



Consumer, Industry, and Government Leaders Debate Financial Policy

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More than 250 consumer advocates, government representatives, and industry officials from across the country came to Washington, DC on December 3rd and 4th, 2009 to participate in the Consumer Federation of America's 21st annual Financial Services Conference. The conference covered many issues but focused primarily on three areas — consumer finance, securities and derivatives regulation, and home mortgages.

On consumer finance, the proposal to create a Consumer Financial Protection Agency was a focal point of discussion. Senator Jeff Merkley (D-OR) explained the rationale for the proposed Agency as follows: "As important as the Credit Card Act was, it is not the right answer for consumer protection. We cannot say there are tricks and traps in the system we are going to legislate on those individual tricks and traps. We need to have the ability in real time to respond to tricks and traps ... that is why the Consumer Financial Protection Agency (CPFA) is so important." Travis Plunkett, Legislative Director for the Consumer Federation of America, highlighted the present policy fragmentation that the CPFA bill aims to correct, "Right now, there are seven agencies that enforce 20 consumer protection laws." Plunkett said.

A debate on the merits was held, with Georgetown Law Professor Adam Levitin arguing in favor of the Consumer Financial Protection Agency and Chris Stinebert, President and CEO of the American Financial Services Association, in opposition. For Stinebert, "the most frightening part" of creating a Consumer Financial Protection Agency is that, "It does not have any boundaries or limits. It will create an agency that will be here 100 years from now based on a single process of consumer protection. It is basically wide open to interpretation of whatever that agency decides to do. At the cornerstone of our concerns is the uncertainty this creates." Levitin countered that, "Concern for unintended consequence is a bit of a false issue. It is not just regulation that has unintended consequences. It is markets that have unintended consequences. Otherwise we would have to conclude that the intended consequence of deregulation was this financial crisis." More positively, Levitin argued that a Consumer Financial Protection Agency, by setting clear rules and limiting the number of financing options could help convert consumer finance into an industry where consumers could more easily comparison-shop, driving prices down. "That is not the financial services industry that we know and love," Levitin sardonically noted. Effective consumer protection, he added, "might get the market right and make it more efficient."

On securities, Mary Schapiro, Chair of the U.S. Securities and Exchange Commission, led off the discussion. On the regulatory front, Schapiro emphasized three themes: 1) developing a "fiduciary" standard to anyone who sells securities regardless of whether that person is an "investment advisor" or a "broker-dealer"; 2) reduction of automatically deducted mutual fund

fees (the so-called 12b-1 fees); and 3) better funding for the SEC to ensure compliance. Schapiro noted that presently an “investor on Main Street has about a 10-percent chance of walking into an investment adviser who has been inspected by the SEC in the previous year.”

Schapiro also argued for legislation to create oversight and transparency for derivatives that would be at least equal to what would “apply to any other over-the-counter security.” Obama Administration official Gary Gensler seconded Schapiro on this point. Gensler, Chairman of the U.S. Commodity Futures Trading Commission, argued, “I spent 18 years on Wall Street. I believe the industry plays a fundamental role in pricing and risk. It doesn’t mean they don’t sometimes get things wrong. It doesn’t mean the system as organized is flawless. I believe the system right now does not have this very critical market in a transparent venue ... The most comprehensive crisis in 80 years requires a systemic response.”

Michael Barr, Assistant Secretary in the Treasury Department, in his remarks emphasized regulatory holes in the mortgage market. “Today,” Barr noted, “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.” The Consumer Financial Protection Agency, Barr argued, “will cover mortgage brokers, mortgage companies, finance companies, payday lenders, and banks.”

Two panels examined the mortgage market in further detail. The first looked at efforts to stem foreclosures. Thomas Lawler, Assistant Director in the Office of Homeownership Preservation at the U.S. Department of Treasury, conceded that the Obama administration’s efforts at loan modification have had disappointing results. While participation in 3-month “trial” modifications has been high, conversion to permanent loan modifications has been low. As Lawler noted, “On average, [with trial modifications] borrowers save \$640 a month. That’s the good news. The challenge is that the conversion rate [to permanent loans] is very low ... in the low tens of thousands ... we are disappointed in that number. We think it should be closer to 375,000.”

Faith Schwartz, Executive Director of the Hope Now Alliance, a nonprofit organization that has helped 2.5 million avoid foreclosure through loan modifications, recognized that even as workouts exceed foreclosure sales, the tide of foreclosure has not peaked and that instead “foreclosure starts are escalating.” Deborah Goldberg, Director of the Hurricane Relief Project at the National Fair Housing Alliance, pointed out that the context has been “stunning in a bad way” with foreclosure “coming in waves: The first wave was subprime. The second wave has been the option ARMs. The third wave is the unemployment. And there may be a fourth wave in the FHA market.” The crisis, she added, “has fallen disproportionately on people of color.” Goldberg argued that, “It is time to revisit the issue of bankruptcy reform and give judges the ability to modify mortgages. Without that leverage, without that stick that goes along with the carrots ... servicers don’t have enough incentive to get people into loan modifications.”

A second panel examined the broader issue of regulation going forward. Mike Calhoun, President of the Center for Responsible Lending, an affiliate of the community development financial institution Self-Help, expressed concern regarding the gap between rhetoric and action. “We have seen the greatest financial crisis since the Great Depression,” Calhoun noted, “and we

have been unable to enact mortgage standards to address the crisis.” By contrast, John Courson, President and CEO of the Mortgage Bankers Association, urged measured reform, “We have to be careful to not overreact,” Courson cautioned. “The last thing we want to do is to stifle competition and put fences around innovation ... From a lender standpoint, we have to take the responsibility to make sure the product is transparent — and there does need to be accountability.” In particular, Courson argued against separating “prudential [safety and soundness] regulation from consumer protection regulation.” Calhoun countered that this would dilute consumer protections and pointed out that the principle of separation between industry regulation and consumer protection is not new. The government, Calhoun noted, “does not have “environmental protection embedded in the Department of Commerce.”

Calhoun also highlighted another issue, namely that loans made by Self-Help had performed well, even in the midst of the financial crisis. “Our borrowers have performed almost as well as prime fixed-rate borrowers and better than prime ARM borrowers. These were junk mortgages, not junk borrowers,” Calhoun emphasized. Kathleen Ryan, Senior Counsel for Consumer & Community Affairs at the Federal Reserve and Ira Rheingold, Executive Director of the National Association of Consumer Advocates both highlighted the importance of mandating “all in” (inclusive of all fees) annual percentage rate (APR) measures to help consumers more effectively compare mortgages and avoid hidden fees.

For more information on the Consumer Federation of America, see: www.consumerfed.org.