Taskforce on Federal Consumer Financial Law

Draft **: Competition and Financial Consumer Protection**
And appendices
Dodd-Frank Act and Enumerated Statutes on Competition /
History of Competition and Credit

Introduction

In the United States, as in any market economy, goods and services reach their customers through markets. Most familiar to consumers are retail markets, where millions of stores, dealers, and workers sell everything from groceries to automobiles to health care. On the way to retail outlets, the necessities and comforts of life pass through intermediate markets in the transformation from raw materials and human talent to finished products and services. The availability and affordability of it all depends on the capacity and efficiency of the markets through which the streams of commerce flow. Intuition and experience agree with economic theory that markets work best for buyers when they can choose among competing sellers.

Redacted

All markets rest on a foundation of financial markets. Financial services – the means by which people spend, save, and borrow – reach consumers through markets as well. Consumers cannot acquire the necessities and comforts of life without cash or credit to pay now or pay later. If currency and credit are inaccessible, goods and services are, too. If financial instruments are unnecessarily expensive, they will raise the cost of purchasing and reduce the rewards of saving. Poorly functioning financial markets exact tolls on consumers, whether they are dealing in the markets or excluded from them.

A financial market is not working if people who can afford its offerings cannot acquire them. Nor is it working if participants who can afford its features cannot avoid excessive overcharges. Nor is it working when consumers cannot avoid deceptive, unfair and abusive acts. It is the goal of financial consumer protection to prevent this behavior, and to remedy the injuries that occur when such practices harm consumers.

Because harm to consumers can come from countless sources and take on many forms, effective consumer protection must rely upon numerous methods to diminish the danger of mistakes, malfunctions, and malfeasance. Enforced judiciously, consumer protection laws can reinforce the conditions of markets that function well. Sanctions against misleading and deceptive claims improve the probability that consumers will make good decisions, because confused and misled consumers are more likely to make expensive mistakes. Standards that make information clearer and more coherent can facilitate comparisons among competing alternatives. Because credit markets involve promises of future performance, parties must be able to expect counterparts to honor obligations.

Legal systems that provide for contractual clarity and efficient enforcement can enhance confidence in expectations.

Deception and abuse are antithetical to efficient markets, which rely on voluntary exchange of goods and services. Law enforcement that suppresses misappropriation, extortion and other variants of theft, unfairness and abuse therefore improves market performance. Of course, uncertainties and misunderstandings can accompany transactions, especially those that span months or years, so a well-functioning market relies on rules and procedures that deal with unanticipated mistakes, economic distress, and contractual breaches in an efficient manner.

With potential hazards coming in many forms from many sources, no single measure can protect consumers from them all. Likewise, no single solution can remedy every injury that consumers may suffer. Accordingly, a robust regime of consumer protection deploys a combination of approaches and measures. The Dodd-Frank Act gave the Bureau a full complement of consumer protection tools, and these are described in other chapters. This chapter concerns a tool that is often overlooked in discussions of consumer protection and the Bureau's powers – the preservation of competition.

Before the Dodd-Frank Act laid out the powers of the Bureau, the statute described the purpose of the agency and objectives Congress intended it to pursue. A single sentence stated the purpose:

> The Bureau shall seek to implement and, where applicable, enforce Federal consumer financial law consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive.[1]

Elaborating on that purpose is a set of Objectives, each of which, implicitly or explicitly, gives a role to competition:

> The Bureau is authorized to exercise its authorities under Federal consumer financial law for the purposes of ensuring that, with respect to consumer financial products and services—
>
> **(1)** consumers are provided with timely and understandable information to make responsible decisions about financial transactions;
>
> **(2)** consumers are protected from unfair, deceptive, or abusive acts and practices and from discrimination;

[1] 2 U.S. Code § 5511 (a).

> **(3)** outdated, unnecessary, or unduly burdensome regulations are regularly identified and addressed in order to reduce unwarranted regulatory burdens;
>
> **(4)** Federal consumer financial law is enforced consistently, without regard to the status of a person as a depository institution, in order to promote fair competition; and
>
> **(5)** markets for consumer financial products and services operate transparently and efficiently to facilitate access and innovation.[2]

These objectives rest on the proposition made explicit in the purpose of the Bureau – that competition is fundamental to consumer protection. The first two objectives are to ensure the flow of information that enables consumers to choose wisely among competing alternatives. The third objective, reducing unwarranted regulatory burdens, removes unnecessary costs, which can impede competition from smaller companies and raise prices beyond consumers' reach. With respect to the fourth objective, the Congressional call for enforcement that gives no advantage to any sector could not be a clearer mandate for fair competition among financial service providers. As for the fifth, the goal of preserving markets that facilitate access and innovation refers to the most recognized aspect of effective competition – expanding quantities and lowering costs of goods and services. This objective also highlights one of the most dynamic aspects of competition in the financial sector. Major advances in the history of consumer finance have been marked by innovations that made credit more convenient, more accessible, and less expensive.[3]

In emphasizing the importance of competition to the mission of financial consumer protection, Congress drew upon a consensus that has enlightened trade regulation for centuries. The consensus includes a large body of academic research, a century of Federal economic policy, and a comprehensive assessment of consumer finance by a commission Congress created fifty years ago, the National Commission on Consumer Finance. After two years of research into virtually every aspect of consumer finance, the Commission concluded that "a truly competitive consumer credit market, with adequate disclosure of relevant facts to an informed consuming public, together with legislation and regulation to eliminate excesses, will foster economic growth and serve to optimize benefits to the consumer."[4] These benefits did not come at the expense of consumer protections. To the contrary, explained the Commission, "Painful as competition may be for the participants, it provides the ultimate protection for most consumers."[5]

---

[2] 12 U.S.C. § 5511(b).
[3] In addition to the direct objectives assigned to the Bureau, Congress placed a limitation of its authority in order to prevent it from supplanting competition. The Bureau is prohibited from setting interest rates. It is well recognized that allowing supply and demand to determine prices (and the price of credit is no exception) is the mechanism by which markets function, and the res
[4] Milstein, Letter to the President and Congress, December 31, 1972.
[5] NCCF 214

The Report supported its conclusion with the observations that competition enhances consumer welfare more effectively than any other influence on commercial behavior, and is "the best regulator of the consumer credit marketplace."[6] Accordingly, the Commission envisioned an important role for antitrust enforcement, which should be "particularly alert to the dominance of consumer credit markets by a few firms, by barriers to entry, and to restrictive arrangements in the credit industry."[7] Antitrust enforcement could not be expected, however, to remove competitive impediments that were anchored in regulation. The Commission therefore advocated the repeal of laws that fixed rates or prohibited services that consumers could access in competitive markets, and it urged the removal of legal barriers segregated financial institutions into sectors and prevented lenders in one from serving borrowers in another.[8]

That competition is critical to consumer protection was neither novel nor controversial when the Commission espoused the idea. The best-selling economic textbook of the time (indeed of all time) was teaching the same lesson to college students and demonstrating how that lesson applied to credit markets.[9] Professor Paul Samuelson, who had won the Nobel Prize in Economics in 1970, explained in his text that year how competition can empower borrowers to obtain credit "at the cheapest possible terms" just as it allows shoppers to get the best prices from butchers.[10] He had made the same point to the Massachusetts legislature in 1969, when he testified on the proposed Uniform Consumer Credit Code:

> A great deal of practical experience has accumulated among our various states and from careful comparisons across countries, to show that the consumer is most improved by effective…competition so that a range of alternatives are open to each consumer and so that each lender knows that his monopoly power to exploit the needy borrower is severely limited by these alternative opportunities. The same principles have been found to prevail in the market for small loan finance as in the markets for the necessities of life.[11]

Samuelson was far from the first economist to recognize the importance of competition, its role in protecting consumers, and its application to finance. Similar observations can be found in the work of Adam Smith, often regarded as the original economist.[12] In a

---

[6] Id. at 4
[7] Id. at 3
[8] Id.
[9] Samuelson, Economics, 8th Edition (1970) 578-79. The remarkable popularity of the textbook is reported in Elzinga, Kenneth G., "The Eleven Principles of Economics," Southern Economic Journal, April 1992, 58:4, 861–79.
[10] Samuelson, Economics, at 579.
[11] Statements of Former Senator Paul Douglas and Professor Paul Samuelson on the Uniform Consumer Credit Code, National Conference of Commissioners of Uniform State Laws, January 29, 1969 p. 8.
[12] See Samuelson at 1. The coincidence of Smith's publication with another notable event in 1776, the Declaration of Independence, was not by chance, said Samuelson: "[P]olitical freedom from the tyranny of monarchy was closely related to the emancipation of free-market pricing from the interfering hand of state regulation."

treatise he published in 1776, *The Wealth of Nations*, Smith observed that the market, like an "invisible hand," would direct sellers' self-interest to the service of buyers.[13] His prediction came with a critical caveat, however. The market had to be competitive for buyers to benefit from the invisible hand. Smith concluded that best incentive to keep a seller honest and fair was the fear of losing customers to a competitor. That was the "real and effectual discipline" that "restrains his fraud and corrects his negligence."[14] And to Smith there was no question whether the principle applied to financial firms. Competition among banks, he said, "obliges all bankers to be more liberal in their dealings with their customers, lest their rivals should carry them away. In general, if any branch of trade, or any division of labor, be advantageous to the public, the freer and more general the competition, it will always be more so."[15]

By 1972, a consensus had formed among economists as to the circumstances that advance competition and the conditions that impede it. The Commission drew upon this consensus and applied the analytical framework to the observations and data from remote and then-recent history of credit markets. For the most part, the conditions that qualified as catalysts of competition and contributors to consumer welfare remain recognized as factors that contribute today. By the same token, the obstacles identified as impediments to competition and costs to consumers have been found again and again in markets across the economy. Those circumstances and their effects – both favorable and unfavorable – will be the focus of this chapter.

Nothing in the fundamentals of financial markets suggests they would suffer from a lack of competition. The principal resources – financial and human capital, communication and information technology – are readily available and highly mobile. Financial intermediaries need offices, of course, but not the massive mines and factories of heavy industry to extract raw materials and process them into finished goods. Transportation costs are miniscule for both the inputs that the institutions acquire and the outputs they deliver; funds of any amount move cheaply and easily.

To be sure, financial intermediation – from the acquisition of capital to the delivery of services – requires efficient organizations, talented personnel, and sophisticated business models. Institutions with expertise, and scale are more likely to succeed in obtaining capital at low costs and offering financial services on attractive terms.[16] Some services require national and global networks to be feasible and desirable. Above all, a reputation

---

[13] Smith, Wealth of Nations (1776) 14. Smith also recalled the butcher in explaining the working of a free market. In one of the most famous passages from the treatise, he wrote, "It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest."
[14] Wealth of Nations 129.
[15] WON 313 (Smith also explained how competition encouraged prudence, and in a premonition of modern concerns about institutions too big to fail, hypothesized how competition could diminish the risk of financial system failures.)
[16] A study performed for the Commission noted relatively modest scale economies for loan offices. CR 286, n.3. Modern scholarship agrees. [cite]

for integrity and reliability is a critical credential in financial affairs, and a history of honorable behavior confers credibility. Successful incumbents are likely to have advantages over newcomers.

But incumbents with advantages over newcomers are neither unique to financial services nor incompatible with competition. Companies can multiply and industries can grow even when economies of scale and venerable reputations give advantages to familiar firms. Nowhere has this been more evident than with consumer credit, which has seen a proliferation of new lenders and new products, aggregate growth, adaptation of market leaders, and decline or departure of companies that could not keep pace with the others. These are the hallmarks of competitive markets.

Notwithstanding propitious conditions and encouraging indications of competition in credit, the Commission identified numerous problems that prevented financial markets from performing as effectively as a competitive market would be expected to do. Among the impediments to competition were various forms of restrictive licensing, limitations on services that companies could provide, geographical and sectorial barriers between institutions, and other conditions that made credit needlessly expensive to some and entirely unavailable to others. Some of the impediments were imbedded in regulation and legislation. Others stemmed from perceived anticompetitive behavior in the industry.

These concerns warrant reexamination. If such conditions persist today, they could be thwarting or diminishing the forces that would otherwise have given consumers the benefits of better rates, greater access, and more services that robust competition can deliver.[17] Collectively, they could have imposed significant costs on consumers. The chapter will first review the historical background to the Commission's findings and recommendations on the state of competition in consumer finance. The discussion then turns to the findings themselves. Then the chapter describes the evolution of credit markets since the Commission's report and assesses trends that help explain the competitive circumstances consumers face today in credit markets. Finally, the chapter identifies measures that could improve the quality, quantity, and affordability of financial services available to consumers.

Competition and Consumer Credit Before World War II

The Commission's Report began with a brief description of the development and structure of consumer credit, and its role in growing American economy. Colonial life depended on credit. Farmers bought seeds, supplies, and food on account. Farm debt

[17] Many of the conditions and controls have been the subject of lobbying, litigation, or legislation. Arguments for the conditions have ranged from appeals for safety and stability to complaints about unfair competition. Whatever the rationale, when competitors in a segment mount campaigns to insulate themselves from competition, it suggests that profits will flow to them if they prevail, and it is therefore worthwhile to assess whether those profits stem from diminished competition that imposes costs on consumers.

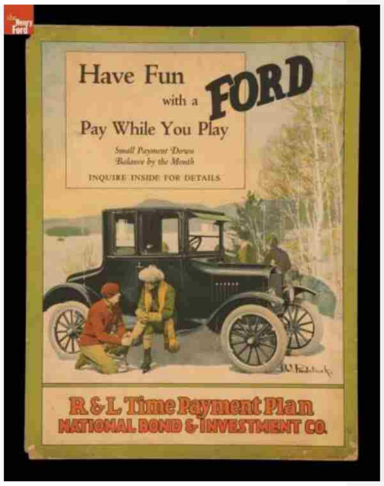
could accumulate for months as the expenses of plowing, planting, food and shelter mounted, finally to be repaid when the crops came in. City dwellers regularly purchased on credit as well, especially durables like furniture. But credit was not limited to large transactions. Cash was scarce in the colonies, so promises to pay were the means of exchange at merchants of all types.[18] By the middle of the 19th century, credit in the form of installment payments became a popular method of purchasing pianos, books, and sewing machines. In the early 20th century, consumer installment loans helped the automobile business evolve from a patchwork of workshops to an industry of sprawling factories.

Principal providers of consumer credit in the young United States were noted in the Report. Merchants remained a ubiquitous source as economic activity gravitated to the urban centers of the industrial revolution. Growing cities presented a variety of alternatives to merchants' advances. Flourishing markets emerged for small loans as finance companies offered loans to consumers who ran short between paydays. Pawnbrokers remained a popular option for consumers, and entirely new institutions appeared. The Report noted the arrival of credit unions and Morris Plan Banks around 1910, for example, and it could have noted many others – immigrant banks, industrial banks, thrift institutions. Largely absent from the origins of consumer credit, however, was the commercial bank. With few exceptions, traditional banks did not join the direct competition for consumer finance until it was well developed in the United States.[19]

Perhaps no historical episode illustrates the synergy between credit, competition, and economic growth better than the origins of automobile financing. Henry Ford built his first car in 1896 and used the $200 he got from its buyer to work on his second car. Recognizing the need for more capital to increase capacity (some thirty manufacturers were producing 2,500 motor vehicles a year by 1899),[20] he went into debt, defaulted, and declared bankruptcy. Then he tried again, failed again, and declared again. Undaunted, he took another foray into capital markets, this time with the Ford Motor Company (FMC) in 1903, which he envisioned would "build a motor car for the great multitude…so low in price that no man will be unable to own one."[21] The Model T was the result of that vision when it arrived in dealerships with a price tag of $850 in 1908.

Most working families could not write checks for $850, worth about $24,000 in 2020 dollars. The Model T would have remained a rare luxury reserved for the rich, if the

[18] See the historical appendix for examples of credit in the colonial economy.
[19] Report at 5. Of course, to the extent that commercial served the companies financing consumer loans, the banks played an indirect role.
[20] [HYPERLINK "https://www.history.com/topics/inventions/automobiles"]
[21] Ford quote available at [HYPERLINK "https://www.autodesk.com/products/fusion-360/blog/moving-millions-henry-ford-made-automobile-affordable-every-american/"].)



average consumer could not borrow the money to buy a car. In an era when personal debt still carried a social stigma (moralists of the day decried "consumptive credit"), Ford declined to become the creditor of his own customers. Instead of financing purchases of the Model T, the company offered a Weekly Purchase Plan, in which buyers could deposit $5 a week at their dealership until they had saved enough to buy their new cars.[22] Most consumers who started a plan never finished it. Ford might have foundered yet again if consumers had not found another way to buy their cars. They did, thanks to finance companies that entered a market Ford had shunned. The Model T succeeded, and Ford led the industrialization of the twentieth century.[23]

Between 1917 and 1922, according to one study, the number of finance companies making car loans grew from a dozen to a thousand. By 1925, over 1,600 were in the market.[24] The competition helped increase automobile ownership from one in thirteen families in 1918 to four in five by 1929, when production reached 5.3 million vehicles, [25] three quarters of which were bought on credit.[26]

The history of credit and cars is hardly unique. Consumer debt rose from an estimated $3.3 billion to $ 7.6 billion from 1920 to 1929.[27] Automobiles accounted for about half of it in 1926, followed by household furniture (with 19 percent), pianos (7 percent), while sewing machines, phonographs, washing machines, radios, jewelry, clothes, and tractors rounded out the top ten categories.[28] Good customers of The Hudson store could obtain a personal charge token, the forerunner of modern credit cards. Marshall Field's strategy

[22] Henry Ford Museum of American Innovation, [HYPERLINK "https://www.thehenryford.org/collections-and-research/digital-collections/artifact/355541/"].

[23] Id. at [HYPERLINK "https://www.thehenryford.org/collections-and-research/digital-collections/artifact/149966"]. Neglecting the demand for consumer finance may have cost Ford. The Motor Company improved efficiency, reduced prices, updated models, and added options, but it steadfastly refused to finance the cars it sold. Its smaller competitor, General Motors, recognized the importance of credit to car buyers and in 1919 created its own financing arm, General Motors Acceptance Corporation. For the next decade, GM customers without enough cash to buy a car could choose between GMAC and external financing. They took advantage of the competition, flocked into dealerships and drove out in new cars. Not until 1928, when Ford introduced the Model A, did the company join the credit competition. By then it was too late to prevent GM from overtaking Ford as the nation's top auto maker.

[24] Calder, Financing the American Dream, Princeton University Press, (1999) at 192.

[25] Mac's Motor City Garage, "The year in Cars: 1929," (2013), available at [HYPERLINK "https://www.macsmotorcitygarage.com/the-year-in-cars-1929/"]

[26] [HYPERLINK "https://www.history.com/topics/inventions/automobiles"]

[27] Lendol Calder, Financing the American Dream, Princeton University Press (1999), 18.

[28] Id. at 203.

was to know its customers personally (sometimes with information from credit reports).[29] "By 1930, most appliances, radios and furniture were bought on the installment plan," according to one historian.[30]

Innovation drove competition in the early decades of consumer credit. The thrift industry, an innovation of the 1800s, became a major source of large consumer loans of the twentieth century. These precursors of savings and loans (known as "building and loans" then) were membership institutions that collected savings from shareholders to finance home purchases. After the first one opened in 1831, they spread to a handful of states before the Civil War, and then to every state in the union by 1890. In 1914, one survey counted 6,600 thrifts nationwide.[31] Their loans differed from bank mortgages. Thrifts offered longer terms and amortized loans, whereas banks typically collected interest during the term and payment in full at expiration. From all the sources available, one estimate urban real estate mortgages rose from $11 billion in 1920 to $27 billion in 1929.[32]

A variation of the thrift model that developed in the early 1800s, specifically for a consumer clientele, was the mutual savings bank, the first of which were founded by charitable organizations. Their original purpose was, as described in an FDIC history, "to help the working and lower classes by providing a safe place where the small saver, then shunned by commercial banks, could deposit money and earn interest." At first these banks invested very conservatively, confining their portfolios to government bonds and other safe securities. By the turn of the century, they were financing a wider variety of long-term loans, including mortgages, and they grew rapidly, from 10 in 1820 to 637 in 1910. Total deposits grew from $1 million to more than $3 billion.[33]

Financial innovation accelerated in the early 1900s, with the arrival of two new types of institutions. In 1909, the first credit unions opened, an adaptation of similar institutions in Europe. They caught on quickly, on the strength of its organization as a nonprofit entity, which gave them the cost advantage of tax-free status and allowed them to offer lower rates on loans. A year later came the first Morris Plan Bank, which offered a financing method that appealed to consumers who could not qualify for legal loans under the usury caps at the time. Morris Plan Banks avoided usury sanctions by dispensing only part of the loan as cash and keeping part in the form of a hypothetical deposit, which had the

[29] See historical appendix.
[30] Stephen Smith, "The American Dream and Consumer Credit," American Public Media, (2018), [HYPERLINK "http://americanradioworks.publicradio.org/features/americandream/b1.html"];
[31] David Mason, Savings and Loan Industry (U.S.), available at [HYPERLINK "https://eh.net/encyclopedia/savings-and-loan-industry-u-s/"]. At the time, according to FDIC, about 25,000 state and national commercial banks were operating in the US. [HYPERLINK "https://www.fdic.gov/about/history/timeline/1900-1919.html"] 1911
[32] Caldor.
[33] Federal Deposit Insurance Corporation (FDIC). 1997. *History of the Eighties: Lessons for the Future.* Vol. 1, *An Examination of the Banking Crises of the 1980s and Early 1990s*. Washington, DC: FDIC. Ch. 6

effect of raising the interest rate on the borrowed cash (and also the benefit of building capital). Sometimes called "industrial banks" because many of their customers labored in mills and factories, Morris Plan Banks obtained specific legislative authorization in many states. By one estimate, over a hundred Morris Plan Banks operating in 142 cities had $220 million in loans outstanding in 1931.[34]

A challenge familiar to a large portion of the American population today also confronted their counterparts a century ago. Between 1870 and 1920, immigration lifted the foreign-born population of the United States to 14 percent (a level not seen again until 2010). Nearly 30 million Europeans came to America during the so-called Age of Mass Migration. The number of newcomers was remarkable, considering the US population did not pass 100 million residents until the 1920 Census.

For many immigrants, running low on cash and looking for a job, the steamship agents who had handled their voyages became their first financial institutions. These agents opened what came to be known as immigrant banks. Generally unregulated (and therefore difficult to count precisely) the banks kept immigrants' modest savings, provided information in native languages, and offered other services for populations on the path to assimilation.[35] Among the services offered were personal bonds and remittances back to the old country. The latter became big business for the immigrant banks. Collectively, they handled an estimated 90 percent of money transfers from naturalized Americans to their families back home. The success of the steamship agents attracted other merchants who combined financial services with sales of consumer goods. At their peak, thousands of immigrant banks were providing financial services for otherwise unbanked Americans.

For smaller loans, consumers went where people in a bind had long gone – to merchants who sold on account; to small-dollar lenders, pawnshops, neighbors, and families. Like the general store on the frontier, the twentieth-century store was still an important source of credit. A popular article purportedly revealing "What Every Grocer Knows" reported in 1913 that "there weren't 15 percent of the people who paid cash and got cash discounts."[36] Most of the grocery shoppers who reportedly overextended themselves were women, who the author asserted had "no exact idea of money."

---

[34] David Mushinski, Ronnie Phillips, "The Role of Morris Plan Lending Institutions in Expanding Consumer Microcredit in the United States," in G. Yago et al. (eds) *Entrepreneurship in Emerging Domestic Markets (2008)*
[35] Influence of Immigrant Banks and Agencies in America, available at [HYPERLINK "https://www.gjenvick.com/Immigration/OtherIssuesAndProblems/1913-InfluenceOfImmigrantBanksAndAgenciesInAmerica.html"] (quoting, Report of the Commission on Immigration on the Problem of Immigration in Massachusetts, Boston: Wright & Potter Printing Company, State Printers, 1914. GGA Image ID # 149ea7a6d6).
[36] "What Every Grocer Knows: Fifteen Years' Observation of the American Housekeeper by a Grocery Clerk," *McClures* 41 (September 1913): 125-129 (cited in Caldor 216).

The shoppers to which the grocer referred were mainly women. Much of the criticism of consumer credit targeted women, who did most of the shopping in America. A best-selling novella in 2007, "Keeping Up with Lizzie," portrayed a woman whose borrowing brings herself, her family, and her community to the brink of ruin. The book inspired a 1921 movie of the same title and a comic strip, "Keeping Up with the Joneses" which delivered regular disdain of conspicuous consumption in the middle class.[37]

Shoppers who did not have the cash to put food on the table and could not find a merchant who sold on account had other alternatives, and they resorted to them often. The most popular option was to patronize one of the many small-dollar lending companies that were nearby in the neighborhoods. In urban areas of more than 30,000 residents, according to a study in 1911, one worker in five borrowed from a small-dollar lender.[38] A survey of New York City's municipal employees that same year found one in three had taken out small loans.[39] Among these lenders were companies that made "salary loans," the precursors of today's payday loans:

> One 1908 study concluded that there were at least thirty known salary lenders operating in New York City, and likely many others whose presence could not be ascertained because they did not advertise publicly….One transportation company employee in New York City estimated that at least 90 percent of his coworkers had taken out salary loans."[40]

Data on small-dollar lenders remain elusive because usury laws in many states prohibited the rates they charged, and the most aggressive lenders were likely the least conspicuous. Lenders that advertised and operated in prominent locations were easy prey for prosecutors, if any illegal lending was going on. New York brought hundreds of cases against small-dollar lenders (1,000 cases in just five months in 1913). Jail time for usury infractions was a risk that these lenders had to take into account.[41]

Behind the campaign against finance companies were reformers, like the Charity Organization Society and the Russell Sage Foundation. They monitored the finance companies, gave assistance to the prosecutors, counseled customers against excessive borrowing, and offered loans at legal rates through lending societies that opened offices in several large cities. Even with law enforcement on their side, and lower rates than private lenders, the societies struggled to attract customers and to cover the costs of

[37] Id.
[38] Caldor at 118.
[39] Id.
[40] Anne Fleming, "The Borrower's Tale: A History of Poor Debtors in Lochner Era New York City," *Law and History Review*, November 2012, Vol. 30, No. 4 at
[41] Federal Deposit Insurance Corporation (FDIC). 1997. *History of the Eighties: Lessons for the Future.* Vol. 1, *An Examination of the Banking Crises of the 1980s and Early 1990s*. Washington, DC: FDIC. Ch. 6

making small loans at legal rates. The authorities could not stop the influx of finance companies that opened to replace the shuttered offices of illegal lenders.

The lenders and charities finally reached a compromise and joined forces to collaborate on small-loan reforms, the primary result of which was the Uniform Small Loan Law. Its primary innovation was to raise the caps on interest rates. Versions of the law were ultimately adopted in half the states, and although the usury ceilings were not high enough to make the smallest loans profitable, the more permissive landscape allowed the established companies to retain a profitable business. At peace with their erstwhile competitors and critics, the finance companies acquired the more successful lending societies, and the sector grew to become a major source of consumer credit throughout the 20th century.[42]

For the borrower whose need was too small or prospects too dim for a finance company, credit had to come from somewhere else. A large population fit this description at the turn of the twentieth century:

> Poverty remained a fact of life for most working-class families and a condition of existence for many. The slightest disturbance in the balance between income and expenses, whether brought on by illness, unemployment, injury, or … a relative in need, sent families looking for money. In these situations, children could be put out to work, meals could be cut back, boarders could be taken in, and charity solicited, but sometimes borrowing money was the only way to pay the bills.[43]

Somewhere else for many borrowers was the same source that had served ancient civilizations – the pawnbroker. In twentieth-century America, pawnbrokers grew to an estimated 2,000 in 300 cities by 1911, and they became frequent creditors to consumers who had no attractive alternatives. Pawnbrokers were sometimes weekly financial bridges for homemakers whose bills came due before payday and seasonal support for mechanics who did not need tools when jobs were scarce. In the Bowery of New York, a reporter estimated that almost the entire population held at least one pawn ticket, and most had a dozen or more in the slow winter months.[44] Other studies offered a range of estimates, most with the caveat that many pawn customers would not admit to their use. Like the buyers on accounts at the stores, the most frequent patrons of pawnshops were women, who typically handled family budgets.

---

[42] See, e.g. Anne Fleming, "The Borrower's Tale: A History of Poor Debtors in Lochner Era New York City," *Law and History Review*, November 2012, Vol. 30, No. 4 at 1054 (citing Clarence W. Wassam, The Salary Loan Business in New York City: A Report Prepared Under the Direction of the Bureau of Social Research, New York School of Philanthropy (New York: Charities Publication Committee, 1908), 25–26.
[43] Caldor at 42, (citing Peter Shergold, *Working-Class Life: the American Standard in Comparative Perspective, 1899-1913,* (Pittsburgh: University of Pittsburgh Press, 1982) (internal citations and quotation marks removed)).
[44] Id. at 44 (citing Charles Barnard, "Pawnshops and Small Borrowers," *Chautaquan*, 19 (April 1894): 72).

Remedial loan organizations entered the pawn markets as well and brought their model of financial counseling combined with lending activities to pawn customers. The Provident Loan Society in New York, for example, attracted customers by offering lower interest rates and nicer surroundings than the typical private pawnshop. Along with these emoluments, however, came more complicated applications and more stringent qualifications for borrowers.[45] Many customers preferred the convenience of the private pawnbroker. Transactions were simpler. Neighborhood proprietors were familiar. Credit was easier. Charities could not make a dent in the pawnbrokers' trade, although a century later, they still try. Provident Loan Society operates five pawnshops in New York City in 2020, as well as an online store.[46] Yellowpages.com lists over 200 other pawnshops in the City.[47]

Despite its contribution to the rising standard of living in the early twentieth century, and notwithstanding the efforts to rehabilitate its reputation, consumer credit could not cast off its stigma as a symptom of society's moral decay. Too many consumers were borrowing too much, according to moral authorities and charitable organizations. The perceived risk worsened as standards of living rose at increasingly rapid rates and debt outstanding rose with them. Describing the attitude of the time and the crescendo it reached in the mid-twenties, the cultural history, "Financing the American Dream," summarized the moral attitudes and public angst:

> As debt levels rose, so did public anxiety over what was disparagingly termed "consumptive" credit. A loud chorus of critics alleged that the installment plan was a grave threat to public morals and a harbinger of economic catastrophe…As it was, many who bought goods on the installment plan felt embarrassed to admit it."[48]

Fear that consumers' profligacy portended catastrophe was unfounded. The resilience of consumer credit was demonstrated convincingly during the worst credit crisis in United States history. The crisis began with the Crash of 1929 and extended into the Great Depression. Dubious debt had put financial markets in precarious conditions. Global capital flows and a domestic recession precipitated massive loan defaults. A credit crunch imposed by the Federal Reserve exacerbated the crisis and turned it into the Great Depression. Ironically, however, the debts that dragged the economy down were not loans to consumers. The credit markets that failed were those in which banks, businesses, and investors were the primary participants.

The first shock to the economy, the Crash of 1929, was devastating to thousands of institutions and individuals, but it was not the cause of a decade of despair. By early

[45] Wendy Woloson, *In Hock: Pawning in America from Indepedence through the Great Depression*, University of Chicago Press, 174 (2012)
[46] [HYPERLINK "https://providentloan.com/en/"]
[47] [HYPERLINK "https://www.yellowpages.com/new-york-city-ny/pawn-shops?page=7"]. Accessed 11/13/20.
[48] Id. at 211.

1930, stocks had regained half the ground lost in the crash, and more importantly, credit markets were largely intact. As Bernanke found in his seminal study of the Depression, "except for a brief period of liquidation of speculation loans after the stock market crash, credit outstanding declined very little before October 1930—this despite a 25 percent fall in industrial production that had occurred by that time."[49] The ruined investors of 1929 were a minority of Americans.

It was not until the credit crisis spread through the banking system that the Great Depression took hold. Bank depositors – some out of work and needing cash, others anxious and hoarding for uncertain times – began to withdraw funds. In effect, customers were calling loans they had made to the banks. The demands came in as the banks' resources were dwindling due to tight monetary policies imposed by the Federal Reserve.[50] The weakest banks ran out of reserves first. When they closed without honoring their obligations, sensational headlines spread the news, and depositors elsewhere rushed to their banks, causing more to fail. The runs came in waves, and the waves crested in panics that overwhelmed thousands of banks in 1930, 1931 and 1932. By 1933, authorities in 37 states had partially or completely closed their banks. In March, just as President Roosevelt was taking office, the tide engulphed the lender of last resort, when the twelve Federal Reserve Banks closed their doors. In less than three years, a third of the nation's banks had failed, depositors had lost $1.3 billion, and credit had become unaffordable for many – if available at any price.[51]

In marked contrast to the dysfunction of the banking system was the performance of consumer credit markets. Consumer credit began the 1930s on a more prudential foundation than business borrowing, and competition enabled consumers to find refuge from the turbulence that devastated capital markets. Unlike investor debt, installment loans had not reached unsustainable levels in the twenties. In 1930, the average car loan had less than five months of payments remaining. Virtually all were paid off. Auto repossessions in the darkest years of the decade did not exceed 0.5 percent of autos

---

[49] Ben S. Bernanke. "Nonmonetary Effects of the Financial Crisis in Propagation of the Great Depression," American Economic Review, June 1983, v. 73, pp. 257-76.
[50] Their ultimate source of funds, the Fed, returned to restrictive monetary policies. It was following the prevailing monetary theory at the time, which prescribed contracting credit when the economy declined. The result was a shrinking of the reserves that banks needed to fulfill depositors' demands. A third of the money supply had disappeared by 1933. Gary Richardson, Alejandro Komai, Michael Gou, and Daniel Park, "Stock Market Crash of 1929, Federal Reserve History, available at [HYPERLINK "https://www.federalreservehistory.org/essays/stock_market_crash_of_1929"]
[51] See, e.g., Milton Friedman and Anna J. Schwartz. A Monetary History of the United States, 1867-1960, Princeton University Press, 1963; The panic did not subside until an emergency order, one of the first actions of the newly inaugurated President Roosevelt, temporarily closed all the nation's banks. They were allowed to reopen once the government relaxed the restrictions that had contributed to the scarcity credit. The order, on March 6, 1933 was ratified by the Emergency Banking Act, three days later. They reopened after the government eased reserve rules and allowed banks that survived to release more funds. In June, the Banking Act established the FDIC and the promise of insured bank accounts. Gradually, the financial sector regained the confidence of depositors.

financed. Delinquencies rose at general finance companies as well but remained below the rates on commercial loans. At the two largest finance companies, Household Finance Company charged off only 1.02 percent of its loans in 1930, and Beneficial Finance repossessed collateral on only 0.025 percent of its chattel mortgages that year.[52] One report could find only two failures of finance companies in 1930, in contrast to over 800 banks in just two months at yearend.[53]

The dynamics of competition in consumer finance can be seen in the sector's performance as the Depression dragged on. While banks were closing and commercial credit was shrinking, consumer lenders were expanding. In the year after the crash, Beneficial and Household opened 80 offices between them and increased loans by 12.8 and 18.8 percent, respectively, in 1930. One Household office made over 300,000 loans in a year. It also turned away 200,000 applicants, reflecting the poor prospects of many consumers as the Depression was spreading.[54] But consumers had other alternatives, and they turned to them as well.

Mutual savings banks were more resilient than commercial banks during the Depression. The FDIC history noted that "during the 1930s MSBs were far less prone to bank runs than either commercial banks or savings and loan associations. Indeed, nearly every year during the 1930s MSBs experienced a net savings inflow…. [E]xisting institutions continued to prosper during and long after the Depression."[55]

Merchants intensified their competitive efforts in the face of the downturn, in part by ramping up consumer lending. In July 1930, Montgomery Ward blanketed the country with advertisements announcing that all items in the catalog (except groceries) would be available on time payments. Sears responded with a rate reduction on its installment sales. Competitors followed suit, and the competition created new credit. Between 1932 and 1937 the four major mail-order retailers quadrupled sales on credit.[56] Other retailers – department stores, clothiers, furniture stores, and jewelers – likewise increased installment lending.

At the end of the decade, a Census Bureau retrospective on the worst of the Depression observed that "consumers did not repudiate debts en masse…."[57] One way they were able to avoid default was by borrowing to pay off previous loans. According to NBER, between 25 and 75 percent of personal-finance loans from 1934 to 1937 were made to refinance existing debts. Consumer borrowers fared better, and consumer lenders performed better, than their commercial counterparts did in the Depression.

---

[52] Calder at 270 (citing *Business Week*, 11 February 1931, at 14).
[53] Caldor 271.
[54] Caldor at 268.
[55]
[56] Caldor at 275 (citing Nugent, *Consumer Credit and Economic Stability at 110)*
[57]Id. (citing, U.S. Bureau of the Census, *Sixteenth Census: 1940 … Retail Trade: 1939, Part I* (GPO, 1941) at 40.)

Some commercial banks recognized the opportunities that consumer lending offered, and the more enterprising institutions entered the market as well. One of the First was National City Bank in New York, which opened a personal loan department in 1928.[58] Between 1929 and 1936 the number of commercial banks making consumer loans more than tripled, from 208 to 685.[59] Business lending continued to lag during the thirties, and a contraction in 1937 erased much of the recovery that had begun in 1933. By the end of the decade, bank balance sheets gave a disappointing reflection of the overall economy. Total bank lending had dropped by more than half, but most of the decline came from business credit. An encouraging exception was the proportion of loans that banks made to consumers, which doubled from 9 percent in 1929 to 20 percent ten years later. Consumer credit had helped stabilize a commercial sector that was struggling to regain momentum.

The entry of commercial banks into the competition for consumer loans gradually displaced another institution. With the federal interest caps on customer deposits (set at zero for demand deposits), commercial banks gained some of the advantages that Morris Plan Banks had used to enhance their returns. No longer unique, the Plans that had entered the market "when there were not adequate institutions to supply consumer credit [departed after] commercial banks had adopted their basic lending practices,"[60] began to exit. In the words of the Commission, "Morris Plan banks paved the way for commercial banks to enter instalment lending and became virtually indistinguishable from those banks whenever they were given the privilege of accepting demand deposits."[61] When they became indistinguishable from more efficient alternatives, Morris Plan Banks could not compete. It did not help competitors of commercial banks when regulators outlawed the payment of competitive interest rates on deposits in order to bolster the banks' profits and stability:

> [T]he potential profitability of established banks was improved by the prohibition of paying interest on demand deposits and the delegation of power to the Board of Governors to set maximum time deposit rates, a power which was exercised under Regulation Q. Not surprisingly economic studies of the industry found that substantial rents were earned by banks in the New Deal era. Ignoring the culpability of the Federal Reserve in failing to mitigate the shocks of the early 1930s and thereby driving many more banks to the wall, policy makers and

58 NCCR at 93.
59 Lendol Calder, *Financing the American Dream*, Princeton University Press (1999) Id. at 285 (citing Nugent, *Consumer Credit and Economic Stability* (1939), at 343; other statistics in paragraph from Caldor, Ch. 6).
60 David Mushinski, Ronnie Phillips, "The Role of Morris Plan Lending Institutions in Expanding Consumer Microcredit in the United States," in G. Yago et al. (eds) *Entrepreneurship in Emerging Domestic Markets (2008),* 121.
61 NCCR at 5.

> regulators took the system of unit banking as a given and saw the restriction of competition as a means to ensuring the solvency and profitability of banks.[62]

Much of the prosperity of the first half of the twentieth century in the United States, and the worst economic crisis, can be traced to developments in financial markets. When credit was abundant, economic activity advanced and standards of living rose. When credit was scarce, production declined and jobs disappeared. Unfortunately for the nation and its banks, a single source happened to be the lender of last resort. When that source presided over a contraction of credit, the economy suffered the consequences.

Fortunately for consumers, the other sources of credit were plentiful. Thousands of merchants, finance companies, credit unions, and other financial institutions gave consumers the wherewithal to share the wealth of a growing economy. These sources also offered consumers some insulation from tumultuous capital markets that buffeted heavy industries and commercial banks. Financial innovators developed new methods to attract funds and new ways to supply credit to consumers. Financial entrepreneurs entered markets and expanded as demand for credit grew. Competition for the consumer was keen. In good times and bad, for wealthy and poor, competition gave consumers access to credit.

During World War II, the factories that consumer credit had underwritten a generation earlier were recommissioned to turn out tanks, planes, and other war materiel. Industrial production finally recovered, and consumers played an important role in the recovery, this time as creditors. Although borrowing for consumer goods declined, consumers' savings became a significant source of the debt that financed the war. Eighty million people (in a population that numbered 132 million in the 1940 Census) bought $180 billion in War Bonds.[63]

Credit and Competition in the Post World War II Economy

The end of the war and the revival of the consumer economy marked the period that occupies most of Commission's analysis of credit and competition. Defining the terms of that analysis, the Commission resorted to a familiar definition: "when the number of sellers is so large and entry is so easy that no seller has power over price," competition could be expected to make credit affordable and available.[64] A competitive market could be expected to "lower prices to the lowest level consistent with covering production costs

[62] Eugene White, "Lessons From The History Of Bank Examination And Supervision In The United States, 1863-2008, in Alfredo Gigliobianco and Gianni Toniolo, eds., *Financial Market Regulation in the Wake of Financial Crises: The Historical Experience* (November 2009) available at [HYPERLINK "https://www.bancaditalia.it/pubblicazioni/collana-seminari-convegni/2009-0001/1_volume_regolazione.pdf"].
[63] Corporate Finance Institute, War Bond History, available at [HYPERLINK "https://corporatefinanceinstitute.com/resources/knowledge/other/war-bonds/"]
[64] Id. at 109.

and profitability just sufficient to bring capital into the industry."[65] Credit availability was measured by "the degree to which creditors are willing to provide credit at the free market rate in a world without imperfections." In other words, the Commission viewed competition to have the most potential to offer the lowest rates for consumers and achieve the greatest access to credit. The Report then assessed the state of that competition and whether it was delivering the expected results.

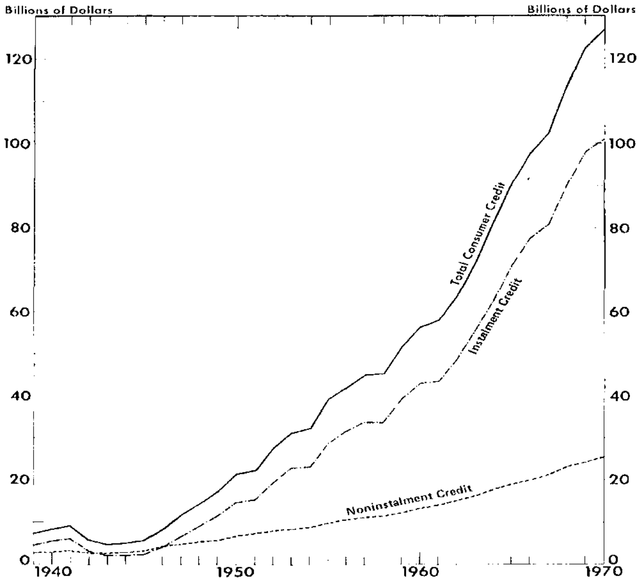
In most respects, the Commission found competition in consumer finance to be working well in 1970. Interest rates appeared to respond to supply and demand, and consumers seeking credit generally could obtain it at market rates. But the Commission also found differences in access and variations in rates across states and sectors. Depending on where consumers lived or borrowed, some paid higher rates and borrowed less, while others enjoyed lower rates and borrowed more. The disparities could not be attributed to capital costs other fundamentals. However, when credit was expensive and rare, it often coincided with indications of competitive shortcomings. The Commission described what it perceived as the more significant successes and shortcomings.

National Trends

In a national overview of consumer credit, the Commission focused on different sectors of financial service providers. Some sectors had consolidated, some had disaggregated, and others had seen cycles of both. Overshadowing all the sectoral analysis was the dramatic growth in sources of consumer finance. A chart in the Report displayed the trends in consumer credit broken down by repayment methods, either "instalment" or "noninstalment," the latter including single payment loans, nonrevolving credit, money owed to service providers, and similar debts, and the growth took a dramatic upward turn in 1945, as did the US economy that grew at its fastest sustained pace in a century between 1950 and 1973:[66]

[65] Cite
[66] Report, Exhibit 2 -1, at 9; C.I. Jones Stanford GSB, "The Facts of Economic Growth," in *Handbook of Macroeconomics*, Volume 2A © 2016 Elsevier B.V. ISSN 1574-0048, [HYPERLINK "http://dx.doi.org/10.1016/bs.hesmac.2016.03.002"], NBER, available at [HYPERLINK "http://web.stanford.edu/~chadj/facts.pdf"].

CONSUMER INSTALMENT AND NONINSTALMENT CREDIT OUTSTANDING, 1939-1970



Fueling this growth were tens of thousands of potential competitors in the business of making loans to consumers. Some 13,600 commercial banks held over $50 billion in consumer credit in 1970, more than any other segment and about 40 percent of the total outstanding in the United States.[67] Finance companies – about 3,700 in 1965, operating out of an estimated 13,000 to 14,000 offices – accounted for the second largest portion, with 30 percent of the consumer credit outstanding. Outnumbering both banks and finance companies were 23,650 credit unions, although their share of credit outstanding came in lower, at 12 percent in 1970. Probably more numerous than any other sources were retailers, who held about 14 percent of consumer credit outstanding as the 1960s ended, but a precise tally of their number was not available.[68] Outside these main categories, other lenders (such as savings and loan associations and mutual savings banks) amounted to about 1.5 percent of the credit outstanding.[69]

Dollar volumes of the holdings of these sectors reflected the dramatic growth of installment credit outstanding – from under $15 billion to over $100 billion – over the

[67] Report at 8.
[68] Report at 11
[69] Id.

two decades ending in 1970.[70] Banks and finance companies each held more than twice as much as all the institutions combined just twenty years earlier. Credit unions and retailers each held almost as much as the entire amount outstanding in 1950.

Exhibit 2-4 of the Commission's Report showed the volumes and shares of installment debt[71] by institutional sectors in 1950 and 1970.

Amounts outstanding
(Dollar amounts in millions)

	December, 1950		December, 1970	
	Amount	*Percent*	*Amount*	*Percent*
Commercial banks	$5,798	39.4	$41,895	41.4
Finance companies	5,315	36.1	31,123	30.8
Credit unions	590	4.0	12,500	12.4
Miscellaneous[a]	102	0.7	1,546	1.5
Retail outlets	2,898	19.7	14,097	13.9
Totals	$14,703	100.0	$101,161	100.0

[a]Miscellaneous lenders include savings and loan associations and mutual savings banks.
Details may not add to totals because of rounding.

Source: Board of Governors of the Federal Reserve System.

Aggregate growth would bode well for competition, as it is easier for new companies to enter and small rivals to thrive in a market that is expanding. Customers in a market for the first time – like the early automobile buyers choosing between Ford and GM – are less likely to have developed loyalty to an established firm. And entry itself can accelerate the expansion of a market, as new companies and smaller rivals hustle to establish themselves and grow their businesses.

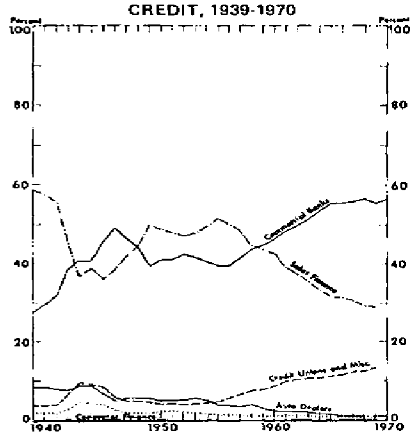
One indicator of competition is the volatility of shares of the sellers in a market, as credit unions, finance companies, commercial banks, and Morris Plan Banks had demonstrated before the War. Changing shares can reflect rivalry among firms already within a market, entry of new firms into the market, and innovation that disrupts historic patterns. When established firms charge more than necessary to cover the costs of providing the goods and services they sell, the resulting profits invite entry by others. Inferior quality, untapped innovation, and poor service are other signals that alert existing and potential competitors to the prospect of extraordinary rewards for anyone who can improve upon the status quo. New entrants and opportunistic rivals empower consumers to discipline companies who do not perform. Such discipline can manifest itself in the movement of consumers from one seller to another, in the movement of companies to into and out of a

[70] See Table 2-1 in CICO Chapter for a longer series.
[71] These figures do not include "noninstalment" debt.

market, and in the revitalization of underperforming incumbents. In markets where consumers can shift their allegiance, market power is unlikely to persist for long, if it arises at all.

The Commission tracked shares of the institutional sectors that held consumer credit in the decades ending in 1970. At first glance, shares appeared relatively stable. Banks, with 31 percent in of installment credit 1970, had added two percentage points to their 1950 share of 29 percent. Finance companies and retailers lost about five and six points from their 1950 shares of 36 percent and 20 percent, respectively, while credit unions added eight points, impressive growth on a percentage basis, given the 4 percent that the sector held at the beginning of the period. Still, credit unions remained in fourth place among the four main categories of consumer lenders on a national basis.

HOLDERS OF AUTOMOBILE INSTALMENT CREDIT, 1939-1970

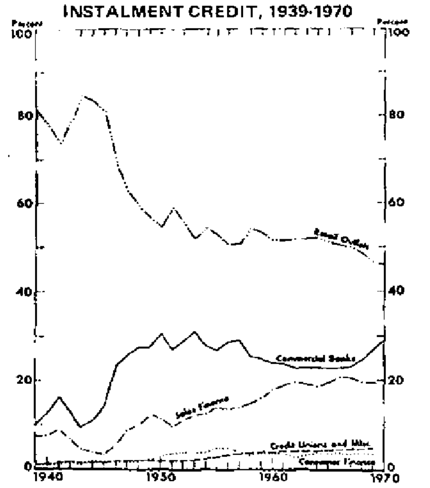


The picture changes dramatically when these sectors are examined more closely. In loans for automobiles, home appliances, and home improvement – rapidly growing industries in the post-war economy – institutions gained and lost shares to an extent that belied the seeming stability of their positions at the beginning and end of the period. For example, sales finance companies (many affiliated with automobile industry) dominated lending for vehicles in 1940, with almost 60 percent of the credit outstanding, twice the share of commercial banks.[72] The lead did not last long. In just a few years, banks bypassed finance companies and were making about half the overall lending for autos in the late forties. Finance companies recovered just as quickly, overtaking banks and maintaining the lead source of auto loans for most of the fifties. But as the sixties loomed, banks once again had resumed their growth, finishing the decade with almost twice the share of their chief rivals. By 1970, in a much larger market, banks held almost 60 percent of the auto installment credit, twice as much as the finance companies. It was also in the late fifties and sixties that credit unions grew steadily. Over 30% of their loans in 1971, amounting to more than $3 billion, financed auto purchases.[73] Meanwhile, the small share attributable to auto dealers nearly disappeared.

[72] Exhibit 2-5 of the Commission's report illustrated these shifts.
[73] NCCF at

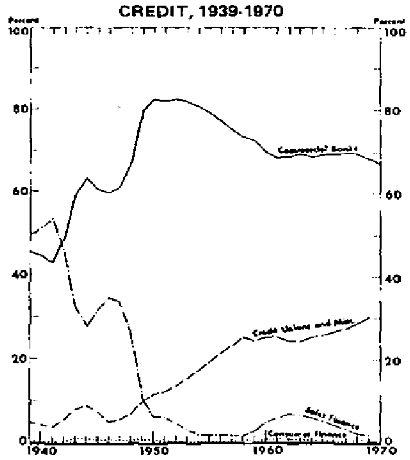
In the market where consumers sought to finance expensive purchases of appliances, furniture and other items at retail stores, the retailers themselves began the period with a seemingly commanding lead over the other sources of credit, only to take a precipitous fall. In the early forties, retailers held more than 80 percent of installment credit in this category. By 1970, their share had dropped below 50 percent. Commercial banks and sales finance companies more than doubled their shares over the same period, reaching about 25 percent and 20 percent, respectively.[74]

HOLDERS OF OTHER CONSUMER GOODS INSTALMENT CREDIT, 1939-1970



SOURCE: National Commission on Consumer Finance based on FRB d

HOLDERS OF REPAIR AND MODERNIZATION CREDIT, 1939-1970



In one category of credit the segment leader virtually disappeared. Sales finance companies held half the outstanding credit for modernization and repair in the early 1940s. Banks were a close second, with credit unions far behind. By 1970, sales finance companies' share was approaching zero. Banks and credit unions each had added 25 points to their 1940 shares and finished the period with almost all the loans for these home improvement projects. Credit unions grew six-fold, from about five percent to 30 percent.[75]

With different types of institutions vying for the same types of loans, and sectors taking substantial shares from other sectors, competition was obviously crossing

[74] Id.
[75] Id.

institutional lines. Inside the sectors, the forces the firms faced were likely more turbulent still. New entrants would have posed constant threats to established institutions. According to NCUA, federal credit unions numbered nearly 6,000 in 1952.[76] The Commission tallied over 23,000 (likely state and federal) in 1972. Between 1950 and 1970, banks added roughly 20,000 branches. Bank credit cards were growing even more rapidly in 1970. At the end of 1967, 390 banks reported some $800 million in credit-card debt outstanding. Three years later over 1,200 banks, still a minority, reported $3.8 billion. Consumers were flocking to new products, new companies, and new offices. Incumbents could not afford to be complacent if they wanted to keep account holders from taking their business elsewhere.

Given the rapid expansion of credit over this period, shrinking shares still may have signified growth, albeit slower growth, but some sectors declined absolutely despite the expansion. Consumers, in numbers large enough to double or decimate sectors in the course of a decade or two, were rewarding companies that offered attractive terms and penalizing those who compared poorly. Later, this chapter describes how the ongoing rivalry among existing lenders and the entry of new sources of consumer credit continued to produce dramatic changes in the nature and structure of the sector since the Commission's report.

Differences Among Institutions and States

If national numerosity alone determined competition, then the thousands of credit sources and their churning market shares might indicate that the balance of power in these markets favored consumers, not lenders. But national trends do not reflect the conditions an individual borrower might face. The markets for most consumer financial services were local or regional in the decades the Commission studied. Retailers offering attractive charge accounts in Pittsburg or banks with low interest rates in Philadelphia were unlikely to help consumers in Chicago.[77] By the same token, consumers shopping for cars anywhere would have found credit cards and home improvement loans to be poor substitutes for auto loans. To be sure, a customer might have been able buy an appliance or roof repair on credit in order to set aside cash for a car, but such substitution is less convenient than choosing among competing auto lenders. For reasons such as these, nationwide tallies of financial providers, aggregate shares of debt outstanding, and may not reveal the vigor of competition or the alternatives available when customers are looking for credit.

[76] See, [HYPERLINK "https://www.ncua.gov/about-ncua/historical-timeline"]. Those entrants either brought new customers to consumer finance or took business from other credit unions or financial institutions. Most likely the newcomers did both.

[77] Even commercial customers tended to bank locally, as the Supreme Court observed in an antitrust case that had found New York to be in a different banking market from Philadelphia in 1963. United States v. Philadelphia Nat'l Bank, 374 U.S. 321 (1963)

The Commission, recognizing that the relevant competition occurred in geographic markets smaller than the entire United States and in product markets narrower than all consumer credit, focused on differences among cities and states, and within sectors, in its analysis of concentration and performance. Geography was typically broken down by states. Lines of business were defined by categories of credit – including automobile loans, retail installment credit, and installment credit for other consumer goods (or OCG) – and comparisons of access and rates in different states. For each category, the Commission assessed quantitative and qualitative evidence bearing on competition. The quantitative factors included structural characteristics – primarily the numerosity and concentration of lenders. Among the qualitative factors were conditions allowing or impeding entry into credit markets, caps on interest rates, and business practices that could restrict competition. These circumstances were checked for potential effects on rates of interest and availability of loans.

Automobiles – The Commission's cross-sectional analysis of lending in different states found both evidence of competition and indications of market power. In automobile loans, for example, "quantities of credit extended vary inversely with market power" (measured by market concentration of banks).[78] Also evident was a predictable corollary of lower quantities: where quantities fell, rates rose. The analysis revealed significant correlations between bank concentration and interest rates that car buyers paid across a broad spectrum of states. A comparison of states at the high and low ends of the spectrum exposed the potential costs of the disparities. Consumers who lived in states with more concentrated banks paid an average premium of about 70 basis points, and they paid this premium whether they borrowed from banks or borrowed from dealers who then sold the loans to the banks.[79]

The difference in interest rates coincided with larger differences in the behavior of borrowers. A significant segment of consumers paid another premium when they took out auto loans in concentrated states, because when banks made fewer loans, dealers filled the gap. In less concentrated states, banks were the leading source of loans, by a wide margin. Direct bank loans accounted for 42 percent of financed sales, almost doubling the 24 percent of the sales financed by dealers (who then sold the loans to banks or finance companies). Where banks were more concentrated, the shares reversed; sales financed by dealers (and indirectly financed by banks) outnumbered sales directly financed by the banks themselves. Dealers extended 37 percent of bank-financed loans, while banks handled 23 percent directly. In other words, dealers' share of bank-backed financing grew by half, while direct bank lending dropped by almost the same proportion, in concentrated states. For consumers, the shift to dealer financing may have had a greater

[78] Report at 112 (In addition, in "all but a few states, rate ceilings are inconsequential as a determinant of the market rate.")
[79] Report at 122.

impact than the rise of bank rates in concentrated states, since dealers charged APRs about two points above banks' direct rates across all states.

The practical significance to consumers of 70 basis points or 2.7 percentage points can be illustrated by considering the effects of those premiums on total payments for a typical 1970 auto loan in today's dollars. An increase of 70 basis points – the direct-loan premium that Commission attributed to market power – would cost the consumer an extra $200 over three years in 2020 dollars for the median loan.[80] An additional 2.7 percentage points – the difference between rates paid by direct borrowers in competitive states and indirect borrowers in concentrated states – would generate extra interest payments of $900 in inflation-adjusted dollars over the life of a three year loan.[81]

It is conceivable, of course, that the consumers who borrowed from dealers would not have qualified for average bank rates, and that some consumers probably preferred to pay for the convenience of borrowing at the dealer. But such explanations do not explain such wide disparities in bank shares and dealer shares of credit extended across states. There is no reason to expect borrowers seeking more convenience or presenting greater risk would cluster in the states where fewer banks charged higher rates.

The Commission cautioned that other factors may have confounded the results.[82] For example, some of the low-concentration states had lower statutory rate ceilings, high-concentration states often allowed branch banking, and higher costs may have explained some of the interest-rate variations. Thus, even though the reported correlations between concentration of banks and the borrowing patterns were statistically significant, the Commission noted that concentration "does not inevitably result in anticompetitive behavior, nor does branch banking inevitably result in high concentration."[83]

Second, the concentration levels the Commission observed were relatively low, even in the states that fell into the highly concentrated category. In those states, the four largest banks on average accounted for 64 percent of the money lent to finance automobile purchases. Thus, more than a third of the loans were made by at least three other banks, and likely more.[84] Intuition suggests that seven or more competitors would be enough to

[80] The premium calculation assumes a loan of $3,000 in 1970 amortized over three years. Adjusted for inflation, $3,000 in 1970 is $20,000 in 2020. The median auto loan in 1971 was $3048, with a maturity of 34.5 months [NCCFR at 15; CPI Inflation Calculator, [HYPERLINK "https://www.in2013dollars.com/us/inflation/1970?amount=3000"].]
[81] The calculation assumes a $3,000 loan amortized over three years in 1970.
[82] Report at 122-23.
[83] Id. at 123. (Developments described later in this chapter reveal that the Commission's concern about branch banking was misplaced.)
[84] For the remainder to be accounted by three banks, each would have had a 12 percent share. If they were not equal in size, and it is rare to find such parity, then the number of additional competitors had to be greater than three.

engage in effective competition. It would be difficult to find academic support and antitrust enforcement to the contrary in the last 50 years.[85]

Third, as the Commission observed, concentration alone does not confer market power, if smaller competitors and new entrants can take business away from established companies that charge monopoly prices. High prices are signals to current and future rivals that extraordinary profits are available in a market. Dominant firms need rivals constrained and entry impeded if they are to succeed in reaping the rewards of market power. In some cases, they enjoyed those conditions, and still do. These are addressed after a review of the other forms of credit in the Commission's report.

Qualified conclusions about the correlations between concentration and competition were warranted. First, as the Commission noted, correlation does not indicate causation. Second, statistical significance does not equate to explanatory power. And third, the quality of the data was questionable. Important measures that were not included could have confound the results, and aggregate data that was used could be a poor proxy for conditions in local market. A study published in 1975 tested the structure-performance hypothesis with more refined data, and it stressed the importance of qualifying the conclusions. Focusing on local markets for installment loans, Beigley and McCall found statistically significant relationships between market power and various measures of concentration, but that the relationships were not "of a magnitude to be of great operational significance in determining a bank's market power."[86]

Financing Retail Goods – For category of other consumer goods (those mostly bought at retailers), the effect of rate restrictions made credit markets difficult for the Commission to assess. Interest rates varied little from state to state for revolving credit. Rates hovered around 18 percent, not necessarily because of competitive conditions, but due to common usury limits. The rate caps made it difficult to disentangle the effects of competition from the effects of rate ceilings. Where rate ceilings were high or nonexistent, competition kept rates below the ceilings.[87] Competition took other forms in retail credit. Where rate ceilings were relatively low, however, the Commission detected excess demand for

---

[85] The antitrust cases from the 1960s that prevented mergers in industries with numerous competitors were criticized at the time and are no longer followed today. See, e.g. Thomas Kauper, The "Warren Court" and the Antitrust Laws: Of Economics, Populism, and Cynicism, Michigan Law Review, Vol. 67, No. 2 (Dec., 1968), pp. 325-342; Orley Ashenfelter, Daniel Hosken and Matthew Weinberg, Did Robert Bork Understate the Competitive Impact of Mergers? Evidence from Consummated Mergers, The Journal of Law & Economics, Vol. 57, No. S3, The Contributions of Robert Bork to Antitrust Economics (August 2014), pp. S67-S100.
[86] Beighley and McCall (1975). Market Power and Structure and Commercial Bank Installment Lending. Journal of Money, Credit, and Banking.
(Market power was measured by the Lerner price-marginal cost index, and concentration was measured by inequalities among individual bank market shares, market shares of the leading bank groups, and numbers of commercial banks.)
[87] The Commission looked for large variations in price or supply, which could indicate varying levels of competition, but did not find them in states with high ceilings.

credit; consumers were unable to obtain loans at rates they would have been willing to pay.

Convenience was an important factor for consumers when financing retail purchases. Credit granted at the point of purchase was more attractive than the option of going elsewhere for the funds to buy an expensive appliance or piece of furniture, and consumers took advantage of the opportunity. Banks and credit unions combined for less than 10 percent of such purchases.[88] Location was an obvious advantage for retailers, who did not face as much competition from other sources as, for example, auto dealers did.

Higher concentration among retailers was associated with fewer goods financed at stores, but retailer concentration varied relatively little from state to state – significantly less than in the banking sector. In the more concentrated category were states where four stores averaged two thirds of sales, meaning more than two (likely many more, since they were smaller) made up the remainder. In less concentrated states, the top four retailers still exceeded half of all sales. Markets with competitors numbering six, seven, and more are generally regarded as unlikely to suffer from market power. Indeed, the Commission recognized that the retail sector was highly competitive, given that it was a business easy to enter and exit, with a history that frequently displayed both.[89]

How much consumers actually paid for retail credit was difficult to measure, because interest rates were not the only means by which retailers could recover their costs. If a store could not raise the rate on charge accounts because of an interest cap, it could raise the prices of the goods financed. The Report cited research showing that appliance prices in a market with low rate caps were about 5 percent higher than in nearby markets with high or no caps.[90] For customers, increased cash prices indicated that everyone might have been paying interest, whether they purchased with credit or cash. Consumers who paid in cash may have subsidized those who paid with credit.[91] The Commission worried that such a subsidy would have amounted to a regressive transfer from poorer to wealthier consumers, since cash buyers would include those who could not qualify for charge accounts.[92]

Finance Companies and other sources – Finance companies confronted a wide variety of competitive conditions from state to state, and consumers' fortunes in the sector reflected those variations. Loans were more readily available from finance companies

---

[88] Report at 126.
[89] Report at 106.
[90] Report at 106.
[91] Id. at 107.
[92] Id. ([T]he burden of subsidy falls primarily on cash buyers, some of whom may have been unable to obtain credit. Thus state laws that put the price of credit below competitive rates are forcing both the wealthy and the less affluent, who do not use or cannot obtain credit, to subsidize the use of credit by others.")

where economies were stronger, concentration was lower, and the companies enjoyed lower labor costs. As in retail revolving credit, competition kept rates below the legal caps in many markets, and credit was widely available in them. But again, the effects of competition on interest rates themselves were difficult to assess because usury limits in some markets often controlled rates that lenders could charge, and the volume of credit demanded at those rates exceeded the volume available. Perhaps for that reason, the correlations between concentration levels and rates were weak, and again the Commission noted that confounding factors may have explained the associations.

Market restrictions across sectors – Across all the sectors, the most serious disparities in consumers' access to affordable credit were associated with restrictions that directly impaired competition. Where the Commission found concentration, it often found barriers to entry and restrictions on credit practices. Restrictive Convenience and Advantage (C&A) licensing, for example, was associated with reduced availability of loans and increased concentration of finance companies.[93] They were 50 percent more concentrated where entry was impeded, so the entry barriers could explain the observed correlations between concentration and consequences. Concentration may have been a consequence, rather than a cause, of restrictions on competition, just as high interest rates and reduced availability of credit appeared to have been. As the Commission characterized the record:

> There is ample evidence indicating that competition is impaired in a number of states by a variety of conditions affecting all of the major types of consumer credit. A common structural condition of these markets is that they tend to be highly concentrated and difficult for newcomers to enter because of relatively slow growth in demand for credit, or legal restrictions on entry, or some other impediment or combination thereof. By comparison many other state markets appear to be fairly competitive, a judgment which is indicated not only by the existence of contrasting structural conditions but also by related measures of better performance.[94]

Consumers suffered costly consequences in states that protected financial institutions from competition. Different ceilings for different lenders created market segments that allowed a few firms to dominate without fear of encroachment from other segments. For example, Commercial banks in New York were confined to a maximum rate of 11.6 percent, which prevented their entry into "the $500-loan market served by consumer finance companies at 24.8 percent." The Commission noted that borrowers "would have been significantly better off if banks had always been able to charge the same rates permitted licensed lenders." How significant is apparent from a conversion of the amounts into current dollars. Inflation since 1970 has turned the purchasing power of

[93] Report at 130-31.
[94] Report at 136

$500 into $3,400 today.[95] Expressed in 2020 dollars, the difference in interest rates (24.8 instead of 11.6) could have cost borrowers as much as an extra $260 in interest payments on a one-year loan.[96] The disparity would have been greater for loans of longer maturities and for borrowers who would have qualified for lower rates at the banks. It would have been less for borrowers who got better deals at finance companies and those who would not have qualified for the better bank rates.

Banks, for their part, enjoyed protection from finance companies. For example, reported the Commission, "licensed lenders in New York may lend no more than $1,400 to any one borrower, whereas banks may make consumer loans as high as $5,000." Banks could make loans between those amounts without worrying about competition from finance companies. The segmentation created by these restrictions that separated classes of credit grantors, the Commission said, was "blatantly anticompetitive."[97]

The consumers who bore the most serious harm may not have been those who paid the higher rates. At least they got loans. Where rate caps were low and entry restrictions high, lenders rationed loans and turned away applicants. By the Commission's measure, in states with both types of restrictions, people took out fewer loans and smaller loans – about two-thirds as much overall – while rejection rates were almost half again as high as those in states with easier entry.[98] Applicants had little more than a fifty-fifty chance to get a loan in states that regulated rates and entry. The odds were two-to-one in consumers' favor in less restrictive states. Where entry was restricted but rate ceilings were relaxed, rejection rates for credit applicants still rose and the average size and number of loans still lagged, but not by as much. Adverse consequences of entry barriers thus occurred in states regardless of rate ceilings; only the extent of the damage differed.[99]

Regulations limiting entry and access were not, however, the only source of competitive impairment in the credit sector, the Commission believed. It was concerned with private threats to competition as well. Accordingly, the Report called for vigorous antitrust enforcement against restraints of trade, and it identified practices that should be investigated:

---

95 Inflation conversion from Saving.org, available at [HYPERLINK "https://www.saving.org/inflation/"].
96 At 24.8 percent, interest payments would have added up to $475 instead of $215 for the lower rate. A precise comparison would take into account the added expenses of administering smaller loans and poorer credit records of finance-company customers, but it is difficult to dismiss the conclusion that they paid a great deal for the restrictions placed on banks. Interest calculations from Saving.org, at [HYPERLINK "https://www.saving.org/calculators/loan-calculator"].
97 Report at 94.
98 Report at 131.
99 Report at 132.

> Although almost obvious, the Commission recommends that antitrust policy, both Federal and state, be alert to restrictive arrangements in the credit industry. Any hint of agreement among lenders as to rates, discounts, territorial allocations, and the like must be vigorously pursued and eliminated.[100]

The most enduring restrictions are those that businesses can persuade government authorities to adopt. Except in rare instances, government barriers to competition are often beyond the reach of the antitrust laws. Advocacy for competition and consumers remains the only tool left to the enforcers.[101]

Restricted competition was beneficial for the financial institutions, because it allowed "domination by relatively few firms" of affected markets.[102] Typical byproducts of market power are stability and profitability of the insulated incumbents, and those benefits appeal to financial authorities as well. The Commission criticized regulators for their "excessive concern…for the protection of the profitability of existing bank institutions" and disagreed that the restraints served the "needs and convenience" of the public."[103] The Commission could have framed its conclusion more directly in terms of effects on consumers. When regulators allow the welfare of the banks to outweigh the interests of consumers, those who are supposed to benefit from oversight instead pay its costs.[104] For consumers who could get credit despite unfavorable conditions, the costs were higher rates and smaller loans. For consumers who could not, the costs came in the form of doing without the goods or services that credit would have made available or doing business with illegal lenders. It was well known that in the decades the Commission studied that "consumer lending was a standard business activity of criminal organizations operating in many major metropolitan areas across the United States."[105] Restricting legitimate competition sometimes simply sends it to the underworld, where consumer protection depends on the rules and remedies of the juice loans and enforcers.

Numerous findings from the Commission's assessment of competition bear on the potential for discriminatory practices by lenders. Already noted was the analysis of access in the Report, which found that restrictions on competition frequently reduced the availability of credit, leading to rationing that presumably excluded borrowers of lesser

---

[100] Report at 138
[101] The Federal Trade Commission has long advocated against such regulations. (See OECD paper on competition advocacy). Adam Smith made similar observations two centuries earlier. He warned that sellers could be expected to advocate regulations that protected their businesses, and that trade associations were more likely than consumers to organize effective lobbies, and he urged authorities to resist merchants' arguments for protection. **CITE and check for earlier mention.**
[102] Id.
[103] Report at 137.
[104] Id.
[105] Durkin, et.al., at Kindle 362

means and lower credit scores. In the data, the Commission looked specifically for indications of gender discrimination and found widespread evidence of it.[106] The Commission also examined the data for signs of racial discrimination but was unable to find sufficient evidence to draw conclusions.[107] Elsewhere this report (see Chapter __) considers more recent information on discrimination. Later this chapter considers competition and access in modern credit markets.

These findings led the Commission to favor increased competition "as the best means to assure that most consumers pay a fair price for their credit services." To improve competition the Commission proposed a menu of policy changes that would expand consumers' choices and advocated regulations that could improve the wisdom of those choices.[108] To implement its recommendations, the Commission recommended that legislators, regulators, and enforcers strive to design and implement a sound competition policy for consumer credit. The goals of that policy should be these:

- Promoting and maintaining competition among numerous sources of credit. Competition is the key ingredient "of a finance industry capable of providing an adequate supply of credit at reasonable rates"
- Assuring "access *by all* to these alternate sources"
- Preventing "excesses which the "system" may invoke against the borrower."[109]

Among all the available means to improve competition, the Commission concluded that enhancing the ability of potential competitors to enter credit markets would be the most effective policy. In his communication to the President and Congress, the Commission Chairman explained:

> As to our conclusion that free and fair competition is the ultimate and most effective protector of consumers, we have recommended the elimination of restrictive barriers to entry in consumer credit markets by permitting all creditors open access to all areas of consumer credit. We have urged the entry of savings and loan associations and mutual savings banks into the consumer credit market. We have recommended prohibitions on acquisitions that would eliminate potential competition or that would substantially increase concentration in state or local credit markets. We have also urged that rate ceilings which constrain the

[106] Report at 160 (For a review of the role women played a prominent role in consumer credit markets from medieval times to the nineteenth century, see the Appendix.)
[107] Report at
[108] Report at 214, See, e.g Ch. 10. The requirements of the Truth in Lending Act and specific protections for vulnerable consumers –
[109] Report at 2 (emphasis in original).

development of workably competitive markets be reviewed by those states seeking to increase credit availability at reasonable rates.[110]

Thus, the critical prescription for competition in the postwar period was to preserve the competitive dynamic that had characterized credit markets in the first half of the twentieth century. Markets that were open to entry and free of constraints that prevented companies from challenging one another were the most likely to remain competitive and protect consumers.

Competition in Credit, 1970 - 2020

The Commission devoted a chapter of its report to predictions the future of consumer credit. Not surprisingly, many of those predictions failed to capture the nature and size of the markets in which credit is exchanged today. For example, the Commission anticipated, "With a slowdown in the rate of increase in consumer credit and with fewer additions to the types of goods and services financed, credit grantors in the future are relatively more likely to rely on price competition than on nonprice competition."[111]

Fortunately for consumers, the future exceeded expectations. The Commission did not predict the rise of automatic teller machines (although the first one had made its appearance in 1969),[112] let alone banking by smart phones, a phenomenon barely a decade old. For virtually every consumer in 1970, obtaining cash meant going to the bank. Obtaining a loan meant visiting a lender. Searching on the internet was unheard of. The Commission saw the growing use of bank-issued credit cards and the value they would deliver to an increasingly mobile population. It did not predict the extent of their growth, or the effect they would have on the banking sector's share of consumer credit.

The figures in Table 2-1 and 2-2 of Chapter 2 reveal that consumer credit outstanding has increased *thirty-fold* since the Commission's Report.[113] Most of that growth has come from financial services and technologies that were nonexistent or insignificant in 1970. And a good portion of that growth reflects more consumers participating, both absolutely and proportionately, in legal credit markets today than in 1972.

[110] Report at iii.
[111] Report at 203
[112] History.com, This day in history, [HYPERLINK "https://www.history.com/this-day-in-history/first-atm-opens-for-business" \l ":~:text=On%20September%202%2C%201969%2C%20America's,to%20conduct%20basic%20financial%20transactions."]
[113] To be precise, the Commission predicted that the *rate* of the growth of credit would decline after 1970, and that turned out to be correct. The amount of credit outstanding was so small in 1940 that the $100 billion increase through 1970 represented a slightly higher annual rate than the $4 trillion increase since 1970.

The structure of the consumer finance sector appears to have changed significantly in the fifty years since the Commission's report. At first glance, the traditional sources of credit show consolidation:

- The number of FDIC Insured banks dropped from more than 13,000 to less than 5,000 in 2018.[114]
- Federally Insured Credit Unions numbered about 5,200 in the final quarter of 2019[115] The Commission had tallied over 23,000 in 1972.
- Finance companies, which the Commission estimated at 3,700, now number ____.[116]

Dollar volumes and shares of consumer credit from Table 2-1 allow for comparisons of the major sectors around the time of the Commission's Report to those today. The following table highlights the institutional types then and now:

Consumer Credit by Type of Holder

	Billions	Percent	Billions	Percent	Excluding Government
Year	1975	1975	2019	2019	2019
Depository Institutions	$116	56.0%	$1,771	42.3%	61.7%
Finance companies	$33	15.9%	$537	12.8%	18.7%
Credit unions	$26	12.6%	$482	11.5%	16.8%
Nonfinancial business	$33	15.9%	$40	1.0%	1.4%
Pools of securitized assets		0.5%	$14	0.3%	0.5%
Federal government		0.0%	$1,319	31.5%	------
Nonprofit and ed. inst.		0.0%	$28	0.7%	1%
	$207	100%	$4,191	100%	100%

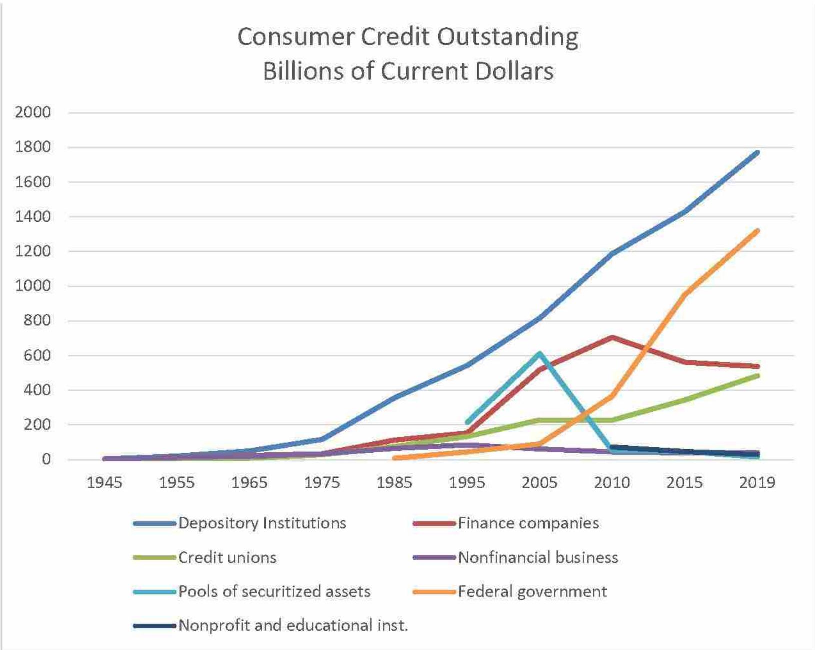
114 FDIC, BankFind Suite: Find Annual Historical Bank Data, available at [HYPERLINK "https://banks.data.fdic.gov/explore/historical?displayFields=STNAME%2CTOTAL%2CBRANCHES%2CNew_Char&selectedEndDate=2018&selectedReport=CBS&selectedStartDate=1934&selectedStates=0&sortField=YEAR&sortOrder=desc"]
115 NCUA Quarterly Reports, available at [HYPERLINK "https://www.ncua.gov/newsroom/press-release/2020/ncua-q1-2020-state-credit-union-data-report-now-available"] (In the eight years from December 2011 and December 2019, 1,800 credit unions exited the business.) CUNA estimated about 5,500 at the end of 2019, down from 11,000 in 1999. See, Monthly Credit Union Estimates, June 2020. [HYPERLINK "https://www.cuna.org/uploadedFiles/Global/About_Credit_Unions/CUMonthEst_Jun20.pdf"].
116 Need a reliable number.

The table reveals an apparent drop in the shares of major types of institutions. For depository institutions (banks, savings, etc.) holdings dropped from 56 percent in 1975 to 41 percent in 2019 (close to their share of in 1972). Finance companies and credit unions also lost share over the period, although their declines since 1975 appeared to be more modest. The share loss of nonfinancial businesses accelerated, dropping from about 16 percent to little more than a single point in 2019.

Declining shares of the top three sources should be viewed in the light of the increase in consumer credit overall and the emergence of the Federal government as a major holder. As a result of the rapidly expanding aggregate credit, each of the major sectors has increased its holdings since 1975. Even nonfinancial institutions, with a one tenth of their 1975 share, hold more dollars of consumer credit than they did forty-five years ago (adjusting for inflation would show a decline). Rising aggregate debt has supported all the sectors as multibillion-dollar businesses – with depository institutions passing a trillion dollars.

But for one new source of credit, the shares of banks, credit unions, and finance companies all would have risen along with their dollar volumes. It was the growth of government-held student loans that shrunk the shares despite the dramatic growth of the private sector. The Federal government did not hold enough credit to warrant tracking at the time of the Commission's Report, and its share still rounded to zero in 1975. Today, the government is the second largest creditor of consumers, after depository institutions. If its holdings were subtracted from the table, the shares of the traditional institutions would all increase by half. Banks (and savings institutions) would rise to around 60 percent, while finance companies and credit unions would approach 20 percent apiece, all above their shares in the early 1970s.

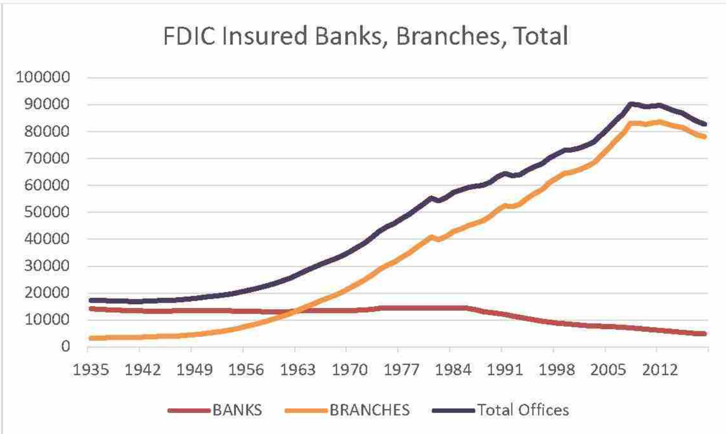
Financial sectors since 1970 fared much like they did in the postwar decades, with some types of institutions growing, others shrinking. Once prominent sources of credit have nearly vanished. In particular, pools of securitized assets rose from miniscule levels and fell back just as quickly in less than two decades. As for the traditional sources that the Commission tracked, banks and credit unions continued their long rise. The latter are now closing in on finance companies, whose shares have fallen over the last ten years. Figure __ [Consumer Credit Outstanding] shows these trends, which suggest a continuation of the rivalry among the sectors that was apparent in the Commission's Report.



For example, changes since the 1970s in sector shares are consistent with inter-sector competition among the traditional sources, just as the shifting shares reflected competition in the first half of the century. Changes likely also indicate dynamic factors at play, such as entry, rivalry, repositioning, and exit of firms. The ensuing discussion examines each sector more closely.

Banks

Growing aggregate shares combined with stable or declining numbers of institutions imply that concentration in consumer credit has increased above the levels the Commission observed. It is a matter of simple arithmetic. Fewer institutions mean higher percentages of the whole. Beneath the aggregates, however, is a different picture. While the number of banks did drop by half, the number of branches tripled, from about 25,000 in 1972 to 78,000 today. The count of total bank offices has declined slightly from its peak of about 90,000 in 2008, but the proliferation of outlets remains near historic highs. The chart below illustrates the trends.[117]



As for credit unions, despite the shrinkage of Federally Insured entities to 5,200, the Bureau of Labor Statistics counted 17,000 total establishments in 2019, much closer to the 1972 tally in the Commission's Report.[118] Likewise, finance company establishments numbered just under 16,000 in 2019[119] – ahead of the 13,000 to 14,000 offices estimated by the Commission in 1970. Overall, the trends show that headquarters of financial institutions have declined while total storefronts have expanded, and for consumers, the storefronts matter. Like gas stations and grocery stores, local offices vie for the consumer's business.

Competition in the banking sector is monitored by both the Department of Justice and the Federal Reserve, which share responsibility for reviewing potential competitive effects of

[117][HYPERLINK "https://banks.data.fdic.gov/explore/historical?displayFields=STNAME%2CTOTAL%2CBRANCHES%2CNew_Char&selectedEndDate=2018&selectedReport=CBS&selectedStartDate=1934&selectedStates=0&sortField=YEAR&sortOrder=desc"]. The same source shows the number of federally insured S&L's declining from over 3,500 to less than 700 between 1984 and 2018.

[118] Bureau of Labor Statistics, Quarterly Census of Employment and Wages, available at [HYPERLINK "https://data.bls.gov/cew/apps/table_maker/v4/table_maker.htm" \l "type=1&year=2019&qtr=4&own=5&ind=522130&supp=0"]

[119] Bureau of Labor Statistics, Quarterly Census of Employment and Wages, available at [HYPERLINK "https://data.bls.gov/cew/apps/table_maker/v4/table_maker.htm" \l "type=1&year=2019&qtr=4&own=5&ind=522291&supp=0"]

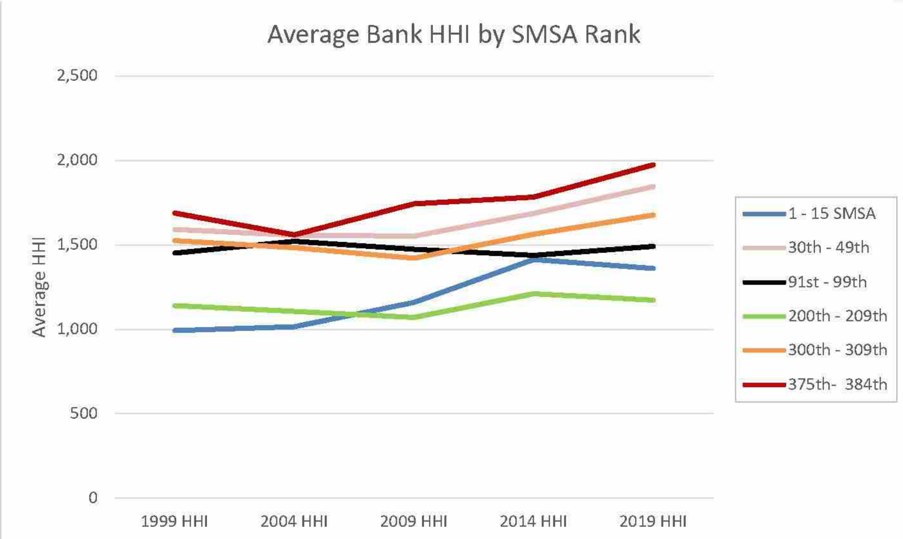
bank mergers. To facilitate that effort the Fed collects and publishes structural data on banks and thrifts in markets across the United States. Concentration is measured by an index, called the Herfindahl Hirschman Index, or HHI, which can range from near zero for a market with thousands of small competitors to 10,000 for a market dominated by one company. The Fed gives close scrutiny to mergers that would significantly increase the index in any market to levels of 1,800 or higher.[120] Mergers that do not move concentration above the threshold and mergers among small institutions in markets above it do not typically raise concerns, because consumers have plenty options at HHI levels around 2,000.

A few examples of larger and smaller markets illustrate the conditions at different points on the HHI scale. The market that includes Houston, Texas has an HHI near 2,300, indicating concentration well above the threshold of scrutiny, and 92 commercial banks, which suggests that customers have a plethora of choices. It is because the top four banks have around 70 percent of total deposits that the score is relatively high. Columbus, Ohio has a score around 2,100, reflecting 48 banks and 9 thrifts.[121] In Fargo, North Dakota, were the HHI is just under 1,800, customers can choose from 34 banks. El Paso, Texas, with a similar score, hosts 14 banks.

Larger markets can accommodate more banks and tend to generate lower scores. The New York City market, for example, with an HHI of 1300, contains 170 banks and 45 thrifts. Chicago, where customers can find 135 banks and 24 thrifts, has an HHI around 950. Even in small metropolitan areas, however, concentration typically remains below 2,000 on the HHI scale. The following chart shows average indexes by size of SMSAs, from the smallest areas to the largest in the Fed's database. Concentration remains below 2,000 for banks and thrifts in most markets.

[120] The Herfindahl Hirschman Index (or HHI), which is the sum of the squares of the percentage shares of the companies in a market. For example, ten companies, each with a share of 10 percent, would result in an HHI of 1,000. The square of 10 is 100, and 100 added ten times equals 1,000. A market comprising five firms of equal size yields an HHI of 2,000 (20 squared x 5). Branches are aggregated by institution, not counted invidually. See, e.g., [HYPERLINK "https://cassidi.stlouisfed.org/index"].

[121] Thrift institutions are discounted by 50% in HHI calculations, in light of their more limited services compared to banks. [HYPERLINK "https://www.justice.gov/sites/default/files/atr/legacy/2014/10/09/308893.pdf"]



122

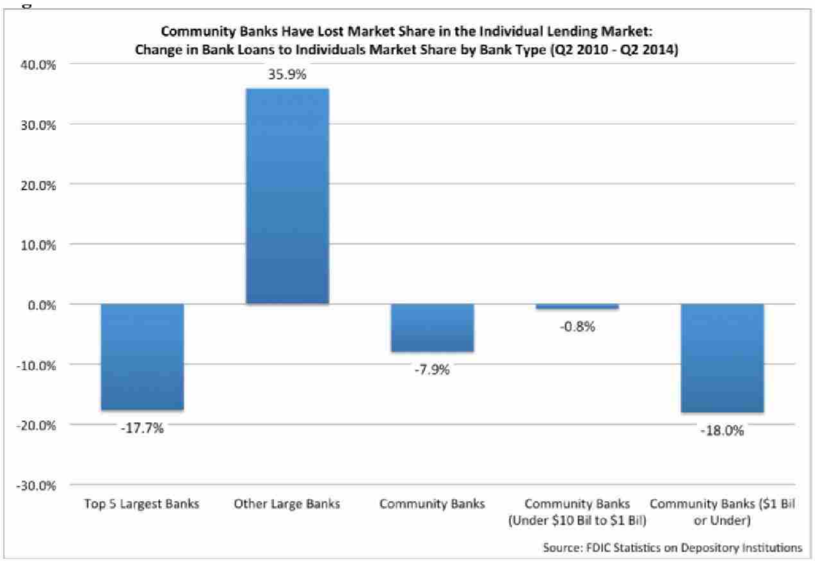
Some indications of the future of competition in banking may be evident from the trends in concentration. Figure ___ shows that in both the larger and smaller markets, concentration was relatively stable between 1999 and 2009, but then rose noticeably in the five years between 2009 and 2014. Over the last five years the rise has reversed in some of the largest markets but continued in smaller population centers.

Within the largest metropolitan markets, the trends in consolidation are unlikely by themselves to suggest potential anticompetitive effects. Banking in big cities has become more concentrated, but not to the point that raises risks of that competition may be suffering. On the other hand, the smaller markets have reached levels that suggest further consolidation could face resistance from competition authorities – if that consolidation occurs by merger. There is little the competition authorities can do to prevent concentration from increasing by attrition, for example when a bank simply exits a market. Both consolidation and attrition are occurring in small markets.

[122]

1-15 Avg Population	7,240,113
32-49 Avg Population	1,591,927
90-99 Avg Population	622,387
200-210 Avg Population	224,861
300-310 Avg Population	134,483
376-384 Avg Population	67,358

An insight into how the changes in concentration can affect the consumer market was described in a 2015 study on community banks.[123] The authors cited Bureau research that had found community banks "can be a lifeline to hardworking families paying for education, unexpected medical bills, and homes."[124] Business pressure, however, was causing these banks to pull back from consumer lending and focus on commercial loans to local companies. Small banks, research has found, have a comparative advantage over large institutions by virtue of the closer customer relationships that the local setting allows. Despite the advantage, the prospects for those banks remain in doubt as well. A chart from the study depicts a shift in lending to individuals:[125]



The Chairman of the FDIC put it more graphically:

[123] Marshall Lux, The State and Fate of Community Banking February 9, 2015, available at [HYPERLINK "https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/files/Final_State_and_Fate_Lux_Greene.pdf"]
[124] Id. (citing Consumer Financial Protection Bureau, Community Banks and Credit Unions, [HYPERLINK "http://www.consumerfinance.gov/small-financial-services-providers/"] (accessed January 10, 2015))
[125] Id., Figure 12, at 19.

> Small banks like these are slowly disappearing from America's landscape. Today, 627 counties are only served by community banking offices, 122 counties have only one banking office, and 33 counties have no banking offices at all.[126]

It bears repeating that structure is just the beginning of a competition analysis. Factors other than concentration can compound or alleviate initial concerns that the census and measure of firms in a market may raise. In sectors where competitors can increase capacity quickly, as is the case in consumer credit, concentration measures exaggerate the significance of large firms. Another ambiguity in bank indexes stems from their units of measurement. HHIs are based on total deposits, which are at best loosely correlated with the various financial services that banks and thrifts provide.[127] Because banks can readily reallocate funds from one investment to another – for example from business finance to consumer credit or from mortgages to auto loans – their ability to compete for consumers is not tied tightly to their total assets. As described earlier, banks facing diminished commercial demand during the Great Depression opened new consumer credit departments, emulating smaller finance companies that were expanding their own operations. Such flexibility means that concentration measures do not fully capture the competitive threat that small rivals or small operations present to established institutions. The structure of a market at any given moment provides a helpful context to an assessment of competition, and trends in structure can be even more revealing, but neither is sufficient to draw conclusions about competition.

After identifying the contours of a market and the qualifying the participants in it, a competition analysis typically turns to the conditions of entry. Consolidation, decline, and even the failure of firms may have little impact on competition if new companies can fill the voids left by companies that decline or depart. Finance companies that opened offices a century ago while authorities were closing others illustrated this phenomenon. Competitive analysis must therefore consider conditions of entry, as it is a powerful antidote to anticompetitive performance and unsatisfied demand.

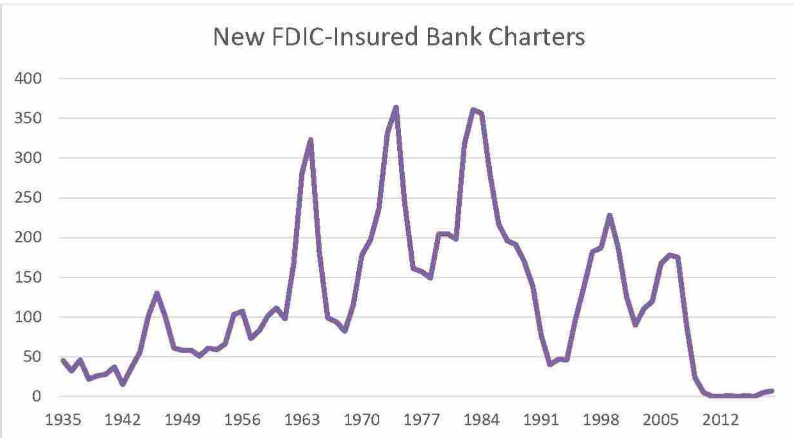
Here the evidence is disconcerting for the banking sector. As is apparent in the trends of new charters for FDIC-insured banks, entry of banks has dropped to the lowest levels in eighty years. After averaging over a hundred a year from 1960 to 2010 – often exceeding two hundred and more – roughly two charters a year have issued in United States since 2010. The phenomenon could be driven by diminished interest in entering the sector,

---

[126] Jelena McWilliams, "BankThink/We can do better on de novos," *American Banker,* December 06, 2018, [HYPERLINK "https://www.americanbanker.com/opinion/fdic-chairman-jelena-mcwilliams-we-can-do-better-on-de-novos"].

[127] A Fed study noted that "HHI is a measure of concentration for the base good, a bank account measured by deposits, and less of a measure of competition for the aftermarkets. Since most bank fees stem from aftermarket good purchases, the standard relationship between concentration and…fees need not apply." Available at [HYPERLINK "https://www.federalreserve.gov/econres/feds/files/2017054pap.pdf"].

higher costs of doing so, or a combination of both. It may be that an FDIC-insured charter is not as important an asset as it once was in the provision of financial services. If so, that could explain a declining demand for the charters. An alternative hypothesis is that insured banks remain an important component in the competitive environment, but that entry has become so costly that efficient providers are discouraged from taking the opportunity. The most recent data suggest a rise in new banks applying for FDIC the last few years, with the annual openings averaging half a dozen in the 2017 to 2019. The pace prompted the Chairman of the FDIC to observe that "never before has the level of new banks been so low for so long — only two new startup banks opened between the end of 2010 and the end of 2016, and just 11 have opened since the end of 2009, most in the past 18 months."[128] Entry conditions in banking merit more attention.



Better data, more sophisticated statistical techniques, and improvements in economic analysis enable more direct assessments than the Commission could make of the intensity of competition. The banking sector is especially amenable to analyses that go beyond inferences drawn from differences in concentration across states. Numerous studies of bank competition have been published in recent years, the results of which indicate a business where competition has been keen. Reviewing the literature in 1994, Shaffer found that most U.S. banking markets "behave quite competitively at the bankwide level,

[128] Jelena McWilliams, "BankThink/We can do better on de novos," *American Banker,* December 06, 2018, [HYPERLINK "https://www.americanbanker.com/opinion/fdic-chairman-jelena-mcwilliams-we-can-do-better-on-de-novos"]

even where highly concentrated," although there may be some exceptions in some individual product lines, such as consumer deposit accounts.[129]

In a recent study that tracked the performance of the banking sector from 1984 to 2016, Mendenhall found that its performance exceeded competitive equilibrium levels.[130] He found output of the banks to be "supercompetitive," greater than that expected from competitive markets, and competition did not suffer from the trend of increasing concentration. To the contrary, the evidence pointed toward improving competition. For example, the spread between cost of funds and interest charged actually declined, from 3.3 percent at the beginning of the of the period studied to 2.9 percent at the end.

Most of the competition studies assess banks' overall business, which includes both commercial and consumer lines. Commercial customers are well equipped to impose competitive discipline; they can take their business anywhere in the country and to sources overseas. Whether consumers realized the benefits of competition that these studies have found requires examination of the services they purchase in the market.

There is no question that consumer choices have expanded since the time of the Commission's Report. Already mentioned are the branches, which grew by the tens of thousands and brought banking to underserved communities and closer to consumers in larger markets. Beyond brick and mortar, innovation has provided a growing volume and variety of banking services. The Automatic Teller Machine first appeared in 1969. Now ubiquitous, these outlets have grown to an estimated 470,000 in 2018.[131] Banks were the original owners and proprietors of ATMs. Today, fewer than half are bank machines; the remainder are operated by independent companies. Whether owned by the user's bank, another bank, or nonbank institution, ATMs connect consumers with their banks and many of the services their banks provide. Among the aspects that distinguish independent ATMs: they are more likely to locate in areas with higher unemployment, lower incomes and lower housing values. Like the consumer lenders of a century ago, independent institutions have brought financial services to communities where banks are relatively rare.[132]

In 1972, the most elementary financial transaction meant a trip to the teller. Consumers no longer need to travel to a bank, a branch, or even an ATM to access sophisticated

[129] Shaffer, Bank Competition in Concentrated Markets, Business Review, March/April 1994.
[130] Mendenhall, Commercial Bank Competition, Riegle-Neal, and Dodd-Frank, August 4, 2017, [HYPERLINK "https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2967998"].
[131] The Locational Study of ATMs in the U.S. by Ownership, available at [HYPERLINK "http://www.akleg.gov/basis/get_documents.asp?session=31&docid=22687"]
[132] And the higher transaction fees that independents charge have inspired efforts to cap them. Id.

financial services. According to the American Bankers Association,[133] 70 percent of U.S. consumers used a mobile device to manage their bank account at least once in September 2019, and a third of U.S. adults used a mobile app to make a payment or transfer money in the year. More often than not, the app they chose did not come from their bank. Payment volume on PayPal and Venmo outpaced activity on the banks' apps. Apple Pay and Starbucks were also well established as alternative payment providers. The advent of these technologies is allowing a new type of bank to enter the market, a bank without any physical retail locations. One survey estimated that 30 percent of the US population either has opened or plans to open an account at an online-only bank.[134]

These developments were made possible by changes in the legal environment of consumer finance, and some of the changes track the recommendations in the Commission's Report. Restrictions the Commission criticized have been amended, repealed or rendered obsolete. Antitrust enforcement has reduced anticompetitive practices. The developments are especially relevant to barriers between institutional segments, geographic markets, interest rate flexibility, loan availability, lender and servicer performance, and discrimination among borrowers.

The opening of geographic markets and the competition between institutions would have been impossible without legal reforms of the sort that the Commission advocated. Pivotal events included a Supreme Court decision in 1978, which settled the question as to which state laws would apply to interstate banks, the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, which lifted restrictions that states had imposed on banks crossing borders, and the Gramm-Leach-Bliley Act of 1999, which expanded the financial services banks could offer.[135] The reduction of these barriers unleashed the proliferation of branches described above, as banks quickly crossed the borders that previously had confined them.

A summary of the literature on barriers and whether their relaxation affected competition in banking found that the spread of branches had been painful for some local banks, especially in rural areas, but beneficial for consumers.[136] Empirical analysis documented some of the effects on access to credit:

---

[133] Release, Survey 95 Percent of Consumers Give High Marks to Digital Banking, November 13, 2019, available at [HYPERLINK "https://www.aba.com/about-us/press-room/press-releases/Survey-95-Percent-of-Consumers-Give-High-Marks-to-Digital-Banking"]
[134] Liz Knueven, Online banking isn't just for millennials anymore — it's quickly becoming the norm Nov 14, 2019, available at [HYPERLINK "https://www.businessinsider.com/personal-finance/online-banking-gaining-popularity-united-states"].
[135] Marquette Nat. Bank v. First of Omaha Svc. Corp., 439 U.S. 299, 99 S. Ct. 540; 58 L. Ed. 2d 534 (1978) (interpreting the National Bank Act of 1864); H.R.3841 - Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, 103rd Congress (1993-1994).
[136] [HYPERLINK "https://www.federalreserve.gov/pubs/feds/2007/200751/200751pap.pdf"]

> We first establish the positive effect of interstate branching deregulations on the density of bank branches in poor counties. We find that the density of bank branches increases by around 30% in poor counties after a state fully deregulates.
>
> Second, we show that interstate branching deregulation is associated with a significant drop in the rate of unbanked households among low-income populations. [Illustrative is] the change in the likelihood of holding a bank account in the years before and after deregulation relative to a control group of states that do not deregulate. We observe a significant increase in the share of banked households following deregulation.[137]

Another study found similar effects. Branches that spread after banks were allowed to cross state lines reduced the percentage of unbanked populations in poor communities.[138] The effect was stronger for populations that were likely to be rationed by banks, "such as black households living in "high racial bias" states, or for households living in rural areas where branch density is initially low."

Legislation and regulations that increase costs or reduce opportunities can compound the challenges facing institutions on the margin of profitability. Considering pressure on banks and credit unions in smaller communities, the US Treasury identified potential effects:

> Community financial institutions' business models have come under pressure from a slow economic recovery and low interest rate environment, additional competition (e.g., internet banks and nonbank lenders), and added compliance costs from new regulations. Together such factors have contributed to a difficult operating environment and the ongoing consolidation of smaller banks and credit unions.…The impact of consolidation has been particularly profound on smaller banks as the number of institutions with assets less than $100 million declined by 85% between 1985 and 2013. Similarly, the total number of credit unions in the country has declined…, with the impact mostly concentrated among smaller credit unions. Feedback provided to Treasury suggests that the cumulative effects of regulatory requirements weigh heavily on community banks and credit unions.[139]

[137] Bank Branch Supply and the Unbanked Phenomenon, available at [HYPERLINK "https://pdfs.semanticscholar.org/e9b6/f210629419b5ec6f53f8227448a29dae61f0.pdf?_ga=2.249876995.461538237.1596483228-41928408.1596483228"]

[138] Claire Celerier and Adrien Matray, "Bank Branch Supply and the Unbanked Phenomenon," Draft, October 17, 2016

[139] US Treasury, A Financial System That Creates Economic Opportunities - Banks and Credit Unions, 56-57. Available at [HYPERLINK "https://www.treasury.gov/press-center/press-releases/Documents/A%20Financial%20System.pdf"] (footnotes omitted).

The concerns expressed by the Treasury are reflected in the findings of academic research. Lux summarized research that found bank consolidation increasing after regulatory and legislative changes made operations more costly. Researchers were typically careful to note the difficulty of finding causal links between events and subsequent developments, but the number of studies finding correlations between different regulatory initiatives and changes in banking markets led the author to suggest that regulation was causing consolidation.

Among the evidence that has accumulated in the literature are studies that have focused on specific compliance costs of Dodd-Frank. A 2014 survey reported that over a quarter of banks with less than $10 billion in assets planned to hire new compliance or legal personnel, while over a third of banks had already hired new staff to deal with new CFPB regulations.[140] A Minneapolis Fed study that year identified the personnel costs of complying with regulations at banks with less than $50 million in assets. Lux described the findings and a Fed Governor's reaction:

> At these institutions, the study found that hiring two additional personnel reduces median profitability by 45 basis points, resulting in one-third of these banks becoming unprofitable. As Fed Governor Tarullo has noted, "Any regulatory requirement is likely to be disproportionately costly for community banks, since the fixed costs associated with compliance must be spread over a smaller base of assets."[141]

A decade of experience under Dodd Frank has begun to generate more direct evidence of effects on competition, allowing analysts to examine whether the concerns were justified. Mendenhall examined the effects of two major reforms – the Riegle-Neal Act and the Dodd-Frank Act – and he found that bank competition clearly increased after Riegle-Neal, and appeared to increase after Dodd-Frank, although the findings with respect to the latter were only marginally significant.[142]

Never far from the subject of competition in financial markets is the question whether competition is consistent with safety and soundness.[143] On one hand is the concern that competition will cause banks to make excessively risky loans. On the other is the expectation that competition will better serve consumers.

[140] Lux, (citing Hester Peirce, Ian Robinson & Thomas Stratmann, "How Are Small Banks Faring under Dodd-Frank?" (Working Paper 14-05, The Mercatus Center at George Mason University, February 2014)).
[141] Id., (citing, Tarullo (speech at the Federal Reserve Bank of Chicago Bank Structure Conference, May 8, 2014)).
[142] Mendenhall, Commercial Bank Competition, Riegle-Neal, and Dodd-Frank,
August 4, 2017, [HYPERLINK "https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2967998"].
[143] The debate was joined by Adam Smith in 1776. (See appendix.)

Empirical research offers some insight. For example, one study found that "increased competition induces banks to become more specialized and efficient" but also induces banks to extend credit to riskier borrowers and suffer higher default rates. However the author did not reach a definitive conclusion as to soundness. Her qualified conclusion was that that the competition was "possibly creating a less stable financial system."[144]

Another study found that in competitive mortgage markets, local banks lowered their lending standards by twice as much as those in concentrated markets, but the pressure did not appear to affect standards at national banks.[145] Implications about soundness were accordingly qualified.

A third study found that both national and local banks reacted to changes in competitive conditions.[146] Using the event of OCC's preemption of state regulations, the authors compared mortgage lending in formerly restrictive states to lending in states that had imposed more limited rules. After the lifting of restrictions, national banks increased originations of riskier loans – for example with deferred amortization or interest-only payments. Local banks followed suit, but only in counties where OCC banks were more concentrated. The changes resulted in lower interest rates for some borrowers and new credit to borrowers would not have qualified for mortgages before the regulatory change.

Easing standards does not necessarily imply imprudent lending. Loans extended to applicants who may not have qualified under stricter standards, may be just as sound, if the new standards are based on superior efficiency and risk assessment, which competitive discipline can instill. One study lends some support to this hypothesis. It analyzed direct evidence of prudential concerns and found competition positively correlated with financial stability.[147] Banks in competitive states were less likely to be targeted for regulatory enforcement and less likely to fail. Banks facing more competition earned lower interest margins, made fewer high-risk investments, had lower profitability, and held less cash and Tier 1 capital than banks facing less competition.

---

[144] Gissler, et al., The Effects of Competition in Consumer Credit Markets, WP 12-24, Consumer Finance Institute, (2018) available at [HYPERLINK "https://doi.org/10.21799/frbp.wp.2018.24"].
[145] Xiaochen Feng (2018). Bank Competition, Risk Taking and their Consequences: Evidence from the U.S. Mortgage and Labor Markets. IMF Working Papers. [HYPERLINK "https://www.imf.org/en/Publications/WP/Issues/2018/07/06/Bank-Competition-Risk-Taking-and-their-Consequences-Evidence-from-the-U-S-46034"]
[146] Di Maggio, Kermani, and Korgaonkar (2018). Partial deregulation and competition: Effects on Risky Mortgage Origination. Management Science. 10.1287/mnsc.2018.3060 [HYPERLINK "https://www.researchgate.net/profile/Sanket_Korgaonkar2/publication/327834191_Partial_Deregulation_and_Competition_Effects_on_Risky_Mortgage_Origination/links/5ba80a8b45851574f7e19b11/Partial-Deregulation-and-Competition-Effects-on-Risky-Mortgage-Origination.pdf"]
[147] Akins et al. (2016). Bank Competition and Financial Stability: Evidence from the Financial Crisis. Journal of Financial and Quantitative Analysis, 1-28. [HYPERLINK "https://doi.org/10.1017/S0022109016000090"].

For these reasons, the implications of consolidation continue to merit careful consideration. Competition could be a cause, a consequence, or both, of consolidation. Likewise, consolidation could be salutary, neutral, or deleterious to competition. It is important to detect the distinctions and directions of causation, if any, in order to avoid false diagnoses and prescriptions that could fail to remedy problems or, worse, exacerbate them. It is even more important to discern as directly as possible the intensity and effect of competition itself, and to assess the external conditions that can affect it.

Credit Unions

Like banks, credit unions have increased lending significantly over the last fifty years, even though the number of institutions has dropped. Also like banks, institutional counts of credit unions underestimate their competitive presence. Branching has kept the number of offices closer to their 1970 levels, and credit unions have become closer alternatives to banks and thrifts for consumer services. For example, credit unions take deposits, lend to consumers, issue cards, and finance purchases. Not surprisingly, studies find evidence of this competition in the rates that the institutions charge. One study found that when credit unions were more prevalent in a market, credit card loan rates fell.[148] Another study, looking at regulation that allowed credit unions to compete more closely with banks, found that the increased competition was especially beneficial for low-income borrowers.[149] The cost of borrowing fell, banks became more efficient, and both banks and nonbank lenders extended more credit to riskier borrowers.

By the critical measure of the price of services, credit unions often beat banks, as they did when the Commission studied the sector fifty years ago. Interest rates on credit cards averaged between 11 and 12 percent at credit unions, lower than average bank-card rates.[150] Other loans tend to be cheaper at credit unions as well. These advantages help explain why credit unions have seen their holdings of consumer credit grow faster than banks. Membership in credit unions passed 120 members in 2019, an increase of about 50 million in twenty years.[151]

---

[148] Feinberg, R., Credit Unions: Fringe Suppliers or Cournot Competitors? Review of Industrial Organization, 20(2), 105-113, (2002).

[149] Gissler, et al., The Effects of Competition in Consumer Credit Markets, WP 12-24, Consumer Finance Institute, (2018) available at [HYPERLINK "https://doi.org/10.21799/frbp.wp.2018.24"].

[150] Creditcards.com, Credit Union and Regional Bank Credit Cards, available at [HYPERLINK "https://www.creditcards.com/credit-union/"]. (The biggest advantage of a credit union credit card? It likely has significantly lower interest, possibly even offering rock-bottom interest on cash advances. In November 2018, the average interest rate offered by credit unions for credit cards was 11.1%, a steady figure over the last 10 years. That compares to the national average rate of 17.08% in March 2020."); See, also, [HYPERLINK "https://www.spglobal.com/marketintelligence/en/about/"].

[151] Cuna.org, Monthly Estimates (June 2020) available at [HYPERLINK "https://www.cuna.org/uploadedFiles/Global/About_Credit_Unions/CUMonthEst_Jun20.pdf"].

Some sizeable differences in the institutions play a role in the competition between the sectors. Credit unions are non-profit entities, owned by their members, and enjoy tax benefits from that status. Consumer credit holdings of the average credit union remain about the third of the size of those in the average bank, and credit unions are restricted to the consumer channel. The limitation means that commercial banks have the benefit, and of course bear the risk, of other holdings as well. Credit unions, although often local and limited to members of identified organizations, vary in size and geographic reach. Large ones operate through branches, ATMs, and online across the country.

Competition between banks and credit unions is also apparent in the rivalry of their respective organizations. The two sectors are frequently at odds over public policy that treats them differently. Bankers' associations have opposed credit-union acquisitions of banks, credit-union loans to businesses, and other extensions that threaten traditional bank services. The banking sector criticizes as unfair the tax advantage of credit unions and cites it as a justification to limit their activities. Credit unions seek to unleash themselves from restrictions such as those against business lending, which would allow them to enter more areas of competition with banks. It is not necessary to take a position on these arguments to conclude that the debate itself reveals potential competition between the two sectors – potential that has not been realized. The barriers against credit-union expansion harken back to those that the Commission deemed anticompetitive fifty years ago.

Finance Companies

For decades the second most important sector of consumer credit, finance companies offer a variety of products that consumers can obtain at banks, credit unions and retail lenders.[152] As the chart on sector growth reveals, however, this sector is losing share. According to the Federal Reserve, consumer receivables outstanding have been flat for the last five years.[153] Enthusiasm for the sector remains high among industry participants, however, and the reason is its ability to take business away from other types of institutions. Experts convened by Experian in 2017 reported that "individuals are largely leveraging personal loans to consolidate debt or perhaps fund an expense like a vacation or an unexpected event. Once the consumer comes into cash, they'll pay off the loan, but consider revisiting a personal loan again if their financial situation warrants it."[154] Among the data supporting the findings were these:

[152] CCAE at 25.
[153] Statistical Release, Finance Companies (June 2020), available at [HYPERLINK "https://www.federalreserve.gov/releases/g20/current/g20.pdf"]. **(Note to Tom D –numbers in the statistical release don't agree with Table 2-1)**
[154] Kerry Rivera, Anticipating and growing personal loans in 2017 (January 26, 2017) [HYPERLINK "https://www.experian.com/blogs/insights/2017/01/personal-loans-trends/"] .

67% of consumers who open a personal installment loan had a revolving trade with a positive balance.

5% of consumers who close a personal loan open another one within a few months of the original loan closure

68% of consumers who open a new personal loan shortly after closing one do so with the same company

Like banks, finance companies range from smaller, local establishments to cross-country networks. Many, including industry leaders, can extend credit entirely online. They offer personal loans, mortgages, auto loans and other types of credit. Banks regard them as attractive acquisitions. In 1972, the Commission reported on banks' buying finance companies in order to extend loans that regulations prevented banks from offering. Today, the finance-company sector remains an inviting business for entry from the banking sector. As recently as September 2020, the appeal was reported in the American Banker, which revealed that "card networks, along with PayPal and Citi, are responding to competition from the likes of Affirm, Afterpay and other "buy now, pay later" lenders. Should traditional credit card lenders be worried?"[155] The answer to this rhetorical question was not necessary to report.

Competition in Credit from the Consumer's Perspective

Competition for the Borrower

The discussion that follows will take the perspective of the consumer, whose welfare is the principal concern of competition policy and the central mission of the Bureau. Because finance supports the consumption of other goods and services, demand for financial services is shaped by the ultimate purposes a consumer has in mind. For both borrowing and saving, the primary consideration is the time horizon – how long a consumer wants the use of money or when a consumer wants to withdraw money deposited for future use. Financial services that simply facilitate transactions, such as payment systems, serve the purpose of enhancing convenience and reducing costs of transactions.

The last portion of the chapter deals with upstream markets. For most financial services, consumers select the vendors. For some, consumers deal with vendors that their retailer selects. Consumers do not select and may not know until months or years later, if ever, who provides services to the lender, who manages the loan, and who collects overdue payments. Two services are of critical importance: sales of information about

[155] Kevin Wack, "Why Visa and Mastercard are suddenly keen on installment lending," American Banker, September 02, 2020, available at [HYPERLINK "https://www.americanbanker.com/tag/consumer-lending"]

creditworthiness – both credit ratings and credit reports – and third-party collection of debts. Finally, the chapter will consider aspects of competition in deposit services and payment systems.

There are few precise distinctions among the lengths that loans can run. Loans in a variety of sizes can last for weeks, months and years. Some useful characteristics emerge, however, from rough distinctions. The analysis will consider three general categories – short term, medium term and long term. Within each category, the analysis will consider the offers available to consumers and the competition that among providers extending those offers. It is possible that the evidence will reveal that some products within each group do not compete in all respects with one another, and equally conceivable that the products in some groups compete with other products outside the groups.

Companies that typically finance purchases in a product category may not present the most attractive alternatives to some consumers. Second mortgages can finance car purchases. As the Commission observed fifty years ago, consumers can reallocate debt to obtain funds regardless of purpose. More often, however, borrowers in the market for short term credit will look at products designed to meet those needs. A loan to repair the car until the next paycheck will likely come from a short-term source. A loan to finance a house or car purchase will likely come from a provider of multi-year, securitized loans. In most cases, however, the competition that affects prices and terms that consumer see will come from providers within categories.

Different consumers often see different terms and conditions. Financial services are among the most customized products or services that consumers acquire. Terms depend on the information and skills that both borrowers and lenders bring to the transactions, expectations, history, attitudes toward risk – and most importantly, on the perceived ability of the borrower to repay. Because of this customization, loan products are often unique to the participants of the original transaction.

The most prominent distinction that influences customization, affordability and availability are the credit histories and credit scores of borrowers. The tables below list consumers within each FICO group. Borrowers with poorer FICO grades find fewer choices in the marketplace. Lenders with greater risk aversion limit their business to consumers in better risk categories. According to one study, "A little less than a fifth of Americans, or 18%, have a FICO® Score of 580 to 669, often considered "subprime" credit scores by lenders. Zooming out, 34% of Americans have a FICO® Score in the 300-to-669 range." Credit card holders, 67 percent of consumers, have an average FICO Score in the low 700s.[156]

[156] Matt Tatham, "2019 Consumer Credit Review," Experian, January 13, 2020 (The [HYPERLINK "https://www.experian.com/blogs/ask-experian/state-of-credit-cards/"] for Americans reached $6,194 in 2019, as

Percent of Americans by FICO© Grades and Scores 2019[157]		
FICO Grade	Score	Share of Total
Very Poor	300-579	16%
Fair	580-669	18%
Good	670-739	21%
Very good	740-799	25%
Exceptional	800-850	20%

Retail Credit Product Groupings		
Short Term	**Medium Term**	**Longer Term**
Payday Loans	Credit Cards	Auto Loans
Small Dollar Loans	Installment loans	Installment loans
Overdraft Protection	Rent-to-own contracts	Mortgages
Pawns	Title Loans	Student Loans
Personal Networks/ P2P	Personal Networks / P2P	Personal Networks/ P2P

At the outset, it is worth noting that ranking consumers and customizing products are themselves forms of discrimination. When based on sound business reasons – such as the risk that a loan will be repaid – such discrimination can enhance lending efficiency, consumer welfare, and system stability. Ignoring such distinctions can bankrupt debtors and creditors like. In extreme cases – like the crises of 1929 and 2008 – indiscriminate lending can devastate financial markets and ruin sectors.

However, when discrimination is unrelated to legitimate business considerations, it can cause consumer harm. Public policy has identified some of the most serious harms and prohibited such discrimination in fair lending laws and regulations. The protection of consumers from prohibited discrimination is the subject of other chapters. Here it is worth considering whether competition discourages ignorant, irrational, or malevolent discrimination.

As a matter of theory, when buyers in a marketplace have numerous choices with whom to deal, they can penalize providers that discriminate by patronizing competitors that do not. Numerous studies of various industries have found evidence that the discipline of competition does indeed reduce discrimination. While those are beyond the scope of this

balances increased 3% compared with 2018, according to Experian data. The average FICO® Score for consumers with a credit card is 727, and 67% of Americans carried a credit card in 2019.) [HYPERLINK "https://www.experian.com/blogs/ask-experian/consumer-credit-review/"].

[157] Check cite. (Id.?)

chapter, it is worthwhile to consider those that have explored credit markets. These tend to confirm the hypothesis that competition inhibits illegitimate discrimination. For example, Lux, et al found that:

> the effect of intensified bank competition is stronger for populations that are ex ante more likely to be rationed by banks, which reinforces the identification of supply effects. First, we find that black households benefit more from branching deregulations than do non-black households only in states with a history of discrimination. For the same level of income, black households are indeed 20% less likely than white households to hold a bank account in states with a history of discrimination, but this gap narrows to only 15% after deregulation, to the level observed in states with no history of discrimination. Second, the effect of branching deregulations increases when the level of income decreases.[158]

Another study considered settings where competition may be attenuated and found that opportunities for discrimination increased. One situation that has been the subject of research and regulation is the market for automobile loans, many of which are made in a private negotiation in the dealership. A study of that sector found that competitive markets did not drive the lowest prices for consumers, because poor transparency in the market allowed dealers to create better deals for themselves than for consumers.[159] In these loans, according to the authors, credit worthiness of the individual borrower and the details of the auto loan (term length, payment-to-income ratio, etc.) significantly influenced price. The study also found, however, that prices paid by consumers varied widely even after controlling for credit worthiness, and minority borrowers paid more than their relative risk and other legitimate factors justified:

> A majority of consumers paid no 'markup' over the credit-based buy-rate, while a small percentage of consumers paid thousands of dollars in additional markup. Moreover, minority borrowers were found to be highly over-represented in the category of those paying significant markups.[160]

Chapter 9 explores how the market has responded to the situation, and how innovation could protect future consumers.

---

[158] Marshall Lux, The State and Fate of Community Banking February 9, 2015, available at [HYPERLINK "https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/files/Final_State_and_Fate_Lux_Greene.pdf"]. (including a survey of the literature).
[159] Cohen (2012). Imperfect Competition in Auto Lending: Subjective Markup, Racial Disparity, and Class Action Litigation. Review of Law and Economics.
[160] Id. A study of mortgages analyzed FHFA data for evidence of discrimination against minority borrowers relative to white borrowers in more concentrated markets. The results "fail to reject the null hypothesis of no noneconomic discrimination." James A. Berkovec, Glenn B. Canner, Stuart A. Gabriel and Timothy H. Hannan, Discrimination, Competition, and Loan Performance in FHA Mortgage Lending, Review of Economics and Statistics, Volume 80 | Issue 2 | May 1998 p.241-250 (Posted Online March 13, 2006 [HYPERLINK "https://doi.org/10.1162/003465398557483"]).

Short-term loans – overdrafts, payday loans, pawnshops, personal loans

Borrowers looking for short term loans will find conditions favorable for competition. The majority of consumers have alternatives available from sources that are not traditionally considered in the segment. Anyone who has a credit card can obtain a loan for fifteen days, a few months, or a year, and people with FICO scores in the mid-600s or above can typically qualify for cards. Their options for short-term loans are virtually unlimited.

For the third of the population with lower scores or thin files, the options are limited to those in the first category - short-term loans. They have access to payday loans, if they live in states that permit lenders to make such loans. Entry barriers are nonexistent, and the numbers of providers are high. It has often been said that "there are more payday loan stores than McDonald's or Starbucks… nearly 18,000 payday loan stores in this country right now."[161] Payday lenders, like the salary lenders of a century ago, are expensive but unlikely to exercise market power.

In addition to payday lenders, borrowers with few other options have access to some 10,000 pawnshops according to the National Pawnbrokers Association. Significant overlaps in product characteristics and prices among pawnshops, payday lenders, and overdraft protection services. Some research has found rates to be comparable,[162] which suggests the three may be in one market. Casting doubt on these implications are surveys that indicate payday borrowers seldom consider pawnshops.[163] The ability of banks to compete for small-dollar, short-term loans may have been hampered by regulations from both OCC (on the direct front) and CFPB (with overdraft rules) in their efforts to enter. P2P and personal networks may be available to those who cannot access any of these sources. These sources are too new and too difficult to measure to allow for confident predictions.

On the question whether payday loans compete with other types of loans, Durkin, et al. report that significant interinstitutional competition arose after the relaxation of rate ceilings and other restrictions in the 1980s and 1990s.[164] Evidence for that competition was described in a 2013 article:

---

[161] NGPF, [HYPERLINK "https://www.ngpf.org/blog/question-of-the-day/qod-which-business-has-the-most-physical-locations-in-the-us-mcdonalds-payday-lenders-or-starbucks/"]

[162] Not found in the resources reviewed to date is an accounting for the cost of convenience of the three options. Payday convenience for example, may be worth more than the difference interest payments, while security forfeitures, if factored into interest rates, would increase borrowing costs at pawnshops.

[163] Cite.

[164] CCAE at 508.

> Competition benefits consumers in the alternative consumer credit markets just as it does in any other market, providing consumers with the opportunity for lower prices, innovation, and higher-quality service. Although prices seem high for both payday loans and overdraft protection, there is no evidence that either product generates sustainable economic profits (as opposed to normal economic returns). Payday loan prices generally reflect underlying risk and operating costs. There is no evidence of supranormal economic (or monopoly) returns to firms in the payday lending industry, indicating the competitive nature of the market. Barriers to entry in the payday lending market appear to be low.[165]

In recent years, however, competition between payday lenders and other sources of credit may have diminished. Since 2003, OCC effectively has effectively prohibited banks from offering short-term, small-dollar loans. When banks tried to compete in the space anyway, for example by offering overdraft protection, the Fed restricted those efforts with additional restrictions in 2009. The effects were immediate, according to Evans, Litan, and Schmalensee, who found, "within days" of the Fed's announcement of its new overdraft rules, banks started scaling back access to free checking, imposed new fees, and eliminated services for consumers.[166]

Some banks still offer overdraft protection and direct-deposit-advance products that may compete with small-dollar lending.[167] Consumers who opt in to such services tend to be credit constrained: compared to others, they have lower credit scores, are less likely to have a general-purpose credit card, and more likely to have low limits on cards they do have.[168] Payday borrowers display similar profiles. In markets where banks offer these products, borrowers may benefit from the additional competition.

Online information available to consumers suggests that pawns, personal loans, and payday loans may be alternatives to one another. According to Credit Karma, the average pawnshop loan is $150, and pawnshops are no longer confined to inconspicuous storefronts and strip malls. Online sites will pawn items worth hundreds or millions of dollars. For consumers considering a pawnshop, however, Credit Karma, a marketer that combines advertising with advice, suggests peer-to-peer options, negotiating extensions

[165] PAYDAY LENDING, BANK OVERDRAFT PROTECTION, AND FAIR COMPETITION AT THE CFPB, Review of Banking & Financial Law, Vol. 33, No. 1, pp. 235-281, at 258 (2013).
[166] Id. at 263 (citations omitted).
[167] CFPB, CFPB Study of Overdraft Programs: A White Paper of Initial Data Findings (June 11, 2013), available at [HYPERLINK "https://files.consumerfinance.gov/f/201306_cfpb_whitepaper_overdraft-practices.pdf"]. ("Between 20% and 27% of accounts opened in 2011 had one or more overdraft or NSF transaction. …Between 13.5% and 27.8% of accounts with at least one overdraft or NSF transaction had at least 10 such transactions.")
[168] CFPB, Data Point: Frequent Overdrafters (Aug. 4, 2017), available at [HYPERLINK "https://www.consumerfinance.gov/documents/5126/201708_cfpb_data-point_frequent-overdrafters.pdf"].

with current creditors, and approaching neighbors and friends. In a clue that a payday loan is another alternative to these sources, Credit Karma cautions against it:

> Getting a [HYPERLINK "https://www.creditkarma.com/advice/i/payday-loans/" \t "_blank"] might also cross your mind if you're in a jam, but they're a financially dangerous option unless you're 100% sure you can pay yours back on time — and even then they're still terribly costly.[169]

With the advice comes advertising for numerous short-term and medium-term loans. Information about products and providers eager to offer them is plentiful.

Surveys of small-loan borrowers found that they considered various options to obtain short-term credit, including skipping payments to existing creditors, borrowing from family, overdrawing their bank account, and taking out a small-dollar loan.[170] Academic research described in Chapter 10 has found that bans on payday loans cause customers to shift to these options; and in states that ban the loans consumers also cross borders to borrow if neighboring states permit them. That consumers resort to these options does not itself indicate that they are all good substitutes. When a service is unavailable altogether, consumers may settle for inferior options they would not have chosen in a competitive market. A survey commissioned by the industry lends some support to the superiority of payday loans over their closest alternatives. Almost 75 percent of the small-loan or payday borrowers surveyed said they could not find an alternative when they took out their last loan.[171] These are borrowers who apparently considered but could not secure credit cards, installment loans, second mortgages and other loans offering more attractive terms. People in these circumstances, like the small dollar borrowers of a century ago, competition may be the last line of consumer protection available.

Medium term loans – Credit Cards, Installment Loans, Rent-to-own, Title Loans

As reported in Chapter 2, the largest contributor to the growth of consumer credit held by banks has been the bank credit card. At the time of the Commission's report, revolving credit at retailers far exceeded the amount on bank cards. Today the positions are reversed. Numerous factors explain these trends, starting with convenience. Consumers who once carried cards for gas stations, department stores, travel companies, and

[169] Anna Baluch, "Is a pawn shop loan a good idea for quick cash?" Credit Karma, Updated July 19, 2019, [HYPERLINK "https://www.creditkarma.com/personal-loans/i/pawn-shop-loans/"]
[170] Advance America, CFPB Small Dollar Rule and Consumer Choice, [HYPERLINK "https://www.advanceamerica.net/news/consumer-issues/cfpb-small-dollar-rule-and-consumer-choice"]
[171] PR Newswire, Payday Borrowers Are Far More Favorable Toward and Informed About Payday Loans than Voters without Payday Loan Experience (March 14, 2016), [HYPERLINK "https://www.prnewswire.com/news-releases/new-survey--payday-borrowers-are-far-more-favorable-toward-and-informed-about-payday-loans-than-voters-without-payday-loan-experience-300235446.html"]

specialty retailers have gradually lightened their load of plastic to a few favorites – commonly including a bank card that could substitute for the other accounts.

Most of the products in this category can substitute for products in the other two. Consumers who qualify for any of the medium-term loans are likely to be sufficiently creditworthy to avail themselves of any of the options in the category as well as any of the short-term options FICO scores. Marketing makes it clear that banks and finance companies are competing across their sector boundary and offering consumers alternatives to credit-card debt. Comparative advertising is often an obvious indication of products that are likely substitutes for one another. As an example, one of the top online lenders makes an appeal to consumers with bank cards that leaves little doubt that an installment loan is an alternative to credit card balances:[172]

It is conceivable that a comparison of alternative sources of credit could determine that credit cards would not qualify as a market solely on the basis of consumer demand for loans. Nonetheless because bank cards have gained such a large share of consumer credit, it is useful to consider the competition just among credit cards. Different cards offer a wide variety of interest rates and other terms. Cards from credit unions routinely offer better rates. The industry makes hundreds of millions of offers a year, enticing consumers to try new cards with lower fees, lower interest rates, more bonuses, and other attractive features. Merchants still take advantage of the opportunity at checkout to offer charge accounts. Consumers routinely acquire new cards to pay off more expensive debts. Credit cards have, however, been found to constitute relevant markets for the payment services

[172] Rocket Loan Home Page, [HYPERLINK "https://www.rocketloans.com/"] Accessed on September 3, 2020.

they provide. One court held that Visa and MasterCard had restrained competition in those markets,[173] and the government secured an order designed to restore competition. After the judgment, the parties settled with the Department of Justice, which released this description:[174]

> Credit card acceptance costs U.S. merchants approximately $35 billion each year. Those costs are collected from merchants in the form of a "swipe fee" they pay every time a credit card is used.…Merchants pass on these billions of dollars in fees to all their consumers in the form of higher retail prices. By preventing merchants from rewarding consumers when they use less expensive credit cards to make a purchase, American Express, MasterCard and Visa have inhibited merchants' ability to reduce card acceptance costs, and therefore their retail prices to consumers.

The proposed settlement requires Visa and MasterCard to allow merchants to offer consumers discounts, rebates, or discounted products and services for using other networks, lower-cost cards, or other forms of payment. Numerous other provisions establish other incentives for competition to improve. If the order has served its purpose, these markets should become more competitive. The rise of rival payment systems since 2010 is an indication that competition in payment systems has emerged. However, it remains to be seen whether effective competition is the proper characterization for credit card markets.

Installment Loans

The National Installment Lenders Association stresses differences between installment, payday, and title loans – an indication of competition across the short-term and mid-term categories of credit:

[173] United States v. Visa USA, Inc., 163 F. Supp. 2d 322 (S.D.N.Y. 2001) ("The proof demonstrates that [Visa and Mastercard] do weaken competition and harm consumers by: (1) limiting output of [rival] cards in the United States; (2) restricting the competitive strength of [rivals] by restraining their merchant acceptance levels and their ability to develop and distribute new features such as smart cards; (3) effectively foreclosing [rivals] from competing to issue off-line debit cards…, and (4) depriving consumers of the ability to obtain credit cards [with] different qualities, characteristics, features, and reputations.); See also, **Ohio v. American Express, 585 US _ (2018)**

[174] Release, Justice Department Sues American Express, Mastercard and Visa to Eliminate Rules Restricting Price Competition; Reaches Settlement with Visa and Mastercard, October 4, 2010, [HYPERLINK "https://www.justice.gov/opa/pr/justice-department-sues-american-express-mastercard-and-visa-eliminate-rules-restricting"].

> These products are about as different as two products could be. [P]ayday companies do not test the ability to repay the loan from cash flow…loans are typically of two weeks or one month's duration, and are payable in one lump sum….Data on these loans is not accepted by any major credit bureau. By contrast, Traditional installment lenders do test the ability to repay, and the loans are payable in equal installments of principal and interest, giving the borrower a clear and manageable roadmap out of debt. Installment loans are reported to the credit bureaus, enabling responsible borrowers to build or repair their credit."[175]

Credit Karma – an information and search engine for credit services returns four companies with eleven options to an inquiry for a personal loan.[176] The APRs for a shopper (presumably anonymous and unscreened) ranged from 18% to over 30%. Clicking a link for a lender allows one to apply for a loan. The ease of searching for loans, comparing offers, and securing funds with an online session, at rates approximating credit card rates, is an indication of competition. But the group of interest today are those consumers somewhere in between, with weak credit and need some short-term cash.

That installment loans attract multiple FICO grades of borrowers and multiple sources of lenders suggests that they present alternatives for consumers considering many purposes. Characterized by one study as credit for the non-prime working classes, but better risks than payday borrowers, the business has grown dramatically. Non-prime borrowers owe an estimated $50 billion on installment loans, borrowed from lenders that have avoided the public opprobrium and regulatory backlash that hounded payday lenders.[177]

Long Term Products – Autos

This sector was found competitive by the Commission in 1970. Auto loans may qualify as a relevant market, given the combination of maturities and security. Car buyers may borrow funds from other sources, and mortgages have often served that purpose, but unsecured loans are likely to be significantly more expensive than a loan backed by the security of a lien on the vehicle. These loans can come from banks, credit unions, thrifts, manufacturers, and the dealers themselves (although auto dealers typically act as middlemen for other institutions that provide credit). Academic research reflects what is obvious from ubiquitous advertising – consumers have abundant choices for auto credit, and knowledge of options and prices is relatively high.

[175] [HYPERLINK "https://nilaonline.org/fundamentals/"] (internal notations deleted).
[176] [HYPERLINK "https://www.creditkarma.com/shop/personal-loans" \l "newloans"]
[177] Profile from Payments Journal, The Ugly Side of Lending: Online Installment Loans [HYPERLINK "https://www.paymentsjournal.com/the-ugly-side-of-lending-online-installment-loans/"]

Some studies that have focused on the effects of borrower qualifications and demand characteristics have found that opportunities for exploiting customers still exist in the personal negotiations that attend an automobile purchase. One study concluded that consumers are more sensitive to maturity and payment size than interest rates, which means that some end up paying more than others with similar qualifications.[178] A 2010 study of negotiations for auto loans found that search costs, incomplete information, and distaste for bargaining leave consumers worse off.[179] The authors estimated better informed consumers capture 15% of the average dealer margin from selling an automobile. Nonetheless a substantial group of consumers did not arm themselves with the information that would have saved them that money.

Personal Networks and Peer to Peer [probably not worth keeping]

Profile, "What Is Peer-to-Peer (P2P) Lending?"[180]

> It has only existed since 2005, but the crowd of competitors already includes Prosper, Lending Club, Peerform, Upstart, and StreetShares.
>
> First, an investor opens an account with the site and deposits a sum of money to be dispersed in loans. The loan applicant posts a financial profile that is assigned a risk category that determines the interest rate the applicant will pay. The loan applicant can review offers and accept one. (Some applicants break up their requests into chunks and accept multiple offers.) The money transfer and the monthly payments are handled through the platform. The process can be entirely automated, or lenders and borrowers can choose to haggle.
>
> Some sites specialize in particular types of borrowers. StreetShares, for example, is designed for small businesses. And Lending Club has a "Patient Solutions" category that links doctors who offer financing programs with prospective patients.
>
> The rates for applicants with good credit are often lower than comparable bank rates, while rates for applicants with sketchy credit records may go much higher. LendingTree.com, for example, offered

[178] Bronson Argyle, Taylor Nadauld, Christopher Palmer, Monthly Payment Targeting and the Demand for Maturity, NBER Working Paper No. w25668 19 Mar 2019 MIT Sloan; National Bureau of Economic Research (NBER)

[179] i. Economics of Auto Loans – Scott Morton, F., Silva-Risso, J. & Zettelmeyer, F. What Matters in a Price Negotiation: Evidence From the U.S. Auto Retailing Industry. Quant Mark Econ (2011) 9: 365. doi:10.1007/s11129-011-9108-1, available at [HYPERLINK "https://link.springer.com/article/10.1007/s11129-011-9108-1"]

[180] Peer-to-Peer (P2P) Lending By JULIA KAGAN, Reviewed By THOMAS J. CATALANO, May 11, 2020 What Is Peer-to-Peer (P2P) Lending?

personal loan rates from 10.19% to 24.98% as of December 2019.1 Peerform posted loan rates at a range of 5.99% to 29.99% as of February 2020.2 The average credit card interest rate was 17.30% as of Feb. 5, 2020, according to CreditCards.com.

Information – Credit Ratings

Writing when computers and data storage were expensive, primitive and rare, the NCCF worried that credit information providers might need to be regulated as public utilities.[181] Advances in data processing and reductions in the cost of data have allowed competition to survive in the sector. However, the performance of the sector has fared poorly in government reviews. The national credit reporting agencies have sued FICO and alleged that it has excluded them from competing for its lucrative services. Whether its performance could be enhanced by competition remains worth exploring.

Concentration at monopoly levels, allegations about exclusionary conduct by the dominant provider, and regulatory actions that impeded entry contribute to significant concerns about competition in this sector. Fannie Mae, Freddie Mac, and CFPB have favored the dominant supplier. Until recently a prerequisite for selling a loan to a Government Sponsored Entities was a FICO score. Numerous companies offer ratings, and the products have been purchased by consumer-information providers, but none have gained significant market share. The most likely entrants, the National Credit Reporting Agencies, were sued by the CFPB for emulating FICO and advertising (allegedly deceptively) their competing products.

The dominant provider of credit ratings, FICO, was used in 90% of transactions.[182] It cites a release from the Mercator Advisory Group,[183] which reported:

> New research from Mercator Advisory Group has found that in the United States, FICO® Scores were in 2016 used in more than 90% of lending decisions,

---

[181] It appears to the Commission that in the long run the credit reporting industry has the ingredients of a public utility. It is as uneconomical to have three credit bureaus in town as it is to have three telephone companies. The necessity for accurate and comprehensive credit data, tile technology, the mobility of the population, and the emergence of the multiparty credit card · all argue for a single credit reporting agency for each metropolitan area linked with similar agencies throughout tile nation. But it is surely not in the public interest to grant a monopoly to one credit reporting agency without both regulating its freedom to set prices and requiring that it provide open access to its store of credit information to all credit grantors. Open access is vital, since any creditor denied entry to tile credit information system must either charge exorbitant rates to cover his risk or severely limit the granting of credit." Report at 213.

[182] (RMR, CONSUMER REPORTING MARKET PROFILE, 7/15/19 @1)

[183] Although not clear, the study appears to be sponsored by FICO [HYPERLINK "https://www.mercatoradvisorygroup.com/Press_Releases/FICO%C2%AE_Scores_Used_in_Over_90__of_Lending_Decisions_According_to_New_Study/"] (emphasis added)

including credit cards, mortgages, and automobile financing. In addition, Mercator performed a study of the frequency in 2016 and 2017 of FICO Score usage in the securitization process for U.S. asset-backed securities (ABS) backed by automobile leases, credit cards, prime auto loans, and subprime auto loans. *The study found that ABS securitizations in those four verticals almost universally cite the FICO Score.*

According a recent report, "The Justice Department has opened an antitrust investigation into Fair Isaac Corp., the financial company whose credit scores underlie nearly all U.S. consumer credit decisions….The probe follows years of complaints from rivals about Fair Isaac's dominance, and comes amid efforts by Congress and financial regulators to inject more competition into the credit score market."[184] Since then, the major credit bureaus have formalized their complaints in an antitrust lawsuit against FICO.[185]

Entry into the credit rating business has been hampered by government actions. The CFPB sued the major credit reporting agencies for advertising alternatives to FICO ratings, alleging that the comparisons to FICO were deceptive.[186] Not mentioned in the actions was CFPB analysis of credit reports showed high correlations, perhaps insignificant variations among competing reports, or the numerous iterations of the FICO ratings, which come in variations tailored for particular uses and change on a continuous basis. More recently, Fannie and Freddie have softened their resistance to ratings from FICO competitors.

Deposits and payments

For much of the twenty-first century, competition policy makers have examined competition in payment systems and expressed concern that the markets have not kept up with the demands of consumers in a world that has experienced a technological revolution. The OECD, for example, published the results of a 2012 roundtable on competition and payment systems.[187] The overview of the proceedings described an assembly of competition experts and agency heads that was unimpressed with the sector and uncertain how to proceed:

---

184 [HYPERLINK "https://www.politico.com/news/2020/03/13/justice-fair-isaac-antitrust-129204"]
185 [HYPERLINK "https://www.cutimes.com/2020/05/12/credit-unions-sue-fico-for-alleged-antitrust-violations/?slreturn=20201015230658" \l ":~:text=Three%20credit%20unions%20are%20suing%20the%20Fair%20Isaac,which%20harmed%20businesses%20and%20led%20to%20higher%20prices"].
186 See, Release, CFPB Orders TransUnion and Equifax to Pay for Deceiving Consumers in Marketing Credit Scores and Credit Products / Credit Reporting Companies Misstated the Cost and Usefulness of the Credit Scores and Products They Sold, Lured Consumers into Costly Recurring Payments (Jan 03, 2017).
187 OECD Policy Roundtables / Competition and Payment Systems (2012) available at [HYPERLINK "http://www.oecd.org/competition/PaymentSystems2012.pdf"]

> The ongoing shift from cash and paper towards electronic payment systems potentially brings large economic benefits. But card payments in particular have remained expensive for merchants, and regulation may have unintended consequences. There is no consensus among economists and policymakers on what constitutes an efficient fee structure for card-based payments, and it is not clear if payment competition might do the trick. Regulation should be geared towards removing barriers of entry in payment markets and banning merchant (pricing) restrictions. The discussion reviewed recent countries' experiences on developments regarding all non-paper based forms of payment such as debit and credit cards, and E-payments (through internet, mobile phones etc.). Many members are investigating these markets, and EU jurisdictions are implementing the EU payments service directive, which aims to provide a single market for payments.

Eight years later, there are signs of progress, but unusual stability remains in the purchase patterns of bank deposits. Meanwhile a history of failed attempts to offer various banking services bodes ill for imminent improvement. The proportion of the population without a bank account remains significant. Payments are still dominated by bank cards. Whether these characteristics stem from indifference on the part of consumers or barriers to competition in the banking sector is worth examination.

Consumer banking services have attracted interest from some of the world's largest companies. According to Business Insider, "Google is planning to break into banking with new checking account offerings"[188]

> "…We think legacy banks are unlikely to feel the sting from Google in these early days — and that Google's bank partners will likely stand to benefit from the tie-up. Incumbent banks have huge customer bases and a wealth of expertise in navigating the regulatory complexities of the banking sector, which big tech companies like Google lack — hence its partnerships with incumbents."

Google could face formidable barriers. Walmart has been trying without success, to enter the banking for years. In the 1990s, it tried to become a thrift holding company, which would have allowed it to open in thousands of American stores. The Bank Holding Company Act imposed restrictions on companies engaged in nonbank businesses from owning banking subsidiaries, but the option for Walmart to own a subsidiary operating a thrift had a venerable tradition; it was the model that Ford Motor Company, Household International, and Sears Roebuck had used to offer financial services their customers. Before Walmart could execute the plan, Congress passed the Gramm-Leach-Bliley Act of 1999, blocking the move. A decade later, Walmart tried again, taking advantage of

[188] Gregory Magana (Nov 14, 2019), [HYPERLINK "https://www.businessinsider.com/google-will-begin-offering-checking-accounts-2019-11"]

another innovation from the early twentieth century. It obtained a charter to operate an industrial loan company (the institutions that specialized in blue collar customers). Those charters allowed a commercial to own a financial institution that could take deposits and make loans. This time the FDIC blocked the move by denying Walmart deposit insurance, the application for which was "fiercely opposed" by bank lobbies.[189] Walmart withdrew its application in 2007. Any prospect of reconsideration, for Walmart or another company like it, was suspended in 2010, when Dodd-Frank imposed a three-year moratorium on deposit insurance for any new industrial loan company.

Walmart offers a variety of financial services, but as of 2014, they are not interchangeable with the bundle of services available at a typical bank. Consumer Reports compared Walmart's effort to a bank and preferred the traditional version.[190] Walmart's four thousand stores, which serve customers who are more likely to be unbanked or underbanked, and which serve communities where banks are more likely to be scarce, have not been able to surmount the barriers to entry that competitors have persuaded regulators to build around their business. In light of the evidence that branch banks bring valuable benefits to underserved areas and populations, the costs of these barriers are likely significant.

Conclusions & Recommendations

The preliminary conclusions from the foregoing review of competitive conditions today are consistent with those described in the NCCF Report and with observations from historians who have studied the credit sector throughout its development. The most important ingredient of competition – ease of entry – remains essentially free of intrinsic impediments in credit markets. The number of suppliers available to serve consumers' demand for credit, across a wide variety of credit products and services, far exceeds levels considered adequate for robust competition. There appears to be no natural barrier to competition in lending.

Nonetheless, some sectors display worrisome symptoms of competitive impairments. Two sectors stand out. The first is the supply of small loans to borrowers with below-average credit qualifications – populations that are disproportionately poor, unbanked, and in great need. Consumers in this sector often resort to inferior options, because better options have been restricted or eliminated by regulation. The second sector is the supply of information, particularly credit ratings and credit reports. That competition among

[189] See, Lawrence J. White, "Walmart and Banking: It's Time to Reconsider," *Money and Banking* (May 15, 2017), available at [HYPERLINK "https://www.moneyandbanking.com/commentary/2017/5/13/walmart-and-banking-its-time-to-reconsider"].

[190] Should Walmart be your next bank? November 2014 ("Attention, shoppers: The retail giant now offers bank-by-smart-phone mobile checking accounts") [HYPERLINK "https://www.consumerreports.org/cro/magazine/2014/11/should-walmart-be-your-bank/index.htm"].

information providers to the sector might be less than robust is ironic, given the rapid advances in information technology over the last fifty years. Information is plentiful and cheap. Monopoly power in this sector would be especially disquieting given that information undergirds virtually all credit transactions. Information that is more expensive, more restricted, or less accurate is likely to raise the cost and reduce the availability of loans in most product categories to consumers in many socio-economic situations.

The impediments to competition in credit markets are not unique to the sector. Nor is the source of the problems. To the contrary, it is commonplace in antitrust experience. Providers of credit have combined with regulatory authorities to create barriers around market niches in which a privileged few can insulate themselves from competition. Sometimes exclusionary behavior suffices to deter rivals. Sometimes insulation comes in the of standards for an industry or society. Many barriers become ossified in the amber of laws and regulations. Enforceable interest rate caps, licensing restrictions, territorial and product limitations, and outright prohibitions of competition are frequent manifestations of these barriers.

Redacted

With respect to finance companies, the NCCF made a recommendation that could apply in many areas:

> The effect of the present fractionalized legislation and regulation upon consumers should be reviewed as well as the progress of efforts to enact state consumer credit legislation. Enactment of consumer credit legislation of the type recommended in this report…should be also reviewed to determine whether any added amendments inhibit the basic aim of ensuring free entry of firms and fair treatment of all consumers. Should this research demonstrate that the states are not fostering an environment in which consumers have access to a wide variety of competitive financial services, that progress of consumer credit legislation at the state level is too slow, and that overall Federal legislation is deemed infeasible, then the Commission recommends that Congress undertake Federal chartering of finance companies in a manner, designed to remedy these deficiencies in the market for consumer credit.

Fifty years later, Clark and Zywicki found in the CFPB a potential fulfillment of the Commission's prescription:

> The creation of the CFPB as a consolidated national regulator of consumer credit products provides a historic opportunity to establish a more coherent regulatory framework that can integrate enforcement, supervision, regulation, and research tools into one regulatory agency.

Two and a half centuries of economic scholarship have refined the definitions and explanations of competition, but the fundamental descriptions remain much the same as they did when Smith first articulated them and when Samuelson's text taught them to a generation of students. Effective competition drives prices down to the costs of providing goods and services. The same principle applies to markets where consumers shop, markets where retailers go to buy supplies, and markets where companies go to procure resources. In other words, competition puts pressure on sellers up and down the stream of commerce to find the best deal they can get and to offer the best deal they can give. It is, as the Commission noted, painful for the participants on the selling side. But it is beneficial to everyone on the buying side. Fortunately for consumers, including consumers of financial services, they are the buyers who benefit from competition.

Appendix A

I. Summary of Statutory References to Competition and Efficiency

- The DFA mentions "competition" in four places:
    - Section 1021(a) (12 U.S.C. § 5511(a))—identifying the Bureau's statutory purposes, including to ensure "that markets for consumer financial products and services are fair, transparent, and competitive."
    - Section 1021(b)(4) (12 U.S.C. § 5511(b)(4))—identifying five objectives for which the Bureau may exercise its authorities, including to ensure that "Federal consumer financial law is enforced consistently, without regard to the status of a person as a depository institution, in order to promote fair competition."
    - Section 1031(c) (12 U.S.C. § 5531(c))—stating that the Bureau may not declare an act or practice to be unfair unless it has a reasonable basis to conclude that the act or practice causes or is likely to cause substantial injury and that "such substantial injury is not outweighed by countervailing benefits to consumers or to competition."
    - Section 1100(f)(2) (12 U.S.C. § 5107(f)(2))—identifying factors that the Bureau must consider when promulgating rules to implement the SAFE Act, including "the need to ensure a competitive origination market that maximizes consumer access to affordable and sustainable mortgage loans."
- The DFA mentions "efficient" markets, regulations, or enforcement in three places:
    - Section 1021(b)(5) (12 U.S.C. § 5511(b)(5))—identifying five objectives for which the Bureau may exercise its authorities, including to ensure that "markets for consumer financial products and services operate transparently and efficiently to facilitate access and innovation."
    - Section 1013(c) (12 U.S.C. § 5493(c))—identifying the functions of the Bureau's Office of Fair Lending and Equal Opportunity, which include "coordinating fair lending efforts of the Bureau with other Federal agencies and State regulators, as appropriate, to promote consistent, efficient, and effective enforcement of Federal fair lending laws."
    - Section 1013(g)(3)(E) (12 U.S.C. § 5493(g)(3)(E))—identifying the duties of the Bureau's Office of Financial Protection for Older Americans, including to "coordinate consumer protection efforts of seniors with other Federal agencies

and State regulators, as appropriate, to promote consistent, effective, and efficient enforcement."

- At least three of the eighteen enumerated consumer laws identify ensuring competition or efficiency as among their purposes:
    - FCRA section 602(a)(1)) (15 U.S.C. § 1681(a)(1))—listing Congressional findings, including that, "Inaccurate credit reports directly impair the efficiency of the banking system."
    - FDCPA section 802(e) (15 U.S.C. § 1692(e))—identifying the FDCPA's purposes, including "to insure that those debt collectors who refrain from using abusive debt collection practices are not competitively disadvantaged."
    - TILA section 102(a) (15 U.S.C. § 1601(a))—listing Congressional findings, including that, "The Congress finds that economic stabilization would be enhanced and the competition among the various financial institutions and other firms engaged in the extension of consumer credit would be strengthened by the informed use of credit."
- By comparison, the FTC Act explicitly prohibits unfair methods of competition:
    - Section 5 (15 U.S.C. § 45)—prohibiting unfair methods of competition and empowering and directing the FTC to prevent persons from using unfair methods of competition.

II. Statutory Text

- Below are the relevant statutory provisions from the Dodd-Frank Act, FCRA, FDCPA, TILA, and FTC Act.
- References to competition are highlighted in yellow.
- References to efficiency are highlighted in blue.

Dodd-Frank Act

DFA section 1021 (12 U.S.C. § 5511). Purpose, objectives, and functions.

(a) Purpose. The Bureau shall seek to implement and, where applicable, enforce Federal consumer financial law consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive.

(b) Objectives. The Bureau is authorized to exercise its authorities under Federal consumer financial law for the purposes of ensuring that, with respect to consumer financial products and services—

(1) consumers are provided with timely and understandable information to make responsible decisions about financial transactions;

(2) consumers are protected from unfair, deceptive, or abusive acts and practices and from discrimination;

(3) outdated, unnecessary, or unduly burdensome regulations are regularly identified and addressed in order to reduce unwarranted regulatory burdens;

(4) Federal consumer financial law is enforced consistently, without regard to the status of a person as a depository institution, in order to promote fair competition; and

(5) markets for consumer financial products and services operate transparently and efficiently to facilitate access and innovation.

DFA section 1031(c) (12 USC 5531(c)). Prohibiting unfair, deceptive, or abusive acts or practices.

. . .

(c) Unfairness.—

(1) In General. The Bureau shall have no authority under this section to declare an act or practice in connection with a transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service, to be unlawful on the grounds that such act or practice is unfair, unless the Bureau has a reasonable basis to conclude that—

(A) the act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers; and

(B) such substantial injury is not outweighed by countervailing benefits to consumers or to competition.

(2) Consideration of Public Policies. In determining whether an act or practice is unfair, the Bureau may consider established public policies as evidence to be considered with all other evidence. Such public policy considerations may not serve as a primary basis for such determination.

DFA section 1100 (12 U.S.C. § 5107). Bureau of Consumer Financial Protection backup authority to establish loan originator licensing system.

. . .

(f) Regulation Authority.—

(1) In General. The Bureau is authorized to promulgate regulations setting minimum net worth or surety bond requirements for residential mortgage loan originators and minimum requirements for recovery funds paid into by loan originators.

(2) Considerations. In issuing regulations under paragraph (1), the Bureau shall take into account the need to provide originators adequate incentives to originate affordable and sustainable mortgage loans, as well as the need to ensure a competitive origination market that maximizes consumer access to affordable and sustainable mortgage loans.

DFA section 1013 (12 U.S.C. § 5493). Administration.

. . .

(c) Office of Fair Lending and Equal Opportunity.—

(1) Establishment. The Director shall establish within the Bureau the Office of Fair Lending and Equal Opportunity.

(2) Functions. The Office of Fair Lending and Equal Opportunity shall have such powers and duties as the Director may delegate to the Office, including—

(A) providing oversight and enforcement of Federal laws intended to ensure the fair, equitable, and nondiscriminatory access to credit for both individuals and communities that are enforced by the Bureau, including the Equal Credit Opportunity Act and the Home Mortgage Disclosure Act;

(B) coordinating fair lending efforts of the Bureau with other Federal agencies and State regulators, as appropriate, to promote consistent, efficient, and effective enforcement of Federal fair lending laws;

(C) working with private industry, fair lending, civil rights, consumer and community advocates on the promotion of fair lending compliance and education; and

(D) providing annual reports to Congress on the efforts of the Bureau to fulfill its fair lending mandate.

. . .

(g) Office of Financial Protection for Older Americans.—

. . .

(3) Duties. The Office shall—

(A) develop goals for programs that provide seniors financial literacy and counseling, including programs that—

(i) help seniors recognize warning signs of unfair, deceptive, or abusive practices, protect themselves from such practices;

(ii) provide one-on-one financial counseling on issues including long-term savings and later-life economic security; and

(iii) provide personal consumer credit advocacy to respond to consumer problems caused by unfair, deceptive, or abusive practices;

(B) monitor certifications or designations of financial advisors who advise seniors and alert the Commission and State regulators of certifications or designations that are identified as unfair, deceptive, or abusive;

(C) not later than 18 months after the date of the establishment of the Office, submit to Congress and the Commission any legislative and regulatory recommendations on the best practices for—

(i) disseminating information regarding the legitimacy of certifications of financial advisers who advise seniors;

(ii) methods in which a senior can identify the financial advisor most appropriate for the senior's needs; and

(iii) methods in which a senior can verify a financial advisor's credentials;

(D) conduct research to identify best practices and effective methods, tools, technology and strategies to educate and counsel seniors about personal finance management with a focus on—

(i) protecting themselves from unfair, deceptive, and abusive practices;

(ii) long-term savings; and

(iii) planning for retirement and long-term care;

(E) coordinate consumer protection efforts of seniors with other Federal agencies and State regulators, as appropriate, to promote consistent, effective, and efficient enforcement; and

(F) work with community organizations, non-profit organizations, and other entities that are involved with educating or assisting seniors (including the National Education and Resource Center on Women and Retirement Planning).

Fair Credit Reporting Act

FCRA section 602 (15 U.S.C. § 1681). Congressional findings and statement of purpose.

(a) Accuracy and fairness of credit reporting. The Congress makes the following findings:

(1) The banking system is dependent upon fair and accurate credit reporting. Inaccurate credit reports directly impair the efficiency of the banking system, and unfair credit reporting methods undermine the public confidence which is essential to the continued functioning of the banking system.

(2) An elaborate mechanism has been developed for investigating and evaluating the credit worthiness, credit standing, credit capacity, character, and general reputation of consumers.

(3) Consumer reporting agencies have assumed a vital role in assembling and evaluating consumer credit and other information on consumers.

(4) There is a need to insure that consumer reporting agencies exercise their grave responsibilities with fairness, impartiality, and a respect for the consumer's right to privacy.

<u>Fair Debt Collection Practices Act</u>

FDCPA section 802 (15 U.S.C. § 1692). Congressional findings and declaration of purpose.

(a) Abusive practices. There is abundant evidence of the use of abusive, deceptive, and unfair debt collection practices by many debt collectors. Abusive debt collection practices contribute to the number of personal bankruptcies, to marital instability, to the loss of jobs, and to invasions of individual privacy.

(b) Inadequacy of laws. Existing laws and procedures for redressing these injuries are inadequate to protect consumers.

(c) Available non-abusive collection methods. Means other than misrepresentation or other abusive debt collection practices are available for the effective collection of debts.

(d) Interstate commerce. Abusive debt collection practices are carried on to a substantial extent in interstate commerce and through means and instrumentalities of such commerce. Even where abusive debt collection practices are purely intrastate in character, they nevertheless directly affect interstate commerce.

(e) Purposes. It is the purpose of this subchapter to eliminate abusive debt collection practices by debt collectors, to insure that those debt collectors who refrain from using abusive debt collection practices are not competitively disadvantaged, and to promote consistent State action to protect consumers against debt collection abuses.

<u>Truth In Lending Act</u>

TILA section 102 (15 U.S.C. § 1601). Congressional findings and declaration of purpose.

(a) Informed use of credit. The Congress finds that economic stabilization would be enhanced and the competition among the various financial institutions and other firms engaged in the extension of consumer credit would be strengthened by the informed use of credit. The informed use of credit results from an awareness of the cost thereof by consumers. It is the purpose of this subchapter to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit, and to protect the consumer against inaccurate and unfair credit billing and credit card practices.

(b) Terms of personal property leases. The Congress also finds that there has been a recent trend toward leasing automobiles and other durable goods for consumer use as an alternative to installment credit sales and that these leases have been offered without adequate cost disclosures. It is the purpose of this subchapter to assure a meaningful disclosure of the terms of leases of personal property for personal, family, or household purposes so as to enable the lessee to compare more readily the various lease terms available to him, limit balloon payments in consumer leasing, enable comparison of lease terms with credit terms where appropriate, and to assure meaningful and accurate disclosures of lease terms in advertisements.

<u>Federal Trade Commission Act</u>

FTC Act section 5 (15 U.S.C. § 45). Unfair methods of competition unlawful; prevention by Commission.

(a) Declaration of unlawfulness; power to prohibit unfair practices; inapplicability to foreign trade.

(1) Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful.

(2) The Commission is hereby empowered and directed to prevent persons, partnerships, or corporations, except banks, savings and loan institutions described in section 57a(f)(3) of this title, Federal credit unions described in section 57a(f)(4) of this title, common carriers subject to the Acts to regulate commerce, air carriers and foreign air carriers subject to part A of subtitle VII of Title 49, and persons, partnerships, or corporations insofar as they are subject to the Packers and Stockyards Act, 1921, as amended [7 U.S.C. § 181 et seq.], except as provided in section 406(b) of said Act [7 U.S.C. § 227(b)], from using unfair methods of competition in or affecting commerce and unfair or deceptive acts or practices in or affecting commerce.

(3) This subsection shall not apply to unfair methods of competition involving commerce with foreign nations (other than import commerce) unless—

(A) such methods of competition have a direct, substantial, and reasonably foreseeable effect—

(i) on commerce which is not commerce with foreign nations, or on import commerce with foreign nations; or

(ii) on export commerce with foreign nations, of a person engaged in such commerce in the United States; and

(B) such effect gives rise to a claim under the provisions of this subsection, other than this paragraph.

If this subsection applies to such methods of competition only because of the operation of subparagraph (A)(ii), this subsection shall apply to such conduct only for injury to export business in the United States.

(4)—

(A) For purposes of subsection (a) of this section, the term "unfair or deceptive acts or practices" includes such acts or practices involving foreign commerce that--

(i) cause or are likely to cause reasonably foreseeable injury within the United States; or

(ii) involve material conduct occurring within the United States.

(B) All remedies available to the Commission with respect to unfair and deceptive acts or practices shall be available for acts and practices described in this paragraph, including restitution to domestic or foreign victims.

* * *

<u>Appendix B</u>

<u>[History of Credit and Competition]</u>

Outtakes

Background:

RMR, AUTO FINANCE MARKET PROFILE (7/1/19)

Auto finance is the third largest source of consumer debt after mortgage and student lending.[191]
• Total outstanding balances as of Q2 2018: $1.25T
• Total number of outstanding accounts as of Q2 2018: 88M
• Total number of new accounts/year: 29.2M from Q3 2017 – Q2 2018
  o Most consumers finance vehicle purchases: 86.1% of new vehicles and 54.7% of
  used vehicles were financed in Q2 2018.
  o In Q2 2018, approximately 56% of new accounts were for prime or super prime consumers, approximately 20% were for near prime consumers, and approximately 24% were for subprime or deep subprime consumers.
• Delinquencies: 2.06% of loans balances were 30-59 days delinquent and 0.61% of loan balances were 60-89 days delinquent in Q2 2018.

<u>Market Structure</u>

• Market share by financial institution type:[192]
  o Banks– 31.6%
  o Captives (manufacturers' finance companies) – 29.0%
  o Credit Unions – 21.3%
  o Finance Companies – 11.1%
  o Buy-Here-Pay-Here – 6.9%
    Delinquencies were at low levels

2% @ 30, .67% @ 60)

Long Term Products – Mortgage lenders and servicers

[Revisions awaiting research and decisions on scope] Concentration in these markets appears to be low, and entry appears to have been significant, which suggest that competition is working. How vigorously they compete is another question. Providers are heavily influenced by two major buyers of mortgage dept – Fannie Mae and Freddie Mac. Numerous requirements have made these transactions quite complicated and opaque to consumers. Ironically, some of the requirements are

[191] Citing Experian–Oliver Wyman Market Intelligence Report 2018 Q2 and Experian State of Automotive Finance Market 2018 Q2.
[192] Citing 2018 Q2 Experian State of Automotive Finance Market Report

intended to have the opposite effect. The costs and benefits of these requirements are addressed elsewhere; here the inquiry will focus on whether competition in these products is effective, and whether it can be improved by clarifying the information material to consumers.

RMR, MORTGAGE MARKET PROFILE (9/3/19)

99% of post 2010 loans are current[193]

The sector is not concentrated, with a 10-firm Concentration Ratio of 40%. Nondepository institutions have 60% of market.[194]

Search engines return scores of results.[195]

CFPB, *2013 RESPA Servicing Rule Assessment Report* (2019), [HYPERLINK "https://files.consumerfinance.gov/f/documents/cfpb_mortgage-servicing-rule-assessment_report.pdf"].

Trends in delinquencies and foreclosures 2003-2017 (pp. 38-40) E.g., percentage of loans that became newly 90+ days delinquent rose from 0.5% at end of 2006 to 2% at end of 2008, but the percentage has since returned to pre-crisis levels.

Other Servicing Marketing Trends (pp. 54-56). Non-depository institutions have increased their share of servicing market and are 6 of the 10 largest services as of 2017, while some large banks have reduced their servicing portfolios in the last few years. Largest 15 services increased their market share in 2007 and 2008, but it has since declined to roughly pre-crisis levels.

Effects of the Rule on Servicing Costs (pp. 100-111). [DHH: this section seems less helpful for our purposes because of data limitations.]

---

[193] RMR cites CreditForecast.com. We'll need to update this statistic in light of Covid-19.
[194] RMR cites (i) Inside Mortgage Finance, Top 100 Lenders 2018 [Subscription-only; (ii) Urban Institute, Housing Finance at a Glance: A Monthly Chartbook (June 2019), [HYPERLINK "https://www.urban.org/sites/default/files/publication/100454/june_chartbook_2019.pdf"].
[195] [HYPERLINK "https://www.consumersadvocate.org/mortgage-rates/a/best-mortgage-rates?v=v3&gclid=EAIaIQobChMI29OE1s6C6gIV18DICh0aXwl-EAMYASAAEgL5EPD_BwE&gca_loc_physical_ms=9061285&gca_loc_interest_ms=&gca_adposition=&gca_device=m&gca_network=g&gca_matchtype=p&gca_adgroupid=19322516942&gca_campaignid=418554902&keyword=mortgage&pd=true"]

CFPB, *ATR/QM Assessment Report* (2019), [HYPERLINK "https://files.consumerfinance.gov/f/documents/cfpb_ability-to-repay-qualified-mortgage_assessment-report.pdf"].

Mortgage Market Pre- and Post-Rule (pp. 69-79). Discusses changes in pricing and costs of different types of loans. Also concludes generally that: "While the above reported trends clearly establish that the revenues and expenses associated with originating mortgage loans have increased over the past decade, it is uncertain whether the increase or some part of it was caused by the ATR/QM Rule." (p. 79)

Effects of the General QM DTI Limit on Loan Performance (pp. 106-115). "Overall, the Rule appears to have reduced the share of mortgages originated with DTI over 43 percent, while potentially increasing the share originated with DTIs at or just below 43 percent. These patterns are studied in more detail in Chapter 5. Further, both above and below the DTI threshold of 43 percent, the improvement in performance of non-GSE loans relative to GSE loans provides some evidence that those loans that continue to be made under the General QM, other non-Temporary GSE QM, or non-QM ATR guidelines are underwritten in a way that reflects consumers' ability to repay." (p. 115)

Effects of the Rule on Access to Mortgage Credit and Cost of Credit (pp. 116-187). See in particular summary of findings on pp. 117-118.

Student Loans

[Revisions pending further research] – a sector where competition has been displaced almost entirely by government supply, the student loan business raises great controversy. Would it perform better if competitive?

RMR – Segment is Dominated by DOE – 92% (RMR 9/5/19)[196]

91+ day delinquencies 8-10% (Id.)

CFPB & DOE, *Private Student Loans* (2012) (report to Congress)[197]

[196] Three RMR research papers (Id. @ n. 4,5) [RMR cited New York Fed data; check updated figures.]
[197] [HYPERLINK "https://files.consumerfinance.gov/f/201207_cfpb_Reports_Private-Student-Loans.pdf"].

This Report has a wealth of information. E.g., data on market shares and the types of institutions that extend private student loans, borrower demographics (e.g., school-type, race), and repayment and delinquency rates, as well as a discussion of consumer protection concerns and potential solutions. The information is dated, as the report is from 2012.

CFPB, *Data Point: Final Student Loan Payments and Broader Household Borrowing* (2018)[198]

94% of borrowers repay student loans early, often with a large lump sum payment. Median lump sum payment equal to 55 times the monthly payment (implying that borrower pays off loan at least 55 months early) (p. 4)

Of 6% who repay student loans on schedule, large share put money formerly allocated to repaying student loans to repaying other debts (e.g., to another student loans or to cred card debt) (p. 4)

CFPB, *Data Point: Student Loan Repayment* (2017) [199]

This article analyzes how consumers are replaying student loans over time. It finds that, controlling for amount, consumers repay student loans at the same rate throughout the 14-year observation period. But consumers now how larger loan balances, so repayment takes longer and may be constraining consumers' ability to access other credit products. In addition, a growing share of borrowers (23%) are not making payments sufficient to reduce their balances.

[198] [HYPERLINK "https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/bcfp_data-point_final-student-loan-payments-household-borrowing.pdf"].
[199] [HYPERLINK "https://files.consumerfinance.gov/f/documents/201708_cfpb_data-point_student-loan-repayment.pdf"]