National
Urban League

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TESTIMONY OF

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NATIONAL URBAN LEAGUE POLICY INSTITUTE

Before the
HOUSE FINANCIAL SERVICES SUBCOMMITTEE
ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

Hearing on

"Improving Consumer Financial Literacy under the New Regulatory System"

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Chairman Gutierrez and Ranking Member Hensarling, I am Stephanie J. Jones, Executive Director of the National Urban League Policy Institute. I thank the subcommittee for the invitation to testify on the President's proposal for a new Consumer Financial Protection Agency (CFPA) and how financial literacy and education can be incorporated in this new financial regulatory framework. Our views and recommendations are based on decades of program delivery experience in urban communities across the country.

Through our frontline housing counseling services in Urban League affiliate programs throughout the country, the National Urban League received first-hand insight into the brewing mortgage housing crisis. Our findings led to National Urban League President Marc Morial's release of our "Homebuyer's Bill of Rights," on March 6, 2007 at the National Press Club's Media Luncheon. This was well before the issue started to trigger shockwaves in international credit markets and sending hedge fund analysts to the unemployment line. At that time, policy makers and government officials were reluctant to support greater regulation to give the market a chance to correct itself. Obviously, it never happened.

Consumer protection is a critical foundation for our financial system. It gives the public confidence that financial markets are fair and enables policy makers and regulators to maintain stability in regulation. Stable regulation, in turn, promotes growth, efficiency, and innovation over the long term. Therefore, the National Urban League supports legislative, regulatory, and administrative reforms to promote transparency, simplicity, fairness, accountability, and access in the market for consumer financial products and services. We are committed to working with Congress, industry associations, and consumer advocates to further the development of a fair and efficient regulatory system that provides sufficient consumer protection and serves the interests of historically disempowered constituencies who reside in underserved communities.

We recognize that the current regulatory structure at both the state and federal level is highly complex for the industry, regulators, consumers, and policymakers to navigate. As financial institutions and service providers increase in size, complexity, and operations, our regulatory system must reflect this evolution. The current economic stresses have also shown that our financial regulatory system must better address the interconnected risks of the capital markets and our banking system. To effectively protect consumers the regulatory system must prohibit unsustainable lending – disclosures and "financial literacy" are not enough.

The fundamental problem at the heart of today's crisis is that loan originators pushed borrowers into loan products that were inherently risky and unsustainable by design, and they did so notwithstanding the availability of the more suitable and affordable loans for which they qualified. Had borrowers been offered the more suitable loans for which many qualified, many more borrowers could have sustained homeownership.

The Federal Reserve has noted that, given the misaligned incentives of originators and the complexity of products and loan features, even with increased information or knowledge, borrowers could not have defended against poorly underwritten, risky products and deceptive practices. *The main problem with these loans was not the inadequacy of the disclosures or the financial literacy of the borrowers. Rather, the fundamental* problem was that – as the federal banking regulators belatedly recognized with respect to non-traditional loans in late 2006 and subprime lending in 2007 – lenders should not have made loans that they knew borrowers would be unable to sustain without refinancing. Therefore, to effectively protect consumers, the regulatory system must monitor and address market incentives that encourage loan originators to push risky or unsuitable loan products.

While the Administration proposes that the CFPA should have sole authority to promulgate and interpret regulations under existing consumer financial services and fair lending statutes, we believe there is a need for layers of protection against financial excess. Think about the financial system as a nuclear power plant, in which you need independent, redundant back-up systems – so if one "super-regulator" fails we don't incur another 20-40 percentage points in government debt through direct and indirect bailouts.

A consumer financial products protection agency should definitely be part of the package.

We strongly agree that the CFPA's jurisdiction should cover consumer financial services and products such as credit, savings and payment products and related services, as well as the institutions that issue, provide, or service these products and provide services to the entities that provide the financial products.

We are concerned that the plan makes no mention of those institutions at the very heart of the mortgage market meltdown – Fannie Mae and Freddie Mac. These two entities were the single largest source of liquidity for the subprime market during its height. In all likelihood, their ultimate cost to the taxpayer will exceed that of TARP, once TARP repayments have begun. Any reform plan that leaves out Fannie and Freddie does not merit being taken seriously.

It can also be argued that the plan also puts far too much faith in regulators to guide markets to where they should be. That is consistent neither with economics nor with recent history. A better plan – one that empowers consumers, rather than regulators – is needed.

Notwithstanding whether or not the CFPA is the most appropriate vehicle, the National Urban League is most interested in the inherent checks and balances to ensure that:

- Consumers have the information they need to make responsible financial decisions;
- Consumers are protected from abuse, unfairness, deception, or discrimination;
- Consumer financial services markets operate fairly and efficiently;
- Traditionally underserved consumers and communities have access to lending, investment and financial services; and
- National community based organizations that have demonstrated effectiveness in reaching under-served minority communities be included as full partners in any consumer protection effort.

The National Urban League Perspective on Financial Literacy

At this time, I would like to reiterate the key points that our National Urban League President, Marc Morial, made on our perspective and experience in the area of financial literacy in testimony before the House

Financial Services Committee on April 15, 2008. From the National Urban League's perspective, one fundamental problem with improving financial literacy is defining the term itself. A formal definition of personal *financial literacy* is the ability to read, analyze, manage, and communicate about the personal financial conditions that affect material well-being. The Urban League Movement employs a more expansive approach to this work which includes the ability to discern financial choices, discuss money and financial issues without (or despite) discomfort, plan for the future, and respond competently to life events that affect everyday financial decisions, including events in the general economy.

Financial literacy is at the core of the Urban League's mission to empower African Americans to attain economic self-sufficiency. The rationale for our emphasis on financial literacy is buttressed by some startling data, as revealed in our annual *State of Black America*® report and the accompanying *Equality Index*™, a statistical measurement of African Americans' progress toward closing the equality gap in wealth, health, education, social justice and civic engagement.

- African Americans' economic standing is 57% that of white Americans (*2009 National Urban League Equality Index*)

- The median net wealth of African Americans is $10,000, versus $109,100 for whites (*2009 National Urban League Equality Index*)

These astonishing statistics highlight the urgency of improving financial education in urban communities. The Urban League strategy is to create culturally competent programs that address both financial principles and long-term behavioral change. The National Urban League operates financial literacy programs in more than 75 Urban League Affiliates throughout the country. Through workshops, one-on-one counseling, and easily accessible learning materials, individuals develop effective money management strategies and, ultimately, build lasting wealth for themselves, their families, and their communities. The Urban League's financial literacy programs provide the education, tools and encouragement for individuals at all income levels to shape their own financial destinies.

Through our program experience we find that the pressing need for improved financial literacy comes from three emerging national trends. First is the deterioration of personal finances. Second is the proliferation of new, and often complex, financial products that demand more financial expertise of consumers. Third is the replacement of defined benefit pension plans with defined contribution plans that shift responsibility to consumers to fund their own retirement. Turbulent market conditions, changing tax laws, and homeland insecurity compound the need for sound financial literacy.

The National Urban League has traditionally worked in tandem with banks and foundations to design, implement, and evaluate various financial literacy curricula. Currently, we administer five such partnerships – each targeting a specific socio-demographic cohort from youth and young professionals to prospective home purchasers and established business owners and investors. In aggregate, these programs provide basic, intermediate and advanced financial counseling and education to more than 25,000 clients per year. Overall evaluation research of our financial literacy programs consistently finds significant correlations between the level of financial knowledge and good financial management practices. Individuals who are familiar with financial concepts and products are found to be more likely to balance their checkbook every month, budget for savings, and hold investment accounts. Similarly, we find that client creditworthiness and consumer literacy determine that financial knowledge is the single best predictor of behavior, such as budgeting, saving, and shopping responsibly, that translate into positive outcomes on credit bureau reports.

In conjunction with financial literacy education, housing counseling also plays a key role in support of the goal to increase financial awareness and sophistication and to close the wealth gap between minority and non-minority households. Based on our experience in recent years, we project that more than 30 of our Urban League affiliates will help about 5,000 families become homeowners this year. Moreover, an additional 10,000 families will continue to work with their counselors to become mortgage-ready during the following year. These 15,000 families represent approximately 1/3 of the clients who will receive one-on-one counseling from Urban League Affiliates supported by HUD grant funds secured under the National Urban League's National Intermediary designation. Of the remaining families who receive homebuyer counseling, a portion will determine that they are simply not in a position to become homeowners – a key, yet basic, indicator of financial awareness and aptitude. We believe that this decision is equally as important as the decision to buy a home. These educated consumers are making a wise decision about their financial capacity to sustain homeownership. In so doing, these families are avoiding subprime, or even predatory, loan products and are putting themselves in a better position to achieve homeownership in the future.

The National Urban League's Housing Counseling Program, through 36 of our affiliates, supports the delivery of a wide variety of housing counseling services to homebuyers, homeowners, low- to moderate-income renters, and the homeless. The primary objectives of the program are to expand homeownership opportunities and improve access to affordable housing. Counselors at our affiliates provide guidance and advice to help families and individuals improve their housing conditions and meet the responsibilities of tenancy and homeownership. Counselors also help borrowers avoid predatory lending practices, such as inflated appraisals, unreasonably high interest rates, unaffordable repayment terms, and other conditions that can result in a loss of equity, increased debt, default, and foreclosure.

In addition to a deeper national commitment to housing counseling – which is also a core tenet of the Homebuyer's Bill of Rights the National Urban League advocates three key objectives that the federal government and the Financial Literacy and Education Commission should pursue to promote economic opportunity for minority and low-income families and communities:

- Expand access to capital and financial services through mainstream banks and thrifts, particularly by ensuring that CRA remains effective We would also urge that Congress modernize the CRA by adopting the Community Reinvestment Modernization Act of 2009 (H.R. 1479).

- Bank the unbanked with innovative new private sector products and services, driven by new incentives for financial services for the poor.

- Promote saving among the poor by catalyzing wide-scale establishment of Individual Development Accounts and other mechanisms that help low-income families save for homeownership and other key assets.

In our view, particular emphasis should be placed on reaching neighborhoods with minority populations, since a recent Federal Reserve study shows that credit scores are significantly lower in census tracts with high minority populations. HMDA data also reinforces this point. Recent surveys show that public understanding of credit scores is low, which provides a great opportunity for the Financial Literacy and Education Commission to lead industry efforts aimed at educating consumers on the role of credit scores in the approval process.

On behalf of the National Urban League, I thank you for the opportunity to offer our views on this most important issue and we look forward to working with you as you work to implement a new regulatory system.