
The Consumer Financial Protection Agency Act of 2009 Interpretation and Analysis

A. Introduction

On June 30, 2009, the Obama Administration sent to Congress legislative language creating a new consumer protection agency as part of its overall proposal to restructure the regulation of the financial services industry. On July 8, House Financial Services Committee Chairman Barney Frank (D-MA) introduced the proposed legislation as the Consumer Financial Protection Agency Act of 2009 (H.R. 3126). Chairman Frank's bill is very similar to the Administration's proposal, except that the prudential regulatory agencies retain all of their Community Reinvestment Act (CRA) responsibilities, and there is no assumption that OTS and OCC are merged into a new national bank regulator.

ABA supports filling gaps in the existing regulatory structure and strengthening the consumer protection mission of the prudential bank regulators. However, H.R. 3126 creates an enormous and unnecessary new federal bureaucracy that would harm the safety and soundness of insured depository institutions and would micro-manage the way consumer products and services are priced, developed, marketed, and delivered.

B. Overview

This legislation creates a controversial and intrusive new consumer regulatory agency with authority over consumer financial products offered by insured depository institutions, including credit unions, as well as state regulated entities engaged in financial services, including nonbanks and affiliates and subsidiaries of insured depository institutions ("covered institutions").

Rather than working with the existing regulatory structure to fill gaps in consumer protection, such as state-regulated mortgage brokers, the proposal would create an entirely new federal bureaucracy to take over the consumer protection functions of the Federal Reserve Board (Fed), Office of the Comptroller of the Currency (OCC), Office of Thrift Supervision (OTS), Federal Deposit Insurance Corporation (FDIC), National Credit Union Administration (NCUA), as well as certain consumer protection functions of the Federal Trade Commission (FTC).

The new entity, the Consumer Financial Protection Agency (the "Agency") would have sweeping rulemaking, supervision, and enforcement authority over virtually all consumer financial activities, except investment products and services regulated by the Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC) and insurance regulated by the states. Although investor protection and insurance products and services are not covered by the legislation at this time, it is clear that over time the Agency would be likely to assert authority over these products and services. Interchange fees are not specifically mentioned, but they could come within the new Agency's jurisdiction.

The cost of this massive and expensive new bureaucracy would potentially be paid for by imposing fees on all consumer financial transactions – potentially millions of check, credit card, and other transactions made by consumers each year.

C. Summary of Major Provisions

New Consumer Protection Agency. The new Agency would be an independent federal agency that would have sole supervisory, examination, and enforcement authority for protecting consumers of financial products.¹

Its jurisdiction would cover not just financial services and credit, savings and payment products, and related services, but all institutions that issue, provide, or service these products and services, and all entities that provide services to the institutions that provide these products, such as credit card networks.

This means that the Agency would not only have jurisdiction over thousands of banks, thrifts, and credit unions and their subsidiaries and affiliates, but also potentially hundreds of thousands of non-bank providers of financial services such as real estate brokers, appraisers, pawn shops, money remitters, check cashers, and unregistered investment advisors, among others.

- The Agency would have a five person board which would consist of four members appointed by the President and confirmed by the Senate (including the Director of the Agency), and the head of the “agency responsible for chartering and regulating national banks.”
- Board members must be U.S. citizens who have “strong competencies and experiences relating to consumer financial products or services,” but there is no requirement that they also have knowledge or expertise in bank safety and soundness issues. Further, unlike other similar laws, the bill contains **no political checks and balances** to prevent extreme positions from being taken. For example, no more than three of the five members of the FDIC’s Board can be from the same political party.

Funding and Fees. The Agency would have an enormous staff and budget which would be funded through fees on consumer financial products and services and assessments on any entity regulated by the Agency.²

- The legislation gives the Agency free rein to decide the amount and frequency of the fees or assessments it imposes and they can be based upon the outstanding volume of consumer credit accounts, total assets under management, or consumer financial transactions.
- It must also set up a “Victims Relief Fund” which is to be funded by any penalties and fines imposed on covered entities.

Regulation. H.R. 3126 delegates sweeping new rule-making authority over consumer protection issues to the new Agency.

¹ Except that nothing in the Act affects the jurisdiction of the Department of Justice, the SEC or the CFTC.

² The Agency would be funded up front by appropriations, but any funds expended must be paid for through fees or assessments on any entity regulated by the Agency.

- It would have sole authority to promulgate and interpret regulations under twelve existing consumer laws such as the Truth in Lending Act (TILA), which includes the Home Ownership and Equity Protection Act (HOEPA); the Real Estate Settlement Procedures Act (RESPA); and, the Home Mortgage Disclosure Act (HMDA),³ and any future consumer financial services or fair lending laws. The Agency would have broad authority to require disclosures or restrictions in contract terms to prevent unfair, deceptive, or abusive practices.
- When it issues rules, the Agency must consider the potential costs and benefits to consumers and covered institutions, including potential reduction in access to credit, and it must consult with other federal agencies as appropriate. It has the authority to make exceptions, taking into consideration the total assets of the institution, volume of transactions, or other factors, including existing laws or regulations applicable to a particular consumer product or service.
- The Agency would **not** have the authority to establish a usury limit, unless explicitly authorized by law. However, states appear to be empowered to set limits on interest rates, which would apply to federally chartered institutions as well as state-chartered institutions. In addition, the Agency would have broad authority to influence interest rates in its design of standard “plain vanilla” financial products (see below).

Examination and Information Gathering. The Agency would have broad examination and information gathering authority, with significant ability to review institution operations. It would have the power to collect information from covered institutions and entities providing services to such institutions, and to make the information public (subject to confidentiality rules).

- This would include ATM information on the number and dollar amount of deposits, “Geo” coding of depositor addresses, and identification of depositor types – e.g., residential or commercial customer.
- It would also issue rules requiring covered institutions to collect small business loan data to facilitate compliance with fair lending laws. Specifically, with respect to any credit application the institution must ask whether the business is a women- or minority-owned business, compile and itemize information about the loan (such as the type and purpose of the loan, amount of the loan, census tract of the business, race and ethnicity of the owners, etc.), and submit the data to the Agency on an annual basis.

Administration. The bill provides details on how the Agency is to be structured and requires several reports. For instance:

- The Agency would have several functional units, such as a unit dedicated to providing information and other services to traditionally underserved areas or consumers, and a unit to deal with consumer complaints.

³ The “enumerated consumers laws” are the: Alternative Mortgage Transaction Parity Act, Electronic Funds Transfer Act, Equal Credit Opportunity Act, Fair Credit Reporting Act (with certain exceptions), Fair Debt Collection Practices Act, Federal Deposit Insurance Act (subsections (c),(d), (e) and (f) of section 41), Gramm-Leach-Bliley Act (sections 502-509), Home Mortgage Disclosure Act, Real Estate Settlement Procedures Act, S.A.F.E. Mortgage Licensing Act, Truth in Savings Act, and the Truth in Lending Act (which includes the Consumer Leasing Act, the Fair Credit Billing Act or the Home Ownership and Equity Protection Act).

- It would be required to establish a “Consumer Advisory Board” to provide it with information on emerging industry practices, and it is required to coordinate with other federal and state agencies to provide consistent regulatory treatment of consumer and investor products and services.
- The Agency would also be required to study and report on the effectiveness of consumer protection regulations at least every year.

Arbitration. The Agency would be required to review and potentially ban or restrict mandatory arbitration clauses. Banning arbitration clauses in consumer and other types of contracts could have severe consequences for both consumers and the financial services industry. For example, it would eliminate any realistic access to justice for consumers with modest-sized claims because they would not be able to join a class action, and most lawyers would not take their case on contingency unless their claim is worth at least \$60,000.

“Plain Vanilla” Consumer Products. The Agency would have authority to define standard consumer financial products or services (“plain vanilla”).

- The Agency could require covered institutions to offer such products alongside other product offerings.
- There would be a strong presumption that “plain vanilla” products are suitable for consumers. Conversely, alternative products may not be presumed to be suitable and would be subject to enhanced regulatory scrutiny with violations potentially triggering costly penalties.

Advertising and Disclosures. The Agency would be authorized to issue rules to ensure “effective disclosure of communication to consumers of the costs, benefits, and risks associated with any consumer financial product or service.”

The disclosures and communications must be “reasonable” and balance communication of the benefits of the product with significant risks and costs. This means that the Agency is empowered to dictate disclosure and marketing practices and subject covered institutions to liability under a vague “reasonableness” standard, and it would have broad authority over all consumer advertising by the financial services industry.

The Agency would have authority over both TILA and RESPA and would be required to issue a single, integrated federal mortgage disclosure form unless it determined that any rule issued by the Fed and the Department of Housing and Urban Development (HUD) prior to the Agency’s creation carried out the same purpose.

Restrictions on Terms and Practices. The Agency would be authorized to restrict product terms and provider practices to prevent unfair, deceptive, and abusive acts or practices for all credit, savings, and payment products.

- In making a determination that an act or practice is “unfair,” the Agency would have to engage in rulemaking and find that there is a reasonable basis to conclude that a particular

act or practice is likely to cause “substantial injury to consumers which is not reasonably avoidable by consumers” and not “outweighed” by any benefits to consumers or competition.

- The Agency would not be required to apply similar rulemaking standards to acts or practices that it considers to be “deceptive” or “abusive.” This authority could be used as a way to “indirectly” influence interest rates and prices without setting an official “usury” limit.
- It would have the authority to set transaction fees since the legislative text provides that it would be unlawful to “advertise, market, offer, sell, enforce, or attempt to enforce, any term, agreement, change in terms, *fee or charge* in connection with a consumer financial product or service that is not in conformity with this title or applicable rule or order issued by the Agency.” However, it does not provide any guidelines for the Agency to consider when establishing the appropriate level of fees.

Duty of Care. The Agency would be authorized to impose a duty of care on covered entities and all their employees who deal or communicate directly with consumers, and on any intermediaries such as an agent or independent contractor that deals directly with consumers to “ensure fair dealing with consumers.”

- The Agency may also prescribe rules regarding compensation practices to promote fair dealing (e.g., to limit “negative” consequences of incentive compensation), but this does not include any limits on the total dollar amount paid in compensation.
- The “duty of care” language is very broad and could be interpreted to cover bank employees such as account representatives, call center staff, and tellers, among others, if the Agency decides that they are providing advice with respect to any aspect of a transaction.

Consumer Access to Information. The bill requires a covered institution to make available in electronic form any information it has concerning a product or service a consumer has obtained from the institution. This includes information about any transaction and any account and any cost, charge or usage data relating to the account. Exceptions are provided for confidential commercial information, fraud, or information required to be kept confidential by law. The Agency is to develop standardized formats for this data.

Community Reinvestment Act (CRA). The Administration’s proposal would have required the Agency to assess a covered institution’s record of meeting CRA requirements, and the prudential regulators would have had to take the Agency’s assessment into account when evaluating applications. However, Section 161 (d) of H.R. 3126 makes it clear that the prudential regulatory agencies are to retain “any function” relating to their responsibilities under CRA.

Enforcement. Enforcement of new and existing consumer protection laws would be through a combination of private rights of action, administrative action by the Agency, the Department of Justice (DOJ), the prudential regulatory agencies, and state Attorneys General and other state authorities.

- Existing consumer protection statutes that contain private rights of action are not affected by any provision in the proposed Act, and the Agency would have administrative enforcement authority over covered institutions.
- The Agency would also have enforcement authority over nonbanking institutions, but state Attorneys General would have specific authority to enforce federal consumer protection laws. However, the Agency could intervene in any state action against a covered institution.
- The Agency would cooperate closely with DOJ, and the Department would have independent authority to enforce all statutes administered by the Agency.
- Although the Agency would have enforcement authority over nonbanks, all of its enforcement personnel would come from the existing banking agencies, and it is hard to see how enforcement will be consistent between insured depository institutions and nonbanks.

Impact on State Law. H.R. 3126 eliminates federal preemption of state consumer protection laws. In so doing, the bill would call into question the viability of the dual banking system and would eliminate all national markets for consumer financial products and services.

- Federal rules promulgated by the Agency would override “weaker” state laws, but the states are free to adopt “stricter” laws. States would also have concurrent authority to enforce the Agency’s regulations.
- The National Bank Act (NBA) and the Home Owners’ Loan Act (HOLA) would be amended to provide that state consumer protection laws apply to national banks and savings institutions, including their subsidiaries and affiliates, as long as those laws do not discriminate against national banks and savings institutions. In addition, the NBA and HOLA are amended to provide that their respective “visitorial” provisions would not prevent or restrict a state Attorney General’s demand for records or the Attorney General’s enforcement of federal or state law.
- State “consumer protection” laws are defined very broadly. They include any law that “accords rights to or protects the right of citizens in financial transactions concerning negotiations, sales, solicitations, disclosure, terms and conditions, advice, and remedies” or that “prevents counterparties, successors and assigns of financial contracts from engaging in unfair or deceptive acts of practices.” It also includes laws of “General Applicability” including any consumer fraud law and laws dealing with repossession, foreclosure, and collections.

The existing system allows national banks and savings institutions to provide products and services on a nationwide basis that provide important benefits to consumers in our highly mobile society. Consumers have benefitted because the national market encourages competition between in- and out-of-state financial services providers. Competition is very likely to be disrupted by a balkanized system of differing state laws. This will result in an enormous amount of litigation at the state level that would eventually make it impossible for federally chartered institutions to provide products and services on a nationwide basis, and as a result, there will ultimately be less innovation and consumer choice.

D. Conclusion

H.R. 3126 creates a new federal Agency that would ultimately harm consumers, the financial services industry, and the economy. The Agency could limit consumer choice by designing products and services that must be offered by all financial firms in preference to products and services designed by the private sector.

Banks and other financial providers would therefore have less incentive to offer innovative new products to consumers – alternatives that individual consumers might want such as lower down payments, rewards, combination accounts, and special internet features. For example, it is unlikely that creative products such as the NOW account (which led to interest on checking accounts), ATMs, rewards credit cards, and the 15-year mortgage would have been government designed and approved products.

The new Agency will be paid for by fees on transactions or accounts, or by assessments on covered entities. In addition, the proposal is filled with vague requirements that will greatly increase litigation. For example, there are very likely to be lawsuits challenging products that are not designed by the government or where the disclosure is not “reasonable.” As a consequence, there will be significant new compliance costs on banks, credit unions, and others that would raise the cost of credit.

The bill would also restrict the availability of credit and the creation of new jobs at the worst possible time. The tremendous uncertainty in lending created by the new Agency with its broad and vague powers to rewrite every consumer protection rule and write new rules, together with the chilling impact on any type of non-standard financing, would be very likely to cause lenders to be more conservative and, in some cases, unable to offer flexible types of loans that consumer want and that businesses need to grow and create new jobs.

The state law provisions of the bill would act as a federal floor inviting states to adopt stricter standards for anything that can be labeled “consumer protection.” This will eliminate national markets for consumer financial products and services because financial institutions will have to offer different products, services, and disclosures in all states with different laws.

Overall, H.R. 3126 creates a new consumer protection Agency and makes massive changes in our regulatory structure that go well beyond what is needed to address abuses and any needed reforms to address the financial crisis, and it should be strongly opposed.