

AFR Americans for Financial Reform

May 22, 2018

Dear Representative:

On behalf of Americans for Financial Reform, we are writing to urge you to vote against HR 4439 and HR 5749, two of the bills under consideration at today's markup.¹ HR 4439 would massively expand the ability of lenders to evade state interest rate limits through the use of "sham lender" or "rent-a-bank" schemes. HR 5749 would reduce requirements for our largest Wall Street banks to hold their own equity capital against potential losses on complex derivatives, increasing the chance of a public bailout.

HR 4439, the "Modernizing Credit Opportunities Act", is presented as merely "clarifying" legal issues around third party lending arrangements. In fact, it would force courts to ignore economic reality and allow high-cost, state-regulated lenders to avoid state-level limits on interest rates if they could claim a bank was involved in the transaction. This would greatly facilitate the ability of payday lenders charging extortionate interest rates to avoid state usury caps. For this reason, the Conference of State Bank Supervisors has also opposed this legislation, stating that "it would allow bad actors to exploit banks' federal preemption to issue harmful loans to consumers in contravention of state law."²

In testimony, Georgetown professor Adam Levitin described the effect of the bill as follows:³

"When confronted with rent-a-bank situations, courts have often focused on the economic realities of the transaction and looked to see which party is the "true lender" on the loan. If the true lender is not a bank or a native tribe, then that party is not able to shelter in federal preemption for the bank or tribal sovereignty. H.R. 4439 would instruct courts to disregard economic realities and instead adhere to a legal fiction that the bank is the true lender simply because it is the originator of the loan. This is a terrible idea. "True lender" doctrine is an important doctrinal tool to police against abuses of the banking system. It's disgraceful that Congress would attempt to protect sham transactions, yet that is precisely what H.R. 4439 does. It deems the bank to be the true lender in a transaction no matter what the underlying facts and circumstances are."

¹ Americans for Financial Reform is an unprecedented coalition of more than 200 national, state and local groups who have come together to reform the financial industry. Members of our coalition include consumer, civil rights, investor, retiree, community, labor, faith based and business groups. A list of AFR members is available at <http://ourfinancialsecurity.org/about/our-coalition/>

² Conference of State Bank Supervisors, "CSBS Opposes HR 4439", May 18, 2018. <https://www.csbs.org/csbs-opposes-true-lender-bill-hr-4439>

³ Levitin, Adam, "Testimony To House Financial Services Committee", January 30, 2018. <https://financialservices.house.gov/uploadedfiles/hhrg-115-ba15-wstate-alevitin-20180130.pdf>

The transactions protected by HR 4439 would include payday loans offered at interest rates of 200%, 300%, or higher, with the intention to entrap the consumer in a cycle of debt. As Pope Francis stated in his recent “Considerations” on the ethical dimensions of our financial system:⁴

“...it is clear that applying excessively high interest rates, really beyond the range of the borrowers of funds, represents a transaction not only ethically illegitimate, but also harmful to the health of the economic system.”

HR 4439 has no other purpose than to facilitate the charging of such excessive interest rates by offering them legal immunity from state usury laws. It must be rejected.

HR 5749, the “Options Market Stability Act”, would create a statutory mandate to reduce capital charges on listed options for the major options clearing banks. Goldman Sachs, Bank of America/Merrill Lynch, and the Dutch bank ABN Amro would gain most of the benefits from this bill. These giant financial institutions would be able to run their option clearing business using less of their own equity capital. This heightens the risk of a public bailout should they fail.

HR 5749 would require certain risk adjustments to capital for cleared options, which would have the effect of reducing the capital banks hold to absorb any losses on options contracts. The bill has been advanced by the Chicago Board Options Exchange (CBOE) on the argument that the requirement for these systemically critical banks to hold capital against options is increasing the price of cleared option products for financial entities. This may be true, but the goal of regulators and Congress is not to minimize the price of cleared options for wealthy investors, but instead to ensure that these options are priced fairly based on the private sector holding equity capital against the risk of loss. Without capital requirements, banks with access to the public safety net such as Bank of America and Goldman Sachs would effectively be receiving a government subsidy that lowered the cost of their services.

Congress should not force regulators to lower capital requirements and effectively subsidize option clearing at the nations’ largest banks. HR 5749 is being advanced while the Trump Administration regulators are already cutting large bank capital requirements in numerous ways, including significant proposed cuts in required leverage capital and changes in derivatives risk adjustments that will also have the effect of cutting derivatives capital, including for listed options. The additional special favors for big banks in HR 5749 should be rejected.

If you have questions, please contact AFR’s Policy Director, Marcus Stanley, at marcus@ourfinancialsecurity.org or 202-466-3672. Thank you for your attention to this letter.

Sincerely,

Americans for Financial Reform

⁴ Dicastry for Promoting Integral Human Development, “Considerations for an Ethical Discernment Regarding Our Present Economic-Financial System”, Holy See Press Office, May 17, 2018.
<http://press.vatican.va/content/salastampa/it/bollettino/pubblico/2018/05/17/0360/00773.html#ing>