

## **Consumer Financial Protection in California**

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Thank you for inviting me to testify today. My name is Richard Cordray, and I had the honor to serve as the founding Director of the U.S. Consumer Financial Protection Bureau for its first six years. My testimony concerns how California can take the initiative to protect consumers in the financial marketplace at a time when the Federal government is retreating from this area. It will touch on theories of financial regulation; the purpose, role, and current status of the CFPB; how federalism affects consumer finance; and the rationale for California to step up and enhance its own capability to protect consumers. California has always prided itself on being a leader in looking out for consumers, and it has the chance to do so again here.

Financial regulation is enormously important for consumers, who often feel frustrated and mistreated in the financial marketplace. The problems they face at a personal level are magnified throughout the economy. The last two generations have seen an explosion of consumer debt, which has risen from about \$1,000 per person to more than \$40,000 per person today. The mass availability of consumer credit has created new opportunities for people but also increases the risks they face, and the risks to our economy. Exotic lending in the mortgage market brought down the entire American economy in 2008, costing millions of jobs, millions of homes, and trillions in lost retirement savings. The regulators lacked the tools to monitor the consumer markets effectively and missed the tell-tale signs. In the end, they were too late to stop the financial crisis from turning into the Great Recession.

In the wake of that catastrophe, which turned out to be worldwide in scope, a chorus of experts called for an overhaul of financial regulation. They converged on the “twin peaks” theory, which has been broadly accepted as the right approach for the 21<sup>st</sup> century. It imposes a distinct separation between the first peak of financial stability, where prudential regulators assure the stability of the financial companies, and the second peak of financial conduct, where other regulators are responsible for consumer protection. This approach creates efficiency by having the same regulator oversee the conduct of both chartered banks and other financial companies, which often compete with one another in the same markets, such as mortgage and auto lending. The separation of the two main functions is also essential to prevent one of these goals from subordinating the other. In a 20<sup>th</sup>-century model, the missing focus was consumer protection. We neglected our oversight of the conduct of the financial companies, and it cost all of us dearly, including 40 million Californians. The Great Recession also brought on a deep fiscal crisis in California that has only recently been healed.

In the past decade, most large Western economies have adopted the twin peaks model: Australia, New Zealand, the U.S., the U.K., Ireland, and South Africa. Others are progressing toward the same destination. But right now, California is still operating on the obsolete model with its built-in conflict of interest between promoting the safety and soundness of financial companies versus regulating how they treat consumers. The two goals are sometimes at odds, and the financial regulator depends in part for its funding on dues paid by those companies. That is not the right answer for a state as important as California, which now boasts the fifth largest economy in the world. For these reasons, Californians deserve a modernized structure with a more concentrated focus on consumer financial protection.

At the federal level, the CFPB was created to fulfill this role. In less than a decade, it has proved to be a great success. It has amplified the voices of consumers, receiving and handling over 1.6 million complaints since it opened its doors. It has enforced the law vigorously, returning \$12.4 billion to more than 30 million Americans, which works out to about a billion dollars for Californians alone. Its reforms to the mortgage and credit card markets have saved consumers billions of dollars per year, putting a halt to the irresponsible and predatory lending that brought on the financial crisis, damaged our economy, and hurt so many Americans. It also has reined in harassing debt collectors, forced improvements to the credit reporting companies, and stopped many sloppy or abusive practices by auto lenders and student loan servicers.

Right now, the CFPB has been retreating from some of its responsibilities under its new leadership. It has backed away from a strong federal rule on payday lending, from actions to prevent violations of the Military Lending Act, and from aggressive oversight of student loan servicers. I am aware that you are going to hear more about these issues from other panelists who are expert in these areas and will discuss them in more detail. But this is the perfect time for California to step forward to shore up consumer financial protection, even as the Trump administration is currently defaulting on some of its obligations under federal law.

The financial reform law that created the CFPB, known as the Dodd-Frank Act, expressly provided for more expansive protections at the state level that can go beyond federal protections. To put it simply, the law says clearly that federal law sets a floor, not a ceiling, on consumer financial protection in this country. Congress thus opened the door for more vigorous protection of consumer rights through state officials who can ensure that these laws are strong and that they are enforced effectively. These efforts not only protect consumers – who simply deserve to be

treated fairly by financial companies – but it also levels the playing field by protecting more ethical companies from having to compete against bad actors that are willing to cut corners and violate the law to get an advantage in the market. That is the worst form of unfair competition, and stronger enforcement of consumer laws can help root it out.

We also need to do a better job of educating consumers about the risks and challenges of more complicated credit products. Over the past decade, many consumers have been exposed to the hazards of mortgage instruments with increasingly exotic features; they now have access to revolving credit, often on multiple credit card accounts with different interest rates and vastly different terms; and they may be juggling various other credit obligations as well. Yet nobody would claim that this country is suddenly doing a better job of educating consumers about their obligations – not in the home, not in school, not at work, and nowhere else. That is a task we need to take much more seriously than we now do or have done. By taking the initiative, California can help lead other states forward.

This work matters greatly in our society, which is marked by growing income inequality and huge wealth inequality. The focus on putting more money into people’s pockets should be matched by a similar focus on keeping more money in their pockets, rather than having it drain away in nickel-and-dime fees, frauds and scams, or abuses that may be perpetrated by big financial companies. In a simpler time, Benjamin Franklin declared in his *Poor Richard’s Almanac* that “a penny saved is a penny earned.” In today’s world, a penny saved from financial predators is a penny that is very well earned indeed. A single bad financial experience can ruin a person or a family, and a constellation of bad experiences can undermine entire communities, as we saw in the runup to the financial crisis just a decade ago.

In 1962, President Kennedy gave a speech to Congress in which, for the first time, he spoke directly about the role of the consumer in our society. He noted that: “Consumers, by definition, include us all. They are the largest economic group in the economy . . . Two-thirds of all spending in the economy is by consumers. But they are the only important group in the economy who are not effectively organized, whose views are often not heard.” His words are just as true today. The push to protect consumers later resulted in such landmark bipartisan legislation as the Truth in Lending Act, the Equal Credit Opportunity Act, and the Fair Debt Collection Practices Act, enacted under both Republican and Democratic administrations. Thirty years later, these efforts at the federal level had fallen behind the rapid pace of developments in the financial marketplace. The laws needed to be updated, and an outmoded regulatory structure meant that the laws were being systematically under-enforced, with grave consequences for all Americans. The CFPB was an essential and welcome centerpiece of those reforms. As the federal government now again seems to be abdicating its role, it is crucial for this country that the states are taking up the mantle of consumer financial protection. I am encouraged to see that California is prepared to lead the way.

Thank you. I would be glad to answer any questions you may have.