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New banking bureaucracy may not help consumers

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(PhysOrg.com) -- There's a better way to help banking customers than the new Consumer Financial Protection Bureau (CFPB) that opened for business July 21, says a banking expert at Washington University in St. Louis.

“I’m a big advocate of consumer protection and of transparency,” says Anjan Thakor, PhD, the John E. Simon Professor of Finance at Olin Business School.

“But I would like to have seen a case made for where the existing consumer protection legislation failed and what the alternatives were for dealing with that, as opposed to creating a new government bureaucracy ,” he says.

The CFPB, which was formed as part of the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act, is an independent bureau housed within the Federal Reserve system. Its aim is to promote fairness and transparency for mortgages, credit cards and other consumer financial products.

“I think the premise of this bureau is that somehow current disclosure laws are not enough, and that’s what banks complain about,” says Thakor, a prolific author and internationally noted expert on banking and financial institutions. “I don’t think anyone argues with the need for consumer protection, transparency and information disclosure.

“The disagreement is over the best way to do that. The answer from the administration seems to be to create an oversight watchdog bureau to tell banks what they should do.”

Banks are not necessarily happy about that, Thakor says.

“What banks are nervous about is that they don’t know what this bureau is going to ask them to do,” Thakor says. “Their biggest concern is that many of these bureaucracies eventually devolve into offices that impose enormous reporting duties on banks. It becomes a bureaucratic nightmare to keep track of, document and report so much information. It is going to be costly.”

Thakor says the benefit of the bureau is transparency so consumers don’t get fleeced on credit card fees or mortgage fees, hidden fees or predatory lending.

“But there are already consumer protection laws on the books for all of these things. It’s not like these are neglected items of consumer protection.

“We have regulatory agencies entrusted with enforcing these laws. If people think these laws don’t work, and there are examples of where they have not worked well, we should find out why these laws did not work and what we can do to improve them before creating a new bureaucracy.”

Thakor hasn’t seen any concrete cases listing the failures of current consumer protection laws and in particular why these could not be modified/improved to ensure better consumer protection.

“If the laws are broken, let’s fix them,” he says. “That’s how regulation evolves. We enact legislation in response to crises or market failures, and then we learn that we did not do it right the first time, so we tweak things until they work reasonably well.

"We do not always enact new laws simply because there is some belief that the previous law with the same intent did not work perfectly. I just haven't seen that evolution and refinement process in this case," he says.

The bureau, which will be funded through bank fees, may raise costs for consumers, Thakor says.

"Anything that banks pay for, we end up paying for," he says. "It doesn't come out of thin air. It's very expensive. This may be extremely worthwhile in intent, but it may turn out to be just an albatross.

"Bureaucracies, once created, never go away."

Provided by Washington University in St. Louis

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