Consumer Financial Protection by Federal Agencies

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Summary

Consumers interact with the financial system as borrowers, savers, and investors. They do business with a panoply of firms and intermediaries and with each other. A wide range of federal laws and regulation seeks to protect them from unethical, fraudulent, and unfair financial practices and to ensure that they receive adequate information to assess the risks and costs of financial services and products.

Consumer financial protection responsibilities are divided among a number of federal agencies, including

- the Federal Trade Commission (FTC), which is the principal federal regulator of consumer transactions that do not involve a regulated financial institution, and which works to protect consumers against unfair, deceptive, or fraudulent practices in the marketplace;
- the Federal Reserve, which has primary responsibility for writing rules to enforce the consumer provisions of federal banking laws;
- the Securities and Exchange Commission (SEC), which regulates the public stock and bond markets;
- the Commodity Futures Trading Commission (CFTC), which monitors trading in futures markets and is charged with preventing commodity price manipulation;
- the Department of Housing and Urban Development (HUD), which regulates certain aspects of home mortgage lending;
- the Department of Labor, which regulates employer pension plans;
- the Department of Education, which has some oversight responsibility over student lending; and
- the Farm Credit Administration (FCA), which oversees nonbank lending to farmers.

The Obama Administration has proposed creating a new Consumer Financial Protection Agency (CFPA) to focus exclusively on consumer protection. The agency would focus primarily (but not exclusively) on banking services; institutions and firms regulated by the SEC and CFTC, for example, would be outside its scope. Legislation in the House—H.R. 3126 (Representative Frank), the Consumer Financial Protection Agency Act of 2009—generally follows the Administration's proposal. For more on the CPFA, see CRS Report R40696, *Financial Regulatory Reform: Analysis of the Consumer Financial Protection Agency (CFPA) as Proposed by the Obama Administration and H.R. 3126*, by David H. Carpenter and Mark Jickling.

This report briefly sets out the current division of consumer financial protection responsibilities among the various federal agencies. It will not be updated.

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The proposal to create a new agency dedicated entirely to consumer financial transactions reflects a view that the effectiveness of consumer protection needs improvement. The Obama Administration's white paper on financial regulatory reform argues that current efforts are inadequate because there are gaps in regulation, some regulators lack necessary tools, and some agencies are conflicted between consumer protection and other objectives.[1] An alternate view is that regulators have adequate tools and authority, but have not used them well. From this perspective, redrawing jurisdictional lines is unlikely to produce substantial consumer benefits.

It is difficult to create an objective measure of the effectiveness of consumer financial protection. While agencies can cite statistics on the number of enforcement cases brought, perceptions of how well consumers are protected in a particular financial market can be quickly revised after a major scandal comes to light. This was the case recently with the Securities and Exchange Commission, which was unable to detect the $65 billion Madoff Ponzi scheme despite multiple tips and targeted investigations.

To assist the debate over the need for a new agency, this report briefly sets out the current range of consumer financial protection programs at the federal level.

The Federal Trade Commission[2]

The Federal Trade Commission's (FTC's) consumer protection authority covers a very broad range of businesses and financial transactions. It is the primary federal regulator of consumer transactions that do not involve a regulated financial institution, such as a bank or stock broker. The FTC's Bureau of Consumer Protection works to protect consumers against unfair, deceptive, or fraudulent practices in the marketplace. The bureau conducts investigations, sues companies and people who violate the law, develops rules to protect consumers, and educates consumers and businesses about their rights and responsibilities. The bureau also collects complaints about consumer fraud and identity theft and makes them available to law enforcement agencies. The bureau has seven divisions:

- *Advertising Practices* protects consumers by enforcing truth-in-advertising laws, with particular emphasis on claims for food, over-the-counter drugs, dietary supplements, alcohol, and tobacco and on conduct related to high-tech products and the Internet, such as the dissemination of spyware.
- *Consumer and Business Education* plans, develops, and implements creative national campaigns to alert consumers to their rights and to explain compliance to industry.
- *Enforcement* litigates civil contempt and civil penalty actions to enforce FTC federal court injunctions and administrative orders that address consumer protection issues, including advertising and financial practices, data security, high-tech fraud, and telemarketing and other scams. The division also coordinates FTC actions with criminal law enforcement agencies through its Criminal Liaison Unit; litigates civil actions against those who defraud

[1] U.S. Treasury, *Financial Regulatory Reform: A New Foundation*, p. 55.

[2] The description that follows draws on the FTC's website at http://ftc.gov/bcp/about.shtm.

consumers; and develops, reviews, and enforces a variety of consumer protection rules.

- *Financial Practices* protects consumers from deceptive and unfair practices in the financial services industry, including protecting consumers from predatory or discriminatory lending practices, as well as deceptive or unfair loan servicing, debt collection, and credit counseling or other debt assistance practices.
- *Marketing Practices* leads the FTC's response to Internet, telecommunications, and direct-mail fraud; deceptive spam; fraudulent business, investment, and work-at-home schemes; and violations of the Do Not Call provisions of the Telemarketing Sales Rule.
- *Planning & Information* collects, analyzes, and makes available to law enforcement consumer fraud, identity theft, and National Do Not Call Registry complaints; and assists in the distribution of redress to consumers.
- *Privacy and Identity Protection* safeguards consumers' financial privacy; investigates breaches of data security; works to prevent identity theft and aids consumers whose identities have been stolen; and implements laws and regulations for the credit reporting industry, including the Fair Credit Reporting Act.

The Federal Reserve and Other Banking Agencies[3]

The Federal Reserve (Fed) writes, interprets, and in some cases enforces regulations to carry out the provisions many of the major consumer protection laws. These regulations may cover not only banks but also certain other businesses, including finance companies, mortgage brokers, retailers, and automobile dealers. Transactions covered involve credit, charge, and debit cards issued by financial institutions; credit cards issued by retail establishments; automated teller machine transactions and other electronic fund transfers; deposit account transactions; automobile leases; mortgages and home equity loans; and lines of credit and other unsecured credit. Among the Fed's consumer rules are

- *Regulation Z*, pursuant to the Truth in Lending Act, requires banks and other creditors to provide detailed information to consumers about the terms and cost of consumer credit for mortgages, car loans, credit and charge cards, and other credit products.
- *Regulation A (Equal Credit Opportunity)* prohibits lenders from discriminating against credit applicants, establishes guidelines for gathering and evaluating credit information, and requires written notification when credit is denied.
- *Regulation C (Home Mortgage Disclosure)* requires certain mortgage lenders to disclose data regarding their lending patterns.
- *Regulation E (Electronic Fund Transfers)* establishes the rights, liabilities, and responsibilities of parties in electronic funds transfers and protects consumers when they use such systems.

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[3] Much of what follows is drawn from a Federal Reserve publication at http://www.federalreserve.gov/pf/pdf/pf_6.pdf.

- *Regulation M (Consumer Leasing)* implements the consumer leasing provisions of the Truth in Lending Act by requiring meaningful disclosure of leasing terms.
- *Regulation P (Privacy of Consumer Financial Information)* governs how financial institutions use nonpublic personal information about consumers.
- *Regulation AA (Unfair or Deceptive Acts or Practices)* establishes consumer complaint procedures and defines unfair or deceptive practices in extending credit to consumers.
- *Regulation DD (Truth in Savings)* requires depository institutions to provide disclosures to enable consumers to make meaningful comparisons of deposit accounts.
- *Regulation GG (Prohibition on Funding of Unlawful Internet Gambling)* requires U.S. financial firms that participate in designated payment systems to establish and implement policies and procedures reasonably designed to prevent payments connected to unlawful Internet gambling.

The Fed enforces compliance with its consumer protection rules by the banks it supervises directly, which include state banks that are members of the Federal Reserve System and U.S. branches of foreign banks. Other bank regulators enforce the Fed's rules with regard to the institutions they supervise. The Office of the Comptroller of the Currency (OCC) enforces compliance by national banks; the Office of Thrift Supervision (OTS) for federally-chartered savings and loans; and the National Credit Union Administration (NCUA) for federal credit unions. The Federal Deposit Insurance Corporation (FDIC) also has a bank examination role, but its primary consumer protection function is to guarantee the safety of bank deposits.

Each regional Federal Reserve Bank has specially trained examiners who regularly evaluate banks' compliance with consumer protection laws and their Community Reinvestment Act (CRA) performance. Most banks are evaluated every 48 months, although large banks are examined every 24 months and poorly rated banks are examined more frequently.

The Fed responds to inquiries and complaints from the public about the policies and practices of financial institutions involving consumer protection issues. Each reserve bank has staff whose primary responsibility is to investigate consumer complaints about state member banks and refer complaints about other institutions to the appropriate regulatory agencies. The Fed's responses not only address the concerns raised but also educate consumers about financial matters.

The Federal Reserve Board maintains information on consumer complaints in a database, which it regularly reviews to identify potential problems at individual financial institutions and, as required by the Federal Trade Commission Improvement Act, to uncover potentially unfair or deceptive practices within the banking industry. Complaint data are a critical component of the risk-focused supervisory program and are used as a risk factor to assess a bank's compliance with consumer regulations.

Department of Housing and Urban Development

The Department of Housing and Urban Development (HUD) has authority to prescribe rules and regulations to achieve the purposes of the Real Estate Settlement Procedures Act of 1974 (RESPA). HUD's regulations pursuant to RESPA are referred to as Regulation X. RESPA governs the settlement process for residential real estate and requires advance disclosure of settlement costs to home buyers and sellers. In addition, the law prohibits certain kickbacks and referral fees that cause unnecessary increases in the costs of settlement services and limits the amounts that buyers are required to place in escrow accounts before settlement.

Securities and Exchange Commission

The Securities and Exchange Commission (SEC) regulates securities markets to protect investors from fraud and to ensure that markets are fair. There are two prongs to the SEC's investor protection efforts: disclosure and direct regulation of market intermediaries.

Disclosure requirements apply to all companies that sell stocks or bonds to the public. Such firms are required to register their securities with the SEC prior to sale. Registration involves disclosure of detailed information about the company, its business, financial condition, and principal officers, in addition to information about the securities offering itself. To keep the information in the initial registration statement current, companies are required to file periodic financial statements, such as quarterly and annual reports. SEC filings are available to the public without charge; the essential purpose of disclosure requirements is to give investors accurate and complete information about securities they may wish to buy or sell. Failure to disclose financial problems or other material information is a violation of securities law.

Certain market institutions and participants are required to register with the SEC and comply with a range of laws and regulations governing their dealings with public investors. SEC registrants include stock exchanges, brokerage firms, investment advisers, mutual funds, and others. In many areas, the SEC delegates its market regulation activities to self-regulatory organizations (SROs), including the Financial Industry Regulatory Authority (FINRA) and the stock exchanges. Failure to comply with SEC or SRO rules may lead to a revocation of registration, as well as civil and criminal penalties.

The SEC is organized into four operating divisions:[4]

- The *Division of Trading and Markets* is responsible for maintaining fair, orderly, and efficient markets. The staff of the division provide day-to-day oversight of the major securities market participants: the securities exchanges, securities firms, self-regulatory organizations, clearing agencies that help facilitate trade settlement, transfer agents (parties that maintain records of securities owners), securities information processors, and credit rating agencies.
- The *Division of Corporation Finance* oversees corporate disclosure of information to the investing public. The division's staff routinely reviews the disclosure documents filed by companies.
- The *Division of Investment Management* exercises oversight and regulation of the investment management industry, including mutual funds and the professional fund managers who advise them; analysts who research individual assets and asset classes; and investment advisers to individual customers. The division is focused on ensuring that disclosures about these investments are useful to retail

[4] See http://www.sec.gov/about/whatwedo.shtml.

customers, and that the management fees and other costs which consumers must bear are not excessive.

- The *Division of Enforcement* assists the Commission in executing its law enforcement function by recommending the commencement of investigations of securities law violations, by recommending that the Commission bring civil actions in federal court or before an administrative law judge, and by prosecuting these cases on behalf of the Commission. As an adjunct to the SEC's civil enforcement authority, the division works closely with law enforcement agencies to bring criminal cases when appropriate.

Commodity Futures Trading Commission

The Commodity Futures Trading Commission (CFTC) regulates the futures markets in much the same general way as the SEC oversees securities markets. The agency enforces the provisions of the Commodity Exchange Act (which includes numerous customer protection and anti-fraud provisions), makes its own rules to protect public customers of the futures exchanges, and also relies on SROs to carry out certain functions, including the registration of various classes of market intermediaries. Parallel to the SEC, the CFTC's mission carries market surveillance and enforcement programs, but these are on a smaller scale than the SEC's, in part because the number of small investors in futures is much smaller than the number of individuals who own stocks and bonds.

Another key goal of the CFTC is to prevent manipulation of commodity prices, which could have negative impacts on consumers and the economy.

The consumer protection functions of the CFTC reside primarily in two operating divisions:

- the *Division of Market Oversight*, which is responsible for fostering markets that accurately reflect the forces of supply and demand for the underlying commodity and are free of abusive trading activity, oversees trade execution facilities, and performs market surveillance, market compliance, and market and product review functions, and
- the *Division of Enforcement*, which investigates and prosecutes alleged violations of the Commodity Exchange Act and CFTC regulations. Violations may involve commodity futures or option trading on U.S. futures exchanges or the improper marketing and sales of commodity futures products to the general public.

Department of Labor

The Department of Labor (DOL) oversees private employer pension plans under the Employee Retirement Income Security Act (ERISA). It sets minimum standards for most voluntarily established pension and health plans in private industry to provide protection for individuals in these plans.[5]

[5] See http://www.dol.gov/dol/topic/retirement/index.htm.

ERISA requires plans to provide participants with plan information, including important information about plan features and funding; sets minimum standards for participation, vesting, benefit accrual and funding; provides fiduciary responsibilities for those who manage and control plan assets; requires plans to establish a grievance and appeals process for participants to get benefits from their plans; gives participants the right to sue for benefits and breaches of fiduciary duty; and, if a defined benefit plan is terminated, guarantees payment of certain benefits through a federally chartered corporation, known as the Pension Benefit Guaranty Corporation (PBGC).

In general, ERISA does not cover retirement plans established or maintained by governmental entities, churches for their employees, or plans which are maintained solely to comply with applicable workers compensation, unemployment or disability laws.

The Employee Benefits Security Administration (EBSA) of the Department of Labor is responsible for administering and enforcing the provisions of ERISA. As part of carrying out its responsibilities, the EBSA provides consumer information on pension plans, as well as compliance assistance for employers, plan service providers, and others to help them comply with ERISA.

Department of Education

The Department of Education has some oversight responsibility over student lending. Section 433 of the Higher Education Opportunity Act (P.L. 110-315) specifies a number of disclosures that must be made to student borrowers (and in some cases, their parents).[6] The disclosures include

- the cost of the loan—the current interest rate and all fees;
- the date repayment begins, the maximum repayment periods, and the minimum repayment amount; and
- the consequences of default.

In addition, colleges and universities are required to provide exit counseling information for student borrowers under the federal Perkins and Stafford Loan programs. Such counseling must cover repayment options (including applicable deferment, forbearance, consolidation, and discharge provisions) as well as the total amount owed. Borrowers must be notified when student loans are sold by the original lender to a third party.

Farm Credit Administration

Although some lending to farmers is under the jurisdiction of the banking agencies, the Farm Credit Administration (FCA) also has a role. Where lenders to farmers are not covered by the Truth in Lending Act (TILA)—for example, when the lender is an agricultural cooperative—the Farm Credit Act of 1971, as amended by the Farm Credit Amendments Act of 1985 and the Agricultural Credit Act of 1987, extends consumer protection to Farm Credit System loans. FCA regulations (12 CFR Part 614, Subpart K) require qualified lenders to provide truth-in-lending type disclosures on loans exempt from the TILA. In addition, FCA Regulation 12 CFR § 614.4336 contains special disclosure requirements relative to loans intended for sale.

[6] See http://www.ed.gov/policy/highered/leg/hea08/index.html.

The Role of the States

Finally, it should be noted that federal consumer protection programs are complemented by those of the states. Each state has commissions or agencies that regulate banking and securities and, in some cases, as other aspects of consumer finance as well. Federal law often divides regulation of financial institutions or professionals between federal and state agencies. For example, under the Investment Advisers Act of 1940, advisers with less than $25 million in client funds under management are the responsibility of the states, whereas the SEC may require registration of advisers who exceed that threshold.

In many areas, state financial regulation is preempted by federal law. In others, such as insurance, there is no federal regulatory scheme and the states have exclusive jurisdiction.

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