# Wall Street Reform and Consumer Protection Act:

# Myths vs. Facts

**MYTH: The bill will put in place permanent bailouts -- encouraging risky behavior by financial institutions which assume the government will come to their rescue.**

FACT: Completely untrue. Under this bill, the days of taxpayer-funded bailouts are over. The bill establishes a process to dissolve failing large financial institutions in a way that does not wreakhavoc on the whole economy; but this is no bailout. These financial institutions will be allowed to fail, but in a way that protects the economy. Under this authority, as a last resort, federal regulators will shut down these institutions that pose a risk to the whole economy. They will fire the managers, fire the executives, wipe out shareholders, sell off the assets, but protect our financial system and taxpayers from collateral damage. For a market to function, those who invest and lend in that market must know that their money is actually at risk. Institutions and investors must be responsible for their decisions.

Any costs incurred in unwinding these financial institutions will be borne by Wall Street firms and the big banks—not taxpayers. Dissolution will be paid for first by shareholders and creditors, by any remaining assets of the failed company and then through an industry-funded effort. The bill requires big banks and other financial institutions (with $50 billion in assets) to foot the bill for any future dissolutions of individual companies. These institutions would pay assessments based on a company's potential risk to the whole financial system if they were to fail.

This bill institutes preventive medicine by making the financial marketplace more accountable and transparent, long before we get to the point of a rescue. We strengthen supervision of large and risky financial institutions with stronger capital standards and rules against excessive and overly risky leverage.

**MYTH: This bill adds unnecessary government bureaucracy with a new Consumer Financial Protection Agency (CFPA) that duplicates the work of existing agencies and increases regulatory burdens on businesses.**

FACT:The new agency will consolidate and streamline enforcement of roughly 20 laws currently overseen by seven different agencies. The functions would not be duplicated; rather, they would be streamlined into a single agency, thereby reducing regulatory burden and expense, not increasing it – with the added benefit of more effective consumer protection.

This new agency is necessary as existing regulators failed to stop abusive lending practices before these practices harmed millions of consumers and ultimately the entire economy. Right now, consumer protection is a minor and sometimes ignored responsibility for a number of agencies but not top priority for any one of them. Agencies have ignored their consumer protection mandates in the past, and former Federal Reserve Chairman Alan Greenspan never implemented a law passed in 1994 to regulate subprime lending. American consumers deserve much better than this. The CFPA will clean up this mess and make consumer protection its sole priority.

**MYTH: This bill will assert more government control over financial markets.**

FACT: To prevent risky financial dealings by Wall Street and the big banks from decimating the savings and homes of American families and from freezing access to credit for American's small businesses, this bill reins in Wall Street and strengthens accountability in Washington. Putting in place these kinds of common sense rules of the road will improve transparency, foster competition, and strengthen the health of the marketplace. The central objective of reform is to establish a safer, more stable financial system that can deliver the benefits of financial innovation even as it guards against the dangers of excessive risk. We must ensure that our financial system creates opportunity and long-term wealth while reducing risk.

**MYTH: The bill increases the deficit and increases taxes.**

FACT: The net cost of the bill is <u>fully paid for</u> from the TARP. The TARP was set up to save the financial system from collapse and the cost of this legislation to prevent a future collapse is a necessary cost in that effort. Most of the costs associated with these reforms are paid for by the financial industry through fees and assessments—on large banks and non-regulated financial companies such as payday lenders and check cashing operations, and not on local community banks or credit unions.

This is a small price to pay to avert another financial disaster, and these reforms will help spur our economy and thereby reduce the federal deficit through restored confidence that our financial institutions are sound— all while we better protect consumer and investors.

**MYTH: We should just let these large institutions go through bankruptcy, instead of getting the government involved.**

FACT: Bankruptcy will not stop the type of financial panic that we saw in the fall of September 2008. Even President Bush, Vice President Cheney and their Republican Treasury Secretary and the Chairman of the Federal Reserve rejected using the Bankruptcy Code as a model for dissolving large, interconnected financial institutions. Only in the case of Lehman Brothers did they allow bankruptcy to proceed. The aftermath, with a 500 point drop in the stock market, was such a disaster that two days later the Bush Administration bailed out AIG because the markets could not sustain another major bankruptcy filing by a large financial firm.

Bankruptcy, while appropriate in many instances, can be a lengthy process that may not always allow for the speedy resolution of a large financial firm in time to avoid a broad financial panic that could result in major financial and economic disruptions. As Lehman Brothers navigated bankruptcy court, Business Week reported "Scores of hedge funds that had hundreds of millions in cash and other securities parked with Lehman's prime brokerage operation in London have had their accounts frozen. A number of these hedge funds have filed formal objections with the bankruptcy court and at least one fund, New York-based Bay Harbour Management, is mounting a legal challenge to the court's hastily-approved sale of Lehman's brokerage arm to Barclays Capital. Now a new and even more troubling scenario is arising: legal disputes stemming from the estimated $1 trillion in derivatives transactions that Lehman had entered into on behalf of itself and some of its customers." [Business Week, 10/2]

Under the bill's dissolution authority, the FDIC will be able to unwind a failing firm expeditiously and in an orderly manner so that existing contracts can be dealt with and secured creditors' claims can be addressed—much like is done today when commercial banks become insolvent.

**MYTH: The CFPA limits consumer choices of financial products and stifles innovation.**

FACT: There will be no limits on innovation. When we create choices for consumers, we create competition in the industry that benefits everyone. All that will be limited are abusive practices of the sort that led to the current crisis. The status quo has limited consumer choice by crowding out of the market better loans for which many borrowers qualified but were not offered. The CFPA will ensure that consumers are offered the best loans for which they qualify, and not just the riskiest loans that are most lucrative for originators.

**MYTH: The new CFPA will raise costs for consumers as firms have to comply with new rules and standards and will pass on these costs to consumers. Consumers will have to pay more just to fund the agency.**

FACT: An agency that could have helped prevent the risky lending practices that resulted in trillions of dollars of losses in Americans' retirement savings and home values is well worth the modest costs involved. They pale in comparison to the costs of regulatory failure. Moreover, as the CFPA will streamline enforcement of laws and rules that currently fall under seven different government agencies, costs to the companies and prices for consumers may well decline.

**MYTH: This legislation will hurt community and small banks and merchants—those that didn't cause the financial meltdown but were hurt by it.**

FACT: The bill ensures that small banks and credit unions, which play a key role in their communities, are not subject to undue regulatory burdens.

- Banks and thrifts under $10 billion in assets and credit unions under $1.5 billion in assets will continue to have their consumer protection examinations done by their existing regulators.
- CFPA will play a backup role unless the primary regulators fail in their oversight, and these institutions will not see their assessments for consumer protection exams change under this bill.

Merchants, retailers and other non-financial businesses will be excluded from the regulation and oversight of CFPA when they extend credit directly to consumers for the purchase of goods or services. Merchants and retailers can continue to provide credit and layaway plans without becoming subject to new regulation as long as they do not choose to resell the credit. Merchants and others are still subject to federal law through the Truth in Lending Act, which was passed almost 30 years ago. Also, doctors and other businesses that bill their customers after a service is provided will be excluded.

**MYTH: The bill is a job killer and will drive up interest rates.**

FACT: This is more scare tactics and fear mongering from the same crowd that said health care reform was going to kill grandma. Defenders of risky business on Wall Street are ignoring the destruction that lax oversight caused in the financial lives of Americans and American businesses—and also ignore the increased investment and entrepreneurship that a stable and growing economy will generate. Instituting strong consumer protections, improving transparency, and rewarding responsible investing are some of the best ways to foster competitiveness and grow our economy.

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## Questions & Answers

**Q: Why is the Administration continuing the TARP? Shouldn't we end TARP and put the money toward deficit reduction?**

A: The TARP will be preserved a while longer for the very reason it was created: to stabilize the financial system, and to help get credit flowing to Main Street. In the first round, large financial institutions took TARP money but didn't necessarily lend it to small businesses and families. Redirecting some TARP money to putting consumer and small business protections in place and to free up credit is in keeping with its original purpose.

Last year, Congress insisted on tough conditions on the financial rescue to maximize the returns to the taxpayers for this investment -- refusing to provide President Bush with a blank check -- and those efforts are paying off. A new report shows that the Treasury Department expects to recover all but $42 billion of the $364 billion disbursed in the first year to ailing financial institutions, with the portion invested in banks actually showing a profit. As a result, the Obama Administration now projects a $200 billion reduction in the deficit for this year.

Using a portion of the TARP funds to spur American job creation is critical for deficit reduction. A growing economy helped give us the budget surpluses of the '90s. Some have offered a false choice between creating jobs and reducing the deficit. Creating jobs reduces the deficit.

**Q: Why are you acting on this before the Financial Crisis Inquiry Commission reports next year?**

A: We have spent months developing common sense solutions to the financial meltdown we faced—and Wall Street reforms are now the next critical step to stabilize and grow our economy. People are right to be outraged by what happened on Wall Street, and Americans overwhelmingly support reform of Wall Street as part of our economic recovery. Of course, this is an ongoing process and will not end with this legislation; the commission's recommendations will guide future reforms.

**Q: Will this legislation help consumers with rising credit card interest rates?**

A: Yes. The new CFPA will have ongoing authority to rein in the credit card industry. They can also take on the issues of predatory lending, payday loans, check cashers, and overdraft fees. This bill builds on the consumer protections built into the Credit Cardholders Bill of Rights signed into law earlier this year.

**Q: What does this do to the Federal Reserve?**

A: The bill increases transparency at the Federal Reserve, which has played an enormous role in shoring up big banks and other financial institutions in this crisis. The reforms subject the Fed's lending programs to scrutiny by the non-partisan Government Accountability Office.

**Under the bill, the Federal Reserve's use of Section 13(3) authority – to extend short-term borrowing and secured loans to individuals, partnerships, or corporations in "unusual and exigent circumstances" -- will be subject to significant new restrictions. Use of this authority will require approval by two-thirds of the members of the Council and the consent of the Treasury Secretary after certification by the President that an emergency exists. This authority may not be used to provide assistance to individual companies, and Congress will be able to disapprove further use of the authority.**