Debt Deception: Broad Reach of New Consumer Financial Agency May Fall Short in Some Areas

Article By:

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On paper, the new Consumer Financial Protection Bureau's reach is breathtaking, from overseeing behemoths like Bank of America Corp. to small businesses like pawn shops. But whether it will curb abusive lending practices that mire many Americans in debt may not be apparent for years.

When it officially opens its doors on July 21, the bureau will have to grapple with lenders and Republicans in Congress who want to chip away at that reach. Already, Elizabeth Warren, the Obama administration's appointee charged with launching the bureau, is warning that making a lot of new rules won't work because businesses quickly find ways to get around rules.

Yet, in writing the financial reform law last summer that created the new agency, Congress has already restricted the bureau's power over a few special interests. Others are already looking for ways to escape regulation.

For example:

- Community banks and even big banks with assets of less than $10 billion will continue to report to regulators who failed to prevent predatory lending during the mortgage frenzy, including abuses by smaller banks;
- Most auto dealers fall completely outside the bureau's reach, even though consumer advocates complain that predatory lending practices in dealer showrooms are epidemic;
- Payday lenders have been especially creative and aggressive in trying to avoid new regulations being imposed on them.

An investigation by the Center for Public Integrity has raised questions as to whether these cracks in the bureau's oversight could become deep crevasses that allow predatory lending to flourish despite the birth of a new regulatory agency.

Perhaps the most compelling argument for creating a new agency as part of the sweeping Dodd-Frank reform law was that the financial regulators had failed to use their powers to clamp down on abuses in mortgage lending. The Federal Reserve had the authority to ban deceitful practices but did little with it. Bank regulators rarely bothered to delve into individual mortgage loans, allowing banks to spew out loans borrowers couldn't afford and even loans with fraudulent documentation.

Despite their negligence, these same regulators — the Comptroller of the Currency and the Federal Deposit Insurance Corp. — will be in charge of enforcing new rules crafted by the Consumer Financial Protection Bureau for all but the biggest banks.

In fact, the examination process for most banks will change little, since current regulators already have examiners who are supposed to serve as consumer watchdogs, said Steve Verdier, executive vice president of the Independent Community Bankers of America.

"We were arguing that banks shouldn't be subject to conflicting examination procedures, and frankly, we won that argument," Verdier said.

Yet consumer advocates counter that smaller banks were guilty of some of the same abusive practices as the major banks.

Congress also carved out an exemption for car dealers, even though no other business garners more complaints to the Better Business Bureau.

Duane Overholt, a former car salesman who created the website StopAutoFraud.com, says he's deluged with requests for help from unhappy car buyers each week. The most common complaint he hears is from car buyers who were called days or weeks after driving a new vehicle off the lot to be told they didn't qualify for a loan. Buyers are told to bring the car back, unless they are willing to pay more for it. In the industry, this is called "yo-yoing."

Americans owe roughly $850 billion for the cars they drive, more than they owe on their credit cards. And the consequences of getting steered into a car loan they can't afford can be devastating, said consumer advocate Rosemary Shahan, of Consumers for Auto Reliability and Safety.

"A lot of times you lose your job when you lose your car," she said.

Warren said at the time that she was disappointed when Congress caved to auto dealers.

"I'm shocked that car dealers are willing to say publicly that they want to have the legal right to hide tricks and traps," she said.

Payday lenders also lobbied furiously to get carved out of financial reform but lost in Congress. Now, the group plans to take their case directly to the new bureau once it has a staff, said Steven Schlein, a spokesman for the industry's trade group. One of their arguments is that the payday lending advertising is already regulated by the Federal Trade Commission. But consumer advocates counter that payday lenders deceptively trap borrowers in a cycle of debt without adequate supervision.

But a few creative payday lenders have worked hard to avoid regulation. One tactic they've tested is opening their business on Native American reservations and arguing that they are beyond the reach of the courts. Others have located offshore and opened Internet payday lending sites to avoid regulation.

We'll be telling that story today, with more stories to come on auto dealers and community bankers.

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