of consumers.

One of the other things that I wanted to mention that has not been mentioned yet was the Office of Financial Literacy. I think this is a very important aspect of the Consumer Financial Protection Bureau because I think consumers should be learning about consumer finance even before they become consumers.

Senator MENENDEZ. You know, Mr. Chairman, I want to read some quotes that existed from the Chamber of Commerce and the American Bankers Association. All of these are quotes that created concerns about bills that created a new Federal financial regulatory bureau, and I think observers will be able to tell which one I am talking about:

> There is no important aspect of the economic life of this country, whether it be agriculture or industry, banking or commerce, which will not be adversely affected by this bill.

> Nobody with any practical acquaintance with business process could look at these regulations and arrive at any verdict other than that they will cripple and retard business rather than help revive it. The fact is even so clear that it is hard to keep from wondering if such a result were not actually intended.

> This bill, if passed by Congress, will not only destroy our security markets but also a necessary consequence interrupt the flow of credit and capital into business.

> The bill is so unsound that it will ultimately force its own repeal.

Now, not one of these quotes, Mr. Chairman, is about the CFPB. Each quote is about the creation of the FDIC and the Securities and Exchange Commission from the 1930s when they were initially created in response to the Great Depression. Each quote sounds like what we are currently hearing about the CFPB and was created as a response to the financial catastrophe of 2008. And I just for the life of me cannot understand why it is that we have such an aversion—this would be the equivalent of saying, well, we do not like what the EPA does so we will not let it have a head; we do not believe in Medicare the way it is so we will not let it have a head of the agency. So we are destined at the end of the day not to have a well-performing agency, certainly as well as it could perform, without having leadership at the end of the day that can make sure that it is responsive to the Congress and the original intentions that we had for this Consumer Financial Protection Bureau.

And the same types of, I think, shrill and overblown rhetoric that has marked the current debate is what I see in the speeches that took place in the releases that were issued as it related to the FDIC and the SEC, two entities that we nowadays think, notwithstanding some of their shortfalls here and there, have acted in the interests of the marketplace, have acted in the interests of investors, have acted in the interests of depositors, have acted in the interests of consumers. I think that is really the case here as well.

Thank you, Mr. Chairman.

Chairman JOHNSON. Senator Shelby has a few more questions.

Senator SHELBY. Thank you, Mr. Chairman, for your indulgence.

Professor Levitin, in your testimony today you have clearly expressed, I believe, your belief that the OCC, the Office of the Comptroller of the Currency, and other financial regulators have not done a good job of overseeing our financial system. I think that is a given. Accordingly, do you support reforming the OCC and other regulators to make them more accountable?

Mr. LEVITIN. Yes.

Senator SHELBY. Thank you.

Mr. Calhoun, in your testimony you severely criticized the Office of the Comptroller of the Currency's actions in the lead-up to the financial crisis, noting several areas where the OCC acted irresponsibly and where its actions had adverse consequences. It is worth noting that other than the Bureau that we are talking about here, the Comptroller is probably the least accountable of our financial regulators. At least a lot of people believe that.

Do you believe, sir, that the OCC should be held accountable for its actions? Do you?

Mr. CALHOUN. I believe that it should, but I think primarily by——

Senator SHELBY. OK. You do believe it should be as a regulator, should be held accountable for its actions, don't you?

Mr. CALHOUN. I think it has accountability in many respects now.

Senator SHELBY. I did not ask you that. I asked you——

Mr. CALHOUN. Yes. I think everyone thinks——

Senator SHELBY. OK. If so, would you support an effort to make them more accountable to Congress? Would you support an effort to make the OCC and other regulators more accountable to Congress?

Mr. CALHOUN. We would support an effort to make the OCC comparable with the CFPB because they are the two pillars of financial oversight—consumer protection and safety and soundness—and we think that they should be comparable because they do represent the two interests that need to be at the table and balanced.

Senator SHELBY. But would you support—again, let me be clear. My question is this: Would you support efforts in the Congress to make the OCC and other financial regulators more accountable to the Congress? Either yes or no.

Mr. CALHOUN. I do have concerns about interference there, and there were protections put in that——

Senator SHELBY. So you would not support it then? You are modifying your position?

Mr. CALHOUN. No. I think the specifics matter. For example, in the savings and loan crisis, we saw intervention that prevented the regulators from stepping in and preventing greater collapse in that industry. And so it is a difficult balancing, but there are reasons to have protections and independence with the financial regulators because those short-term interventions are the tyranny of small decisions that create huge consequences. And, again, I would not want, for example, the OCC to be subject to intervention every time they tried to close down a bank.

Senator SHELBY. Neither would we.

Mr. CALHOUN. And that is what happened in the past.

Senator SHELBY. They have got to have the ability to do their job, the power to do their job. But my question to you, again: Would you support efforts to make them more accountable? If they fail the American people, which most people believe that the financial regulators failed the American people—the Federal Reserve, the FDIC, the Comptroller of the Currency, and so forth, I believe from this point here on the Committee, failed the American people leading up to the financial crisis. My question again: Would you support efforts to make them more accountable?

Mr. CALHOUN. I do not think the problem is their lack of accountability. I think the problem has been——

Senator SHELBY. Oh, you do not? You do not believe that?

Mr. CALHOUN. No. I think the problem has been the lack of——

Senator SHELBY. Have you followed this—have you followed the hearings on what led up to the crisis? I think you need to go back and look at them if you do not believe it is lack of accountability.

Everybody says, just about that I know, before this Committee and anywhere else that kept up with it, that it is a problem of accountability.

Mr. CALHOUN. That surprises me somewhat because I have not seen the proposals to change——

Senator SHELBY. I would suggest——

Mr. CALHOUN.——the structure.

Senator SHELBY. I hope you will go back and look at this because I think you are standing alone here.

Professor?

Mr. LEVITIN. Senator, I think that there is an important point that Mr. Calhoun is trying to make here, which is that accountability is important. No one debates that.

Senator SHELBY. Absolutely.

Mr. LEVITIN. And I would hope everyone on this panel would agree that we should seek more accountability for the Federal bank regulators.

Senator SHELBY. Absolutely.

Mr. LEVITIN. The question, though, is: How do we do that? And not every form of accountability is equally effective or equally appropriate.

Senator SHELBY. That is right, but accountability is important, isn't it?

Mr. LEVITIN. Without a doubt.

Senator SHELBY. Mr. Pincus.

Mr. PINCUS. Senator, I just wanted to make two points, if I may, in response to your question. I think first of all, there is sort of a fundamental question of Government here——

Senator SHELBY. Absolutely.

Mr. PINCUS.——about who ultimately everybody is accountable to, which is the people, and I do think accountable to elected officials. Although we might not all like everything that Congress and the President do every time, ultimately they are the people in whom the people have reposed their trust, and it seems to me that is a pretty fundamental part of our Government. And, therefore, when somebody says, for example, it is an interference because in an appropriations bill there is a provision that says to a regulator you may or may not do something, that is something that both Houses of Congress approved and the President signed, and it seems to me maybe it is bad, but it is what the people's representatives decided.

And I wanted to make one point about the OCC because I think it ties into your question, which is: I think several people on the panel have said we want to make the Bureau's Director on a par with the Comptroller, and so I think it is very important to note that the statutory language is very different. The Comptroller statute does not have the limitation on the President's removal power that I read before that the Bureau provision does, and that is the reason why—and I just want to correct Professor Levitin's statement. It was the Office of Legal Counsel at the Department of Justice that issued that opinion on behalf of the Attorney General saying that the Comptroller serves at the pleasure of the President, and the reason why is because that statutory language is different. Another difference in the statutory language is the language in the

Comptroller statute that talks about the Treasury Secretary's ability to exercise general direction over the Comptroller—again, not present at all in the CFPB statute.

So if the goal was to put them both on the same par, that has not been reached.

Senator SHELBY. To create a bureaucracy, a powerful bureaucracy that is not accountable to the Congress for its funds or really real oversight there, isn't that a big mistake?

Mr. PINCUS. I think it is, Senator. I think it really goes against, as I said, 224 years——

Senator SHELBY. That is right.

Mr. PINCUS. And, also, I think it is important to go back to the—in the face of statements that this would be some shocking hobbling of the Bureau, this is what the President originally proposed. It is not as if this is something—and what the House of Representatives passed, albeit in a staged process. This is not something that, you know, has been thought up by people and has not been advocated by people who are very strong advocates of consumer protection. And as you said in your opening statement, no one is asking to change the Bureau's substantive powers a bit. It is just to create——

Senator SHELBY. Or its mission.

Mr. PINCUS. Or its mission. It is just to create the kinds of responsiveness that really the Constitution mandates.

Mr. LEVITIN. Senator, if I may.

Senator SHELBY. Go ahead.

Mr. LEVITIN. The CFPB is subject to oversight by Congress. That oversight is not through the appropriations process, but that is actually, I think, quite right. I should not be one to speak to you about how the appropriations process worked, but appropriations bills involve lots of horse trading, and they are not policy bills. Overall they are compromises, and they do not focus on the specific policy issues at hand. We should want that kind of—that is the kind of oversight that Congress currently has now, that if the CFPB does something that Congress does not like, Congress can act and tell the CFPB, "Don't do that." And that is a much better form of oversight than oversight through appropriations. The appropriations process is meant to be a funding process, not an oversight process.

Senator SHELBY. Well, we all know that the Pentagon, our defense, very important, the FBI, all of our law enforcement people, are subject to appropriations. They are subject to the oversight of the Appropriations Committee because they are subject to the annual appropriations.

I have another question for Mr. Schaefer. The new Bureau will have the power, as I understand it, to write rules prohibiting products that are "abusive." If the Bureau deems one of your products to be abusive and you believe that the product provides value to your members, what recourse do you have to have the Bureau's decision reviewed or perhaps overturned?

Mr. SCHAEFER. Senator, I would hope that there would be some type of appeal process. We are very interested in the—there is supposed to be an Office of Regulatory Burden Monitoring within the CFPB. They are——

Senator SHELBY. You hope. You are using the word "hope." We all hope so, but go ahead.

Mr. SCHAEFER. It is my understanding there is a chance of that happening. But, you know, it would be very unlikely in a credit union environment where we would create a product that was so offensive that the CFPB would not approve of it.

There is also a small financial institution department that I believe Elizabeth Vale runs that takes a close look at how the regulations impact smaller financial institutions. But to address your question directly, I believe that the CFPB should have some type of appeal process whereby all financial institutions could redress concerns that they might have with their products.

Senator SHELBY. Mr. Schaefer, my last question. In your testimony you state that, and I will quote you, "Regulators should be mindful of the impact of mass implementation of regulation on smaller financial institutions"—which we all are concerned about. You also state that, "Larger institutions will benefit from economies of scale on a per account cost basis, further tipping the scale toward [too big to fail] institutions."

Do you believe, sir, that the Bureau is immune from this same concern? Have you thought about it?

Mr. SCHAEFER. Well, they do seem to have a predilection toward considering the concerns of smaller financial institutions. Actually, Mr. Kelly and I, even though usually banks and credit unions are on the other side, we have a common interest, as I do with many of my banker friends in North Carolina, in ensuring that the impact of the regulation does not unduly harm small financial institutions. The cost of regulation is higher per account for us than it is for Bank of America, and so we ask that they take that into account.

Are they immune from it? No. But do we think that they will reasonably take that into account? Yes. We believe that they have shown an interest in doing that.

Senator SHELBY. You would hope so, anyway.

Mr. SCHAEFER. I would hope so, sir.

Senator SHELBY. Thank you, Mr. Chairman.

Chairman JOHNSON. Thank you again to all of our witnesses for your testimony and for being here with us today. We look forward to the CFPB beginning its important work.

The hearing record will remain open for 7 days for additional statements and questions.

This hearing is adjourned.

[Whereupon, at 12:04 p.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

Written Testimony of Mike Calhoun
President, Center for Responsible Lending

Before the Senate Banking Committee

on

"Enhanced Consumer Financial Protection After the Financial Crisis"

Tuesday, 19 July 2010
538 Dirksen Senate Office Building

Good morning, Chairman Johnson, Ranking Member Shelby, and Members of the Committee. Thank you for the opportunity to testify on the need to maintain strong consumer financial protections in the wake of the financial crisis.

I am President of the Center for Responsible Lending (CRL), a nonprofit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, a nonprofit community development financial institution. For thirty years, Self-Help has focused on creating asset-building opportunities for low-income, rural, women-headed, and minority families, primarily through financing safe, affordable home loans. In total, Self-Help has provided over $5.6 billion of financing to 64,000 low-wealth families, small businesses and nonprofit organizations in North Carolina and across America.

In my testimony today, I demonstrate that unsustainable lending pushed us into the financial crisis, and that sustainable lending and responsible consumer financial services products are needed to restore and maintain economic health. An independent Consumer Financial Protection Bureau (CFPB), as enacted by the Dodd-Frank Act (DFA or Dodd-Frank), is critical to reestablishing these sustainable lending practices. Indeed, consumer spending, as 70 percent of gross domestic product, fuels the economy, so promoting a fair, equitable, and transparent consumer marketplace is key to financial stability. Maintaining the independence of the CFPB is necessary to doing so.

I. Federal Banking Regulators Failed to Exercise Oversight Over the Unsustainable Lending Practices that Caused the Financial Crisis

Almost four years ago, CRL released a report warning that reckless and abusive lending practices would lead to approximately two million subprime foreclosures.[1] At the time, our report was denounced by the mortgage industry as absurdly pessimistic. Sadly, the system was even more larded with risk than we reported, and the damage has been far worse, spreading from the subprime to the prime sectors, catalyzing a housing-led recession and triggering historic levels of unemployment.

With all the complexity of today's financial crisis, it's easy to lose sight of the key factor that led to the crisis: unsustainable lending beginning in the 1990s, when abusive subprime lenders put increasing numbers of families into expensive and unnecessarily risky home loans, most often refinancing existing home loans while stripping out much of the equity that those families had built.[2] Federal regulators should have been policing the marketplace and creating fair rules of the game by requiring underwriting to ensure that borrowers could actually afford the loans they received.

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[1] *See* Ellen Schloemer, Wei Li, Keith Ernst, and Kathleen Keest, *Losing Ground: Foreclosures in the Subprime Market and Their Costs to Homeowners*, (December 2006), available at http://www.responsiblelending.org/mortgage-lending/research-analysis/foreclosure-paper-report-2-17.pdf.
[2] *See* CRL issue paper, *Subprime Lending: A Net Drain on Homeownership* (March 27, 2007), *available at* http://www.responsiblelending.org/pdfs/Net-Drain-in-Home-Ownership.pdf.

Instead, federal regulators aided and abetted the lending binge, ignoring the inherently risky practices in the marketplace. Indeed, the financial crisis is largely the result of the breakdown of this nation's regulatory system. The agencies responsible for protecting depositors, shareholders, taxpayers, borrowers, and the general financial system failed. They stood by as predatory practices and dicey lending became commonplace, ravaging the mortgage market and setting off a chain reaction of financial devastation. I offer several examples of this regulatory failure below.

Federal Reserve Board (FRB or Board)

For many years, the FRB failed to effectively use its authority to regulate the mortgage market against unfair or deceptive acts and practices (UDAP) under the Home Ownership and Equity Protection Act (HOEPA) of 1994. In 2000, House Banking Committee Chairman Jim Leach said to the Board:

> Congress six years ago passed a law which was very strong in its sense of purpose in outlawing predatory lending in effect. And then, because Congress felt that the subtleties of this were beyond the Congress, we gave two federal regulators, most specifically the Federal Reserve Board of the United States, the authority to make definitions and to move in this direction. . . . So the question becomes if there is a problem out there: If Congress has given very strong authority to regulators and the Federal Reserve, are regulators and the Federal Reserve AWOL?[3]

At that time, consumer advocates urged the Board to use its HOEPA authority to prohibit abusive practices such as prepayment penalties on mortgages with interest rates greater than conventional rates.[4] While the FRB was failing to act, dozens of states passed their own regulations to address abusive practices.[5]

The Board did eventually act, using its HOEPA authority in July 2008 and participating in 2006 and 2007 in joint agency mortgage lending guidance. Although CRL commended Chairman Bernanke and the Board for promulgating this rule in 2008, it came far too late to stem the tide of foreclosures and the larger financial crisis that ensued; had it been issued just three or four years earlier, countless foreclosures could have been prevented.

Office of the Comptroller of the Currency (OCC)

The OCC also played a key role in the mortgage meltdown, both by actively blocking state consumer protection laws through the expansion of federal preemption and by simultaneously failing to adequately monitor the nationally-chartered lending institutions under its purview.

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[3] Representative Jim Leach, Hearing on Predatory Lending Practices, U.S. House Committee on Banking and Financial Services (May 24, 2000).

[4] Testimony of Martin Eakes, CEO, Center for Community Self-Help, Before the House Committee on Banking and Financial Services, May 24, 2000.

[5] *See* Wei Li and Keith S. Ernst, *The Best Value in the Subprime Market: State Predatory Lending Reforms,* Center for Responsible Lending (Feb. 23, 2006), *available at* http://www.responsiblelending.org/mortgage-lending/research-analysis/rr010-State_Effects-0206.pdf.

From the late 1990s, when anti-predatory lending laws were enacted by several states to provide substantive protections for consumers and place responsible checks on mortgage lending, the OCC worked to expand the reach of its powers and preempt state laws.[6] These state laws were designed both to protect homeowners and to preserve a safe, well-functioning market. Not only did the OCC's stringent preemption policies block strong regulation of federally-chartered entities, but also the immunity of federally-regulated entities prompted arguments from state-chartered entities that strong state reforms would create an uneven playing field on which they could not compete. These arguments served to chill action by state policymakers, and the result was too often a playing field with no rules.

At the same time that the OCC thwarted state efforts, it also ignored evidence of predatory lending within national banks and their affiliates and subsidiaries, simply repeating the mantra that there was no predatory lending in the national banks.[7] Only one OCC enforcement action against national banks from 2000 through 2006 involved subprime mortgage lending.[8] As another example of the OCC's failures, Countrywide booked $161 billion in payment option adjustable rate mortgage loans underwritten only to a very low teaser rate while it was under the watch of the OCC.[9]

The OCC and other banking regulators did not issue the Interagency Guidance on Nontraditional Mortgage Product Risks until late 2006 and the Statement on Subprime Mortgage Lending until June 2007. If the OCC had spent more time performing its duties of oversight rather than attempting to make its charter the most appealing, it could have played an important role in

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[6] Former Comptroller John D. Hawke, Jr. described the OCC's use of its power to override state laws protecting consumers as "one of the advantages of a national charter," and asserted that he was "not the least bit ashamed to promote it." The fact that the OCC is funded by assessments from the banks it regulates, rather than by Congressional appropriations (in 2005, 97 percent of the OCC's operations were funded by revenues from assessments), feeds a race to the bottom to attract institutions to its charter. *See* OCC, Annual Report, Fiscal Year 2005 at 7, *available at* www.occ.treas.gov/annrpt/2005AnnualReport.pdf; Jess Bravin & Paul Beckett, "Friendly Watchdog: Federal Regulator Often Helps Banks Fighting Consumers– Dependent on Lenders' Fees, the OCC Takes Banks' Side Against Local, State Laws," at A1 *Wall St. Journal* (Jan. 28, 2002).

[7] *See, e.g.*, OCC News Release 2003-8: OCC Issues Guidelines to National Banks to Guard Against Abusive Lending Practices (Feb. 21, 2003) (comments by Comptroller Hawke that "while the OCC has *no reason to believe that any national bank is engaging in predatory lending*, the agency's guidance will help prevent problems from arising in the future by prescribing steps national banks should take to avoid abusive practices."); Statement Of Comptroller Of The Currency John D. Hawke, Jr. Regarding The Issuance Of Regulations Concerning Preemption And Visitorial Powers (Jan. 7, 2004) ("We have no evidence that national banks (or their subsidiaries) are engaged in such practices to any discernible degree."); OCC, News Release 2004-3: OCC Issues Final Rules on National Bank Preemption and Visitorial Powers; Includes Strong Standard to Keep Predatory Lending out of National Banks (Jan. 7, 2004) ("There is scant evidence that regulated banks are engaged in abusive or predatory practices").

[8] Robert Berner & Brian Grow, "They warned us about the Mortgage Crisis," *Business Week* (October 9, 2008). The OCC's response to consumer complaints has been equally unimpressive. Although the OCC is required to have a separate consumer affairs division, 15 U.S.C. § 57a(f)(1), and largely relies on direct consumer contact with the bank as "the most effective way to resolve a complaint …" *See* OCC, Annual Report Fiscal Year 2004, at 19 (Oct. 2004), *available at* http://www.occ.treas.gov/annrpt/2004AnnualReport.pdf; OCC, 2004 Report of the Ombudsman, at 38 (Dec. 2004), *available at* http://www.occ.treas.gov/2004Report.pdf.

[9] Countrywide Financial Corporation, "3Q 2007 Earnings Supplemental Presentation," October 26, 2007.

averting this crisis. Even today, the OCC continues to push for broad preemption standards even though DFA scaled back the level of federal preemption.[10]

The OCC's thwarting of state efforts continued despite repeated warnings from consumer advocates. For example, as early as 2003, CRL highlighted to the OCC the evidence of predatory lending among national banks and their subsidiaries such as Guaranty National Bank of Tallahassee,[11] Wells Fargo, and First Franklin.[12] And in 2004, Self-Help CEO Martin Eakes testified the following before this very committee: "Abusive practices may well be profitable in the short term, but are ticking time bombs waiting to explode the safety and soundness of national banks in the years ahead. The OCC has not only done a tremendous disservice to hundreds of thousands of borrowers, but has also sown the seeds for future stress on the banking system."[13]

Office of Thrift Supervision (OTS)

The OTS, which today is part of the OCC as a result of Dodd-Frank, offered a stunning record of regulatory ineptitude through the collapse of three institutions under its watch – NetBank, IndyMac and Washington Mutual (WaMu).

An Inspector General's report in the wake of the September 2007 failure of NetBank concluded that the OTS ignored clear warning signs about the bank's risky lending.[14] The Inspector General found that the OTS "did not react in a timely and forceful manner" to "repeated indications of problems in NetBank's operations" – problems that had been evident for years in OTS examinations.[15]

Yet NetBank's failure was simply a prelude to the downfalls of IndyMac and WaMu. Never before in American history have two banks so large failed within months of each other. IndyMac's failure was the fourth largest bank failure in American history, and WaMu's collapse was the largest ever. The OTS failed to take effective action to halt the unsafe and unfair lending practices that eventually doomed both. And even as it became clear that these two banks' loan performances and financial returns were rapidly taking a turn for the worse, the OTS failed to act aggressively to alleviate the damage. In fact, the regulator prevented the Federal Deposit

[10] For a full discussion, *see* Comments of the Center for Responsible Lending, Consumers Union, National Consumer Law Center (on behalf of its low-income clients), Public Citizen, and Sergeant Shriver Center on Poverty Law to the OCC on its preemption proposal (June 27, 2011).
[11] This bank failed and was taken over by the FDIC on March 12, 2004. *See* http://www.fdic.gov/bank/individual/failed/gnb.html.
[12] Center for Responsible Lending, "Comments on OCC Working Paper" at 8-10 (Oct. 6, 2003), *available at* http://www.responsiblelending.org/pdfs/CRLCommentsonOCCWorkingPaper.pdf. The practices included charging exorbitant broker fees, imposing unfair prepayment penalties, evading HOEPA and other consumer protection laws, the high prevalence of 2/28 ARM loans accompanied by 3-year prepayment penalty provisions, as well as racial steering and lending discrimination. *Id.*
[13] Martin Eakes, testimony before the Senate Banking Committee (April 7, 2004). Quoted Senate Banking Committee Report on S. 3217 (which eventually became Dodd-Frank), see http://www.gpo.gov/fdsys/pkg/CRPT-111srpt176/pdf/CRPT-111srpt176.pdf.
[14] Office of Inspector General, Department of the Treasury, "Material Loss Review of NetBank, FSB," April 23, 2008; OIG-08-032, p. 1.
[15] *Id.* at 3.

Insurance Corporation (FDIC) from taking timely action by declining to put the two banks on the government's list of troubled banks until just before they went under – far too late to make any difference. WaMu and IndyMac were not guileless victims of financial hurricanes they had no control over; the OTS had readily available information about their unsafe and unfair lending practices, but declined to intervene.

The Role of the States

The federal regulators' failures are especially clear in light of the states' efforts. When the federal government failed to act, a number of states moved forward to pass laws to address abusive practices. Research assessing these laws has shown them to have been successful in cutting excessive costs for consumers without hindering access to credit.[16] And other states benefited as well. Spearheaded by active states such as North Carolina, Iowa, Massachusetts, and Illinois, among others, the state Attorneys General pursued enforcement actions and settlements against some of the larger institutions that employed widespread abusive practices. These settlements held bad actors accountable for their actions, brought relief to borrowers and influenced the marketplace nationwide. The success of the states despite the OCC's preemption doctrine especially underscores the failure of federal regulators to act.

II. <u>The Creation of CFPB and Attempts to Weaken It</u>

It was in the context of these massive federal regulatory failures that Congress enacted the Dodd-Frank Act, which included the creation of an independent CFPB. The history of the financial crisis is one in which prudential regulators – tasked with evaluating both safety and soundness and consumer protection concerns – largely focused on short-term profitability, giving short shrift to consumer protection. Even the best-meaning financial regulator will always prioritize its primary function (protecting the safety and soundness of the banks it regulates) over a subsidiary requirement (protecting consumers), particularly where it perceives the two goals to be in conflict. Unfortunately, the lesson was not learned that protecting consumers and bolstering the safety-and-soundness of financial institutions go hand-in-hand in the long term; for example, failing to underwrite loans beyond their teaser rates may lead to greater revenues in the short-term, but the longer-term failure of those loans has a severe adverse impact on individual financial institutions and the economy.

By enacting the CFPB, Congress wisely consolidated the consumer protection functions of the federal prudential regulators into one independent agency with a mission to protect borrowers from abusive financial practices. This will not only benefit borrowers; it also will help ensure the long-term sustainability of financial institutions (which, as we have seen, may fail when their revenues come from unsustainable and abusive consumer lending practices). The CFPB will also help strengthen the overall economy and help prevent another financial crisis.

CFPB's Authority and Structure

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[16] Roberto G. Quercia, Michael A. Stegman and Walter R. Davis, *Assessing the Impact of North Carolina's Predatory Lending Law*, Housing Policy Debate, (15)(3): (2004); Wei Li and Keith S. Ernst, *The Best Value in the Subprime Market: State Predatory Lending Reforms* (2006) *available at* http://www.responsiblelending.org/pdfs/rr010-State_Effects-0206.pdf.

Congress gave the CFPB broad rule-writing authority and some supervision and enforcement authority. CFPB rules generally are applicable to all entities. However, the CFPB has supervision authority only over certain institutions: depositories with more than $10B in assets, payday lenders, mortgage-related companies (e.g., mortgage brokers and servicers), private student lenders, and large non-bank entities (to be defined by rule in the future). Prior to enactment of DFA, these non-bank entities were wholly unsupervised by the federal government, and some had little oversight from the states. By bringing many of these previously unregulated entities into the CFPB's purview, DFA helps to even the playing field between bank- and non-bank financial institutions.

To preserve the CFPB's effectiveness, Congress put in place an independent CFPB funding source to match that of the other financial regulators. The Bureau's funding comes primarily as a transfer from the Federal Reserve Board, subject to a statutory cap, although the Director may request additional funding to be appropriated from Congress. This was intended to keep the CFPB on par with other federal banking regulators, which receive their funding without being subject to the Congressional appropriations process, reducing the potential that special interests will attempt to handcuff the agency through the appropriations process.

In addition, Congress put in place a single director who is clearly accountable for the actions (or lack thereof) of the Bureau. Directors who overstep their authority or who do not go far enough to protect consumers cannot deflect blame for their actions. A single director is also parallel to the regulatory structure of the OCC.

Limits to the CFPB's Authority in Dodd-Frank

Although the CFPB does have broad authority to write rules, supervise certain financial institutions, and enforce federal fair lending and consumer protection laws against certain entities, Congress added many checks to the Bureau's power. For example, like all agencies, it must comply with the Administrative Procedures Act. In addition, like only two other agencies and no federal banking regulator, the CFPB must convene small business panels under the Regulatory Flexibility Act before issuing a proposed rule, a process that is expected to add at least six months to the rulemaking process. The CFPB must also specifically consider the benefits and costs of proposed rules to both consumers and businesses, and its actions are subject to judicial review. In addition, the Financial Stability Oversight Council (FSOC) may veto any CFPB rule by a two-thirds vote if it concludes that the rule would pose a risk to the safety and soundness of the banking system or put the stability of the financial system at risk. The CFPB must also publicly review its rules every five years to ensure that they are not overly burdensome and to address key problems, and the CFPB's funding is statutorily capped, unlike any other federal banking regulator.

DFA also put in place additional checks on the CFPB. For example, the CFPB must submit to Congress annual financial reports and is required to report to Congress twice yearly to both justify its budget and provide details on its activities. In addition, the Government Accountability Office must audit the CFPB's expenditures each year and submit a report to Congress, and the CFPB is required to submit its financial plans, forecasts, and quarterly financial reports to the Office of Management and Budget. In addition, the Inspector General of the Federal Reserve Board must inform Congress about the CFPB's work.

Current Proposals to Restructure the CFPB

Despite these checks on the CFPB's powers, several bills and amendments have been introduced in this Congress to modify the CFPB before it even becomes operational. These include:

- S. 737 and the House financial services appropriations bill would permanently tie all of the CFPB's funding to the appropriations process. This would put the Bureau's effectiveness at risk by allowing large banks and other financial players to exert undue influence on the rulemaking process. This proposal is in stark contrast to the funding source of other banking regulators, which remain free of the appropriations process to protect the integrity of the supervision process.
- S. 737 and H.R. 1121 would change the governing structure of the Bureau from a unitary directorship to a five-member Commission. This would result in less accountability, as commissioners could avoid responsibility by pointing to the other four people who make up the Commission. H.R. 1121 would reserve one of the five commission slots for the FRB, which as outlined above failed to act to protect borrowers against predatory lending practices until it was far too late to avoid a crisis. S. Amdt. 391 to S. 782 would go even further. It would establish a six-person Board, with three of the Board members reserved for prudential regulators (the OCC, FDIC, and FRB). An even number of Board members on its own would make it hard to establish a clear majority to enact consumer protection rules; reserving three spots for prudential regulators would make it nearly impossible to do so. It was, after all, the prudential regulators who failed to act when they had the authority to do so leading up to the financial crisis. Again, this is in stark contrast to the OCC, which can move forward with regulations and enforcement actions under the leadership of a single director.
- H.R. 1315 would expand FSOC's veto authority in harmful ways. It would lower the threshold vote required for the veto from a two thirds vote to a simple majority, and it would change the threshold for the veto from one of systemic risk to the financial system as a whole to the safety and soundness of financial institutions. This would undermine the purpose of the CFPB and fly in the face of the causes of the financial crisis outlined above. Prudential regulators, by putting short-term safety and soundness over consumer protection, actually created long-term systemic risk to the entire financial system. Giving prudential regulators greater ability to overturn CFPB rules makes no sense given this history.

  In addition, sometimes practices that are abusive to banks' customers are beneficial to the safety and soundness of institutions that engage in it. For example, today many financial institutions routinely reorder debit card transactions from highest to lowest to maximize the overdraft fees they can charge. Certainly, this contributes to the revenues of those institutions in the near-term, but in the longer term, it harms the financial stability of banks' customers who could otherwise put that money to productive use in the economy. It also drives some out of the banking system altogether, and it runs counter to principles of fairness and transparency necessary to a competitive, healthy marketplace.

Similarly, during the subprime crisis, mortgage brokers benefited greatly from "yield spread premiums," which provided them with greater compensation from lenders if they placed borrowers in loans with higher interest rates than the borrowers qualified for, and the banks who gave those rewards benefitted from the higher-priced loans that resulted. Dodd-Frank expressly eliminated the practice; CFPB's rules to implement the law would run afoul of the proposed congressional standard because some mortgage brokers would be harmed by no longer being able to mislead customers. And, for a time, regulators and banks insisted that the practices could not be risky because they were profitable. By equating short-term profitability with safety and soundness, the industry and its regulators failed to understand that in the long run, abusive practices erode the stability of the people the banks ultimately depend on – their customers.

Individually and together, these proposals would cripple the effectiveness of the CFP and hamper its role to create a faster economic recovery and, just as important, to prevent another financial crisis from emerging in the future.

III. <u>An Effective CFPB Remains Critical Today</u>

Unfortunately for consumers, financial abuses continue today, making the CFPB's success as important as ever. Below we provide an overview of several abusive practices that greatly harm consumers. In each of these cases, federal banking regulators have done little to protect consumers from these abusive products. The CFPB, with its consumer protection mission, is in the best place to establish basic rules of the road to enhance both consumer protection and a robust competitive market.

Mortgage Servicing

Widespread mortgage delinquencies have laid bare many of the abuses and failures that have existed within the mortgage servicing industry even before the current crisis. For at least a decade, community-based organizations, housing counselors, and advocates around the country have documented a pattern of shoddy, abusive, and illegal practices by many mortgage servicers. Mortgage servicers have staff who are trained for collection activities rather than loss mitigation, infrastructure that cannot handle the present level of demand, and business records that are an utter mess.[17] Unfortunately, the prudential regulators chose not to use their authority to regulate this industry in the past; as a result, there is now a greater need than ever for the CFPB to serve as a cop on the beat.

Overview of Servicing Abuses

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[17] *See, e.g., In re Ocwen Loan Servicing, LLC Mortg. Servicing Litigation*, 491 F.3d 638 (7th Cir. 2007) (allegations by a class of homeowners that Ocwen systematically charged late fees for payments that were sent on time); *Federal Trade Commission (FTC) Settlement* (2003) resulted in $40 million for consumers harmed by illegal loan servicing practices, *available at* http://www.ftc.gov/fairbanks (FTC alleged, among other things, that Fairbanks illegally charged homeowners for "forced placed insurance" and violated the Fair Debt Collection Practices Act); and *FTC Settlement with Countrywide, available at* http://www.ftc.gov/countrywide (Countrywide agreed to pay $108 million dollars to homeowners in response to the FTC's allegations that Countrywide charged illegal fees to homeowners during Chapter 13 bankruptcy proceedings).

Abusive practices have become so ingrained in the servicing culture that they are now endemic to the industry. The harm to which borrowers have been subjected as a result of these abuses cannot be overstated. Numerous homeowners are burdened with unsupported and inflated mortgage balances or have been subjected to unnecessary and/or wrongful foreclosures before loss mitigation measures have been fully considered. These abuses include the following:

- *Dual track.* Servicers actively pursue foreclosure even when they are already working with homeowners on a modification, often leading to unnecessary foreclosures before a decision on the loan modification has been made.
- *Foreclosing even when investors would receive more from a sustainable modification.* It is in the best interests of investors and borrowers, and a requirement under the Home Affordable Modification Program (HAMP), that servicers modify a mortgage loan when its net present value (NPV) positive, *i.e.*, when the expected return to investors from a modified loan is greater than the expected return from a foreclosure. Unfortunately, this is not happening systematically.
- *Improper denial and delay of loan modification requests.* Delay can be in servicers' interests because fees, which eventually flow directly to servicers (either from the homeowner directly or through the proceeds of a foreclosure sale down the road), continue to accrue. A ProPublica study highlights the problems this creates for distressed borrowers: The homeowners interviewed spent an average of more than 14 months waiting for a HAMP modification (a process that should only take a few months), and "as a result of the delays, homeowners fall further behind, putting them in danger of foreclosure and making it less likely they'll qualify for a modification. About two-thirds of these homeowners were still current on their mortgages when they began the process, but most have now fallen behind."[18]
- *Forcing homeowners into multiple temporary modifications.* All modifications are not created equal. Extended temporary modifications are good for servicers' interests but harm those of borrowers. Temporary modifications can represent a best-of-both-worlds situation for servicers, who continue to charge fees as if the borrower is in default but without the cost of having to finance principal and interest advances to investors. Many borrowers go from one temporary modification to another, continuing to accrue high fees that drive them even further underwater.
- *Force-placed insurance.* Servicers too often force-place very expensive hazard or other insurance and charge the borrower's account when the borrower's insurance has not lapsed (or is not needed as may be the case with flood insurance), often driving an otherwise current borrower into delinquency and even foreclosure.
- *Improper fees.* Servicers sometimes charge unlawful default- and delinquency-related fees for property monitoring and broker price opinions.
- *Requiring borrowers to give up legal rights in order to receive a modification.* This is even more egregious considering that some temporary modifications are not in borrowers' interests, making legal rights the only effective bargaining chip for such borrowers to enter into permanent and affordable modifications.

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[18] *See, e.g.*, Paul Kiel & Olga Pierce, "Homeowner Questionnaire Shows Banks Violating Gov't Program Rules," *ProPublica* (Aug. 16, 2010), available at http://www.propublica.org/article/homeowner-questionnaire-shows-banks-violating-govt-program-rules.

- *Misapplication of borrower payments.* This results in inappropriate and unauthorized late fees and other charges, as well as misuse of borrower funds improperly placed in "suspense" accounts, which creates income for servicers.
- *Mismanaged escrow accounts.* Servicers sometimes improperly manage borrower accounts for real estate tax and insurance escrows, including by failing to disburse payments for insurance and taxes on time, causing cancellation and then improper force-placing of insurance, as well as tax delinquencies and tax sales.
- *Failing or refusing to provide payoff quotations to borrowers.* This may prevent borrowers from obtaining a refinance loan or a short sale.
- *Abuses in the default and delinquency process.* Servicers sometimes fail to properly send notices of default; prematurely initiate foreclosures during right-to-cure periods and immediately following transfer from another servicer, and without proper notices to borrowers; initiate foreclosure when a borrower is not in default or when borrower has cured the default by paying the required amount; and fail to adhere to loss mitigation requirements of investors.

The Need for CFPB Action

In today's housing market, when millions of families are in default and at risk of losing their homes, servicers should work to minimize the number of foreclosures by offering modifications whenever possible and economical. This requires servicers to distinguish between necessary (NPV negative) and unnecessary (NPV positive) foreclosure cases so that they can proceed swiftly with the necessary foreclosures and offer sustainable, long-term modifications when foreclosure is unnecessary.

Instead, the servicing system is compounding the problem by proceeding with many unnecessary foreclosures, which harms not only investors and homeowners, but also neighborhoods and communities as well as the larger economy through spillover effects and other negative externalities. Perverse financial incentives in pooling and servicing contracts illustrate why servicers press forward with foreclosures when other solutions are more advantageous for investors. Servicers are generally paid a fixed percentage of the outstanding balance on a loan for servicing a mortgage when payments are being made on the loan. The traditional mortgage servicing paradigm was marked by a collections mentality, and compensation reflected that mentality. The foreclosure crisis, however, created a need for massive underwriting of loan modifications, and as a result, fees paid for servicing a non-delinquent loan are much too low.[19] According to Amherst Securities, with a typical servicing fee of 25 basis points per year ($625/year on a $250,000 loan), servicers are overpaid for traditional servicing (which costs servicers only about $48/year) and underpaid for loss mitigation on non-performing loans (which costs about $900/year).[20] On the flip side, servicers may charge and collect a variety of fees after

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[19] Testimony of Laurie Goodman of Amherst Securities Group to the Subcommittee on Housing Transportation, and Community Development of the Senate Committee on Banking, Housing, and Urban Affairs, National Mortgage Servicing Standards and Conflicts of Interest (May 11, 2011), available at http://banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=484c5b2b-6924-459f-898e-3ae075feeb15.

[20] *See* Laurie Goodman, et al, "Alternative Compensation Arrangements for Mortgage Servicing – The Debate Begins," *Amherst Mortgage Insight* (Feb. 2, 2011): "[T]here is widespread awareness that the current system (in

the homeowner goes into default and can recover the full amount of those fees from the foreclosure proceeds, providing strong incentives for proceeding with foreclosure.[21] Unfortunately, borrowers cannot protect themselves by shopping for a better servicer, because they are tied to whoever services their loan for as long as the loan is outstanding.

The conflicts of interest between investors and servicers continue, and ultimately borrowers, communities, and the overall economy all suffer. A robust and independent CFPB is needed to create basic ground rules in servicing that apply to all and that are enforced as to all.

Debt Settlement Industry

Debt settlement is another industry that demonstrates the need for the CFPB. Debt settlement companies advertise that they can eliminate consumer debt by negotiating reduced debt payoffs with a consumer's creditors for unsecured debt such as credit card debt and medical bills, with the consumer often paying up-front for services.[22] In reality, little debt is actually settled.

As discussed in more detail below, the limited existing data show that, at best, debt settlement is beneficial for only a small percentage of consumers struggling with debt; many debt settlement participants are left worse off than if they had never enrolled in the program. This harms the economy in that it drains consumers' resources that could otherwise be channeled back into the economy in a more productive way. Moreover, debt settlement companies require that consumers stop paying their debts – usually credit card debts – thereby having a negative impact on the bottom lines of the banks that usually end up having to write off the debt.

Available Data Show Poor Results for Debt Settlement Programs

Robust data on the debt settlement industry are not available; our hope is that more data will become available once the CFPB gets up and running. The few data that are currently available demonstrate the need for greater oversight of the industry.

The data most favorable to the industry come from The Association of Settlement Companies (TASC), one of two debt settlement industry trade associations, in a comment letter to the

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which a minimum servicing fee is part of the mortgage rate) was not designed for current market conditions. This minimum servicing fee is far too high for performing loans and far too low for non-performing loans.

[21] For a thorough discussion of the servicing incentive structure, see Testimony of Diane Thompson before the Senate Banking Committee (Nov. 16, 2010), *available at* http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.Testimony&Hearing_ID=df8cb685-c1bf-4eea-941d-cf9d5173873a&Witness_ID=d9df823a-05d7-400f-b45a-104a412e2202; *see also* Diane Thompson, "Why Servicers Foreclose When They Should Modify and Other Puzzles of Servicer Behavior," (National Consumer Law Center Oct. 2009), available at http://www.nclc.org/images/pdf/foreclosure_mortgage/mortgage_servicing/servicer-report1009.pdf.

[22] *See, e.g.*, http://debtmerica.com/ ("Resolve Debt in as little as 24–48 months"); http://www.freedomdebtrelief.com/debtreduction.php ("FDR's Fresh Start Program, also known as Debt Negotiation or Debt Settlement, is an aggressive approach to becoming free of unsecured debts."); www.dmbfinance.com ("DMB Financial's typical client has seen over 50 percent of their unsecured debt negotiated away and is debt free in as little as 36 months.").

Federal Trade Commission.[23] The data show that nearly two-thirds of consumers who enrolled in a debt settlement program terminated before completing the program, while less than one-quarter actually "completed" the program.[24] The TASC survey found:

- 65.6 percent of those enrolled terminated before completion.
- 42.8 percent of those enrolled had no debt settled at all.
- Only 24.6 percent of consumers successfully "completed" the program (with at least 70 percent of debt settled).

Additional data come from the Colorado Attorney General whose second annual report, released in September 2010 (with data from 2006-2009), showed a similarly low success rate for debt settlement companies:[25]

- More than 60 percent of consumers who had signed up in 2006, 2007 or 2008 had already terminated as of Dec. 31, 2009. More than 40 percent of those who had enrolled in 2009 had also terminated.[26]
- By the end of 2009, only 11.35 percent of consumers who had enrolled more than three years earlier and 9.53 percent of those who enrolled in 2007 had completed the program.
- The average program term was 39.18 months.
- Through the end of 2009, enrollees paid an average of nearly $1,000 in fees, regardless of whether any debt was ever settled.

The limited data that exist indicate that, at best, debt settlement is beneficial for only a small percentage of consumers struggling with debt; many debt settlement participants actually end up financially worse off than when they entered the program. Tellingly, the industry has admitted that to require a debt settlement company to meet a standard that a "majority (at least 50 percent) of its clients successfully complete its program and obtain a reduction in debt that is significant

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[23] Letter from the Association of Settlement Companies (TASC) to the Federal Trade Commission, commenting on the FTC's proposed amendments to the Telemarketing Sales Rule on the marketing of debt relief services at 9-11 (Oct. 26, 2009), available at http://www.ftc.gov/os/comments/tsrdebtrelief/543670-00202.pdf. TASC was an industry trade group for the debt settlement industry. It has recently rebranded itself as the American Fair Credit Council. *See* http://www.americanfaircreditcouncil.org/.

[24] Completion is defined as at least 70 percent of debt settled. It is interesting that the industry counts success as settling 70 percent of debt, but represents that it will eliminate consumers' debt, and charges its fees based on 100 percent of the debt.

[25] *See* "Press Release: Attorney General Unveils First Annual Report On Debt Settlement, Credit Counseling Business Practices," available at http://www.coloradoattorneygeneral.gov/press/news/2009/10/15/attorney_general_unveils_first_annual_report_debt_settlement_credit_counseling; 2009 Annual Report – *Colorado Debt Management Service Providers*, available at http://www.coloradoattorneygeneral.gov/sites/default/files/press_releases/2010/09/24/2009_dm_annual_report.pdf. *2008 Annual Report – Colorado Debt Management Service Providers*, available at http://coloradoattorneygeneral.gov/sites/default/files/uploads/uccc/2008%20DM%20Annual%20Report.pdf. Moreover, 28.38 percent of those who enrolled in 2008 cancelled before the year was done. *See 2008 Annual Report.*

[26] *See* "Press Release: Attorney General Unveils First Annual Report On Debt Settlement, Credit Counseling Business Practices," available at http://www.coloradoattorneygeneral.gov/press/news/2009/10/15/attorney_general_unveils_first_annual_report_debt_settlement_credit_counseling; *2008 Annual Report – Colorado Debt Management Service Providers*, available at http://coloradoattorneygeneral.gov/sites/default/files/uploads/uccc/2008%20DM%20Annual%20Report.pdf.

and exceeds the fees charged by the company, ... *requires an unrealistic measure of programs' success rate*"[27] [emphasis added].

Adverse Impacts of Debt Settlement Programs

The American Bankers Association explained in a comment letter to the FTC that "many [debt settlement] consumers find themselves deeper in debt, with a seriously impaired credit record, and facing continued collection efforts – including collection lawsuits and garnishment proceedings – following their engagement of a for-profit debt relief provider."[28] In addition, stopping payments to creditors as part of a debt settlement plan can reduce a consumer's credit score anywhere between 65 and 125 points.[29] Missed payments can remain on a consumer's credit report for seven years, even after a debt is settled.[30] Even worse, many consumers who enroll in debt settlement programs end up having to file for bankruptcy.

FTC Action on Debt Relief

On 29 July 2010, the FTC issued amendments to the Telemarketing Sales Rule (TSR) relating to debt relief services, including a ban on advance fees and some other limited conduct restrictions for covered providers and transactions. However, there are notable gaps in the rule because of the FTC's limited jurisdiction and the scope of the TSR. For example, the rule excludes nonprofits, intrastate calls, certain transactions with face-to-face contact, and internet-only transactions. In addition, the rule does not require any data collection or reporting.

Following the FTC rule, many debt collection industry players have moved away from the advance fee model that dominated the industry before the rule was in place. The FTC rule thus did improve the industry. However, whether these players will be more successful in settling debts for consumers and in providing a net benefit to these consumers remains to be seen. The fee structures charged by the majority of these companies continue to be not well aligned with the interests of the consumers; fees are calculated based upon the amount of debt enrolled in the program and not based upon the amount of money saved for consumers through a settlement. Given the other harms engendered by debt settlement programs, consumers can still often find themselves paying fees early in the program but still ending up worse off.

Some debt settlement providers have sought to evade the FTC's advance fee ban, largely by contracting with attorneys or others to hold pro forma face-to-face meetings with potential customers but who do not actually do the work. In such cases, the debt settlement company

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[27] U.S. Government Accountability Office Rep. No. GAO-10-593T, *Debt Settlement: Fraudulent, Abusive, and Deceptive Practices Pose Risk to Consumers* at 13 (Apr. 22, 2010) [hereinafter "*GAO Report*"], available at http://www.gao.gov/new.items/d10593t.pdf.

[28] Comments of the American Bankers Association to Federal Trade Commission re Telemarketing Sales Rule – Debt Relief Amendments, Matter No. R411001 at 2 (Oct. 26, 2009), available at http://www.ftc.gov/os/comments/tsrdebtrelief/543670-00199.pdf.

[29] *GAO Report* at 10, 14.

[30] *Id.*

charges up front and ongoing advance fees whether or not any debt is ever settled for consumers.[31]

Need for CFPB Action

Notwithstanding the FTC's limited but helpful action on debt relief, stronger monitoring and oversight of the overall industry and more complete data collection relating to the impact of current practices are needed to ensure that debt relief activities are productive enterprises that increase, rather than decrease, the ability of consumers to bounce back from insurmountable debt and become productive consumers who contribute positively to the economy again.

Oversight and supervision of the debt settlement industry would also bring long-term benefits to the economy. When consumers are struggling financially, they cut their spending significantly. High or inappropriate program fees for debt settlement keep consumers from settling debt quickly. They also prevent consumers from returning to responsible spending habits that would help keep and create jobs in their local communities and add to the local tax base through sales and income taxes. Ensuring that debt settlement companies across the board – including non-profit entities, lawyers, and any other actors – are engaging in conduct that provides a net benefit for the majority of consumers services, will bring about a quicker financial turnaround for consumers, and consequently, a quicker economic recovery.

Payday Lending

Payday lending harms borrowers and is a net drain on the economy, diverting consumers' resources that could otherwise be channeled into the economy in a more productive way. Independent academic research cited below demonstrates that payday lending increases a borrower's chances of filing for bankruptcy, becoming delinquent on a credit card, having a hard time paying other bills, delaying medical care and prescription drug purchases, and losing their bank account (becoming unbanked). All of these have negative overall impacts on the economy and warrant intervention by the CFPB to ensure an equitable, fair and transparent consumer marketplace for credit that works for consumers and uplifts the economy.

Payday Loan Product and Industry

Payday loans are short-term cash loans based on personal checks held for future deposit or on electronic access to the borrower's bank account, depending on the terms of state laws. Borrowers write a personal check or provide electronic access to their bank accounts for the amount borrowed plus the finance charge and receive cash. Lenders hold checks until the next payday when loans and the finance charge must be paid in one lump sum, with a single paycheck. To pay a loan, borrowers can redeem the check for cash, allow the check to be deposited, or pay the finance charge to roll the loan over for another pay period.

[31] *See, e.g.*, Press Release, "Attorney General Madigan: Pocketbook Issues Continue to Top Consumer Concerns in 2010; Madigan Files Lawsuit Aimed at New Wave of Consumer Debt Settlement Scams" (Mar. 2, 2011), available at http://illinoisattorneygeneral.gov/pressroom/2011_03/20110302.html.

Payday loans typically range from $100 to $1,000, depending on state legal maximums. The typical loan term is about two weeks. The finance charge for a payday loan ranges from around $15 per $100 borrowed to $30 per $100, resulting in annual interest rates from 391 percent to 782 percent for a two-week extension of credit.[32]

In order to obtain a payday loan, a borrower merely has to have an open bank account, a source of income from a job or public benefits such as Social Security, and a valid form of identification. Lenders do not determine if a borrower can afford to repay the loan from the borrower's income rather than from taking out a new loan. Although failing to repay is typically reported to mainstream credit reporting services, successful repayment of a payday loan is not reported, and therefore, does not improve a consumer's credit score.

Overview of Problems in Payday Lending Industry

Payday loans are advertised as a way to receive a loan for an occasional financial emergency, yet in reality, most borrowers find themselves in long-term, high-cost debt traps because the predatory structure of the payday lending business model sets these borrowers up for failure.[33] The fundamental problems with the payday loan product that lead to long-term payday debt include: (1) the high annual percentage rate on these loans, (2) the short time period in which a borrower has to repay the debt in one balloon payment, (3) the holding of a check or access to the borrower's bank account as collateral, and (4) a lack of consideration of the borrower's true ability to repay the loan in the required timeframe.

The vast majority of payday lenders' business comes from borrowers who take out significant numbers of loans because of the high cost and short repayment period; payday loans are not designed to be taken out just once. Consider the following:

- The average payday borrower takes out nine loans a year, generally on a consecutive basis with more than one transaction per month.[34]
- CRL's national report, *Phantom Demand*, found that a full three quarters of payday loan volume is generated by borrowers who, after paying back the first loan, must re-borrow before their next pay period.[35] In other words, most of the "demand" for payday loans is created by payday loans themselves, and not by consumers' independent financial need.[36]

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[32] Payday loans are subject to Truth in Lending requirements, per court decisions and a Federal Reserve Board ruling in 2000. *See* Federal Reserve Board, Official Staff Commentary § 226.2(a)(14)-2, issued March 24, 2000.
[33] FDIC's Office of the Inspector General (OIG), Challenges and FDIC Efforts Related to Predatory Lending, Audit Report No. 06-011, June 2006 ("Characteristics potentially associated with predatory lending include, but are not limited to, (1) abusive collection practices, (2) balloon payments with unrealistic repayment terms, (3) equity stripping associated with repeated refinancing and excessive fees, and (4) excessive interest rates that may involve steering a borrower to a higher-cost loan.") Payday lending is listed as an example. "Payday Loans are small-dollar, unsecured, short-term advances that have high fees relative to the size of the loan. When used frequently or for long periods, the total costs can rapidly exceed the amount borrowed." *Id.*
[34] Uriah King, Leslie Parrish & Ozlem Tanik, *Financial Quicksand: Payday lending sinks borrowers in debt with $4.2 billion in predatory fees each year*, Center for Responsible Lending (Nov. 30, 2006) *available at* http://www.cha.wa.gov/?q=files/paydayloanstudy.pdf.
[35] Leslie Parrish & Uriah King, *Phantom Demand: Short-Tern Due Date Generates Need for Repeat Payday Loans, Accounting for 76 percent of Total Volume* (July 9, 2009), available at http://www.responsiblelending.org/payday-

- Nationally, over 90 percent of all loans go to borrowers with five or more loans annually; 60 percent of all loans go to borrowers with 12 or more transactions per year; and 24 percent of loans go to borrowers with 21or more loans per year.[37]
- CRL's recent report, *Payday Loans, Inc.: Short on Credit, Long on Debt* found that in their first year of borrowing, the average payday borrower remained in debt for 212 days of the year.[38] The report also found that payday borrowers tend to become more frequent users of payday loans as time passes: the group averaged nine loans in the first year and 12 in the second year; eventually, nearly half (44 percent), defaulted.[39]

Adverse Impacts for Payday Borrowers

The predatory elements of payday loans cause borrowers to take out one loan after another, without reducing principal. In most cases, payday borrowers end up far worse off than if they had never taken out their first payday loans. For example:

- *Payday loan borrowers are worse off than consumers who have no access to payday loans.* Colby College researchers simulated families trying to pay bills despite budgetary constraints over a 30-month period. Borrowers who used the typical volume of payday loans per customer per year for this industry were found to be worse off financially than those without access to payday loans.[40]
- *Using payday loans causes financial hardship for families.* A University of Chicago Business School doctoral student compared households in states with and without access to payday loans over a five year period and found that access to payday loans increases the chances that a family will face hardship, have difficulty paying bills, and have to delay medical care, dental care, and prescription drug purchases.[41] These finding are bolstered by findings in the Detroit Area Study (DAS), conducted by a University of Michigan law professor. Comparing payday loan users with similar low- to moderate-income households in Detroit who did not use payday loans, the DAS found almost three times the rate of bankruptcy, double the rate of evictions and phone cutoff, and almost three times the rate of having utilities shut off.[42]

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lending/research-analysis/phantom-demand-short-term-due-date-generates-need-for-repeat-payday-loans-accounting-for-76-of-total-volume.html.

[36] *Id.*

[37] Uriah King & Leslie Parrish, *Springing the Debt Trap: Rate Caps are Only Proven Payday Lending Reform* (Dec. 13, 2007), available at http://www.responsiblelending.org/payday-lending/research-analysis/springing-the-debt-trap.html.

[38] Uriah King & Leslie Parrish, *Payday Loans, Inc.: Short on Credit, Long on Debt* at 5 (Mar. 31, 2011), available at http://www.responsiblelending.org/payday-lending/research-analysis/payday-loan-inc.pdf. The report was based upon 11,000 Oklahoma payday borrowers who were tracked for 24 months after their first payday loan.

[39] *Id.* at 6-7.

[40] Bart J. Wilson, David W. Findlay, James W. Meehan, Jr., Charissa P. Wellford & Karl Schurter, *An Experimental Analysis of the Demand for Payday Loans* (Apr. 1, 2008), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1083796.

[41] Brian T. Melzer, *The Real Costs of Credit Access: Evidence from the Payday Lending Market* (Nov. 15, 2007), available at http://home.uchicago.edu/%7Ebmelzer/RealCosts_Melzer.pdf.

[42] Michael S. Barr, *Financial Services, Savings, & Borrowing Among LMI Households in the Mainstream Banking*

- *Using payday loans increases the chance of losing a bank account.* Harvard Business School researchers examined involuntary bank account closures in states where payday loans are available and states where these loans are prohibited to determine the impact of loan availability on account closure. The study found that an increase in the number of payday loan outlets in a county is associated with an 11 percent increase in involuntary bank account closures, even when other variables such as income and poverty rate are taken into account.[43] Researchers focused on Georgia, a state that bans payday loans but is surrounded by states that permit the product.[44] Counties at least 60 miles from the border with payday loan states had a 15.6 percent decline in account closures when Georgia expelled payday lending.[45]
- *Payday loan users who also have credit cards are twice as likely to become delinquent on the card.* Researchers at the Chicago Federal Reserve Bank, Vanderbilt University, and the University of Pennsylvania examined a large sample of payday loan users who also had a credit card from a major issuer.[46] They found that taking out a payday loan makes a borrower almost twice as likely as other credit card customers to become seriously delinquent on their credit car during the next year (11 percent for payday borrowers vs. six percent for all credit card users overall).[47]
- *Using payday loans causes borrowers to file for bankruptcy.* In a large Texas study, researchers found that payday borrowers were about twice as likely to file for bankruptcy in the two years following payday use compared with similarly-situated payday loan applicants who were turned down for payday loans.[48]

Need for CFPB Action

The CFPB will play a critical rule in ensuring a fair, equitable, and transparent consumer marketplace for credit in general, including payday loans. CFPB action on payday loans would also even the playing field between banks whose lending activities are regulated at the federal level (even, as discussed below, for payday loans offered by banks) and payday lenders whose activities are not federally regulated.

As previously discussed, if the financial crisis taught us anything, it should be that reasonable underwriting of loans, and particularly a determination that the borrower can afford to repay a loan without relying on another loan or an appreciating real estate market to come up with the money to pay it off, is crucial to long term stability. In the case of mortgage loans, federal banking regulators did not act to effectively address predatory and unaffordable mortgages when the housing market continued to rise, as borrowers could refinance into new mortgages whenever

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& Alternative Financial Services Sectors (Federal Trade Commission Oct. 30, 2008). Presentation of findings available at http://www.clevelandfed.org/research/Conferences/2009/2-6-2009/Keys_presentation.pdf.

[43] Dennis Campbell, Asis Martinez Jerez & Peter Tufano, *Bouncing Out of the Banking System: An Empirical Analysis of Involuntary Bank Account Closures* (June 6, 2008), available at www.box.frb.org/economic/eprg/conferences/payments2008/campbell_jerez_tufano.pdf.

[44] *Id.*

[45] *Id.*

[46] Sumit Agarwal, Paige M. Skiba & Jeremy B. Tobacman, *Payday Loans and Credit Cards: New Liquidity and Credit Scoring Puzzles?* (Jan. 13, 2009), available at http://ssrn.com/abstract=1327125.

[47] *Id.*

[48] Paige M. Skiba & Jeremy Tobacman, *Do Payday Loans Cause Bankruptcy?* (Oct. 10, 2008), available at http://www.law.vanderbilt.edu/faculty/faculty-personal-sites/paige-skiba/publication/download.aspx?id=2221.

a problem arose (and numerous mortgage lenders like Countrywide, Ameriquest, IndyMac and others took advantage of this and profited handsomely). Once the housing market cooled and borrowers could no longer refinance out of unaffordable loans, however, the whole system crashed – bringing down lenders, borrowers and the economy. The same problem occurs with payday lending, as borrowers essentially refinance unaffordable payday loans by getting new ones. When the borrowers come crashing down, however, their inability to pay other debts and purchase products, their potential loss of a bank account or fall into bankruptcy are consequences that affect the economy, not just the individual. For these reasons, supervision, oversight and policy action by the CFPB is needed.

Overdraft and Payday Loans Offered by Banks

Overdraft Loans

For many years, banks would extend overdraft coverage as a courtesy without a fee, but in the past two decades, they have switched to charging for this service. Today, these charges cost consumers billions of dollars.[49] The most common triggers of overdraft fees are small debit card transactions that could easily be denied at no cost when the account lacks sufficient funds.[50] Most institutions offer far lower cost alternatives called "formal" overdraft protection, such as contractual lines of credit or links to credit cards or savings accounts, but too many institutions aggressively steer customers to their highest cost overdraft coverage.[51] Research has shown that the majority of these fees are paid by customers who are least able to recover from them.[52] Over time, overdraft fees leave these already-struggling consumers worse off, less likely to be able to meet their ongoing expenses, and contribute to greater numbers of unbanked households.[53]

In November 2009, the Federal Reserve Board issued an "opt-in" rule, requiring that institutions obtain customers' consent before charging overdraft fees on debit card purchases and ATM transactions. This rulemaking helped raise widespread awareness about these fees. But the rule merely established a baseline protection for debit card and ATM overdraft fees that virtually every other credit product already enjoys: consent. Consent requirements for credit cards and mortgages have never removed the need for substantive protections in those areas.

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[49] *See* Leslie Parrish, *Overdraft Explosion: Bank fees for overdrafts increase 35% in two years*, Center for Responsible Lending (Oct. 6, 2009), *available at* http://www.responsiblelending.org/overdraft-loans/research-analysis/crl-overdraft-explosion.pdf.

[50] 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.

[51] Leslie Parrish, *Banks Target, Mislead Consumers As Overdraft Deadline Nears*, Center for Responsible Lending, (August 5, 2010), *available at* http://www.responsiblelending.org/overdraft-loans/researchanalysis/Banks-Target-And-Mislead-Consumers-As-Overdraft-Dateline-Nears.pdf.

[52] FDIC Study of Bank Overdraft Programs (Nov. 2008). In addtion, two CRL surveys, conducted in 2006 and 2008, found that 71 percent of overdraft fees were shouldered by only 16 percent of respondents who overdrafted, and those account holders were more likely than the general population to be lower income, non-white, single, and renters.

[53] Overdraft fees are a significant reason that individuals who had bank accounts at one time are no longer banked. *See* Dennis Campbell, Asis Martinez Jerez, and Peter Tufano, *Bouncing Out of the Banking System: An Empirical Analysis of Involuntary Bank Account Closures*, Harvard Business School (June 6, 2008) (noting that virtually all involuntary bank account closures, when the financial institution closes a consumer's account, occur because the account became overdrawn an excessive number of times).

The Board's rule failed to address the fundamental substantive problems with the overdraft product: a balloon repayment paid directly out of the customer's next deposit, regardless of whether the repayment leaves the customer with enough funds to live on; fees out of all proportion to cost; the frequency with which the fees are charged; manipulation of transaction posting order to increase fees; and aggressive marketing and steering of high-volume overdrafters into high-cost programs.

The Board's consent rule did trigger a shift in the marketplace. The largest issuer of debit cards, Bank of America, stopped charging debit card point-of-sale overdraft fees altogether, joining Citi, which never has. But other issuers, large and small, aggressively marketed overdraft "opt-in," targeting the customers who generate the most fees and steering them to the highest-cost credit the bank offers.[54] As a result, although overdraft fees have decreased in the aftermath of the rule,[55] its impact has not reached those most likely to be trapped in debt as a result of the high cost of the product. Consequently, banks that have taken the high road so far are left vulnerable to pressure from investors to backslide.

Bank Payday Loans

Banks have more recently added another high-cost, short-term balloon repayment product to the mix: payday loans, in which banks deposit funds into the customer's account and repay themselves the loan amount plus the fee upon the customer's next deposit. Most banks offering this product charge a fee of $10 per $100 borrowed.

Consultants are actively pushing bank payday loans, touting dramatic increases in fee revenue. A recent industry webinar recommended that banks consider issuing high-cost, triple-digit APR loans,[56] and payday loan software is being marketed to banks with promises that, within two years, revenue from the product "will be greater than all ancillary fee revenue combined."[57] Bank payday programs are not pushed as a way to *substitute* for overdraft fees; rather, they promise to be an additional way banks to generate revenue. One marketing flier promises that offering the payday loan product will result in little-to-no "overdraft revenue cannibalization."[58]

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[54] Center for Responsible Lending Research Brief, *Banks Collect Opt-Ins Through Misleading Marketing*, April 2011, *available at* http://www.responsiblelending.org/overdraft-loans/policy-legislation/regulators/banks-misleading-marketing.html.

[55] A recent study by Market Rates Insight found that service fee revenue decreased $1.6 billion in the six months following the enactment of the opt-in rule. *See* http://www.marketratesinsight.com/Blog/post/2011/06/21/Reg-E-lowered-account-service-fees-by-2416-billion-since-enactment.aspx.

[56] Overdraft Rules, Part II: Interpreting the Ambiguous Guidance, Web Seminar, Banking Technology News, February 8, 2011.

[57] Fiserv Relationship Advance program description available at http://www.relationshipadvance.com/; *see also* Fiserv unveils Relationship Advance: *Full-service solution provides a safer, more cost-effective alternative to courtesy overdraft programs*, Press Release (Nov. 18, 2009), *available at* http://investors.fiserv.com/releasedetail.cfm?ReleaseID=425106; Jeff Horwitz, *Loan Product Catching On Has a Couple of Catches*, American Banker, Oct. 5, 2010.

[58] Ibid.

Bank payday loans have already caught on with several regional and national banks, who combined hold approximately 13% of total deposits at national banks and savings institutions.[59]

By calling their payday loan product a "direct deposit advance" or "checking account advance," banks attempt to differentiate it from other payday loans. But these distinctions are superficial at best and fiction at worst. Payday loans by banks have all the hallmark characteristic of those made by storefronts:

Comparison of Loan Features: Bank vs. Storefront Payday Loan		
	Bank Payday Loan	**Storefront Payday Loan**
Cost of typical loan	365 percent APR[60]	391 percent APR[61]
Repayment timing and amount	Due in full upon the customer's next deposit	Due in full at customer's next payday
Access to checking account funds for repayment	Bank repays itself automatically from the customer's next deposit, whether it is a paycheck or public benefits, like unemployment or Social Security	Lender has customer's post-dated check or electronic access to the customer's checking account
Underwriting borrower's ability to repay loan without funds provided by an additional payday loan	None	None

By making payday loans, banks undermine state law in states that do not permit payday lending by storefronts and federal law restricting payday loans made to military service members and their families.

Research that CRL plans to release in a report later this week demonstrates that bank payday lending leads to a debt trap, just as storefront payday lending does.[62] Our analysis finds that:

- **Bank payday loans are very expensive. At a cost of $10 per $100 (what most banks offering the product charge), they carry an annual percentage rate (ARP) of 365 percent based on the average loan term of 10 days,**

[59] Based on total bank and savings institutions deposits of $9.4 trillion for 2010, as reported by the FDIC *Statistics on Depository Institutions*
[60] Most banks offering payday loans charge $10 per $100 borrowed, and our research has found that the typical loan term is 10 days; this equates to a 365% APR.
[61] A loan at the typical cost of $15 per $100, repaid in two weeks, equates to 391% APR.
[62] For our analysis, we used data from a demographically-representative consumer panel tracked by Lightspeed Research Inc. Our analysis included data for 614 checking accounts whose transaction-level online and offline banking account activity was electronically captured.[62] The dataset contains 12 months of data on 184,221 transactions. We identified instances of bank payday loan repayments within 55 accounts, and analyzed these for loan term, repayments, and other relevant factors

- **"Short-term" bank payday loans often lead to a cycle of long-term indebtedness; on average, bank payday borrowers take out 16 loans per year and are in payday debt for 175 days per year,[63] and**
- **Nearly one-quarter of all bank payday borrowers are Social Security recipients, who are 2.6 times more likely to have used a bank payday loan than bank customers as a whole.**

Recognizing the problems associated with payday lending, the FDIC cautioned banks about the practice in 2005 and advised that the longest a bank should keep borrowers in payday debt was 90 days over the course of a year.[64] Similarly, the National Credit Union Administration recently advised that small loans more expensive than 18 percent APR (and even then only up to 28 percent APR) should be limited to three every six months (equating to six per year).[65] Banks making payday loans are keeping borrowers trapped in payday debt, *on average*, for nearly twice as long as the *maximum* length of time the FDIC advised, and in many cases for much longer.

Banks claim to offer consumers "protections" against long-term use, specifically cooling-off periods (breaks between payday loans) and payment plans.[66] But even the storefront payday industry's "Best Practices"[67] call for limits on rollovers and encourage lenders to offer the option of an extended payment plan; traditional payday lenders easily evade these "protections" and these practices have not significantly reduced the debt trap that payday lending creates.[68]

Similarly, banks restrict customers from "renewing" their payday loans but allow back-to-back transactions. They also provide for cooling-off periods, but only after a customer has been in debt for many months. It's not surprising, then, that bank payday borrowers end up indebted for a significant portion of the year. Indeed, an insider at one bank offering payday loans admitted, "Many [borrowers] fall into a recurring cycle of taking advances to pay off the previous advance taken."[69] Some banks offer payment plans but only in limited circumstances, such as when a customer has already taken out three payday loans, or in exchange for an additional $50 fee.

The OCC recently proposed weak guidance addressing the bank payday loans. It suggests safeguards like those noted above, including permitting installment plans (while still, presumably, allowing the "default" arrangement to be a short-term balloon repayment) and

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[63] Mean statistics are 10.68 days per loan and 16.4 loans per person.
[64] FDIC Financial Institution Letters, Guidelines for Payday Lending, FIL 14-2005, February 2005
[65] NCUA, Short-Term, Small Amount Loans, Final Rule, Sept. 2010, http://www.ncua.gov/GenInfo/BoardandAction/DraftBoardActions/2010/Sep/Item3b09-16-10.pdf.
[66] *See*, e.g., *Biggest banks stepping in to payday arena: The big guns' entry into payday lending may finally bring fringe financial product out of the shadows and into the financial mainstream, despite howls of protest from consumer groups and the risk of tighter regulation*, Star-Tribune (Sept. 6, 2009) and Lee Davidson, *Do banks overcharge?*, Deseret Morning News (Jan. 22, 2007).
[67] *See* Best Practices for the Payday Advance Industry, Community Financial Services Association, *available at* www.cfsa.net/industry_best_practices.html.
[68] See Uriah King and Leslie Parrish, *Springing the Debt Trap: Rate cap are only proven payday lending reform*, Center for Responsible Lending (Dec. 13, 2007). In the vast majority of states that ban renewals or refinancing of existing payday loans, the borrower, lacking the funds to both repay the loan and meet other obligations, simply repays one loan and immediately takes out another. This is often called a "back-to-back" transaction, and the effect it has on the borrower's finances is identical to a renewal.
[69] David Lazarus, *120% rate for Wells' Advances*, San Francisco Chronicle, Oct. 6, 2004.

requiring cooling off periods. We are concerned that this guidance risks to legitimize payday lending by banks, instead of sending the message it should be sending—that banks should not be making payday loans.

Need for CFPB Action

In both the areas of overdraft and payday loans made by depositories, federal action is needed. On the overdraft front, the Federal Reserve Board started the process by requiring opt-in to overdraft programs, but other consumer protection is necessary, as abuses still abound. With respect to bank payday loans, the OCC and the FRB have thus far allowed banks to trap customers in exorbitant, long-term debt. A regulator focused on consumers' interests is needed to address this problem before it becomes more pervasive. The CFPB should take early action to stop banks from making payday loans.

IV. Conclusion

In summary, a robust CFPB that provides oversight of consumer financial services is necessary to the stability of the marketplace and the economy. Congress enacted the CFPB in reaction to federal prudential regulators' failure to halt the unsustainable lending practices that caused the foreclosure crisis, which then sparked the broader financial crisis. Today, proposals to weaken the CFPB threaten the Bureau's effectiveness, which could return us to the days of the Wild West in which risky and abusive practices were allowed to flourish unchecked, and in some cases even encouraged, when short-term safety-and-soundness concerns prevailed over consumer protection and long-term system risk concerns. With the transfer date just a few days away, it is imperative that we remember the lessons learned about the causes of the financial crisis and support the CFPB, which will bring much needed fairness, equity and transparency to the marketplace and help stabilize the economy.

Thank you for the opportunity to testify. I look forward to answering your questions.

PREPARED STATEMENT OF MARCUS SCHAEFER

PRESIDENT AND CEO, TRULIANT FEDERAL CREDIT UNION

JULY 19, 2011

Introduction

Truliant Federal Credit Union appreciates the opportunity to provide input into the public policy dialog regarding the enhancement of consumer protection. We would like to thank Chairman Johnson, Ranking Member Shelby, Senator Hagan, and Members of the Committee for having us here today.

Our mission is to "Enhance the quality of life of our members and to become their preferred financial institution". Headquartered in Winston-Salem, NC, Truliant is a full service, not-for-profit financial cooperative with assets totaling approximately $1.5 billion. We serve over 180,000 member-owners and their families who work for over 900 Select Employer Groups, including Cook Medical, TIMCO Aviation Services, Klaussner Furniture, or who reside, work, or worship in our communities with a concentration in the Piedmont Triad area and in Charlotte, NC.

Truliant offers a full range of financial services including savings, checking, certificates, money market, IRAs, and Rainy Day Savings. Loan services include first mortgage and home equity, new and used auto, personal lines, and VISA credit cards. We offer small business services including member business and SBA loans. We provide state-of-the-art home banking and electronic bill payment programs, mobile access, and remote deposit capture. Through our Credit Union Service Organization, we offer financial planning and a very popular auto buying service.

As a member-owned financial institution, we can offer lower loan rates, higher savings rates, low (and often no) fees as we help member-owners execute sound financial plans for their future. Central to all our services is our emphasis on financial literacy education and counseling to our member-owners and for our communities. Over 55 percent of our member-owner households earn less than $45,000 per annum. Affordable, well-informed financial service access and delivery is key to our mission.

Truliant maintains an overarching commitment to improve our member-owners' lives by understanding and meeting their financial needs. This focus translates into our TruService culture. Our staff engages our member-owners to bring about real change and help them meet their long-term objectives—rather than the traditional product-pushing sales approach so prevalent in modern banking. For example, a benefit of low interest rates has allowed us to reposition hundreds of member-owners into lower cost mortgages and car loans.

Our operating principle is "Consumer BE Aware"; NOT Consumer Beware. Well before the financial crisis we instituted our Points of Differentiation that embody the spirit and practice of improving member-owner financial lives. For example:

- *We have not sold our credit card accounts to the large credit card issuers.*
- *We never offered an opt-out courtesy pay overdraft protection program.*
- *We don't advertise a car loan rate to member-owners unless the majority has the credit standing to qualify.*
- *We don't allow indirect auto loan car dealers to mark-up our rate.*
- *We help our member-owners become debt free on their primary residence by retirement.*
- *We support public policy that informs and educates the consumer on financial decisions while improving personal balance sheets.*

Our experience at Truliant is that consumers have been needlessly financially disadvantaged by a history of questionable practices and procedures by both mainstream and non-bank providers. Examples include opt-out overdraft protection, the sequence of clearing checking debits, extending credit to borrowers with terms they could not reasonably meet in ordinary circumstances, overly complex disclosure materials, and punitive credit card practices. These practices, which seem to be acceptable "gotchas" rather than consumer-focused services, argue for some balance toward better information sharing. Congress has addressed some of the more egregious practices, and heightened consumer awareness post-financial crisis may have driven providers to become more consumer-friendly in the near term.

Even with reforms including the Card Act, Regulation E rule changes, and the consumer protection initiatives of individual regulators, including the National Credit Union Administration, it make sense to have a regulator focused on consumer protection.

Clearly, controlling practices of non-bank providers, such as unregulated mortgage brokers, who in some cases were able to lure our member-owners into products that did not improve their financial lives, is needed. We noted 13 finance companies operating in the small manufacturing town of Asheboro, North Carolina, which lead to our extending services there. As we offered Volunteer Income Tax Assistance at Truliant this spring, I observed that many of the national tax preparers continued to offer high-priced, tax-refund anticipation loans. A consumer protection regulator could address these practices either directly or through a national initiative to improve financial literacy for consumers of varying degrees of education and experience. We all want our children to make better decisions for themselves.

Even for traditional financial service providers, we support clear language and visual presentations like the "Federal box" required of credit card disclosures. Warnings should be issued for overly complex consumer products that "trick" the consumer into overpaying for services or making decisions not generally in their long-term best interests (*e.g.,* variable rate mortgage that reset with payments beyond the likely ability to repay).

However, regulators should be mindful of the impact of mass-implementation of regulation on smaller financial institutions, particularly credit unions, where the cooperative structure has historically resulted in pro-consumer practices.

Seemingly small regulatory dictates can have a large impact on these institutions and ignore their "local knowledge" of how to best communicate with members. Larger institutions will benefit from economies of scale on a per account cost basis, further tipping the scale toward TBTF institutions.

There may be unintended consequences to consumer-friendly financial institutions as the "bad actors" are reined in by "one-size-fits-all" regulations. Implementation of the Card Act requiring that specific credit card statement language regarding late payments be used resulted in hundreds of panicked calls by Truliant member-owners who were not delinquent. The staff time required to explain the language mandated by the Federal Reserve could have gone to advising our member-owners on how to better build their financial foundation.

Conclusion

Truliant supports streamlining and simplifying existing overlapping regulation to improve consumer understanding while reducing cost to the financial institution that can be passed on to the member-owner. We welcome combining TILA and RESPA to improve usability by the consumer and financial institutions. Streamlining ECOA and FCRA could have similar benefits.

Truliant supports regulation that allows and promotes innovation in financial services that is also helpful to the consumer. The consumer protection regulator will need to carefully balance these two deliverables. Consumer protection is not a one-time fix, but an ongoing effort that will span different political landscapes. We support a balanced governance structure that would not make the regulator ineffectual or one that allows for public policy to become overly politicized. Thank you again for the invitation to speak on behalf of Truliant. I welcome your questions and discussion on this matter.

PREPARED STATEMENT OF ALBERT C. KELLY, JR.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER, SPIRITBANK,
ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION

JULY 19, 2011

Chairman Johnson, Ranking Member Shelby, and Members of the Committee, my name is Albert C. Kelly, Jr., Chairman and Chief Executive Officer, SpiritBank, a $1.3 billion bank headquartered in Bristow, Oklahoma. I am also the chairman-elect of the American Bankers Association. I appreciate the opportunity to present the views of the ABA on the new Bureau of Consumer Financial Protection (Bureau). The ABA represents banks of all sizes and charters and is the voice of the nation's $13 trillion banking industry and its two million employees. ABA is uniquely qualified to comment on the issues related to the Bureau. Not only will the agency's rule-making impact every bank—large and small—but ABA's membership represents the full range of banks over $10 billion that will be under direct supervision by this new agency.

SpiritBank has survived many economic ups and downs for 95 years. Our long tradition of service is not unique among banks. In fact, there are 2,735 banks—35 percent of the banking industry—that have been in business for more than a century; 4,937 banks—64 percent—have served their local communities for more than half a century. These numbers tell a dramatic story about the staying power of banks and their commitment to the communities they serve. It is a testament to the close attention to customer service.

My bank's focus, and those of my fellow bankers throughout the country, is on developing and maintaining long-term relationships with our customers. We cannot be successful without such a long-term philosophy and without treating our customers fairly.

We are very proud of our relationship with the people and small businesses we serve. They are, after all, our friends and neighbors. The success of SpiritBank is inextricably linked to the success of our customers and our community. Let me give you just a glimpse of SpiritBank's close ties with our community:

- We held $847 million in small business loans within our communities at year-end 2010. The new rigors of regulation and capital requirements have meant that we cannot continue to lend at this level.
- We funded 25,960 mortgage loans for families in 10 States last year, none subprime, for a total of $3.8 billion.
- We contributed over $550,000 dollars last year and our 330 employees have logged thousands of hours of service to schools, charitable organizations, and civic and community organizations throughout our area—in a year in which our investors saw no return to them. We far exceeded this amount in years when the economy has been good.
- We started an Entrepreneurial Spirit Award in one of our large communities, launching 20 to 30 companies each year at an annual cost to us of $100,000 each year.

The banking industry fully supports effective consumer protection. We believe that Americans are best served by a financially sound banking industry that safeguards customer deposits, lends those deposits responsibly, and processes payments efficiently. My bank's philosophy—shared by banks everywhere—has always been to treat our customers right and do whatever we can to make sure that they understand the terms of the loans they are taking on and their obligations to us. Traditional FDIC-insured banks—more than any other financial institution class—are dedicated to delivering consumer financial services right the first time. Not only do we have the compliance programs and top-down culture to prove it, we are required to have the financial wherewithal—in terms of capital, liquidity and asset quality—to be there when our customers need us.

Fair service to our banking customers is inseparable from sound management of our banking business. Yet despite this axiom, the Dodd-Frank Act erected a Bureau that divides consumer protection regulation from safety and soundness supervision. Therefore, it is critical that improvements be made to assure this new Bureau is accountable to the fundamentals of safe and sound operation, to the gaps in regulating non-banks that motivated financial reform, and to the principles of consistent regulatory standards consistently applied.

There are several features of the Bureau that make improved accountability imperative. In addition to the weakening of any connection between the Bureau's mission and safety and soundness concerns, Dodd-Frank gave the Bureau expansive new quasi-legislative powers and discretion to re-write the rules of the consumer financial services industry based on its own initiative and conclusions about the needs of consumers. The prerogative of Congress to decide the direction and parameters of the consumer financial product market has essentially been delegated to the Bureau. The resulting practically boundless grant of agency discretion is exacerbated by giving the head of the Bureau ***sole*** authority to make decisions that could fundamentally alter the financial choices available to customers.

Furthermore, the proliferation and fragmentation of enforcement authority that Dodd-Frank has distributed among the Attorneys General in every State and the prudential regulators unleashes countless competing interpretations and second-guessing of the supposed baseline “rules of the market.” This will result in complicating and conflicting standards.

At risk is the entire body of rules that has governed the development, design, sales, marketing, and disclosure of all financial products; they are subject to change under the Bureau, and could change dramatically in many instances. When developing and offering products, firms rely on the basic rules of the road, knowing that they are subject to careful changes from time-to-time. This uncertainty can cause firms to pull back from developing new products and new delivery systems. It also makes banks think twice about various types of lending if they are uncertain what the rules will be when they try to collect the loan a few years out. This problem should not be underestimated.

For all these reasons and others, it is ABA's first priority to improve the accountability of the Bureau. Establishing accountability supersedes other important priorities regarding the Bureau, including ensuring appropriate bank-like supervision of non-banks for consumer protection. During consideration of the legislative proposals that became the Dodd-Frank Act in the last Congress, ABA recommended provisions designed to increase the accountability of the CFBP because we were greatly concerned about the concentration of authority in a single director of this agency. Our concern was focused on the fact that the Bureau has authority over already supervised insured depositories as well as unsupervised or lightly supervised non-banks. Our concern remains the same. We urge the Congress to pass statutory provisions that ensure such accountability before the Bureau is established with a single director.

To restore the necessary accountability of the Bureau, ABA offers several recommendations:

- Strengthen accountability by making meaningful structural changes;
- Reinforce the focus of the Bureau's authority on the regulatory gaps; and
- Improve consistency in the application of consumer protection standards.

I will address each of these broad suggestions in turn and propose specific steps that Congress should consider to address the concerns about the Bureau's accountability. Before that, though, I think it is very important to dispel a myth that continues to color the debate on the Bureau: that community banks like mine are exempt from the new Bureau. ***Community banks are not exempt.*** All banks—***large and small***—will be required to comply with rules and regulations set by the Bureau, including rules that identify what the Bureau considers to be "unfair, deceptive, or abusive." Moreover, the Bureau can require community banks to submit whatever information it decides it "needs."

The Bureau will have direct supervisory authority for consumer compliance of larger banks (with assets greater than $10 billion)—which adds another layer of regulation and supervision—and can join the prudential regulator by doubling up during any small-bank exam at the Bureau's sole discretion. It is also true that bank regulators will examine smaller banks for compliance at least as aggressively as the Bureau would do independently. In fact, the FDIC has created a whole new division to implement the rules promulgated by the new Bureau, as well as its own prescriptive supervisory expectations for laws beyond FDIC's rulemaking powers. Thus, the new legislation will result in new compliance burdens for community banks and a new regulator looking over our shoulders.

This is no small matter. The CFPB, while significant, is only one change among hundreds that will adversely affect the banking industry and the communities we serve. Already there are 2,762 pages of proposed regulations and 607 pages of final regulations—and this is before the CFBP undertakes any new changes or rulemakings. It is important to understand that our bank, indeed, any small business, can only bear so much. Most small banks do not have the resources to easily manage the flood of new rules.

The totality of all the changes, brought about by Dodd-Frank, including those expected under the Bureau, and the excessive regulatory second-guessing by the regulators has consequences for our communities. Higher costs, restrictions on sources of income, limits on new sources of capital, and excessive regulatory pressure, all make it harder to meet the needs of our communities. Jobs and local economic growth will slow as these impediments inevitably reduce the credit that can be provided and the cost of credit that is supplied. Fewer loans means fewer jobs. Access to credit will be limited, leaving many promising ideas from entrepreneurs without funding. Capital moves to other industries, further limiting the ability of banks to grow. Since banks and communities grow together, the restrictions that limit one necessarily limit the other.

Let me now turn to specific recommendations for improvements and ABA's thoughts on the several new legislative proposals that are under consideration.

I. First Priority: Strengthen Accountability with Meaningful Structural Changes

ABA believes that a board or commission structure is appropriate to address the unfettered authority of the Bureau's director to impose new rules. Having only one Senate-confirmed director vests too much power in one person and lacks any effective checks and balances. A board or commission would help to provide accountability and balance. It would also broaden the perspective on any rulemaking and enforcement activity of the Bureau, and would provide needed balance and appropriate checks in the exercise of the Bureau's authority. It will facilitate continuity of the organization and enhance predictability about rulemaking over time.

ABA believes that the board or commission should include members with consumer finance business experience and direct safety and soundness regulatory expertise. Such expertise provides an important and necessary perspective as standards are set and enforcement activities undertaken. Such an important feature will also improve accountability and help redress the separation between consumer protection and sound financial management.

ABA also urges Congress to consider requiring one of the seats in the board or commission be filled with the recently created, statutorily mandated position of the Vice-Chairman for Supervision of the Federal Reserve Board. We believe that the inclusion of the Vice-Chair for Supervision provides necessary and current safety and soundness experience that directly addresses a pivotal deficiency of the existing structure. The Vice-Chair for Supervision is a unique official who has oversight responsibility both for large financial holding companies (which include the nation's biggest banks and credit card issuers) and State-chartered community banks that are Federal Reserve members. This broad responsibility and expertise would be invaluable to achieving the missing accountability for safety and soundness that the current structure lacks.

Another fundamental structural flaw of the Bureau's structure is that ***only*** the Director is appointed by the President and approved by the Senate. A board or commission structure corrects this shortcoming.

ABA also supports changing the voting standard for the Financial Stability Oversight Council's (FSOC) review of Bureau rulemaking ***to a simple majority*** rather than a two-thirds vote. It should clearly be sufficient to set aside a Bureau rule if a simple majority of the nation's top regulators believes the Bureau has acted in a manner that adversely impacts the safety and soundness of the American banking or financial system. The stakes are too high to let one agency's rule create such significant risk. The very purpose of the FSOC was to avoid problems that could lead to risks that threaten the economy. To ignore the majority viewpoint of those with this responsibility is completely counter to the mission of this council. Congress should erase the super-majority requirement for FSOC authority set in Dodd-Frank and replace it with a simple majority requirement.

In addition, ABA believes that the standard for the FSOC review of Bureau actions—systemic risk—is also flawed. Much harm can be inflicted that would impair whole subsets of legitimate market players without necessarily rising to the level of a banking, let alone a financial, system risk. For example, a Bureau rule that severely threatens the viability of community banks will not create a system risk. But each bank that disappears from the community makes that community poorer. Customers that have been served by local banks for decades may face fewer choices, less access to credit, and higher costs. Will the FSOC really conclude that the loss of large numbers of community banks rises to the level that demands a systemic risk ruling? ABA strongly urges Congress to re-calibrate the review standard by which the FSOC may act in setting aside a Bureau rule so that action may take place on less than system-wide impacts or risks.

Furthermore, the FSOC review process for Bureau rules is administratively cumbersome and complicated, filled with timing pitfalls. For example, a petition must be filed that attests to objecting agency "good faith" within 10 days of rule publication; it must be transmitted "contemporaneously" to Congressional committees; a stay of 90 days duration may be applied for, but without a stay the petition will be deemed denied if the FSOC does not issue a decision in 45 days. As constructed, this convoluted process represents precisely the kind of bureaucracy that gives government bureaus a bad name. ABA urges Congress to fix this review process so that there is at least some reasonable expectation that it can be successfully invoked.

II. Reinforce the Focus of the Bureau's Authority on Regulatory Gaps

Even the strongest proponents of the Bureau acknowledge the fact that traditional banks were not the cause of the financial crisis. Rather, unsupervised non-bank lenders and unregulated packagers of collateralized mortgage obligations (CMOs) were allowed to take excessive risks in spite of existing laws that could have stemmed the tide of corrosive market conduct by non-depositories. The system failed to enforce laws—***already on the books***—against predatory practices by many of those firms and it failed to bring market discipline to bear on underwriting standards against which bankers were hard pressed to compete. Yet here we are, the surviving bankers, facing a new bureaucracy charged with making sense of the often conflicting, never intuitive, and always burdensome compliance obligations.

As we noted above, establishing accountability is the number one priority. Once that goal is achieved, the Bureau must be held accountable for directing its resources to the glaring gap in regulatory oversight—a failure to supervise and pursue available enforcement remedies against ***non-bank*** lenders committing predatory practices or other consumer protection violations. To this end, ABA sees value in Section 1016(c)(6) of the Dodd-Frank Act requiring the Bureau to report on actions taken "with respect to covered persons which are not credit unions or depository institutions." In addition, we welcome current efforts to define the Bureau's non-bank supervisory scope as it prepares for the future exercise of that supervisory authority.

ABA believes that the best way to keep the Bureau accountable to the Dodd-Frank objectives in section 1021(b) would have been to have the Bureau concentrate solely on rationalizing the laws and powers already on the books before passing any new authority. Unfortunately, in the process of transferring existing unfair and deceptive acts or practices authority, the unwarranted addition of "abusive" was inserted.

This addition opens wide all manner of after-the-fact excuses for rewriting the conditions of transactions entered into by customers who had complete information and competitive alternatives. It is an end run around the well-established statutory criteria that Congress and the courts have defined for conduct that is either deceptive or unfair. ABA strongly urges the Congress to eliminate the term "abusive" from the Bureau's prohibitions. This is the most effective method of keeping the Bureau focused on and accountable to the task of reforming the more-than-adequate authorities it has inherited from its predecessor regulators and shaping those into simpler, more effective, and less burdensome consumer protections.

III. Improve Consistency in the Application of Consumer Protection Standards

As discussed above in detail, the Bureau represents an unaccountable regulatory entity. While this alone is bad enough and should be addressed, the problem is magnified by other authorities granted in Dodd-Frank. The Act gives license to pile on additional State law requirements and gives unfettered authority to State Attorneys General and prudential regulators—acting on their own initiative—to enforce Bureau statutory authorities and rules. Both of these expansive powers erode Bureau accountability for achieving uniform rules for all consumers to be protected by and all providers to abide by. Even if one can make the Bureau answerable for its market defining rules, neither Congress, nor bankers nor customers can rely on such rules remaining intact in the States where they all reside. This broad delegation of legislative license, interpretive power and prosecutorial discretion—without adequate check by either the Bureau or other Federal banking agencies—exposes all banks to uncertain market expectations, compounded compliance obligations, and potentially crippling litigation risk.

Accordingly, ABA recommends that Congress consider three possible constraints on these threats to consistent consumer protection standards consistently applied:

- Adopt statutory language prohibiting States from imposing additional consumer protection requirements without meeting the same cost benefit, credit access and burden reduction objectives that Dodd-Frank imposes on the Bureau (and demonstrated with the same level of data analysis expected of the Bureau).
- Adopt statutory language precluding prudential regulators or enforcement authorities from establishing rules, guidance, supervisory expectations or prosecutorial actions that extend obligations with respect to consumer financial products or services beyond requirements contained in rules of the Bureau.
- Adopt statutory language limiting State Attorneys General from seeking remedies of any conduct by a covered person occurring prior to the last exam report date of any exam by the Bureau or a prudential regulator.

The premise of the Bureau of Consumer Financial Protection was that it would result in a single set of rules of the road for consumers, industry and investors to abide by for the benefit of all. If we are to hold the Bureau accountable to this premise, we must hold accountable all those who derive authority from its existence to abide by the same rules of the road. To do otherwise—by allowing new rules to be written or applying new interpretations each time a State border is crossed—would completely undermine the reliance of all citizens on the Bureau's rules.

Conclusion

The banking industry fully supports effective consumer protection. Traditional FDIC-insured banks have a long history of delivering consumer financial services right the first time and banks have the compliance and top-down culture to prove it.

It is an inescapable fact that fair service to our banking customers is inseparable from sound management of our banking business. Yet despite this axiom, the Dodd-Frank Act erected a Bureau that divides consumer protection regulation from safety and soundness supervision. It is for this reason that Congress should act to enhance the accountability of the Bureau by dealing with the problems brought about by the extensive new powers of the agency, the unfettered authority of the Director to impose new rules, the separation of consumer protection from financial institution safety and soundness, the gaps in regulating non-banks, and the expanded and unaccountable enforcement authority of prudential regulators and State attorneys general.

My bank's philosophy—shared by banks all across this country—has always been to treat our customers right and do whatever we can to make sure that they understand the terms of the loans they are taking on and their obligations to us. We will continue to do this, but now there will be many new hurdles that we will have to jump to serve our customers' most basic needs that will inevitably add cost, time, and hassle for my customers.

Banks are working hard every day to make credit and financial services available. Those efforts will be made more difficult by the hundreds of new regulations expected from the Dodd-Frank Act. I worry about how my bank will handle all the new compliance obligations; I cannot imagine how the median size bank with $156 million in assets and 37 employees can handle this truckload of new compliance obligations. Even more troubling is what it means for my community. The more time bank personnel devotes to parsing regulatory requirements, the less time they can devote to the financial and credit needs of bank customers. Thus, it is critically important that

Congress be vigilant in overseeing the regulatory actions of the Bureau and other rules stemming from the Dodd-Frank Act to assure they do not restrict access to responsive financial products by responsible American families.

PREPARED STATEMENT OF LYNN DRYSDALE

MANAGING ATTORNEY, CONSUMER UNIT, JACKSONVILLE AREA LEGAL AID, INC.

JULY 19, 2011

Introduction

Chairman Johnson, Ranking Member Shelby and Members of the Committee, thank you for the opportunity to bring the consumer perspective to the Enhanced Consumer Finance Protections: After the Financial Crisis. Specifically I hope to illustrate just a small part of the problems consumers face which renders the Consumer Finance Protection Bureau ("the CFPB") an essential tool to level the playing field between consumers and businesses governed by the authority of the Bureau. My testimony represents a snapshot of the problematic experiences of consumers, particularly older Americans and members of the armed services I represent in Florida. I will share with you stories of individuals who have suffered because of our failed financial regulatory system. Their stories demonstrate a need for a strong independent Consumer Financial Protection Bureau that has both rule writing and enforcement power over banks and non-banks that provide financial products.[1] I have testified before the Federal Trade Commission, the Federal Reserve Board and before this Committee in 2006 when I spoke in support of the *Department of Defense Report on Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents.* The Senate passed the Talent-Nelson amendment to the John Warner Defense Authorization Act of 2007 in 2006 to prohibit predatory practices and rein in the fees charged in several types of consumer finance transactions.

Today I will use the stories of the consumers I work for who could be assisted by the Bureau and recommend the full support of this Committee for the CFPB.

Why the Consumer Finance Protection Bureau is Important

Times are difficult for many consumers, including consumers who prior to the financial crisis never considered themselves vulnerable to illegal, deceptive or unfair practices of finance companies, lenders, debt collectors or credit reporting companies. This new class of targeted consumers is added to the older Americans and members of the armed services who have historically been targeted for abuse. Existing bank regulators have clearly failed to design and enforce fair rules of the road for credit, leaving these consumers exposed to tricks and traps on high cost loans and abusive mortgages that cost families their homes. With so many consumers

[1] Since 1988, I have been a consumer protection attorney with Jacksonville Area Legal Aid, Inc. and represent low-income consumers in the greater Northeast Florida area. I am a co-chair of the Board of Directors of the National Association of Consumer Advocates, chair of the Florida Bar Association's Consumer Protection Law Committee, teach mortgage foreclosure, debt collection and motor vehicle sales and financing litigation to attorneys all over Florida and nationwide, including the Judge Advocates in Newport News, Rhode Island. I am also an adjunct Consumer Law professor at the University of Florida College of Law.

being targeted and access to the courts being diminished it is important that a strong, unified Bureau focused on protecting consumers.

The CFPB should have broad authority to write rules, supervise a wide variety of financial institutions, and enforce Federal consumer protection laws—all with the ultimate goal of ensuring a more fair and equitable financial playing field for consumers.

As consumer advocates have previously shared with this Committee, the idea of a Federal consumer protection agency focused on credit and payment products has gained broad and high-profile support because it targets the most significant underlying causes of the massive regulatory failures that occurred in recent years. Federal agencies did not make protecting consumers their top priority; ignored many festering problems that grew worse over time; when acting to protect consumers (and they often did not), the process was cumbersome and time-consuming. In the end, agencies often did not become involved to stop some abusive lending practices until it was too late. Finally, regulators were not truly independent of the influence of the financial institutions they regulated.[2]

In my testimony, I will highlight three main points:

1. The range of consumers being negatively affected by aggressive lenders with a wide variety of high cost and risky consumer financial products has grown exponentially during the financial crisis.
2. Victimized consumers are not being protected by most States, either because high cost lenders have crafted products which ostensibly take them out of the regulatory power of the State small loan laws and claim that State credit laws do not apply to them. Also, lenders are moving to the Internet to provide illegal products behind the veil of secrecy, putting them beyond the grasp of many State regulators with diminishing resources to pursue them. Many loan products on the market today are grossly one-sided and include unilateral, mandatory arbitration clauses utilized to deprive consumers of their day in court and to limit their remedies.
3. Because of the restrictions on availability of new credit, creditors and debt collectors are stepping up efforts to collect debt through illegal, unfair or deceptive means in my clients' stories.

Range of Consumers Hurt by Predatory Lending Increased During Financial Crisis

American consumers did not create the financial crisis with products such as no document mortgage loans, triple-digit interest rate loans secured by automatic access to a consumer's bank account or motor vehicle, and spurious open-ended credit. Nor did they profit from steering homeowners who qualified for safe, affordable mortgages into exploding adjustable rate loans. But consumers are paying the price of unfair and irresponsible financial products through record foreclosures, rising unemployment rates, abusive debt collection practices and a struggling economy. Even in good economic conditions, consumers are always under fire, whether it's from lending scams or deceptive marketing. The need for effective consumer protection regulation and enforcement is always there. However, the current financial crisis seems to emphasize this need even more as it has become a breeding ground for increased deceptive and abusive practices by lenders.

Recent Consumer Protection Laws, particularly those intended to protect Active Duty Servicemembers and their Families are being ignored or coverage is being evaded by carefully crafted loan products.

Military servicemembers are particularly affected by these deceptive and abusive practices. After President Bush signed the Military Lending Act (MLA), implemented by rules adopted by the Department of Defense, many consumer advocates were encouraged that those fighting for our country would be protected from abusive lending and collection activities. Unfortunately, lenders tweaked their product designs to get around the DOD covered credit definitions or are ignoring the law and are still charging triple digit interest rates and calling with threats of court martial and imprisonment for failure to pay these exorbitant terms. For example, I mentioned a servicemember in my testimony 5 years ago who was being charged 1,000 percent interest rates. He spent 5 years faithfully attempting to pay off $10,000

[2] For additional background on why there is a need for a strong Consumer Finance Protection see Testimony of Travis Plunkett, Legislative Director, Consumer Federation of America, before the Senate Committee on Banking, Housing and Urban Affairs, (July 14, 2009) available at: *http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.Testimony&Hearing_ID=9a56da23-60cb-4fd0-ac04-f94ead7d1859&Witness_ID=18d80e15-8970-49d1-8867-54b81d389272.*

worth of payday loan debt incurred as a result of his wife's illness and still owed $12,000. The lender kept the servicemember paying with threats of court martial and imprisonment. A year after the MLA became law reducing the interest rate caps to 36 percent for new loans he was still getting threats of court martial, loss of security clearance and/or imprisonment despite the prohibitions in State and Federal consumer collection protection laws which have historically prohibited this conduct for all debt collectors.

Even in connection with new loans to active duty servicemembers, these same lenders are still putting borrowers' bank accounts at risk and charging triple digit interest rates well in excess of the 36 percent interest rate cap and are still threatening criminal prosecution. This and other lenders provide their loans through the Internet to avoid any type of State or Federal regulation. They are also taking borrowers' wages before they obtain judgments against the borrowers by requiring its borrowers to sign documents allowing an assignment of wages in violation of 16 C.F.R. § 444.2(a)(3). This company and many others just like it avoid State credit protection laws, State and Federal debt collection laws and FTC regulations by operating on the Internet. These companies also avoid the consequences of their illegal behavior by including unilateral, mandatory arbitration clauses in their contract.

Other payday lenders get around the ban on loans secured by checks or automatic access to a borrower's bank account as well as interest rate caps imposed by the MLA and State credit protection laws by crafting their loan products as open-ended transactions or by setting their loan terms at greater than 180 days. These lenders charge triple-digit interest rates, require electronic access to borrowers' bank accounts as security for the loan, and claim they do not have to provide the cost of credit information required by the Federal Truth in Lending Act, 15 U.S.C. 1601, *et seq.* in payday loans by merely pretending the borrower has the right to use the loan like a line of credit when in fact no further sums will be provided or by setting the loan term for in excess of 181 days rendering the loan outside of the protections of the MLA.

An example of a loan product targeted to servicemembers is an installment loan with a loan company with whom I've worked. It stated its interest rate was 32.77 percent which would appear to be within the MLA cap and many State small loan rate caps. However, the lender set the loan term to fall outside the MLA protections and is, therefore, ostensibly not covered by the MLA. The stated interest rate also did not include charges for a required insurance product which if included in the interest rate calculation would bring the rate to 66 percent rendering the loan criminally usurious in Florida where many borrowers are located. In addition to using the loan term to avoid the MLA interest rate cap, this particular lender claimed to be a subsidiary of a national bank.

Under Dodd-Frank, this type of bank subsidiary would not be able to use the National Banking Act to evade State law consumer protection laws. Dodd-Frank ends preemption for bank operating subsidiaries by reversing *Watters v. Wachovia Bank*[3] and the regulation Watters upheld. This "anti-preemption" provision of Dodd-Frank is important to all consumers, including those who are not covered by the MLA such as military veterans and older Americans.[4] National Banks and their subsidiaries can no longer successfully claim to be exempt from application of State consumer protection laws by hiding behind the National Banking Act, 12 U.S.C. § 85.

Automobile title loans were also one of the problematic products listed in the *Department of Defense Report on Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents*. Now even after the passage of the MLA and in violation of State law, lenders still provide triple-digit rate automobile title loans and secure loans with the title to the borrower's vehicle, a practice prohibited by the Military Lending Act. A family's vehicle is probably their most valuable asset and this type of loan puts the vehicle at serious and unnecessary risk of repossession for a loan a fraction of the value of the vehicle owned by the borrower.

For example, Mr. B used the free and clear title to his truck as security for a $2,200 loan. The stated interest rate is 24 percent but he is charged $900.00, more than a third of the value of the loan for a "collateral damage waiver." This fee is kept by the lender, is required to get the loan and provides no benefit to the servicemember who is paying $4,712.88 for a $2,200.00 loan. When he missed a payment, the truck was repossessed meaning he lost his truck and the equity he had in the truck. The lender will only provide a loan in an amount equal to a third to a fourth of the value of the truck so the lender received months of payments plus the excess equity in the truck. The lender avoided the application of the MLA by

[3] 550 U.S. 1 (2007).

[4] Dodd-Frank §§ 1044, 1046.

extending the term of the loan and avoided State lender laws by illegally disguising interest as the fake insurance product.

Another type of loan highlights the ineffectiveness of the present regulatory structure and the need to enforce Federal Truth in Lending and VA pay and pension laws intended to protect Veterans who have served our country. Companies have been stealing veterans' pensions through high cost loans branded as veterans' pensions loans. These like other loans targeted to servicemembers and veterans have names that make them appear to be affiliated or approved by the military and have flags and military symbols in their advertisements. A veteran is offered the right to "sell" his or her right to receive future benefits. These loans are structured as sales to avoid Truth in Lending and cost of credit laws and to hide the true costs of the loans which can run into the triple digits. Therefore, veterans lose the right to receive their pensions and pay exorbitant interest rates for the right.

The Bureau will Provide a Unified and Focused Entity To Address the Many Facets of the Mortgage Foreclosure Crisis

Much has been said about the mortgage foreclosure crisis. These issues have many layers. I've heard story after story of active duty servicemembers losing their homes while they are stationed overseas and State-side families who are struggling with the threat and reality of eminent foreclosure while their spouses are overseas. For example, we have received requests for assistance from military families who are being evicted from their homes by companies that have bought their home at foreclosure sales when the family did not even know their home was in foreclosure.

I know Congress is attuned to these issues based upon a recent forum relating to illegal foreclosures against U.S. Servicemembers and their families held by the Senate Committee on Commerce, Science and Transportation and the House Committee on Oversight and Government Reform on July 12, 2011. It is not uncommon for our office to hear of stories like those of Army National Guard Warrant Officer Charles Pickett and Army Captain Kenneth Gonzales. Foreclosures are proceeding when borrowers are not in default and without their knowledge while they are deployed for service to our country. The Director of the Office of Servicemember Affairs, Hollister K. Petraeus spoke of the importance of the CFPB role in preventing these abuses. Our office sees real life examples of servicemembers fighting insurgents in Afghanistan and fighting Wells Fargo in an illegal foreclosure in the States or coming home to find their homes foreclosed upon and boarded up. Members of the military are supposed to receive special notice and delay of the foreclosure proceedings but many of them never receive this notice. It is not clear which agency if any is addressing these loan servicing issues harming our most deserving consumers.

I have many veteran clients with FHA and VA loans who are entitled to specific pre-foreclosure default servicing before a mortgage foreclosure is filed. Borrowers who have paid a premium for an FHA loan or served our country in order to be eligible for a VA loan do not get the assistance required by Federal law and their mortgage loan contracts to help them avoid foreclosure. For example, I represent an older American widow with a VA loan she and her deceased Veteran husband obtained. Instead of working with her, the company servicing her loan sent a blizzard of form letters and either ignored her request for a loan modification or continuously lost her paperwork when she tried to follow the loss mitigation procedures. Her loan was sent to a law firm to foreclose. When the servicer did not have the assignments needed to foreclose, their attorney created and signed a fake assignment of mortgage to make it appear the company owned the loan when it did not. In fact the servicer did not own the loan until more than a year after the fake assignment was prepared and signed. This widow will lose her home as a result of the servicer's failure to comply with VA requirements contained in the note and mortgage and based upon fake documents. This also is the experience of a veteran who has been receiving the "lost document" run around for almost 2 years in an effort to utilize the VA protections to which he is entitled because of his service of our country.

This failure to evaluate loan modification documents or to continuously lose the documents is one of the main reasons why the HAMP program has not had the intended effect of helping all consumers save their homes. The use of fake documents is also rampant. I have clients who are being sued by two different companies represented by two different law firms for the same loan. Both companies cannot own her loan but each continues to add foreclosure related fees to the amounts she owes. Servicers also have no incentive to modify loans because they are being paid in full by the loan guarantors Fannie Mae, Freddie Mac and Ginnie Mae. In other words our children, when they reach adulthood, will be paying off the debt created by the same entities that created the mortgage aspect of the financial crisis. These entities are being paid up front all the expense of all tax payers while homeowners are losing their homes, neighborhoods are deteriorating and homes sit vacant by the thousands further depressing the market.

Because loan servicers are not complying with the loss mitigation requirements imposed by the Servicemember Civil Relief Act and with FHA, VA, Fannie Mae, Freddie Mac loans and loans held or serviced by entitles which received TARP funds, borrowers in trouble are turning to foreclosure assistance companies that offer to help keep consumers from losing their homes. These companies promise to stop foreclosures and collect hundreds if not thousands of dollars from homeowners already deep in debt. This money could be going toward the delinquency in the home payments but instead is taken by these foreclosure relief companies who pocket the money and move on to the next state of victims. The Federal Trade Commission has already said they will not be pursuing enforcement actions against these companies. Because of tight State budgets and the interstate nature of these companies, State regulators do not have the resources to address these companies preying on foreclosure victims.

The Bureau is Needed To Address Increased Illegal Debt Collection Activity

I have also noticed an increase in aggressive debt collection tactics. I have several clients who are being sued by debt buyers for debt that has already been repaid, was forgiven through litigation or discharged in bankruptcy. Because credit is more difficult to obtain, debt collectors are being more aggressive in trying to collect old debt.

The creation of false documents to support debt collection is not limited to mortgage foreclosure. It is also common, if not the norm, for debt buyers to create fake documents because they do not have the paperwork to prove they own the debt or the amounts owed. When they buy the debt, they only pay pennies on the dollar and they do not get the paperwork needed to back up their claims.

Not Only Are Our Homes Not Safe From Big Banks but Door-to-Door Sales and Finance Companies Seek us out for Illegal Products

Door-to-Door sales provides the delivery system for another form of false open-ended credit. The sales staff canvas neighborhoods including those whose demographics are primarily older American consumers, neighbors surrounding military bases and other vulnerable consumers to offer products such as water purifying equipment, solar panels and security systems. They offer on-the-spot financing. Sales staff use scripts and have a specialized routine most likely to trick homeowners into buying products financed by false open-ended credit. For example, I have represented over a dozen older American homeowners. Each time the story is the same, the salesman shows up at their house with a water testing kit, draws some tap water, places a tablet in the water and watches with the older American homeowner as their water clouds up. Then the salesman adds another tablet and the water magically clears. The salesman then explains the cloudiness means the homeowners' water is dangerous to their health and that they can save their health and save money with water conditioned with their system. They usually will not leave until the consumer signs on the bottom line, spending hours at a time at the consumer's home.

The Truth in Lending cost of credit disclosures are not provided until after the equipment is installed. It is not until the disclosures are provided that the homeowner learns the payments are much more than they can afford. If there is a default on the loan, the lender sues the older American homeowner in a city which is a 4-hour drive from the consumer's home. They cannot afford to travel to court or to hire an attorney and a judgment is entered against them.

These companies also target young military families like clients of mine with little children and tell them their water is dangerous and will cause cancer if not treated. Salesmen refuse to leave until the contract is signed, staying through the consumers' dinnertime while their children want dinner, install the equipment and then days later provide the financing contracts. The salesman promised the interest rate would be really low because of their good credit and when the contract is presented; after the equipment is installed the interest rate is 17 percent which was significantly higher than the low rate they were promised because of their good credit score. The airman has to pay because he knows if he does not he may lose his security clearance has to pay even though the equipment makes their water taste bad and leaves their clothes yellow.

Why We Need a Consumer Financial Protection Bureau

Unfortunately, there are too many consumer victim stories to tell and this is why we need a strong Consumer Financial Protection Bureau (CFPB) with full authority to protect consumers, particularly our most vulnerable members of society. The

CFPB will help protect consumers from many of the fraudulent, abusive, and deceptive practices I have shared with you this morning. Notably:

- *The CFPB will put teeth into predatory lending laws:*
  - Predatory lenders often get away with their deceptive practices because the Federal Trade Commission (FTC), which regulates debt collectors and mortgage brokers, has very few attorneys devoted to consumer protection and lacks basic tools such as rulemaking and oversight/monitoring authority. In the past 5 years, the FTC has filed only one case against a mortgage broker. The CFPB will strengthen the enforcement and regulation of laws such as the Truth in Lending Act.
  - The Federal Deposit Insurance Corporation (FDIC) and Federal Reserve Board regulate predatory lending practices, but both are also charged with promoting the stability of the banks that make loans. By avoiding this kind of conflict of interest, the CFPB would increase the likelihood of fraudsters getting caught.
- *The CFPB will combat abusive debt collectors and debt buyers:*
  - Debt collectors and buyers also ignore the law without penalty. Despite nearly 500,000 complaints under the Fair Debt Collection Practices Act (FDCPA) in the past 5 years, the FTC has filed only 8 cases against debt collectors. The CFPB would devote more resources and help strengthen enforcement, so that debt collectors no longer think they can get away with shady practices that they know are illegal.
  - Currently, no Federal law or regulation requires debt buyers to keep records of what they are buying or even to possess original documentation. By consolidating and streamlining rulemaking and enforcement of consumer protection laws, the CFPB could identify this and similar loopholes in consumer protections and promote new, necessary protections.

The CFPB's launch is only a few days away; it vital that we provide them with the necessary support to be a successful consumer watchdog agency. Thank you for the opportunity to testify today. If you have any questions or comments regarding this testimony, please feel free to contact me.

Statement
of the
U.S. Chamber
of Commerce

ON: **"Enhanced Consumer Financial Protection After the Financial Crisis"**

TO: U.S. Senate Committee on Banking, Housing, and Urban Affairs

DATE: **July 19, 2011**

The U.S. Chamber of Commerce is the world's largest business federation, representing the interests of more than 3 million businesses of all sizes, sectors, and regions, as well as state and local chambers and industry associations.

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 115 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.

Mr. Chairman, Ranking Member Shelby, and members of the Committee:

My name is Andrew Pincus, and I am a partner in the law firm Mayer Brown LLP. Thank you for the opportunity to testify before the Committee today on behalf of the U.S. Chamber of Commerce and the hundreds of thousands of businesses that the Chamber represents.

The Chamber strongly supports sound consumer protection regulation that deters and punishes financial fraud and predation and requires that consumers receive clear, concise, and accurate disclosures about financial products. Everyone, businesses as well as consumers, benefits from a marketplace free of fraud and other deceptive and exploitative practices.

At the same time, consumer protection regulation must be efficient and focused, furthering these goals while avoiding duplicative and unjustified regulatory burdens. Unjustified burdens harm all Americans by diverting resources essential to fueling economic growth and, perhaps even more importantly, by preventing small businesses from obtaining the credit they need to expand—and create the new jobs that our economy so desperately needs.

We are heartened that the government officials working to organize the Bureau appear to endorse these goals, but good intentions by themselves do not ensure good results. The ability of a regulatory agency to carry out its mission successfully is influenced by—among other things—its organizational structure; its ability to coordinate effectively with other agencies operating in related areas; and its ability to maintain over the long term a consistent, evidence-driven approach to regulatory and enforcement issues.

The Bureau's unique and unprecedented structure deviates radically from the fundamental principles of accountability and checks and balances that have been a basic feature of our Federal Government for the past 224 years. We have significant concerns that this novel structure will make it impossible for the Bureau to carry out its mission successfully. Indeed, even though the Bureau has not yet come into existence, decisions already appear to be skewed toward inefficient and unjustified approaches as a result of the agency's structural defects.

My testimony today makes two basic points:

- The Bureau's current structure confers on its Director unprecedented unchecked power of extraordinary breadth, far beyond that wielded by any other federal regulator of individuals and businesses.

  Arguments that the Director's authority is the same or similar to the power of other federal agency heads are simply false: there is no other agency head who exercises sole decisionmaking authority with regard to rulemaking, enforcement and supervision actions, and every other matter—and need not obtain the concurrence of colleagues on a multi-member commission; ***and*** who also has policy independence from the President such that he or she may be removed from office only "for inefficiency, neglect of duty, or malfeasance in office"; ***and*** who also has plenary power to appoint every one of the agency's employees; ***and*** who also has the ability to spend more than half a billion dollars without congressional approval (*see* chart attached as Appendix A).

  Similarly false is the contention that a multi-member commission would impose radical constraints on consumer protection activity. The commission model is the norm for federal agencies, was proposed by the President and approved by the House for this very agency, and has permitted the Federal Trade Commission ("FTC") to pursue a vigorous consumer protection agenda.

- The Bureau's unique structure appears to have resulted in a number of actions in recent months that demonstrate a troubling lack of accountability and fundamental misunderstanding of the extent of its statutory authority and its proper regulatory role.

  Thus, the Bureau has failed to provide anything close to an adequate justification for the expenditures that it has made to date and those that it plans for the future; the Bureau appears to be overreaching its statutory authority and wasting resources in the approach adopted for creating the consumer complaint database; and the Bureau has thus far refused to provide meaningful guidance regarding how it will divide enforcement authority with other state and federal regulators, in particular the FTC.

Some have argued that it is more important to get a confirmed Director in place than to address these structural flaws, but the Chamber strongly believes that unless the Bureau's structural flaws are remedied now, these problems in execution will inevitably worsen and spread, harming consumers, legitimate businesses, and our entire economy.[1]

I. NEED FOR CHECKS AND BALANCES

The fundamental principle of American government is that those who exercise power must be accountable to the people, acting through their elected representatives. Every government agency must satisfy this basic standard. Congress has for this reason historically, and uniformly, subjected all federal agencies, including independent regulators, to robust checks and balances that ensure their accountability and fidelity to law.

The need for these traditional constraints is particularly acute where the regulation of consumer finance is concerned. Consumer finance is critical to the strength of the American economy—and a major generator of beneficial innovation. Government action that imposes unjustified regulatory costs on lending institutions will limit consumer choice, threaten safety and soundness, and prevent businesses from obtaining the credit they need to expand—and to create the new jobs that our economy so desperately needs. American consumers and businesses alike can ill-afford such an outcome.

The risks of agency tunnel-vision, overreach, and politicization are real for all government regulators, including the Bureau. If these risks are not properly addressed at a ***structural*** level, agencies inevitably will, over time, abandon sound regulatory principles. Indeed, as discussed below, there are troubling initial signs that the unprecedented concentration of unreviewable and unchecked power in the Bureau's Director is already having ill effects.

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[1] One argument advanced in favor postponing action to address these fundamental structural flaws is that the Bureau's plan to begin to exercise on the statutory transfer date its supervision authority under Section 1025 of the Act with respect to very large banks, savings associations and credit unions, will unfairly subject those entities to a greater regulatory burden than that borne by nondepository covered persons, who are not subject to supervision under Section 1024 until a Director takes office. But many of these nondepository institutions remain subject to regulation by the Federal Trade Commission and by state Attorneys General and other state regulators. And any delay can be remedied by acting quickly to subject the Bureau to the same level of accountability as other federal agencies.

II. UNPRECEDENTED LACK OF CHECKS AND BALANCES IN THE CFPB'S CURRENT STRUCTURE

In light of the fundamental importance of checks and balances in our system of government, we have deep concerns about the unprecedented lack of accountability of the Director of the CFPB.

A. The CFPB's Radical Structure Concentrates in a Single Individual Extraordinarily Expansive Power to Regulate the Private Sector

The Bureau's structure has a number of features that, when taken together, concentrate an amount of unchecked authority in a single individual—the Director—that is unprecedented for a federal agency that regulates private entities and individuals:

First, the Bureau will be headed by a ***single Director*** with complete, unilateral authority to make all regulatory and enforcement decisions and to hire and fire all personnel, including his or her own deputy.

By contrast, since the creation of the Interstate Commerce Commission in 1887, independent regulatory agencies have almost always been headed by a bipartisan, multi-member commission, usually consisting of five-members who serve for staggered fixed terms.[2] That is the structure of the Federal Deposit Insurance Corporation ("FDIC"), the National Credit Union Administration ("NCUA"), the Federal Trade Commission ("FTC"), the Securities and Exchange Commission ("SEC"), the Commodity Futures Trading Commission ("CFTC"), the Federal Communications Commission ("FCC"), the Federal Energy Regulatory Commission ("FERC"), the Consumer Product Safety Commission ("CPSC"), and other agencies. The Federal Reserve also follows this model, although there is no requirement of bipartisan representation on the Board of Governors. Congress has almost uniformly rejected periodic attempts to replace these multi-member regulatory commissions with a single administrator.

Second, the Bureau's Director does not serve at the pleasure of the President. Rather, during his or her five-year term, the Director may be removed only "for inefficiency, neglect of duty, or malfeasance in office."[3] That standard eliminates the

[2] The Bureau, although located for organizational purposes within the Federal Reserve System, is completely insulated from the Federal Reserve's supervision and control, and thus functions as an independent agency. *See* page 5, *infra*.

[3] Dodd-Frank § 1011(c)(3).

President's power to remove the Director based on a policy disagreement: once nominated and confirmed, the Director cannot be overruled by the President.

Moreover, although the Bureau is located within the Federal Reserve as an organizational matter, the Board of Governors of the Federal Reserve is expressly prohibited from reviewing any action of the Director.[4] The President too lacks the power to conform the Bureau's regulatory decisions to his own policy views and to reconcile them with the conflicting policy views of other agencies.[5]

Third, the Bureau is exempt from the congressional appropriations process. It is funded instead by a transfer of money from the Federal Reserve in an amount determined solely by the Director, subject only to a cap that already exceeds $550 million, will increase 10% for the next fiscal year, and is subject to automatic inflation adjustments thereafter.[6]

Once again, the Director has authority that is not subject to checks or balances. We are not aware of any other federal official responsible for regulating private sector activity who exercises sole authority over an agency; has sole power to determine whether and how to spend hundreds of millions of dollars outside the congressional appropriations process; and serves for a fixed term and is subject to removal only for cause (and therefore exempt from Presidential control).

To be sure, as some have pointed out, none of these features is unique in and of itself. But the ***combination*** of all of these features ***is*** unique. The chart attached to my testimony (as Appendix A) makes clear that ***no federal regulatory agency has the same combination of features as the Bureau, which concentrate unprecedented power in a single individual***—the Director—who is virtually unconstrained by the well-established checks and balances that traditionally have been relied upon to guide and constrain agency action.

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[4] Dodd-Frank § 1012(c)(2) & (3).

[5] The statute does contain provisions for "review" of Bureau regulations—but not other decisions—by the Financial Stability Oversight Council, but the substantive and procedural constraints on the review process make that review process entirely illusory. *See* pages 16-17, *infra*.

[6] *See* Dodd-Frank § 1017(a)(1) (providing that "the Board of Governors shall transfer to the Bureau from the combined earnings of the Federal Reserve System, the amount determined by the Director to be reasonably necessary to carry out the authorities of the Bureau under Federal consumer financial law"); *id.*§ 1017(a)(2) (setting amount) .

While no agency should have such unbridled authority, the CFPB's extraordinarily far-reaching powers and large budget mean that the absence of normal constraints raises extremely grave concerns.

To begin with, the Bureau is not limited to regulating banks and other financial service businesses. Because the Bureau's authority extends to any person or business who engages in any of 10 specified activities that are common throughout the economy, as well as service providers to such businesses,[7] the Bureau will be regulating numerous Main Street businesses well outside the financial services sector.

The standard the Bureau will be enforcing is also very broad—the prevention of "unfair, deceptive, or abusive acts or practices" in the market for consumer financial products. The CFPB will have sole discretion to issue rules establishing what these terms mean and how they will be applied. While the FTC has proscribed unfair and deceptive practices for years, generating decades of case law to guide the CFPB's rulemakings on these standards (as well as its compliance and enforcement activities), the "abusive" standard is new and will require immediate interpretation by the Bureau. In issuing this interpretation, the CFPB will be writing on what is essentially a blank slate—and the standard likely will continue to evolve into the future. Misuse of these powers could substantially harm the participants in the markets for consumer financial products—including consumers themselves.

The Bureau also has the power to override safety and soundness regulators. With respect to regulations, the check provided by the Financial Stability Oversight Council ("FSOC") is illusory, as I discuss below. But even that illusory constraint does not apply to the Bureau's enforcement actions—and those organizing the Bureau have repeatedly indicated that they plan to follow the approaches taken by the FTC and the SEC and define the statutory obligations of regulated businesses with respect to the "unfair, deceptive, or abusive" standard principally by bringing enforcement proceedings, and not through the issuance of rules.[8] The Bureau may

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[7] *See, e.g.*, Dodd-Frank §§ 1002(15) & (26), 1024, 1031, 1036. The statute's exemptions (*see id.* § 1027) are quite narrow by comparison.

[8] *Oversight of the Consumer Financial Protection Bureau*: Hearing Before the Subcommittee on Financial Institutions and Consumer Credit, 111th Cong. 18 (2011) (testimony of Elizabeth Warren, Special Advisor to the Secretary of the Treasury for the Consumer Financial Protection Bureau) ("Warren Financial Institutions Subcommittee Testimony") ("While there certainly is a place for rules aimed at specific abuses, we do not envision new rules as the main focus of how the CFPB can best protect consumers.").

institute any enforcement action that it wishes and seek far-reaching relief, without any obligation even to consult with federal safety and soundness regulators.[9]

In carrying out the CFPB's regulatory, enforcement, and supervisory activities, moreover, the Director will have very substantial spending authority. To put the Bureau's potential $550 million-plus budget into perspective, in FY 2010, the budget of the CPSC was $118 million, and the budget of the FTC (for both consumer protection *and* antitrust activities) was $292 million. Both of those agencies are, of course, subject to the appropriations process.

The Director's broad authority, combined with the unique lack of accountability, leads to a position with unprecedented unchecked power over the nation's economy.

B. Myths About the CFPB's Structure

Many inaccurate statements have been made in recent months asserting that the Director's power is subject to meaningful constraints. It is important to dispel those myths so that Congress and the public understand the truly extraordinary nature of the Bureau's structure .

Myth #1: A commission structure is a radical approach that would undermine consumer protection

The CFPB's unaccountable structure is not at all inherent in the idea of an independent consumer financial protection agency. To the contrary, as I have discussed, a commission structure is the norm for independent federal regulatory agencies.

Indeed, the President's June 30, 2009 draft legislation proposing the creation of a Consumer Financial Protection Agency adopted the commission model,[10] as did the financial reform legislation reported by the House Energy and Commerce Committee in 2009.[11] And although the House-passed bill provided for a single director to serve

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[9] *Compare* Dodd-Frank § 1022(b)(2) (requiring consultation in the rulemaking process) & *id.* § 1025(E)(3) (establishing process for resolving conflicts between Bureau and prudential regulators in the supervision process), *with id.* §§ 1053-1054 (no such requirement in enforcement process); *see also id.* § 1055 (describing broad relief, including injunctive relief, available in enforcement proceedings).

[10] Sections 111-114, H.R. 3126, 111th Cong., 1st Sess. (2009) (as introduced), *available at* http://www.gpo.gov/fdsys/pkg/BILLS-111hr3126ih/pdf/BILLS-111hr3126ih.pdf.

[11] H.R. Rep. 111-367, Pt. 1, 111th Cong., 1st Sess. 8-9 (2009).

for 30 months from the date of the bill's enactment, a five-member commission would have come into existence at the end of that period.[12]

It was not until the Senate-passed version of the legislation that the commission model was dispensed with entirely in favor of a single, tenure-protected director serving for a fixed five-year term. That modification was then adopted in the final compromise legislation.

Professor Warren also has recognized the effectiveness of the commission approach. When she first introduced the concept of such an agency in a 2007 article for the journal "Democracy,"[13] she identified the model for her proposed "Financial Product Safety Commission" as the CPSC, which is a multi-member, bipartisan decision-making body. That structure already has demonstrated its effectiveness in the consumer-protection context: in the words of Professor Warren in that article, "[t]he evidence clearly shows that CPSC is a cost-effective agency."[14]

Legislation substituting a multi-member commission for the Bureau's current single directorship thus would represent a ***return to the original vision*** for this agency, and would be consistent with the structure of virtually all other independent regulatory agencies.

A multi-member commission structure is also good policy. Expertise exercised in a non-partisan fashion, not the political imperative of the moment, should guide the Bureau's regulatory agenda. This common-sense notion counsels strongly in favor of governance by a commission, particularly given the legal difficulty, technical complexity, and economic importance of the Bureau's consumer protection mandate. The commission model inherently forces decision-makers to deliberate and compromise in making decisions, thus encouraging intellectual rigor and impartiality in regulatory approach. The need to accommodate multiple viewpoints also affords an important check against a regulatory agenda driven by one individual's potentially idiosyncratic or ill-considered policy views.

Some argue that a single Director can act more quickly and decisively than a commission. But there is no indication that the FTC's multi-member commission

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[12] Section 4103, H.R. 4173 (111th Cong., 1st Sess.), *available at* http://thomas.loc.gov/cgi-bin/query/F?c111:2:./temp/~c111k9XSYV:e988931.

[13] *See* Elizabeth Warren, *Unsafe at Any Rate*, Democracy, Summer 2007, available at http://www.democracyjournal.org/pdf/5/Warren.pdf.

[14] *Id.* at 17.

model, for example, has prevented that agency from acting rapidly when necessary; to the contrary, the FTC is recognized as a very responsive and effective regulator.[15] Moreover, speed does not necessarily mean better decision-making. This is a particular concern given that both the President and Congress lack ready tools with which to effectively check harmful action by the Bureau.

A robust deliberative process is particularly important when it comes to the CFPB because of the inherent tradeoffs and informational challenges involved in the regulation of consumer finance. For example, more stringent rules and even the prohibition of some types of credit could protect some credit users from fraud and, in some cases, the consequences of their own poor choices. But it also could lead to higher prices and less access to credit for small business—with potentially significant adverse implications for consumer well-being and economic growth. Smart, evidence-based decision-making in this complex area will depend on full consideration of a diversity of inputs and views. Only a multi-member Commission can guarantee such a process.

Finally, a commission approach would also facilitate continuity and stability in the Bureau's regulatory agenda. As the Bureau is currently structured, all of the accumulated knowledge gained by the Director during the course of his or her tenure would be lost upon departure. As a new appointee settles in and gets up to speed on the substantive issues, the agency may experience discontinuity and an extended period of mission drift. If a vacancy coincides with a different party assuming the Presidency, the departure of the incumbent director could lead to significant substantive policy shifts, presenting substantial uncertainty for regulated parties.

A multi-member commission with staggered terms, by contrast, ensures the continuous presence of a significant number of experienced members at all times, and prevents any gaps in agency effectiveness. And a commission structure helps ensure that a change in the party affiliation of the President is accompanied by a period of smooth and gradual transition.[16]

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[15] The contrast with the FTC's consumer-protection model is particularly instructive. The FTC's Bureau of Consumer Protection has a mission very similar to that of the CFPB, focusing its efforts on preventing unfair and deceptive marketing. But the final decision on whether to act rests with the FTC's bipartisan commission, not with the Bureau of Consumer Protection. I am not aware of any significant body of thought that this arrangement does not operate effectively, or that it should be changed.

[16] Some have raised the concern that a commission structure would lead to gridlock if stalled confirmations render the CFPB unable to act. This concern is baseless. Legislation can easily be crafted to alleviate any such concern, and indeed the drafters of H.R. 1121, the Responsible Consumer Financial Protection Regulations Act, have done precisely that. H.R.

Myth #2: The CFPB's current structure is not unusual

Some have claimed that there is nothing unusual about the CFPB's structure, pointing to the OTS, the OCC, the Federal Reserve, and the FDIC as supposed precedents. But the significant differences between those entities and the CFPB in fact demonstrate clearly the extent to which the latter represents a radical departure from established practice.

Both the OCC and the OTS are part of the Department of the Treasury, and the Executive Branch has taken the position that that the heads of both components serve at the pleasure of the President.[17] By contrast, the President can remove the CFPB Director only "for inefficiency, neglect of duty, or malfeasance in office"—a highly restrictive standard.

These dramatically different removal standards have important real-world implications. If the President believes that the Comptroller has adopted a dangerous regulatory approach that threatens significant economic harm, he can change the policy by removing that individual. By contrast, if the President reaches the same conclusion about the CFPB Director, he may well be powerless to exercise the power of removal (unless the approach is so unreasonable as to satisfy the "for cause" standard)—or to do much else to prevent the harm.

As the Supreme Court has recognized, "[t]he power to remove officers . . . is a powerful tool for control." *Edmond v. United States*, 520 U.S. 651, 664 (1997). And the authority to remove at will—which the President has with respect to the Comptroller—is a much more powerful tool for control than the authority to remove for cause.

1121 makes clear that "[n]o vacancy in the members of the Commission shall impair the right of the remaining members of the Commission to exercise all the powers of the Commission." It further provides that one member would serve as an initial quorum until more than two members have been appointed, and that thereafter two members shall constitute a quorum any time the commission's membership drops to three or two members (although, in the latter case, the quorum will only last for six months). Moreover, the bill would provide that each member of the CFPB Commission may continue to serve for up to one year after the expiration of his or her term of office, or until a successor has been appointed.

[17] *See* Memorandum Opinion for the General Counsel, Department of the Treasury, and the Chief Counsel, Office of Thrift Supervision, *Re: Post-Employment Restriction of 12 U.S.C. § 1812(e)* (Sept. 4, 2001).

Other significant accountability checks applicable to both the OCC and the OTS also do not apply to the CFPB. The Secretary of the Treasury, not the Comptroller and the OTS Director, appoints the Deputy Comptrollers and the OTS Deputy Directors. And the Comptroller and the OTS Director carry out their duties under the Secretary's "general direction" (Comptroller) and "general oversight" (OTS), although they enjoy some measure of protection from his interference in their enforcement and rulemaking activities. By contrast, the Bureau's Director will "appoint and direct[] all [its] employees," including the Bureau's Deputy Director.[18] And the Board of Governors of the Federal Reserve System can exercise no direction or oversight over the CFPB—despite its status as a part of the Federal Reserve.

Thus, for multiple reasons, the Comptroller and OTS Director are politically and legally accountable—both to the President directly and indirectly through the Secretary of the Treasury—in a way that the CFPB Director simply is not. The fact that defenders of the CFPB's current structure have identified these two agencies as its closest analogues, despite the obvious differences in conception and function, simply highlights the unprecedented nature of the Director's power.

Banking regulators such as the Federal Reserve and the FDIC supply even weaker precedents. To be sure, like the CFPB, they are outside the budget process. But they have multi-member leadership, which in the FDIC's case must be bipartisan, and thus are subject to the very significant protection afforded by collective decision-making—an accountability check that simply is not present when a single Director is in charge.

Myth #3: The CFPB is the "most accountable" agency in the federal government

Some have claimed that, despite the evidence to the contrary, the CFPB is in fact politically accountable—supposedly, the "most accountable" agency in the federal government. The radical structure of the agency demonstrates that this claim is simply not true. While some checks and balances do apply to the Bureau's activities, they are far too weak to impose any real discipline on the agency.

Substantive standards and judicial review. Defenders of the Bureau's current structure have pointed out that the Dodd-Frank Act requires it to adhere to

18 Dodd-Frank §§ 1011, 1013.

certain substantive standards in exercising its rulemaking and enforcement discretion. They also have noted that the CFPB's regulations are subject to judicial review (and congressional override), and must be prescribed in accordance with the requirements of the Administrative Procedure Act ("APA") that govern informal rulemakings.[19] But saying these things is saying nothing at all, because an agency would not pass muster under the Constitution if it did not have to follow a set of congressionally-mandated substantive and procedural requirements in exercising its authority. That is a basic precondition for the rule of law, not a sufficient guarantee of accountability.

Indeed, the content of these substantive and procedural requirements affords little confidence that they will constrain overreaching by the CFPB. For example, the Dodd-Frank Act defines an act or practice as "abusive" if it "materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service," or if it takes "unreasonable advantage" of a consumer's "lack of understanding" of the "material risks, costs, or conditions of the product or service" or a consumer's "inability" to protect his own interests "in selecting or using a consumer financial product or service."[20] These standards are far from specific—consumers vary greatly in their ability to understand terms, conditions, and material risks and costs, and to protect their own interests—and leave much to subsequent interpretation by the Bureau and the courts. Depending on how the standards are interpreted, they may do little to constrain the CFPB's regulatory authority.

It also is significant that the requirements governing CFPB rulemakings are less robust than those that the FTC must follow in exercising its authority under section 18(a)(1)(B) of the Federal Trade Commission Act ("FTCA"). That provision, which broadly authorizes the FTC to prescribe rules which define and seek to prevent "unfair or deceptive acts or practices," was the model for the CFPB's authority to prescribe rules that identify as unlawful and prevent "unfair, deceptive, or abusive acts or practices" relating to consumer finance. Even after the transfer date, in fact, the FTC will retain its general rulemaking authority under section 18(a)(1)(B) with respect to consumer financial products and services (as we discuss below, the Dodd-Frank Act instructs the two agencies to negotiate an agreement to avoid duplication or conflict). Thus, while the FTC and the CFPB will be exercising overlapping regulatory authority, and will be applying a similar standard in doing so, the CFPB will be subject to less rigorous procedural requirements than the FTC–even though the Bureau has the broader authority to regulate "abusive" acts and practices.

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[19] *See, e.g.*, Warren, *supra* note 13, at 18-19.

[20] Dodd-Frank § 1031(d).

Congress imposed the more elaborate procedures set forth in the FTCA out of a concern that the standard APA procedures were insufficient to protect against the threat that FTC rules would have an adverse economic impact on small businesses and consumers, particularly given the reach of the Commission's authority throughout the economy. The economic importance of consumer finance, and the broader scope of the CFPB's rulemaking authority, leave little doubt that the Bureau poses an equal if not greater risk than the FTC of misusing its rulemaking power in such a manner. Yet, once again, the CFPB faces weaker constraints than a sister regulator with similar powers.[21]

SBREFA Panels. Defenders of the status quo also have identified the need for the Bureau to comply with the Small Business Advocacy Review panel process under the Small Business Regulatory Enforcement Fairness Act ("SBREFA") as an important guarantor of its accountability. The Bureau, like the Environmental Protection Agency and the Occupation Safety and Health Administration, is statutorily required to convene such panels to assess proposed regulations expected to have a significant impact on a substantial number of small businesses and to recommend less burdensome alternatives.[22] This requirement is a very important part of the Bureau's existing legal framework given the potential harm to small businesses that could result from ill-advised rulemaking in the consumer finance area. But, for several reasons, the panel process is an imperfect accountability mechanism, and one that is unlikely to impose a robust ***independent*** check on the Bureau's activities that affect small businesses.

First, the Bureau itself is responsible for the threshold determination that a proposed regulation is expected to significantly impact a substantial number of small entities, and the terms "significant" and "substantial" are not statutorily defined. Thus, it will in large part be up to the Bureau whether or not a panel is even convened. Moreover, case law has established that agencies may only consider ***direct*** impacts on small businesses in determining whether or not to convene a SBREFA

[21] The Dodd-Frank Act itself imposes significant procedural requirements—over and above the mandates of the APA—on the Comptroller's authority to issue rules or orders interpreting the statute's preemptions standard (*see* Dodd-Frank § 1044(b)(3) & (5), (c) & (d)); again, no such requirements apply to rulemaking by the Bureau.

[22] *See Who's Watching the Watchmen? Oversight of the Consumer Financial Protection Bureau*: Hearing Before the H. Subcomm. on TARP, Financial Services, and Bailouts of Public and Private Programs of the Comm. on Oversight and Government Reform (May 24, 2011) (testimony of Elizabeth Warren, Special Advisor to the Secretary of the Treasury for the Consumer Financial Protection Bureau); Dodd-Frank § 1100G.

panel, and may not consider indirect "ripple effects"—even those that are reasonably foreseeable.[23]

Second, the Bureau does not have to adopt the panel's recommendations, which are advisory, and need only supply a reasoned explanation for adopting or rejecting them. If the Bureau's leadership is determined to push ahead with a regulation despite its adverse impact on small businesses, this hurdle will not prove difficult to overcome.

Third, SBREFA covers only the rulemaking process, and those organizing the Bureau have made clear that its preferred method of regulation will be through supervision/examination and enforcement actions. That means that small business considerations need not be taken into account in all, or even most, of the Bureau's activities.

Indeed, actions speak louder than words, and it is noteworthy that those organizing the Bureau appear to be ignoring SBREFA with respect to the significant rulemaking efforts that they have begun. Thus, there is no indication that the Bureau's organizers have initiated the SBREFA process with respect to their proposed reforms of mortgage disclosure forms[24]—even though these changes plainly will affect small businesses. And the same is true with respect to the recently-initiated effort to identify the entities that will be subject to the Bureau's supervision authority[25]—again, even though the supervision program, which may include registration and other requirements that would be especially burdensome to small businesses and could adversely affect the availability of the forms of consumer credit on which small businesses rely. Those pointing to the SBREFA process as an important check on the Bureau's authority should explain why the Bureau's organizers have failed to follow the SBREFA process thus far.[26]

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[23] *See Mid-Tex Elec. Coop., Inc. v. FERC*, 773 F.2d 327, 342 (D.C. Cir. 1985).

[24] *See* CFPB Mortgage Disclosure Team, "Know Before You Owe: We're Back," *available at* http://www.consumerfinance.gov/know-before-you-owe-were-back/(soliciting public comment).

[25] *See* 76 Fed. Reg. 38,059 (June 29, 2011).

[26] While the SBREFA requirement does not take effect until the transfer date, there is no reason why voluntary compliance with SBREFA could not have been part of the initial rulemaking processes that the Bureau's organizers have undertaken. That is especially true when—as in the instance of the mortgage disclosure rule—significant decisions have already been made (narrowing the possible approaches to several different disclosure options), decisions that could and should have been illuminated by the information that the SBREFA analysis would provide.

Inspector General Oversight. Defenders of the Bureau's current structure also point to oversight by the Inspector General of the Federal Reserve Board (and, for now, the Inspector General of the Treasury Department) as contributing to the Bureau's supposedly high level of accountability. Inspector general review to root out waste, fraud, and abuse is an essential component of good governance, and all major federal agencies are subject to such oversight. But inspector general review does not compensate for the other deficiencies in the Bureau's structure, particularly because there is no inspector general who is dedicated solely to that task. The Inspector General of the Federal Reserve has many other responsibilities, and may have difficulty marshalling the manpower and resources necessary to give the Bureau's activities the close attention that they deserve. As a result, there is a real risk that inspector general oversight of the Bureau will be ***less*** robust than it is for other federal agencies with their own dedicated inspectors general.

Thus, far from constituting a guarantor of accountability, the current mechanism for inspector general oversight of the Bureau—and, in particular, the lack of an inspector general dedicated to that task—is just another of the many factors that render the Bureau less accountable than other federal agencies.

Budget Justification. The budget justification and financial reports that the Bureau must submit to Congress have also been identified as among the important mechanisms for "meaningful oversight and accountability of the CFPB."[27] I will address this issue in greater depth below, but the obvious problem with relying on the budget justification process as an accountability check is that the Bureau is not dependent on annual appropriations, and can obtain its guaranteed funding from the Federal Reserve regardless of how much supporting material it provides to Congress. The Bureau therefore has no incentive to participate seriously in the budget justification process.

Indeed, as discussed below, the "justification" that the Bureau has submitted for its planned expenditure of over $329 million in FY 2012 was found by the House Appropriations Committee to be wholly inadequate to permit any kind of meaningful congressional review of those expenditures.

Myth #4: The Federal Reserve will control the CFPB's budget

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27 Warren Financial Institutions Subcommittee Testimony, *supra* note 8; Dodd-Frank §§ 1016, 1017.

Some have suggested that the CFPB lacks the same level of control over its budget as the other financial regulators. The statutory text shows that this claim is highly misleading. The Dodd-Frank Act expressly states (in section 1017(a)) that the Federal Reserve "***shall*** transfer to the Bureau, from the combined earnings of the Federal Reserve System, the amount determined by the ***Director*** to be reasonably necessary to carry out" the CFPB's functions, up to a cap of between 10 and 12 percent of the Federal Reserve's operating budget. Thus, up to the cap prescribed in the Act, it is clear that the Director—not the Federal Reserve—will decide what the CFPB's budget will be. And that cap—as noted, over $550 million—is not much of a limit.

Myth #5: The FSOC will guarantee the CFPB's accountability

Finally, some have pointed to the ability of a two-thirds majority of the FSOC to overturn CFPB rules that threaten the safety and soundness of the U.S. banking system or the stability of the U.S. financial system as constituting a strong guarantor of the CFPB's accountability. In fact, there are a number of reasons why this review authority is unlikely to place any meaningful constraint on the CFPB.

First, under current law, the FSOC veto applies only to rules, not enforcement actions. As noted, those responsible for organizing the Bureau have indicated their preference for establishing standards via enforcement actions rather than rulemaking, and indeed plan to dedicate over half the Bureau's budget to enforcement and supervision activities (with another quarter dedicated to consumer education and complaints, and the final quarter dedicated to all other activities, including rulemaking).

Second, the standard for exercising the veto is very restrictive—a rule must threaten the safety and soundness of the entire U.S. banking system or the stability of the U.S. financial system. Thus, any rules that threaten the safety and soundness of some financial institutions, or even an entire sector of the financial system, but do not arise to the level of posing a systemic risk, would not appear to qualify.

Third, two-thirds of the FSOC must agree to a veto, meaning that even a unanimous vote of the five prudential regulators—the Federal Reserve, FDIC, OCC, NCUA, and the Federal Housing Finance Agency—would not suffice. Yet these are the entities responsible for ensuring the safety and soundness of the U.S. financial system. Finally, it should be remembered that the CFPB's Director is one of the FSOC's ten members, rendering it even harder to obtain the necessary two-thirds majority when the CFPB's own rules are at issue. In fact, assuming that the CFPB

Director will always vote against overturning one of his or her own rules, only two of the nine remaining FSOC members need agree for the rule to come into force.

This essentially illusory FSOC "oversight" process thus is no substitute for the necessary regulatory coordination between the CFPB and other federal and state regulators in order to avoid conflicting rules and guidance.

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These facts support only one conclusion: the CFPB's current structure places more unreviewable power in the hands of a single unelected official than any other federal regulatory law. And the unprecedented combination of the CFPB's unaccountable structure with its vast and unclear powers creates a significant foreseeable risk that, at some point in the future, it will act in a way that does serious harm to the American economy—including the very consumers it is meant to protect. When that time comes, it will be too late for Congress to make the necessary legislative corrections. The time to act is now.

III. THE CFPB'S UNACCOUNTABLE STRUCTURE ALREADY SEEMS TO BE PRODUCING TROUBLING CONSEQUENCES

Although the Bureau has not yet come into existence, the structural problems identified above already have revealed themselves in disturbing ways. Three areas in particular warrant mention: (1) the CFPB's wholly inadequate effort to justify its FY 2011 and 2012 expenditures to Congress; (2) the CFPB's apparent plans to establish a consumer complaint database in manner that likely exceeds its statutory authority, and that wastes taxpayer dollars by failing to rely on the FTC's existing complaint infrastructure; and (3) the CFPB's failure to provide any meaningful guidance to date regarding how it intends to divide regulatory and enforcement authority with other state and federal regulators, and in particular with the FTC.

A. Inadequate Justification For The CFPB's FY 2011 and FY 2012 Expenditures

Budget oversight is the critical means by which the Congress ensures that revenues raised by the United States are spent effectively and efficiently, protecting the American taxpayers who supply those funds. The need for such oversight applies to the Bureau just as much as it does to other agencies—perhaps even more so because of the absence of other mechanisms for accountability. And in these times of extreme budgetary constraints, ensuring that taxpayer funds are spent properly is more important than ever.

As already noted, although the Bureau is exempt from the congressional appropriations process, the Dodd-Frank Act attempts to provide at least some measure of oversight by requiring the Bureau to submit annual financial reports and semi-annual budget justifications to Congress. Those responsible for organizing the Bureau have acknowledged the importance of these accountability mechanisms, yet their compliance efforts to date have been meager at best.

The Bureau has announced plans to expend $329,045,000 in fiscal year 2012, an increase of more than 130% over the $142,825,000 that it plans to spend in the current fiscal year. But the Bureau has provided very little justification for this very large expenditure of funds. As the House Appropriations Committee explained in its recent report on the Financial Services and General Government Appropriations Bill for FY 2012:

> Unlike other agencies, the BCFP does not describe or explain the relationship between its policy objectives and the budgetary resources, performance measures or goals, significant proposals that effect obligations in the five to ten year period and their relationship to the current year and budget year, or the budgetary effect of workload, strategic planning, capital planning, or investments in information technology. In the absence of this fine print, the Committee cannot discern what the BCFP plans to do, how it will do it, or how much it will cost.
> The Committee is disappointed that an agency dedicated to transparency and accountability was not more forthcoming about how it plans to spend taxpayer money . . .[28]

[28] H.R. Rep. 112-xx, 112th Cong., 1st Sess. at 7 (2011), *available at* http://appropriations.house.gov/UploadedFiles/FY_2012_FIN-SERVICES_FULL_COMMITTEE_REPORT.pdf.

The CFPB's budget document (*see* http://www.consumerfinance.gov/wp-content/uploads/2011/02/CFPB-2012-CJ.pdf) consists primarily of blank space, interspersed with a few paragraphs of text and a couple of tables. To be precise, the entire content of the document consists of a one-sentence "Mission Statement," a one-page description of "Bureau Vision and Priorities," a one-page "Program History and Future Outlook," and two tables—covering a single page—describing "Operating Levels" and

This very significant lack of transparency is possible only because the Bureau is not dependent on congressional appropriations, and therefore may provide Congress with little information without fear of consequence. At the same time, federal taxpayers are of course bearing the full financial burden of the Bureau's expenditures: if those funds were not transferred from the Federal Reserve to the Bureau, they would be transferred from the Federal Reserve to the Treasury, and used to reduce the federal budget deficit.[29]

The House Appropriations Committee seeks to address this lack of transparency and accountability by capping the Bureau's fiscal year 2012 expenditures at $200,000,000, directing the Bureau to provide an operating plan within 60 days of the date of enactment of the appropriations act, and requiring the Bureau to obtain an appropriation for expenditures in future years.[30]

The Appropriations Committee's actions are a step in the right direction, and we support its efforts. But even they would provide no assurance that the Bureau will expend the $200 million authorized in FY 2012 wisely and efficiently, because the Bureau's operating plan will not be provided until *after* the appropriations act is signed into law.

The approach that CFPB has taken in its budget justification is entirely inconsistent with the oft-repeated claim that the Bureau "is the most constrained and

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"Resource Detail[s]." A half-page of text following these tables notes that "CFPB budget estimates are based on the best available information at the time the Budget was prepared"—although the CFPB did not share that information with Congress. Such a high-level description of broad policy objectives and estimated resource needs makes it impossible for Congress to conduct a meaningful review of what the CFPB plans to do, how and why it plans to do it, and how much those activities will cost. For a sample of the budget detail provided to Congress by virtually all other federal agencies, see the Federal Trade Commission's *summary* of the justification provided to Congress, see http://www.ftc.gov/ftc/oed/fmo/budgetsummary12.pdf. As the Committee is aware, the full justifications provided to the Appropriations Committees by federal agencies run into the hundreds of pages.

[29] *See, e.g.*, Federal Reserve, Annual Report 2010, at Table 4 (reflecting deduction of funds provided to CFPB before distribution to U.S. Treasury), *available at* http://www.federalreserve.gov/publications/annual-report/2010-federal-reserve-banks.htm#8.

[30] *See* Sections 101 & 102 of H.R. xxx; H.R. Rep. 112-xxx, at 7-8, *available at* http://appropriations.house.gov/UploadedFiles/FY_2012_FIN-SERVICES_FULL_COMMITTEE_REPORT.pdf.

the most accountable agency in government."[31] The Bureau's approach also vividly demonstrates why the Bureau's current structure, in particular its insulation from the budget process, renders it almost entirely unaccountable to Congress and, ultimately, to the American people.

B. The Bureau Appears to be Exceeding its Statutory Authority and Wasting Resources in Creating the Consumer Complaint Database

The Dodd-Frank Act requires the Bureau to establish, "or utiliz[e] an existing database to facilitate the centralized collection of, monitoring of, and response to consumer complaints regarding consumer financial products or services."[32] The Act also appears to require financial institutions subject to the Bureau's primary enforcement authority to comprehensively respond to regulators regarding complaints submitted to the database, including by providing a description of steps taken to respond to the complaint or inquiry.[33] Little has been revealed about the current plans for implementing these requirements. But what has been disclosed suggests that the Bureau will be following a course that is of dubious legality and that, even if ultimately deemed legal, could have extremely harmful consequences for businesses engaged in perfectly lawful practices.

First, the Bureau apparently will be creating its own dedicated complaint database, even though it has not explained why such an expensive and redundant new infrastructure is needed (or even how much it will cost). The Dodd-Frank Act expressly allows the Bureau to rely on an existing complaint database, and the Act's legislative history makes clear that Congress expected "the Bureau to work with other federal agencies, such as the [FTC], to make use of the FTC's existing consumer complaints collection infrastructure where efficient and advantageous in facilitating complaint monitoring, response, and referrals."[34] To my knowledge, the responsible officials have not explained why it would not have been "efficient and advantageous" for the Bureau to share the FTC's existing, and widely-admired, automated complaint database (which is configured to allow the Bureau to operate a separate, autonomous database using the FTC structure), rather than expending the substantial resources required to create a whole new architecture.

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31 Warren Financial Institutions Subcommittee Testimony, supra note 8, at 16.

32 Dodd-Frank § 1013(b)(3).

33 *Id.* § 1034(b).

34 S. Rep. No. 111-176, at 162 (2010).

Indeed, the inefficiencies and disadvantages of having two separate databases are obvious. In submitting complaints, consumers are unlikely to be able to distinguish clearly between the CFPB, on the one hand, and the FTC, FDIC, and other agencies that also collect such complaints, on the other. Indeed, given the overlapping jurisdictions of these agencies, it is hard for even knowledgeable observers to draw an intelligible line. Moreover, given the existence of other databases, the Bureau's database is likely to give a skewed perspective of how consumers perceive financial products or services—for example, regarding the extent of relative consumer confusion about a particular product. Negative comments in the Bureau's database may be counterbalanced by potentially contrary information in the databases of the other agencies. Use of the same database structure would allow the agencies to compare submissions more easily and efficiently.

It is unimaginable that CFPB would have chosen to expend its scarce resources in this way if it had to provide to Congress—and to the public—a real justification for its spending, or if the decision was being made by a bipartisan group of five knowledgeable officials rather than a single individual.

Second, although officials have not provided much information about how the complaint database will function, there have been disturbing indications that the Bureau will be accepting—and indeed actively seeking out—unverified third-party complaints of dubious reliability. This approach could unfairly damage the reputations of legitimate businesses that have done nothing illegal.

For example, a Privacy Act notice that the Bureau issued in January could be read to suggest that the Bureau will be collecting complaints originated by third parties claiming to be acting on "behalf" of a consumer (or consumers generally), but that are not in fact acting as the agent, trustee, or authorized representative of a particular consumer. As the Chamber explained in a comment letter responding to the notice, such an approach is at odds with Congress's apparent intent in enacting the relevant provisions of the Dodd-Frank Act, and deviates from the course taken by the FTC and FDIC in implementing their own complaint databases.[35]

The approach also makes little sense from an information-gathering perspective. It risks duplicating complaints submitted by consumers with actual

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[35] *See* Letter for Ms. Claire Stapleton, CFPB Implementation Team, from David Hirschmann, President and Chief Executive Officer, Center for Capital Markets Competitiveness, U.S. Chamber of Commerce, and Lisa A. Rickard, President, U.S. Chamber Institute for Legal Reform, *Re: Notice of Proposed Privacy Act System of Records, Treasury DO.315*, at 2-4 (Feb. 9, 2011).

firsthand experience with a financial product. It also likely would diminish the quality and reliability of the information gathered. And it could facilitate misuse of the Bureau's collection function by outside groups to target a particular company or type of product or service based on an unfounded belief that the product or service was inappropriate, or some other improper motivation.

Also troubling is Professor Warren's suggestion that the Bureau will use so-called "crowd-sourcing" techniques to collect information about allegedly deceptive consumer financial practices. As reported by the National Law Journal based on an interview with Ms. Warren, these techniques generally involve the collection of data from "online collaborations like Wikipedia that are built through contributions from thousands or even millions of people."[36] The vacuuming up of massive amounts of raw Internet data for inclusion within the database, including possibly information posted on websites such as Wikipedia (or social media such as Facebook or Twitter), and never even submitted to the Bureau, would multiply exponentially the risk of intentional manipulation of the database. In addition, of course, this approach would render it virtually impossible for the Bureau to verify the identity of the person or entity making a particular complaint. We doubt that Congress intended the database to be used in such an indiscriminate fashion.

The harmful effects from these approaches would be exponentially worse if the Bureau makes the complaints public—an option that officials apparently are actively considering. In addition to being bad policy, this approach may well be illegal. The Dodd-Frank Act mentions the sharing of complaints with federal and state regulators,[37] but does not expressly authorize the sharing of complaints with the public. This is in sharp contrast with the Consumer Product Safety Improvement Act of 2008 ("CPSIA"), which in section 6A(a)(1) expressly requires the CPSC to establish and maintain a database on the safety of consumer products that is "publicly available," "searchable," and "accessible through the Internet website of the Commission." Particularly given the reference to state and federal authorities in the Dodd-Frank Act, it may be inferred that Congress, by not including the same language regarding public disclosure in the Act as it did in the CPSIA, did not intend to authorize the Bureau to make the complaints public. Even if the Act does not legally foreclose such an approach, the CFPB should not begin implementing any kind of plan to publicize complaints before both implementing robust safeguards to ensure their reliability and establishing a procedure for companies to challenge their veracity.

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36 Warren Outlines Sweeping New Approach to Consumer Financial Protection, Nat'l L.J., Oct. 29, 2010.

37 Dodd-Frank Act § 1031.

Third, it appears that those organizing the Bureau intend to have the complaint database up and running, and accepting consumer complaints, by the transfer date of July 21, 2011. Bureau employees also apparently are working with the five largest credit card companies to begin receiving complaint referrals as of that date.[38] But assuming that no Director will have been appointed by July 21, it is not at all clear who would have the authority to establish the database and to require companies to respond to complaints submitted to it. The Inspectors General of the Treasury Department and the Federal Reserve have expressed the view that the Bureau itself will continue to be without authority after the transfer date in the absence of a director, and that the only authorities that the Secretary of Treasury will be able to exercise on the Bureau's behalf in that circumstance will be those contained in subtitle F of Title X of the Dodd-Frank Act.[39] The authority to establish a complaint database is contained in section 1013 of that Act, and the obligation of companies to response to complaints submitted to the database is contained in section 1034. Neither of those provisions is in subtitle F.

Fourth, it is troubling that the Bureau's Privacy Act notice solicited comments on the database—and numerous comments were filed in February—but there has been no public response to the comments or explanation of how the Bureau plans to proceed. This lack of transparency reinforces the concerns about the lack of accountability already discussed.

C. The Bureau Has Not Provided Meaningful Guidance Regarding the Division of Regulatory and Enforcement Authority with Other State and Federal Regulators, in Particular the FTC

Multiple regulators and enforcement authorities have power that overlaps with that exercised by the Bureau. For example, the Dodd-Frank Act expressly preserves a significant portion of the FTC's consumer protection power. It also not only preserves the consumer protection authority of state Attorneys General and other state regulators, but also grants them the additional authority to enforce federal law. As a consequence, the Chamber's members are very concerned about the

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38 *See* Carter Dougherty, *Banks Push Consumer Bureau to Keep U.S. Complaint Line Private*, Bloomberg, May 13, 2011.

39 Letter to The Honorable Spencer Bachus, Chairman, Committee on Financial Services, and The Honorable Judy Biggert, Chairman, Committee on Financial Services, Subcommittee on Insurance, Housing and Community Opportunity at 5-6 (Jan. 10, 2011).

possibility—the likelihood, really, given the large number of regulators—of duplicative and inconsistent regulatory actions.

The Act specifically requires a division of authority between the Bureau and the FTC. Yet, in the year since the statute was enacted, neither agency has provided much indication about how they will carry out this division.

Nor has the Bureau provided meaningful guidance regarding how its authority will be divided with that exercised by the state Attorneys General. Although the Bureau and the National Association of State Attorneys General have entered into a memorandum of understanding, that document is nothing more than an agreement to consult with one another, and contains little about the substance of that coordination. It says nothing at all, for example, about the establishment of rules to prevent overlapping and inconsistent enforcement actions. In the past, the problem of regulators with overlapping enforcement responsibilities "piling on" against regulated businesses has done substantial harm by duplicating efforts and generating inefficiencies. The Chamber's concern is that the problem will be even greater now that there is a new federal agency on the scene, and that so little progress has been made in clearly delineating each regulator's respective turf.

Turning to the substantive question of how authority should be divided, the Chamber's view is that the FTC should continue to oversee non-financial businesses, while the Bureau should focus only on businesses that are entirely or principally financial in nature (rather than businesses only tangentially engaged in activities triggering Bureau jurisdiction). We also believe that the States should be encouraged to take action before the Bureau steps in at the federal level.

Regardless whether the Bureau adopts these substantive proposals, it should clearly define its jurisdiction as soon as possible. An *ad hoc* approach serves no one's interests. It wastes the time of regulators in endless debates about who will take the lead in specific enforcement situations. And it leaves businesses eager to understand their legal obligations with no clarity regarding which agency to approach, necessitating reaching out to all agencies that could possibly have enforcement jurisdiction. At this stage, the Bureau and the FTC should at minimum declare their intention to adopt a presumptive division of authority. Even assuming that presumption could be overridden in a particular case, it would at least give businesses some clarity.

IV. CONCLUSION

Well-regulated, transparent, efficient financial markets are the lifeblood of the

American economy. Both businesses and consumers will benefit from the right reforms, which include making sure that regulators are structured to be accountable to the people's representatives, to function effectively, and to work well together. The CFPB is no exception to this principle. We urge Congress to work on a bipartisan basis to revise the Bureau's structure so that it comports with the basic principles of accountability and checks and balances that have been part of our government for the past 224 years.

Thank you again for the opportunity to testify before the Committee today. I look forward to answering your questions.

APPENDIX A

	Checks and Balances on Leadership Power and Decision Making						Budget Oversight
	Commission/ Board Structure	Requirement of Bipartisan Representation on Commission/ Board	Outside Officials Serve on Agency's Decisionmaking Body or Appoint Some of Its Top Officials	Head Subject to At-Will Removal by the President	Cabinet Official Statutorily Authorized to Supervise Agency	Dedicated Inspector General	Budget Dependent on Appropriations
CONSUMER FINANCIAL PROTECTION BUREAU	✗	✗	✗	✗	✗	✗	✗
Federal Reserve System	✓					✓	
National Credit Union Administration	✓	✓				✓	
Office of the Comptroller of the Currency			✓	✓	✓		
Office of Thrift Supervision			✓	✓	✓		
Social Security Administration			✓			✓	✓
Consumer Product Safety Commission	✓	✓				✓	✓
Federal Communications Commission	✓	✓				✓	✓
Federal Deposit Insurance Corporation	✓	✓	✓			✓	
Commodity Futures Trading Commission	✓	✓				✓	✓
Securities and Exchange Commission	✓	✓				✓	✓
Federal Energy Regulatory Commission	✓	✓					✓
Federal Trade Commission	✓	✓				✓	✓

GEORGETOWN UNIVERSITY LAW CENTER

Adam J. Levitin
Professor of Law

Written Testimony of

Adam J. Levitin
Professor of Law
Georgetown University Law Center

Before the United States Senate
Committee on Banking, Housing, and Urban Affairs

"Enhanced Consumer Financial Protection After the Financial Crisis"

July 19, 2011
10:00 am

Witness Background Statement

Adam J. Levitin is a Professor of Law at the Georgetown University Law Center, in Washington, D.C., where he teaches courses in bankruptcy, commercial law, consumer finance, contracts, and structured finance. He has previously served as the Robert Zinman Scholar in Residence at the American Bankruptcy Institute and as Special Counsel to the Congressional Oversight Panel supervising the Troubled Asset Relief Program (TARP). Before joining the Georgetown faculty, Professor Levitin practiced in the Business Finance & Restructuring Department of Weil, Gotshal & Manges, LLP in New York, and served as law clerk to the Honorable Jane R. Roth on the United States Court of Appeals for the Third Circuit.

Professor Levitin holds a J.D. from Harvard Law School, an M.Phil and an A.M. from Columbia University, and an A.B. from Harvard College, all with honors.

Professor Levitin has not received any Federal grants nor has he received any compensation in connection with his testimony, and is not testifying on behalf of any organization.

Mr. Chairman Johnson, Ranking Member Shelby, Members of the Committee:

My name is Adam Levitin, and I am a Professor of Law at the Georgetown University Law Center in Washington, D.C., where I teach courses consumer finance, contracts, and commercial law.

I am here today to testify before the Committee about the need for enabling the new Consumer Financial Protection Bureau (CFPB) to carry out its mission of ensuring a fair, equitable, and transparent consumer financial products marketplace and protecting consumers from unfair, deceptive, or abusive financial products. The creation of the CFBP was one of the most significant parts of the Dodd-Frank Wall Street Reform and Consumer Protection Act. It is important that the CFPB be given a chance to get up and running and before Congress entertains reforms to the Bureau's structure.

The CFPB will go on-line this Thursday, July 21.[1] But the CFPB will not be able to exercise the full powers granted it by Title X of the Dodd-Frank Act, until and unless a Director is appointed by the President. Instead, the Treasury Secretary will become the acting Director, but will be limited to exercising the CFPB's powers under subtitle F of Title X.[2] These powers include enforcement of existing federal consumer financial protection laws and bank examination authority.[3] Absent the appointment of an initial Director, however, the CFPB may not examine non-banks or exercise its organic rulemaking powers, as these powers are granted to the CFPB in other subtitles of Title X of the Dodd-Frank Act.

This past weekend the White House announced that it would be nominating Richard Cordray as Director for the CFPB. Mr. Cordray, currently serving as head of enforcement for the CFPB, is an outstanding and superbly qualified nominee with an impressive record as an advocate for consumer financial protection as the former Attorney General of Ohio. I urge the Senate to act expeditiously on the nomination, so that the CFPB may exercise its full powers and carry out the mission tasked to it by Congress.

* * *

In this written testimony, I address two points: the need for a CFPB and the oversight of the CFPB.

The CFPB was a much-needed response to a deep flaw in the regulatory architecture that left consumer financial protection an "orphan mission" among federal regulators, consistently subordinated to the protection of bank safety-and-soundness—that is the protection of bank profitability. A dedicated, unconflicted consumer financial protection regulator is necessary not only to deal with the "bad apples" that exist in any market because of the strong incentives in the consumer finance marketplace for all financial service providers to avoid transparent products.

In recent months there has been a great deal of attention paid to the accountability and oversight of the CFPB, even before the Bureau is operational. What is remarkable about this concern is the deafening silence about accountability and oversight for the existing federal bank regulators, on whose watch the financial crisis occurred. Congress required a limited, one-time audit of the Federal Reserve[4] and limited the Federal Reserve's ability to bail out individual

[1] *See* Pub. L. 111-203, § 1062, 124 Stat. 1376, 2039-40, July 21, 2010.
[2] Pub. L. 111-203, § 1066, 124 Stat. 1376, 2055, July 21, 2010.
[3] Pub. L. 111-203, § 1061, 124 Stat. 1376, 2035-39, July 21, 2010.
[4] Pub. L. 111-203, § 1109, 124 Stat. 1376, 2127, July 21, 2010.

firms (but not entire industries) under section 13(3) of the Federal Reserve Act,[5] and eliminated the Office of Thrift Supervision.[6] But there were no substantive, lasting changes made to the oversight of the Federal Reserve, the Office of the Comptroller of the Currency, the FDIC, the SEC, or the CFTC. These agencies failed epically in their missions of ensuring the safety-and-soundness of US financial institutions and systemic stability, but their oversight has not be changed, whereas the CFPB has not even opened for business and yet it is being proscribed as a "rogue" agency.

Many of those now raising concerns about CFPB oversight were opposed to the creation of the CFPB in the first place. None of them have expressed similar concerns about the oversight of financial regulatory agencies that failed in their missions. Given that the CFPB has, in fact, been designed to be more accountable than any other federal bank regulator, it is hard to ascribe concerns about CFPB accountability and oversight to anything other than a political distaste for consumer financial protection.

As I detail below, the CFPB has unprecedented (and possibly unconstitutional) checks on its authority. To date, the CFPB implementation team has won nothing but praise from its prospective regulates for the thoughtfulness and inclusiveness of its initial steps in the regulatory process.[7] Until and unless actual problems with the CFPB's operations emerge, there is no reason to adjust its oversight structure. In short, there is no evidence of an oversight problem that needs to be addressed. At this point, it is hard to understand concerns about CFPB oversight other than attempts to hobble the CFPB before it can get up and running.

I. WHY A CONSUMER FINANCIAL PROTECTION BUREAU?

A. The Regulatory Architecture Pre-Dodd-Frank Left Consumer Financial Protection an "Orphan Mission"

Although the financial crisis is not yet three years old, it is important to recall the reasons for creating a CFPB in the first place.[8] A critical reason for the creation of the CFPB was the recognition that the current system of consumer financial protection does not work and contributed significantly to the housing bubble and financial crisis. In the current system (set to expire on July 21), 17 separate federal consumer financial protection statutes are enforced by ten federal agencies with other primary and often conflicting missions.[9] Figure 1, at the end of this testimony, illustrates the current crazy quilt structure.

Some of these agencies have the ability to promulgate regulations, some also exercise supervisory authority over financial institutions, and some can only enforce existing regulations. Sometimes authority is over a class of institutions, and sometimes it is over a particular type of product. This situation makes industry-wide rule-making extremely difficult. For example, a rulemaking that would cover all credit cards necessitated coordination between the Federal Reserve Board, the Office of Thrift Supervision, and the National Credit Union Administration. The result was that consumer protection became a bone in regulatory turf wars and inaction dominated.

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[5] Pub. L. 111-203, § 1101, 124 Stat. 1376, 2113, July 21, 2010.
[6] Pub. L. 111-203, Title III, 124 Stat. 1376, 1520-1570, July 21, 2010.
[7] Kate Davidson, *New CFPB Mortgage Disclosures Win Praise for Content and Process*, AM. BANKER, May 19, 2011.
[8] Adam J. Levitin, *The Consumer Financial Protection Agency*, Pew Financial Reform Project, Briefing Paper, No. 2, 2009.
[9] *Id.*

Only one agency currently tasked with consumer financial protection, the Federal Trade Commission, even has consumer protection as its primary role. The FTC, however, has very limited jurisdiction in financial services—it cannot regulate federally-chartered or insured banks, thrifts, or credit unions. This leaves only bit-players in financial services within the FTC's regulatory ken. The result has been that because consumer protection has been everyone's responsibility, it has been no one's responsibility, and accountability and performance have suffered therewith. Put another way, because no agency had as its sole mission consumer financial protection and authority over the entire consumer finance industry, consumer financial protection frequently fell between the cracks—it was an orphan mission.

Nowhere can this problem be seen more clearly than in the run up to the financial crisis. Many factors contributed to the crisis, but none more so than an orgy of unsound leverage in the home mortgage market. Federal financial regulators had sufficient ability to limit the excesses in the mortgage lending market. The Federal Reserve Board had the power to restrict some of the most predatory products under the Home Owners Equity Protection Act, and the Office of Comptroller of the Currency and Office of Thrift Supervision had broad ability to rein in the most egregious bank and bank service company activities both in direct lending and in the warehouse lending and securitization that financed non-bank mortgage lenders. None of them acted.

Astonishingly, the financial crisis has not chastened these regulators. This past year, in the midst of the nation's worst foreclosure crisis ever, the Federal Reserve Board proposed a rule-making that would have gutted the Truth in Lending Act right of rescission, the strongest defense homeowners have against foreclosures.[10] The Federal Reserve Board again proved itself deaf to consumer protection concerns in its recent rule-making under the Durbin Interchange Amendment, in which ignored basic economics to question whether there would be any consumer savings as the result of lowered interchange fees. And the Office of the Comptroller of the Currency, which used preemption to shield subprime mortgage lenders from state regulation without substituting its own consumer protections,[11] has proposed revised preemption standards that flagrantly disregard Congress's express directions on preemption in the Dodd-Frank Act.[12]

Had the CFPB existed in 2004-2008, it might well have saved this country from the housing bubble and subsequent collapse. Had the CFPB existed in 2004-2008, it could have regulated the mortgage market to curtail predatory lending practices, such as widespread use of payment-option adjustable rate mortgages ("pick-a-pay" mortgages) and other unsustainable financial products. The CFPB could also have insisted on the very standards that Congress demanded in title XIV of the Dodd-Frank Act, including that mortgage lending be conditioned on the ability to repay, not the ability to refinance.

Congress rightly recognized the severe shortcomings of the current system of consumer financial protection when it enacted Title X of the Dodd-Frank Wall Street Reform and Consumer Protection Act and created the Bureau of Consumer Financial Protection. In so doing,

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[10] Donna Borak, *Consumer Groups, Lawmakers Press Fed to Withdraw TILA Plan*, AM. BANKER, Jan. 6, 2011.

[11] *See* Watters v. Wachovia Bank, N.A., 550 U.S. 1 (2007) (upholding OCC preemption of state attempts to regulate subprime mortgage lenders); Adam J. Levitin, *Hydraulic Regulation: Regulating Credit Markets Upstream*, 26 YALE J. ON REG. 143 (2009) (detailing OCC and OTS preemption of state mortgage regulations without substituting equivalent federal regulations).

[12] Pub. L. 111-203, § 1044, 124 Stat. 1376, 2014, July 21, 2010; Letter from Treasury General Counsel George W. Madison to Acting Comptroller of the Currency John Walsh, June 27, 2011 (stating that OCC's approach to preemption was incompatible with the text and legislative history of Section 1044(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act).

it consolidated consumer financial protection into a single agency with a single director who can be held accountable for the agency's performance. Congress also gave the new agency sufficient funding and budgetary independence to ensure that consumer financial protection, like other parts of bank regulation, will not be held hostage to politics because it is too important to financial stability. The new agency has substantial powers to regulate consumer financial products, but it is also subject to even more substantial safeguards that make it more accountable than any other comparable federal agency.

B. Competition in the Consumer Finance Market Discourages Product Transparency, so Regulatory Involvement Is Necessary

The CFPB's mission is to ensure a fair, equitable, and transparent consumer financial products marketplace and protecting consumers from unfair, deceptive, or abusive products. Unfortunately, the dynamics of the consumer finance market place discourage transparency and easy-to-price products. It is precisely this dynamic that calls for regulatory involvement to foster transparency and thus encourage optimal competition.

Transparently priced products have smaller profit margins because consumers can comparison shop more easily on an apples-to-apples basis, as it were. This creates a strong incentive for financial service providers to market complex, opaquely priced products that cannot be readily compared with other products. This is done by having multiple price-points on products or by bundling products together or by having behaviorally-contingent pricing, such as late fees. As a result, it is very difficult to know in advance the total cost of using most consumer financial product.

Consider the purchase of a new car. One can easily shop around on the web for price quotes, but those are quotes for the car itself (and frequently not for exactly the model the dealer has in stock). The car, however, is sold as part of a bundle of goods and services. The total price paid is a combination of the sale price on the car, warranties, financing costs, trade-in value, rust-proofing, gap insurance, etc. It is extremely difficult to do comparison-shopping on the all-in price of the car purchase.

A similar story exists for credit cards. Credit cards have multiple price points—typically a purchase APR, a cash advance APR, and a default APR, an overlimit fee, an annual fee, a late fee, a foreign transaction fee, and numerous other possible fees. They also have rewards programs, which are a type of negative pricing. Unless a consumer knows exactly how he or she will use a card, it is impossible to know just how much the card will cost to use and therefore how it compares with other cards. The Credit CARD Act of 2009 rectified some of these problems, such as the possibility that interest rates would change on cardholders retroactively, but the complexity of credit card pricing still bedevils consumer attempts to compare total costs of use in advance.

In the world of mortgages, it is only slightly better. It is relatively easy to compare the cost of simple, largely standardized products like 30-year fixed-rate mortgages, especially as the Real Estate Settlement Procedures Act requires disclosure of the closing costs in advance.[13] But adjustable-rate products and prepaid interest (points) complicate comparison-shopping. Moreover, there is no place a consumer can go to get mortgage quotes from every lender in the market. The mortgage market is a market where financial institutions from across the US should

[13] 12 U.S.C. §§ 2603 (requiring use of uniform settlement statement), 2604(c) (requiring good faith estimate of settlement costs).

be competing on every loan. Yet mortgage brokers typically offer quotes from only three or four lenders, and on-line sites like Lending Tree have similarly limited stables of lenders. Comparison is easier, but the menu is restricted.

All of this produces an inefficient consumer finance marketplace in which consumers often overpay for products they neither need (credit life or gap insurance, e.g.) nor want (e.g., American Express provides cardholders with insurance for repatriation of remains if you die abroad—an irrelevant benefit to those who do not travel abroad).[14] Consumer financial products should be commodities—with very thin commodity profit margins; they involve the ultimate fungible—money. Consumer financial product pricing, however, is anything by commoditized. That inefficiency is very profitable, however, to financial institutions that are able to craft their products to take advantage of consumer misperception of total cost.

In this marketplace, it is very difficult for financial institutions, like community banks and credit unions, that offer fair, transparent, simple products to compete. While their products are in fact price-competitive, especially when customer service is accounted for, consumers do not recognize this. For example, a credit card lender that listed only one, all-in interest rate and no fees would have to list a much higher APR than card lenders that use multiple interest rates and also have multiple fees. That high APR would likely scare away potential customers, even if the all-in cost of using the card was lower than that of other cards.[15]

All of this speaks to a need for regulatory involvement in the consumer financial market place to encourage more transparent pricing and thus better price competition to benefit consumers. Federal regulation of consumer financial services is primarily through disclosure regulation. Disclosure has only recently become the focus of serious scientific examination; previously it was prescribed as a regulatory fix as a matter of faith, not knowledge. We are quickly learning that while disclosure can have a powerful impact on consumer behavior, the manner in which it is done has an enormous impact on its effectiveness. Done well, disclosure is an important tool producing the information necessary to make markets work. Done poorly, disclosure can actually create market inefficiency. Having an agency like the CFPB that can develop deep expertise on consumer financial products is likely to result in better and more effective disclosures and thus more transparent consumer financial products and more efficient markets.

II. The CFPB Is More Accountable Than Any Other Comparable Federal Agency

Some members of Congress have expressed concern about the CFPB's accountability. As noted above, it is hard to understand these concerns as anything other than cover for a political agenda of gutting the CFPB because there are not the votes to kill off the Bureau outright. As a purely factual matter, concerns about CFPB accountability are puzzling. As detailed below, the CFPB has an extensive and unusual set of oversight provisions that make it more accountable than any other federal financial regulator. Table 1, below, compares the oversight of the CFPB with that of the Environmental Protection Agency, Federal Deposit Insurance Corporation, Federal Reserve Board of Governors, Federal Trade Commission, Office of the Comptroller of the Currency, Office of Thrift Supervision, Securities and Exchange

[14] This sort of bundling is similar to the problem with cable TV, where consumers are forced to buy bundles of channels that include many channels that they never watch.

[15] *See* Adam J. Levitin, *New Credit Card Tricks, Traps, and 79.9% APRs*, CREDIT SLIPS, Dec. 18, 2009, *at* http://www.creditslips.org/creditslips/2009/12/new-credit-card-tricks-traps-and-799-aprs.html.

Commission, and the Social Security Administration. The EPA and the Social Security Administration are included in the comparison because the wide-swathes of the economy they effect.

Table 1 shows in succinct form, that the CFPB and these other agencies all share several key oversight devices: APA rulemaking, APA adjudication, Congressional oversight, and moral suasion by the Administration. Beyond that, there is variation in oversight devices. The CFPB is not subject to the same additional oversight devices as the other agencies, but it is certainly subject to significant additional oversight via the annual GAO audit, OIRA SBREFA reviews, a budgetary cap, and the FSOC veto. This is far greater oversight than there is for the other federal bank regulators—OCC, the OTS, the Federal Reserve Board, and the FDIC—or for the SEC. The particular oversight mechanisms that apply to the CFPB are detailed below.

TABLE 1. COMPARISON OF OVERSIGHT OF CFPB AND OTHER AGENCIES

	EPA	FDIC	FRB	FTC	OCC	OTS	SEC	SSA	CFPB
APA Rulemaking	YES	YES	YES	YES	YES	YES	YES	YES	YES
APA Adjudication	YES	YES	YES	YES	YES	YES	YES	YES	YES
Budget Subject to Appropriations	YES			YES			YES	YES	
Budget Capped									YES
OIRA Review of Economically Significant Regs	YES			YES	YES	YES		YES	
OIRA SBREFA Review	YES								YES
FSOC Veto									YES
Annual GAO Audit									YES
Term in Office <5 Years	YES								
5-member Commission		YES	YES	YES			YES		
Bipartisan Representation Requirement		YES		YES					
Presidential Removal without Cause	YES				?	?			
Congressional Oversight	YES	YES	YES	YES	YES	YES	YES	YES	YES
Moral Suasion by Administration	YES	YES	?	YES	YES	YES	YES	YES	YES

Administrative Procedures Act Safeguards

The CFPB is subject to the Administrative Procedures Act and must follow notice-and-comment procedures for rulemaking and adjudication.[16] This means that the CFPB will be required to take account of and respond to a range of views and concerns on any regulatory issue on which it undertakes rule-making and that these rule-makings can be challenged in federal court.

OIRA Small Business Impact Reviews

CFPB rulemaking is subject to Office of Information and Regulatory Affairs (OIRA) review for small business impact.[17] Only the Environmental Protection Agency (EPA) and Occupational Safety and Health Administration (OSHA) are subject to similar requirements.

Specific Statutory Limitations on CFPB Rulemaking

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[16] P.L. 111-203, § 1053, 124 Stat. 1376, 2025, July 21, 2010, *codified at* 12 U.S.C. §5563 (making CFPB hearings and adjudications subject to the Administrative Procedures Act, 5 U.S.C. §§ 553-554).

[17] P.L. 111-203, § 1100G, 124 Stat. 1376, 2112, July 21, 2010; 5 U.S.C §§ 601-612; Executive Order 12866 of September 30, 1993.

The CFPB is specifically limited by statute in its rule-making power. Title X of the Dodd-Frank Act requires that the CFPB make particular findings, including cost-benefit analysis, in order to exercise its authority to restrict or prohibit acts and practices as unfair, deceptive, or abusive.[18] It is also worth emphasizing what the CFPB *cannot* do:

- The CFPB cannot force financial institutions to extend credit.
- The CFPB cannot mandate the offering of any financial product.
- The CFPB cannot require financial institutions to offer "standard" or "plain vanilla" products if they offer "alternative" products.[19]
- The CFPB cannot require consumers to purchase financial products.
- The CFPB cannot impose usury caps.[20]
- The CFPB cannot regulate non-financial businesses.[21]
- The CFPB cannot create private rights of action.

At most, then, the CFPB can curtail the offering of certain financial products. This is a critical point because it means that it is virtually impossible for CFPB actions to be a source of systemic risk because it cannot force financial institutions to make loans that they do not wish to make.

Statutory Budget Cap

The CFPB is subject to a budgetary cap, unlike any other federal bank regulator. Unlike most regulatory agencies, federal bank regulators are budgetarily independent; they are not funded through the appropriations process. Viewed in this framework, the CFPB is actually less independent than other federal bank regulators. If the Office of Comptroller of the Currency or FDIC or OTS wishes to increase their budget, they can simply increase their assessments on banks without so much as a by-your-leave to Congress. Similarly, the Federal Reserve can simply print money. The CFPB, however, is restricted to a capped percentage of the Federal Reserve's operating budget.[22] This means that the CFPB actually has less budgetary independence than any other federal bank regulator.

The budgetary independence of bank regulators and the CFPB represents what prominent conservative legal scholar Richard Epstein has termed "second order rationality," namely steps people take to protect themselves against their own lack of self control. It is tempting for Congress to play politics with bank regulation or consumer protection. Thus, if bank regulators' budgets were subject to the appropriations process, the agencies' effectiveness and thus the President's Constitutional obligation to enforce federal laws could be held hostage by a minority in either house of Congress.

The independent funding of the bank regulators and CFPB is designed to guard against that very possibility. The CFPB's budgetary independence recognizes that federal budgets are complex, negotiated deals that don't allow for proper airing of policy issues. In a federal budget, the CFPB's funding might be held hostage for issues that have nothing to do whatsoever with the CFPB like deficit reduction. One of the insights from the mortgage crisis is that consumer

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[18] P.L. 111-203, § 1031, 124 Stat. 1376, 2005-06, July 21, 2010, *codified at* 12 U.S.C. § 5531

[19] Notably, this "plain vanilla" concept was formerly required by the Federal Home Loan Bank Board, which required federal thrifts that offered adjustable-rate mortgages to also offer borrowers fixed-rate mortgages. 45 Fed. Reg. 79493, Dec. 1, 1980; 12 C.F.R. § 545.6-4(a) (1980).

[20] P.L. 111-203, § 1027(o), § 1027(o), 124 Stat. 1376, 2003, July 21, 2010, *codified at* 12 U.S.C. § 5517(o).

[21] P.L. 111-203, § 1027(a), 124 Stat. 1376, 1995-98, July 21, 2010, *codified at* 12 U.S.C. § 5517(a).

[22] P.L. 111-203, § 1017(a)(2), 124 Stat. 1376, 1975, July 21, 2010, *codified at* 12 U.S.C. § 5497.

protection is simply too central to economic stability to subject to the politic of the appropriations process.

S. 737, the Responsible Consumer Financial Protection Regulations Act of 2011 (the "Moran Bill") would subject the CFPB—but no other federal bank regulator—to the annual appropriations process. I strongly urge the Committee to reject this proposal. Subjecting the CFPB to the appropriations process would do far greater damage to consumers and the economy than any wayward action by the CFPB. If the CFPB is subject to appropriations, it will be a cyclical and ultimately ineffective agency, as its budget becomes a political football.

GAO Review

The CFPB's budget is subject to an annual audit by the Government Accounting Office, with the results reported to Congress.[23] No other federal bank regulator is subject to such an audit.

Financial Stability Oversight Council Veto

CFPB rulemaking is subject to a veto by the Financial Stability Oversight Council. This is unique for federal bank regulators.[24] The OCC and OTS's preemption actions, for example, are not subject to review by other federal regulators, even though they were a key element in fostering the excesses in the housing market.[25] The FSOC veto provides an unusually strong check on CFPB rulemaking, not least because no CFPB director would wish to risk a FSOC rebuke.

Congressional Oversight

The CFPB is subject to oversight by Congress itself. The CFPB Director must make periodic reports to Congress and appear before Congressional committees.[26] This Committee's actions, as well as those of the House Financial Services Committee and House Government Oversight and Reform Committee, show that this oversight is serious, diligent, and exacting, with no less than six hearings in the past four months focused on the CPFB.[27] Congressional oversight is perhaps the best guarantor that the CFPB will not abuse the authority delegated to it.

Moral Suasion

The CFPB Director may be removed only "for cause," a standard that also applies to the Federal Reserve Board, the FDIC, the FTC, and SEC. The standard may also apply to the OCC

[23] P.L. 111-203, § 1017(a)(5), 124 Stat. 1376, 1976-77, July 21, 2010, *codified at* 12 U.S.C. § 5497.

[24] The only other federal regulatory agency that I have identified that is subject to an override by another agency is the Public Company Accounting Oversight Board (PCAOB). The Supreme Court found the PCAOB structure to be unconstitutional. Free Enterp. Fund v. Pub. Company Accounting Oversight Bd., 130 S. Ct. 3138 (2010).

[25] *See* Watters v. Wachovia Bank, N.A., 550 U.S. 1 (2007) (upholding OCC preemption of state attempts to regulate subprime mortgage lenders); Adam J. Levitin, *Hydraulic Regulation: Regulating Credit Markets Upstream*, 26 YALE J. ON REG. 143 (2009) (detailing OCC and OTS preemption of state mortgage regulations without substituting equivalent federal regulations).

[26] P.L. 111-203, § 1016, 124 Stat. 1376, 1974, July 21, 2010, *codified at* 12 U.S.C. § 5496.

[27] *See, e.g.*, "Consumer Financial Protection Efforts: Answers Needed," Hearing Before the House Committee on Oversight and Government Reform, July 14, 2011; "Mortgage Servicing: An Examination of the Role of Federal Regulators in Settlement Negotiations and the Future of Mortgage Servicing Standards," Joint Hearing Before the House Committee on Financial Institutions, Subcommittee on Financial Institutions and Consumer Credit and the Subcommittee on Oversight and Investigations, July 7, 2011; "Who's Watching the Watchmen? Oversight of the Consumer Financial Protection Bureau," Hearing Before the House Committee on Oversight and Government Reform, Subcommittee on TARP, Financial Services, and the Bailouts of Public and Private Programs, May 24, 2011; "Legislative Proposals to Improve the Structure of the Consumer Financial Protection Bureau," Hearing Before the House Committee on Financial Institutions, Subcommittee on Financial Institutions and Consumer Credit, April 6, 2011; "Oversight of the Consumer Financial Protection Bureau," Hearing Before the House Committee on Financial Institutions, Subcommittee on Financial Institutions and Consumer Credit, Mar. 16, 2011.

and OTS Director; the United States Code is silent in this respect.[28] Even when a for-cause dismissal standard applies, however, a President may exercise considerable moral suasion over the head of an agency. There are few individuals that would refuse a Presidential request to resign even if they were within their legal rights to do so.

III. Restructuring the CFPB from a Unitary Directorship to a Five-Person Commission

One proposal for "reforming" the structure of the CFPB—the Moran Bill, S. 737 (and its House analog, the Bachus Bill, H.R. 1121)—would replace the CFPB's unitary director with a five-person commission.[29] While I understand the belief that a five-person commission might result in a more collegial rule-making discourse, there are several strong reasons to eschew such a structure, which will ultimately render the CFPB less effective and less accountable.

In structuring administrative agencies, Congress has variously elected between two models: the Founders' traditional model of a unitary agency director and the Progressive/New Deal era model of five-person commissions. The Founding Fathers' model for executive agencies featured a single principal officer appointed by the President with the advice and consent of the Senate. This model is reflected in the federal cabinet agencies. Thus, the Treasury is governed by a single Secretary, rather than by committee. The traditional unitary director model is also featured in the Office of Comptroller of the Currency, the Office of Thrift Supervision, the Internal Revenue Service, the Social Security Administration, Medicare, and the Environmental Protection Agency. This model enhances accountability and enables streamlined, decisive leadership and decision-making.

An alternative agency model arose during the Progressive era and was warmly embraced by New Deal liberals. That is the five-person commission. Thus, Progressive era agencies like the Federal Trade Commission and the classic New Deal agencies like the Securities and Exchange Commission, Federal Deposit Insurance Corporation, and National Labor Relations Board feature five-person commissions, and the National Credit Union Administration has a three-member board. The multi-member commission model is also featured by the Federal Reserve Board of Governors, the Federal Communications Commission, Federal Election Commission, Equal Employment Opportunity Commission, Federal Mine Safety and Health Review Commission, Commodities Futures Trading Commission, and Consumer Product Safety Commission. For some of these agencies there is a limit of the number of commissioners who may belong to any political party, while other agencies, like the Federal Reserve Board, have geographic appointment requirements.

The scholarly literature on agency design has not achieved any consensus as to the superior form of organization.[30] Instead, it recognizes that there are trade-offs involved. Thus, the five-person commission model encourages more collegial discourse and deal-making, but

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[28] An internal Treasury Department Legal Memorandum assumes as a passing point that the OTS Director (and presumably the Comptroller) serves at the pleasure of the President, but this memorandum has no controlling legal effect, and the United States Code is silent on the matter. See Memorandum Opinion for the General Counsel, Department of the Treasury, and the Chief Counsel, Office of Thrift Supervision, Re: Post Employment Restriction of 12 U.S.C. § 1812(e) (Sept. 4, 2001).

[29] S. 737, the Responsible Consumer Financial Protection Regulations Act of 2011 (the "Moran Bill"); H.R. 1121, the Responsible Consumer Financial Protection Regulations Act of 2011 (the "Bachus Bill").

[30] *See, e.g.*, Rachel E. Barkow, *Insulating Agencies: Avoiding Capture Through Institutional Design*, 89 TEX. L. REV. 15 (2011). The last time the federal government formally examined the question of agency structure, in 1971 during the Nixon Administration, the President's Advisory Council on Executive Organization (known as the "Ash Council," after its Chairman Roy L. Ash) issued as *Report on Selected Independent Regulatory Agencies*, Feb. 11, 1971, that recommended replacing multi-member commissions with single-executive agencies.

comes at the expense of accountability and efficiency. Moreover, it often provides little protection for the minority party on the commission; minority commissioners' views are typically disregarded and provide extremely limited protection against abuses by the majority.

In the case of the CFPB there are particularly salient reasons *not* to adopt a multi-member commission structure. For consumer financial protection, we should want a structural bias toward action rather than inaction. We have seen the result of financial regulators asleep at the switch. The price tag was hundreds of billions of dollars in taxpayer-funded bailouts of Wall Street. It is hard to believe that any member of Congress would want to replicate such a situation. Ensuring that the CFPB retain an organization structure than enables efficient, issue-driven decision-making requires maintaining the CFPB's current single director structure.

The CFPB's Unitary Directorship Fosters Efficient Decision-making and Avoids Gridlock and Horse-Trading

A single director is able to exercise decisive leadership in promulgating rules and enforcing them. A single director also does not have to engage with horse-trading with other commission members to wrangle up votes on an issue. This means that each issue will be decided on its own merits, rather than as part of a multi-issue deal involving commissioners' pet projects. Such a streamlined decision-making structure avoids the gridlock that often faces commissions. The five-person commission structure proposed by S.737 and H.R. 1121, would induce inefficiency in government, as it permit rules to be promulgated only when a quorum (generally 3/5 commissioners) affirmatively votes for the rules.

The quorum requirement is a particular concern because of the frictions in the Senate confirmation process. Numerous administrative and judicial positions remain unfilled today because of the difficulty at achieving confirmation of nominees given the Senate's internal rules that effectively create supermajority requirements not found in the Constitution. The effect has been not only to block many nominations, but also to chill potential nominations. The Senate's confirmation process has become so dysfunctional that a bipartisan group of Senators (including Majority Leader Reid, Minority Leader McConnell, and Senators Schumer, Alexander, Collins, and Lieberman) has introduced legislation, S. 679, which would reduce or streamline the number of executive branch positions requiring Senate confirmation by one-third.

This state of affairs presents the most serious threat to the effectiveness of the modern administrative state—federal agencies have had to operate without directors or chairmen or even quorums because of the increased frictions in the confirmation process. As a result, these agencies are less effective or simply ineffective at ensuring that the law is carried out. Thus, in recent years, the Federal Trade Commission, the Consumer Product Safety Commission, and the National Labor Relations Board have all gone through spells where they have been unable to operate because a quorum did not exist.

Simple math says that five confirmations are more difficult to achieve than a single confirmation (even if multiple appointments sets up opportunities to make political deals on appointments). Put differently, adopting a five-person commission instead of a unitary directorship is likely to hobble the CFPB. While I would hope that the production of gridlock is not the motivation for such a proposal, it could well be the consequence.

A Five-Person Commission Would Create Unnecessary Big Government Bloat and Waste

Changing from a unitary directorship to a 5-person commission would also contribute to big government bloat. There is no reason to pay five people top-of-the-executive-branch pay scale salaries and benefits for work that could be done by one person, not to mention the personal staff, office space, and other accommodations for five commissioners. A five-person commission is simply wasteful and should not be pursued, particularly when we are facing a federal budget crisis.

A Five-Person Commission Would Reduce CFPB Accountability

A single CFPB director is clearly accountable to both Congress and the American people. A CFPB Director who oversteps his authority or who fails to do enough to protect consumers cannot deflect blame for his actions. A gaggle of commissioners, on the other hand, can always avoid responsibility by pointing to the other four people who make up the commission. If Congress wants to maximize CFPB's accountability, responsiveness, efficiency, and effectiveness, the unitary directorship should be retained.

The CFPB's Unitary Directorship Is Necessary as a Counterweight to the OCC

A major reason for the creation of CFPB was to create a counterweight to the strength of the federal bank regulators. The primary mission of federal bank regulators is to ensure the safety-and-soundness of their regulatory charges. ***Safety and soundness means, first and foremost, profitability.***

It is axiomatic that a financial institution that is not profitable cannot be safe and sound. Consumer financial protection, however, is often inconsistent with bank profitability. Financial institutions only engage in unfair, deceptive and abusive acts and practices because they are profitable; they are not done for spite or Sadism. Predatory mortgage lending, for example, exists only because it is profitable.

Federal bank regulators have repeatedly shown that they will favor bank profitability over consumer protection. Thus, a major impetus for the creation of the CFPB was to separate consumer protection regulation from safety-and-soundness regulation so that consumer would not be subordinated to bank profitability.

To do so effectively, however, it is necessary to give the CFPB the same tool-kit as the most powerful of the federal bank regulators, the Office of the Comptroller of the Currency (OCC). The OCC has a unitary director, an independent source of funding, and substantial statutory independence from Treasury. This allows the OCC to act quickly and decisively and without undue quotidian political pressure and without the politicking and horse-trading that goes on with multi-member commissions. The OCC has proven itself to be a capable and aggressive advocate for the interests of national banks, even at the expense of the national interest. Indeed, the OCC has insisted on such an extreme view of its ability to preempt state law, even post-Dodd-Frank that it was rebuked by the Treasury Department, an unprecedented occurrence.[31]

The CFPB is deliberately designed to be a parallel and counterweight to the OCC to allow consumer protection concerns to be given equal weighting to bank profitability (also

[31] Letter from Treasury General Counsel George W. Madison to Acting Comptroller of the Currency John Walsh, June 27, 2011 (stating that OCC's approach to preemption was incompatible with the text and legislative history of Section 1044(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act).

known as safety-and-soundness) and avoid the problems that result when consumer protection is subordinated to bank profitability. This requires having a unitary directorate, rather than a multi-member commission.

If the Committee is convinced, however, that a five-person commission is the proper structure for the CFPB, I would urge the Committee to also adopt a five-person commission structure for the Office of Comptroller of the Currency, which would then be the sole federal financial regulator with a unitary directorship. What is good enough for consumers should be good enough for banks.

I would urge the Committee against adopting a five-person commission model for the CFPB. The CFPB has not yet had a chance to get up and running and there is no reason to think that the unitary directorship is a particular problem; the CFPB should be given a chance to prove itself before it is reconfigured by Congress. Given the multiple safeguards that already exist to ensure that the CFPB does not act arbitrarily and capriciously action, it becomes apparent that changing the CFPB from a unitary directorship to a five-member panel would add little. Instead, switching to a five-member panel would tilt the balance at the agency to gridlock and inaction, would add unnecessary big government bloat, and would reduce accountability.

IV. FINANCIAL STABILITY OVERSIGHT COUNCIL REVIEW AUTHORITY

A second area of proposed "reform" of the CFPB would be to lower the thresholds for the Financial Stability Oversight Council veto. I am not aware of a Senate bill that proposes such a change, but H.R. 1315, the Consumer Financial Protection Safety and Soundness Improvement Act, (the "Duffy Bill"), would amend section 1023 of the Dodd-Frank Act[32] to reduce the thresholds for a Financial Stability Oversight Council veto of CFPB rulemaking. It would do so in two ways.

First, it would reduce the necessary vote from a supermajority of 2/3s of the FSOC members (including the CFPB Director), that is 7 out of 10 votes if all members were present, to a simple majority of FSOC members, not including the CFPB, that is 5 of 9 votes. It would also reduce the necessary finding from the CFPB "regulation or provision would put the safety and soundness of the United States banking system or the stability of the financial system of the United States at risk" to a less exacting finding merely that the CFPB rulemaking is "inconsistent with the safe and sound operations of United States financial institutions." Finally, by deleting section 1023(c)(5) of the Dodd-Frank Act, the bill would require the FSOC to take a vote if any FSOC member raised an objection to a CFPB rulemaking.

The FSOC veto power provides an unnecessary and possibly unconstitutional check on the CFPB and should be eliminated, rather than made more stringent.[33] Irrespective, *the Duffy Bill's proposed finding for an FSOC veto would render virtually every CFPB rulemaking in doubt.* Indeed, under the Duffy Bill's proposed standard—whether the CFPB rulemaking is "inconsistent with the safe and sound operations of United States financial institutions"—it would be impossible for the CFPB to implement several recent pieces of Congressional

[32] P.L. 111-203, § 1023, 124 Stat. 1376, 1985, July 21, 2010, *codified at* 12 U.S.C. § 5513.

[33] I would urge that if Congress adopts the five-person commission model for the CFPB per the Bachus Bill, it should eliminate the FSOC veto over CFPB actions.

legislation, including Title XIV of the Dodd-Frank Act, the Mortgage Reform and Anti-Predatory Lending Act.[34]

As noted, above, safety and soundness means, at core, profitability. To the extent that a proposed CFPB regulation would reduce the profitability of a financial institution, it would reduce that institution's safety and soundness. Thus, any CFPB regulation, even if it merely increased compliance costs, would be "inconsistent with the safe and sound operations" of a financial institution.

While bank regulators have argued that consumer protection goes hand in hand with safety and soundness because it is unsafe for a bank to systematically exploit its customers or engage in unfair and deceptive practices, the run up to the financial crisis provides clear evidence that federal bank regulators were unwilling to put the brakes on unfair and deceptive mortgage lending. Similarly, the run up to the Credit CARD Act of 2009 shows that federal regulators were unwilling to act on unfair and deceptive credit card acts and practices until Congress itself started to move. Only then did the Federal Reserve, OTS, and NCUA hustle to amend their unfair and deceptive acts and practices (UDAP) regulations.

To understand just how overbroad the Duffy Bill's proposed rule is, consider, for example, consider if there had been a CFPB in 2005, and it had proposed a rule that would have severely restricted the underwriting of payment-option adjustable-rate mortgages (so-called pick-a-pay mortgages) to borrowers who have demonstrated an ability to repay. Such a rulemaking would have put an end to the "Countrywide special," that was the hallmark of Angelo Mozillo and Countrywide, the nation's largest mortgage lender.

Such a restriction would have significantly curtailed Countrywide's mortgage lending business, and would surely have resulted in the OCC or OTS demanding an FSOC veto. Yet such a move could hardly be called radical. Congress itself passed just such a requirement in section 1411 of the Dodd-Frank Act,[35] and a parallel requirement for credit cards in section 109 of the Credit C.A.R.D. Act of 2009.[36]

Indeed, we actually have an example from 2008 of a bank regulator challenging a proposed consumer financial protection regulation on safety-and-soundness grounds. In August 2008, Comptroller of the Currency John C. Dugan wrote to the Federal Reserve Board to urge it to insert two significant exceptions to the proposed Regulation AA (governing unfair and deceptive acts and practices) rule on credit cards that would limit the ability of card issuers to reprice (or, colloquially, "rate jack") cardholders.[37] Duggan wrote that the restrictions "raise safety and soundness concerns" because they limited the ability of issuers to re-price their loans if issuers determined that the risk profile of the customer had worsened.[38] If the CFPB had proposed such a rule, the OCC would surely have challenged it before the FSOC as "inconsistent

[34] P.L. 111-203, §§ 1401-1498, 124 Stat. 1376, 2137-2212, July 21, 2010.

[35] P.L. 111-203, § 1411, 124 Stat. 1376, 2142, July 21, 2010, *codified at* 15 U.S.C. § 1693c ("no creditor may make a residential mortgage loan unless the creditor makes a reasonable and good faith determination based on verified and documented information that, at the time the loan is consummated, the consumer has a reasonable ability to repay the loan, according to its terms, and all applicable taxes, insurance (including mortgage guarantee insurance), and assessments.").

[36] P.L. 111-24, 123 Stat. 1743, § 109, May 22, 2009, *codified at* 15 U.S.C. § 1665e ("A card issuer may not open any credit card account for any consumer under an open end consumer credit plan, or increase any credit limit applicable to such account, unless the card issuer considers the ability of the consumer to make the required payments under the terms of such account.").

[37] Letter from Comptroller of the Currency John C. Dugan to Jennifer Johnson, Secretary, Board of Governors of the Federal Reserve System, Re: Docket Number R-1314, August 18, 2008.

[38] *Id.*

with the safe and sound operations of United States financial institutions." Yet, Congress itself passed an even tougher restriction on credit card repricing less than a year later.[39]

Under the Duffy Bill's standard, several laws passed by Congress in recent years, such as the Credit C.A.R.D. Act and the Mortgage Reform and Anti-Predatory Lending Act would themselves be unenforceable by regulation because the laws themselves might reduce bank safety-and-soundness (i.e., profitability), so any faithful rule-making would have to as well. The effect of the Duffy Bill would be to eviscerate several recent, popular, consumer financial protection statutes.

The CFPB is a new agency tasked with protecting the financial security of American families, ensuring that they can get the information necessary to make responsible, informed financial choices. Congress created the Bureau to ensure that American families can trust the financial products they use to help them achieve their goals, rather than ensnare them with tricks and traps that lead to financial distress. The Duffy Bill's proposed expansion of the FSOC veto would place bank profits ahead of the well-being of American families, and would put us on a return course to the financial crisis of 2008.[40]

CONCLUSION

The Consumer Financial Protection Bureau has not even had an opportunity to begin to exercise its regulatory authority. It is simply premature to consider reforms to its oversight, as it is not yet clear whether any changes to the oversight structure are needed, much less what those changes are. At this point, concerns about oversight are simply cover for political attacks on the CFPB's very existence. Let's give the CFPB a chance to prove itself and not return to the pre-2008 period when the lack of effective consumer financial protection facilitated the destructive housing bubble and financial collapse from which we have still not recovered.

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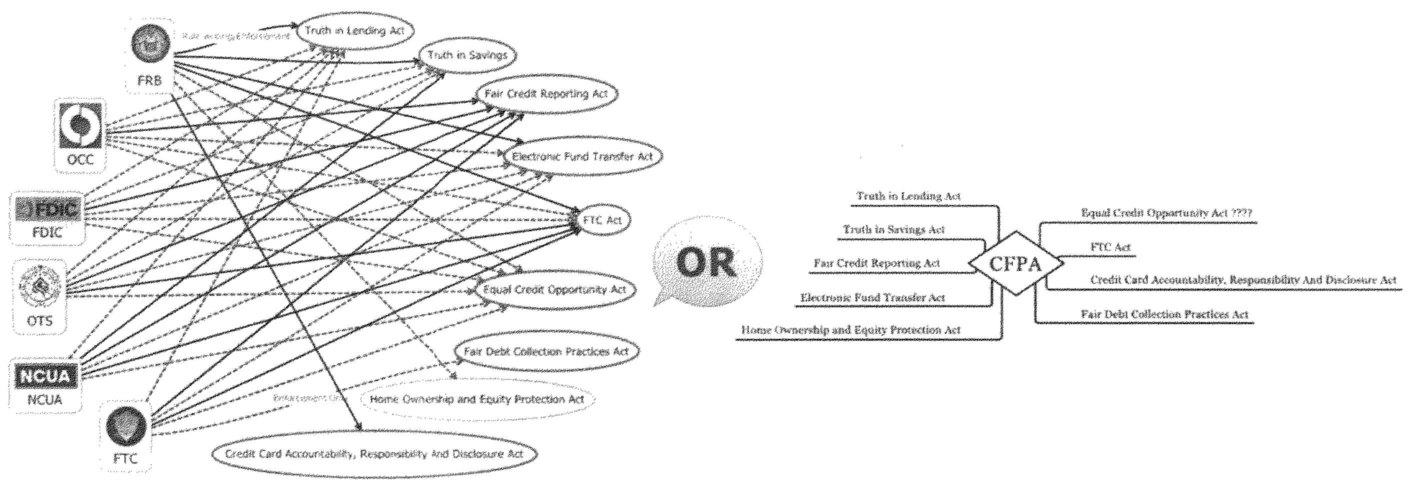
[39] P.L. 111-24, § 101, 123 Stat. 1736-37, May 22, 2009, *codified at* 15 U.S.C. § 1666i-1.

[40] I would also note that the FSOC veto under section 1023 of the Dodd-Frank Act is already of dubious constitutionality. On June 28, 2010, a fortnight before the enactment of the Dodd-Frank Act, the Supreme Court handed down its judgment in a case captioned *Free Enterprise Fund v. Public Company Accounting Oversight Board*, 130 S. Ct. 3138 (2010). In this case, the Supreme Court held that it was an unconstitutional violation of the separation of powers to restrict the President in his ability to "remove a [principal] officer of the United States, who is in turn restricted in his ability to remove an inferior officer, even though that inferior officer determines the policy and enforces the laws of the United States". *Id.* at 3147. This ruling raises the question of whether by giving the FSOC veto power over CFPB rulemaking, Congress has impermissibly restricted the power of the President to "take Care that the Laws be faithfully executed" through his appointee as Director of the Bureau of Consumer Financial Protection. It also raises the concern that the CFPB is not truly an independent agency as it would be subject to a veto exercised in part by cabinet agencies.

The existing FSOC veto power is already constitutionally suspect, and proposals such as the Duffy Bill, which would make exercise of the veto authority mandatory and on a hair-trigger basis, would only increase the likelihood that section 1023 of the Dodd-Frank Act offends the Constitution. I would strongly urge the Senate to request opinion of counsel on the FSOC veto's constitutionality before taking any action in regard to it.

Figure 1. The Current Consumer Financial Protection Regulatory Structure vs. the Regulatory Structure with the Consumer Financial Protection Bureau.[41]



RESPONSE TO WRITTEN QUESTION OF SENATOR REED FROM MICHAEL D. CALHOUN

Q.1. There are some who support loan modifications that are achieved through interest rate reductions, term extensions, or the forbearance of principal but oppose loan modifications that come in the form of principal reductions.

- Can a loan modification that involves principal reduction maximize value for the bank, investor and homeowner? Could you explain how this might be the case?

A.1. Principal reduction is an important tool for avoiding unnecessary foreclosures and improving our overall housing market. Studies, such as those by Amherst Securities, show that if homeowners are deep underwater on their loans, owing far more than their home is worth, the probability is high that the home will go into foreclosure. This is a loss for not only the homeowner, who is forced to leave the house, but also the investors who own the loan or mortgage security, as houses are selling for very low prices at foreclosure sales, and the investors receive far less than they would receive from a modified loan with a reduced principal. In addition, these avoidable foreclosures are adding to the oversupply of foreclosed houses that continue to drag down the housing market and the overall economy. Since both the homeowner and the investor benefit from a responsible loan modification, a number of servicers have begun programs that provide principal reduction as part of their loan modification procedures. One program, for example, offers the homeowner reduced principal in exchange for an agreement to share with the investor a portion of any home appreciation in the event the house value goes up and the house is sold. Several structural impediments associated with the securitization process discourage optimal use of principal reductions. These include the general misalignment of servicer incentives with the investors' interests, as well as conflicts of interest for servicers who also own second mortgages on the same property.

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

AARP
The power to make it better.

STATEMENT FOR THE RECORD

SUBMITTED TO THE

SENATE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

on

"Enhanced Consumer Protection After the Financial Crisis"

July 19, 2011

AARP
601 E Street, N.W.
Washington, D.C. 20049

For further information, contact:
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On behalf of our members and all Americans age 50 and older, AARP appreciates the opportunity to submit written comments in connection with the July 19, 2011, hearing of the Senate Banking Committee on "Enhanced Consumer Protection after the Financial Crisis."

Consumer Financial Products and the Older American

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

Although older households long have been considered among the most frugal and resistant to consumer debt, changing economic conditions -- particularly declining pension and investment income and rising costs for basic expenses such as prescription drugs, health care, and utilities -- have forced many seniors to rely increasingly on credit to make ends meet.[1]

To meet the challenges of this dynamic marketplace and ensure the economic security of older persons, AARP has recommended that the quality of consumer information in the marketplace be improved to increase the level of consumers' financial literacy, particularly among baby boomers, minorities and low-income people.

But education alone is not enough. Many people often are unaware of the terms and conditions that govern credit products because the required legal documents and consumer disclosures are beyond the understanding of a large portion of the population. When coupled with bad advice, abusive practices, or fraud, the variety and complexity of credit products can be intimidating and confusing for even the most well informed consumers. As such, we must also commit to increasing consumer protections to prevent harmful financial services and practices that – as the recent economic turmoil clearly demonstrates – threaten not only individual financial security, but also that of the nation.

The scope and extent of abusive and deceptive consumer practices is astounding. Billions of dollars are lost every year through various types of fraudulent and deceptive consumer practices that affect thousands of consumers. Moreover, older Americans are

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[1] *See* Deborah Thorne, Elizabeth Warren, Teresa A. Sullivan, *Generations of Struggle* (June 2008) available at http://www.aarp.org/money/budgeting-saving/info-06-2008/2008_11_debt.html.

disproportionately affected by these deceptive consumer practices. Although older people make up just 12 percent of the population, they constitute a full 30 percent of the victims of consumer fraud crime. Women, who make up an increasingly larger percentage of the older population by virtue of a longer life expectancy, are the majority of the victims. Consequently, consumer fraud is listed by every state as the major non-violent crime perpetrated against people.[2]

Not only are older people more likely targets of consumer fraud, they are also different from younger consumers in the intensity of the overall impact of such abuse on their lives. Having lower or fixed income and fewer years of work to recover from a financial setback makes older people particularly vulnerable. Fear of losing independence and control over their finances may contribute to their reluctance to pursue a remedy when an abuse occurs. Many consumers do not know how or to whom to complain even if they do want to seek a remedy.

It is well established that the failure of the regulatory system to rein in abusive types of consumer loans in areas where federal regulators had clear authority to act, and either chose not to do so or acted too late to stem serious problems in the credit markets, was a major factor in the recent financial crisis. As such, a key goal for AARP in the Wall Street Reform and Consumer Financial Protection Act (Dodd-Frank Act) was strengthened consumer protection to restore market accountability and responsibility, rebuild confidence, and ensure the stability of the financial markets. Surveys conducted by AARP demonstrate that Americans age 50+, regardless of party affiliation, want Congress to act to hold financial institutions accountable.

When Congress passed the Dodd-Frank Act, it did so to address in a coordinated fashion some of the worst abusive practices that put all Americans at risk. AARP supported the creation of the Consumer Financial Protection Bureau (CFPB) with the sole mission to serve as an independent watchdog for American consumers. The CFPB will help ensure that consumers have the information they need to make the financial choices that are best for them and prevent abusive and deceptive financial practices. A streamlined and coordinated approach to financial regulation and consumer protection will better protect the financial security of all Americans.

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[2] *See Top 10 List Of Consumer Complaints of 2008 Resource List*, (March 2010), available at http://naag.org/top-10-list-of-consumer-complaints-of-2008-resource-list.php (listing Debt Collection, Auto Sales, Home Repair/Construction, Credit Cards / Internet Goods and Services (tie), Predatory Lending/Mortgages, Telemarketing/Do-Not-Call, Auto Repair, Auto Warranties / Telecom/Slamming/Cramming (tie) as top 10 consumer complaints).

In particular, the CFPB must address the following practices that continue to threaten the financial security of older people:

Mortgages

Bad mortgage lending was a leading cause in the downturn of the economy. Reform of mortgage origination and servicing practices is an essential element in its recovery. Although interest rates are currently at historic lows, the housing sector generally, and mortgage lending in particular, are in a holding pattern. While Congress has enacted significant reform targeted at the most egregious mortgage origination abuses, including the inability to repay, kickbacks that drove up the price of borrowing, and curbs on the toxic adjustable rate mortgages that plagued the market in recent years, a great deal of work remains to be done. The mortgage origination protections must be implemented with clear and strong regulations. Just as importantly, homeowners must be protected from the abusive servicing practices that add high and often unwarranted fees and insurance to their mortgage accounts; from an inadequate "loan modification" process that saves few homes; and from the shoddy and fraudulent conduct that underlies far too many of the foreclosures nationwide.

It has long been understood that older homeowners were often the targets of the predatory lending practices that began in the early 1990's. Older homeowners had equity in homes they had owned for decades. Yet they were living on fixed incomes, making home maintenance and repair difficult. They were – and remain -- often vulnerable: they may be without a support network; conversely, they may be rearing grandchildren and otherwise providing housing and support for other family members; or they may be suffering from some diminished capacities. Experience with countless older homeowners over the years has repeatedly demonstrated that, despite good – often sterling – credit ratings, they were steered to subprime lenders whose unscrupulous practices are now well documented.[3] Despite legal and legislative advocacy by AARP and countless others, far too many older Americans who entered into questionable mortgages currently face foreclosure and eviction from homes they have lived in for decades.

AARP believes the CFPB must play a major role in ensuring a fair mortgage marketplace going forward and in redressing past wrongdoing.

Credit Cards

Despite enacting important protections in 2009, more must be done to protect consumers from unfair or predatory practices, hidden fees, and complicated terms and conditions in

[3] *See* Alison Shelton, *AARP Insight on the Issues 9* (Sept. 2009), http://www.aarp.org/money/credit-loans-debt/info-09-2008/i9_mortgage.html.

credit card agreements. Consumers need protection from efforts to evade the protections of the CARD Act, as well as the marketing of expensive and predatory credit card products, and complex fee structures that hide the true expense of credit and make it difficult for consumers to shop for the lowest priced credit card products that meet their needs.

Overdraft Fees

Despite new rules requiring consumers to "opt in" before being charged overdraft fees on their ATM and debit cards, many consumers continue to be charged unfair overdraft fees by banks. The most vulnerable consumers – those with the least amount of money – are often hardest hit by practices such as aggressive or deceptive inducement to opt in to overdraft protection, reordering of transactions to increase fees, and steering consumers into accounts or fee structures that maximize imposition of fees without informing them of less expensive overdraft protection options. Consumers should be protected from banking practices that unfairly siphon off their limited income.

Prepaid Debit Cards

Consumers increasingly use prepaid debit cards for purchases. In part this has resulted from government benefit administrators utilizing prepaid debit cards to help reduce the cost of benefits disbursement. Despite the convenience provided by such cards, they can be very costly to consumers. Many charge high fees for periodic statements or transaction information, to check balances, decline transactions, to access funds at an ATM, or to load funds onto the card. Moreover, consumers do not understand that prepaid debit cards carry less protection than other payment instruments such as ATM or credit cards. Prepaid cards do not give consumers full protection from loss, theft or unauthorized charges. They may also open unbanked consumers to the risk that payday lenders may seek to secure loans with the receipt of public benefits deposited onto prepaid cards. In light of the increasing use of such cards, protections should be enhanced to ensure that consumers are not harmed by high fees, inappropriate assignment of exempt public benefits, and misrepresentations of the terms and conditions for use of such cards. In particular, government benefits administrators must take additional steps to protect beneficiaries against high costs and fees.

Other Abusive Loans

High cost lending practices by both mainstream and alternative financial services providers that charge high fees and interest costs that can exceed 400% seriously threaten the financial security of the most vulnerable borrowers.[4] Vulnerable borrowers who cannot meet their most basic needs of food, shelter, or healthcare are most often the targets. Deceptive practices include those by payday, auto and auto title lenders, as well as car dealers, who often exact high tolls on those who can least afford it. At tax time, many consumers are targeted by tax preparation companies to get an instant refund -- really a loan – for which consumers are unknowingly charged hefty tax preparation and loan fees. Billions of dollars of Earned Income Tax Credits -- intended to keep hard working families out of poverty -- are siphoned off in high fees and charges; sadly, most of the borrowers are eligible to have their taxes prepared for free, with quick refunds through electronic deposit, without paying all the fees. Federal preemption of state consumer protection laws has opened the door to increased abuse, leaving consumers further exposed to unregulated and often deceptive lending practices. It is time to close the door to abusive high cost lending practices, no matter who the lender.

Credit Reports

Fair and accurate credit reporting is essential to protecting the financial security of consumers. A consumer's credit report impacts not only the price and availability of credit but also of auto and homeowner's insurance, access to housing, and opportunities for employment. Unfortunately, consumers have difficulty correcting their credit reports when they contain significant inaccuracies that result from mistakes, incorrect and outdated information, fraudulent accounts due to identity theft, and mixed up files of different consumers. Consumers also need better guidance on how to check and correct their credit reports. Because so few consumers understand what will cause a decrease or increase in their scores, or the magnitude of the impact of particular actions such as closing a credit card account, making a late payment or filing for bankruptcy, more consumer education is needed to give them consumers he tools they need to improve their financial outlook. Lack of information and the wide variety of credit scores in the marketplace makes consumers more vulnerable to predatory lending, credit repair scams or higher priced lending and insurance than for which they should qualify. Much more needs to be done to ensure credit reporting is fair, accurate, and transparent.

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[4]*See* Ann McLarty Jackson, Donna V.S. Ortega, Elizabeth Costle, George Gaberlavage, Naomi Karp, Neal Walters, Vivian Vasallo, *A Portrait of Older Underbanked and Unbanked Consumers: Findings from a National Survey* (Sept. 2010), available at http://www.aarp.org/money/credit-loans-debt/info-09-2010/D19394.html.

Debt Collection

The Federal Trade Commission and state attorneys general have received more complaints about the debt collection industry than any other for more than ten years, and the number of complaints is increasing. As more and more consumers carry ever higher levels of debt, the debt collection industry, assisted by technological advances in data storage and communications capabilities, has been transformed into a trillion dollar debt buying and collection industry over the span of a decade.

Debt once considered to be uncollectible is charged off by creditors and sold at auction for pennies on the dollar. Using increasingly aggressive and often illegal collection tactics, collectors pursue alleged debtors well after the statute of limitations has run, often with little or no documentation to prove the ownership or amount of a debt. Unrepresented debtors who do not understand how to protect their interests or assert valid defenses have little, if any, ability to protect themselves or may unknowingly agree to extend the time a debt may be collected by making a minimal payment in an attempt to end harassing collection attempts.

Abusive collection tactics have caused significant harm and suffering to consumers, as well as taxed the resources of state Attorneys General. The high level of fraud inherent in the current collection environment should be addressed comprehensively.

Forced Arbitration

Consumers who purchase financial products or services routinely are required to give up their access to justice if the company violates the law. By inserting a forced arbitration agreement in a standard contract, a business can exempt itself from any possibility that it will be held accountable in any meaningful way for violations of the law. Forced arbitration clauses already are ubiquitous in contracts of adhesion for every type of consumer service and product. The recent Supreme Court decision in *AT&T Mobility, LLC v Concepcion*[5] undermines consumer challenges to forced arbitration clauses because the Supreme Court has held that federal law preempts certain state contract law defenses. Forced arbitration creates an unlevel playing field for consumers, without review by any court – further eroding consumer protections. The ability of corporations to include a forced arbitration clause in a standard form contract places an even higher burden on already cash strapped public enforcement systems to monitor harmful and deceptive acts and practices.

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[5] *AT&T Mobility, LLC v. Concepcion,* 131 S. Ct. 1740 (2011).

Conclusion

These examples are but a few of the abusive financial services practices that face consumers, demonstrating the significant need for the CFPB. One key lesson is clear – consumers need help to protect themselves in the increasingly complex and rapidly changing technological global marketplace. As was so painfully demonstrated just a few short years ago, the threats to personal financial security are threats to the nation's financial stability and security. Thank you for this opportunity to share AARP's views.