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The Consumer Financial Protection Agency Act: Attempting to Improve Bad Policy

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During last year's presidential campaign, Barack Obama noted that "you can put lipstick on a pig, but it's still a pig." This phrase neatly sums up the ongoing House Financial Services Committee markup of H.R. 3126, the Consumer Financial Protection Agency (CFPA) Act of 2009. Despite honest attempts to improve the bill, the overall concept is still badly flawed, and any result that comes close to the original concept will be a major mistake.

There is simply no rationale for creating such an agency that a coordinating council of state and federal financial regulators cannot accomplish easier and at a lower cost.[1] Having said that, there are a number of issues that could be either improved or worsened during the markup, and for that reason, the committee's action will be important.

Can States Offer Stricter Standards? Chief among these issues is the question of allowing ambitious state officials to compete to offer ever more stringent standards. Even with a few modifications, the current language of the CFPA does allow states an unusual amount of leeway to increase regulation on even federally regulated financial services firms. Such a standard could seriously damage the national market in financial services by forcing providers to meet up to 51 separate consumer regulatory regimes. The higher costs would be borne by consumers.

The best result would be to have the offending language removed from the bill. Failing that, one possible alternative would be to allow a federally regulated financial services firm to apply to its federal regulator for a ruling on whether it must comply with a state standard instead of the federal one. State-chartered and state-regulated firms would still remain subject to those state actions.

While still cumbersome and potentially confusing, this standard would at least allow a responsible regulator with a national focus to determine if the proposed state law is reasonable or would damage the national market for financial products.

Who Regulates Credit Reporting Agencies? Another key question remains precisely what types of entities would be subject to the CFPA. The original language was extremely broad and has been already narrowed several times, most recently by one of Chairman Barney Frank's manager's amendments. However, uncertainty remains, especially over the question of credit rating agencies such as Fitch's, Standard and Poor's, and Moody's, which are currently regulated by the Securities and Exchange Commission (SEC).

There is no question that credit ratings agencies made major errors in rating securitized instruments leading up to the 2008 financial crisis, but the SEC is well aware of the problems and has already taken steps to correct them. Moving that regulation into a

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new agency will only delay needed reforms and add another level of uncertainty to an issue that needs to be resolved quickly.

***Changed* Does Not Necessarily Mean "Improved."** Even if these and many more issues are resolved, it does not mean that the overall concept is sound. The CFPA would cause many more problems than it would solve and should not be part of any financial regulatory reform.

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1. For details, see David C. John, "How to Protect Consumers in the Financial Marketplace: An Alternate Approach," Heritage Foundation *Backgrounder* No. 2314, September 8, 2009, at *http://www.heritage.org/Research/Regulation/bg2314.cfm.*

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