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Protecting Consumers from Themselves

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Last year's monstrous Dodd-Frank financial regulation bill contained a number of awful little programs – one of which was the Consumer Financial Protection Bureau (CFPB), the brainchild of Elizabeth Warren, a Harvard Law School professor. Ostensibly, this bureaucracy was created to protect consumers from a predatory financial system by creating new disclosure requirements, promoting "fair competition," and holding companies accountable if they break the law.

On May 24, Warren appeared before the House Oversight and Government Reform Committee to discuss her role and the CFPB writ large. Warren, whose appointment has been stridently opposed by Republicans, faced a tough crowd – and for good reason.

The Cato Institute's Alan Reynolds discovered that Warren co-authored a 100-page article in the November 2008 Pennsylvania Law Review, "Making Credit Safer." As Reynolds states, "Her thesis is that 'many consumers are uninformed and irrational,' so they need to be protected from themselves." Quite the paternalist!

When the government restricts banking options from consumers that it deems "risky,"--which is exactly what the Dodd-Frank legislation does and what the CFPB will continue to do--it sends the message that Americans aren't responsible enough to make their own choices. It's condescending to assume that bureaucrats know what's best for individuals, or can sort out who does or doesn't deserve a loan. We need to stop relying on technocrats to fix the country's woes – because quite simply, they can't, and their fixes often create more problems than they solve.

Banks operate by borrowing money at low rates and loaning it out at higher rates – making a profit in the difference. The higher rates that they charge borrowers are calculated, in part, by the risk that banks feel their customers pose. When customers are a higher risk and more likely to default, banks charge higher rates, which help to offset possible losses from defaults. Should banks not be allowed to charge higher rates to these high-risk customers, they will simply choose to not lend to them at all – and leaving those customers with fewer options to access needed capital.

The market protects consumers. Businesses operate and thrive based on their reputations. If businesses and corporations are exploitative, they'll lose market share. And if businesses lie, deceive, or collude, that's called fraud – which is still against the law – and they can be prosecuted accordingly. We don't need a brand-spanking-new agency to do that.

As far as "predatory lending" is concerned (payday loans, for example), by and large, consumers know what they're getting into. When people take out such loans, they realize they are paying a premium for this service – and are charged accordingly. They weigh the pros (short-term cash) against the negatives (higher cost), and when it is deemed necessary – perhaps to keep their checking account from becoming overdrawn, and from incurring additional fees – they act.

Prohibiting and restricting the use of these banking products is akin to price-fixing – and no good has come from that in the past. Price fixing and its cousin rate-setting will lead to shortages of capital. Those consumers who need these services to cover short-term expenses – young people, the poor, and business start-ups – will be hurt by lack of access.

As documented by the Heritage Foundation, the CFPB's authority is vast – and frighteningly, virtually unchecked. As such, there is a very real possibility that this agency will become tyrannical because of its lack of accountability.

Ultimately, consumers should be allowed to make their own banking decisions, free from government interference. As Congress goes forward with its plan to defund and repeal laws and agencies that hurt Americans and slow growth, the Consumer Financial Protection Agency should be at the top of the list. It's expensive, unnecessary, and burdensome, and it will hurt the very consumers that it claims to help.

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