Encourage Credit Access Innovation

The abuses of the subprime crisis have made it all too easy to overlook the myriad benefits of consumer credit. Innovations in mortgages, credit cards, and unsecured loans such as payday advances have made it possible for more people to borrow money they need for a variety of purposes—from starting a business to advancing one's education. In the mid-1990s, a college student named Sergey Brin used personal credit cards to start the search engine business that would become Google.

In 2007, Austan Goolsbee, now a top economic adviser to President Barack Obama, warned in *The New York Times* that, "regulators should be mindful of the potential downside in tightening too much." Such restrictions, he wrote, would hurt "someone with a low income now but who stands to earn much more in the future" with the help of access to credit.

The Obama administration and Congress have seemingly ignored this advice. The Credit Card Accountability, Responsibility and Disclosure (CARD) Act of 2009 limits card issuers' ability to raise rates and impose penalty fees on high-risk borrowers. It has limited overall credit—working against other policies aimed at getting credit flowing—and caused overall rates to rise sharply for responsible card holders who pay on time or who pay their entire balance. Rules issued by the new Consumer Financial Protection Bureau (CFPB) will likely have the similar effect of punishing the prudent with more costly credit as a result of paternalistically protecting the imprudent.

Government certainly has a role in preventing fraudulent lending practices, but it should leave payment terms and interest rates up to the interested parties to negotiate. It should also reduce the paperwork burden of traditional lending institutions that raises costs that are passed on to borrowers. It should lift the cap on business lending by credit unions and lift the moratorium on retailer-affiliated industrial lending companies to spur competition among credit providers. Congress should:

- **Reject attempts to put interest rate or price controls on credit vehicles.** Repeal most of the CARD Act and prevent the CFPB from imposing nanny-state prohibitions on innovative credit products.
- **Repeal or scale back a variety of regulations that impose myriad paperwork requirements on financial institutions**. Such regulations—from Sarbanes-Oxley provisions to the Internet gambling ban—indirectly make services more expensive to borrowers and depositors at all income levels by adding to their overall costs. These rules hit small community banks and credit unions especially hard.

- **Reduce "know your customer" requirements on banks and other financial institutions to investigate their customers' backgrounds**. These rules often overwhelm law enforcement with useless reports and have adverse impacts on the low-income "unbanked" population by making it more difficult to open a bank account.
- **Lift the cap on lending that credit unions can make to member businesses**. The cap currently stands at just 12.25 percent of a credit union's assets, keeping these institutions from competing to serve the small business lending market. The cap has only been in place since 1998, and no such cap exist for other types of loans, such as mortgages and car loans. From a safety and soundness perspective, there is nothing about business lending that is inherently more dangerous than other loans.
- **Lift the moratorium on nonfinancial businesses forming limited-purpose banks, known as Industrial Lending Companies (ILCs).** This moratorium, first imposed by the Federal Deposit Insurance Corporation and then codified for two years by the Dodd-Frank Act, has led some of the nation's most well managed firms—including Wal-Mart, Home Depot, and Berkshire Hathaway—to shelve plans to form ILCs to offer financial services to their customers. Consumers suffer from this lack of competition in the banking sector. It is laughable to argue that somehow these banks pose an inherent risk, given the risks that practices of traditional banks posed during the financial crisis.

John Berlau