

Prepared Statement of

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Before the

Committee on Energy and Commerce
Subcommittee on Commerce, Trade, and Consumer Protection
United State House of Representatives
Washington, D.C.

at a hearing on

The Proposed Consumer Financial Protection Agency:
Implications For Consumers And The FTC

July 8, 2009

I. Introduction

Chairman Rush, Ranking Member Radanovich, and Members of the Committee:
I am Stephen Calkins, Associate Vice President for Academic Personnel and Professor of Law at Wayne State University and a former General Counsel of the Federal Trade Commission.¹ I appreciate the opportunity to appear before you today to share some observations in connection with the important subject you are addressing.

I do not pretend to be an expert in bank regulation. Nor, for that matter, am I taking a position for or against the bill you are considering. Rather I appear before you to make three points:

- The Federal Trade Commission (“FTC” or “Commission”) is an extraordinary agency with unique attributes and a unique role, and, although by no means perfect, it has performed its mission well. Many of the consumer protection laws that now protect consumers reflect work done by the agency in the consumer financial services area.
- The proposed Consumer Protection Agency Act of 2009 would fundamentally change the functioning of the agency, both with respect to protection of consumers in the financial services market and more generally.
- Before imposing these restrictions on the Commission’s authority, Congress should consider carefully whether the gains outweigh the harms and whether those gains could be achieved without causing such extensive harm.

¹ I am appearing solely in my personal capacity, and do not represent or speak for Wayne State University, the Federal Trade Commission, or any other entity or individual. Since the proposed new legislation on which I am testifying has only just been released, this statement necessarily represents only my initial views.

II. The Federal Trade Commission

The Federal Trade Commission is a tiny agency, as federal agencies go, with only 1100 employees. Yet it has a very special role. It is the one agency charged with protecting consumers, and it has performed that assignment admirably.

The FTC has special strengths. It is bi-partisan, with no more than three Commissioners coming from one party. It combines law enforcement with research and reporting, hearings and workshops, advocacy and amicus briefs, and consumer and business education and outreach. A unique strength of the FTC is the combining two functions—competition enforcement and consumer protection—within a single agency.² This improves both functions, by bringing a consumer emphasis to competition enforcement and economic rigor to consumer protection.

The Commission has a long history of important contributions in the area of credit and financial products, even though it has had to operate with only limited jurisdiction (banks and insurance are excluded). The FTC played an important role in supporting passage of early consumer credit protection statutes and in prosecuting a multitude of financial frauds. The FTC in the 1970's issued a rule outlawing the use of the so-called "holder-in-due-course" doctrine in consumer credit contracts, and its investigations and cases provided the foundation for credit-protection laws such as the Equal Credit Opportunity Act, portions of the Fair Credit Billing Act, and the Fair Debt Collection Practices Act. More recently, it stepped up and became the leading consumer privacy

² *More Than Law Enforcement: The FTC's Many Tools—A Conversation with Tim Muris and Bob Pitofsky*, 72 Antitrust L.J. 773, 776-81 (2005); Thomas B. Leary, *Competition Law and Consumer Protection Law: Two Wings of the Same House*, 72 Antitrust L.J. 1147 (2005); Report of the American Bar Association Section of Antitrust Law, Special Committee on the role of the Federal Trade Commission, 58 Antitrust L.J. 43 (1989).

protection law enforcement agency and used its array of powers to become a leading data security protection agency. Although some have said it could have moved faster and done more, it responded to another need by bringing a series of major predatory lending cases. I have followed the agency's work in both the consumer protection and competition fields for many years and believe that, while constrained by limited resources, the FTC is an agency that time and again has taken innovative actions to protect consumers, including with respect to financial services.

III. The Consumer Protection Agency Act of 2009 Would Fundamentally Change the FTC's Role

In a way, the FTC should feel complimented, since the new agency is in part modeled closely after the FTC. Like the FTC, it would have a governing board of five members, although one slot is reserved for the Director of the National Bank Supervisor. (It is unfortunate that the agency departs from the FTC model to allow all five Board members to be from the same party. A strength of the FTC is the bi-partisanship and continuity that comes from shared leadership.)³ Like the FTC, it would have a broad array of powers—adjudication, rulemaking, litigation, etc.—and it would have some powers the FTC has long wanted. It is noteworthy that the Agency would be specifically given some of the authority that is the hallmark of the FTC, such as research and reporting, consumer education, and “collecting and tracking information on

³ A few other small points: It is wise to use five-year terms (rather than the FTC's seven-year terms) so there can be both change and continuity. But the bill should clarify that although Board Members serve five year terms, the President may change at any time which Board Member serves as Director of the Agency. Compare Section 1012(c)(1) (“An appointed Board member, including the Director of the Agency, shall serve for a term of 5 years.”). And it would be unfortunate to call both the chief executive of the agency and the reserved Board Member “Director,” since that is likely to invite confusion.

consumer” complaints.” Section 1014(c)(3). The Agency would be entrusted with the same “unfairness” and “deception” authority that the FTC has administered since 1938 when the Wheeler-Lea Act amended the FTC Act. Section 1031. (Indeed, one can foresee warring interpretations of those terms once two federal agencies are in the business of regularly defining and applying them. Would Agency decisions be precedent for the Commission, and vice versa?) All that would be missing would be the Commission’s bi-partisanship and its critically important competition authority, which are so important to the FTC’s success.

The new agency would not only have many of the FTC’s powers, it also would replace the FTC in a broad part of the FTC’s consumer protection mission. “All consumer financial protection functions of the Federal Trade Commission are transferred to the Agency.” Section 1061(a)(5)(A). The new agency would have all of the FTC’s “powers and duties . . . relating to consumer financial protection functions.” Section 1061(a)(5)(B).

The extent of this transfer can be understood only by working through the definitions. “Consumer financial protection functions” are defined incredibly broadly to include “research, rulemaking, issuance of orders and guidance, supervision, examination, and enforcement activities, powers, and duties relating to the provision of consumer financial products or services” Section 1061(d). “Consumer financial product or service” is defined as “any financial product or service to be used by a consumer primarily for personal, family, or household purposes.” Section 1002(8). “Financial product or service” is defined as “any product or service that, directly or indirectly, results from or is related to engaging in 1 or more financial activities.” Section

1002(19). And “financial activities” includes a list seemingly of every imaginable activity that relates to money or finance—and, for good measure, adds “any other activity that the Agency defines, by rule, as a financial activity for the purposes of this title” with the sole exception of insurance. Section 1002(18).

Note the cumulative effect of the inclusive: the FTC has to transfer all functions “relating to the provision of consumer financial products or services,” and a “financial product or service” is one that, “directly or indirectly, results from or is related to engaging” in a (broadly defined) financial activity. As written, this would call for transferring significant parts of the Commission’s Bureau of Competition and Bureau of Economics. See, e.g., *FTC v. Ticor Title Insurance Co.*, 504 U.S. 621 (1992) (joint setting of title insurance rates as an unfair method of competition). Nor is this an issue as to which there is a simple “fix” by, for instance, transferring only functions related to the Commission’s “unfair and deceptive acts and practices” authority, since the Commission has used both this authority and its competition authority in the same case, see *Negotiated Data Solutions LLC* (2008), and of course it conducts research on a wide variety of issues.

The breadth of authority given to the new Agency is illustrated by Section 1053. The Agency is authorized to enforce compliance with, among other things, any “Federal law that the Agency is authorized to enforce . . . and any regulations or order prescribed thereunder, unless such Federal law specifically limits the Agency from conducting a hearing or adjudication proceeding” Since the Agency would be given “all powers and duties” vested in the Federal Trade Commission “relating to consumer financial protection functions,” Section 1061(a)(5), the Agency could enforce the entire FTC Act

and all regulations and orders issued thereunder. The only limit would be the very expansive “relating to consumer financial protection functions” wording, and the Agency is allowed to define for itself what is included therein. See Section 1002(18)(0).

Even if one considers only the FTC’s Bureau of Consumer protection, the bill calls for a substantial transfer. I have heard that up to 30% of the Bureau of Consumer Protection’s lawyers work on financial practices. My own view is that a 30% figure could understate the extent to which consumer protection enforcement would be shifted out of the FTC.

One of the dramatic contemplated changes to the Commission’s historic role concerns advice and guidance. The Commission was established by Congress in part to advise business on proper practices. Over the years, the Commission has been in the forefront of writing reports, holding hearings, writing rules and guidelines, filing amicus briefs, giving speeches, and on and on. Much of that would be prohibited by the new law. If the new Agency can “issue regulations or guidance” to assure compliance with any enumerated consumer law or “the laws for which authorities were transferred . . . , and any regulations thereunder,” then the new agency “shall have the *exclusive authority* to prescribe rules, issue guidance, conduct examinations, require reports, or issue exemptions with regard to any person subject to that law.” Section 1022(d) (emphasis added). This would seem to prohibit issuance even of antitrust and economics related guidance with respect to the FTC Act. Even with respect to consumer protection, it would seem to prohibit many if not most of the Commission’s efforts to do studies, hold workshops, issue reports, and give guidance.

I have heard it suggested that the new legislation would move authority for

specific consumer statutes but not for Section 5 of the FTC Act. Although there is conflicting language in the proposed bill, I do not read the current version of the bill this way. If all power and authority (and resources) are transferred, what can be left behind? Section 1101 states that in an investigation or proceeding “in which it appears to the Commission that an unfair or deceptive act or practice is being committed in connection with the marketing, sale, provision or delivery of a consumer financial product or service, the Commission shall consult and coordinate” with the Agency “as the agencies deem to be appropriate.” But how likely is it that the FTC, once there is a transfer of functions, would be in a position to bring a case? Would it make sense to investigate only part of the issues posed, for instance, by deceptive automobile commercials? Even if the FTC preserved authority to enforce Section 5, what would be the point of doing so if the FTC could not conduct studies or issue reports or give advice? It would not longer be the FTC that was enforcing Section 5, but a very different agency.

To gain a better sense of the impact of this legislation on the FTC, I reviewed the FTC’s most recent annual report: The FTC in 2009 (March 2009). The FTC’s consumer protection law enforcement activities include topic after topic that apparently would be transferred to the new agency: subprime credit, mortgage servicing, foreclosure rescue, fair lending, mortgage advertising, debt collection,⁴ payday lending, credit repair operations, advance fee loans or credit cards, magazine subscriptions

⁴ For instance, the FTC would have to transfer authority related to “collection of debt related to any consumer financial product or service,” but since the latter includes any service indirectly related to collecting a debt related to any consumer financial product or service, the circle would likely continue until there is little work related to debt collection that the FTC would not have to transfer.

(defined as credit transactions, Section 1002(10); *Mourning v. Family Publications Service, Inc.*, 411 U.S. 356 (1973)), tax refunds, free gift cards (Section 1002(10)(L)), payment systems (see Section 1002(10)(K) (“money transmitting”)), credit card processing (see Section 1002(10)(J) (“financial data processing”), debt consolidation, phishing, and, to some extent, data security and privacy. See Annual Report at 45-59. Reported hearings and workshops focused on phishing, debt settlement, protecting personal information, RFID, mortgages, the mobile marketplace, and fraud. *Id.* at 66-67. A majority of these presumably would be transferred. Also to be transferred would be a majority of the items listed under consumer protection “Advocacy Letters, Comments, and *Amicus* briefs” and “Congressional testimony.” *Id.* at 67-71. The list of what authority would *not* be transferred is considerably shorter than the list of what *would* be.

Here is how the FTC wrapped up its Annual Report by “Looking Ahead”:

On the consumer protection side, the Commission will continue to protect cash-strapped consumers from unfair and deceptive credit schemes and ensure they get the information they need to make informed decisions about the use of credit in this challenging economy. Addressing the full life cycle of financial services transactions affecting consumers, the Commission will work to protect consumers in the areas of subprime credit, payday lending, fair lending, mortgage advertising and servicing, and debt collection and settlement. It will also continue its empirical work on how consumers absorb financial information and how they perceive disclosures associated with routine financial transactions, so consumers can be armed with understandable information with which to protect themselves. As the nation considers how it can control the impact of its consumption on the environment, the Commission will be at the forefront of ensuring that consumers are getting truthful information about how products affect the environment.

Id. at 95. If this bill is passed, only that final sentence about the environment would remain in full effect.

The bill would preserve “backstop enforcement authority.” Section 1061(b). Under this provision, the Commission could “recommend in writing . . . that the Agency initiate an enforcement proceeding,” and if the Agency does not do so within 120 days, the Commission “may initiate an enforcement proceeding” Section 1022(e)(3). I am reasonably confident that this authority would be rarely used.

There are several reasons for this. First, the legislation clearly contemplates a sweeping transfer of responsibility. What this appears to mean is that agency staff working in financial services also would be transferred. Once the FTC loses the talented staff who are expert on these issues, it is unlikely that it will be in a position to develop many cases.

Although the Commission could recruit and train new staff, it is unlikely to do so. For one thing, it appears to be the point of this legislation (at least in part) to get the FTC out of this business. It does not appear consistent with the spirit of this legislation for the FTC to be investing resources in developing cases.

Inter-agency dynamics also counsel against an active FTC role. Why would good staff work to develop cases only to turn them over to another agency? Staff like to bring cases, not position *other* staff to bring them. Also, these are often cases in which timing is urgent, because wrongdoers are harming consumers and absconding with assets. Why incur unnecessary delay?

The 120-day provision is patterned, to some extent, on the current process by which the FTC can refer civil penalty matters to the Department of Justice. 15. U.S.C. § 56(a)(1) (45-day notice before commencing an action; if Attorney General fails to commence an action the FTC may). Only rarely does this result in the FTC proceeding

on its own. ABA Antitrust Section, Consumer Protection Law Developments 268 n.319 (2009). More fundamentally, one can observe that the FTC relies far more heavily on its consumer redress and disgorgement authority (where it can proceed alone) than on civil penalty authority requiring review by DOJ. Although the new bill uses slightly different wording that the DOJ civil penalty authority (it refers to recommending an enforcement action rather than commencing one), this is not a big enough change to make a difference.

Indeed, the new backstopping authority would function very differently from the existing civil penalty referral provision. Today the Commission can collect complaints, hold workshops, conduct hearings, give advice, and file amicus briefs, and then, where appropriate, ask DOJ to file a civil penalty action. Tomorrow, would staff work on a transferred function without any of the panoply of agency tools that are one of the hallmarks of the FTC? My guess is that this “backstop” authority is really intended to be just that. Should the day come that the new Agency, with leadership all from a single party, abandons the field, the FTC theoretically could step in. Unfortunately, the FTC would lack the resources and expertise to perform this role with any kind of speed, and it could not use its normal array of tools. My guess is that the vision of an effective “backstop” is likely more theoretical than real.

IV. Conclusion

As noted in my beginning, I am not here to support or oppose the proposed legislation. Obviously it was written by bright people to address some serious issues. There is some appeal to the suggestion to prefer activity-based regulation to entity-based regulation. No one who has bought a house and experienced the mortgage

disclosure process involved therein (which the FTC does not control) can think that the current system of mortgage disclosure has worked well. And of course we have been through some very tough economic times. If this bill represents the only way to address these issues, there is much to be said for it.

Although I cannot quantify the benefits of this legislation, I can observe that it appears likely to cause an important agency that is working well to lose a substantial part of its staff, its authority, and its mission. The unique FTC blending of bi-partisan expertise and competition and consumer protection would no longer be brought to bear on an important part of the economy. Much of what the Commission has been doing it would no longer do.⁵ The bill would interfere with the FTC's work in consumer protection not just with respect to financial services, read narrowly, but also more generally, since the heart of many frauds is abuse of the underlying payment system.

It is difficult to balance the benefits and costs of the proposed legislation. I do urge caution and care and examination of alternatives. (It is interesting, for instance, that the bill would fully preserve the authority of the Department of Justice, the SEC, and the CFTC.) Legislation as sweeping as this should not to be enacted in haste.

⁵ Should this bill pass, the FTC's responsibilities would shrink, which makes this an appropriate time to ask whether any artificial limiting of the agency's jurisdiction should be removed. One obvious candidate is telecommunications: in the deregulated modern world, there is no reason why the FTC Act should not apply to telecommunications firms just as it applies to most businesses.

WITNESS DISCLOSURE STATEMENT

Name: Stephen Calkins

I am not testifying on behalf of any government entity.

I am not testifying on behalf of any other entity.

I have not received a Federal grant or contract on or after October 1, 2006, but I was General Counsel of the Federal Trade Commission from 1995 to 1997, and the FTC arranged for me to make a presentation to the OECD in October 2004.

I am not representing any entity or entities. I am speaking only for myself.

Stephen Calkins

July 6, 2009