TESTIMONY TO MARYLAND CONSUMER PROTECTION COMMISSION

December 5, 2017

Thank you for the opportunity to testify before you today on behalf of Americans for Financial Reform. AFR is a coalition of more than 200 national, state and local organizations who have come together to advocate for stronger and more effective oversight of the financial industry. Members of our coalition include consumer, civil rights, investor, retiree, community, labor, and faith based groups.[1]

We are approaching the tenth anniversary of the 2008 financial crisis, but we have still not left it behind. During the Great Recession that followed the financial collapse, almost nine million workers lost their jobs and almost seven million families lost their homes.[2] In Maryland alone, almost 100,000 workers lost their jobs during the recession. But the impact of the crisis has echoed beyond the immediate recession that followed, as severe as that was. Recent research has found that economic growth since the financial collapse has actually been slower than in the decade following the 1929 stock market crash that began the Great Depression.[3]

The financial crisis was of a severity and magnitude that had not been imagined possible. Economists and financial regulators believed that the idea of a financial disruption leading to such a large decline in economic activity was a historical memory and not a contemporary possibility. Years after the collapse, former Federal Reserve chair Alan Greenspan asked plaintively "why was virtually every economist and policymaker of note so blind to the coming calamity?"[4] The experience of the financial crisis thus led to a significant rethinking of the scope and nature of financial regulation, a shift from the deregulatory conventional wisdom that had driven American financial policy since the 1970s.

The legislative result of this process was the Dodd-Frank Act, the most significant step toward enhanced regulation of the financial sector in decades. The Dodd-Frank Act included crucial steps such as the establishment of the Consumer Financial Protection Bureau (CFPB) to protect consumers from exploitative lending, and rules to enhance the stability of the banking and financial system by requiring additional loss absorbency and improved risk management.

Although the Dodd-Frank Act is at the center of the move toward re-regulation of finance, it is not the only element. Another important step was the Department of Labor (DOL) move to clarify and enforce the fiduciary responsibilities owed to investors by professionals offering

[1] A list of AFR members is available at http://ourfinancialsecurity.org/about/our-coalition/
[2] Americans for Financial Reform, "The Costs of the Crisis", July, 2015. http://bit.ly/2jeY6fx
[3] Blanchard, Olivier and Lawrence Summers, "Rethinking Stabilization Policy: Back to the Future", Peterson Institute of Economics, October 8, 2017. http://bit.ly/2ymjhEm
[4] Greenspan, Alan, "We Never Saw It Coming", *Foreign Affairs*, October 15, 2013. http://fam.ag/1Kznvqh

financial advice to retirement savers. This long-overdue "fiduciary rule" is a key step in protecting the rights of consumers in self-directed retirement accounts.

I know the Commission has already received extensive testimony regarding the Dodd-Frank Act, so I will not review the details of the legislation again here. Instead, I want to focus on the current moment and ask how the change in presidential administrations is likely to affect the oversight of the financial system and the protection of consumers, and also what the role of states like Maryland should be in responding to this change.

In doing so I want to make three broad points:

1) The Dodd-Frank Act and other regulatory steps are less radical and less disruptive to the financial sector than often portrayed. In fact, the financial sector has done well under the Dodd-Frank Act.

2) In part because of this, it is unlikely that the current Administration or Congress will completely eliminate significant elements of Dodd-Frank. However, we are at the beginning of a wave of more technical regulatory and legislative changes that present a major under-the-radar threat to effective financial oversight and consumer protection.

3) States have a number of important tools with which to respond to this stealth deregulation.

The Financial Sector Has Done Well Under the New Dodd-Frank Regulatory Regime

Today it is over seven years after the passage of the Dodd-Frank Act. The finance and insurance sector has grown from 6.6% of the economy when Dodd-Frank was passed to 7.4% today, an increase of more than 10 percent.[5] This indicates that finance has continued to grow faster than other sectors of the economy under Dodd-Frank. In an almost twenty trillion dollar economy this growth represents an increase of hundreds of billions of dollars in value added in the financial sector.

It is interesting to compare this growth to what happened after the passage of New Deal financial reforms, to which Dodd-Frank is sometimes compared. When Franklin Roosevelt was elected in 1932, the financial sector accounted for 5.7% of value added. Seven years later, in 1939, it was just 4% of the economy, a decline of almost a third.[6]

This reflects not only general differences between the two economic periods, but the fact that the Dodd-Frank regulatory reform is less radical and sweeping than the New Deal reforms, and places fewer real constraints on financial sector growth. Dodd-Frank granted tremendous

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[5] Bureau of Economic Analysis interactive tables on GDP by industry, accessed December 4, 2017. Available at https://www.bea.gov/iTable/index_industry_gdpIndy.cfm
[6] Phillipon, Thomas, "Has The US Financial Industry Become Less Efficient?", *American Economic Review,* April 2015, Data Appendix. http://bit.ly/1gRuAEB

discretion and autonomy to regulators to shape and choose the ways in which regulatory reforms were implemented. Regulators used this autonomy to accommodate existing financial business models and to ensure that new regulations were not excessively disruptive to financial actors.

We can see the results of this accommodation in the profitability and revenues of key segments of the financial sector. For example, in 2016, 95.7 percent of community banks earned a profit, an increase from 78.8 percent in 2010 when Dodd-Frank was passed.[7] Indeed, the banking sector as a whole earned record revenues in 2016.

We can also see growth in key outputs of the financial sector. The chart below shows real annual growth rates in lending since the passage of Dodd-Frank as compared to long-run historical averages and the pre-financial crisis period. Although overall lending growth rates are somewhat lower than the unsustainable levels observed just before the financial crisis, they exceed historical averages. Business lending growth rates are well above historical averages.

PERIOD	**REAL ANNUAL GROWTH RATES IN BANK LENDING**	
	TOTAL	BUSINESS LENDING
Historical Average: 1973-2016	3.7%	2.7%
Pre Financial Crisis: 2003-2008	7.4%	7.6%
Post Dodd-Frank: 2011-2016	4.1%	8.9%

SOURCE: Federal Reserve Release H-8, AFR calculations.

Some of this may be due to recovery from recession, but the very strong growth in business lending especially hardly seems compatible with a story that describes Dodd-Frank as very harmful to banking activity.

Claims that financial regulations have crippled the capital markets are also refuted by the facts. Spurred by low interest rates, U.S. corporate bond issuance set new volume records each year between 2012 and 2016, and is on track to do so again in 2017.[8] Other metrics of bond market

[7] Federal Deposit Insurance Commission, Quarterly Banking Report, Q4 2010 and Q4 2016, https://www.fdic.gov/bank/analytical/qbp/
[8] SIFMA Research and Data, available at https://www.sifma.org/resources/archive/research/

health, such as trading volumes and costs, are also strong, with trading volumes reaching new heights and trading costs dropping to record lows.[9]

Despite the evidence that Dodd-Frank has been enforced in an accommodative manner that has allowed the financial industry to thrive, lobbyists have presented new regulations as the cause of all manner of harm to banks. Most notably, the decline in the number of small community banks has been blamed on Dodd-Frank and increased financial regulation. However, this decline is a long-standing trend. The number of community banks has declined every single year since 1984, almost entirely due to a decline in the number of very small banks below $100 million in size. This decline was accelerated by the impact of the financial crisis itself. Almost 5 percent of all U.S. banks failed between 2008 and 2011, and most were community banks. It is true that the smallest community banks have more difficulty absorbing the fixed costs of regulation, and it is entirely appropriate to assist them with this burden. However, both the Dodd-Frank statute and current regulations contain significant exemptions for the smallest banks.[10]

We Are at the Beginning of a Wave of "Stealth" Deregulation

Even though the financial sector has generally done well under Dodd-Frank, there are still of course ways in which the new regulations constrain financial profits. The CFPB's enforcement of ability to pay requirements for mortgages limits predatory lending practices that can create short-term profits at the expense of long-term consumer harm. Increases in loss absorbency at major banks such as increased capital requirements lower return on equity, if not revenues. The Department of Labor's own economic analysis showed that better enforcement of fiduciary responsibilities among investment advisors would transfer tens of billions of dollars from the bottom line of sell-side companies to the returns of retirement savers, by making it more difficult for brokers to steer investors into products that benefited the broker at the expense of the customer.

This creates pressure for changes to financial regulatory rules. At the same time, the great scope for regulatory discretion under Dodd-Frank and other elements of our regulatory system means that it is generally not necessary to repeal or eliminate "headline" elements of new financial regulatory laws in order to make the changes desired by financial actors. These changes can be made by regulators acting independently to change their own rules, or facilitated by relatively subtle and technical statutory changes.

One can see examples of both types of changes today. AFR analyzed the first report by the new Administration's Treasury, which is on banking regulation, and compared it to recommendations by The Clearing House, a major big bank lobby. We found that the Treasury report

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[9] Adrian, Tobias, Michael Fleming, Or Shachar, and Erik Vogt, "Market Liquidity After the Financial Crisis", Federal Reserve Bank of New York Staff Reports No. 796, October, 2016. http://nyfed.org/2elYG8l

[10] Further detail on community bank issues is provided in my June 9, 2016 testimony to the House Small Business Committee, which I have also submitted to the Commission and is available at https://smallbusiness.house.gov/uploadedfiles/6-9-16_stanley_testimony.pdf

recommended pro-industry action in 85 percent (17 out of 20) of the broad areas where The Clearing House had called for deregulatory changes, and that over 75 percent (31 out of 40) of specific deregulatory requests were exactly reflected in the Treasury report. All of these changes reduced risk controls and loss absorbency at big banks, and none increased them. We further found that 29 out of the 31 specific deregulatory recommendations could be made by regulators independently without any Congressional action. (Our analysis is attached).

This is just one example of the types of deregulatory changes that can be made without any need for Congressional action. Another example would be rewriting fiduciary protections. The Department of Labor has already acted to delay key enforcement provisions of the finalized fiduciary rule by over 18 months, allowing industry to avoid compliance over that period with little chance of any penalty. During that period, we believe it is likely that the Department of Labor and the Securities and Exchange Commission (SEC) will act to rewrite the fiduciary rule to significantly reduce limitations and accountability for conflicted investment advice that could harm investors.

But beyond regulatory changes, we are also seeing a wave of potential legislative changes gaining momentum. In the House of Representatives, industry's strategy for modifying financial regulations has shifted from advocating a single large and dramatic bill (the CHOICE Act, which was advanced earlier this year) to advocating for numerous smaller bills. Just from October to December of this year, the House Financial Services Committee has marked up or will soon mark up a total of over sixty separate items of deregulatory legislation.[11] While each bill may appear relatively obscure and technical on its own, many have significant impacts in terms of reducing consumer lending protections, risk controls on banks, and other important elements of regulation. Recent legislation is targeting everything from consumer protections for buyers of manufactured homes (mobile homes) to protections for investors in securities markets to capital requirements for large banks. I am also submitting a set of AFR's recent letters on House markups to the Commission to give further background on the type of legislation being advocated.

The Senate will be the key battleground when it comes to whether these bills actually become law. Today, even as we speak, the Senate Banking Committee is marking up a bill that includes some two dozen deregulatory changes, including changes that would reduce mortgage protections, create loopholes in important risk controls for community banks and larger banks, and reduce state regulatory jurisdiction over securities. These changes are not as extreme as some being considered in the House and do not include some of the more prominent items on industry's wish list, but they are still significant.

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[11] See House Financial Services markup schedule for the 115th Congress, October-December 2017, available at https://financialservices.house.gov/calendar/?EventTypeID=311&Congress=115

What Can States Do?

States have a variety of tools they can use to try to step in for Federal regulators and protect consumers when Federal agencies fail to take needed action.

The most significant change due to the Dodd-Frank Act is the increase in the statutory power of states to enforce consumer laws. State Attorneys General can enforce CFPB regulations, and also have the authority to enforce the statutory CFPB powers enumerated in Title X of the Dodd-Frank Act. Further, under new pre-emption standards established by Dodd-Frank, states can enforce both state consumer laws and Title X powers against national banks unless they prevent or significantly interfere with the exercise of national bank powers.[12] The ability to enforce the general Title X prohibition against unfair, deceptive, and abusive acts and practices may be particularly valuable.[13]

State consumer law powers are likely to be especially valuable in the area of mortgage protections at regional banks. Many items of legislation currently being advocated by industry would significantly reduce mortgage protections at banks up to $10 billion or even $25 billion higher in asset size. (For reference, the largest state chartered bank in Maryland, Eaglebank, is currently $7.2 billion in size).

Ed Mierzwinski's testimony today highlights some other areas where it is likely the current regime at the CFPB will weaken regulations or enforcement and states can step in to address consumer abuses. Most notably, the recently finalized rule governing payday and auto title lending may be overturned by Congress or eventually negated by the CFPB itself. This is an area that states can and should address.

It is also notable that financial sector lobbyists are gearing up to attack the CFPB's authority over insurance products linked to consumer lending, such as title insurance, forced placed insurance, and credit insurance products. If they are successful, jurisdiction over these products would fall more exclusively to state insurance regulators. Many of these markets are known for abuses, especially those associated with lender-affiliated insurance. This is an area where state jurisdiction is clear.

Another area where Federal regulations are likely to be significantly loosened is the Home Mortgage Disclosure Act, the major tool for determining patterns of racial discrimination in lending. It is possible that exemptions from this law will be significantly expanded. This is an area where states could seek to gather information no longer being collected by the Federal government.

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[12] Wilmarth Arthur E., "The Dodd-Frank Act's Expansion of State Authority to Protect Consumers of Financial Services", 36 J. Corp. L. 893 (2011). http://bit.ly/2iUDyvX

[13] Saunders, Lauren, The Role of the States Under the Dodd-Frank Act of 2010, National Consumer Law Center, December, 2010. http://bit.ly/2jTvPe3

States can also step in to try to protect retirement savers from deceptive practices by brokers who purport to provide unbiased advice to investors. Aggressive enforcement by states of rules against deceptive trade practices could provide some of the benefits of a strong fiduciary standard when, as discussed above, the Department of Labor will likely weaken or fail to enforce this rule.

A recent study by the Consumer Federation of America and AFR (also submitted to the Commission) found that major brokerage firms and insurance companies misleadingly characterized themselves to investors as trustworthy fiduciary advisors while at the same time telling the courts that they were simply acting as salespeople.[14] Notably, the National Securities Market Improvement Act of 1996 preserves the ability of state securities regulators to "bring enforcement actions with respect to fraud or deceit, or unlawful conduct by a broker or dealer, in connection with securities or securities transactions."[15] Unlawful conduct by a broker or dealer could potentially include a breach of fiduciary duty, and deceit could include presenting oneself as a trustworthy advisor while in fact acting as a sales person.

Some states have already acted at the state level to formally extend fiduciary standards from financial planners to broker-dealers who present themselves as advisors. Such efforts are advancing or under consideration in New York, Texas, Connecticut, and, most prominently, Nevada, which has passed legislation (S 383) to do so.

Finally, we would like to join Ed Mierzwinski in encouraging the Commission to contact Maryland's Congressional delegation to urge them to resist efforts at statutory deregulation. Given the level of discretion provided to financial regulators in the Dodd-Frank Act, and the strongly deregulatory bias of the Trump Administration, there is simply no call for statutory change to reduce oversight of the financial system. It is important to reinforce this message to members of Congress, who are currently faced with a blizzard of legislative proposals backed by the immense lobbying resources of the financial sector.

Thank you very much for the opportunity to testify before you today.

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[14] Consumer Federation of America and Americans for Financial Reform, Financial Advisor or Investment Salesperson: Brokers and Insurers Want to Have It Both Ways, January 18, 2017. http://bit.ly/2AyIyuy

[15] See the Committee Report for the Securities Amendments of 1996, available at https://www.congress.gov/104/crpt/hrpt622/CRPT-104hrpt622.pdf