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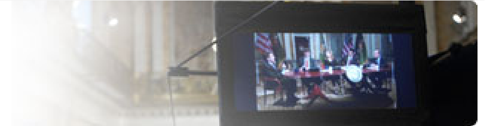

Assistant Secretary Michael S. Barr Remarks to Consumer Federation of America’s 21st Annual Conference, “The Consumer in the Financial Services Revolution” December 3, 2009

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Thank you, Steve for inviting me to speak to you today.

Your conference today could not be more timely. This is truly a critical time in our work to reform consumer protection in financial services and more broadly, the system of regulation in the financial sector.

CFA's leadership was instrumental in getting strong legislation passed to protect Americans from unfair and abusive credit card practices.

And now, we have a chance to build on that success and achieve fundamental reform to better protect responsible consumers of all financial products and services.

President Obama has put forward a comprehensive plan for reform, closing loopholes in our laws that fed the financial crisis.

The goals of the Administration's financial reform proposal are straightforward: we need to give responsible families and investors the basic protections they deserve; we need to close loopholes and lay the foundation for a safer, more stable financial system, one less prone to panic and crisis; we need to safeguard families and taxpayers from bearing unnecessary risks and costs that ought to be borne by shareholders and creditors; and we need to ensure that our financial system and economy work for everyone.

Chairman Frank has now passed a comprehensive package through the House Financial Services Committee which is expected to move to the full House for consideration quite soon. Chairman Dodd is working aggressively to finalize a bill for markup in the Senate Banking Committee.

And while we are pleased with the progress of legislation on financial reform, it is imperative that we keep pushing towards the goal – and to push hard, now – to achieve lasting reform.

In the years leading up to the crisis, Wall Street firms took huge risks with borrowed funds and little of their own capital at stake. This was a period during which they failed to appreciate the incredible risk they were unnecessarily creating for the economy and American taxpayers. Firms offering mortgages and credit cards lured families in with promises of low interest rates and did not make them aware of the fine print, hidden fees, and future payment increases. It's true that many took on too much debt and took out loans they couldn't afford; however, millions of Americans behaved responsibly and still found themselves in jeopardy because of the sharp practices of some in the financial industry.

Regulators failed, too. Regulators of financial institutions were sometimes lax and inconsistent and capital requirements way too low. Protections for consumers were woefully inadequate. And key parts of the system were simply not regulated. Financial regulators failed to adequately use even their existing authorities. And when the crisis struck, it quickly became apparent that the government did not have the tools to handle the failure of major firms without the risks of destabilizing the financial system and imperiling the economy.

In the panic that followed, our financial system nearly ground to a halt , costs in lost jobs and retirement savings, homes foreclosed upon, shuttered plants, and struggling small businesses has been truly extraordinary.

Now, following unprecedented actions by the Executive branch and Congress, we have pulled the economy back from the brink. Today, important parts of the financial system are back to functioning on their own and some of the damage to families' savings has been repaired.

The progress of recovery must not distract us, however, from the need for fundamental financial reform. The regulatory system that failed so terribly leading up to the financial crisis is precisely the one we have today. The weaknesses that contributed to the financial crisis persist. To ensure the vitality and stability of our economy going forward, we need comprehensive financial reform.

There are at least four key principles that we must follow in order to create a more stable financial system – one that works for American families and for American businesses.

First, financial institutions and their investors must be held responsible for their decisions. No financial system can operate efficiently if financial institutions assume that the government will protect firms from the consequences of failure. We must build a system in which individual firms, no matter how large or important, can fail without risking catastrophic damage to the economy.

Second, there must be unmistakable accountability in government supervision of the biggest firms. In our judgment, the Federal Reserve is the agency best equipped for the task of supervising the largest, most complex firms. It is the only agency with broad and deep knowledge of financial institutions and the capital markets necessary to do the job effectively.

Third, to protect American families and businesses, we need to do more to advance the stability of the financial system. Financial firms are deeply intertwined, which allows financial distress to spread contagion across the system. The risk of such contagion means that capital, liquidity and margin requirements must be increased, system-wide – and set with a view to ensuring the stability of the financial system as a whole, not just the solvency of individual institutions.

Some firms were allowed to sell large amounts of protection against certain risks without adequate capital to back up those commitments. Because of their enormous scale and the critical role they play in transferring risk around our financial system, the Administration has proposed a comprehensive framework of oversight of the over the counter derivative markets, which is crucial to laying the foundation for a safer, and more stable financial system.

And fourth, loopholes and gaps in the existing regulatory framework must be closed. Firms engaged in the same kind of businesses, performing the same essential economic functions, generally should be subject to fundamentally the same regulation and supervision. Today, banks and non-banks operate in the same market and compete for the same customers but non-banks like mortgage brokers, consumer credit companies and payday lenders escape federal supervision almost entirely. This inconsistent regime sparked a race to the bottom in the mortgage lending market, and the consequences are tragic and well known.

This brings me to the President's proposal to create a new agency to protect consumers in the financial services marketplace. Earlier today you heard a debate about this proposal, but there is no debating that today's consumer protection regime helped cause the crisis. There is no debating that today's consumer protection regime invites banks to choose the least restrictive supervisor while leaving non-banks without ongoing supervision, thereby encouraging a race to the bottom. And, there is no debating that today's consumer protection regime is highly fragmented, with no one held accountable which leads to finger-pointing in place of action. In short, there is no debating that our current system is designed for failure. And fail it did.

These deep structural flaws cannot be solved by tinkering with the consumer protection mandates or authorities of our existing agencies. That's why the Administration and Congress are working together to overhaul the current structure and create the Consumer Financial Protection Agency: one agency with mission focus, market-wide coverage, and consolidated authority for consumer financial products and services.

Under the current system, no agency is responsible for looking out for American families in mortgage, credit, and other consumer financial products. While the banking agencies do conduct consumer protection compliance supervision, such supervision has too often been relegated to second class status. The banking agencies have too often focused more on protecting banks or thrifts from "reputation risk" than on protecting consumers. And entrusting the banking agencies with responsibilities to examine for compliance with consumer protection laws did not prevent our major banks and thrifts from retroactively raising rates on credit cards as a matter of policy, or from selling exploding mortgages to unwitting consumers.

In contrast, the new Consumer Financial Protection Agency will have one, and only one, mission: to protect Americans in the consumer financial services marketplace. It will consolidate the patchwork system now divided among seven agencies. This consolidation will streamline the bureaucracy and ensure accountability. The CFPA will be accountable for preventing abuse of American families while preserving access to financial products and services. It will have the authority to establish rules of the road so that a wide range of consumer financial products and services are fairly marketed, sold, and provided to consumers – from mortgage and auto loans, to credit and debit cards, to payday loans and stored value products.

Under the current system, no federal regulator sends consumer compliance examiners to non-bank providers to review their files, interview their salespeople, or analyze their data. Non-bank providers offer a wide range of credit products – from mortgages to payday loans, to auto loans and car title loans, many from large national chains. But they are typically only subject to after-the-fact, infrequent investigations and enforcement actions by the Federal Trade Commission or state attorneys general if at all. This fragmented regulatory structure has led to declining standards, regulatory arbitrage, and a failure by regulatory agencies to respond to emerging practices which may pose special risks to responsible consumers.

That's why we need the Consumer Financial Protection Agency. The CFPA will be able to write and enforce clear rules of the road for the entire marketplace of consumer financial products and services in both the bank and non-bank realms. The CFPA will cover mortgage brokers, mortgage companies, finance companies, payday lenders, and banks. Responsible consumers would get the same protection, no matter who they deal with. For example, the CFPA could adopt consistent regulations for short-term loans, whether they come in the form of bank overdraft protection plans or payday loans or car title loans from non-bank providers.

Writing rules across the entire market will help ensure consistent standards for the benefit of consumers and providers alike, but rules alone are not enough to ensure a fair marketplace. Enforcement must also be consistent. A strong enforcement role for the CFPA will help ensure true consistency and a strong examination and reporting authority will enable the agency to identify weaknesses in firms' compliance systems and identify worrisome trends in the market.

When it identifies a problem, the new agency will be able to use the full potential of supervisory guidance and other tools to tailor an appropriate remedy, stop problems before they spread and cause serious injury, and relieve pressures on responsible providers to lower their standards. The CFPA will end profits based on misleading sales practices and hidden traps, creating a level playing field where banks and nonbanks alike can compete instead on the basis of price and quality.

Rules and their enforcement are just two tools of oversight. Consumers and providers need an agency that has a much broader range of tools. They need an agency that can move the market with supervisory guidance, best practices, and other flexible, less burdensome techniques.

But the CFPA can only depend on softer, more supple techniques to move the market if it has stronger authorities at its disposal. For best practices or supervisory guidance to work, the market needs to know that the agency has strong rule-writing, enforcement, and supervisory powers as well. By giving the agency a wide range of tools, we ensure that it will be able to choose the tool that is the most effective, least costly way to address the problem.

Years-long delays to issue guidance because of inter-agency wrangling will be a thing of the past. And because of fragmented authority, we have had unacceptable delays in consumer protections for mortgages, credit cards, privacy, and the like.

It took the federal agencies until June 2007 to reach final consensus on supervisory guidance imposing even general standards on the sale and underwriting of subprime mortgage practices – two years after evidence of declining underwriting standards emerged publicly in a regulator's survey of loan officers. By that time the subprime explosion was nearly over. It took additional time for states to adopt parallel guidance for independent mortgage companies. And it took a third year for the federal agencies to settle on a model disclosure of subprime mortgages – until mid 2008 – by which point the subprime market had long ago imploded.

The same thing happened with credit cards. For years issuers were allowed to boost fee and interest income with complex and opaque terms and features that most consumers did not notice or understand. So consumers had years of retroactive rate hikes, rate hikes without notice, and low-rate balance transfer offers that trapped them in high-rate purchase balances. The culprit, once again, was fragmented regulation.

Turning to privacy, it has taken six agencies six years to adopt rules to improve the accuracy of information reported to credit bureaus and establish procedures for consumers to file disputes with information furnishers. Clearly consumers deserve better.

In short, the CFPA will have the coverage and authority needed to bring higher and more consistent standards; stronger, faster responses to problems; an end to regulatory arbitrage; a level playing field for all providers; and smarter, more efficient regulation where it is needed.

More than a year after the breakdown last September, there should be no disagreement that reform is urgently needed. Financial reform is critical to restoring economic security to our nation, our communities, our businesses, and our families.

I'd like to thank you all once again for your tireless fight for the interests of American families.

Make no mistake about what we are up against in getting over the finish line: we need to overcome the powerful special interests that are making it their mission to kill financial reform. Lobbyists are working overtime right now to protect the status quo. This is no surprise: the status quo worked just fine for big banks and those who took advantage of low standards and little oversight. But it did not work out for millions of consumers who have lost their jobs, lost their homes, and their retirement savings.

We can't let this happen again, and must redouble our efforts to fight for what American families deserve: a system that will ensure common sense rules of the road and a stable, fair and open financial system.

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