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CONGRESSIONAL TESTIMONY

Regulatory Reforms to Create Hope and Opportunity for Investors, Consumers, and Entrepreneurs

Testimony before the
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Norbert J. Michel, PhD
Senior Research Fellow in Financial Regulations and Monetary Policy
The Heritage Foundation

Chairman Hensarling, Ranking Member Waters, and Members of the Committee, thank you for the opportunity to testify at today's hearing. My name is Norbert Michel and I am a Senior Research Fellow in Financial Regulations and Monetary Policy at The Heritage Foundation. The views I express in this testimony are my own, and should not be construed as representing any official position of The Heritage Foundation.

The 2010 Dodd–Frank Wall Street Reform and Consumer Protection Act spawned approximately 400 separate rulemakings across the financial sector, and was the most extensive financial regulatory bill since the 1930s.[1] It expanded the existing authority of the federal regulators who missed the 2008 financial crisis, created new federal agencies, and dramatically altered the regulatory framework for several distinct sectors within the financial industry.[2] Dodd–Frank failed to adequately address the causes of the crisis, imposed unnecessarily high compliance burdens on firms, worsened the too-big-to-fail problem, and contributed to the unusually sluggish recovery. It extended command-control-type regulation well beyond the banking sector even though this approach has repeatedly failed to keep the banking system sound.

My Heritage Foundation colleague, Salim Furth, and I have used a standard macroeconomic model to quantify the benefits of reducing one of the likely effects of Dodd–Frank: excess borrowing costs.[3] After estimating that these excess borrowing costs are 22 basis points, we estimate that removing this "investment wedge" would have a measurable positive impact on the economy, and that legislation repealing Dodd–Frank would have a budgetary impact that triggers a dynamic score from the Congressional Budget Office.

Our estimates of this Dodd–Frank "repeal" scenario predict that, on average from 2017 to 2026, removing the investment wedge would increase gross domestic product (GDP) 1 percent per year, increase the capital stock by almost 3 percent per year, and decrease the federal debt ratio by nearly 1 percent per year. The model estimates between $64 billion and $340 billion in 10-year revenue gains from removing the investment wedge, and revenue gains between $202 billion and $817 billion over a 20-year horizon.

Ideally, Congress would repeal the Dodd–Frank Act and focus, instead, on policies that improve private incentives in financial markets, increase competition in financial markets, and reduce the ability for private financial firms to mitigate losses with government backing.[4] This testimony focuses on three aspects of the financial regulatory framework that Congress should focus on to strengthen private financial markets and help spur sustainable economic growth. Specifically, it argues that Congress should (1) require

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[1] Ayesha Javed, "Six Years On, 30% of Dodd–Frank Rules Yet to Be Finalized," Bloomberg, July 28, 2016, https://www.bloomberg.com/enterprise/blog/six-years-30-dodd-frank-rules-yet-finalized/ (accessed March 10, 2017).

[2] For a title-by-title examination of Dodd–Frank, see Norbert J. Michel, ed., *The Case Against Dodd–Frank: How the "Consumer Protection" Law Endangers Americans* (Washington, DC: The Heritage Foundation, 2016), http://thf-reports.s3.amazonaws.com/2016/The%20Case%20Against%20Dodd-Frank.pdf.

[3] Norbert J. Michel and Salim Furth, "The Macroeconomic Impact of Dodd–Frank—and of Its Repeal," Heritage Foundation *Issue Brief* No. 4682, April 13, 2017, http://www.heritage.org/sites/default/files/2017-04/IB4682.pdf.

[4] For additional policies that accomplish these goals, see Norbert J. Michel, ed., *Prosperity Unleashed: Smarter Financial Regulation* (Washington, DC: The Heritage Foundation, 2017), http://www.heritage.org/government-regulation/report/fixing-the-regulatory-framework-derivatives, and Michel, *The Case Against Dodd–Frank: How the "Consumer Protection" Law Endangers Americans*.

all failing financial firms to go through bankruptcy; (2) eliminate the Consumer Financial Protection Bureau; and (3) repeal the Durbin Amendment.

Improvements to Bankruptcy Law

Largely due to systemic risk concerns, the current regulatory framework holds depository institutions and certain large financial institutions out of the Chapter 11 bankruptcy proceedings available to non-financial firms. These financial institutions are given special resolution processes under the premise that it will help protect taxpayers, keep financial markets stable, and prevent financial crises from spreading to the broader economy. This policy is a mistake that should be corrected by allowing all firms, banks included, to go through bankruptcy.[5] Aside from the lack of evidence that these special resolution procedures can prevent systemic risks from spreading to the broader economy, there is no objective way to differentiate the economic impact of large failing financial institutions from those of large non-financial firms.

Furthermore, the core idea behind the Chapter 11 bankruptcy process that is open to non-financial firms is that those proceedings will create an orderly wind down of the company, enabling the distressed firm to remain in business and pay its creditors what they are owed over time in an equitable and orderly manner. The process is designed to avoid a mad rush of creditors seeking the money the failed firm owes them in a chaotic manner. The fact that banks have insured depositors is entirely consistent with this type of orderly resolution process.

There has never been a clear economic reason that this process would create systemic problems if it were open to financial firms, and a main problem with the pre-2008 crisis framework was that the bankruptcy code included special exemptions (safe harbors) for derivatives and repurchase agreements (repos). These safe harbors from core bankruptcy provisions distorted financial markets leading up to the 2008 crisis because they gave derivative and repo users preferred positions relative to other types of creditors. The safe harbors were justified on the grounds that they would prevent systemic financial problems, but that theory proved false in 2008.[6]

A firm (the debtor) that files for bankruptcy protection under Chapter 11 of the U.S. Code literally makes this filing to gain protection from creditors who may seek control of the firm's assets because they fear nonpayment. The court creates an "estate" that consists of virtually all of the debtor's assets as of the petition date. To ensure that the estate remains a viable business, the bankruptcy filing triggers a provision known as the automatic stay, a kind of financial time-out. The stay even prohibits secured creditors from selling or seizing the collateral (cash or securities) they hold, and it remains in effect until a bankruptcy judge—sort of a referee in the process—says otherwise. The debtor and the creditors then begin a coordinated effort to resolve the debtor's financial situation equitably across similar creditors.

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[5]Given the current system of federally backed deposit insurance administered by the Federal Deposit Insurance Corporation (FDIC), bank resolutions would likely require some form of special resolution procedures in combination with bankruptcy-type procedures. These resolution processes are beyond the scope of this testimony. For additional information, see Mark Calabria, "Deposit Insurance, Bank Resolution, and Market Discipline," in Michel, *Prosperity Unleashed: Smarter Financial Regulation*.
[6]This section is based largely on Norbert J. Michel, "Fixing the Regulatory Framework for Derivatives," in Michel, *Prosperity Unleashed: Smarter Financial Regulation*; the chapter includes many additional citations of supporting evidence.

The automatic stay is a key part of the process but it is one of several key components. The following is a list of other key bankruptcy provisions.

- **A set off provision.** Creditors generally have to seek the court's permission to set off what they owe the debtor against any amounts the debtor may owe them.
- **A prohibition on preferential transfers.** The debtor (or a court-appointed trustee) can generally force creditors to return any preferential transfers. For instance, a creditor may have to return a payment made within 90 days of bankruptcy if that payment would have made the creditor better off than had the transfer not been made. The amount would have to be returned to the estate so that it would improve the collective position of the creditors.
- **A prohibition on fraudulent (and constructive) conveyances.** Sales or transfers of assets at less than fair value within two years of the filing date can be reversed to benefit all creditors.
- **Nullification of ipso facto clauses.** Creditors are generally prohibited from terminating their contracts with the debtor simply because the firm filed for bankruptcy protection. In fact, even if a contract includes a clause that makes the debtor's bankruptcy a default (an ipso facto clause), the clause is generally not enforceable.

Many creditors do not like these protections because a bankruptcy filing strips them of contractual rights that they would normally have. Naturally, all creditors of a failing firm want their money first, before the value of the aggregate claims necessarily declines. So it is no surprise that these protections have been whittled down through time, and that there are various safe harbors from these bankruptcy provisions. Interestingly, derivatives and repo counterparties have one of the best deals of any group: They have safe harbors from all five of the key protections discussed above, leaving them in a preferred position relative to ordinary creditors.

These counterparties were given the safe harbors under the theory that doing so would help mitigate systemic risk. Essentially, the idea was that the safe harbors were necessary to prevent counterparties from "running," so as to prevent the derivatives markets from "seizing up" (perhaps because of rapidly declining asset prices). Lobbyists began making very vague arguments to this effect in the 1980s, and safe harbors expanded slowly until 2005. The 2005 Bankruptcy Abuse Prevention and Consumer Protection Act expanded these safe harbors for essentially any derivative or repo user, and turned all sorts of mortgage-related securities into, for legal purposes, repos.

As a result, starting in 2005, any derivative or repo user enjoyed safe harbors from all five of these key bankruptcy protections. Thus unlike ordinary creditors, derivatives and repo counterparties, could, for example, terminate their contract immediately upon a debtor filing bankruptcy, and seize and sell collateral. Proponents of these special exemptions have argued that safe harbors allow counterparties to quickly cancel contracts and enter new hedges (with other counterparties), thus ensuring their financial health and avoiding financial market distress.

A major problem with this story, aside from the empirical record, is that even systemic risk concerns cannot possibly justify blanket safe harbors for the entire market.[7]

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[7]The Federal Deposit Insurance Corporation (FDIC) has for decades implemented a special failure-resolution process for banks that imposes a one-day stay on a bank's derivative and repo counterparties, making the case for economy-wide safe harbors even less compelling.

At best, only the largest counterparties would get safe harbors, a fact that makes it clear safe harbors necessarily provide preferential treatment to certain creditors over others.[8] Furthermore, the evidence does not support that this preferential treatment works to mitigate systemic risk—it shows the opposite. As the 2008 crisis was unfolding, Bear Stearns's counterparties ran before Bear was even considering bankruptcy, AIG's counterparties increasingly demanded additional collateral for its Credit Default Swaps (CDS), and JP Morgan seized $17 billion in securities and cash (collateral) from Lehman before the bankruptcy filing *and* demanded an additional $5 billion.

Lehman effectively had no choice but to come up with the additional collateral, thus worsening its liquidity position, because it knew that it could not file for protection to get the collateral back. The lead attorney in the Lehman bankruptcy case also testified to Congress that the lack of an automatic stay contributed to confusion at the outset of the filing. Aside from the added incentive to run, the safe harbors likely induced firms to rely more heavily on derivatives and repos than they would have in absence of the special protections. For instance, Bear Stearns's liabilities consisted of only 7 percent repos in 1990, but by 2008 they consisted of 25 percent repos. Data also show that the portion of total investment bank assets financed by repos doubled between 2000 and 2007.

Whether the growing market led to legislative action to further support the market, or whether the legislative amendments to the bankruptcy code led to the growing market is irrelevant. Regardless, the market would not have supported such high increases in leverage without the special protections, which is precisely why the safe harbors should not be provided. The safe harbors also lead to more subtle adverse effects, such as diminishing the incentive to monitor counterparties and to prepare (or even file) for bankruptcy.

It is certainly true that eliminating these safe harbors may cause firms to rely less on these short-term debt instruments, and to price in higher risks than they do currently. This outcome is not a market failure: It is precisely how competitive markets function when the participants have the proper incentives to monitor their risks. The Financial CHOICE[9] Act implements an improved bankruptcy process for large financial firms by adopting the text of H.R. 2947, the Financial Institution Bankruptcy Act of 2016. This change would improve the status quo by subjecting derivatives and repos to an automatic 48-hour stay. Such an improvement is welcome, but the complete elimination of the exemption and all safe harbors that derivatives and repos enjoy would be optimal. Such a change would strengthen private markets by maximizing the benefits of increased competition and lowering reliance on government preferences that mitigate private firms' financial losses.

The Consumer Financial Protection Bureau

Title X of Dodd–Frank created the CFPB by transferring enforcement authority for 22 specific consumer financial protection statutes to the new agency and by codifying

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[8] In 1983, Fed Chair Paul Volcker suggested a safe harbor was necessary to protect the repo market given that repos were a main tool of monetary policy. Volcker also argued that limiting these special protections to repo transactions of $1 million or more would suffice, thus avoiding the need to provide broad exceptions to existing bankruptcy laws.

[9] The acronym CHOICE stands for Creating Hope and Opportunity for Investors, Consumers and Entrepreneurs.

a new, ill-defined type of consumer protection. The fact that Title X transferred these statutes shows that there was no shortage of consumer financial protection prior to the creation of the CFPB. Given that the authority for approximately 50 rules and orders stemming from more than 20 federal statutes was divided among seven federal agencies, all layered on top of state-based consumer-protection laws, perhaps consolidating federal authority in one agency could have improved consumer-protection enforcement.

The CFPB's proponents never made the case, however, that creating another federal agency would provide such an improvement. Regardless, Dodd–Frank created the CFPB by going well beyond simply consolidating enforcement authority for these federal statutes. Dodd–Frank consolidated some federal consumer financial protection authority in the CFPB,[10] gave the CFPB supervisory authority, expanded the concept of consumer protection, and gave the CFPB a controversial structure dissimilar from the typical federal agency.

Pre-Dodd–Frank Consumer-Protection Framework. Prior to the late 1960s, consumer protection in credit markets was largely a function of state government.[11] In 1968, Congress began to move further into the long-standing province of the states in regulating consumer transactions with passage of the Consumer Credit Protection Act (CCPA).[12] Title I of the CCPA, the Truth in Lending Act (TILA), mandated disclosure of credit charges "clearly and conspicuously" as specified by the Federal Reserve System.[13] As declared by Congress, the purpose of the TILA was to "assure a meaningful disclosure of credit terms"[14] rather than dictate the conduct of lenders or the content of loans agreements. The TILA is still a major component of federal consumer-protection law,[15] but it is just one of many statutes passed after 1968. The following list describes the major federal consumer financial protection statutes enacted in the 10 years following the TILA.[16]

- **The 1970 Fair Credit Reporting Act (FCRA).**[17] The main purpose of the FCRA was to "require that consumer reporting agencies adopt reasonable procedures for

[10]In creating the CFPB, Congress transferred consumer financial protections from the Federal Reserve, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Department of Housing and Urban Development. See 12 U.S. Code § 5581 (delineating the transfer of consumer financial services functions to the CFPB), and Federal Trade Commission, "Consumer Finance," 2016 (explaining that the FTC shares authority with the CFPB to enforce the consumer-protection laws with respect to non-bank financial institutions ranging from mortgage brokers to debt collection firms), https://www.ftc.gov/news-events/media-resources/consumer-finance (accessed March 27, 2017).
[11]Thomas A. Durkin, Gregory Elliehausen, Michael Staten, and Toddy Zywicki, *Consumer Credit and the American Economy* (Oxford, England: Oxford University Press, 2014), p. 417.
[12]Consumer Credit Protection Act (CCPA) of 1968, Public Law 90–321.
[13]The Federal Reserve's implementing regulation for TILA is known as Regulation Z. The Dodd–Frank Act transferred authority for enforcing Regulation Z, now found at 12 C.F.R. Part 226, to the CFPB.
[14]15 U.S. Code § 1601.
[15]Budnitz, "The Development of Consumer Protection Law."
[16]A more complete list of consumer-protection statutes transferred to the CFPB is in Dodd–Frank Title X, Subtitle H.
[17]The Fair Credit Reporting Act, codified to 15 U.S. Code § 1681, was Title VI of Public Law 91–507. This law, commonly referred to as the Bank Secrecy Act of 1970, required, among other things, "insured

meeting the needs of commerce for consumer credit, personnel, insurance, and other information in a manner which is fair and equitable to the consumer."[18]

- **The 1974 Real Estate Settlement Procedures Act of 1974 (RESPA).**[19] The RESPA was passed largely to see that borrowers "are provided with greater and more timely information on the nature and costs of the settlement process and are protected from unnecessarily high settlement charges."[20]
- **The 1974 Equal Credit Opportunity Act (ECOA).**[21] The ECOA was intended to promote adequate disclosure of information to and about credit consumers, and also to shield protected classes of consumers from discrimination when applying for credit.[22]
- **The Privacy Act of 1974.**[23] The Privacy Act established a code of fair information practices to govern the collection, maintenance, use, and dissemination of information about individuals that is maintained in systems of records by federal agencies.
- **The 1974 Fair Credit Billing Act.**[24] The Fair Credit Billing Act amended the TILA "to protect the consumer against inaccurate and unfair credit billing and credit card practices."[25]
- **The 1975 Home Mortgage Disclosure Act of 1975 (HMDA).**[26] A primary goal of the HMDA was to "provide the citizens and public officials of the United States with sufficient information to enable them to determine whether depository institutions are filling their obligations to serve the housing needs of the communities and neighborhoods in which they are located."[27]
- **The 1978 Electronic Fund Transfer Act of 1978 (EFTA).**[28] The purpose of the EFTA was to protect individual consumers engaging in electronic fund transfers, such as transfers through automated teller machines, point-of-sale terminals, telephone bill-payment plans, and remote-banking programs.[29]

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banks to maintain certain records," and "certain transactions in United States currency be reported to the Department of the Treasury."

[18] Fair Credit Reporting Act § 602; 15 U.S. Code § 1681(b).

[19] Public Law 93–533, 88 Stat. 1724, codified to 12 U.S. Code § 2601.

[20] 12 U.S. Code § 2601 et seq.

[21] The Equal Credit Opportunity Act (ECOA) was Title V of Public Law 93–495, an act which, among other things, established a National Commission on Electronic Fund Transfers. The ECOA is codified at 15 U.S. Code § 1691.

[22] For an overview of policy concerns, see John Matheson, "The Equal Credit Opportunity Act: A Functional Failure," *Harvard Journal on Legislation*, Vol. 21 (1984), p. 371, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1874297 (accessed September 30, 2016).

[23] Public Law 93–579, 88 Stat. 1896; 5 U.S. Code § 552a.

[24] The Fair Credit Billing Act was Title III of Public Law 93–495, and it is codified to 15 U.S. Code § 1601.

[25] Fair Credit Billing Act § 302; 15 U.S. Code § 1601(a).

[26] The Home Mortgage Disclosure Act of 1975 was Title III of Public Law 94–200, codified to 12 U.S. Code § 2801.

[27] Home Mortgage Disclosure Act § 302(b).

[28] 15 U.S. Code § 1693 et seq.; the Electronic Funds Transfer Act was Title XX of the Financial Institutions Regulatory and Interest Rate Control Act of 1978 (Public Law 95−630; 92 Statute 3641).

[29] Dodd−Frank transferred rulemaking authority under the EFTA from the Fed Board of Governors to the CFPB.

For decades, this combined state-federal legal framework governed the offering of consumer credit and outlawed *deceptive* and *unfair* practices in financial products and services. Even Senator Elizabeth Warren (D–MA), the intellectual architect of the CFPB, has acknowledged this fact, stating "credit transactions have been regulated by statute or common law since the founding of the Republic."[30] Simply put, there was no dearth of consumer-protection law in financial markets.

Radical Shift in Consumer Protection. For decades prior to the financial crisis, consumer-protection laws required disclosure of key mortgage terms and prohibited deceptive and unfair practices. The Federal Trade Commission (FTC) was the primary federal consumer-protection agency outside banking, while banking regulators were primarily responsible for consumer protection in depository institutions. Under this framework, it was illegal for businesses to engage in *deceptive* or *unfair* practices when marketing their offerings to consumers. The Federal Trade Commission Act (15 U.S. Code 41 et seq.) was amended in 1938 to prohibit "unfair or deceptive acts or practices."[31] Federal banking regulators, including the Federal Deposit Insurance Corporation (FDIC), the Federal Reserve Board, the Comptroller of the Currency, and the National Credit Union Administration, had authority to enforce unfair or deceptive acts or practices in or affecting commerce under their statutes in a manner consistent with carefully crafted FTC limiting principles applicable to *unfairness* and *deception*.[32]

Title X of Dodd–Frank empowers the CFPB "to exercise its authorities under Federal consumer financial law for the purposes of ensuring that, with respect to consumer financial products and services, consumers are protected from unfair, deceptive, *or abusive* acts and practices."[33] (Emphasis added.) The statute does not define the term *abusive*, but it characterizes as abusive any action that materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service, or takes unreasonable advantage of any of the following:

1.) A lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;
2.) The inability of the consumer to protect its interests in selecting or using a consumer financial product or service; or,
3.) The reasonable reliance by the consumer on a covered person to act in the

[30]Elizabeth Warren, "Unsafe at Any Rate," *Democracy Journal* (Summer 2007), http://democracyjournal.org/magazine/5/unsafe-at-any-rate/ (accessed March 27, 2017).
[31]See, generally, Federal Trade Commission, "Bureau of Consumer Protection," https://www.ftc.gov/about-ftc/bureaus-offices/bureau-consumer-protection (accessed November 4, 2016).
[32]See 15 U.S. Code § 45(n) (defining "unfairness"). See also Federal Trade Commission, FTC Policy Statement on Unfairness, 104 F.T.C. 949, 1070 (1984), https://www.ftc.gov/public-statements/1980/12/ftc-policy-statement-unfairness (accessed March 31, 2017), and Federal Trade Commission, FTC Policy Statement on Deception, 103 F.T.C. 110, 174 (1984), https://www.ftc.gov/public-statements/1983/10/ftc-policy-statement-deception (accessed March 31, 2017). See also, e.g., FDIC Compliance Manual, Chapter 7 (Federal Trade Commission Act, Section 5 Unfair or Deceptive Acts or Practices), https://www.fdic.gov/regulations/compliance/manual/7/VII-1.1.pdf (accessed March 31, 2017).
[33]Dodd–Frank, Section 1021, 12 U.S. Code § 5511.

interests of the consumer.[34]

The agency has issued neither guidance nor rules to define abusive practices, but, presumably, such practices are something other than unfair or deceptive practices. Furthermore, CFPB officials have not shown much willingness to provide clarity—even when asked explicitly to do so by Congress. During a 2012 hearing of the House Financial Services Committee, for example, when asked by lawmakers to define "abusive," CFPB Director Richard Cordray said:

> the term abusive in the statute is…a little bit of a puzzle because it is a new term.... We have been looking at it, trying to understand it, and we have determined that that is going to have to be a fact and circumstances issue; it is not something we are likely to be able to define in the abstract. Probably not useful to try to define a term like that in the abstract; we are going to have to see what kind of situations may arise.[35]

Under this framework, financial firms must operate under a vague legal standard to which they might never be able to adhere. Aside from the near impossibility of complying with such an unclear standard for abusive acts or practices, there is no objective way to measure a consumer's ability to understand terms and conditions of financial products and services.[36] Forcing financial firms into such a role, where they are effectively required to verify consumers' understanding of terms rather than merely disclosing relevant information, goes well beyond the long-established consumer-protection framework. This change is based on a hostile view of free enterprise, puts little faith in individuals' ability to understand their world, and comes dangerously close to absolving one party—the borrower—in a financial contract from any real responsibility.

The Obama Administration and congressional Democrats regularly blamed the financial crisis on firms that exploited consumers, thus flooding the market with mortgages that lenders knew would not be repaid.[37] Because deliberately deceiving borrowers was illegal under existing law, this narrative relied on the claim that consumers could not understand that these mortgages were dangerous. One problem with this explanation is that it falsely assumes that mortgage contracts themselves are dangerous, thus mitigating the counterparties' responsibility to uphold their contractual obligations.

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[34] Dodd–Frank, Section 1031, 12 U.S. Code § 5531.

[35] "How Will the CFPB Function Under Richard Cordray," transcript of hearing before the Subcommittee on TARP, Financial Services, and Bailouts of Public and Private Programs, Committee on Oversight and Government Reform, U.S. House of Representatives, January 24, 2012, http://oversight.house.gov/wp-content/uploads/2012/06/01-24-12-Subcommittee-on-TARP-Financial-Services-and-Bailouts-of-Public-and-Private-Programs-Hearing-Transcript.pdf (accessed March 31, 2017).

[36] See Katz, "Title X and the Consumer Financial Protection Bureau: Limiting Americans' Credit Choices"; Todd Zywicki, "The Consumer Financial Protection Bureau: Savior or Menace?"; and Diane Katz, "The CFPB in Action: Consumer Bureau Harms Those It Claims to Protect," Heritage Foundation *Backgrounder* No. 2760, January 22, 2103, http://www.heritage.org/housing/report/the-cfpb-action-consumer-bureau-harms-those-it-claims-protect#_ftn11.

[37] See, for example, U.S. Department of the Treasury, "Financial Regulatory Reform: A New Foundation—Rebuilding Financial Supervision and Regulation," June 17, 2009, p. 55, https://www.treasury.gov/initiatives/wsr/Documents/FinalReport_web.pdf (accessed March 25, 2017).

Another problem is that it assumes borrows cannot understand which products and services are good for them, but that regulators and elected officials can.

In the words of Oren Bar-Gill and Elizabeth Warren, the academic architects of the CFPB, borrowers suffer "cognitive limitations" and borrowers' "learning is imperfect."[38] This explanation is fatally flawed because it ignores that regulators and elected officials must suffer from the same cognitive limitations as borrowers. Ignoring this fact, it necessitates that federal regulators—not lenders and borrowers—determine which types of loans are acceptable, thus restricting both the supply and demand sides of credit markets, as well as individuals' freedom to enter into contracts of their choosing.

Unaccountable Structure Inconsistent with Rule of Law. Dodd–Frank gave the CFPB wide-ranging supervisory, enforcement, and rulemaking authority over banks and non-bank financial firms.[39] With so much overlapping authority prior to Dodd–Frank, it is difficult to argue that adding yet another regulatory agency could have improved the pre-Dodd–Frank framework. Not only did Dodd–Frank give the CFPB the power to regulate terms and marketing of virtually every consumer credit product, even those already regulated, under the guise of an ill-defined new type of consumer protection, but it made the CFPB a relatively unaccountable regulatory agency. No other federal regulatory agency possesses the same combination of structural features as the CFPB.

Although nominally a part of the Federal Reserve Board, the CFPB is not accountable to the Fed. Technically, the CFPB is classified as an executive agency, but it is more like an independent agency within another independent agency. Rather than an agency headed by a multimember, bipartisan commission, the CFPB is headed by a sole director, appointed for a five-year term by the President, removable only for cause (malfeasance or dereliction of duty), rather than *at will*.[40] Additionally, the CFPB's budget is completely outside the standard Congressional appropriations process and, instead, statutorily set to a fixed percentage of the Federal Reserve's operating budget.[41]

Its actions are also insulated from judicial review by statutorily mandated *Chevron* deference, which requires courts to defer to the CFPB's interpretation of any ambiguous statutory provisions under its jurisdiction, in preference to any competing

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[38] Oren Bar-Gill and Elizabeth Warren, "Making Credit Safer," *University of Pennsylvania Law Review*, Vol. 157, No. 1 (November 2008), https://www.law.upenn.edu/live/files/112-bargillwarren157upalrev12008pdf (accessed December 21, 2016).

[39] Dodd–Frank §§ 1022, 1024, 1025, and 1026, codified at 12 U.S. Code §§ 5512, 5514, 5515, and 5516.

[40] In a recent case, a federal court asked the CFPB to identify all "historical or current examples it could find of independent agencies headed by a single person removable only for cause." The Bureau was able to identify only three examples: the Social Security Administration, the Office of Special Counsel, and the Federal Housing Finance Agency (created in 2008). See *PHH Corporation, Et Al., Petitioners V. Consumer Financial Protection Bureau, Respondent*, U.S. Court of Appeals, District of Columbia Circuit, October 11, 2016, p. 29, https://www.cadc.uscourts.gov/internet/opinions.nsf/AAC6BFFC4C42614C852580490053C38B/$file/15-1177-1640101.pdf (accessed April 22, 2017).

[41] This was 12 percent in FY 2015 for a total of $618.7 million. See CFPB, "Financial Report of the Consumer Financial Protection Bureau," November 16, 2015, http://files.consumerfinance.gov/f/201511_cfpb_report_fiscal-year-2015.pdf (accessed February 22, 2016).

interpretations by other agencies.[42] CFPB proponents deny any lack of accountability by pointing out that the Financial Stability Oversight Council (FSOC) can veto the CFPB's rules, but the FSOC's oversight authority is very narrow.

The Dodd–Frank Act authorizes any member agency of the FSOC to petition the FSOC to set aside a regulation provided that the agency follows specific conditions set forth in Section 1023 of Dodd–Frank.[43] For example, Treasury, as a member agency of the FSOC, can petition the FSOC to set aside a final rule provided the FSOC decides "that the regulation or provision would put the safety and soundness of the United States banking system or the stability of the financial system of the United States at risk."[44] A member of the FSOC can petition the FSOC for a 90-day stay of a rule (or to set aside such rule) provided that the member:

> (A) In good faith attempted to work with the Bureau to resolve concerns regarding the effect of the rule on the safety and soundness of the United States banking system or the stability of the financial system of the United States;[45] and
> (B) Files the petition with the Council not later than 10 days after the date on which the regulation has been published in the Federal Register.[46]

Any veto of the CFPB rule would then require the approval of two-thirds of the members serving on the FSOC. It is clear that the CFPB was designed to evade the checks and balances that apply to most other regulatory agencies. The recent PHH[47] and Ally Financial cases exemplify why so much authority should not be given to any type of independent regulatory agency and how doing so can harm competitive private markets without any clear benefit.

In the case of PHH, a financial firm offering a full range of residential mortgage services, the CFPB selected a company for investigation, and then alleged that the company had violated Section 8 of RESPA by taking reinsurance fees as kickbacks. Despite previous Housing and Urban Development Department guidance that suggested PHH's practices were fully within the rules and regulations, the CFPB inserted its own interpretation of the law and assigned an administrative law judge (ALJ) to an

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42Todd J. Zywicki, "The Consumer Financial Protection Bureau: Savior or Menace?" *George Washington Law Review*, Vol. 81, No. 3 (April 2013), p. 856, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2130942 (accessed August 16, 2016). Also see Paul Larkin, "The World After Chevron," Heritage Foundation *Legal Memorandum* No. 186, September 8, 2016, http://www.heritage.org/research/reports/2016/09/the-world-after-chevron; Diane Katz, "The CFPB in Action: Consumer Bureau Harms Those It Claims to Protect," Heritage Foundation *Backgrounder* No. 2760, January 22, 2013, http://www.heritage.org/research/reports/2013/01/the-cfpb-in-action-consumer-bureau-harms-those-it-claims-to-protect; and Diane Katz, "Consumer Financial Protection Bureau: Limiting Americans' Credit Choices," Heritage Foundation *Backgrounder* No. 3102, April 28, 2016, http://www.heritage.org/research/reports/2016/04/consumer-financial-protection-bureau-limiting-americans-credit-choices.

43Section 1023(f) authorized the FSOC to prescribe procedural rules to implement this section of Dodd–Frank, but the FSOC has not issued these rules.

44Dodd–Frank, § 1023(a).

45Dodd–Frank, § 1023(b)(1)(A).

46Dodd–Frank, § 1023(b)(1)(B).

47PHH corporation was founded in 1946 by Duane Peterson, Harley Howell, and Richard Heather. See https://www.linkedin.com/company/phh-corporation (accessed April 24, 2017).

administrative proceeding rather than initiate a federal court case. The CFPB asserted that the statute of limitations did not apply to administrative proceedings.

After the ALJ's ruling, the CFPB Director decided the ALJ's penalty was too lenient, and he imposed an additional $103 million fine on top of the ALJ's $6.4 million fine. PHH fought the CFPB in court, and a three-judge panel of the Circuit Court of Appeals for the District of Columbia ruled in favor of PHH. The court also ruled that the bureau's single-director model is unconstitutional.[48] The decision states that the unilateral power wielded by CFPB Director Richard Cordray "represents a gross departure from settled historical practice" and "poses a far greater risk of arbitrary decision making and abuse of power, and a far greater threat to individual liberty, than does a multi-member independent agency."[49] The Court further ruled:

> The U.S. government's executive power to enforce federal law against private citizens is essential to societal order and progress, but simultaneously a grave threat to individual liberty. The Framers understood that threat to individual liberty. When designing the executive power, the Framers first separated the executive power from the legislative and judicial powers. To ensure accountability for the exercise of executive power, and help safeguard liberty, the Framers then lodged full responsibility for the executive power in the president of the United States, who is elected by and accountable to the people.[50]

The PHH incident is a clear-cut case of an unaccountable federal agency flouting the basic principles of the rule of law. Private firms—financial or otherwise—cannot safely operate in such an environment without the expectation of being wrongly persecuted by the government that is supposed to protect all of its citizens from such actions.

The CFPB's enforcement actions concerning Ally Financial provide another example of why federal agencies should not be given such independence.[51] In this instance, the CFPB fined Ally for discriminating against minority borrowers even though Ally had no direct contact with the borrowers and despite the fact that the CFPB's method for discovering such racial discrimination did not actually identify the race of the supposedly harmed individuals.[52] No federal agency should be empowered

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[48]For a full timeline of events, including regulatory rulings that predate the PHH case by decades, see Amy Tankersly, "CFPB v. PHH, explained," Housing Wire, October 25, 2016, http://www.inman.com/2016/05/19/cfpb-v-phh-explained/ (accessed April 22, 2017). Also see Diane Katz, "Court Ruling Reins in Unaccountable Financial Regulation Agency," Daily Signal, October 11, 2016, http://dailysignal.com/2016/10/11/court-ruling-reins-in-unaccountable-financial-regulation-agency/?_ga=1.129240399.234929671.1471295889.

[49]*PHH Corporation, Et Al., Petitioners V. Consumer Financial Protection Bureau*, p. 9.

[50]*PHH Corporation, Et Al., Petitioners V. Consumer Financial Protection Bureau*, p. 3.

[51]The problems in this case are magnified by a separate legal overreach known as disparate impact. See Roger Clegg and Hans A. Von Spakovsky, "Disparate Impact Isn't Enough," *National Review*, March 22, 2014, http://www.nationalreview.com/article/373958/disparate-impact-isnt-enough-roger-clegg-hans-von-spakovsky (accessed April 22, 2017).

[52]See AnnaMaria Andriotis and Rachel Louise Ensign, "U.S. Government Uses Race Test for $80 Million in Payments," *The Wall Street Journal*, October 29, 2015, https://www.wsj.com/articles/u-s-uses-race-test-to-decide-who-to-pay-in-ally-auto-loan-pact-1446111002 (accessed April 22, 2017), and Yuka Hayashi, "Consumer Watchdog Pushed Discrimination Case on Vulnerable Firm: Report," *The Wall Street Journal*,

to take these kinds of actions against American citizens, and allowing federal regulators such independence harms the very foundation of free enterprise.

There is no doubt that adequate consumer financial protection existed prior to the 2008 financial crisis—unfair and deceptive practices were illegal. At best, a case can be made for consolidating the various consumer financial protection statutes under one existing federal agency, such as the FTC. However, no compelling case can be made that a new federal agency was—or is—needed to protect consumers from financial fraud. The CHOICE Act greatly improves the status quo by (among other things) making the CFPB director removable at will, putting the agency through the regular appropriations process, eliminating the abusive behavior concept, and relegating the CFPB to an enforcement-only agency. Ultimately, Congress should eliminate the CFPB.

The Durbin Amendment

Congress can further strengthen private markets and maximize the benefits of increased competition by repealing Section 1075 of the Dodd–Frank Act, known as the Durbin Amendment.[53] The Durbin Amendment represents a major policy mistake because, among other deficiencies, it amounts to Congress adjudicating a legal dispute, a role for which it is ill-suited. More than a century ago, with the 1890 Sherman Act, Congress fulfilled its role by creating the basic legal framework for resolving anticompetitive price-fixing disputes.

Congress simply is not designed to be a finder of fact in legal disputes, and there is absolutely no good reason that federal courts should not adjudicate any such dispute over interchange fees. Repealing the Durbin Amendment would be a victory for the rule of law that is consistent with the separation of powers created by the Constitution. The Durbin Amendment also represents a serious policy mistake because it implements price controls, an often-imposed government policy that invariably fails to help the people politicians seek to help.

Section 1075 of Dodd–Frank required the Federal Reserve Board of Governors to cap the debit card interchange fees that large banks charge.[54] These fees, charged to merchants every time consumers swipe their debit cards, have long been a source of controversy. Since the 1980s, as the volume of card transactions increased, retailers have complained that the fees are too high because large banks and card network companies collude to fix prices.[55] Retailers are currently engaged in an antitrust class action lawsuit

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November 24, 2105, https://www.wsj.com/articles/consumer-watchdog-pushed-discrimination-case-on-vulnerable-firm-report-1448404301 (accessed April 22, 2017).

[53]See Norbert J. Michel, "Repealing the Durbin Amendment: A Vote for the Rule of Law," Heritage Foundation *Issue Brief* No. 4644, January 4, 2017 http://thf-reports.s3.amazonaws.com/2017/IssueBriefs/IB4644.pdf.

[54]Section 1075 amended The Electronic Fund Transfer Act (15 U.S. Code § 1693 et seq.).

[55]The share of U.S. consumer expenditures paid for with cards increased from approximately 3 percent in 1986 to 25 percent in 2000, and the controversy over debit card interchange fees grew during this period. James Lyon, "The Interchange Fee Debate: Issues and Economics," *The Region*, Federal Reserve Bank of Minneapolis, June 1, 2006, https://www.minneapolisfed.org/publications/the-region/the-interchange-fee-debate-issues-and-economics (accessed December 23, 2016). Lyon notes that debit and credit cards represented less than 20 percent of noncash payment transactions in 1995, and they exceeded 40 percent of noncash transaction volume by 2003. Also see Brian W. Smith, Abbott B. Lipsky Jr., Andrew J. Robinson, and William J. Rinner, "Why the Market Should Set Credit Card Interchange Fees," Legislative Comment

over *credit* card interchange fees, and it is likely a similar suit would have been filed over *debit* card interchange fees had the Durbin Amendment not been enacted.[56]

Basic Overview of Interchange Fees and Durbin. When retail consumers swipe their debit (or credit) card to make a purchase, it triggers a series of transactions that involve the following clients:

- The retail customer (the cardholder);
- The retail store (the merchant);
- The cardholder's bank (the card-issuing bank);
- The merchant's bank; and
- The network platform (the card association, often Visa, MasterCard, Discover, or American Express).[57]

When a retail customer swipes his card to make a purchase, he signals the merchant's bank to estimate whether he (the cardholder) has enough funds to make the purchase. This electronic information is sent, via the network platform, back to the cardholder's bank, which either authorizes or denies the sale. When the cardholder's bank approves a purchase, it keeps a percentage of the sale amount and then sends the remainder, via the network platform, to the merchant's bank. The network platform and the merchant's bank also keep a percentage of the sale amount for their services.

Collectively, these percentages are referred to as *interchange fees*, and they typically sum to approximately 2 percent.[58] However, the total fees in a debit transaction actually consist of separate fees charged by distinct parties in the transaction. For instance, the card-issuing bank typically charges an "interchange transaction fee."[59] Separately, the card network typically charges both the issuer and the acquiring bank

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in Bank Accounting and Finance, October–November 2008, pp. 39–44, https://www.mastercard.com/us/company/en/docs/Interchangefees.pdf (accessed December 23, 2016).

[56]See *In re Payment Card Interchange Fee and Merchant Discount Antitrust Litigation*, Case 12-4671, Document 1556-1, June 30, 2016, https://www.paymentcardsettlement.com/Content/Documents/Second%20Circuit%20Opinion.pdf (accessed December 29, 2016). Litigation began in 2005, and a federal appeals court recently threw out a $7.25 billion settlement. See Robin Sidel, "Battle Over Cards Heats Up as Court Rejects Visa, MasterCard Deal With Retailers," *The Wall Street Journal*, June 30, 2016, http://www.wsj.com/articles/visa-mastercard-class-action-settlement-rejected-by-u-s-court-1467300658 (accessed December 29, 2016).

[57]As of 2012, in addition to Visa and MasterCard, there were 13 debit card network operators. See Zhu Wang, "Debit Card Interchange Fee Regulation: Some Assessments and Considerations," Federal Reserve Bank of Richmond *Economic Quarterly*, Vol. 98, No. 3, 3rd Quarter 2012, pp. 159–183, https://www.richmondfed.org/~/media/richmondfedorg/publications/research/economic_quarterly/2012/q3/pdf/wang.pdf (accessed December 23, 2016).

[58]In other words, merchants typically keep about 98 percent of the retail price the customer agreed to pay. See Richard Epstein, "Durbin's Folly: The Erratic Course of Debit Card Markets," *Competition Policy International*, Vol. 7, No. 2 (Fall 2011), http://econ.as.nyu.edu/docs/IO/22936/Epstein_02272012.pdf (accessed December 23, 2016).

[59]Federal Reserve Brief for The Respondent in *Opposition, National Association Of Convenience Stores (NACS) et al., v. Board of Governors of Federal Reserve System*, November 2014, https://www.justice.gov/sites/default/files/osg/briefs/2014/11/24/14-200_nacs_v_federal_reserve.pdf (accessed April 22, 2017).

"network processing fees," known as "switch fees," and the acquirer generally charges the merchant what's known as a "merchant discount."[60]

The merchant discount is typically the difference between a transaction's gross amount and the amount the acquiring bank credits to the merchant's account. In general, the merchant's discount reflects the full value of the interchange fee and all other fees to process the transaction. However, the merchant discount was, historically, far from a flat percentage. For instance, prior to the Durbin Amendment, card networks offered small ticket merchants, those with a high volume of low dollar transactions, special volume discounts.

In this framework, merchants *voluntarily* contract to accept cards in their stores, and many choose to contract with Visa and MasterCard networks because doing so provides access to a large customer base. Many large retail merchants have long complained that they have little ability to negotiate these fees, and some have even argued that card networks and issuing banks are price-fixing cartels that use "market power to set excessively high interchange fees."[61]

In 2011, Senator Durbin echoed these complaints in a letter to Wells Fargo Chief Executive John Stumpf. According to Durbin, "interchange fee rates are uniformly and centrally fixed by the card network companies Visa and MasterCard on behalf of Wells Fargo and thousands of other banks."[62] Rather than allow the existing regulatory agencies and courts to decide the veracity of these serious legal charges, Senator Durbin introduced a bill to adjudicate the dispute by implementing price controls.[63] In a 2011 press release Senator Durbin explained that he learned about the issue years ago from a friend, identified as a "grassroots businessman," who told him "these credit card companies and their banks are killing us."[64]

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[60] *National Association Of Convenience Stores (NACS) et al., v. Board of Governors of Federal Reserve System*, U.S. Court of Appeals, District of Columbia Circuit, No. 13–5270, Decided March 21, 2014, http://caselaw.findlaw.com/us-dc-circuit/1661023.html (accessed April 22, 2017).

[61] Zhu Wang, "Debit Card Interchange Fee Regulation." See also Renee Haltom and Zhu Wang, "Did the Durbin Amendment Reduce Merchant Costs? Evidence from Survey Results," Federal Reserve Bank of Richmond *Economic Brief*, December 2015, https://www.richmondfed.org/-/media/richmondfedorg/publications/research/economic_brief/2015/pdf/eb_15-12.pdf (accessed December 23, 2016).

[62] Richard J. Durbin, "Letter to Wells Fargo CEO John Stumpf," October 19, 2011, http://www.durbin.senate.gov/newsroom/press-releases/letter-to-wells-fargo-ceo-john-stumpf (accessed December 21, 2016).

[63] The core provisions of federal anti-trust law are found in the 1890 Sherman Act and the 1914 Clayton Act, both of which have been refined over time through amendment. The Department of Justice and the Federal Trade Commission enforce federal anti-trust law, and price fixing is one of the behaviors traditionally deemed unlawful. See Alden F. Abbott, "A Brief Overview of American Antitrust Law," paper given at The Competition Law & Policy Guest Lecture Programme, The University of Oxford Centre for Competition Law and Policy, January 2005, https://www.law.ox.ac.uk/sites/files/oxlaw/cclp_l_01-05_1.pdf (accessed December 23, 2016).

[64] News release, "Response to *The Wall Street Journal*'s Editorial on Swipe Fee Reform," Senator Richard Durbin (D–IL), March 17, 2011 http://www.durbin.senate.gov/newsroom/press-releases/response-to-the-wall-street-journals-editorial-on-swipe-fee-reform (accessed April 22, 2017).

The Durbin Amendment amended the Electronic Fund Transfer Act[65] by adding a new section 920 regarding debit card interchange fees.[66] The statute now requires the Federal Reserve to set debit card transaction fees so that they are "reasonable and proportional to the cost incurred by the issuer with respect to the transaction."[67] The statute also exempts from these price caps any card-issuer who, "together with its affiliates," has assets of less than $10 billion.[68] In other words, small banks that issue debit cards are ostensibly exempt from the price controls.

The Fed's final rule, issued in July 2011, stipulates that an "issuer may not charge or receive any interchange transaction fee that exceeds the sum of $0.21 plus 5 basis points (0.05 percent) of the transaction's value."[69] The $0.21 represents the base amount, and it corresponds to the per transaction allowable cost, excluding fraud losses.[70] The 5 basis points are an *ad valorem* amount that corresponds to the average per transaction fraud losses of the median card issuer, as estimated by the Federal Reserve.[71]

Price caps were *not* applied to the fees charged by the card networks. The interchange fee on the typical transaction is now approximately half the pre-Dodd–Frank fee, but early evidence suggests that the Durbin Amendment has had "limited and unequal impact" on reducing merchants' overall cost of accepting debit cards.[72] The Durbin Amendment also imposed routing restrictions on debit card transactions, as well as reporting requirements for card issuers and networks.

In particular, the Section 920(b)(1) required the Federal Reserve to promulgate a rule that prohibits card issuers and networks from restricting the number of networks on which any debit transaction can be processed to only one network (or less than two affiliated networks).[73] In contrast to the interchange fees, small banks are not exempt from the Durbin Amendment's routing restrictions. The Durbin Amendment clearly represents an attempt to settle a debit-card-merchant dispute by taking the side of the retail trade associations against large banks.

The Case for Repealing Durbin. Proponents have portrayed the Durbin Amendment as consumer-friendly, but it defies all logic and reason that large merchants, as a return favor to Congress for capping the debit-card interchange fees, would simply pass billions in savings on to retail consumers. Furthermore, debit-card interchange fees only represent one of many types of fees banks charge, so there is no reason to expect banks to refrain from making up any lost revenue by charging customers higher fees for other services. It is hardly surprising that early research suggests that banks have tried to do just that. For instance, evidence shows that banks have:

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[65] 15 U.S. Code § 1693 et seq.

[66] Federal Reserve System, "Debit Card Interchange Fees and Routing; Final Rule," *Federal Register*, Vol. 76, No. 139 (July 20, 2011), pp. 43394–43475, https://www.gpo.gov/fdsys/pkg/FR-2011-07-20/pdf/2011-16861.pdf (accessed April 22, 2017).

[67] Section 1075(a)(2), 15 U.S. Code § 1693o–2.

[68] Section 920(a)(6)(A), 15 U.S. Code § 1693o–2(a)(6)(A).

[69] Federal Reserve System, "Debit Card Interchange Fees and Routing; Final Rule," p. 43420.

[70] Ibid., p. 43422.

[71] Ibid., p. 43424.

[72] Haltom and Wang, "Did the Durbin Amendment Reduce Merchant Costs?"

[73] Federal Reserve System, "Debit Card Interchange Fees and Routing; Final Rule," p. 43394.

(1) Reduced the availability of fee-free current accounts. The total number of banks offering free current accounts fell by 50% between 2009 and 2013. In comparison, fee-free banking actually increased at banks not subject to the Durbin Amendment.
(2) More than doubled the minimum monthly holding required on fee-free current accounts between 2009 and 2012, from around $250 to over $750.
(3) Doubled average monthly fees on (non-free) current accounts between 2009 and 2013, from around $6 to more than $12.[74]

Separately, Federal Reserve research shows that, even though the interchange fee on the typical transaction is now approximately half the pre-Dodd–Frank fee, the Durbin Amendment has had "limited and unequal impact" on reducing merchants' overall cost of accepting debit cards.[75] Not only has the cost of accepting debit cards failed to decline for many merchants, it has actually *increased* for some.[76]

Price controls are always destined to end badly and the Durbin Amendment is no exception. It is terrible public policy and it is little more than a giveaway to a special interest group. Congress should never have passed the Durbin Amendment because it is a legislative body ill-suited to adjudicate legal disputes. Of the three branches of the U.S. government, the judicial branch—not Congress—was set up for exactly this purpose. Congress already did its job by writing the nation's anti-trust laws, so it should repeal the Durbin Amendment to help restore the proper separation of powers between the three branches of the U.S. government. Repealing the Durbin Amendment—as the CHOICE Act does—would also help to strengthen private markets by allowing competitive forces, rather than government bureaucrats, to dictate how the debit-card interchange fees can be efficiently and effectively applied.

Conclusion

The 2010 Dodd–Frank Wall Street Reform and Consumer Protection Act was the most extensive financial regulatory bill since the 1930s. Rather than address the true causes of the financial crisis, it expanded the authority of the federal regulators who missed the 2008 financial crisis. It created new federal agencies, imposed unnecessarily high compliance burdens on firms, codified many of the too-big-to-fail actions used during the crisis, and contributed to the unusually sluggish recovery because it came at exactly the wrong time.

My Heritage Foundation colleague and I estimate that one aspect of Dodd–Frank—excess borrowing costs—imposes a 22 basis point burden on the economy, and that removing this added cost would have a measurable positive impact on the economy.

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[74] Todd J. Zywicki, Geoffrey A. Manne, and Julian Morris, "Price Controls on Payment Card Interchange Fees: The U.S. Experience," George Mason Law & Economics Research Paper No. 14-18, October 15, 2014, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2446080 (accessed April 22, 2017).
[75] Renee Haltom and Zhu Wang, "Did the Durbin Amendment Reduce Merchant Costs? Evidence from Survey Results."
[76] Ibid.

Our estimates of this Dodd–Frank "repeal" scenario predict that, on average from 2017 to 2026, removing Dodd–Frank's investment wedge would increase GDP 1 percent per year, increase the capital stock by almost 3 percent per year, and decrease the federal debt ratio by nearly 1 percent per year, providing up to $340 billion in 10-year federal revenue gains.

Ideally, Congress would repeal the Dodd–Frank Act and focus, instead, on legislation that improves incentives, increases competition, and lowers the reliance on government backing of losses in financial markets. This testimony has described three policies that Congress could enact to strengthen private financial markets in this manner that would help spur sustainable economic growth: (1) requiring all failing financial firms to go through bankruptcy; (2) eliminating the Consumer Financial Protection Bureau; and (3) repealing the Durbin Amendment. Each of these actions would improve private incentives and maximize the benefits of competitive forces to strengthen financial markets so that citizens can produce sustainable economic growth that provides widespread wealth-building opportunities in the U.S.

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