Written Testimony before the **House Financial Services Subcommittee on Financial Institutions and Monetary Policy**

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Chairman Barr and Ranking Member Foster, thank you for the opportunity to present testimony on behalf of my organization, Americans for Financial Reform (AFR), an advocacy organization and coalition born out of the 2008 global financial crisis that advocates for a fairer and more equitable banking system. The Global Financial Crisis laid bare how Wall Street and banks extract resources from workers and communities to line the pockets of those at the top. AFR was instrumental in securing the passage of the Dodd-Frank Act, my generation's largest reform of the financial system. Currently, our mission includes maintaining the progress made in that law and advocating for laws and regulations needed now to build a more equitable, sustainable, and stable economy.

Unfortunately, many of the proposals being discussed today represent regression from the path to creating a more equitable banking system that works for working-class communities, like the one I grew up in, East Flatbush, Brooklyn, New York. Today, I will discuss the importance of strong safeguards for consumers' financial data; the dangers in the continual expansion of Big Tech's role and power in the banking and financial services industries; and the importance of maintaining a competitive landscape for banks through stronger bank merger guidelines and creating a level playing field between banks and nonbank financial institutions.

Consumer Protections and Data Privacy

Any legislation seeking to enhance consumers' rights regarding their financial data and privacy should build upon Gramm-Leach-Bliley, not undermine it, especially as Gramm-Leach-Bliley was conceived in a world before the proliferation of ecommerce and digital banking services. The Financial Data Privacy Bill being considered before the committee today is branded as a bill that seeks to protect consumers' data; however, it conspicuously omits the role of the agency tasked with looking out for consumers in the financial marketplace, the Consumer Financial Protection Bureau (CFPB).

Additionally, this bill includes broad preemption provisions that will nullify stronger protections in existing state laws, and it provides consumers a very narrow private right of action that is much more limited than what states, such as California, currently provide. It also does nothing to deal with the problem of forced arbitration language, which currently leaves many consumers with no effective way to vindicate their rights in court. For all of these reasons, it does not deliver on the promise of consumer protection, and would only stand in the way of the robust consumer protection regime we need.

As social media platforms facilitate payment transactions, they receive valuable data on the social connections and outside lives of the sender and receiver, data that global companies find extremely valuable. Only a few days ago, it was announced that Twitter is applying for licenses to facilitate in-app payment services.[1] With such a comprehensive picture of consumer behavior, dominant platforms can more easily take over adjacent markets, engage in predatory pricing, increase the cost of advertising on their sites, and thus accumulate more economic power. They can and will use the integrated information,

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[1] Hannah Murphy. "Elon Musk pushes forward with Twitter payments vision." Financial Times. January 2022.

our financial data and online lives, to both enhance existing products and offer new services (like credit scoring) to new groups of consumers.

This is why we can not afford to go small on data privacy legislation. If securitization and capitalization was at the forefront of yesteryear's financial system, then accumulation and control of consumer data will be the bedrock of the new one. Congress needs to act seriously and boldly here and pass a robust privacy bill of rights for consumers.

Inadequate Customer Recourse

Any viable privacy legislation bill must include a strong private right of action for consumers. Prior drafts of the Financial Data Privacy Bill legislation limited liability in ways that would harm the public. It made financial institutions liable *only* for damages resulting from the unauthorized access to the customer's account using nonpublic information. Furthermore, the customer had no recourse if their information was stolen but their account was not accessed. We look forward to further reviewing and commenting on updated drafts of the bill.

Preemption

The Financial Data Privacy Bill has an extremely broad preemption provision that effectively renders state laws that provide broader data privacy protections for consumers toothless, such as California's Privacy Rights Act (CPRA).[2] Illinois, Virginia, and Colorado have also enacted meaningful privacy protections for consumers that would be eliminated by the proposed federal bill.[3] Additionally, while this legislation expands liability to "data aggregators"–companies that acquire, analyze, and monetize troves of consumer financial data–the benefit gained by doing so is minimal because they too will be subject to the preemption clause. This coupled with a very weak federal private right of action for consumers when compared to many states create a doubly whammy for consumers looking for restitution.[4]

Consumers were able to file class action lawsuits against data aggregators like Plaid and Yodlee for engaging in a number of illegal practices under state law, like violating California's anti-phishing laws to acquiring consumer account credentials for the purpose of accessing data from consumer banking accounts.[5] Under this draft legislation, these companies would have evaded responsibility and consumers would have not been able to recover damages.

Help Consumers by Supporting Strong Implementation of Section 1033

Congress should be working to support the CFPB as it drafts rules to finally implement Dodd-Frank's Section 1033. This law provides consumers with a clear and explicit right to access their data and introduces new competition to the market, providing consumers with opportunities to more easily switch banks and access new or better products.

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[2] American Association of Justice. "Oppose Financial Services Privacy Legislation that would Gut Consumer Rights". 31 January 2023. Pg 2.

[3] Id

[4] Id

[5] Merken, Sara. [Fintech firm Plaid agrees to $58 mln deal to end privacy case](). Reuters. 6 August 2021.

A strong implementation of Section 1033 will be critical to beating back anti-competitive, data-hoarding behavior and putting safeguards in place to protect consumers' access to and control over their data. in their financial lives. The massive amount of consumer data that large financial institutions have amassed gives them a significant advantage over competitors. Many new market entrants rely on a consumer's ability to access and transfer their financial data in order to provide services.

Silicon Valley and Wall Street: What Can Go Wrong?

I would be remiss if I did not discuss one of the primary reasons we need expanded consumers' rights regarding data privacy protection. This is the direct result of the blurring boundaries between Silicon Valley and Wall Street. The blending of these two industries create novel risks for consumers, depositors, and financial stability. The partnership of these industries has come in the form of digital wallets, online peer-to-peer payment services, industrial loan company charters, buy-now-pay-later companies, increased partnerships between traditional banks and financial technology companies known as fintechs, and of course the rise of cryptocurrencies.

While customers should always be afforded the right to know when their data is being collected, how it is used, and which third-party affiliates have access to it, data privacy legislation is just one tool in the toolkit needed to effectively address the blending of these two powerful industries. The following sections discuss various products and services stemming from financial technology and policy solutions to minimize dangers to consumers posed by these products. Sometimes the need for such protections is waved away by simply celebrating products as "financial innovation." But calling something "innovative" is no substitute for asking tough questions about who benefits and how, who is left behind, what dangers and risks the products pose, and how to mitigate them.

Digital Wallets & Socialized Payment Processors

These novel fintech companies and products, while presenting convenient methods for consumers to bank and transact with businesses and peers, should be adequately regulated and include safeguards to protect customers from misuse, fraud, and unmanageable debt. In my previous testimony before the FintechTask Force in April of last year, I discussed many of the shortcomings of digital wallets and peer-to-peer payment systems, including the fact that they lack the same protections consumers enjoy with debit and credit cards, and their platforms being ripe ground for scammers looking to capitalize on vulnerable populations.[6]

These companies store customers' web browsing history, geolocation, and sensitive transaction data. Bad actors who breach these companies' servers need not steal their customers' nonpublic personal identifiable information to identify and harm consumers.

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[6] Testimony of Renita Marcellin before the United States House of Representatives: House Financial Services Committee. 28 April 2022.

Dangers of Industrial Loan Company Charters
Large commercial companies, including Big Tech, seeking to offer banking services through an Industrial Loan Company (ILC) charter also violate well-established public policy in our country to separate commercial and banking enterprises. Historically, commercially-owned banks have denied services to competitors and generally engaged in imprudent activities to spur activity on the commercial side of their business.[7] Despite these dangers, there has recently been a noticeable uptick in the number of applicants for ILC charters, including the application by Rakuten, Japan's e-commerce giant.[8]

The parent of an industrial loan company is not robustly supervised by a federal financial regulator, when compared to consolidated supervision of a bank holding company and its affiliates by the Federal Reserve.[9] Nonetheless, as a result of both policy and circumstance, the Fed has repeatedly bailed out non-banks in times of crisis. Thus, by allowing commercial firms to take advantage of federal deposit insurance and other privileges given to a bank, including preemption of state interest rate caps, without the accompanying responsibilities, we are creating a moral hazard, plus heightening the effects of the next financial crisis, whenever it arrives.[10]

AFR has long advocated for closing the ILC loophole, and was happy to be part of a broad coalition of advocates and bank industry trade groups who supported Congressman Chuy Garcia's bipartisan bill last year that aimed to do just that.[11] We look forward to working with this committee this Congress to achieve this long standing goal.

Buy Now, Pay Later Products
Another example of technology companies offering credit-like products, is the advent of Buy Now, Pay Later (BNPL) products, a new twist on an old practice. BNPL products do not underwrite for a consumer's ability to repay, often rely on the expectation of late fees, can be difficult for consumers to manage, and can trigger punitive overdraft or non-sufficient fund (NSF) fees if linked to a bank account. Further, these products can lead consumers into accumulating unmanageable amounts of debt and lack the same dispute or refund rights that credit cards have should a consumer be unsatisfied with their purchase.[12]

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[7] Wilmarth, Arthur E., Jr., "*Wal-Mart and the Separation of Banking and Commerce"*, 39 Connecticut Law Review. 2007. Pgs 1539, 1598-1606.
[8] Hrushka, Anna, "Rakuten to continue ILC charter pursuit, subsidiary CEO says," BankDive. Aug 2020
[9] Wilmarth, Arthur E., Jr., Comment letter to the Federal Deposit Insurance Corporation regarding FDIC Docket RIN 3064-AF31 – Notice of proposed rulemaking: "Parent Companies of Industrial Banks and Industrial Loan Companies," 85 Fed. Reg. 17771. 10 April 2020.
[10] Testimony of Raúl Carillo before the United States House of Representatives: House Financial Services Committee. 29 September 2020.
[11] Americans for Financial Reform et al. Support for H.R. 5912, The Close the ILC Loophole Act. 5 April 2022.
[12] Torres, Marisabel. Center for Responsible Lending, Testimony to Task Force on Financial Technology U.S. House Committee on Financial Services Hearing on "Buy Now, Pay More Later? Investigating Risks and Benefits of BNPL and Other Emerging Fintech Cash Flow Products" 2 November 2021.; Wang, Penelope. "The Hidden Risks of Buy-Now, Pay-Later Plans" Consumer Reports. 14 February 2021.

BNPL programs may negatively impact consumer credit reports and scores, as some BNPL companies report negative credit activity like defaulting on a loan.[13] Additionally, although some companies are introducing programs to report all payment history to the credit bureaus, even positive payments may have a negative impact on a consumer's credit score since each loan is a separate credit item that gets opened and closed very quickly, reducing the average age of the consumer's credit lines.[14]

BNPL products have largely evaded oversight by federal and state regulators, and although these products could well serve some consumers, adequate consumer protections should apply. Congress should work on supporting the Consumer Financial Protection Bureau as it creates rules of the road–including applying Truth in Lending Act (TILA) and fair lending laws–for this group of products to better serve consumers.

Bank-Fintech Partnerships

Banks are increasingly partnering with a wide range of third-party non-bank fintechs. Some of these business partnerships may provide important benefits to individual customers. But others exist primarily as a means for the nonbank company to borrow a bank charter in order to evade state consumer protection laws. "Rent-a-bank schemes" in particular, tend to hide behind these partnerships.

For example, high-cost online lenders, such as EasyPay, use these partnerships to launder their loans through banks such as Transportation Alliance Bank (TAB Bank) in order to skirt state laws so they can pedal predatory triple-digit interest rate loans, up to 189% APR, to consumers in violation of state interest rate caps.[15] Predatory lenders use these schemes to take advantage of vulnerable populations, such as veterans and military service members. It is worth mentioning that only a few days ago, the FDIC decreased TAB's Community Reinvestment Act's (CRA) rating to "Needs to Improve" from "Satisfactory," the most common rating, for violating the Unfair or Deceptive Acts or Practices of the Federal Trade Commission Act.[16]

We applaud the bipartisan effort that overturned the OCC's "true lender" rule through the Congressional Review Act, a rule that despite its moniker would have allowed these rent-a-bank schemes to flourish. However, Congress can take additional action to ensure these bank-fintech partnerships truly serve consumers, including but limited to the following:

a) Amplify calls for the FDIC to initiate rulemaking that will prohibit its supervised institutions from assisting predatory lenders with evading state interest rate limits.[17]

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[13] Paul, Trina. "'Buy Now, Pay Later' Loans Can Decrease Your Credit Score Even if You Pay on Time—Here's What You Need to Know" CNBC. 3 September 2021.

[14] Id

[15] Stop the Debt Trap. "Predatory Lenders TAB Bank and EasyPay Finance Harm Veterans and Military Servicemembers with Loans up to 189% APR." May 2020.

[16] Jon Hill. "FDIC Ding Of Fintech Partner Bank May Signal Tougher Stance." Law360. February 2023.

[17] Americans for Financial Reform Ed Fund. "Letter Urging the FDIC to Stop Permitting its Supervised Institutions to Front for Predatory Lenders Evading State Interest Rate Limits." February 2022.

b) Introduce and pass the Veterans and Consumers Fair Credit Act, which would cover banks and extend to veterans and all consumers the 36% rate cap that today protects active duty servicemembers and their families.
c) Introduce and pass legislation to prevent the OCC from creating another "Special Purpose Fintech Charter."
d) Pass legislation that would give the federal and state banking regulators greater oversight authority of third-party partners and vendors, including regulators such as the National Credit Union Administration and Federal Housing Finance Agency.

Barriers to New Entrants

The Promoting Access to Capital in Underbanked Communities Act attempts to increase the number of de novo bank charters by lessening the capital requirements and other regulatory hurdles new banks must meet to be approved. This proposed legislation presents the wrong solution for a problem that seems to be resolving as economic conditions improve.

There is substantial evidence to suggest that the number of new banks is correlated with economic indicators rather than regulatory hurdles. For example, de novo charters fell by almost 50 percent from 175 new charters in 2007 to only 90 in 2008, and continued to fall precipitously in 2009 to only 24 new charters.[18] This time period of course marks the beginning stages of the great global financial crisis and the resulting recession, which was already being felt in many parts of the country at that time. When the recession was at its peak, 25 percent of community banks failed between 2009-2011.[19] A Fed Reserve study also showed that the number of new entrants closely correlates to the Fed Funds rate and interest rates in general.[20]

Furthermore, between 2017-2021, de novo charter approvals have increased almost every year.[21] Although the FDIC has yet to publish complete data for 2022, by May of last year, there were already six de novo charter approvals, which if continued at that rate, charter approvals would again outpace the preceding year.[22]

More telling than any of these statistics, is the fact that a 2016 FDIC study concluded that most de novo banks do not fail during their early years when they are required to have high capital cushions relative to established banks but instead fail when their capital requirements are similar to that of other banks.[23]

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[18] FDIC. BankFind Suite. Annual Historical Bank Data.
[19] Kowalik, Michal et al. "Bank Consolidation and Merger Activity". Federal Reserve Bank of Kansas City. Economic Review. First Quarter 2015. Pg 2.
[20] Adams, Robert and J. Gramlich. "Where Are All The New Banks? The Role of Regulatory Burden in New Charter Creation". Federal Reserve Board. 16 December 2014. Pg 3.
[21] Supra note 18.
[22] Mangulabnan, Xylex and N. Melican. "New bank charter applications of 2022: 1st new Wash. charter in 13 years files". S&P Global Market Intelligence. 8 June 2022.
[23] FDIC Center for Financial Research. Yan Lee, Chiwon Yom. "The Entry, Performance, and Risk Profile of De Novo Banks." April 2016.

This only underscores the role capital requirements play in creating resilient banks. All banks, especially new ones, must have an adequate capital cushion to absorb their losses during times of stress to avoid failing and potentially causing contagion. The structural reforms of Dodd-Frank that strengthened capital and liquidity regulation were effective in reducing the likelihood of failure and increasing market and consumer confidence in individual banks.

AFR, therefore, can not support any legislation that effectively rolls back capital requirements for banks, especially when the evidence indicates that de novo banks are more resilient with higher capital cushions.

Excessive Consolidation in the Banking Sector

One cannot discuss barriers to entry into the banking market without discussing the markedly increased consolidation in the industry. Ironically, between 2011-2014, the period that saw only one de novo bank chartered, voluntary bank mergers increased every year from 73 in 2011 to 162 mergers in 2014.[24] In fact, the same study done in 2014 by the Kansas City Fed concluded that voluntary mergers between unaffiliated banks was the primary factor in the decline of the number of banks since the recession.[25]

It has been shown time and time again that underregulated mergers both lead to an unfair playing field for new entrants, and are frequently not in the public's interest. The current merger review process by both the Department of Justice and federal banking regulators has failed to protect communities from ever larger banks exercising market power to impose higher costs on consumers and reduce the volume or quality of banking services. Furthermore, regulators, despite their statutory mandate, have allowed the largest banks, growth widely attributed to mergers, from becoming so large they pose a risk to the entire financial system and real economy.[26]

Are Increased Bank Mergers Serving the Public Interest?

The 1956 Bank Holding Company Act requires banking regulators to consider not only the impact on competition (the primary consideration of the Department of Justice), but also if a proposed merger would serve the "convenience and needs of the community."

Bank mergers have raised bank fees and the costs to maintain accounts, especially among the larger banks. The increased fees and higher minimum balance requirements make it harder for lower-income households to get or maintain an account.[27] These growing fees have made owning a bank account more costly for lower-income families. High bank account fees were a primary reason unbanked households

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[24] Adams, Robert and J. Gramlich. "Where Are All The New Banks? The Role of Regulatory Burden in New Charter Creation". Federal Reserve Board. 16 December 2014. Pg 4.

[25] Michal Kowalik, Troy Davig, Charles S. Morris, and Kristen Regehr. "Bank Consolidation and Merger Activity Following the Crisis." Kansas City Federal Reserve Bank. Quarter One 2015. Pg 45.

[26] United States Code. Title 12. Subsection 2901 and Subsection 2903.

[27] Bord, Vitay M. Harvard University. "Bank Consolidation and Financial Inclusion: The Adverse Effects of Bank Mergers on Depositors." 1 December 2018. Pg 8.

did not have a bank account, according to the FDIC.[28] People of color are substantially more likely to be unbanked. Black households were nearly six times more likely than white households to be unbanked and Latinx households were nearly five times more likely to be unbanked (16.9 percent, 3 percent, and 14 percent, respectively).[29]

For these reasons, we call on the federal banking regulators and the Department of Justice to strengthen the 1995 merger review guidelines and call on Congress to amplify the call for stronger guidelines.

Conclusion

The topics discussed today and their accompanying policy solutions have far-reaching consequences for consumers. The modern banking landscape now features a prominent "shadow banking sector" and the intertwining of the banking and technology industries. Congress must continue to build upon the progress it made in the Dodd-Frank Reform Act and not misguidedly roll back these necessary structural reforms. Additionally, during the last Administration, regulators actively worked to undermine many provisions in that bill, including gutting one of the main reforms enacted to properly regulate non-banks– the designation of large non-banks as systemically important financial institutions (SIFIs).

As we saw in 2008, much of the risk that led to panic and contagion, originated with behemoth non-banks such as Prudential, Metlife, GE Capital. SIFI designation was created as a tool for regulators, above all the Federal Reserve, to finally gain insight into the dealings of an entire conglomerate and how any risk created by these non-banks can flow into the banking sector. Unfortunately, rules enacted in 2019 purposely made the process of designating a nonbank as a SIFI especially onerous and cumbersome. It is important that Congress bolsters the Financial Stability Oversight Council's (FSOC) ability to rewrite those rules in order to use designation as a tool for financial stability, and not propose legislation that would further hamstring effective regulation.

In conclusion, technology has the potential to shape our banking system for the better. We can use it to develop Ecash, a digital version of the dollar, proposed by Congressman Lynch, or use it as the Fed is doing to implement realtime payments.[30] However, we can not allow technological innovation to be touted as a reason to avoid proper regulation and hurt consumers in the process. Thank you for your invitation to speak before you all today and we at AFR look forward to working with Members of the committee to implement many of the proposals I discussed today.

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[28] Appam, Gerald et al. Federal Deposit Insurance Corporation. "2017 FDIC National Survey of Unbanked and Underbanked Households." October 2018. Pg 4.
[29] Ibid. Pg 3.
[30] Congressman Stephen Lynch. "Rep. Lynch Introduces Legislation to Develop Electronic Version of U.S. Dollar." March 2022.