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At a hearing on

Financial Services and Products: The Role of the FTC in Protecting Consumers, Part II

Before the he U.S. Senate Committee on Commerce, Science, and Transportation

The Honorable John D. Rockefeller, IV
Chairman

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Chairman Rockefeller, Senator Hutchison, members of the committee. My name is Edmund Mierzwinski and I am Consumer Program Director for the Federation of State Public Interest Research Groups, or U.S. PIRG. The state PIRGs are non-partisan, non-profit public interest advocacy organizations that take on powerful interests on behalf of their members.

Among the key issues that the organization has focused on over the years is fairness in the financial services marketplace. We have published reports on skyrocketing bank fees, on inaccuracies in credit reports and other privacy threats, on credit card marketing to college students, on predatory payday loan and rent-to-own stores that seek self-serving exceptions from consumer protection and lending laws and on the need for strong reinvestment laws to ensure that heavily subsidized financial firms serve the interests of the local community. Throughout all these efforts we have urged Congress and federal regulators to enact and enforce strong federal laws but as a floor not ceiling of consumer protection so that states and their attorneys general can react quickly to new threats to their citizens and communities. We have also sought to preserve and enhance the rights of consumers to enforce those laws themselves.

Summary: U.S. PIRG strongly supports the proposed Consumer Financial Protection Agency (CFPA). We also support a robust Federal Trade Commission (FTC). The Obama administration's proposed Wall Street reform legislation, as enacted by the House in December,[1] effectively provides for both.

U.S. PIRG supports establishment of a new, independent federal Consumer Financial Protection Agency (CFPA) to protect consumers from unfair credit, banking, payment and debt management products, no matter what company – bank or non-bank -- sells them and no matter what agency may serve as the primary prudential regulator for that company or bank. Having one agency for all financial products will prevent regulatory arbitrage, promote efficient rulemaking and give consumers one-stop shopping for their financial complaints.

U.S. PIRG also supports enhancement of the authorities of the Federal Trade Commission (FTC). Even after Congress establishes a CFPA, the Federal Trade Commission will still maintain broad authority over important parts of the marketplace and will also act as the CFPA's enforcement partner in many areas. Its efforts to protect consumers will be enhanced if it is given greater ability to impose civil penalties, the ability to seek redress for aiding and abetting violations and modernized, more efficient rulemaking authority under the Administrative Procedures Act.[2]

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[1] The original administration CFPA and FTC improvement language was released on 30 June 2009 and is available at http://www.financialstability.gov/latest/tg189.html (last visited 15 March 2010). The Wall Street Reform and Consumer Protection Act, HR 4173, passed the House on 11 December 2009. See Section 4901. This week, Senator Chris Dodd, Chairman of the Senate Banking Committee, released his own comprehensive reform proposal, which does not appear, as filed, to address issues of expanding FTC authorities as discussed herein.

[2] With assistance from this committee, Congress has recently given the FTC expedited rulemaking authority in the areas of unfair practices related to mortgage loans. See Omnibus Appropriations Act of 2009, Pub. L. No. 111-8, § 626, 123 Stat. 524 (Mar. 11, 2009) as modified by the Credit CARD Act of 2009, Pub. L. No. 111-24, § 511(a)(1)&(2), 123 Stat. 1734 (May 22, 2009).

It is time to modernize the FTC's authorities so that it can respond to new threats to consumers and communities. Some of these threats – foreclosure relief and debt settlement scams and other frauds – are on the rise because the federal bank regulators allowed unsafe and unsustainable practices that led first to the failure of the financial system and then to the collapse of the economy. The FTC can play a critical role in protecting consumers from its aftermath and ensuring that it won't happen again.

We also support return to a system where federal financial protection law serves as a floor not as a ceiling and where consumers are again protected by the three-legged stool of baseline federal protection, strong state enforcement and private enforcement.

Discussion:

In our view, while the current economic crisis may have been directly caused by Federal Reserve inattention to the housing bubble that grew and then burst into flames -- as it was lit by the match of exotic, risky financial instruments used by reckless Wall Street firms deemed too big or too interconnected to fail -- the unregulated urge by banks, other lenders, and mortgage companies to extract even greater profits by selling predatory financial products acted as an accelerant to that fire. Those predatory products harmed consumers, families, neighborhoods and communities and helped make the mortgage meltdown into an economic catastrophe for consumers on Main Streets here and around the world.

Unfortunately, over the years the Congress in some cases and, in particular, the federal banking regulators in nearly all cases have opposed our views that consumers needed to be protected from unfair or predatory financial practices. For at least the last fifteen-twenty years, federal bank regulator disdain for consumer protection and antipathy toward state attorney general authority has contributed to an atmosphere that led to a spectacular rise in those predatory lending practices by banks, credit card firms and mortgage companies. At the same time, the resources and authorities of the FTC to act in the areas it was allowed to act in were constrained.

That rise in predatory lending was also fueled by regulatory arbitrage at the federal level that allowed banks to pick and choose the most pliant bank regulator for themselves and also their non-bank affiliates. That contributed to a regulatory race to the bottom. As the report of the House Energy and Commerce Committee on its passage of CFPA legislation explained:

> Consumer protection in the financial arena is governed by various agencies with different jurisdictions and regulatory approaches. This disparate regulatory system has been blamed in part for the lack of aggressive enforcement against abusive and predatory loan products that contributed to the financial crisis, such as subprime and nontraditional mortgages.

> FTC has broad authority to protect consumers from unfair, deceptive, and unlawful practices with respect to credit and debt. The authority of the FTC is limited, however, to those functions conducted by non-depository institutions. Depository institutions are overseen by the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the Federal Reserve, the National Credit Union Administration, and the Federal Deposit Insurance Corporation.[3]

Consumer financial products which compete directly against one another are often covered by different laws and thus provide different rights and obligations to the consumer and to the provider. Although many new products are emerging every day, no agency has the single job of evaluating whether or how existing laws and rules should be changed to address emerging financial products. Worse, those bank regulatory agencies have a different, primary job — protecting the safety of the financial system. The new CFPA will have the single job of protecting financial consumers. Even the FTC, a strong consumer protector, has many other jobs.

The idea of a new federal consumer protection agency focused on credit and payment products has gained broad and high-profile support because it targets the most significant underlying causes of the massive regulatory failures that occurred. First, federal agencies did not make protecting consumers their top priority and, in fact, seemed to compete against each other to keep standards low, ignoring many festering problems that grew worse over time. If agencies did act to protect consumers (and they often did not), the process was cumbersome and time-consuming. As a result, agencies did not act to stop some abusive lending practices until it was too late. Finally, regulators were not truly independent of the influence of the financial institutions they regulated.

The New CFPA Needs a Stronger FTC As A Partner

Congress can eliminate these weaknesses and inefficiencies in the federal government by creating a single federal agency – the CFPA -- with exclusive authority in all consumer protection areas except enforcement. In the area of enforcement, the CFPA should be assisted by a bolstered FTC. The FTC also needs the strengthened authorities to continue its efforts in areas where it remains the primary enforcer in the consumer marketplace.

Establishing a new CFPA – while also enhancing the FTC's enforcement authority -- will remedy many of the inherent flaws in the current system. We believe that as enacted by the House, the Wall Street Reform and Consumer Protection Act, HR 4173, offers an approach that the Senate should consider taking.

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[3] 111the Congress, Rept. 111-367, House of Representatives, at page 91, 9 December 2009.

It establishes a new CFPA as an independent agency[4] to write rules for all financial products (subject to a few carved-out exceptions) over the entire financial sector, so that no matter where a consumer buys a financial product, at a bank or a non-bank, she has equal protection. But the House bill also improved the Obama proposal because it carefully preserves the FTC as an enforcement partner of the CFPA while eliminating some of the original bill's consultative and procedural impediments that may have hampered both agencies. At the same time, the House-passed bill significantly improves FTC's existing authorities. It also retains FTC authority under the FTC Act and the FTC's enforcement authority under the enumerated statutes, concurrently and in coordination with the CFPA.

As Professor Prentiss Cox has explained, it makes sense to consolidate rulemaking in the new agency but to allow for broad enforcement authority under an "open" model, with the FTC – and state Attorneys General -- as partners.

> Enforcement of consumer protection laws and rule-making for consumer protection are different activities that require different models to be effective. Unified rule-making authority in an agency dedicated to consumer protection goals presents an extraordinary opportunity to reform the consumer finance system to ensure products and sales practices that meet minimum standards of fairness for consumers. Public enforcement, on the other hand, is best accomplished in an open model; a system that allows multiple public entities the opportunity to gauge compliance.[5]

But in addition, as this committee recognized when it recently used the Appropriations process to enact reforms championed by Senator Dorgan and Chairman Rockefeller to the FTC's rulewriting authority over mortgage loans,[6] the FTC has had only limited weapons in its arsenal against corporate wrongdoing. These shackles and constraints – most enacted in the 1970s – must be removed if the FTC is to be expected to do its job in the 21st century.

Recommendations for the Committee to Improve the FTC's Authorities:

The House-passed bill, HR 4173, the Wall Street Reform and Consumer Protection Act, makes the following changes to strengthen FTC authorities as recommended by President Obama's blueprint for financial reform. We support the House approach and urge the committee to work with Chairman Dodd and Senator Shelby, at an appropriate time, to add these provisions to the Wall Street reform package before it is finalized.

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[4] The final Senate CFPA proposal may be weaker, however. Senator Dodd's draft this week places the CFPA inside the Federal Reserve Board as a bureau – although maintaining some independence through firewalls -- and subjects its rules to a veto of 2/3rd of the proposed new Systemic Risk Council. Although the Senate proposal as introduced places all four corners of the financial sector – big banks, small banks, mortgage companies and other non-bank lenders – under CFPA's rules, the CFPA does not have full enforcement authority over non-mortgage, non-banks, making it even more imperative that FTC authorities be bolstered, since the non-bank lenders not fully covered will include predatory payday lenders, rent-to-own stores, auto title pawn loan firms and their ilk.

[5] Testimony of Prentiss Cox, University of Minnesota Law School, "The Proposed Consumer Financial Protection Agency: Implications for Consumers and the FTC," Hearing of the Subcommittee on Commerce, Trade and Consumer Protection, U.S. House of Representatives, 08 July 2009.

[6] See Omnibus Appropriations Act of 2009, Pub. L. No. 111-8, § 626, 123 Stat. 524 (Mar. 11, 2009) as modified by the Credit CARD Act of 2009, Pub. L. No. 111-24, § 511(a)(1)&(2), 123 Stat. 1734 (May 22, 2009).

First, the Obama proposal as enacted in the House passed bill changes the FTC's cumbersome Magnuson Moss rulemaking process to the more prevalent Administrative Procedures Act (APA) rulemaking process used by other agencies. In his recent testimony to this committee, FTC Chairman Jon Leibowitz called Magnuson-Moss rulemaking both "draconian" and "medieval." He was not being redundant.[7] As many have noted, the FTC's inability to swiftly enact predatory mortgage lending rules was a contributor to the mortgage meltdown. From testimony before the committee by a leading expert, Kathleen Keest, a former state assistant attorney general:

> Though the FTC has authority to enforce the Truth in Lending Act and the Equal Credit Opportunity Act, among others, the nature of the recent abuses were such that its UDAP authority was the primary weapon available to it. However, the FTC's ability to wield that weapon is governed by rules of engagement which make it difficult to prevent abuses.[…] *Rule-making: The FTC's "Mag-Moss" Albatross…*[8]

Those UDAP (Unfair and Deceptive Acts and Practices) authorities were limited, as noted, by the "albatross" of the Magnuson-Moss rulemaking provisions. As noted above, the Congress has already extended APA rulemaking authority for "unfair or deceptive acts or practices regarding mortgage loans, which may include unfair or deceptive acts or practices involving loan modification and foreclosure rescue services." We recommend, however, that the APA rule-making be granted to the FTC in all its consumer protection roles, as provided by the House bill.

Second, the Obama proposal as enacted in the House passed bill gives the FTC the right to sanction professionals aiding and abetting illegal schemes by others. U.S. PIRG has long supported improving aiding and abetting statutes to better protect consumers. It is highly likely that many schemes designed to extract wealth from consumer pocketbooks involve lawyers, accountants, bankers and others advising the seller. Clarifying aiding and abetting liability will help assure that all those involved in the scheme or the scam can be reached by the law.[9] Our goal is not to reach deep pockets, as opponents will assert, it is to deter fraud by requiring well-compensated professionals to pay attention and to be held accountable when they do not.

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[7] Testimony of FTC Chairman Jon Leibowitz, "Financial Services and Products: The Role of the Federal Trade Commission in Protecting Consumers," Hearings of the Senate Committee on Commerce, Science and Transportation, (oral statement), 4 February 2010.

[8] Testimony of Center for Responsible Lending, by Kathleen E. Keest, Hearing Before the Senate Committee on Commerce, Science and Transportation, Subcommittee on Interstate Commerce, Trade and Tourism 0n "Improving Consumer Protections in Subprime Home Lending" April 29, 2008

[9] In 1994, the Supreme Court eliminated the Securities and Exchange Commission's aiding and abetting authority under the Exchange Act in *Central Bank of Denver v. First Interstate Bank of Denver,* 511 U.S. 164. U.S. PIRG was an (unsuccessful) friend of the court in the case. It had been the widely held view that the FTC had a similar cause of action under Section 5 of the FTC Act for aiding and abetting unfair or deceptive acts and practices. While the Congress in the (otherwise dreadful for small investors) 1995 Private Securities Litigation Reform Act (Public Law 104-369) reinstated the SEC's aiding and abetting authority for knowing violations it has not reinstated the FTC's implied authority. Regrettably PSLRA also did not reinstate a similar previous implied private right of action for aggrieved investors under the Exchange Act. See also: Prepared statement of the Federal Trade Commission on "Financial Services and Products: The Role of the Federal Trade Commission in Protecting Consumers," Hearing of the Senate Committee on Commerce, Science and Transportation, 4 February 2010, at footnote 43.

Third, the Obama proposal as enacted in the House passed bill give the FTC the authority to impose civil penalties for violations of the FTC Act. Currently, a firm that violates the FTC's core enforcement mechanism - Section 5's prohibition on unfair and deceptive acts and practices -- gets a free bite of the apple. The inability of the FTC to impose civil penalties for first offenses limits its ability to police the marketplace. Unless a firm violates a trade rule that the FTC enforces, such as the Fair Credit Reporting Act, or violates an existing consent decree or order, the FTC cannot impose civil penalties. This lack of a credible threat of punishment is an inadequate deterrent against wrongdoing. The proposals also wisely eliminate onerous requirements requiring the FTC to ask permission of the Department of Justice – and to give it a 45-day right of first refusal -- before bringing a civil case involving civil penalties.

Finally, we would also support establishing a private enforcement right for consumers under Section 5 of the FTC Act and also under the new CFPA Act. Congress should provide a private right of action to enable consumers to enforce their own right to be free of unfair and deceptive acts and practices, for neither the FTC's nor the CFPA's resources will ever be adequate to police the entire market, and public enforcement will never move fast enough to protect them.

Conclusion

We appreciate the opportunity to testify before you today on the important matter of reinvigorating the FTC's authorities to protect the public and police the marketplace at the same time as the Congress establishes a new, Consumer Financial Protection Agency.