



U.S. House of Representatives
Committee on Financial Services
Subcommittee on Financial Institutions
and Consumer Credit

*

Hearing:

“Examining Regulatory Relief Proposals for Community
Financial Institutions, Part II”

Tuesday, July 15, 2014

*

Statement of the
American Financial Services Association

Re: H.R. 5062, the “Examination and Supervisory
Privilege Parity Act”

About AFSA

Founded in 1916, the American Financial Services Association (AFSA) is the national trade association for the consumer credit industry, protecting access to credit and consumer choice. Our 350 members include consumer and commercial finance companies, auto finance and leasing companies, credit card issuers, industrial banks and industry suppliers. Prior to enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) in 2010, AFSA members were always responsible for adhering to the federal consumer statutes and regulations, but most were exclusively licensed and examined by the states in which they conducted business. Today, as covered persons pursuant to the Dodd-Frank Act, they are subject to the full jurisdiction of the Consumer Financial Protection Bureau (CFPB or Bureau).

Statement of Interest

AFSA represents banks as well as captive finance companies, sales finance companies and retail installment sales finance companies. These consumer finance companies – many of which are small local or regional businesses – are licensed and supervised by state banking agencies or consumer credit authorities. Unlike banks or credit unions, their extensions of credit are funded by placing their own capital at risk, rather than through insured deposits.

This statement will focus on the matter of supervisory privilege, and specifically the “Examination and Supervisory Privilege Parity Act” (H.R. 5062), introduced on July 10, 2014, by Reps. Perlmutter and Barr.

Consumer Finance Companies and the CFPB

The Dodd-Frank Act of 2010 established the CFPB to regulate and supervise both banks and nonbank financial institutions engaged in the offering of consumer financial products or services. As a result, consumer finance companies find themselves subject to a new layer of federal supervision and enforcement for the first time. In general, AFSA urges Congress and the CFPB to seek a balance between consumer protections and the desire to maintain access to and the affordability of credit for consumers. One key way to promote this balance is by protecting the privilege and confidentiality of any nonpublic, proprietary information disclosed to the CFPB and other regulators by or about the financial institutions under their jurisdiction.

Background on Supervisory Privilege

A strong supervisory privilege plays an important role in supporting an effective and open examination process. Straightforward communications between regulators and the regulated entities are critical, and are made possible by the maintenance of privilege. There is precedent for this degree of protection in the longtime practice by bank regulators of asserting the confidentiality of records related to entities under their supervision. When challenged, the courts have upheld this confidence. In 1992, the U.S. Court of Appeals for the D.C. Circuit sustained the assertion of privilege by the Federal Reserve Board and Office of the Comptroller of the Currency in denying the discovery of confidential supervisory information related to a national

bank. In its opinion, the court discussed the justification for bank examination privilege as follows:¹

Bank safety and soundness supervision is an iterative process of comment by the regulators and response by the bank. The success of the supervision therefore depends vitally upon the quality of communication between the regulated banking firm and the bank regulatory agency. This relationship is both extensive and informal. It is extensive in that bank examiners concern themselves with all manner of a bank's affairs... Because bank supervision is relatively informal and more or less continuous, so too must be the flow of communication between the bank and the regulatory agency. Bank management must be open and forthcoming in response to the inquiries of bank examiners, and the examiners must in turn be frank in expressing their concerns about the bank. *These conditions simply could not be met as well if communications between the bank and its regulators were not privileged.* (emphasis added)

CFPB Seeks Access to Confidential Information

During testimony before the Financial Services Committee on July 19, 2012, CFPB Deputy Director Raj Date stated, "Supervision depends on confidential information being shared with regulators, full stop. You cannot create a supervisory relationship that is going to be meaningful additive to the system unless institutions can count on that..." He asserted that access to confidential information is important to enabling an effective supervisory regime, and that the CFPB would therefore insist that confidential information be shared by institutions under its jurisdiction. Mr. Date acknowledged that to the extent any doubt remains about whether surrendering such information could waive any attorney-client privilege, "then statutory remedy is something, as Director Cordray has pointed out, something that we would welcome."²

Status of the Nonpublic, Proprietary Information of Nonbanks

In establishing the CFPB, Congress neglected to extend bank supervisors' historical protections over privileged information to either the CFPB or the state regulators of nonbanks, with whom the Bureau is expected to share information and coordinate examinations. Therefore, the proprietary information of nonbank consumer finance companies does not enjoy the same legal protections as that of banks when disclosed during the course of supervision or other regulatory processes.

Recognizing the importance of promoting effective supervision, Congress enacted H.R. 4014 in December 2012 to protect privileged information disclosed to the CFPB by covered persons. H.R. 4014 amended the Federal Deposit Insurance Act (FDI Act) to add the CFPB to the list of federal regulators with whom no applicable privilege is waived when disclosing privileged information by or about a company under supervision. The FDI Act also permits enumerated agencies to share such privileged information with "state bank supervisors" without waiving the privilege. However, in the case of a nonbank institution, federal law currently provides

¹ In re Subpoena Served upon Comptroller of Currency, 967 F.2d 630, 633–34 (D.C. Cir. 1992)

² Hearing on "The Impact of Dodd-Frank on Consumer Choice and Access to Credit." U.S. House Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit. 19 July 2012.

comprehensive protection of existing privilege *if and only if* the company does business exclusively in states where it is regulated by state bank supervisors, per se.

Current Law Provides Uneven Protections for Nonbanks

Across the country, nonbank consumer finance companies do not always fall under the jurisdiction of state bank supervisors. This exposes such entities to significant legal risk, given the uncertainty surrounding whether privilege will withstand the transfer of information by the Bureau to, and among, state agencies not specifically referenced in federal law. Such uncertainty will necessarily chill communications between the CFPB and the companies it supervises, undermining the agency's effectiveness.

According to an informal survey conducted by AFSA, there are at least 15 states where an agency other than the state bank supervisor currently has either partial or full jurisdiction over nonbanks offering consumer credit in that state. For example, the Office of the Consumer Credit Commissioner in Texas and Colorado's Attorney General each oversee nonbank consumer finance companies in their respective states. Furthermore, state governments periodically reorganize their regulatory regimes – raising the issue of whether a nonbank currently under a given state's banking agency would be protected if that state alters its regulatory jurisdiction in the future.

With the CFPB conducting examinations of state-regulated nondepository financial institutions, it is imperative for Congress to extend all applicable privileges to the range of institutions subject to supervision by the Bureau. Congress should ensure that the same protections apply to all consumer creditors to ensure an effective and equitable examination and investigatory process.

AFSA Supports H.R. 5062

The "Examination and Supervisory Privilege Parity Act" (H.R. 5062) would amend the Consumer Financial Protection Act of 2010 to specify that privilege is maintained when information is shared by certain nondepository covered persons with federal and state financial regulators. AFSA believes this bill will achieve parity in the statutory treatment of nonpublic, proprietary information disclosed by nondepository financial institutions with that of their depository peers, and will thereby promote greater candor with regulators and more efficient regulation. As some state laws and regulations use the terms "privileged" and "confidential" interchangeably with regard to the treatment of nonpublic, proprietary information, Congress may wish to consider broadening the scope of this bill to reflect that fact. In any case, AFSA urges Congress to advance this legislation at the soonest possible opportunity, as covered persons face greater risk to the sanctity of their proprietary information as they disclose more documents to the CFPB with each passing day.

*

AFSA thanks the Financial Services Committee for the opportunity to provide a statement on this issue. If you have any questions, please contact AFSA's Executive Vice President, Bill Himpler, at 202-466-8616 or bhimpler@afsamail.org.