

Remarks by
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It is a pleasure to be with all of you this afternoon. It is a particular honor to address *both* Women in Housing and Finance *and* The Exchequer Club, who have come together for this first special event of 2005.

I'm going to talk about how we use disclosures to accomplish consumer protection objectives in the banking business, and how that approach is in danger of breaking down. Despite good intentions and enormous resources expended, it's not working as well as it should for consumers, and it is imposing unnecessary burdens on bankers. But, there is something we can do about it, and I'll talk about that as well.

As we take stock of the banking industry today, the financial state of the industry is healthy and it is strong. Measured in quantitative terms – earnings numbers, capital levels, asset quality statistics – the industry's performance and its capacity to weather some recent challenging economic times is admirable. The stability and prosperity of the banking system should continue to serve as a pillar of strength for the national economy as well as a source of reassurance to individual consumers who look to banks as trusted institutions and repositories of their savings.

One notable reason for the industry's recent success is that, over the past decade or so, a major reorientation of the banking industry has occurred, bringing great benefit to American consumers – and to the industry itself. Banking has become more consumer-driven and more attuned to consumer needs than ever before. The industry has come to depend increasingly on the consumer as a steady and solid source of earnings. These changes have brought consumers new financial options and opportunities, which have contributed to rising homeownership, increased small business formation, and greater convenience and financial access.

This success has occurred in a regulatory environment that encourages competition, choice and the operation of free markets for bank products and services. Although banks are highly regulated, bank regulation typically does not dictate the prices, terms and detailed features of the financial products and services banks are authorized to provide. This approach has enabled U.S. banks to evolve and grow their businesses, expand their product offerings, and better serve their customers.

How banks treat their customers is vital to the soundness, stability and future of their franchise, and consumer protection is an important component of bank regulation. While I'm sure bankers would say that they are subject to extensive consumer protection requirements, most of these do not dictate the terms, conditions and prices of banks' products and services, but rather require various forms of consumer-oriented disclosures. The rationale for this approach is that, through disclosure, consumers have the broadest access to products and services, and also have the information necessary to make rational decisions in their economic self-interest; in other words, to protect themselves. This avoids the government stepping into a role of dictating prices and terms of financial products and preserves the healthy effects of competition, choice and the operation of free markets.

With the increasing significance of consumer business to the banking industry today, and with disclosures at the foundation of our consumer protection regime, it is important that disclosures *work* to effectively inform consumers of what they want to know. I worry, however, that this approach is on the verge of breaking down, and if it's not re-focused, more prescriptive legislation and regulation could result. And it's reached that point not because consumers are getting too little information, but because they are getting *too much* information that's not what they're really after; and because the volume of information presented may not be *informing* consumers, but rather *obscuring* the what's most helpful to their understanding of financial choices.

In recent years, regulators – and Congress – with the best of motives, have approached many new consumer issues in the financial services arena by requiring more and more information to be provided to consumers – constantly playing catch-up with rapidly evolving market practices. Even the precise presentation of the information is sometimes specified for some transactions: prominent, “clear and conspicuous,” and more recently, apparently reflecting that “clear and conspicuous” has often really meant “obtuse and lengthy,” Congress has required consumer notices to be “clear, conspicuous and *concise*.”

So where has this brought us? Do you feel enlightened by the disclosures you get, or do you feel like you have been enveloped in a cobweb of details and legalese?

How many of you have a mortgage or home equity line of credit? How many of you actually read *and understood* the documents you received in the application and approval process?

How many of you have credit cards? How many of you have been dazed by the detail and fine print of your credit card agreement? Have you ever actually tried to read it? How many could tell me under what circumstances your credit card company is allowed to change your rate and what your options are if that happens?

How many of you care about your privacy rights, but have pitched out all those privacy notices where your bank or broker or insurance agent vows that it cares about your privacy?

This current state of affairs breeds understandable frustration and cynicism among consumers. Consumers who see just a haze of fine print, instead of the information they want and need, may understandably conclude that certain information is *deliberately* being obscured. Surely, no banker – or bank regulator – wants consumers to think that.

And how does the current regime impact the industry that provides all this information? To take an example, according to one estimate, the privacy notices mandated by the Gramm-Leach-Bliley Act alone could cost the industry hundreds of millions of dollars annually. Now consider all the other types of consumer disclosure requirements to which banks are subject and imagine the aggregate cost. What activities and initiatives suffer because banks must bear these costs?

Banks large and small complain about the costs and burdens of various consumer compliance requirements. The interagency regulatory burden reduction project ably led by FDIC Vice Chairman John Reich has highlighted these concerns. Community banks, in particular, assert that the impact has implications for their long-term viability. I believe that these concerns are sincere and that they have merit.

And this industry reaction rings not just as a complaint about costs. The expense associated with developing and distributing disclosures would be more palatable if they better accomplished their purpose: to get vital information into the hands of consumers to make informed choices and to promote healthy competition among financial providers. But the evidence suggests that, despite all this investment in disclosures, we have quite a distance to go to accomplish this goal.

I don't mean to suggest that we should discard the basic approach of reliance on disclosures and consumer choice to accomplish important consumer protection objectives. One of the great strengths of our financial system is that, with limited exception, the government does *not* dictate the price and terms of products and services that may be offered. But, in order for this free market to work, consumers need to have the means to make *informed* decisions.

To better accomplish this, I respectfully suggest that just about every major participant in the processes of developing, designing, implementing, overseeing and evaluating consumer disclosures for financial products and services needs to rethink their approach to those tasks. This includes Congress, regulators, bankers, and consumer advocates.

With much trepidation, I'll start with Congress. In recent decades, when Congress has passed laws with a consumer protection component, the legislation frequently includes specific requirements concerning the content of information to be provided to consumers. Also, it has been typical of recent legislation for the agencies charged with drafting rules to implement those requirements to be given very short deadlines to finish their work. In the case of the GLBA privacy standards, for example, seven financial regulatory agencies were expected to propose and finalize regulations

implementing complex statutory requirements and exceptions that were consistent on an inter-agency basis, *in six months*.

Typically, the job of drafting these rules falls to compliance specialists and lawyers, who, predictably, go to great lengths to ensure that every “i” is dotted, every “t” is crossed, and that all legal nuances are provided for. The results can be expected to be comprehensible to other lawyers and compliance experts – who are justifiably concerned about civil liability from the consequences of noncompliance with complex compliance requirements. But are the results comprehensible to the typical bank customer of average education, attention span, and eyesight? It can take great fortitude to wade through multiple pages and paragraphs until the single passage that addresses a consumer’s particular interest is unearthed.

Let’s compare this example to the experience of the Food and Drug Administration developing another type of consumer disclosure, the “Nutrition Facts” label that we consult to make sure that we get our vitamins and minerals – and not too many calories, carbs, sodium, or fat. Think about how frequently you check out the calorie count on a candy bar or bag of potato chips, the carbs for a loaf of bread, sodium in a can of soup, or the fat content of different brands of yogurt. The “Nutrition Facts” box may be the most prevalent and frequently used consumer disclosure in the marketplace today. And the clear labeling of nutrition content has not only enabled consumers to find products with the nutritional characteristics they’re seeking, it has influenced food producers to develop products that consumers want. In other words, these disclosures have been effective and *useful* to consumers.

How did this happen? The effort that led to the FDA’s nutrition labeling began with a clear statement by Congress of the *objective* the FDA was charged to accomplish. While Congress did specify certain nutrition facts to be disclosed, it also provided the FDA with the flexibility to delete or add to these requirements in the interest of assisting consumers in “maintaining healthy dietary practices.” It left to the FDA’s discretion the design and format of the nutrition label.

Based on the direction and goals set out by Congress, the FDA took several *years*, in an effort that involved intensive research not only by nutritionists, but also by social scientists who polled focus groups to elicit ideas on the kind of information consumers *wanted* to see, experimented with dozens of different formats, and tested those formats with target consumer audiences to determine what actually worked. The “Nutrition Facts” box disclosure was the result of painstaking laboratory and fieldwork, notably including extensive input by consumers.

What might we learn from this? First, that Congress should consider more emphasis in financial services legislation on articulating the *goals* to be achieved through a particular consumer protection disclosure regime, rather than the precise elements of mandated disclosures. And, second, that Congress should look for opportunities to require, and *please provide adequate time for*, regulators to include consumer testing as part of their rulemaking processes.

And what about the regulators? Clearly, we need to change too. We need to embrace consumer testing when we design, or attempt to redesign, consumer protection measures. Let's just admit that we can't throw a bunch of lawyers – however talented – into a room and expect that they are going to come up with consumer disclosures that are understandable to most people. There's a critical element that's been missing from our consumer disclosure rulemaking processes – testing *how consumers interpret* particular disclosures and how to make disclosures *usable* to them. And we also need to think about how we can build in periodic reviews to determine if the disclosures are still desired and effective.

Enhanced consumer input as part of the regulatory process, using the techniques that market researchers use, also will help deal with the problem of information overload by enabling agencies to focus rulemaking requirements on the information that is actually useful to consumers.

A good example of a current effort in this regard is the interagency undertaking to consider revisions to the GLBA privacy notices. In 2004, the OCC, the FTC and other federal banking agencies published an Advance Notice of Proposed Rulemaking outlining and seeking comment on a new approach to privacy notices – one that would make these notices easier for consumers to understand and use. The agencies sought comment on several sample versions of streamlined, short-form notices, with key information presented in a simplified check-the-box or yes/no format, and more detailed information available in a “layered” approach, either in another accompanying document, or upon request.

Importantly, the agencies also retained expert consultants to test privacy notices with consumers. It's startling, but true, that this is the first time in years that the banking agencies have tested *first* to see what disclosures were effective with consumers *before* promulgating a regulation requiring them. Based on what I've heard from the experts, I expect the results will be enlightening and humbling, and will reinforce my conviction that drafting consumer disclosures is a task that must *not* be left to the lawyers.

Another adjustment agencies need to make is to recognize that disclosure regulations generally will never keep pace with market developments, and that it is simply impossible to come up with regulations to address every new issue that crops up or each new business practice that may appear sharp or unfair. The regulatory process simply is not fast enough. Moreover, some people will make questionable decisions even with the benefit of the best disclosure practices. Just think of the things you've eaten even *after* you noted their nutritional content!

What this does mean, though, is that regulators must be willing to step up to the plate to cause correction of certain behaviors – even where a practice is not specifically prohibited, or a disclosure or action is not specifically required by a regulation. Effective consumer protection oversight by the banking agencies needs to be a combination of enforcement of specific regulatory standards and application of qualitative supervisory

judgment. Just because a practice isn't specifically an illegal practice doesn't mean that it's an acceptable practice for a federally regulated financial institution.

The banking agencies have a variety of tools available to implement this approach. I am pleased to say that the OCC pioneered the use of an important one of those tools – section 5 of the Federal Trade Commission Act – as a means to address practices by banks that may be unfair or deceptive.

At the OCC, we also use advisories to alert national banks to practices and developments that require their attention and response, and we recently issued an advisory on certain credit card marketing practices. Although we supervise many of the major credit card issuers, we are not the rule-writers for the disclosures they are required to make under the Truth in Lending Act. But what we have done, through our recent advisory, is highlight information practices that we view as unacceptable because of the compliance, legal and reputation risks they present. Even though these practices may not be prohibited – or even addressed – by Reg Z, we believe they are not consistent with sound banking practices.

We are in the process of reviewing and evaluating the disclosures of major national bank credit card issuers, and we will use the results of that process to advise individual banks on any corrective steps that we believe are appropriate. At this stage in the process, I think I can say two things: first, on the whole, I am encouraged that the reaction to our effort has been constructive, and second, I am optimistic that this process can result in real benefits for credit card customers of national banks and for the banks as well.

That brings me to the banking industry. Bankers complain that banks are subject to excessive regulatory burden. Much of that burden is in the form of various types of disclosures and notices that they are required to provide, which they contend are not used or useful to their customers. Personally, I think there's merit to those complaints. But, it does trouble me that, when presented with the prospect of lessening burden and saving costs by providing a streamlined, short form privacy notice containing only certain key information – some in the industry seem to balk. Marketing departments get uneasy because simple and straightforward disclosure of a bank's information sharing policies and an easy means for customers to opt out of that sharing might mean – *that customers will actually understand those policies – and decide to opt out!* The tension here is that shorter, focused consumer disclosures can meaningfully reduce regulatory burden, but, if they are done well, they will also empower consumers to make some decisions that a particular bank may not like.

I could make a similar point about credit card disclosures. This industry is highly competitive and card issuers are always soliciting for new customers. But whether you are opening a brand new account, or considering a balance transfer from an existing account, how easy is it for you to compare important terms beyond the APR? Can you shop for a card based on an issuer's ability to raise your rates or change other fees and terms?

If we could better identify the key information that credit card customers today really want and provide for its disclosure in a format that is easily understood and comparable between different card issuers, consumers could make informed choices in selecting a card and how they use it. I commend the recent action by the Federal Reserve Board to initiate a rulemaking process under Reg Z to address credit card disclosures, and in particular their plan to use consumer focus groups in that process. I hope this effort will result in some fundamental changes in the content and presentation of information that is disclosed to credit card customers, not just an overlay of additional disclosure requirements. It's a golden opportunity to better inform consumers *and* lessen regulatory disclosure burdens *and* enable consumers to comparison shop.

Finally, a few words about the role of consumer advocacy organizations. Consumer advocates have a vital role in the bank regulatory environment. They bring issues and concerns to our attention and they advise us of important trends. And they serve as a valuable reality check, telling us things we need to know, although not always what is pleasant to hear.

In that spirit, I'll turn the tables for just a moment. First, what seems to be absent in the dialogue with consumer organizations is a discussion of the interplay of how to better inform consumers by disclosing *better*, but not necessarily more, information, and the impact of regulatory disclosure burdens on banking institutions. And why aren't consumer organizations berating us to do consumer testing to find out what consumers really want and think is important? The time has come to think in these terms, and consumer organizations have opportunities in connection with the privacy notices project I mentioned and the Fed's review of Reg Z to offer us some fresh ideas.

Second, consumer organizations play a vital role in enhancing the financial literacy, and therefore, the financial capacity, of consumers. A component of *informed* consumer choice is the capacity of customers to appreciate the significance of key information when it is disclosed to them. Many consumer organizations are positioned to ascertain and highlight for different groups of consumers the features of financial products of most consequence to that type of consumer. We need to encourage and enhance those efforts.

Can each party to the process muster the resolve to change their approach? It will be hard, and we all need to recognize that it will take time, but I hope we can. The benefits will be better-informed, better-protected consumers; clearer accountability concerning consumer treatment and consumer behavior; reduced regulatory burden; and a more robust financial services marketplace for all.

Thank you very much.