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The Consumer Financial Protection Bureau: Title X of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010

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Transcript from Speech Given at Dodd-Frank Symposium, March 11, 2011

I'm going to take us back to the beginning of the day and the meltdown. When we had the meltdown, Consumers Union and many other consumer advocates said: "It's time for a fundamental change." We looked at the fact that everybody was talking about systemic risk, we said OK, that's good, we need to deal with that, we're all taxpayers, but let's also talk about risks to households. We asked for a change in the federal regulatory culture in the banking regulators. We wanted a federal agency, bureau, whatever you'd like to call it, independent of the banking industry, focused on the safety of consumer financial products and an active role for state consumer protection. It's a long bill but Title Ten is not that long; you can read it in one day. I recommend you do so, because you will see that, in fact, it creates a structure to achieve a market with safe consumer financial products and an active role for state consumer protection.

Everybody said that the meltdown took us all by surprise, and to a great degree that was true, but predatory practices in sub-prime lending were not new. Legal services advocates in Philadelphia, in Atlanta, and in New York had been talking about harmful lending practices that drained precious home equity from individuals and communities since the late 1990s. In the year 2000, led by the National Consumer Law Center; Consumers Union and other groups begged the Federal Reserve Board to amend the Homeowners Equity Protection Act (HOEPA) regulations to address some of these practices. Almost ten years later the Government Accountability Office (GAO) said there was a regulatory failure. I think what happened between the problems we saw in low-income neighborhoods and the meltdown is that securitization took these practices to scale. For the first time, it was actually possible to make a profit by making a bad loan. "Keep the fee and pass the risk," is what we called it when we spoke in Congress. The slicing and dicing spread and amplified that risk around the world.

The Dodd-Frank solution is the Consumer Financial Protection Bureau

[1] At the time the remarks were delivered, Ms. Hillebrand served as a Senior Attorney and the Financial Services Campaign Manager for Consumers Union of U.S., Inc.

(CFPB): one government agency that will be accountable to policy makers, to you and me, and to the good players in the industry, to make sure that there is the appropriate amount of policing of the marketplace for consumer financial services. The law provides for an independent director and a secure budget through the Federal Reserve System. There is a veto on regulations; it's narrowly tailored because the whole point was to break the regulatory gridlock where all the banks had to talk to each other forever before anything got done in response to emerging problems. In case you think we don't need another government agency, I have a slide here from the Consumer Federation of America that shows what we had before, with lines going in every direction: eight government agencies responsible for different pieces of law, none of them having a product-based focus, none of them having a charge to look at what is coming up in the market.

I'm going to give you some information about the CFPB that you may already know if you are reading every single news story about the CFPB and following all the speeches. The concept is simple: the CFPB is to protect both consumers and law-abiding competitors. Without the CFPB, a financial service provider who is doing sensible and responsible lending with real underwriting faces a disadvantage when its competitors are offering something different that looks cheaper, but really bears a lot of extra risk to the customer. The responsible provider is going to lose that customer. The CFPB is designed to change that result. Its regulations are going to protect not just the individual consumers, but competitors who want to compete fairly and openly and tell the truth about their products. There have also been many statements that this will be a data-driven agency, with a strong degree of transparency both for the public and for the industry. Finally, baked into the statute is the idea that the power of the states will be unleashed to help to watch and protect the market. I'm going to come back to that later and discuss the role of the states.

So, the basic concepts coming out of the statute: research, rule-writing, supervision, enforcement, fair lending and financial education are key functions. It is very important that, setting aside insurance and regulated investment products, by and large most types of consumer financial products, services, and providers will all be under the same rules, and these rules will apply both to banks and non-banks. Increasingly, these segments are competing with one another for the consumer's dollar, for the consumer's wallet. The idea is to stamp out the regulatory arbitrage. Let consumers make choices based on the merits of the products, and let providers all operate under the same rules, so you don't have a situation where a bank can't do something that another kind of lender is doing and pulling the customer away from that perhaps more responsible lender.

There are some nuances on supervision, but the concept I want to emphasize is the idea baked into the statute: one federal supervisor, many enforcers. There will be one supervisor at the federal level for consumer protection. For big banks it's going to be CFPB, smaller banks keep the supervisor that they have. There will be many enforcers. State Attorneys General will enforce some of these new rules. The CFPB will have enforcement power, the Federal Trade Commission (FTC) keeps some of its enforcement power over non-bank entities, there's also a process for the primary regulator on safety and soundness to engage in enforcement.

There are also some specific units described by the statute. It's been said this will be a data-driven agency, a research-driven agency. One thing I want to emphasize about the structure is that research, markets, and regulation are together, so the folks who write the rules will have the same boss as the folks who are doing the research. There are some specific groups designed and charged with studying and knowing what's going on in the market - not because every change should be regulated, but because you can't make smart decisions about what should be addressed and what should be left to develop unless you know what's going on in the market. There's a lot of thought that part of what happened in the meltdown is the regulators didn't know what was going on in those markets. The other thing I want to emphasize is that supervision and enforcement will be together. As you may know, bank supervision is the part that is usually performed quietly, on the inside. Enforcement is more public – so there is more than one tool in the toolbox to try to address problems.

There are some fundamental principles evident in the way that the CFPB is being designed. Some of these are baked into the statute and some of them are being developed in the implementation of market-based teams with a clear connection to the regulatory development and the evidence-based approach to government. You've heard Professor Warren and others talk about ending gotchas; the idea is that people should be able to make their own good choices, but not if there's hidden risk in the product which interferes with the ability of an individual to evaluate it. There is the statutory ban on unfair, evasive, and abusive practices, and it's been pointed out that the "unfair and deceptive" are existing rule-making powers that the Federal Reserve Board, the Office of Thrift Supervision (OTS) and the National Credit Union Administration (NCUA) had. Those are being added to the CFPB and abusive is a new federal standard. The concept here is to clean up the market—both for consumers and for law-abiding competitors—using supervision and enforcement, and clear rules when those are needed, and a big value on transparency and responsiveness to the public.

Now, I thought I might skip all of these slides about the text of the statute, but maybe I'll give you a brief run-through. If you are taking deposits, or providing some of those products that seem to substtiute for a bank account but may not fall under bank account regulation, you are going to be covered. If you are just a grocery store who sells a payment card but doesn't have anything to do with setting its terms and conditions, you are not covered. If you're just Safeway and you sell that payment card but you don't have to do anything with setting its terms and conditions, you're not covered. There are a lot of sensible ideas in the structure of the CFPB. For example, registered financial advisors are not covered, but people who are claiming to be an advisor while in fact selling a product like debt management or debt settlement will be covered. There is also a provision on a "purpose to evade" that allows the agency to pull things in if necessary.

You've heard about the auto dealer exemption and the retailer exemption, and my colleagues talked about the insurance and the investor exemptions. I'm not going to walk you through these very complicated exemptions but they come back to a very simple concept: motor vehicle dealers are exempt when it is about selling the car or leasing the car. If it's about the credit, they're not exempt. So, by and large, auto dealers are going to be exempt, unless they're making the loans directly and are keeping them on the books themselves - the so-called "buy here and pay here" which you sometimes see in low-income neighborhoods and used car lots. The third-party lender for whom the dealer arranges the loan is still covered; it's only the auto dealer that is exempt, not the lender, who might be using the dealer as a conduit to new clients. Also, Congress didn't say that auto dealers can do whatever they like, instead they chose to leave to the Federal Reserve Board the job of developing and keeping up to date regulations applicable to auto dealers under the statutes otherwise being transferred over to the CFPB. Congress also gave the FTC some streamlined rule-making authority to address auto dealer issues.

The retailer text is complex, but the concept again is quite simple. Retailers are not covered when they are selling or brokering non-financial goods and services. If the retailer is not charging interest it is not covered. If the retailer is not selling its portfolio of credit, it is not covered. If the retailer is particularly small and it is charging interest, it is still not covered. The basic idea here is: a retailer will be covered when the size of the credit outweighs the goods, so that it starts to look like it's a credit business and not just to facilitate the sale. Retailers and merchants also are covered with respect to regulations under those transferred and enumerated statutes. Those are the ones that are just moving over from the Federal Reserve Board. They were covered before, under the Federal Reserve Board's regulations, now they'll be covered, as those rules are administered by a different source.

You've heard about the unfair deceptive and abusive, I just want to highlight that this is a specific statutory prohibition and then there are sub-parts that describe what the Agency's power is with respect to promulgating rules. However, there is a stand-alone ban on abusive practices in Section 1031.

These things become illegal on July 21.

I'm not going to walk you through all of the definitions, you can read those, but there is a long-standing definition of unfair. There is no definition of deceptive but perhaps we will see some rules that will help to define that. In the area of "abusive" it's actually a two-part test. A prior speaker described the three provisions under that second part but there's also an "or" in there. You'll see at the end of the first part, this test: "materially interferes with the ability of the consumer to understand the term or condition, or takes unreasonable advantage of these specific conditions." The CFPB's organic rule-making authority—unfair deceptive and abusive rulemaking power—that's the substantial new rule-making power in Title 10. The rest of it is transferred, so all those statutes where the Federal Reserve Board wrote the rules and the different federal regulatory agencies enforced the rules, those are being moved over. Often one product will be subject to more than one of these rules, so putting them all in one place makes a lot of sense.

Turning to the structure for supervision for compliance with consumer laws, essentially, big banks are with the CFPB, smaller banks stay where they are, and there are some obligations to cooperate in the statute. On the non-bank side, there are certain things that go to the CFPB by category of provider; others where there will have to be a rule to define who is a larger participant in a market for a financial product or service, plus an area where a determination that there is a special risk sparks supervisory jurisdiction. The statute says that the CFPB's non-bank supervision will be risk-based, so there's still going to be a very important role for the states that oversee many of the non-bank entities. In the area of enforcement, there should be many enforcers. State Attorneys General will be able to enforce both state and federal law with respect to national banks. There's an odd wrinkle here: state Attorneys General cannot enforce those statutory provisions on unfair, deceptive and abusive practices but they will be able to enforce the rules under those provisions. This means that there may be a bit of a delay before we see state Attorneys General being active in the unfair deceptive and abusive practices because the rules have to come out first.

I want to turn now to the kinds of information about the market that will be developed and become available to the industry and the public as a result of the CFPB. The statutory functions of CFPB include collecting, investigating, and responding to consumer complaints. It has to have a unit with a toll-free number, a website, and a database. The Privacy Act notice on this has already come out. It describes one of the purposes of this future database as providing information for the regulators and for the public.

Finally, there's a very significant reduction in the federal preemption of state laws in the Dodd-Frank Act as part of Title 10. There's a complete end to the special charter-based preemption for affiliates and subsidiaries of national banks and the federally chartered thrifts. The Homeowners' Loan Act field preemption has been eliminated. Instead, the rule will be the same for national banks and for federally chartered thrifts. There is then a special rule in Dodd-Frank for state consumer financial protection laws. A state law will still be preempted if it discriminates against a national bank. That comes out of the 1860s and the things that were happening in the U.S. at that time. State consumer financial protection laws also will be preempted if they significantly interfere with the exercise by a national bank or thrift with its powers. "Prevent or significantly interfere"—I'm sure we'll have litigation on that for a long time. State laws can also be preempted if they are expressly preempted by another federal law.

Note that the elimination of federal thrift field preemption applies to all state laws, not just to state consumer financial protection laws. Similarly, the elimination of charter-based preemption for subsidiaries and affiliates also applies to all state laws, not just to consumer financial protection laws. Turning to the question about rules the CFPB puts out: will those preempt state law? The answer is "no." Dodd-Frank uses the standard preemption formula that is found in the Electronic Fund Transfer Act (EFTA), the Truth in Lending Act (TILA), and in other older federal consumer laws that are working quite well. It says that state laws are preempted if they're inconsistent with federal law and they are not inconsistent if the state law is stronger, as long as you can comply with both.

All of this is going to start July 21. The statute does allow an extra ninety days to move employees from other agencies—although federal banking regulators also have to put the Office of the Comptroller of the Currency (OCC) and the OTS together as a side effect form Dodd-Frank. There is going to be a lot of hard work done in Washington to make all these things happen. The cut back in preemption starts on the same day, as well as that statutory ban on unfair deceptive and abusive practices, and the consumer community is hopeful that new information about what's going on in the marketplace reflected in consumer complaints and inquiries will become available very soon after July 21.

I can't close without telling you that consumer groups are also are very pleased to see many of the other improvements in the Dodd-Frank Act outside of Title 10: the additional oversight for systemically important firms; shining some light into the shadow banking system; and the skin-in-the-game mortgages issue. If you take a look at Title 14, you'll see it's very different from Title 10. It has a series of very specific rules and obligations that are going to make a difference in the long run.