Testimony of

Edward L. Yingling

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Committee on Banking, Housing and Urban Affairs

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Chairman Dodd, Ranking Member Shelby, and members of the committee, my name is Edward L. Yingling. I am President and CEO of the American Bankers Association (ABA). The ABA brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $13.5 trillion in assets and employ over 2 million men and women.

ABA appreciates how this committee has responded to the financial crisis in a thoughtful, deliberative, and thorough manner. Changes are certainly needed, but the pros and cons and unintended consequences must be carefully evaluated before dramatic changes – affecting the entire structure of financial regulation – are enacted. That is why hearings like this one today are so important.

I am pleased to present the ABA's views today on the proposal to create a new consumer regulatory body for financial services that would operate separate and apart from any future prudential regulatory structure. We believe that a separate consumer regulator should not be enacted, and, in fact, is in direct contradiction with an integrated, comprehensive approach that recognizes the reality that consumer protection and safety and soundness are inextricably bound. Consumer protection is not just about the financial product, it is also about the financial integrity of the company offering the product. Simply put, it is a mistake to separate the regulation of the banking ***business*** from the regulation of banking ***products***.

Financial integrity is at the core of good customer service. Banks can only operate safely and soundly if they are treating customers well. Banks are in the relationship business, and have an expectation to serve the same customers for years to come. *In fact, 73 percent of banks (6,013) have been in existence for more than a quarter-century, 62 percent (5,090) more than half-century, and 31 percent (2,557) for more than a century.* These banks could not have been successful for so many years if they did not pay close attention to how they serve customers. Satisfied customers are the cornerstone of the successful bank franchise. The proposal for a new consumer regulator, rather than rewarding the good banks that had nothing to do with the current problems, will add an extensive layer of new regulation that will take resources that could be devoted to serving consumers and make it more difficult for small community banks to compete.

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. ***Traditional*** FDIC-insured banks – more than any other financial institution class – are dedicated to delivering consumer financial services right the first time and have the compliance programs and top-down culture to prove it. Certainly, there were deficiencies under the existing regulatory structure. Creating a new consumer regulatory agency, however, is not the solution to these problems. It would simply complicate our existing financial regulatory structure by ***adding another extensive layer of regulation***. There is no shortage of laws designed to protect consumers. Making improvements to enhance consumer protection under the existing legal and regulatory structures – particularly aimed at filling the gaps of regulation and supervision of nonbank financial providers – is likely to be more successful, more quickly, than a separate consumer regulator.

Certainly the members of this committee should look at this consumer agency proposal from the point of view of consumers, who are paramount. Later in this testimony, we will discuss how the proposal in our opinion is not the best approach for consumers and will actually undermine consumer choice, competition, and the availability of credit. However, we would also ask you to look at this issue from another point of view. While all banks would be negatively impacted, think of your local community banks, and credit unions also for that matter. These banks never made one subprime loan, and they have the trust and support of their local consumers. As members of this committee have previously noted, these community bankers are already overwhelmed with regulatory costs that are slowly but surely strangling them.

Yet a few weeks ago, these community banks found the Administration proposing a potentially massive new regulatory burden that will fall disproportionately on them. The largest banks, which will certainly bear a significant burden as well, do have economies of scale. Non-banks, the state regulated or unregulated financial entities that include those who are most responsible for the crisis, are covered, at least in part, by the new agency – and that is positive. However, based on history, their regulatory and enforcement burden is likely to be much less. In fact, according to the Administration proposal, the new agency will rely first on state regulation and enforcement for these entities, and yet we all know that the budgets for such state regulation and enforcement are completely inadequate to do the job. Community banks, on the other hand, are likely to have greatly increased fees to fund a system that falls disproportionately and unfairly on them.

In both the Administration's white paper and the legislative language submitted by Treasury, it is now clear that the new agency would have vast and unprecedented authority to regulate in detail all bank consumer products and services. The agency is even empowered, in fact encouraged, to create its own standardized products and services – whatever it decides is "plain vanilla" – and may ***compel*** banks to offer them. Even further, the agency is given the power, and basically urged, to give the products and services it designs regulatory preference over the bank's own products and services. The agency is even encouraged to require a statement by the consumer acknowledging that the consumer affirmatively was offered and turned down the government's product first.

The proposal goes beyond simplifying disclosures – which is needed – to require that all bank communication with consumers be "reasonable." This is a term so vague that no banker would know what to do with it. But not to worry – the proposal offers to allow thousands of banks, and thousands of non-banks, to pre-clear all communications with the agency.

All existing consumer laws, carefully crafted over the years by Congress, are transferred to the new agency, but they are rendered nothing more than floors. The new agency can do almost anything else it wants. CRA enforcement is apparently to be increased on these community banks, although they already strongly serve their communities. And that is not to mention the inherent conflicts, discussed below, that will occur between the prudential regulator and the consumer regulator, with the bank caught in the middle. All this cost, regulation, conflicting requirements and uncertainty would be placed on community banks that in no way contributed to the financial crisis.

We share the vision that greater transparency, simplicity, accountability, fairness and access can be achieved by establishing common standards ***uniformly applied*** that reflect how consumers make their choices among innovative products and services. But this vision cannot be achieved by ignoring the experience of our recent financial crisis and failing to ***directly*** address those deficiencies that led to it. It is now widely understood that the current economic situation originated primarily in the ***unregulated or less regulated non-bank sector***. For example, the Treasury's plan noted that 94 percent of high cost mortgages were made outside the traditional banking system. Many of these non-bank providers had no interest in building a long-term relationship with customers but, rather, were only interested in profiting from a quick transaction without regard to whether the mortgage loan or other financial product ultimately performed as promised. Thus, an important lesson learned is that certain unsupervised non-bank financial service providers and their less regulated financiers – the so-called shadow banking system – undermined the entire system by abusing consumer and investor trust.

A second lesson learned is that consumer protection and financial system safety and soundness are two sides of the same coin. Poor underwriting, and in some cases fraudulent underwriting, by mortgage brokers, which failed to consider the individual's ability to repay, set in motion an avalanche of loans that were destined to default. Good underwriting is the essence of both good consumer protection and good safety and soundness regulation. Loans that are based on the ability to repay protect the institution from losses on the loans and protect consumers from taking on more than they can handle. Thus, what is likely to protect both the lender and the customer cannot be, nor should be, separated.

These lessons lead to two fundamental building blocks of any reform of consumer protection oversight.

1. ***Uniform regulation and uniform supervision of consumer protection performance should be applied to non-banks as rigorously as it has been applied to the banking industry.***
2. ***Regulatory policymakers for consumer protection should not be divorced from responsibility for financial institution safety and soundness.***

Separating the safety of the institution from the safety of its products means each agency has only half the story. Without building upon these keystones, the hope for better transparency, simplicity, accountability, fairness and access will not be realized, and we will have missed the opportunity to build a strong consumer protection infrastructure across the financial services industry.

Unfortunately, the Consumer Financial Products Agency (CFPA) proposal, in our opinion, contains a number of very serious flaws. The proposal:

- Severs the connection between consumer protection and safety and soundness – forcing each side to attempt to work independently and freeing each to contradict the valid goals of the other – to the detriment of consumer choice and safety and soundness.
- Subjects banks to added enforcement, but leaves the "first line of defense" for the supervision and examination of non-banks to the states, which suffer from a lack of resources for meaningful enforcement. ***This is where the failure of non-bank regulation was most severe under the current system***. Once again there would be perverse incentives for financial products to flow out of the closely examined banking sector to those who will skirt the meaning, and even the language, of regulations.
- Excludes competitor financial products from its reach – including securities, money market funds, and insurance – thus further belying the promise of uniform or systemic oversight and creating incentives for development of products outside the scope of the CFPA that may be risky for consumers.
- Renders all the consumer laws created by Congress largely moot, as the very broad power of the CFPA would authorize the agency to go well beyond such laws in every instance.
- Imposes government designed one-size-fits-all products – so-called plain vanilla products – and places them in a preferred position over products that are designed by the private sector for an increasingly diverse customer base. These government products would be given regulatory preference over the products designed by the individual banks, and consumers could even be required to sign a notice that they have first turned down the government's product.
- Requires communications with consumers to be "reasonable", an incredibly vague and unworkable standard that will cause tremendous uncertainty for years to come.

- Basically ends uniform national standards, quickly creating a patchwork of expensive and contradictory rules that will create uncertainty, increase consumer costs, and lead to constant litigation.
- Saddles providers, and, indirectly, consumers with a new regime of fees to fund yet another agency.
- Will inhibit innovation and competition, limit consumer choices, and lessen the availability of credit.

To be successful in the regulation, examination, and enforcement of non-banks, the agency will have to be very large and have a significant budget. We believe a better course exists. ABA offers to work with the Administration and the Congress to achieve meaningful regulatory reform to improve consumer protection and preserve financial system integrity. As the crisis has proven, a strong banking industry is indispensible to a strong economy; and a sound banking system is the greatest single protection of consumer access to financial services fairly delivered. Traditional banking is back in style, but that does not mean improvements cannot be made. We pledge to work with this committee to find the best solutions to assure that consumers have the protection they deserve for any financial product.

I would like to further discuss several points today:

- Consumer regulation ***should not be separated*** from safety and soundness regulation.
- The key focus of change should be on ***closing existing gaps in supervisory oversight*** across the financial institution marketplace, not on adding yet another vast layer.
- The proposal would give the agency unprecedented authority to control the products and services offered by banks and make all current consumer laws mere floors.
- The undermining of uniform national standards will increase costs and cause litigation and tremendous uncertainty.
- The question of how to pay for this new agency was left very vague and raises significant issues.
- The proposal will inhibit innovation and competition, limit consumer choices, and dramatically lessen the availability of credit.
- The regulatory authority to address consumer concerns is already there for highly regulated banks, particularly with the new focus on unfair and deceptive practices. However, improvements can be made, and ABA will work with the committee to make such improvements.

I will address each of these points in turn.

I. Consumer regulation should not be separated from safety and soundness regulation.

Consumer regulation and safety and soundness regulation are two sides of the same coin. Neither one can be separated from the other without negative consequences; nor should they be separated. An integrated and comprehensive regulatory approach is the best method to protect consumers and protect the safety and soundness of the financial institution. While certainly improvements can be made, the current regulatory structure applied to banks provides an appropriate framework for effective regulation for both consumer protection and bank safety and soundness. As I note throughout this testimony, that same framework was virtually non-existent for non-bank providers of financial products.

FDIC Chairman Sheila Bair, testifying recently before Congress, summarized the synergies between both these elements: "The current bank regulation and supervision structure allows the banking agencies to take a comprehensive view of financial institutions from both a consumer protection and safety and soundness perspective. Banking agencies' assessments of risks to consumers are closely linked with and informed by a broader understanding of other risks in financial institutions. Conversely, assessments of other risks, including safety and soundness, benefit from knowledge of basic principles, trends, and emerging issues related to consumer protection. Separating consumer protection regulation and supervision into different organizations would reduce information that is necessary for both entities to effectively perform their functions. Separating consumer protection from safety and soundness would result in similar problems."[1]

Attempts to separate out consumer protection from safety and soundness will lead to conflicts, duplication and inconsistent rules, which will likely result in finger pointing as inevitable problems arise. What are banks to do ***when the consumer and safety and soundness regulators disagree, as they inevitably will?***

Almost every consumer bank product or service has both consumer issues and safety and soundness issues that need to be balanced and resolved. It is important to remember that one person's deposit funds another person's loan. It makes little sense to regulate the terms, conditions and prices of deposit products or loan products separately from the business aspects of a bank's fundamental process – turning deposits into loans.

As I mentioned at the outset, the very nature and application of good underwriting standards is by definition both a consumer protection and a safety and soundness issue. A second simple example is check hold periods. Customers would like the shortest possible holds, but this desire needs to be balanced with complex

[1] Bair, Sheila, C. *Modernizing Bank Supervision and Regulation,* testimony before the Committee on Banking, Housing and Urban Affairs, U.S. Senate, March 19, 2009.

operational issues in check clearing, and with the threat of fraud, which costs banks – and ultimately consumers in the form of increased costs that are passed on – billions of dollars.

Similarly, the Electronic Funds Transfer Act contains numerous important consumer protections, developed and modified over the years based on experience, new technologies, and new types of fraud. Separating the consumer consideration from the safety and soundness, anti-fraud, and systems considerations would certainly seem unworkable.

Banks also have extensive duties under "know your customer" regulations designed to fight money laundering and terrorism. These critical regulations must be coordinated with consumer and safety and soundness regualtion. A simple example is in the account opening process, which is subject to extensive consumer and "know your customer" regulations. It would be unworkable to separate these as well.

And what about employee training? Banks spend billions of dollars training employees to comply with the heavy regulations to which banks are subjected. Examiners examine banks for their training programs. Front-line employees must have training in numerous consumer, safety and soundness, and anti-money laundering regulations. ABA offers dozens of courses in compliance for front-line employees. How would such training be effectively coordinated between agencies with differing views and objectives? Is the new agency going to examine banks and non-banks equally for compliance training? It cannot be left to the states, where there is little precedent for extensive examining for compliance training outside banking.

Rather than take to heart the lesson of the inseparability of safety and soundness and consumer protection, the Administration's proposal creates a different form of regulatory fragmentaion along the fault lines of the jurisdiction of a new bureacracy. A look at the proposal's enumeration of existing rule-making authorities to be transferred – mostly from the Federal Reserve Board – to the CFPA reveals an assortment of likely interagency conflicts that will generate future regulatory gaps rather than bridge the current ones.

For instance, consumer privacy is placed in the CFPA, but identity theft protection is left out. The Electronic Funds Trasfer Act is assigned to CFPA, but the rules for clearing electronic check images that make funds available for customers to access with their debit cards remains with the Federal Reserve. Truth in Lending Act rule-making over mortgages is assigned to the CFPA, but flood insurance coverage (FDPA) and private mortgage insurance (HOPA) laws protecting consumers who obtain mortgages remain with the banking agencies. These and other anomalies in the Administration proposal will set true consumer protection reform on the back-burner as countless hours and dollars are wasted grappling with the regulatory morass that will result from this ill-advised structural reform. The thirty-year investment in coordinated supervision (FFIEC) will be washed away and replaced by interagency conflicts that are hard-wired in the new bureacracy without a means to resolve them.

Finally, we are very concerned about conflicts over CRA. The banking industry has worked hard in serving its communities and in complying with CRA. We agree that CRA has not led to material safety and soundness concerns, and that bank CRA lending was prudent and safe for consumers. That is not to say that there is no debate about the correct balance between outreach and sound lending. However, that debate – that tension – is resolved now in a straightforward manner because the same agency is in charge of CRA and safety and soundness. To separate the two is a receipe for conflicting regulatory demands, with the bank caught in the middle.

In the above examples and in many other areas, two different regulators – one focused on consumers and another focused on safety and soundness – will almost certainly come up with two different and conflicting rules and answers that, when added together, only create new costs, overlap and duplication, as well as an untenable situation for the financial institution.

II. The key focus of change should be on closing existing gaps in regulation, not on adding yet another bureaucratic layer.

The biggest failures of the current regulatory system, including consumer protection failures, have not been in the regulated banking system, but in the unregulated or weakly regulated sectors.[2] As Members of Congress from both parties have noted, to the extent that the system did work, it is because of prudential regulation and oversight of ***banking*** firms. While improvements within the banking regulatory process can certainly be made, the most pressing need is to close the regulatory gaps ***outside*** the banking industry through better supervision and regulation – both on the consumer protection and safety and soundness sides of the coin.

Take the case of independent mortgage brokers and other non-bank originators. Again, as the Administration's own proposal states, 94 percent of the high cost mortgages occurred outside the regulated banking sector. And it is likely that an even higher percent of the most abusive loans were made outside our sector. In contrast to banks, these non-bank firms operate in a much less regulated environment, generally without regulatory examination of their conduct, without strong capital provisions, and with different reputational concerns. They have not been subjected to the breadth of consumer protection laws and regulations with which banks must comply. Equally important, a supervisory system does not exist to examine them for compliance even with the comparatively few laws that do apply to them. In addition, independent brokers typically do not have long-term business relationships with their customers. Instead, they originate a loan, sell the loan to a third party, and collect a fee. This results in a very different set of incentives and can and does

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[2] Before the recent crisis, a coalition of 46 state Attorneys General recognized that based on consumer complaints received, as well as investigations and enforcement actions undertaken by them, predatory lending abuses were largely confined to the subprime mortgage lending market and to non-depository institutions. Almost all of the leading subprime lenders were mortgage companies and finance companies, not banks or direct bank subsidiaries. We stress the past tense, because their lack of financial robustness assured that they would not be around to answer for their consumer protection misdeeds.

work at cross-purposes with safe and sound lending practices. Proposals are also being offered with respect to credit derivatives, hedge funds, and others, and the ABA supports closing these regulatory gaps.

In stark contrast to the weakness of oversight or examination of consumer compliance issues for most other financial service providers, bank regulators have an extraordinarily broad array of tools at their disposal to assure both consumer protection and safety and soundness. Banks are regularly examined for compliance with consumer regulations, and regulators devote significant resources to supervision and training in consumer compliance issues.[3] These enforcement and supervisory options are coordinated through the Federal Financial Institutions Examination Council (FFIEC)[4], which sets standards for ***both*** consumer and safety and soundness examination.[5] The need is for the same bank-like structure, supervision and examination to be applied to non-bank financial service providers.

There obviously have been consumer concerns with respect to banks – we certainly know of this committee's concerns with credit card practices – but if the great majority of abuses occurred outside the banking industry (with toxic subprime mortgages, for example), why would Congress create a new regulatory agency that will end up focusing its resources predominately on banks and not non-banks? We see that the intention is to have regulations that cover most providers. However, regulation without enforcement can be worse than no regulation in that it gives rogue institutions a veneer of legitimacy. All evidence tells us that the states will not have the resources to enforce all these regulations. We have, frankly, little confidence that the CFPA will apply equal examination and enforcement on non-bank lenders and others, or that it will have the resources to do so. This concern is exacerbated by the incredibly vague funding provisions in the legislative

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3 Bank regulators are just as concerned about consumer protection as are law enforcement authorities, but the bank regulators are better able to achieve their objectives through an enormous array of enforcement and supervisory options that allow them to meet their broader mandate for law enforcement as well as financial stability. These range from the behind-the-scenes citation in an exam report as a matter requiring attention to the public actions of issuing a cease-and-desist or civil money penalty order or even closing a bank and imposing lifetime bans from participating in banking activities. Bank examiners can direct a bank to stop taking an action or to take some different action. These tools are most appropriately and effectively exercised by one regulator that is focused on achieving the balance described above.

4 The FFIEC, represented by the Federal Reserve, OCC, FDIC, OTS and NCUA, is charged with prescribing "uniform principles and standards for the federal examination of financial institutions" designed to "promote consistency in such examination and to insure progressive and vigilant supervision."

5 In addition, the FFIEC agencies have set forth common standards for determining a bank's rating for consumer compliance performance. This rating stands as an identifiable grade, separate and apart from the CAMEL rating, so that boards of directors and regulators can hold management directly accountable for the quality of their institution's consumer compliance management programs and performance. Moreover, the FFIEC's agency members have endorsed top-down consumer compliance programs expected of banks that contain system controls, monitoring of performance, self-evaluation, accountability to senior management and the board, self-correcting processes, and staff training.

The breadth of this supervisory authority is extensive. Consumer compliance management plays a role in every operational aspect where a bank comes into contact with customers – from the marketing of products, through account opening and credit administration, to handling personal information and monitoring for financial crime. Further, banks hold their employees accountable for meeting their obligations. Every bank invests heavily in consumer compliance with dedicated compliance professionals who take great pride and apply tremendous effort to assure that consumers are being treated fairly.

language. How big is this agency to be? If it is not large, it cannot conceivably enforce its regulations on the thousands of institutions it is supposed to regulate. If it is big, how is it to be paid for?

III. The proposal gives the CFPA unprecedented authority to control the products and services offered by banks.

As stated earlier, the proposal calls for an unprecedented delegation of legislative authority to the agency to control the way consumer products and services are designed, developed, marketed, delivered, and priced by banks and other financial service providers. In fact, the agency is encouraged to design products and services, mandate that banks offer them, regulate the products not designed by the agency more heavily than the government product, and require consumers to sign a document that they do not want the government-designed product. The agency can even heavily regulate compensation systems under very open-ended authority. All communications to consumers about products and services would have to be "reasonable," a vague and unworkable standard if there ever was one. This would appear to give the agency an incredible amount of control over banks' and others' products without any real legislated standards. Simply put, this would appear to be the most powerful agency ever created in that it has almost unlimited power to regulate and even mandate the products offered by the regulated.

It also would very much undermine incentives for innovation and better customer choice. Certainly banks and non-banks would be less likely to create new products or consumer enhancements. Any deviations from the government-designed product would be subject to additional regulation and clearances. Coupled with the prohibition that it is unlawful "to advertise, market, offer, [or] sell … a financial product or service that is not in conformity with the [Act]," the Administration's proposed new structure places banks and non-banks alike at extreme risk when innovating and will chill efforts to respond to consumer demand for beneficial products and services.

Proponents of the agency have regularly used the catch-phrase that we regulate toasters to keep them from blowing up (through the Consumer Product Safety Commission), but we don't regulate mortgages that can blow up consumers' finances. There are a number of problems with this analogy, including that mortgages are regulated and that, unlike a toaster with electrical problems, a financial product may often be a problem or not depending on to whom and how it is offered. More fundamentally, unlike the proposed CFPA, the Consumer Product Safety Commission is not set up to design a toaster; mandate that anyone selling toasters offer the government toaster; and furthermore, to adjust regulation, disclosures, and liability to put the government toaster in a preferred position. Of course such a government toaster could not meet the multitude of preferences of single people on the run, small families, large families, those with small kitchens, those with large kitchens, those that just want toast, those that just want toast and English muffins, and those that want a multi-functional toaster oven, etc. And, of course, such a government plain-vanilla toaster with such built in advantages would discourage innovation in the creation of new options for consumers and competition in the offering of alternatives.

In many cases, the government financial product might not fit with the institution's business plan. Niche banks, which serve important constituencies, such as small business owners or low income communities, would be required to offer products that simply do not fit. There will even be safety and soundness issues. For example, some banks that maintain all their loans in portfolios do not, and should not, hold 30-year fixed "plain vanilla" mortgages.

Furthermore, the incredible authority given to the proposed agency means that all the consumer laws enacted and modified by Congress over the years, which have resulted in hundreds and hundreds of pages of regulations, are to a large degree moot. They are mere floors; and, in fact, floors with holes in them. This new agency can do pretty much anything it wants in any of the areas specifically covered by the laws, and any other area relating to consumer financial products for that matter. In the final analysis, the basic premise of the Administration's proposal is to invite Congress to abdicate its legislative responsibilities to address the ever-evolving financial marketplace and delegate plenary discretion to a seemingly all-knowing and all-powerful agency.

For example, this Congress just passed an extensive, tough new law on credit cards. Combined with the previous law, this creates a comprehensive congressionally crafted set of rules governing cards. Yet the proposed CFPA legislation would grant the agency authority to do practically anything it wants in the credit card area with respect to terms, delivery, disclosures, compensation and even mandated products, as long as it does not do less than the new card law. One wonders why Congress undertook such extensive reform of the credit card law if it was going to give almost open-ended authority to the CFPA shortly thereafter.

IV. The undermining of national standards will increase costs and cause tremendous litigation and uncertainty.

The Commerce Clause of the Constitution was designed to allow products and services to flow freely across state lines. It is hard to think of an area of our economy where this should be encouraged more than in financial services, where the market for products from loans to deposits is national in scope. With changes in technology – such as the Internet – and the incredible mobility of our society, the free flow of financial services is even more pronounced. Furthermore, the National Bank Act, enacted during the Civil War, was created to provide for a national bank system that would not be subject, in its basic bank functions, to state laws. This national banking system, as part of the dual banking system, has served us well. However, a national system cannot function effectively if all national bank consumer products are subject to fifty different state laws. As we have noted, the safety and soundness regulator will not be able to do its job if it has no authority over consumer laws, much less if that authority is held by not only the federal consumer regulator, but every state regulator, legislature, and attorney general as well.

The multitude of rules – and do not underestimate how incredibly complex they would be – would subject banks to tremendous legal costs in order to comply, and also to deal with constant litigation. Every product, form, and customer communication would have to be checked and rechecked regularly for compliance with changing laws in all fifty states. Customers will move to other states regularly, and the bank would have to assume its customers could be in any state.

There are many areas where problems will arise. ATM cards could be subject to different rules by state, resulting in their not being useable in every state at great inconvenience to travelers, who could be left stranded without funds. On-line banking could be affected as differing rules would apply, depending on where the customer is located.

Costs to consumers would increase as banks try to address all the different rules. Innovation would be discouraged as any changes would have to be tested against all the different state rules. The European Union is working to develop common rules in order to have greater efficiencies and innovation, and yet the Administration's proposal would go in exactly the opposite direction – toward balkanization. From a consumer's standpoint, such regulatory complexity will be translated to account or loan agreement legalese to rightfully protect the bank from elaborate and conflicting requirements – all to the detriment of simplifying consumer products and making transactions more transparent. Proponents of the proposal talk about providing one page of simple disclosures – a goal much to be sought; but how can such a goal be achieved if there would have to be page after page of disclosures to cover all the state law differences?

V. The question of how to pay for this new agency was left very vague and raises significant issues.

To discharge its powers consistently over both banks and non-banks, this new agency will have to be extraordinarily large. It will need to regulate, and in many cases examine, not just banks and credit unions, but finance companies, pay-day lenders, mortgage brokers, mortgage bankers, appraisers, title insurers and many others – apparently even pawn shops.

However, under the proposal, no one has any idea how large this agency is to be. If it is small, its focus will inevitably be on the already regulated banks, even though, as already noted, 94 percent of the high cost mortgages came from outside banks. That would be incredibly unfair and counterproductive. To do its job as advertised by proponents, this agency would need to ensure that the thousands of non-banks under its jurisdiction are reporting, examined, and subject to enforcement in the same way banks will be. While the states are supposed to be a front line of defense, it is not credible to argue that states will have the budgets to implement such reporting, examination, and enforcement even to a minimal degree. Therefore, the new agency will need to do it, or its whole rationale falls apart.

Where is this agency's budget to come from? Apparently, the budget is to be based on fees on financial service products. The Consumer Products Safety Commission, said to be the model for the CFPA, is not funded by toy or appliance manufacturers, but rather by an appropriation. However, if the CFPA is to accomplish its goals and to effectively regulate non-banks, it would need to be considerably bigger than the Consumer Products Safety Commission. Banks are already heavily burdened with funding their regulators, directly and indirectly (e.g., deposit insurance premiums fund the FDIC's regulatory costs). These costs cannot simply be split apart to pay for the banks' part of the consumer regulator, as the tremendous efficiencies that result from combining safety and soundness and consumer regulation will be lost.

How is the agency to collect fees from non-bank providers? On what basis? How is it going to know about new entrants, unless they are required to register with the agency? As new types of providers spring up, how are they to be incorporated? There will, in fact, have to be a large bureaucracy just to collect the fees. Of course, these new costs, basic economics tells us, will ultimately be passed on to the users of the products, and so consumers will end up paying for this large new agency.

Obviously, these are very difficult questions that were not addressed in the Administration's proposal, but which should be answered before proceeding. Given the incredibly broad authority and ambitions of the proposal, it is impossible for Congress to judge what it will, in fact, do without knowing the size it is going to be.

VI. The proposal will inhibit innovation and competition, limit consumer choices, and dramatically lessen the availability of credit.

The proposal will, first, create tremendous uncertainty in the financial community about what the rules will soon be. The entire body of rules that has governed the development, design, sales, marketing, and disclosure of all financial products would be subject to change, and be expected to 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. Now there would be no certainty. This lack of certainty will cause firms to pull back from developing new products and new delivery systems. And it will chill lending, as firms will not know what the rules may be when they try to collect the loan a few years out.

This problem should not be underestimated. Why design a new product if you do not know what regulatory rules will be applied to it? Why stretch to make a loan to a deserving consumer when it may be determined after the fact that your stretch terms and disclosures were unreasonable and the contract is therefore unenforceable. Everyone will be on hold, to some degree, waiting for the development, which will take years of regulatory action and judicial interpretation, of an entirely new roadmap.

What makes this situation particularly difficult is that the proposed legislation, and the narrative provided with it, contains vague terminology that has little or no legal history. What on earth does "reasonable" mean for disclosures and communications? The legal concept of "unfair and deceptive", developed over many years, is also changed. It will take years for these new legal concepts to be defined fully by the courts. In the meantime, lenders will have no idea what their potential legal rights and liabilities will be.

Second, you have the huge cost for legal and other work for redoing the basis on which products are offered today. The current design of many products and disclosures is thrown into question by the concepts of this proposal. This is a cost that, again, will ultimately be borne in large part by consumers.

For example, credit card companies are in the process of spending hundreds of millions of dollars to change their systems, their disclosures, their risk models, and basic parts of the product to meet the new regulations and law. If this proposal is enacted, given the testimony of Treasury, it seems quite likely that additional significant changes will be made in regulations. How is the financial industry to plan for such uncertainty?

Third, the regime surrounding government designed products will undermine innovation and the availability of credit. As noted previously, the government designed products, given regulatory advantages, will undermine the incentive to develop new products. If an institution develops an idea that could enhance the basic product for all consumers or a subset of consumers, adding it will cause the product to no longer be "government approved" and will subject it to discriminatory regulation and legal uncertainty. Why bother? Ideas that could give consumers benefits or lower costs will never see the light of day.

The impact on lending will be profound. First, loan adjustments, which are made constantly in today's world, to fit a borrower's needs or allow the loan to be made simply will not happen. Those most hurt will be lower income consumers. Furthermore, the very large uncertainty and potential legal liabilities will cause less credit to be available, at the very time when credit is already scarce. Out government is in danger of designing policies that are absolutely contradictory – encouraging more credit to be available, while at the same time, through the President's proposal, designing a legal morass that will have a dramatic effect in lowering the availability of credit.

VII. Improvements can be made.

ABA agrees that improvements can and should be made to protect consumers. The great majority of the problems occur ***outside*** the highly regulated traditional banks, but there are legitimate issues relating to banks as well. The ABA is committed to working with Congress to address these concerns and implement improvements. In that regard, let me outline some concepts that should be considered.

- ***Enhance capabilities to apply unfair and deceptive practices:*** As you know, the Federal Reserve Board and the OTS have long had a very powerful tool called unfair and deceptive practices or UDAP. This had not been used as a broad regulatory tool for banks prior to the extensive credit card rule. However, use of this authority would address many of the issues raised. The UDAP authority is already in place. The ABA supports legislation the House passed last year to extend this authority in a coordinated fashion to the OCC and FDIC. The FTC has this authority for non-banks, but there have been severe constraints in using it. Congress should work to give the FTC the capability and funding to apply it to non-banks much more aggressively.

- ***Improve disclosure, using consumer testing:*** Disclosures can and should be improved, although it will not be easy. Current disclosures are by-and-large driven by lawyers and the need to cover the many legal complexities involved to protect against the real threat of litigation. Congress, the regulators, the industry, and consumer advocates need to overcome this bias. Progress has been made through the insights gained from consumer testing. Simple disclosures, perhaps in combination with larger, separate ones required for legal purposes, should be made in ways that most benefit consumers. Concepts gleaned from behavioral science relating to how consumers really react should be included in disclosure design.

- ***Enable basic products without stifling competition, innovation and consumer choice:*** In some cases financial products have become overly complex and difficult, if not impossible, for consumers to understand. This is not unusual in our economy as many product offerings – from consumer electronics, to telephone plans, to insurance – have become very complex. Often this complexity results from efforts to add options that consumers may want. Sometimes, as we all know, the complexity induces consumers to buy products or enhancements that are not right for them or for which they pay too much. However, as discussed previously, ABA believes the answer is not to have the government design products, mandate that they be offered, and give them an advantage over private sector products. Nevertheless, there is a need to have product options that are basic and easily compared, and to have, at the same time, a flexible, private-sector driven system that does not stifle competition and innovation. For example, the private sector, perhaps through the ABA as the industry's trade association, could consult with the regulators, Congress, and consumer advocates to develop basic product forms that could be easily compared.

- ***Develop centralized call centers for consumer complaints:*** It is difficult, perhaps impossible, for many consumers to understand whom they should call in the government to register concerns or complaints. ABA supports a centralized call center for consumers that could forward complaints to the right agency and serve as a coordinated information source.

- ***Require regular reports to Congress:*** The structure of consumer regulation ***within*** agencies can be reviewed and strengthened. Regular reports to Congress could be required.

- ***Empower the systemic risk oversight regulator to look specifically at consumer issues that pose systemic concerns:*** One clear lesson from the mortgage crisis is that consumer issues can raise systemic issues. If a systemic regulator had been in place, we would hope that it would have identified the rapid growth of subprime lending as a problem that had to be addressed well before it grew to such a hurricane force. The systemic regulator could be given the power to require regulatory agencies to address in a timely manner systemic consumer issues.

Conclusion

The ABA has very serious concerns about the proposed CFPA and the authorities it is to be given under the President's proposal. We believe it will result in a huge regulatory burden, particularly for community banks, while non-banks, which are primarily responsible for the crisis, will have ineffective enforcement.

Healthy, well-regulated banks have already been hurt deeply by unscrupulous players and regulatory failures. They watched mortgage brokers and others make loans to consumers that a good banker just would not make. They watched local economies suffer when the housing bubble burst. Now they face the prospect of another burdensome layer of regulation. It is simply unfair to inflict another burden on these banks that had nothing to do with the problems that were created. The separate consumer regulator will only add costs to these banks, particularly community banks, which already suffer under the enormous regulatory burden placed on them. As you contemplate major changes in regulation – and change is needed – I urge you to ask this simple question: how will this change impact those thousands of banks that did not create the problem and are making the loans needed to get our economy moving again? Another question that should be asked is: how will this proposal really assure strong enforcement and examination of the non-banks?

Furthermore, the proposal will dramatically undermine incentives to innovate and to offer new products from which consumers will benefit. Competition will be lessened, as the government designed products limits avenues for competition. Finally, the availability of credit will be reduced, particularly in the short run, because of great uncertainty about the new, evolving rules and the increased legal liability.

As outlined above, we believe that separating safety and soundness regulation from consumer regulation would be a mistake. Nevertheless, there are important improvements that can and should be made in the consumer arena, and we will work with members of this committee to make such improvement in this arena, as well as on the many other important issues in regulatory reform.