

## Testimony of John Berlau, Senior Fellow, Competitive Enterprise Institute

### Before the House Financial Services Committee, Subcommittee on Consumer Protection and Financial Institutions

#### Hearing: “Banking the Unbanked: Exploring Private and Public Efforts to Expand Access to the Financial System”

July 21, 2021

Chairman Perlmutter, Ranking Member Luetkemeyer, and honorable members of this Subcommittee, thank you for this opportunity to present testimony on behalf of my organization, the Competitive Enterprise Institute (CEI), at this hearing on the vital topic of financial inclusion.

CEI is a Washington-based free-market public policy organization, founded in 1984, that studies the effects of regulations on job growth and economic well-being. Our mission is to advance the freedom to prosper for consumers, entrepreneurs, and investors.

At CEI, we have long championed private-sector innovation that promotes financial inclusion and warned about government red tape that contributes to the problem of the unbanked. We sounded the alarm about Dodd-Frank Section 1075, also known as the “Durbin Amendment,” that transferred through price controls much of the cost of processing debit cards from retailers – including very large retail chains -- to some of the nation’s poorest consumers. We pointed out that largely as a result of this measure in the 2010 law, the percentage of free non-interest checking accounts as measured by the financial publication Bankrate slid from 76 percent in 2009 to just 39 percent in 2012.<sup>1</sup> Later, a study by George Mason University law professor Todd Zywicki and Geoffrey A. Manne and Julian Morris of the International Center for Law and Economics found that the Durbin Amendment contributed to more than 1 million Americans becoming unbanked.<sup>2</sup>

In the last few years, there has been progress in more Americans being part of the banking system, as the share of free checking accounts climbed back up to 47 percent in the 2020

---

<sup>1</sup> John Berlau “Free Checking Nearly Extinct Thanks To Dodd-Frank; Will Credit Card Rewards Follow?” Competitive Enterprise Institute Blog, September 28, 2012, <https://cei.org/blog/free-checking-nearly-extinct-thanks-to-dodd-frank-will-credit-card-rewards-follow/> ; Catherine New, “Free Checking Accounts Inch Toward Extinction As Cost of Banking Rises,” Huffington Post, September 17, 2012, [https://www.huffpost.com/entry/free-checking-account-cost-of-banking\\_n\\_1909504](https://www.huffpost.com/entry/free-checking-account-cost-of-banking_n_1909504).

<sup>2</sup> Todd J. Zywicki, Geoffrey A. Manne, and Julian Morris, “Price Controls on Payment Card Interchange Fees: the U.S. Experience,” George Mason University Law and Economics Research Paper Series No. 14-18, [https://www.law.gmu.edu/assets/files/publications/working\\_papers/1418.pdf](https://www.law.gmu.edu/assets/files/publications/working_papers/1418.pdf).

Bankrate survey<sup>3</sup>, and fintech apps such as Dave and Earnin help people keep track of their money and offer free or very low-cost advances on their paychecks. But there is still much more to be done in terms of clearing barriers to financial inclusion. Innovators in every region of America – from the coasts to middle America - where I hail from originally – are creating financial products and services to serve every sector of American consumers and small-business entrepreneurs. The government has a role in ensuring clear disclosure and swift punishment of fraud but should refrain from either heavy-handed regulation or the creation of state-owned financial services entities that could smother and crowd out this innovation. And it should clear away existing regulation that is either outdated or, in a term my colleagues and I have used to describe red some red tape that was cleared away as a hindrance to combating the pandemic, was *never-needed*.<sup>4</sup>

I thank the committee for presenting the three bills to my fellow witnesses and me for our assessments. I'm pleased to say I generally like the approach of one of the bills, the "Expanding Financial Access for Underserved Communities Act." However, I can't say the same for the other two offerings, the "Access to No-Fee Accounts Act" and the "Public Banking Act of 2021."

First, the positive. The "Expanding Financial Access for Underserved Communities Act" allows, but does not mandate, credit unions to expand their fields of membership to include a variety of underserved areas. This lifts regulatory barriers to individual credit unions that decide it makes good business sense to add new customers based on their mission of service. And the credit union supervisory agency, the National Credit Union Administration, will review such plans by credit unions for safety and soundness.

I applaud this type of approach, which is consistent with what my colleagues and I have been advocating in terms of policies that add competition through liberalization to the financial system. We have pushed for both bank and credit unions regulators to streamline approvals for new, or "*de novo*", entrants and are pleased that both the NCUA and the Federal Deposit Insurance Corporation (FDIC) are making *de novo* approvals a priority, even though they still have a long way to go reach the number of new financial institution approvals of decades past. We also have long advocated that Congress raise or repeal the arbitrary cap on credit union member business lending that serves no safety and soundness purpose and exists mainly to protect banks from competition in making business loans.<sup>5</sup>

But while the credit-union bill is a bottom-up approach to financial inclusion, the other two offerings are top-down approaches that would worsen the lot of the unbanked as well as many

---

<sup>3</sup> Mathew Goldberg, "Survey: Interest Checking Account Fees Hit Record High, While Average Yield Ties Record Low," Bankrate, October 21, 2020, <https://www.bankrate.com/banking/checking/checking-account-survey/#noninterest>.

<sup>4</sup> Kent Lassman and David McIntosh, "Kill the Never-Needed regulations slowing the economic recovery," *Washington Examiner*, May 28, 2020, <https://www.washingtonexaminer.com/opinion/kill-the-never-needed-regulations-slowing-the-economic-recovery>.

<sup>5</sup> John Berlau and Lindsay Lewis, "A simple way to grow America's economy and create jobs," *The Hill*, September 29, 2015, <https://thehill.com/blogs/congress-blog/economy-budget/255228-a-simple-way-to-grow-americas-economy-and-create-jobs>.

other American consumers of the financial system. The “Access to No-Fee Accounts Act” is a version of what has been called “Fed Accounts,” in which the Federal Reserve would directly compete with banks and credit unions to provide deposit accounts to consumers. This approach raises a host of problems involving privacy, data security, crowding out private-sector innovation, and depriving banks and credit unions of deposits necessary to make loans.<sup>6</sup>

On privacy, Fed Accounts give the Fed, a government entity, direct access to consumer financial transactions without a warrant.<sup>7</sup> The data would also likely be vulnerable to hacking, as the government’s record on data breaches is certainly no better than that of the private sector.<sup>8</sup> Drew Johnson, national director of Protect Internet Freedom and senior fellow at the Taxpayers Protection Alliance, notes that under such a scheme, “the federal government could learn how much a mother paid for her son’s piano lesson, how friends chose to split a dinner bill, where an individual traveled using a rideshare app, how much a couple spent on concert tickets for their anniversary, and billions of other nuggets of information the government, frankly, has no right to know.”<sup>9</sup>

The approach of the “Public Banking Act of 2021” raises similar concerns to Fed Accounts, plus has some uniquely troubling aspects of its own. Like plans for Fed Accounts, proposals for banking units owned by the U.S. Postal Service or state governments pose threats to privacy, data security, and innovation. The provisions in this bill to grant a federal charter and provide a new type of deposit insurance to these entities also pose risks of taxpayer bailouts for poorly managed public banks.

But perhaps the biggest concern of this particular bill is that financial *exclusion* – rather than inclusion -- of a legal industry is one of its stated goals. On page 23, the bill prohibits banks with this charter from “providing loans to, making investments in, or otherwise engaging in any activity that is financial in nature, or incidental to such financial activity, for a fossil fuel project.” Ironically, the state-owned Bank of North Dakota, which may be touted as an example of public banking at this hearing, would be disqualified as a “covered bank” under this bill because it provides financing for drilling and fracking in the oil-rich regions of the state.<sup>10</sup> This bill’s prohibition on banks dealing with industries that are legal, yet which government officials deem as “unwoke,” clashes with the supposed theme of this hearing of financial inclusion. It is a

---

<sup>6</sup> Paul H. Jossey, “Central Bank Digital Currency: The Fed’s Coming Power Grab,” *National Review*, June 3, 2021, <https://www.nationalreview.com/2021/06/central-bank-digital-currency-the-feds-coming-power-grab/>.

<sup>7</sup> John Berlau, “Government-Run Payment Systems Are Unsafe at Any Speed,” OnPoint No. 264, Competitive Enterprise Institute, June 10, 2020, pp. 5-6, [https://cei.org/sites/default/files/John\\_Berlau\\_-\\_Government-Run\\_Payment\\_Systems\\_Are\\_Unsafe\\_at\\_Any\\_Speed.pdf](https://cei.org/sites/default/files/John_Berlau_-_Government-Run_Payment_Systems_Are_Unsafe_at_Any_Speed.pdf).

<sup>8</sup> Amelia Brust and David Thornton, “Appeals court rules OPM data breach left people vulnerable to harm,” Federal News Network, June 27, 2019, <https://federalnewsnetwork.com/opm-cyber-breach/2019/06/appeals-court-rules-opm-data-breach-left-people-vulnerable-to-harm/>.

<sup>9</sup> Drew Johnson, “Wasteful Fed Wants Millions for Real-Time Payments Redundancy,” Newsmax, May 21, 2019, <https://www.newsmax.com/drewjohnson/paypal-square-venmo/2019/05/21/id/917034/>.

<sup>10</sup> Oscar Perry Abello, “What a Public Bank Can Do for Real People,” *Yes Magazine*, February 19, 2020, <https://www.yesmagazine.org/issue/world-we-want/2020/02/19/public-bank-north-dakota>.

deliberate attempt to make a legal industry “unbanked,” despite harmful consequences to the workers and consumers in the industry’s orbit.

My CEI colleagues and I have been consistent in saying that government officials should not use the banking industry to launch indirect attacks on industries they disfavor. We support the “SAFE Banking Act,” sponsored by Chairman Perlmutter, to prevent the federal government from punishing banks and credit unions that service marijuana businesses that operate in states where the substance is treated as legal under state law.<sup>11</sup> We also supported Ranking Member’s Luetkemeyer’s efforts to uncover and then end “Operation Choke Point,” in which various federal agencies during the Obama era pushed banks to cut off business with industries ranging from guns to small-dollar lenders.<sup>12</sup> CEI believes that the federal government should neither discourage nor encourage banks and credit unions in dealing with legal industries, whether marijuana, guns, or oil and gas.

It is legitimate in a democracy to debate whether industries should be restricted or even banned. But as long as an industry is legal, its practitioners should not be forced to leave themselves and their stakeholders vulnerable to crime and other effects of being unbanked because the government has pressured banks and credit unions to shut off access to them. In all transactions involving controversial but legal industries, individual financial firms should be allowed to make their own assessments of reputational risks.

There are many more things Congress and policy makers can do to ensure a financial system that can serve all legitimate consumers and entrepreneurs. The Truth in Lending Act needs to be revised so that the measure of annual percentage rate (APR) isn’t used to measure the cost of short-term, small-dollar loans that don’t come close to being held by borrowers for a year.<sup>13</sup> As the great economist Thomas Sowell points out, “Using this kind of reasoning—or lack of reasoning—you could ... say a hotel room rents for \$36,000 a year, [but] few people stay in a hotel room all year.”<sup>14</sup> Given the flaws in this measure of interest rates and the demonstrated negative effects of price controls, Congress should certainly refrain from enacting a top-down federal APR cap on small-dollar loans.

A competitive market -- free of heavy-handed regulation and state-backed entities that would suppress innovation and do other harms -- is one where all types of entrepreneurs create products

---

<sup>11</sup> Michelle Minton and John Berlau, “House-passed SAFE Banking Act Would End Federal Threat to Banks Dealing with Legal Cannabis Businesses,” Competitive Enterprise Institute News Release, April 20, 2021, [https://cei.org/news\\_releases/house-passed-safe-banking-act-would-end-federal-threat-to-banks-dealing-with-legal-cannabis-businesses/](https://cei.org/news_releases/house-passed-safe-banking-act-would-end-federal-threat-to-banks-dealing-with-legal-cannabis-businesses/).

<sup>12</sup> Blaine Luetkemeyer, “Evidence Is Now Clear: Operation Choke Point Hurt Lawful Businesses,” *American Banker*, October 24, 2018, <https://www.americanbanker.com/opinion/evidence-is-now-clear-operation-choke-point-hurt-lawful-businesses>.

<sup>13</sup> Matthew Adams and John Berlau, “The Annual Percentage Rate Is the Wrong Metric for Assessing the Cost of a Short-Term Loan,” OnPoint No. 268, Competitive Enterprise Institute, April 7, 2021, <https://cei.org/wp-content/uploads/2021/04/revised-apr-paper.pdf>.

<sup>14</sup> Thomas Sowell, “Payday Loans,” *National Review*, November 2, 2011, <http://www.nationalreview.com/articles/281908/payday-loans-thomas-sowell>.

and services for all types of consumers, enabling a financial system and an economy that is both dynamic and inclusive. Thank you again for inviting me to testify. I look forward to your questions.

*Mr. Berlau gratefully acknowledges the assistance in preparing this testimony of his CEI colleagues Guy Denton, Paul Jossey, and Ryan Nabil*

