Introduction to the 2004 Annual Survey of Consumer Financial Services Law: Where Do We Go From Here?

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As always, this year's Annual Survey reports on significant developments in the law of consumer financial services. It also reflects dramatically increased tension between state and federal regulators over their respective roles in regulating consumer financial services, and concern about privacy and security of consumers' personal information, evidenced by the passage of major federal legislation in the area that preempts state laws.[1]

This *Introduction* briefly explores the impact that disparate state and federal regulation of consumer financial services has on how and by whom these services are offered, and suggests that a more rational and coherent approach to such regulation is necessary.

The controversy between state and federal regulation is no mere turf war. The history of the dual banking system gives context to the different roles played by the states and the federal government, but the effect goes significantly beyond the regulation of banking *per se*. The states have traditionally been the primary regulator of consumer financial services, but that role has been steadily eroded by federal legislation and regulation since the 1970s, when the enactment of the federal Fair Credit Reporting Act[2] and the Truth in Lending Act[3] started a trend of significant federal consumer protection.[4]

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1. Fair and Accurate Credit Transactions Act of 2003 (the "Fact Act"), Pub. L. No. 108–159, 117 Stat. 1952 (2003), amending the Fair Credit Reporting Act (FCRA), 15 U.S.C. §§ 1681–1681v (2001); S. 877 Title 1—Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003 ("Can-Spam Act of 2003"), Pub. L. No. 108–187, 117 Stat. 2699 (2003).

2. 15 U.S.C. §§ 1681–1681v.

3. 15 U.S.C. §§ 1601–1667e (2000).

4. To name just a few: the Equal Credit Opportunity Act, 15 US.C. §§ 1691–1691f (2000), Consumer Leasing Act, 15 U.S.C. §§ 1667–1667f (2001), Electronic Fund Transfer Act, 15 U.S.C. 1693–1693r (2001), Truth in Savings Act, 12 U.S.C. 4301–4313 (2001).

The federal consumer protection scheme generally has had very limited preemptive effect, leaving the states free to continue to regulate the consumer financial services business and enact their own more protective statutes. Some states (e.g., California and Massachusetts) have both regulated and legislated vigorously, while others have not. At the same time, federally-chartered providers of consumer financial services have enjoyed the preemptive benefits of their federal charter, leaving them (and perhaps their operating subsidiaries) immune from state licensing and, in many cases, regulatory schemes. National banks and federal savings associations have challenged restrictive state laws on a number of fronts and have generally been successful in avoiding these state restrictions on their operations. In the meantime, federal regulators have weighed in on behalf of institutions under their jurisdiction, issuing regulatory pronouncements on the preemptive effect of the National Bank Act and the Home Owners' Loan Act as to national banks and federal savings associations, respectively.

Most recently, in January 2004, the OCC issued rules on activities and operations, including real estate lending, of national banks and their operating subsidiaries that will have the effect of precluding states from regulating virtually all real estate lending operations of such entities.[5] One of the articles in this year's Survey addresses the underpinnings of the OCC's actions in this area.[6] This action by the OCC has sparked opposition from the states and members of Congress, but will probably be left undisturbed, at least for the short term.

Thus consumers and consumer financial services providers that do not enjoy the benefits of preemption are left with an uncertain hodgepodge of federal and state laws and regulations with which to contend. And it is state-chartered financial institutions and state-licensed providers, the vast majority of which are well-intentioned, well-respected members of the business community, that are put at a tremendous disadvantage, because they must comply with federal, state, and, in some cases, local regulation of their activities.

Is this good for business? Probably not. Piecemeal and often contradictory regulation is expensive to comply with, stifles innovation, and hamstrings rapid response to technological change and consumer demand. But, the assumption has been that increased regulation is good for consumers. Is it? The authors think the answer is far from clear.

Do these divergent state and federal schemes and wildly-differing enforcement really address abuses in a meaningful way? It appears that there is no shortage of abusive lenders, nor has there been a substantial decrease in credit and debit card fraud, despite numerous laws designed to curb these problems. Might these abuses be addressed more efficiently by the marketplace, through meaningful, broad-based consumer education (rather than complex disclosure), competition, and the effective use of the existing statutory and regulatory framework?

5. Bank Activities and Operations, 69 Fed. Reg. 1895 (Jan. 13, 2004) (visitorial powers); Bank Activities and Operations, Real Estate Lending and Appraisals, 69 Fed. Reg. 1904 (Jan. 13, 2004) (preemption).

6. *See* Julie L. Williams and Michael S. Bylsma, *Federal Preemption and Federal Banking Agency Responses to Predatory Lending*, 59 BUS. LAW. 1193 (2004).

What can be done to address the disparities in regulation and enforcement and the significant barriers to entry for legitimate and responsible banks, lenders, ATM service providers, and other consumer financial services businesses that do not or cannot enjoy the benefits of a federal charter, and the stifling of expansion and technology innovation caused by this regulatory Tower of Babel?

We have seen one response in the Fair and Accurate Credit Transactions Act of 2003,[7] with federal preemption of conflicting state laws that restrict information sharing. But preemption on a wholesale level is neither a realistic nor necessarily a desirable goal. There is certainly the need for thoughtful action by state regulators and legislators. The National Conference of Commissioners on Uniform State Laws can provide a leadership role in this debate by issuing realistic proposals for uniform laws that also address the impact of such laws on those businesses that do not have federal charters. The Conference of State Bank Supervisors should also play an important part in seeking uniformity in regulation of consumer financial services providers, both through legislative change and regulatory agreements.

Most importantly, however, state legislatures need to recognize the increasingly national nature of consumer financial services, the extreme disadvantage under which state-chartered and state-licensed entities operate and the negative impact that piecemeal and contradictory regulation has on businesses and, ultimately, consumers, who are denied meaningful choice and the benefits of healthy competition and innovation, in the name of "consumer protection" that fails to address abuses adequately.

7. *See supra* note 1.