Financial Regulatory Reform: Analysis of the Consumer Financial Protection Agency (CFPA) as Proposed by the Obama Administration and H.R. 3126

David H. Carpenter
Legislative Attorney

Mark Jickling
Specialist in Financial Economics

July 17, 2009

Congressional Research Service
7-5700
www.crs.gov
R40696

CRS Report for Congress
Prepared for Members and Committees of Congress

Summary

In the wake of what many believe is the worst U.S. financial crisis since the Great Depression, the Obama Administration has proposed sweeping reforms of the financial services regulatory system, the broad outline of which has been encompassed in a nearly 90-page document called the President's White Paper (the White Paper or the Proposal). The Proposal seeks to meet five objectives:

(1) "Promote robust supervision and regulation of financial firms";

(2) "Establish comprehensive supervision and regulation of financial markets";

(3) "Protect consumers and investors from financial abuse";

(4) "Improve tools for managing financial crises"; and

(5) "Raise international regulatory standards and improve international cooperation."

The Administration likely will offer specific legislative proposals that would implement each of the five objectives of the White Paper. On June 30, 2009, the Obama Administration made available the first such legislative proposal, called the Consumer Financial Protection Agency Act of 2009 (the CFPA Act or the Act). The Act would establish a new executive agency, the Consumer Financial Protection Agency (the CFPA or the Agency), to protect consumers of financial products and services. On July 8, 2009, Representative Barney Frank, Chairman of the House Financial Services Committee, introduced very similar legislation, H.R. 3126, which also is entitled the CFPA Act of 2009.

This report provides a brief summary of the President's CFPA Act and delineates some of the substantive differences between it and H.R. 3126, as introduced. It then analyzes some of the policy implications of the proposal, focusing on the separation of safety and soundness regulation from consumer protection, financial innovation, and the scope of regulation. The report then raises some questions regarding state law preemption, sources of funding, and rulemaking procedures that the Act does not fully answer.

Contents

Contacts

Introduction

In the wake of what many believe is the worst U.S. financial crisis since the Great Depression, the Obama Administration has proposed sweeping reforms of the financial services regulatory system, the broad outline of which has been encompassed in a nearly 90-page document called the President's White Paper (the White Paper or the Proposal).[1] The Proposal seeks to meet five objectives:

> (1) "Promote robust supervision and regulation of financial firms" through the creation of an oversight council of the primary federal financial regulators; the provision of systemic risk oversight powers for the Federal Reserve; heightened prudential standards for financial firms; and increased federal oversight of institutions that are unregulated or only lightly regulated under current law;
>
> (2) "Establish comprehensive supervision and regulation of financial markets" by enhancing regulation over credit rating agencies; requiring originators and issuers to retain a long-term interest in securitized loans; regulating over-the-counter (OTC) derivatives; and providing the Federal Reserve with new oversight authority of payment, settlement, and clearing systems;
>
> (3) "Protect consumers and investors from financial abuse" through the creation of a new executive agency devoted exclusively to consumer protection of financial products and services;
>
> (4) "Improve tools for managing financial crises" by establishing an insolvency regime for systemically significant financial institutions and improving the Federal Reserve's emergency lending powers; and
>
> (5) "Raise international regulatory standards and improve international cooperation" by coordinating oversight of international financial firms and other regulatory changes.[2]

The Administration likely will offer specific legislative proposals that would implement each of the five objectives of the White Paper. On June 30, 2009, the Obama Administration made available the first such legislative proposal, called the Consumer Financial Protection Agency Act of 2009 (the CFPA Act or the Act).[3] The Act would establish a new executive agency, the Consumer Financial Protection Agency (the CFPA or the Agency), to protect consumers of financial products and services. On July 8, 2009, Representative Barney Frank, Chairman of the House Financial Services Committee, introduced very similar legislation, H.R. 3126, which also is entitled the CFPA Act of 2009.

This report provides a brief summary of the President's CFPA Act and delineates some of the substantive differences between it and H.R. 3126, as introduced. It then analyzes some of the policy implications of the proposal, focusing on the separation of safety and soundness regulation from consumer protection, financial innovation, and the scope of regulation. The report then

[1] Financial Regulatory Reform, Obama Administration White Paper, available at http://www.financialstability.gov/docs/regs/FinalReport_web.pdf (hereinafter, White Paper).

[2] White Paper at 3-4.

[3] Consumer Financial Protection Agency Act of 2009, available at http://www.financialstability.gov/docs/CFPA-Act.pdf (hereinafter, CFPA Act).

raises some questions regarding state law preemption, sources of funding, and rulemaking procedures that the Act does not fully answer.

Summary of the CFPA Act

Under the Act, the CFPA would be headed by a board consisting of four members appointed by the President, subject to the advice and consent of the Senate, for five-year staggered terms and subject to removal only for cause. The board also would have one ex officio member, the Director of the National Bank Supervisor[4] (proposed in the White Paper to be a new government agency, which would be established under subsequent legislation, in charge of prudential regulation of all federally chartered insured depositories).[5] The Agency would be funded through appropriations and potentially through fees assessed by the CFPA against covered entities.[6]

The CFPA would be established to "seek to promote transparency, simplicity, fairness, accountability, and access in the market for consumer financial products and services" to ensure that consumers are able to make educated decisions regarding financial products and services; that they are "protected from abuse, unfairness, deception, and discrimination"; that markets operate efficiently and fairly; and that "traditionally underserved consumers and communities have access to financial services."[7]

To implement these goals, the CFPA would have authority over a vast array of financial activities, including deposit taking, mortgages, credit cards and other extensions of credit, investment advising by entities not subject to registration or regulation by the Securities and Exchange Commission or the Commodity Futures Trading Commission, loan servicing, check-guaranteeing, collection of consumer report data, debt collection, real estate settlement, money transmitting, financial data processing, and others.[8] The CFPA would not have authority over insurance activities other than mortgage, title, and credit insurance.[9] The range of entities engaged in financial activities that would be subject to the CFPA also is expansive under the Act, including banks, credit unions, and mortgage brokers to name a few. The proposed legislation defines those covered by the Act to be

> any person who engages directly or indirectly in a financial activity, in connection with the provision of a consumer financial product or service [used primarily for personal, family, or household purposes]; or any[one who] provides a material service to, or processes a transaction on behalf of, [such] a person.[10]

Additionally, the Act would consolidate in the CFPA consumer protection regulatory and enforcement authority, which is currently shared by a number of federal agencies. The Act would

[4] H.R. 3126 refers to "the head of the agency responsible for chartering and regulating national banks," rather than a National Bank Supervisor. See the "H.R. 3126, Chairman Frank's CFPA Act of 2009" section of this report.

[5] CFPA Act § 1012. See, also, H.R. 3126 § 112.

[6] CFPA Act § 1018. See, also, H.R. 3126 § 118.

[7] CFPA Act § 1021. See, also, H.R. 3126 § 121.

[8] See definition of "financial activity," CFPA Act § 1002(18). See, also, H.R. 3126 § 101(18).

[9] See definition of "financial activity," CFPA Act § 1002(18). See, also, H.R. 3126 § 101(18).

[10] CFPA Act § 1001(9). See, also, H.R. 3126 § 101(9).

transfer to the CFPA the "consumer financial protection functions"[11] and many of the employees performing those functions from the Board of Governors of the Federal Reserve System (Federal Reserve), the Office of the Comptroller of the Currency (OCC), the Office of Thrift Supervision (OTS), the Federal Deposit Insurance Corporation (FDIC), the Federal Trade Commission (FTC), and the National Credit Union Administration (NCUA).[12] However, according to the guidelines of the White Paper, these agencies, with the exception of the OTS,[13] would retain safety and soundness supervisory and examination powers outside the purview of consumer protection over certain regulated entities.[14]

The CFPA also would be the primary federal regulator, examiner, and rulemaker[15] with enforcement authority under many of the federal consumer protection laws, including

(A) the Alternative Mortgage Transaction Parity Act[16];

(B) the Community Reinvestment Act[17];

(C) the Consumer Leasing Act[18];

(D) the Electronic Funds Transfer Act[19];

(E) the Equal Credit Opportunity Act[20];

(F) the Fair Credit Billing Act[21];

(G) the Fair Credit Reporting Act[22] (except with respect to sections 615(e), 624, and 628[23]);

(H) the Fair Debt Collection Practices Act[24];

---

[11] The CFPA Act defines "consumer financial protection functions" as "research, rulemaking, issuance of orders or guidance, supervision, examination, and enforcement activities, powers, and duties relating to the provision of consumer financial products or services, including the authority to assess and collect fees for this purpose." CFPA Act § 1061(d). See, also, H.R. 3126 § 161(d).

[12] CFPA Act §§ 1061-1066. See, also, H.R. 3126 §§ 161-166.

[13] The White Paper proposes the elimination of the thrift charter. White Paper at 32-34.

[14] White Paper at 19-42. The White Paper does propose changes with regards to who regulates whom and the scope of supervision. For a detailed discussion of the current regulatory system, see CRS Report R40249, *Who Regulates Whom? An Overview of U.S. Financial Supervision*, by Mark Jickling and Edward V. Murphy.

[15] CFPA Act § 1022. See, also, H.R. 3126 § 122.

[16] 12 U.S.C. §§ 3801 *et seq.*

[17] 12 U.S.C. §§ 2901 *et seq.* This act is not included as an "Enumerated Consumer Law" in H.R. 3126. See the "H.R. 3126: Chairman Frank's CFPA Act of 2009" section of this report.

[18] 15 U.S.C. §§ 1667 *et seq.* This act is not specifically referenced in H.R. 3126's definition of "Enumerated Consumer Law"; however, the bill does transfer enforcement authority over this act to the CFPA. H.R. 3126 § 184(b)(2).

[19] 15 U.S.C. §§ 1693 *et seq.*

[20] 15 U.S.C. §§ 1691 *et seq.*

[21] 15 U.S.C. §§ 1666-1666j. This act is not specifically referenced in H.R. 3126's definition of "Enumerated Consumer Law"; however, the bill does transfer enforcement authority over this act to the CFPA. H.R. 3126 § 184(b)(2).

[22] 15 U.S.C. §§ 1681 *et seq.*

[23] 15 U.S.C. §§ 1681m(e), 1681s-3, 1681w.

[24] 15 U.S.C. §§ 1692 *et seq.*

(I) the Federal Deposit Insurance Act, subsections 43(c) through (f)[25];

(J) the Gramm-Leach-Bliley Act, sections 502 through 509[26];

(K) the Home Mortgage Disclosure Act[27];

(L) the Home Ownership and Equity Protection Act[28];

(M) the Real Estate Settlement Procedures Act (RESPA)[29];

(N) the S.A.F.E. Mortgage Licensing Act[30];

(O) the Truth in Lending Act (TILA)[31]; and

(P) the Truth in Savings Act.[32]

The CFPA would be required to monitor the market and the innovation of new products and services. In order to do so, the Act would provide the Agency the authority to examine covered persons, including national banks, federal credit unions, and federal savings and loan associations.[33] Under current law, examination powers generally rest exclusively in the institutions' primary regulators.

Rather than explicitly imposing new regulation on financial activities and products, the Act primarily (though, not exclusively[34]) leaves such decisions to be made by the CFPA through future rulemaking and guidance. The Agency would have the authority to promulgate rules and issue guidance and orders to meet the objectives of the CFPA Act.[35] The standard rulemaking procedures provided by the Act would require the Agency to weigh the costs and benefits to both consumers and industry, including the potential effect the rule would have on the availability of financial products and services.[36] The Agency also would have to "consult with the Federal banking agencies ... regarding the consistency of a proposed rule with prudential, market, or systemic objectives administered by such agencies."[37] Within three years[38] of any CFPA

[25] 12 U.S.C. § 1831t(c)-(f).

[26] 15 U.S.C. §§ 6802-6809.

[27] 12 U.S.C. §§ 2801 *et seq*.

[28] 15 U.S.C. § 1639.

[29] 12 U.S.C. §§ 2601-2610.

[30] 12 U.S.C. §§ 5101-5116.

[31] 15 U.S.C. §§ 1601 *et seq*.

[32] 12 U.S.C. §§ 4301 *et seq*.

[33] CFPA Act §§ 1022(c) and 1024. See, also, H.R. 3126 §§ 122(c) and 124.

[34] However, the Act would impose some substantive regulations. For example, the Act would require disclosure of new data points under the Home Mortgage Disclosure Act. CFPA Act § 1086(f).

[35] CFPA Act § 1022(a). See, also, H.R. 3126 § 122(a). The CFPA would be expressly prohibited from setting a usury cap without specific authorization by law. CFPA Act § 1022(g). See, also, H.R. 3126 § 122(g). The Act specifically provides the Agency the authority to prohibit or limit arbitration clauses. CFPA Act § 1025. See, also, H.R. 3126 § 125.

[36] CFPA Act § 1022(b). See, also, H.R. 3126 § 122(b).

[37] CFPA Act § 1022(b). See, also, H.R. 3126 § 122(b).

[38] The Agency may delay the report for up to five years after the effective date if it determines that three years is not enough time to adequately review the rule. CFPA Act § 1024. See, also, H.R. 3126 § 124.

"significant rule or order" becoming effective and after a public comment period, the Agency must publish a report assessing the effectiveness of the rule or order.[39] The Act does not specify what would be considered "significant," presumably leaving these determinations to the Agency.

The Act imposes additional procedures upon specific types of rulemaking. For instance, the Agency would be authorized to promulgate rules on unfair or deceptive practices in connection with consumer financial services and products. However, the Agency could only promulgate a rule deeming an act unlawfully *unfair* if

> the Agency has a reasonable basis to conclude that the act or practices causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers and such substantial injury is not outweighed by countervailing benefits to consumers or to competition.[40]

Other examples of specific rulemaking authority for which the CFPA Act would impose requirements in addition to the Act's standard rulemaking procedures outlined above include disclosure requirements;[41] minimum standards for the prevention and detection of "unfair, deceptive, abusive, fraudulent, or illegal transactions";[42] provision of "standard consumer financial products or services" that may serve as a comparison to similar, but less traditional products or services;[43] and imposition of duties, including compensation practices, on covered persons.[44]

All of these steps and restrictions exceed the normal notice and comment procedures of the Administrative Procedure Act, which generally apply to agency rulemaking.[45]

The Act would *not* preempt state consumer protection laws that provide greater protections to consumers, but would preempt otherwise conflicting state laws. The CFPA would decide whether or not particular state laws conflict with the Act,[46] with specific decisions subject to judicial review.[47] Any generally applicable state consumer law would apply to national banks and savings and loans unless it discriminates against them or conflicts with the Act.[48] Additionally, any state consumer law regulating state banks or state savings and loans that was enacted in compliance with federal law also would apply to national banks and savings and loans unless it discriminates against the federally chartered institutions or conflicts with the CFPA Act.[49] Depending on how

[39] CFPA Act § 1024. See, also, H.R. 3126 § 124.

[40] CFPA Act § 1031. See, also, H.R. 3126 § 131.

[41] CFPA Act §§ 1032 and 1034. See, also, H.R. 3126 §§ 132 and 134.

[42] CFPA Act § 1035. See, also, H.R. 3126 § 135.

[43] CFPA Act § 1036. See, also, H.R. 3126 § 136.

[44] CFPA Act § 1037. See, also, H.R. 3126 § 137. The Agency would only be able to enforce violations of duties prescribed under the authority of § 1037 in accordance with an adjudicatory proceeding described in great detail in §§ 1051-1058 of the Act. CFPA Act § 1037. See, also, H.R. 3126 § 137.

[45] 5 U.S.C. § 553. See, also, CRS Report RL32240, *The Federal Rulemaking Process: An Overview*, by Curtis W. Copeland.

[46] CFPA Act § 1041. See, also, H.R. 3126 § 141.

[47] For a description of judicial review of statutory interpretation by agencies, see CRS Report R40595, *Cuomo v. Clearing House Association, L.L.C: National Banks Are Subject to State Lawsuits to Enforce Non-Preempted State Laws* , by M. Maureen Murphy.

[48] CFPA Act §§ 1043(b)-(c) and 1046(b)-(c). See, also, H.R. 3126 §§ 143(b)-(c) and 146(b)-(c).

[49] CFPA Act §§ 1042(d) and 1046(d). See, also, H.R. 3126 §§ 142(c) and 146(d).

they are interpreted by the Agency and the courts, these provisions could result in a departure from current federal banking law, which the OCC and other banking regulators interpret as preempting many state consumer laws.[50]

H.R. 3126, Chairman Frank's CFPA Act of 2009

There are three major substantive differences between H.R. 3126, as introduced, and the Obama Proposal. One is that H.R. 3126 does not transfer oversight and enforcement authority over the Community Reinvestment Act to the CFPA, as proposed by the Obama Proposal.[51] A second is that H.R. 3126 does not envision the elimination of the thrift charter, and by extension, the Office of Thrift Supervision. The President's White Paper proposes eliminating the thrift charter and converting such entities into state or national banks, while also modifying the regulatory framework to which banks are subject.[52] It is still unclear how (or if) Congress will propose to change the prudential regulation of financial institutions, including banks and thrifts. The fact that H.R. 3126 continues to reference thrifts and the Office of Thrift Supervision is not an indication that changes will not be made to them in the future—just that such changes have yet to be made and are not proposed in H.R. 3126.[53] As a result of their variant treatment of thrifts, the President's CFPA Act and H.R. 3126 divide regulatory authority differently, which is primarily manifested in the two proposals' conforming amendment sections. Similarly, H.R. 3126 does not make reference to a National Bank Supervisor like the President's CFPA Act. Instead, H.R. 3126 refers to "the head of the agency responsible for chartering and regulating national banks."[54]

Would the CFPA Be An Improvement?

The Treasury's White Paper argues that the CFPA is necessary because recent events in financial markets have exposed the inadequacy of the current regulatory framework. As an example, the White Paper cites overly complicated, nontraditional mortgages that were unsuitable for the many borrowers who lost their homes to foreclosure.[55] By creating an agency dedicated exclusively to consumer protection, Treasury hopes to raise standards for financial intermediaries and ultimately foster a culture of consumer protection within financial firms. In the White Paper's analysis, the imperative to protect consumers was simply overwhelmed by profit considerations—by its very existence, the CFPA is intended to right the balance.[56]

There are benefits to having a single agency in charge of virtually all consumer financial products and services and consumer protection laws. But there are also costs, which may fall either on

[50] See, e.g., 12 C.F.R. §§ 7.4000 *et seq.* and Part 34. See, also, CRS Report RL32197, *Preemption of State Law for National Banks and Their Subsidiaries by the Office of the Comptroller of the Currency*, by M. Maureen Murphy.

[51] H.R. 3126 § 101(16).

[52] White Paper at 30-31.

[53] However, Chairman Frank has reportedly stated that he does not believe the House Financial Services Committee will pass legislation that would eliminate the thrift charter. Bill Swindell, *Frank: No Need to Scrap Federal Thrift Charter*, CongressDaily, July 15, 2009.

[54] See, e.g., H.R. 3126 § 112(a).

[55] White Paper at 55.

[56] White Paper at 57.

regulated financial institutions or on consumers. The CFPA proposal raises a number of basic questions about the structure and purposes of regulation.

Redundancy?

The powers that CFPA would have are primarily derived from federal banking statutes. This raises the objection that the existing bank regulators already have full authority to do what the new agency would do. What would prevent failures in regulation from being addressed within the existing structure?

One can argue that there is a conflict between safety and soundness regulation and consumer protection. When a banking activity is profitable, regulators tend to look upon it favorably, since it enables the bank to meet capital requirements and withstand financial shocks. According to the White Paper, professional bank examiners are trained "to see the world through the lenses of institutions and markets, not consumers."[57] This conflict may be especially sharp in consumer lending.

Over the past several decades, banks and other financial institutions have expanded the scale and scope of their consumer lending programs. Partly driven by competition from the securities industry (which has largely supplanted banks as a source of funds for large corporations), and partly by the availability of computerized credit scoring models (which dramatically reduce the cost of evaluating borrowers' creditworthiness), mainstream lenders have made credit available to consumers who not long ago would have been viewed as too risky and unqualified.[58]

Credit card and subprime mortgage lending are perhaps the most visible results of this trend. On the one hand, they represent a great expansion in the availability of credit and have allowed many consumers to raise their standard of living. On the other hand, both have been criticized for high costs to borrowers, hidden fees, and/or excessive complexity, to the extent that lending practices have been described as unscrupulous and abusive. If one believes that banks have sought to maintain their profits by offering credit to consumers with limited financial resources and sophistication, many of whom accumulate heavy debt burdens,[59] the case for a CFPA may be strong.

On the other hand, it can be argued that even very expensive forms of credit—such as predatory or payday lending—are welfare-enhancing,[60] that the balance between safety and soundness regulation and consumer protection ought not to be shifted in favor of the latter, and that the CFPA would add a redundant layer of regulation.

[57] White Paper at 56.

[58] Darryl E. Getter, "Consumer Credit Risk and Pricing," *Journal of Consumer Affairs*, vol. 40, Summer 2006, p. 41.

[59] According to the Federal Reserve's Survey of Consumer Finances, 26.9% of the families in the bottom 20% of the income distribution devoted more than 40% of their incomes to debt repayment in 2007.

[60] There is empirical evidence for this. See, e.g., Paige Marta Skiba and Jeremy Tobacman, "Measuring the Individual-Level Effects of Access to Credit: Evidence from Payday Loans," *The Mixing of Banking and Commerce: Proceedings of the 43rd Annual Conference on Bank Structure and Competition*, Federal Reserve Bank of Chicago, 2007, p. 280; and Jonathan Zinman, "Restricting Consumer Credit Access: Household Survey Evidence on Effects Around the Oregon Rate Cap," Federal Reserve Bank of Philadelphia Working Paper 08-32, December 2008.

Financial Innovation

An argument against CFPA is that it could stifle financial innovation. Innovative practices are by definition less well understood than traditional ones,[61] and financial institutions tend to earn higher margins on new products, at least until their competitors enter the market and compete away excess profits. Both factors might appear problematic to a consumer protection regulator, though not necessarily to a safety and soundness regulator.

The White Paper is explicit about favoring and promoting traditional, "plain-vanilla" financial products. The White Paper stresses the need to achieve simplicity, fairness, and reasonable disclosure;[62] and the Act would provide the CFPA the authority to impose duties of care and suitability requirements on financial firms. Opponents of the CFPA might argue that this attitude could lead to the creation of barriers and hurdles—perhaps in the form of slow approval of disclosure forms—to the introduction of new products.

Treasury officials have made clear their concern that the classical economic model of rational, informed consumers, able to act in their self-interest, is not a sound basis for regulation. For example:

> Michael Barr [Assistant Secretary for Financial Institutions], who is leading the consumer-protection efforts, said the "plain-vanilla" financial products have their roots in behavioral economics and psychology. It isn't enough to provide consumers with more disclosure and more information, since people often get easily overwhelmed and make mistakes, said Mr. Barr, a former academic who studied the financial markets.
>
> Most people, for example, don't understand the effects of compounding of interest—which leads them to undersave and to overborrow—a basic human failing that some financial institutions have an incentive to exploit.[63]

The debate over strengthened consumer protection, in other words, involves the age-old question of how much government intervention into markets is warranted: should consumers be protected from their mistakes, or trusted to make decisions that will enhance individual and common welfare? The issue of financial innovation can be framed similarly: is development of new and/or exotic financial products to be encouraged, or are they potentially troublesome if they gain wide currency before the risks are fully understood by regulators and market participants?

Jurisdiction

Under the Treasury proposal, the SEC and CFTC would retain their consumer protection role in securities and derivatives markets.[64] This could be viewed as a flaw, which would preserve the existing fragmented federal regulatory structure. The banking and securities industries have for years offered products that compete with each other—money market funds, brokerage checking

[61] This is the case for all financial products, not just those designed for consumers.

[62] White Paper at 63-67.

[63] Jane J. Kim, "Plain-Vanilla Financing Could Melt Bank Profits – U.S.'s Bid to Help Consumers; Mystery of Compound Interest," *Wall Street Journal*, Jun. 26, 2009, p. C1. Behavioral finance posits that consumers are "hard-wired" to make bad financial choices, and that education is only a partial remedy.

[64] The White Paper does recommend certain enhancements to the SEC's authority: see, e.g., p. 70.

accounts, investment advice through bank trust departments, etc.—and issues of overly complex products, inadequate disclosure, conflicts of interest, and the extent of fiduciary duties are common to both.

Since the onset of the financial crisis, households' losses in real estate have been exceeded by their losses in securities investments.[65] Not all those losses resulted from fraud or regulatory failure, but the SEC's recent record is not notably better than the bank regulators'. The logic of creating a single agency exclusively concerned with consumer financial protection, and excluding securities (and futures[66]) may not be clear.

For comparison, the Financial Services Authority in the United Kingdom has consumer protection powers over all financial industries, including banking, securities, derivatives, and insurance. Its objectives, as posted on its website, appear to mirror those of the proposed CFPA. The Financial Services and Markets Act gives the FSA four statutory objectives:

- Market confidence: maintaining confidence in the financial system;
- Public awareness: promoting public understanding of the financial system;
- Consumer protection: securing the appropriate degree of protection for consumers; and
- The reduction of financial crime: reducing the extent to which it is possible for a business to be used for a purpose connected with financial crime.[67]

Is there a different regulatory structure, where jurisdiction is split differently among multiple regulators, that could lead to a greater balance of the regulatory costs and benefits? Are there other products and services that should be excepted from the CFPA's jurisdiction?

Questions Left Unanswered

Preemption

How narrowly or broadly will the Agency interpret potential conflicts between state and federal law? If interpreted narrowly, then the Act's preemption language could have a detrimental effect on banks and other entities that provide consumer financial products and services in multiple states because they would be working within multiple regulatory regimes, increasing administrative costs that likely would be passed on to consumers.[68] If the Agency interprets conflicts broadly, then interstate actors may only have a single set of rules to follow, but consumers may not be as fully protected from predatory products, services, and practices as they would be otherwise.

[65] Between the end of 2006 and the first quarter of 2009, households lost $4.01 trillion of the value of their real estate holdings, while the value of corporate stock and mutual funds held by households (and non-profits) fell by $5.10 trillion. Federal Reserve, Flow of Funds Accounts, Table B. 100.

[66] Although relatively few individuals trade in derivatives markets.

[67] http://www.fsa.gov.uk/Pages/about/aims/statutory/index.shtml.

[68] This potentially could put entities acting only within a single state at a competitive advantage over interstate actors.

Funding

How much funding would come from fees on covered entities? How would the annual fees be tabulated (e.g., based on number of covered transactions or size of company)? If such fees were assessed, would those costs be passed onto the consumer? Would that be more beneficial to the public as a whole than paying for the Agency through normal appropriations? The agencies from which many of the CFPA employees would be transferred are largely self-funded through fees assessed on the companies under their regulatory jurisdiction. Some have argued that this source of funding played a role in lax regulatory enforcement by federal agencies because banks have an incentive to seek the regulator they believe will have the lightest regulatory touch, while the regulators generate more fees with every institution they bring under their jurisdiction.[69] Would funding the CFPA through fees lead to similar problems? On the other hand, running the Agency will be expensive. The ability of the CFPA to generate at least some of its own funding could reduce the Agency's need for general appropriations.

Rulemaking

Are the Act's rulemaking procedures appropriately drawn? As previously mentioned, agency rulemaking generally only requires public notice of proposed rulemaking and a period for public comment on the matter. The Act would require steps in addition to notice and comment. For instance, the CFPA would have to make findings regarding the costs of potential rules on both industry and consumers. Additionally, the Agency would have to review any significant rule within three to five years after its effective date. The Act would impose other restrictions on rulemaking, as well. If rulemaking procedures are too easily met, then the Agency could go too far, promulgating rules that have a deleterious effect on consumers' access to credit and on industry's profitability. If procedures are so restrictive that the Agency is unable to pass rules in a timely fashion, consumers could be harmed by otherwise preventable predatory products and practices, which also could lead to long-term harm to industry. If overly restrictive, the rulemaking process itself could be expensive, increasing costs to taxpayers and potentially to consumers and industry if the Agency imposes fees on products and services.

Author Contact Information

David H. Carpenter
Legislative Attorney
dcarpenter@crs.loc.gov, 7-9118

Mark Jickling
Specialist in Financial Economics
mjickling@crs.loc.gov, 7-7784

[69] See, e.g., Adam Levitin, *Bank Regulatory Arbitrage and Deregulation: The Number of Bank Regulators Matters*, Credit Slips: A Discussion on Credit and Bankruptcy, available at http://www.creditslips.org/creditslips/2009/06/one-of-the-key-points-of-debate-over-financial-institution-regulation-reform-is-how-many-different-bank-regulators-there-shou.html.