The Same Old Song

Wall Street's repeatedly discredited but **endlessly repeated** arguments against common-sense financial regulation.

burdensome job killer

devastating impact on small businesses and consumers

grave dangers to our economy

AFR Americans for Financial Reform

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AFR is a nonpartisan and nonprofit coalition of more than 200 civil rights, consumer, labor, business, investor, faith-based, and civic and community groups. Formed in the wake of the 2008 crisis, we are working to lay the foundation for a strong, stable, and ethical financial system – one that serves the economy and the country as a whole.

THE FINANCIAL INDUSTRY is on a deregulation rampage. Buoyed by the 2016 election results and the flow of Wall Streeters into top jobs in the Trump administration, industry forces have set out to repeal or undermine many of the new rules adopted after the financial crisis of 2008. While they're at it, they're trying to weaken rules that pre-date the crisis and some of the key agencies responsible for enforcing the rules.

This is an agenda with large and obvious benefits for banks and lenders. A set of proposals put forward by the Trump Treasury Department would boost the profits of the biggest banks by more than 20 percent, Bloomberg calculates. And yet, when industry leaders and lobbyists make their case for deregulation, we rarely hear any mention of its impact on their own companies and paychecks. Instead, they tell us they are looking out for the economic wellbeing of consumers, homeowners, small businesses, and the country as a whole.

One of the industry's immediate objectives, for example, is to block the Consumer Financial Protection Bureau from regulating triple-digit-interest payday, car-title, and installment lenders that trap people in unaffordable debt and suck resources out of economically fragile communities. The American Financial Services Association (AFSA), which lobbies on behalf of a subset of these lenders, wants Congress to strip the Consumer Bureau of its authority over them. Congress should do so because, according to AFSA President Bill Himpler, his member companies, freed from the threat of CFPB oversight, "will create real economic growth by increasing lending, creating jobs, and stimulating local economies."

"WASHINGTON'S REGULATORY WATERBOARDING IS DROWNING COMMUNITY BANKS AND SMALL BUSINESSES AND SINKING THE HOPES AND DREAMS OF MILLIONS OF LOW AND MIDDLE INCOME AMERICANS."

– Rep. Jeb Hensarling, 2017

In a parallel story, the Mortgage Bankers Association is backing legislation to loosen new lending standards adopted after the financial crisis – standards that require verification of a borrower's ability to repay and discourage hidden fees and unexpected interest-rate hikes. Those rules should be rolled back because, MBA Chairman J. David Motley asserts without citing any persuasive evidence (because there is none), overregulation of his industry has "reduced the availability and affordability of mortgage credit," especially for "low-to-moderate income borrowers, minorities and first-time homebuyers."

The big banks, for their part, are pressing lawmakers and regulators to relax new restrictions on risk-taking, including the Volcker Rule, which curbs their ability to gamble with federally guaranteed funds. One of the organizations spearheading this campaign is the Financial Services Roundtable, which represents some of the country's biggest financial institutions. If it succeeds, its member banks will be free to revert to many of the heads-we-win-tails-you-lose practices that, in the years leading to the crisis, allowed a few giant institutions and super-wealthy individuals to pocket millions while putting taxpayers and the nation's economy at risk. In its messaging, however, the Roundtable skips past the subject of Wall Street's past behavior, claiming – again without credible evidence – that the rules it objects to have reduced "the funding options open to entrepreneurs and other job creators," thus "holding back a more robust economic recovery."

THE CFPB'S PROPOSED PAYDAY-LENDING RULE IS A "BURDENSOME JOBS-KILLER" THAT COULD HAVE A "DEVASTATING IMPACT ON SMALL BUSINESSES AND CONSUMERS."

– Edward D'Alessio, Financial Service Centers of America, 2017

Powerful figures in Washington have embraced the industry's arguments as well as its agenda. House Financial Services Committee Chairman Jeb Hensarling (R-Tex.) has been promoting a massive deregulation bill that, besides taking the Consumer Bureau off the payday and mortgage lending beats, would repeal the Volcker Rule and curb the power of a multi-agency council of regulators charged with detecting the kind of risky behavior that could trigger another crisis. Despite heavy industry lobbying for his proposal, however – and despite the opposition of an overwhelming array of public-interest groups – Hensarling portrays his legislation as an effort to protect consumers and businesses against what he calls "Washington's regulatory waterboarding," which, he tells us, is "drowning community banks and small businesses and sinking the hopes and dreams of millions of low- and middle-income Americans."

These scare stories have no basis in reality. But here's another large reason to be skeptical of the arguments we've been hearing from the financial industry and its allies lately: their remarkable similarity to claims made by the same interests in the past – claims powerfully refuted by subsequent events.

In the three examples that follow, we look at the parallels between the rhetoric of today's crusaders for deregulation and the discredited arguments of their predecessors.

Case Study Number 1: Credit Card Reform

ISSUE: The Credit Card Accountability Responsibility and Disclosure (or CARD) Act of 2009, originally introduced by Representative Carolyn Maloney (D-N.Y.), sought to limit the grounds for raising a cardholder's interest rate, require more transparency in credit card agreements and statements, and curtail the use of late fees and fine-print "gotcha" charges that made many cards far more expensive than they appeared. The act specifically banned a number of techniques used to generate extra penalty fee income, such as changing due dates randomly to trick consumers into missing them, and charging late fees for payments that arrived "after 11 am" on the due date. Perhaps most significantly, the legislation barred banks from imposing penalty interest rates on existing balances unless payments came in at least 60 days late.

CLAIMS: The proposed rules would have terrible consequences for cardholders, industry lobbyists declared. After a key House committee vote, American Bankers Association CEO Edward Yingling warned of "higher costs for consumers" and "reduced access to credit for those with an imperfect or limited credit history." When the bill passed the House, Yingling's association put out a statement expressing particular concern over its impact on "the ability of consumers, students and small businesses to get credit cards."

> **"THE CARD ACT WILL LEAD TO HIGHER COSTS FOR CONSUMERS, REDUCED ACCESS TO CREDIT FOR THOSE WITH AN IMPERFECT OR LIMITED CREDIT HISTORY, AND LESS ACCESS TO LOW CREDIT OPTIONS."**
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> – Edward Yingling, American Bankers Association, 2008

That argument was taken up by elected officials like Rep. Pete Sessions (R-Tex.), who predicted that the CARD Act would "discourage lending" and "create a consumer credit crunch" at a time when "consumers and our economy have already had enough stress to deal with." The George W. Bush administration also took took the industry's side, asserting that an early version of Maloney's proposal "would broadly constrain the ability of financial institutions to price risk, likely resulting in less access to credit and in higher interest rates for consumers." The banks even won the support of a key federal regulator, the Office of Comptroller of the Currency. "We believe that particular aspects of the Proposed Rule," said Comptroller (and former bank lawyer) John Dugan, speaking of a narrower proposal later partly incorporated into the CARD act, "would have unintended and undesirable consequences" for consumers and "could result in a significant reduction in credit availability."

By 2009, when the Senate took up this legislation, unfair credit-card practices had become a source of mounting consumer discontent, and some lawmakers were clearly skeptical of industry claims. Even with closer regulation, credit cards would continue to be a highly profitable business, Senator Jeff Bingaman (D-NM) predicted, adding that "I don't think there'll be any shortage of companies willing to provide new credit cards."

RESULTS: Events bore him out. Despite continued industry opposition, the CARD Act was approved by Congress and signed into law in May 2009. Five years later, economist Neale Mahoney took part in a study of its impact. Mahoney approached that question as a skeptic: if credit card companies had to reduce certain charges, they would respond by raising others, he assumed, and the net effect would be a wash.

But that's not what the data showed. Mahoney and his collaborators – Sumit Agarwal of the National University of Singapore, Souphala Chomsisengphet of the Office of the Comptroller of the Currency, and Johannes Stroebel of New York University's Stern School of Business – found "no evidence of an increase in interest charges or a reduction in access to credit." While credit cards continued to be a highly profitable part of the banking business, the legislation had saved American consumers more than $20 billion a year, they concluded.

The CARD Act had led not only to lower fees and interest charges, but also to a narrowing of the gap between stated interest rates and the actual rates that people wound up paying. "While credit cards aren't entirely free of gotchas, pulling out the plastic is much less perilous than it used to be," wrote the consumer columnist Bob Sullivan, summing up the results.

Case Study Number 2: Predatory Mortgage Reform

ISSUE: During the runup to the financial crisis, federal and state lawmakers advanced a number of proposals to combat booby-trapped or badly underwritten mortgages. Beginning in 2005, U.S. Representatives Brad Miller and Melvin Watt sought backing for a bill modeled on legislation in their home state of North Carolina. Although their proposal evolved over the next few years, its key elements included extra consumer safeguards for loans with high fees or balloon payments and a ban on backdoor rewards (kickbacks, in other words) for brokers who succeeded in getting borrowers to accept loans more costly than their incomes and credit histories warranted.

CLAIMS: In 2007, the House took up a compromise version of the measure. Opponents of what had become known as the Miller-Watt-Frank bill – now that it had gained the support of Representative Barney Frank, the new chairman of the Financial Services Committee – said it would drive subprime lenders from the market, make it harder for low-income families to get credit, and thus "harm the very borrowers that we all wish to protect," as John Robbins, chairman of the Mortgage Bankers Association, told a House subcommittee.

The National Association of Mortgage Brokers agreed. Such proposals "could actually harm the consumer by restricting the choices of loan products, terms, and originators available in the market," the brokers' group said,

The Consumer Mortgage Coalition, an alliance of mortgage lenders and servicers, issued a similar warning in a letter to federal bank regulators. "The misfortunes of a few," the coalition said, "should not deprive the many of opportunities to own their own homes and to make their own financial choices …"

By late 2007, loan defaults and foreclosures had reached frightening levels, and Representative Watt urged mortgage lenders to acknowledge the need for tougher regulation "and allow the bill to move forward quickly."

Industry opposition continued, however, and so did the readiness of many of Watt's congressional colleagues to parrot the financial lobby's arguments. "In an attempt to improve conditions in the housing market, this bill instead will likely prevent more hardworking Americans from obtaining a mortgage in a market that is already feeling the pinch," said Representative Marsha Blackburn (R-Tenn.). "They need more help; they do not need roadblocks."

After the Financial Services Committee approved the measure, twelve of its members filed a joint memo of dissent predicting that it would "hurt rather than help the consumers for which it is intended to provide relief." They warned in particular of "dire" effects on "minority applicants and communities," adding that "it would be a true shame if this bill, meant to protect American consumers, were to have the effect of making mortgage credit unavailable to many deserving borrowers who want a piece of the American dream."

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– Rep. Marsha Blackburn, 2007

Representative Hensarling pointed to over-regulation rather than industry misconduct as the big danger. "I just don't want to take the proverbial sledgehammer to the mosquito and bust the wall," he said, belittling the problems that Miller-Watt-Frank sought to remedy.

RESULTS. This debate took place during a period of massive industry fraud. Loans of the kind the proposed legislation sought to prohibit would soon be at the heart of a financial and economic disaster – one that cost millions of Americans their homes or jobs (or both) and stripped millions of others of much of their income and household wealth. The damage to communities of color was especially severe: between 2005 and 2009, African-Americans experienced a decline in household wealth of 53 percent, and Latinos a decline of 66 percent, according to Census Bureau data analyzed by Pew Charitable Trusts.

The financial crisis of 2008 was a product of inaction by regulators as well as lawmakers. One especially influential regulator was Federal Reserve Board chairman Alan Greenspan, who refused to exercise powers his agency already possessed, invoking the industry's arguments to explain why.

Under the Home Ownership and Equity Protection Act of 1994, the Fed had the authority to act against predatory mortgage lending. Yet even as Wall Street was building a global house of cards out of securities and derivatives linked to suspect loans, Greenspan ignored repeated appeals from housing advocates, lawmakers, and an outspoken Fed board member. Instead of calling out the financial industry for its gambling spree, he stuck to his anti-regulation guns, declaring lenders and bankers to be fully capable of monitoring their own risks.

In a 2005 speech, Greenspan saluted the American lending industry for what he described as its remarkable ability to “quite efficiently judge the risk posed by individual applicants and to price that risk appropriately.” The Office of Comptroller of the Currency (OCC) went even further, encouraging banks to thumb their noses at officials in the handful of states that were trying to crack down on predatory lending.

The Miller-Watt-Frank bill passed the House in 2007, but stalled in the Senate. Thanks to a combination of congressional and regulatory failure, lenders were able to carry on with many of their deceptive and dangerous practices, and Wall Street continued to feed the market for their loans, compounding the damage when the collapse finally came.

A number of states did act, however, and their efforts made a positive difference, the OCC’s opposition notwithstanding. North Carolina’s law, according to a retrospective analysis by a group of University of North Carolina researchers, led to a sharp reduction in predatory loans, especially in predatory refinancing loans. There was no decline in the number of home purchase loans, however; nor was there any increase in the cost of loans to borrowers with blemished credit. “These findings suggest strongly that the NC Act is doing what it is supposed to do,” the study concluded.

A 2011 study found a similar pattern across the country. Borrowers in states with strong laws – including Massachusetts, New Jersey, New Mexico, New York, North Carolina, and West Virginia – were more carefully vetted and less likely to receive loans with prepayment penalties, balloon payments, and other tricky features; and they faced a significantly lower risk of default or foreclosure.

Case Study Number 3: Regulating Derivatives

ISSUE. In the spring of 1998, the Commodity Futures Trading Commission (CFTC) sounded a warning. It had to do with the rapidly expanding market in over-the-counter derivatives – complex financial instruments modeled on the futures contracts long used by farmers to guard against shifting commodity prices, but linked to the value of currencies, stocks, and bonds. Derivatives had started out as a risk-management tool, but the CFTC and its Chair, Brooksley Born, were troubled by the growing number of traders who, with little or no direct stake in the underlying assets, seemed to be treating the derivatives market as a betting casino. Because that market operated in an unregulated netherworld between commodity futures (the CFTC’s established area of jurisdiction) and ordinary corporate securities (the province of the SEC), Born and her colleagues worried that there was no way to know the magnitude of the risks being assumed, and no way to tell whether the contracting parties would be able to pay up if their bets went seriously wrong.

Foreseeing a risk of "grave dangers to our economy" if the market remained unregulated and opaque, Born's little-known agency put out a paper outlining plans to study the problem and, if necessary, impose safeguards similar to those already in place for traditional futures.

Reckless derivatives bets had already played a part in the 1994 bankruptcy of Orange County, California, as they soon would in the collapse of the so-called "genius" hedge fund, Long-Term Capital Management. Nevertheless, the financial industry responded with scorn to the CFTC's proposal, and unfortunately for Born – and for the country – she had raised the issue at a time, much like now, when Wall Street held Washington in its thrall.

Soon after her announcement, Born got off a phone call with Deputy Treasury Secretary Lawrence Summers looking "ashen-faced," a colleague would remember later. Summers, she reported, had told her he had "13 bankers in his office" saying "Stop, right away. No more.'" That was Summers' own message, too, and it was echoed by two of the other heavyweights of U.S. economic policy at the time, Federal Reserve Board Chairman Alan Greenspan and Treasury Secretary Robert Rubin.

Derivatives traders "simply do not require the customer protections that may be needed by the general public. Regulation that serves no useful purpose hinders the efficiency of markets to enlarge standards of living."

– Alan Greenspan, 1998

CLAIMS. Born got an earful from Greenspan, Rubin, Summers *and* the banks, and they all told essentially the same story, portraying derivatives as the cutting edge of a dynamic and innovative financial industry, which they seemed to equate with a dynamic and innovative U.S. economy. "OTC derivatives directly and indirectly support higher investment and growth in living standards in the United States and around the world," a presidential working group declared in a counter-paper issued the following spring.

At a congressional hearing on the issue, Greenspan called for a "standstill" of the CFTC's efforts. There was no need for regulation, he said, because the over-the-counter derivatives market involved sophisticated, well-resourced companies and individuals – Wall Street "professionals" who "simply do not require the customer protections that may be needed by the general public." Regulation was not just unnecessary, but dangerous: it was a threat to America's global economic competitiveness since, Greenspan pointed out at another hearing, "Already the largest futures exchange in the world is no longer in America's heartland. Instead, it is now in the heart of Europe."

In the name of averting an imaginary peril, in other words, Born was proposing measures that could cause a real one, according to these more influential authorities. Summers, Born recalled, accused her of setting the U.S. up for "the worst financial crisis since the end of World War Two."

So great was the supposed threat, in the view of Born's critics, that it was not enough merely to persuade the CFTC to back off. The Treasury Department, congressional leaders, and Wall Street lobbyists mounted a campaign for legislation – the Commodity Futures Modernization Act – guaranteeing the ability of the big banks and their counter-parties to go on making derivatives deals without fear of regulatory interference.

RESULTS. There is no way to know how the kind of measures Born envisioned might have affected the course of events. But we do know what happened after Congress wrapped the Commodity Futures Modernization Act into a giant appropriations bill that passed with little debate or dissent in the closing months of 2000.

Proponents of that measure argued that the derivatives market needed formal legal protection in order to continue growing. And grow it did, by leaps and bounds. On the eve of the 2008 financial crisis, banks, hedge funds, public pension funds, and investors around the world were on the hook for hundreds of trillions of dollars in potential obligations, tied in far too many cases to the value of fraudulent and unaffordable U.S. mortgages.

When the market crashed, those commitments were the undoing of Bear Stearns and Lehman Brothers. They helped propel the biggest commercial banks and investment banks, along with giant nonbanks like American International Group, to the edge of collapse – a fate averted only with the infusion of trillions of taxpayer dollars. And they played a huge part in triggering the very outcome that Summers had warned against: "the worst financial crisis since the end of World War Two."

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Nine years later, that disaster remains fresh in our national memory, along with the massive recklessness, deceit and fraud that led to it. Even as millions of American families still struggle to dig out from the wreckage, however, the financial industry has shown a remarkable ability to overlook its own misdeeds as it spins a story about financial regulation as the source of our current economic woes, and about a fresh round of deregulation as a formula for recovery.

These claims would be remarkable, that is, if we had not been hearing the same arguments from bankers, lenders, and their friends and hirelings, with robotic repetition and little or no regard for the evidence, year after year. So there is no reason to be surprised by what they're saying. But there should be no excuse for anyone not on their payroll to believe them.