

# CFPB's unchecked power: New bureau's hunt for financial scalps

By Eric Grover

The Washington Times

Monday, September 3, 2012

The Consumer Financial Protection Bureau is hunting for scalps before the November election to reinforce the narrative that President Obama is protecting consumers from a rapacious and untrustworthy financial services industry.

The Dodd-Frank Act gave the bureau virtually unfettered authority over consumer financial services and funded it from the Federal Reserve to insulate it from congressional oversight. It can act against any product it deems unfair, deceptive or "abusive." The abuse standard is new and gives bureau mandarins a blank check.

Its broad rule-making authority is tantamount to making law, which is Congress' job. Its design, shielding regulators from traditional political checks and balances, is at odds with America's constitutional framework.

The bureau took its first scalp with Capital One's \$210 million settlement for deceptively marketing payment protection and credit monitoring. The \$25 million in penalties it collected will be used to reward administration allies.

Easy-to-vilify payday lenders may be next. The bureau hired law professor Chris Peterson, who urged that cities require payday lenders to advertise themselves as "predatory."

Bureau actions are best understood through two lenses: the political sentiment of those who created and staff it and public-choice theory.

Nobel Prize-winning economist James Buchanan's public-choice theory holds that government bureaucrats act to maximize their own welfare. The bureau's enormous unchecked power acutely demonstrates this problem. It embraces noxious disparate-impact doctrine, which holds that the racial

makeup of the country should not be underrepresented in a portfolio. It can use this to intimidate and prosecute any financial institution.

Bureau architect Elizabeth Warren, director Richard Cordray and Mr. Obama think hapless consumers are victims of predatory financial institutions and, even if all products' material facts are disclosed fully, Joe Six-Pack cannot be trusted to make the "right" choices. Bureau mandarins think they can determine what products deliver value better than can the market interplay of competing financial institutions and consumer choices.

The bureau and the Justice Department contend Equal Credit Opportunity Act violations absent discriminatory intent are proved if an organization's credit allocation doesn't mirror the general population's ethnic mix. If, for example, Samoan Americans are .5 percent of the population, they should be .5 percent of a bank's mortgage portfolio. While that doesn't square with the legislation's text, it is of a piece with the administration's politics.

As Mr. Cordray declared, "We cannot afford to tolerate practices, intentional or not, that unlawfully price out or cut off segments of the population from the credit markets." This is exactly the kind of thinking that brought down the housing market. The willful weakening and politicizing of credit wreaked havoc in the financial sector. If the government learned its lesson from that catastrophe, credit would be more expensive and less available to risky borrowers.

Yet the shibboleth of systematic racial credit discrimination sustains an industry of activists. For example, National Fair Housing Alliance President Shanna Smith has argued that practices having "a disproportionate and discriminatory effect on protected groups create inefficiencies in housing and financial markets." The bureau's politicization of credit with race is in sync with Attorney General Eric H. Holder Jr.'s Justice Department, which extorted a \$175 million disparate-impact settlement from Wells Fargo and demanded that it finance more minorities, irrespective of creditworthiness. Martin Luther King must be turning over in his grave.

If black Americans were discriminated against based on skin color rather than income, assets and credit, one would expect that with comparable terms and pricing they'd have lower delinquency and loss rates than white and Asian borrowers. This then would be trumpeted by the fair housing

alliance, whose existence is predicated on the fiction of widespread race-based credit discrimination.

Allocating credit based on risk and demand is what financial institutions do. Neither is evenly distributed, as little is in life. In the U.S. Olympic trials, the top eight contestants in the men's and women's 200-meter sprint were black Americans. Disparate-impact theory suggests invidious discrimination must be at work, rather than individuals' different choices, talents and performances.

Credit scores enable consumers to leverage good credit and payment history. Credit card issuers rely on race-blind scores to approve accounts. Paraphrasing King, credit scores judge men by their character, not their skin color. But many liberals don't believe in colorblind credit. In a thinly veiled call for intervention, *The Washington Post* reported "a persistent gap between the credit scores of white and black Americans." Logically, the next step is a call for credit-scoring apartheid, which would be disastrous for financial markets.

Critics should not cede the moral high ground. Disparate-impact doctrine is antithetical to the American ideal of equality before the law. As Friedrich von Hayek noted, "There is all the difference in the world between treating people equally and attempting to make them equal. While the first is the condition of a free society, the second means, as Alexis De Tocqueville describes it, 'a new form of servitude.' "

On top of its inappropriate political role, the bureau increases costs, reduces credit and stifles innovation. Former BB&T CEO John Allison estimates regulation accounts for a whopping 20 percent to 25 percent of personnel costs. The Cato Institute's Mark A. Calabria suggests the Consumer Financial Protection Bureau increased consumer credit costs by 200 basis points and reduced job creation by 5 percent. What's to be done?

Disparate-impact doctrine could be found unconstitutional. One lost opportunity occurred in February when, under administration pressure, the city of St. Paul, Mo., withdrew its Supreme Court appeal of a housing-code case because winning might have eliminated application of the doctrine. Big Springs State National Bank has filed a constitutional challenge,

contending the bureau isn't accountable to Congress or the president or subject to meaningful judicial review.

Another angle is that any exercise of authority conditioned on having a director is unconstitutional because Mr. Obama contemptuously "recess"-appointed Mr. Cordray as director when the Senate was in session. His position is not legal.

Congress should not rely on the courts to correct a problem it created. It should rein in the bureau before it does more damage to our already fragile financial system.

*Eric Grover is a principal at Intrepid Ventures.*