I want to thank the Credit Union National Association for hosting me today.

When President Obama came into office just over a year ago, our financial markets were frozen, our economy was shrinking, and many people feared another Great Depression. Today, the efforts of the Administration are helping to stabilize our financial system, grow the economy, and reduce the widespread harm brought by the failed policies of the past. The economy grew at a positive annual rate of 5.7 percent in the last quarter of 2009, compared to negative 5.4 percent in the last quarter of 2008.

But we have much more to do – to create jobs, grow the economy, strengthen our financial system, and rebuild our housing markets. The unemployment rate is unacceptably high, and so is the rate of home foreclosures. Too many American families are feeling deep pain and uncertainty. Small businesses, too, are struggling, as they continue to find it difficult to obtain credit. Without adequate credit, it is harder for businesses to hire more workers. Analysts of all stripes agree that the Recovery Act has created and preserved one to two million jobs and kept the doors open for many small businesses, but we must do better. The President is building on this success with new legislation to promote jobs and new initiatives to support small businesses.

**Comprehensive Financial Reform**

As we work to grow the economy and expand jobs, we must also reform a financial regulatory system that remains fundamentally flawed. These flaws, if not corrected, will weaken long-term growth and expose families, businesses, and taxpayers to unnecessary risk. The pain our country has endured for the past two years should leave no doubt about the high cost of failing to adopt major reform.

The self-evident urgency of reform has not stopped lobbyists from trying to slow progress or weaken reform.

But people who are actually in the business of making loans to families and helping them save, people like you, are acutely aware that we must lay a new foundation for our financial system to ensure growth is sustainable. We must put new rules in place as swiftly as possible to provide the certainty that markets need. And we must enact legislation that provides the basis for those new rules – without delay.

The status quo is not acceptable. The same gaps and loopholes that allowed firms like Bear Stearns and Lehman Brothers to escape meaningful consolidated supervision remain. The same gaps in regulation of over the counter derivatives that permitted AIG to sell its products with inadequate capital and weak oversight remain.

And we cannot let these weaknesses remain lest our new financial system be erected on a crumbling foundation. We must close these loopholes so no major firm escapes serious oversight. We must have comprehensive reform of our financial markets, including for derivatives transactions and securitization of mortgages.

A key test of the sufficiency of any reform proposal is how it addresses the large, complex financial firms that were at the center of the crisis. The financial system did not effectively contain risk-taking by these firms, and the actions that governments took to address the crisis have left us with a significantly increased risk of moral hazard. That is the corrosive problem of "too big to fail."

Our proposal addresses the too big to fail problem directly and forcefully. It imposes stronger prudential standards on all major financial firms, and it will make these standards less pro-cyclical once the system emerges from the crisis. Our proposal makes the system much safer for the failure of a large firm. It builds stronger shock absorbers across financial markets and the financial infrastructure. And it gives the government the tools to wind down failing major non-bank financial firms without risking a broad financial panic.

**Accountable and Effective Oversight of Consumer Financial Markets**

I want to spend the rest of my time talking with you about the markets for consumer financial products and services. These are markets that you know intimately. Consumer products and services are bread and butter for credit unions. You have seen how unfair and opaque practices can undermine you and your members.
And that is precisely why the Administration is proposing to ensure accountable and effective oversight of consumer financial markets. Accountability must be market-wide. There must be clear accountability for ensuring robust standards and enforcement across the entire market. This accountability is lacking in today's system, which fragments the consumer marketplace over seven federal agencies. We have proposed to consolidate authority in a Consumer Financial Protection Agency. It would have the mission of ensuring fair and efficient consumer financial markets where providers can compete on a level playing field regardless of their legal form.

Some have tried to paint this proposal as partisan or ideological. But not so long ago, the administration of President George W. Bush, in its 2008 Blueprint for a Modernized Financial Regulatory Structure, also proposed to assign regulation of consumer financial markets and bank safety and soundness to separate agencies. Under this proposal, a separate business conduct regulator would be responsible for both investor protection and consumer protection. The Bush Administration concluded that assigning consumer and investor protection and prudential regulation to a single agency could lead to one function dominating over the other and a misallocation of resources. The Bush Administration called separating these functions in the long term into distinct agencies, quote, "optimal." So proposals to create a separate and independent consumer financial protection regulator are neither partisan nor ideological; they are bi-partisan and pragmatic.

Two different administrations have agreed that bringing regulation of consumer financial markets regulation out from under prudential regulators is the most effective way to provide the accountability and effectiveness the system is lacking. Creating true accountability requires more than just assigning a mandate to an agency. Real accountability requires a grant of the authority, tools, and resources needed to achieve the mandate. And accountability must be supported by real independence to make and carry out decisions.

Robust Standards and Enforcement for the Entire Consumer Financial Marketplace

A critical objective of consumer regulation should be to ensure fair and efficient consumer financial markets where providers can compete on a level playing field regardless of their legal form. A major barrier to achieving this objective has been limited federal oversight of non-bank providers. I would submit that separating oversight of consumer financial markets from safety and soundness supervision will go a long way toward overcoming this barrier.

Concentrating federal authority for consumer financial regulation in banking agencies has had the predictable result of channeling federal resources disproportionately to compliance and enforcement with respect to banks and credit unions. The federal government spends at least 15 times more on consumer compliance and enforcement for banks and credit unions than for nonbanks – even though there are at least five times as many nonbanks as there are banks and credit unions.

That is a remarkable disparity. And it is unfair, it is inefficient, and it can ultimately undermine safety and soundness – as we saw with the government's failure to prevent bad mortgage practices from growing in the non-bank sector and infecting the banking sector.

Separating consumer market oversight from bank supervision will go a long way toward correcting this misallocation of federal resources. Separation will ensure that oversight of consumer financial services markets is the regulator's highest priority, not incidental to its core mission. And it will ensure that substantial resources are spent on ensuring a level playing field for all providers. The bill that passed the House leaves over 99% of credit unions with the National Credit Union Administration as their primary federal consumer compliance supervisor. This bill also leaves over 98% of banks and thrifts with their prudential supervisor as their primary consumer compliance supervisor. The CFPA will concentrate supervisory resources on big banks and nonbanks to ensure the marketplace you compete in is fair and competitive.

Separating Consumer Protection Will Strengthen Safety and Soundness

Two different administrations have concluded that maintaining separate and independent consumer and prudential functions would strengthen American households, our markets, our banks and credit unions, and our financial system. But now the lobbyists find it convenient to assert that this bipartisan conclusion is wrong. They are saying that separating consumer protection from safety and soundness would undermine our banking system.

A consumer financial markets regulator will be interested in protecting consumers from sharp practices of the type that pervaded segments of the mortgage market before the crisis. The CFPA will be no more interested in weakening underwriting standards, for example, than prudential regulators are interested in weakening capital standards.

Some have raised a different safety and soundness concern – that prudential regulators would lose insight into weaknesses of the institutions they supervise if consumer compliance examinations were conducted by a separate agency. Our proposal fully addresses this concern. It creates a CFPA that will have the resources and incentives to detect weaknesses in banks' consumer practices and bring them to prudential regulators' attention. It requires the CFPA to share supervisory information with the prudential regulator. And it requires the agencies to coordinate closely. We fully expect the system we have proposed will be more likely to bring bank weaknesses to the attention of prudential regulators than a system in which consumer compliance supervision is subordinated to prudential supervision.

Our proposal will strengthen the banking system, not weaken it. More transparent markets, markets where nonbanks are subject to oversight, markets with fewer unfair or deceptive practices – these are markets in which banks and credit unions will be stronger. Dedicating consumer markets regulation to a fully accountable agency will give banks and credit unions a more predictable regulatory environment. Institutions will have more certainty, which will make it easier to build a sustainable business.
There is palpable irony in the assertion that separating functions will undermine safety and soundness. Recent history suggests it is subordination of consumer financial markets regulation, not its separation, that poses the far greater risk to safety and soundness. Prudential regulators have too often delayed action against unfair consumer practices until the threat to bank earnings becomes palpable (as with mortgages), until banks are so dependent on unfair practices that public outrage cannot be ignored (as with overdraft loans), or until both occur (as with opaque and overloaded credit cards).

Delays in addressing failures of consumer markets is deeply damaging to banks and credit unions, not just consumers. Neglect of unfair practices is almost inherently pro-cyclical. That is, it exacerbates the downside of the credit cycle for banks and credit unions. Neglect makes it more likely that opaque credit practices will increase consumer debt beyond sustainable levels, which magnifies the drop in bank earnings when consumers default and deleverage at higher rates. Inattention to consumer market problems is also procyclical in another sense: it delays reform for so long that, when it finally comes, reform is more likely to fall on institutions on the downside of the credit cycle, when they are already struggling. And reform after long delay is likely to be more substantial and impose heavier adjustment costs. Let us not perpetuate a system that undermines banks and credit unions in these ways.

This inertia is structural. Inertia inheres in a system that subordinates regulation of consumer financial markets to safety and soundness regulation. This system misses risks to orderly consumer markets because safety and soundness regulators have their eyes trained on risks to banks, not risks to consumers. It leads to neglect of the nonbank sector, where problems can and do emerge and spread to banks. And this system creates conflicts of interest that undermine the governments’ ability to maintain standards. Charter competition can lead prudential agencies to lower consumer standards; regulators can be slow to address practices that exploit consumer market inefficiencies such as lack of pricing transparency because these practices increase earnings – at least in the short term; and if earnings become too dependent on practices that exploit a lack of transparency, then bank supervisors have an incentive to forbear from addressing these practices and exposing their own failure to ensure stable capital and earnings. Each of these structural flaws was on display in the lead-up to the financial crisis, and none of them has been resolved.

Separating consumer market and bank prudential functions would help resolve these structural problems and, ultimately, strengthen safety and soundness. Separating functions will ensure someone is monitoring risks in consumer financial markets – the whole market, not just pieces of it. It will ensure that the federal government focuses substantially more resources on the nonbank sector so competitive pressures do not threaten bank soundness. And it will reduce and mitigate conflicts of interest that undermine government’s effectiveness and accountability.

A dedicated consumer financial regulator will help break the cycle of long periods of neglect followed by major changes in regulation on the downside of the credit cycle. It will provide banks and credit unions a more predictable regulatory environment, which will help provide them more stable earnings and more certainty upon which to build their businesses. In short, the CFPA will make banks and credit unions safer and sounder.

CONCLUSION

We are working on many fronts – jobs, housing, and financial stability – to promote a healthy economy now and for the long term. There is a necessary role for government to alleviate unnecessary suffering and set clear rules of the road for markets. To make sure government has accountability for providing those rules, we must make sure the right structures and incentives are in place. Our task is urgent. We must not delay. I hope you will join our efforts to support fair and efficient markets for families, end too big to fail, and provide our country a more secure financial future.

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