United States House of Representatives

Committee on Financial Services

Subcommittee on Financial Institutions
and Consumer Credit

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Hearing entitled:

"Examining Regulatory Burdens on
Non-Depository Financial Institutions"

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Statement of Justin G. Friedman

American Financial Services Association

Chairman Neugebauer, Ranking Member Clay and Members of the Subcommittee:

Good Afternoon. My name is Justin Friedman and I direct government affairs for the American Financial Services Association or AFSA, the nation's oldest consumer credit association which is celebrating its 99th anniversary in 2015. I am pleased to be here today to provide testimony to the Subcommittee as it examines regulatory relief for non-depository financial institutions and to discuss proposals to improve the structure of the Consumer Financial Protection Bureau ("CFPB" or "Bureau"). We wish to thank Chairman Neugebauer and Ranking Member Clay for holding a hearing on this issue, which is of keen importance to the consumer credit industry and the households we serve.

Statement of Interest

Founded in 1916, AFSA is the national trade association for the consumer credit industry, protecting access to credit and consumer choice. The association encourages and maintains ethical business practices and supports financial education for consumers of all ages. AFSA has provided services to its members for nearly a century. Our 390 member companies include consumer and commercial finance companies, motor vehicle finance companies including the captives of the automakers, card issuers, mortgage lenders, industrial banks, and other financial services companies that make credit available to consumers and small businesses.

AFSA member companies offer a broad array of financial products, including personal installment loans, retail and commercial sales finance, credit and payment cards, residential mortgages, vehicle loans and leases, and floorplan finance for dealers. Our members provide approximately 80 percent of the nation's vehicle financing. In general, finance companies are responsible for one of every five dollars of consumer credit.[1]

Consumer Finance Companies Serve a Broad and Important Market

While depository institutions play a vital role in the economy and the consumer credit market, Federal Reserve Board statistics show that a substantial share of non-mortgage consumer credit is provided by finance companies and others who raise funds through securitization. In fact, for non-revolving lines of credit, finance companies and banks hold roughly equal shares of the overall pie – about one quarter each. Both are smaller than the share held by the federal government, which of course dominates the student loan market.

Finance companies have a long history of meeting the credit needs of consumers – from buying a car to get to work, to paying college costs for a son or daughter. Finance companies are licensed by each and every state where they do business, so the CFPB has added a complex new layer of federal oversight to our members' existing regulatory regime.

The principal types of credit offered by consumer finance companies are motor vehicle finance and traditional installment loans.

[1] Federal Reserve Board, G.19 Report on Consumer Credit Outstanding (February 2015)

While much has been written and said about the abuses found in certain forms of short-term, small-dollar lending, policymakers should recognize that traditional installment loans are a time-tested and beneficial form of credit for working Americans. I am talking about fixed-rate, fully-amortizing personal loans, which are repaid in equal monthly installments of principal and interest. Traditional installment loans are the safest, most responsible form of small-dollar lending and have been for many decades.

The average loan is for $1500, the average monthly payment is $120, and the average term is 15 months. These are “plain vanilla” loans with transparent, easy-to-understand terms, due dates and payment amounts. Installment lenders report payment behavior to credit bureaus, which helps consumers to build or repair their credit history.

Borrowers commonly use these loans for vehicle repairs, to purchase household appliances and cover unexpected medical expenses – the everyday items and services essential to living a productive and enjoyable life.

AFSA members make automobile financing available directly through branch-based lending and indirectly through dealerships. Their provision of credit helps keep the automotive market a strong, competitive and integral part of the American economy.

While our industry is focused on providing a positive experience for the consumer, it also provides a reliable source of liquidity for auto dealers. Specialized auto lenders do not withdraw from the market during economic downturns, unlike banks that have safety and soundness concerns which may compel them to curb auto lending during times of turbulence.

The Role of State Regulators in Overseeing Non-Depositories

The trope that non-depository lenders are “unregulated” is simply untrue. Like the insurance industry, non-depository institutions were simply regulated by someone else. The states have regulated installment lenders since 1880 – 33 years before the passage of the Federal Reserve Act, 53 years before the passage of the Federal Deposit Insurance Act, and 130 years before the creation of the CFPB.

The framework of modern consumer lending stems from the passage of the Uniform Small Loan Law, first enacted in California in 1909, and eventually throughout the country. The Uniform Law Commission first promulgated the Uniform Consumer Credit Code in 1968 to provide for comprehensive regulation of consumer credit by the states.

The National Association of Consumer Credit Administrators (NACCA) was formed in 1935 to build the capacity of state regulators of consumer credit and to facilitate the administration of laws governing these agencies. It continues to do so today.

The creation of the CFPB imposes new, often duplicative, federal regulatory burdens on these state-regulated entities.

State regulators have a familiarity with local and regional circumstances and issues faced by lenders. This knowledge, along with their geographic proximity to a given lender and the markets in which it operates, means that a state regulator is often the first to identify emerging issues, practices or products that may need further investigation or may pose additional risk to the financial industry and its customers.

Currently, the CFPB may promulgate regulations impacting state-licensed companies without:

- Finding that existing state law or regulation is inadequate;
- Determining an estimate of the number of state-licensed or supervised entities to which the regulation will apply;
- Describing the projected reporting, recordkeeping and other compliance requirements; or
- Identifying the relevant state statutes, regulations and enforcement proceedings with which the new federal regulation may duplicate, overlap or conflict.

No one size fits all. Credit needs, average income and demographics vary from state to state. A given state legislature may choose to allow a product or tolerate a pricing regime of which another state does not approve. Where it comes to state-licensed consumer finance companies, we believe that decision is best left to each state capital to decide what is beneficial to their constituents.

Thomas Jefferson put it best: "Our country is too large to have all its affairs directed by a single government. Public servants at such a distance, and from under the eye of their constituents, must, from the circumstance of distance, be unable to administer and overlook all the details necessary for the good government of the citizens; and the same circumstance, by rendering detection impossible to their constituents, will invite public agents to corruption, plunder and waste."[2]

Supervisory Privilege

On behalf of AFSA's member companies, I wish to thank the Committee for its help in enacting H.R. 5062, the Examination and Supervisory Privilege Parity Act of 2014, legislation that clarified the sharing of information between federal and state agencies that license, supervise or examine nonbanks offering consumer financial products or services.

This legislation resolved a regulatory disparity between depository and non-depository institutions, recognizing the unique situation of non-depositories and their relationships with state regulators. We are pleased that the legislation was introduced and passed in a bipartisan manner.

AFSA hopes that this effort can serve as a model for future proposals to reform the CFPB.

[2] Thomas Jefferson to Gideon Granger, 1800. The Writings of Thomas Jefferson, (Memorial Edition) Lipscomb and Bergh, editors. 10:167

A Review of the CFPB's Governance

AFSA believes that the CFPB's current governance structure is flawed and it should be replaced by a bipartisan, multi-member commission – as is the norm for virtually all independent regulatory agencies of the federal government.

The CFPB's mandate is to regulate the offering and provision of consumer financial products or services and enforce the Federal consumer financial laws.

Unlike most independent regulators, the Bureau is not governed by a bipartisan board. This has been the model for more than a half century for federal agencies that have consumer protection responsibilities (*e.g.* the Federal Reserve Board, Federal Deposit Insurance Corporation, Federal Trade Commission, Consumer Product Safety Commission, Securities and Exchange Commission, and the Commodity Futures Trading Commission). The CFPB is headed by a single political appointee.

Although nominally housed within the Federal Reserve, the Federal Reserve Board of Governors cannot direct activities, terminate staff or review regulatory or enforcement activities. Unlike the traditional independent agency model, the CFPB is guaranteed a percentage of the Federal Reserve Board's budget, depriving Congress of fiscal oversight through the annual appropriations process.

Once a Director of the CFPB is confirmed by the Senate, even the President of the United States has no effective control over the position other than termination for cause.[3] In contrast, the norm among independent agencies structured as commissions is that a new President may designate his or her choice of a chairman.

The Structure of the CFPB should be Reformed

AFSA congratulates the Financial Services Committee on passing 11 bipartisan regulatory relief bills in March. We believe that H.R. 1195, the Bureau of Consumer Financial Protection Advisory Boards Act, will help small business. AFSA also welcomes Chairman Neugebauer's introduction of H.R. 1266, the Financial Product Safety Commission Act of 2015, which alters the CFPB structure to a bipartisan, five-member commission appointed by the President.

Twice before, the House has wrestled with the CFPB single director structure. In the 112th Congress, H.R. 1121, the Responsible Consumer Financial Protection Regulations Act of 2011, was reported by the Committee. In the 113th Congress, the House passed H.R. 2446, the Responsible Consumer Financial Protection Regulations Act of 2013, which would have amended the Dodd-Frank Act to replace the CFPB Director with a five-person commission – one of whom would be the Federal Reserve's Vice Chairman for Supervision, lending necessary experience in bank regulation, plus four other members who "have strong competencies and experiences related to consumer financial protection."

[3] The Dodd-Frank Act even provides that congressional testimony by the Bureau's Director must provide a regulatory Miranda Warning that it does not necessarily represent the views of the President, and the President is prohibited from reviewing any legislative recommendations or comments the CFPB may submit.

While we believe this was a step forward, the previous bills did not address state-licensed entities and the substantial portion of the consumer credit market they serve. As noted above, state regulators are closest to these markets and possess important insight into the practices or products of the lenders they license. State regulators are best positioned to investigate issues that may pose risks to local consumers.

AFSA recommends that at least one member of any CFPB board should have state bank or consumer credit supervisory experience. A similar approach has worked effectively at the Federal Deposit Insurance Corporation and would be appropriate for the CFPB. We believe the unique qualities of credit unions and state-chartered banks require similar representation.

Thus, the new commission could be composed of the Federal Reserve's Vice Chairman for Supervision; a member with non-depository consumer credit supervisory experience; a member with state bank supervisory experience; a member with credit union supervisory experience and a public member possessing strong competencies related to consumer financial protection.

Some fear that any structural reform would harm the mission of the CFPB, but AFSA believes the converse to be true. An agency directed by a commission with a bipartisan membership is better insulated from electoral politics, and most likely to produce sustainable public policy that will protect consumers while promoting access to credit.

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AFSA and its member companies welcome the opportunity to work with Congress as it addresses these important issues.

Appendix: AFSA Members' Customers Value their Services

It is easy for policymakers to become detached from the lives of individual consumers, and to forget that legislative and regulatory initiatives have intended and unintended consequences impacting the people they are intended to protect. For this reason, AFSA believes the following narratives from our customers merit sharing:

> *[AFSA member company] offered me a loan after I had been turned down by other companies and banks. They worked with me to allow me to extend my loan during a period when I was having difficulty paying my bills. We need more companies that are willing to take risks on people with less than perfect credit scores. For them, I am personally grateful.* — Joyce from Marion, Iowa

> *[I was] coming from a small town of Mississippi, for a new beginning [and I was] in need of a dependable ride. With little money on hand, [a] number of places turn me down for a loan, and the Repos I looked at was [sic] just not worth driving off the lot. Two weeks pass by [and then] on TV I saw [AFSA member company]. The very next day, by the end of the day, I was happy riding [sic]and [had] cash in my purse. Thank you [AFSA member company for blessing me.* — JoAnn from Mississippi

> *As my medical bills and other bills were piling up, I just couldn't keep up. The installment loan that I qualified for at [AFSA member company] …helped me get back on my feet. Thank you to [the company]!* — Tim from Cedar Rapids, Iowa

> *Being a single mom can be a challenge. I've worked hard for six years to provide my daughter [with] the very best, but with just a single income, no child support, and no family, things can get tough. When I approached the bank for a loan, I was turned away and referred to [AFSA member]. They have helped me in so many ways.* — Te from Marion, Iowa

> *Several years ago, we purchased a new home on contract in a great neighborhood and school district. My wife and I both had secure jobs of 15 years, but we had been through some challenging times and had to file [for] bankruptcy. In the contract we had one year to secure our own financing. Everywhere we went we were told we had to be out of bankruptcy for two years before we would be eligible for a new mortgage loan. When the first year ended, the contract owner called the contract due. We were so afraid that we would lose our home. Then we found [AFSA member company]. They took our application, analyzed our circumstances and said they could help. [AFSA member company] financed the balance of our contract and told us that when our bankruptcy was at least two years old we could look at refinancing the loan with no penalty. We were able to save our home and pay off the contract owner.* — Customer from Long Grove, Iowa

> *"We have had numerous loans with [AFSA member company] over several years. Our experience with [AFSA member company] has been both pleasant and rewarding. The personnel there has always been courteous and efficient. We chose a traditional*

installment loan because it suited our needs as far as being quick to close with no long waiting period for approval and time-consuming paperwork prior to the closing. The traditional installment loans have helped us reach our financial goals in business and our personal finances. We could not have received the financing we needed as quickly as we needed it with any other loan process. — Ronnie from Purvis, Mississippi