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JOINT INFORMATIONAL HEARING AGENDA

Senators Holly J. Mitchell, Steven Bradford, Chairs

August 15, 2020

*1:00 p.m. or One Hour after Adjournment of Senate Budget
State Capitol – Senate Chamber*

The Governor's proposal for Expanding the Department of Business Oversight into
Department of Consumer Financial Protection and Innovation

I. INTRODUCTION, Chairs and Members

II. GOVERNOR'S PROPOSAL

Manuel P. Alvarez, Commissioner, Department of Business Oversight
Jessica Peters, Legislative Analyst, Legislative Analyst's Office
Kimberly Harbison, Principal Program Budget Analyst, Department of Finance

III. TESTIMONY

Richard Cordray, Former Director, Consumer Financial Protection Bureau
Jyotswaroop Kaur Bawa, California Reinvestment Coalition
Kevin Gould, California Bankers Association
Scott Govenar, California Financial Services Association

IV. PUBLIC COMMENT

BU 1701: DEPARTMENT OF BUSINESS OVERSIGHT (DBO)**Issue: Expanding DBO into Department of Consumer Financial Protection and Innovation**

Summary of the Governor’s Proposal. Retaining all powers, duties, responsibilities and functions of DBO, the Governor’s proposal seeks to expand DBO with new statutory authority, division and offices into the new Department of Financial Protection and Innovation (DFPI). The request seeks \$10.2 million and 44 positions in 2020-21, \$14.8 million and 28 positions in 2021-22, \$19.3 million and 18 staff positions in 2022-23, and ongoing funding. The budget request is accompanied by trailer bill language seeking to expand DBO’s authority to register unlicensed financial product and service providers and promulgate regulations and enforcement to protect consumers against unfair, deceptive and abusive acts and practices (UDAAP) in the California financial marketplace.

BACKGROUND

Department of Business Oversight. DBO was established in 2013 with the merger of regulatory activities of the Department of Corporations (which regulated financial entities such as securities brokers and dealers, financial planners, and mortgage lenders unaffiliated with banks) with the Department of Financial Institutions (which had regulatory powers over state-chartered banks, credit unions, money transmitters, and savings and loan associations). DBO is the state’s main financial marketplace regulator with three main activities: (1) licensing and regulating financial services and providers, (2) overseeing and enforcing safe and sound financial practices, and (3) providing consumer services and education around financial services and products. DBO oversees more than 23 financial service industries and supervises more than 360,000 individuals and businesses with a cumulative total of over \$1.1 trillion in assets in the banked financial institutions alone. To carry out its functions, DBO is currently staffed with 615 positions and has an operational budget totaling \$108 million from a combination of special funds (Credit Union Fund, Local Agency Deposit Security Fund, Financial Empowerment Fund and newly combined Financial Protection Fund). These funds are drawn from licensing fees, examination fees, penalty assessments, reimbursements, settlements or other monies charged by the department from financial service providers currently overseen by DBO.

Federal and State Agencies for Consumer Protection. The Consumer Financial Protection Bureau (CFPB), authorized by the Dodd Frank Act of 2010, is the main federal agency singularly tasked to ensure financial service companies treat consumers fairly. The CFPB and states also have broad authority, granted by Dodd Frank, to provide consumers with more protection against unfair, deceptive, and abusive practices (UDAAP) when accessing financial services and products. The California Department of Justice (DOJ) and local district attorneys have broad authority to bring enforcement actions related to consumer protection and UDAAP violations in the state.

California's UDAAP statute originates mainly from the state's Business and Professions Code (Sections 17200 through 17594) and the Civil Code (Sections 1750 through 1785). It broadly prohibits unlawful, unfair, or fraudulent business practices and deceptive advertising, and it is not undercut by exemptions for particular businesses. In addition to DBO, CFPB and DOJ, the financial marketplace is monitored and regulated by half a dozen agencies at the federal level like the Federal Reserve Board, the Federal Trade Commission, and the Securities and Exchange Commission to name a few.

Existing Challenge and Legislative Response. Despite DBO's activities, Californian consumers still rely on the CFPB for consumer protection. There is weakened consumer financial protection at the federal level, as evidenced by the recent consumer finance deregulation and reduced enforcement activities at the CFPB. In response, the California Assembly passed Joint Resolution 48 (Chapter 199, Statutes of 2018) urging the President and Congress to maintain the integrity of the CFPB. Other states like New York, Pennsylvania, New Jersey, Delaware and Maryland have responded by re-vamping their in-state consumer protection activities. To that end, Assembly Member Limón introduced legislation, AB 1048, last year seeking to enhance DBO's capacity for enforcement and investigation of potential for financial harm. Meanwhile, the DBO continues to be tasked to do more by the Legislature and has been given additional authority to regulate student loan servicers, property assessed clean energy financing, and commercial financing disclosures within the past four years.

GOVERNOR'S PROPOSAL

Trailer Bill Language and Proposed Statutory Authority for DFPI. The Governor's budget request is accompanied by trailer bill language that creates a new California Consumer Financial Protection Law (CCFPL). The CCFPL seeks to clarify DBO's UDAAP authority over existing licensees and expand DBO's jurisdiction to cover currently unlicensed persons (new covered persons) that offer or provide consumer financial products and services in California. Proposed trailer bill language authorizes the new DFPI to do all of the following:

Perform a Broad Range of Activities Related to UDAAPs: The proposal defines unfair and deceptive acts and practices by reference to California's Business and Professions Code (Section 17200) and defines abusive acts and practices by reference to provisions of the federal Dodd-Frank Act (12 USC Section 5481). It authorizes DFPI to enforce UDAAP violations by covered persons and existing licensees, using a range of enforcement authority contained in federal law. The proposal also authorizes DFPI to promulgate regulations identifying UDAAPs in connection with the offer of consumer financial products and services, as well as the offer of financing to small businesses, nonprofits, and family farms. The trailer bill does not require DFPI to promulgate regulations defining UDAAPs before the department may enforce UDAAP violations.

Perform Oversight over Activities of Covered Persons Offering Consumer Financial Products and Services in the State: The trailer bill authorizes DFPI to investigate any currently unlicensed person who offers consumer financial products or services in the state, as well as any service provider to that covered person. DFPI is authorized to promulgate regulations requiring covered persons to register with the department and to prescribe rules to facilitate oversight of covered persons and assessment and detection of risks to consumers.

Clarify DBO's Regulatory Authority Where it Overlaps With the Attorney General (AG): The trailer bill clarifies that nothing in its provisions limits the powers or authorities of the AG, including, but not limited to the AG's authority to pursue UDAAP violations. DFPI is authorized, but not required, to enter into an agreement with the AG with respect to civil actions by each agency. The department is also required to notify other regulatory agencies that will be impacted by the department's enforcement activities under the CCFPL.

Clarify DBO's Regulatory Authority Where it Overlaps With Other Regulators: The CCFPL does not apply to a license or an employee of a licensee of any state agency other than the DFPI, to the extent that licensee or employee is acting under the authority of the other state agency's license. However, to the extent the DFPI takes action to require the registration of a covered person who is also regulated by another agency, the department is required to consult with that agency before promulgating its regulations.

Conduct Activities Related to Research, Innovation, and Education: The trailer bill authorizes the commissioner to investigate, research, analyze, and report on markets for consumer financial products or services; develop and implement outreach and education programs to underserved consumers and communities; and develop and implement initiatives to promote innovation, competition, and consumer access within financial services. These provisions are intended to match up with funding for the two new offices envisioned in the budget proposal.

Issue Annual Reports: The trailer bill requires DBO to prepare and publish an annual report on the department's website detailing actions taken during the prior year under the CCFPL. The report must include, but is not limited to actions taken with respect to rulemaking, enforcement, oversight, consumer complaints and resolutions, education, and research.

Budget Proposal for Increased Staffing and New Offices in the DFPI. A third of additional staff requested is for increased staffing in the regulatory and enforcement workload activities in the Enforcement Division and Legal Division. More than 50 percent of the proposed staffing increase is allocated to new units and new positions in DFPI. More specifically new staffing is requested for the following activities:

The New Division of Consumer Financial Protection: The Administration's proposal seeks to create a new division, staffed with 42 positions over three years. This division will be led by a new Senior Deputy Commissioner appointed by the Governor and confirmed by the Senate. This new division will house the following:

Supervision and Registration Office for registering new covered persons and supervising new classes of financial services and products currently not under the purview of the DBO. The department anticipates more than 9000 newly covered persons to come under the new jurisdictions of the DFPI. Registration fees will be used to provide funding for expanded activities authorized by DFPI and CCFPL.

Market Monitoring, Consumer Research, Insights and Analytics Office for proposed activities around financial market monitoring and research activities including but not limited to consumer credit trends, consumer behavior and adequate access to financial services and products for more effective policies.

Targeted Consumer Education and Outreach Office proposed activities designed to provide financial empowerment tools and information to students, seniors, military service members, and new Californians.

Additionally, the DFPI merges the traditionally separated Division of Financial Institutions and Division of Corporations under a single division and a single Senior Deputy Commissioner of the new Division of Corporations and Financial Institutions.

The New Financial Technology Office: The Administration's proposal seeks to staff a new Financial Technology office with four positions over three years to conduct activities to encourage innovation, enable fintech to operate nationwide, and research emerging and new innovative technologies.

The New Office of Ombudsperson: The Administration's proposal currently places a single staff position to act as an independent, impartial resource for stakeholders.

QUESTIONS. The committee may choose to ask the department and the Administration the following questions.

1. What is the department's implementation plan for this proposal over the next three years?
2. Can the department currently bring enforcement actions against current licensees for engaging in UDAAPs? Will this bill hold current licensees liable for UDAAP violations related to acts that are outside the scope of their licensing laws?

3. How will UDAAP law enforcement activities be coordinated with other supervisory entities in the state like the DOJ and local district attorneys?
4. How does the department plan to enforce the new CCFPL before regulations are promulgated?
5. How many new covered persons does the department anticipate being covered by the CCPFL? What methodology will the department implement to identify, prioritize and require the registration of new covered persons?
6. How does the department intend to register and supervise new covered persons under the purview of federal regulators (like credit reporting companies) and local jurisdictions (like pawnbrokers)?
7. The department plans to use registration fees of new covered persons to fund CCFPL activities beginning 2023-24. What is the revenue influx anticipated? What is the approximate size range of fees is DBO planning to impose?
8. How will the department measure the success of the CCFPL and the newly created offices like the Office of Financial Innovation? What metrics or milestones should the Legislature look for as a measure of success?
9. How will the new Office of Ombudsperson be empowered to be impartial and independent?
10. What are the additional costs, not included in the budget change proposal, associated with expanding and renaming DBO into DFPI?

STAFF COMMENTS. This is an informational hearing and no action is required at this time. However, the Legislature will likely have to act on this proposal in the coming weeks. Staff acknowledges that the Administration and specifically DBO has been actively engaged in discussions with stakeholders, including legislative staff, in order to improve the proposal and address feedback. To that end, the Administration has made various amendments to their original proposal. However, there are still concerns that are continuing to be discussed in hopes of a satisfactory resolution. These include the manner in which this proposal will ultimately apply, or not apply, to current licensees and the role the Legislature will play in respect to oversight as this proposal is implemented.