



**Congressional
Research Service**

Informing the legislative debate since 1914

An Overview of Consumer Finance and Policy Issues

Updated January 14, 2021

Congressional Research Service

<https://crsreports.congress.gov>

R45813



R45813

January 14, 2021

Cheryl R. Cooper
Analyst in Financial
Economics

An Overview of Consumer Finance and Policy Issues

Consumer finance refers to the saving, borrowing, and investment choices that households make over time. These financial decisions can be complex and can affect households' financial well-being both now and in the future. Safe and affordable financial services are an important tool for most American households as they avoid financial hardship, build assets, and work to achieve financial security over the course of their lives. Understanding why and how consumers make financial decisions is important when considering policy issues in consumer financial markets.

Households borrow money for the following common reasons: investments—such as a home or education—to build future wealth, consumption smoothing (i.e., paying later to consume things now), and emergency expenses. Most households rely on credit to finance some of these expenses, because they do not have enough money saved to pay for them. According to the Federal Reserve Bank of New York, mortgage debt is by far the largest type of debt for households, accounting for approximately 69% of household debt. Student debt is the second-largest household debt, followed by auto loans and credit cards.

Consumer financial markets generally share similar market dynamics. In all of these markets, consumers often act in similar ways when making financial decisions and firms tend to act in comparable ways to attract consumers. Therefore, the government tends to consider similar policy interventions when regulating in these markets.

Competitive free markets generally lead to efficient distributions of goods and services to maximize value for society. Yet sometimes, free markets are inefficient when particular issues arise. Common issues in consumer financial markets include (1) information asymmetries between financial firms and consumers and (2) behavioral biases that predictably bias consumers when making financial decisions. In these cases, government policy can potentially correct market failures to bring the market to a more efficient outcome, maximizing social welfare. In consumer finance, three types of policy interventions are common: (1) standardized consumer disclosures; (2) regulation to prevent deceptive, unfair, or abusive financial institution practices; and (3) regulation to prevent discrimination in consumer-lending markets. Yet, policymakers need to be aware of unintended consequences of proposed policies, and often find it challenging to determine whether a policy intervention will help or harm a particular market from reaching its efficient outcome.

In response to the 2007-2009 financial crisis, the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank; P.L. 111-203) established the Consumer Financial Protection Bureau (CFPB) to implement and enforce federal consumer financial law while ensuring consumers can access financial products and services. The CFPB's authorities fall into three broad categories: *rulemaking*, writing regulations to implement laws under its jurisdiction; *supervision*, the power to examine and impose reporting requirements on financial institutions; and *enforcement* of various consumer protection laws and regulations. The CFPB generally has regulatory authority over providers of an array of consumer financial products and services.

The major consumer financial markets include mortgage lending, student loans, automobile loans, credit cards and payments, payday loans and other credit alternative financial products, and checking accounts and substitutes. In addition, two important market structures allow these consumer financial products to be offered: (1) the consumer credit reporting system and (2) the debt collection market. These aspects of the consumer credit system facilitate the pricing of credit offers and the resolution of delinquent consumer credit products for most consumer credit markets.

Contents

Introduction	1
Consumer Finance Policy Issues and Regulation.....	2
Household Balance Sheet Background.....	2
Consumer Finance Markets and Policy Considerations.....	4
Imperfect Information.....	6
Behavioral Biases in Consumer Decisionmaking.....	7
Common Policy Interventions and Considerations	9
Policy Considerations	10
Consumer Financial Protection Bureau (CFPB).....	10
Overview of Major Consumer Finance Markets.....	12
Mortgage Lending Market	12
Student Loans	14
Automobile Loans	16
Credit Cards and Payments	20
Payday and Other Credit Alternative Financial Products	22
Checking Accounts and Substitutes	24
Overview of Consumer Finance Market Support Systems.....	26
Credit Reporting, Credit Bureaus, and Credit Scoring.....	26
Debt Collection and Bankruptcy	29
Conclusion.....	32

Figures

Figure 1. Household Debt Breakdown in Q3 2020.....	1
Figure 2. U.S. Income Distribution in 2019.....	4
Figure 3. U.S. Net Worth Distribution (Assets – Debt) in 2019.....	4

Contacts

Author Information	32
--------------------------	----

Introduction

Consumer finance encompasses the financial lives of individuals and households. Americans aspire for economic advancement and wealth building, a central part of the “American dream.” Safe and affordable financial services are an important tool for most American households as they avoid financial hardship, build assets, and work to achieve financial security over the course of their lives. Households use three types of financial products regularly: credit, insurance, and financial investments. This report will focus on the first category—credit and deposit-taking financial products for personal, family, or household purposes.¹

Most households rely on credit to finance some expenses because they do not have enough assets saved to pay for them. Mortgage debt is by far the largest type of household debt. According to data from the Federal Reserve Bank of New York, as shown in **Figure 1**, mortgages account for approximately 69% of household debt. Student loans are the second-largest type of household debt, followed by auto loans and credit cards.

These and other major consumer finance markets are discussed in more detail in this report under “Overview of Major Consumer Finance Markets,” which provides a brief overview of each financial product, recent market developments, and related policy issues. Major consumer finance markets examined in this report include mortgage lending, student loans, automobile loans, credit cards and payments, payday loans and other credit alternative financial products, and checking accounts and substitutes. In general, this report will focus on the consumer and household perspective, and consumer protection policy issues in each market.

Figure 1. Household Debt Breakdown in Q3 2020



Source: Center for Microeconomic Data, *Quarterly Report on Household Debt and Credit*, Federal Reserve Bank of New York, at <https://www.newyorkfed.org/microeconomic/databank.html>.

This report also discusses two important market structures that allow these consumer financial products to be offered: (1) the consumer credit reporting system and (2) the debt collection market. These aspects of the consumer credit system are important because they facilitate the pricing of credit offers and the resolution of delinquent consumer credit products for most consumer credit markets.

The report begins with an overview of U.S. household finances, consumer finance markets, and common policy issues in these markets.

¹ For an introduction on this topic, see CRS In Focus IF11682, *Introduction to Financial Services: Consumer Finance*, by Cheryl R. Cooper.

The COVID-19 Pandemic and Consumer Finance

The Coronavirus Disease 2019 (COVID-19) pandemic² has had a large and persistent economic impact across the United States.³ Fear of infection, social distancing, and stay-at-home orders prompted business closures and a severe decline in demand for restaurants and travel, among other industries. Consequently, many Americans have lost income and faced financial hardship. Survey results suggest that since March 2020, about half of all U.S. adults live in a household that has lost some employment income.⁴

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) enacted on March 27, 2020, establishes consumer rights to be granted forbearance for federally backed mortgages for up to a year (§4022) and federal student loans (§3513), administratively extended through the end of January 2021.⁵ The CARES Act also protects the credit histories of consumers with forbearance agreements (§4021).⁶

For more information on consumer loan forbearance during the COVID-19 pandemic, including CARES Act rights, regulatory guidance, and impacts on consumers and financial institutions, see CRS Report R46356, *COVID-19: Consumer Loan Forbearance and Other Relief Options*, coordinated by Cheryl R. Cooper. For more information about consumer debt during the pandemic, see CRS Report R46578, *COVID-19: Household Debt During the Pandemic*, coordinated by Cheryl R. Cooper. For resources for consumers having trouble paying their debts during the COVID-19 pandemic, see CRS Insight IN11359, *COVID-19: Financial Relief and Assistance Resources for Consumers*, by Maura Mullins and Jennifer Teefy.

Consumer Finance Policy Issues and Regulation

Consumer finance refers to the saving, borrowing, and investment choices that households make over time. These financial decisions can be complex and can affect households' financial well-being both now and in the future. Understanding why and how consumers make financial decisions is important when considering policy issues in consumer financial markets.

This section provides an introduction to U.S. households' finances, including a breakdown of a household balance sheet and its components. It then provides background on how consumer financial markets operate and general issues in these markets. The section also describes common policy interventions and considerations when using these policy tools. Lastly, this section provides an overview of the Consumer Financial Protection Bureau (CFPB)—the main regulator responsible for consumer compliance of financial products and services.

Household Balance Sheet Background

A household's balance sheet⁷ is similar to a firm's in that it presents a full financial picture, including the household's:

² For background on the Coronavirus Disease 2019 (COVID-19), see CRS In Focus IF11421, *COVID-19: Global Implications and Responses*, by Sara M. Tharakan et al.

³ For background on the economic effects of the COVID-19 pandemic in the United States, see CRS Report R46606, *COVID-19 and the U.S. Economy*, by Lida R. Weinstock.

⁴ For more information on income losses during the COVID-19 pandemic, see CRS Insight IN11457, *COVID-19 Pandemic's Impact on Household Employment and Income*, by Gene Falk.

⁵ P.L. 116-136. For more information on Title IV of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), which contains a number of provisions aimed broadly at stabilizing the economy and helping affected households and businesses, see CRS Report R46301, *Title IV Provisions of the CARES Act (P.L. 116-136)*, coordinated by Andrew P. Scott. For more information about federal student loan debt relief in the context of COVID-19, see CRS Report R46314, *Federal Student Loan Debt Relief in the Context of COVID-19*, by Alexandra Hegji.

⁶ For more information on the credit reporting industry, see CRS Report R44125, *Consumer Credit Reporting, Credit Bureaus, Credit Scoring, and Related Policy Issues*, by Cheryl R. Cooper and Darryl E. Getter.

⁷ Jack Kapoor et al., "Chapter 1," in *Personal Finance*, 12th ed. (McGraw-Hill Education, 2017).

- **Assets**—A point-in-time value of what a household owes, can include *liquid wealth*, such as a savings account or other financial assets from which the household can easily access funds, and *illiquid wealth*, such as a car or home that the household owns.
- **Debts**—A point-in-time value of what a household owes, can include a home mortgage, a student loan, or other types of consumer loans.
- **Net Worth**—Equal to *assets* minus *debts*, measures the wealth of a household, including home equity.
- **Income**—Wages earned from a job or financial investment returns over a period of time (e.g., a year).
- **Consumption**—Household spending over a period of time, such as rent, food, clothing, and entertainment.
- **Savings**—The difference between *income* and *consumption* over a period of time. When a household's income is greater than its consumption, it can save or invest this unconsumed income, increasing the household's *assets* or paying off debt owed, reducing the household's total *debts*.
- **Borrowing**—New *debts* taken out over a period of time. When a household's *consumption* is greater than its *income*, it can either spend *assets* it owns or borrow money, increasing the household's *debts*.

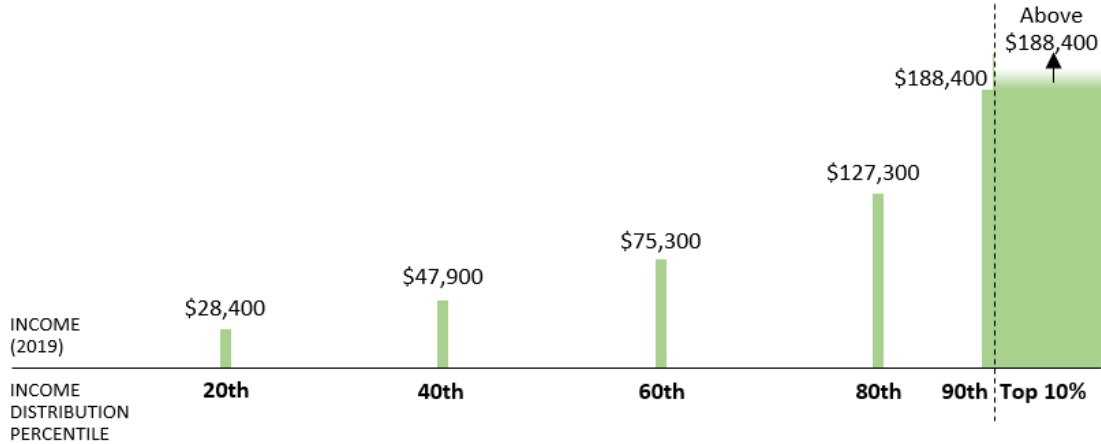
In general, research on household finance suggests that all of the components of a household balance sheet—assets, debts, net worth, income, consumption, savings, and borrowing—are important to understanding a household's financial experience over time. For example, in the event of a *financial shock*—an unexpected expense such as a car or home repair, a medical expense, or a pay cut—households with a lower income or little liquid savings are much more likely to experience difficulty making ends meet.⁸ As this example suggests, all of the balance sheet's components need to be accounted for when considering consumer decisionmaking.

As demonstrated in **Figures 2 and 3**, household income and net worth in the United States are both distributed unevenly. According to the Federal Reserve Board's (Fed's) Survey of Consumer Finances, the bottom 20% of U.S. households ranked by income have an income below \$28,400, whereas the top 10% have an income above \$188,400.⁹ Likewise, the bottom 25% of U.S. households ranked by net worth have a net worth below \$12,400, whereas the top 10% have a net worth above \$1,220,200. These distributions reflect the variation of household balance sheets within the United States and are due to many factors such as age, size of household, and household decisions about jobs, homeownership, and other factors.

⁸ The Pew Charitable Trusts, *How Do Families Cope with Financial Shocks? The Role of Emergency Savings in Family Financial Security*, October 2015, at https://www.pewtrusts.org/~media/assets/2015/10/emergency-savings-report-1_artfinal.pdf; and Scott Fulford and Marie Rush, *Insights from the Making Ends Meet Survey*, Consumer Financial Protection Bureau (CFPB), Research Brief No. 2020-1, July 2020, at https://files.consumerfinance.gov/f/documents/cfpb_making-ends-meet_survey-results_2020-07.pdf.

⁹ Neil Bhutta et al., *Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances*, Board of Governors of the Federal Reserve System, Federal Reserve Bulletin vol. 106, no. 5, September 2020, p. 37, at <https://www.federalreserve.gov/publications/files/scf20.pdf>.

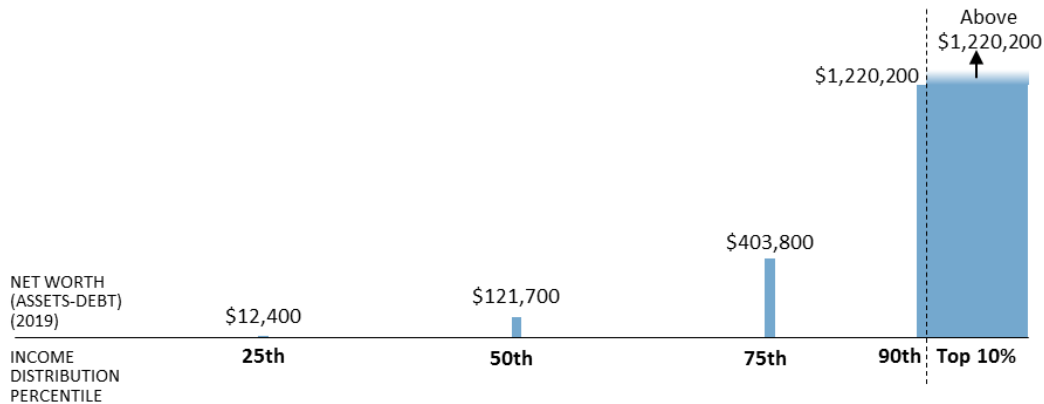
Figure 2. U.S. Income Distribution in 2019



Source: Neil Bhutta et al., *Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances*, Board of Governors of the Federal Reserve System, Federal Reserve Bulletin vol. 106, no. 5, September 2020, p. 37, at <https://www.federalreserve.gov/publications/files/scf20.pdf>.

Notes: This report uses the income classifier from the Survey of Consumer Finances respondent-reported measure of *usual* income, which captures household income with transitory fluctuations smoothed away to approximate the economic concept of *permanent* income.

Figure 3. U.S. Net Worth Distribution (Assets – Debt) in 2019



Source: Neil Bhutta et al., *Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances*, p. 37.

Consumer Finance Markets and Policy Considerations

This report examines household borrowing, with a particular focus on consumer financial products, such as mortgages, credit cards, and auto loans, which allow a household to borrow and make payments. As described in the previous section, consumer behavior in these markets may be driven by other parts of the balance sheet, such as the need to build assets or withstand a financial shock. Three common reasons households use credit are as follows:

- **Asset Building**—Using credit to make investments can allow a household to build wealth over time. For example, a household can use a mortgage to pay for an asset, such as a house, that may appreciate over time. A household also can use student loans to fund education expenses to make a higher income in the future. In both cases, households are using credit to fund household investments that may lead to greater wealth in the future.
- **Consumption Smoothing**—Using credit to move income across time periods allows a household to consume future income now. For example, recent college graduates might use credit cards to pay for expenses before their new jobs begin. This money is more valuable to graduates now, before they have wages, than in the future, when they have enough income to meet living expenses.
- **Financial Shocks or Emergencies**—Using credit to pay for unexpected expenses allows a household to compensate for an emergency, such as a car or home repair, a medical expense, or a pay cut. For example, a consumer might take out a payday loan to repair a car and continue to go to work. This money is also more valuable to the consumer during the financial emergency, than in the future.

Each consumer financial market is unique and governed by various distinct laws and regulations. However, consumer financial markets generally share similar market dynamics. In all of these markets, consumers often act in similar ways when making financial decisions and firms tend to act in comparable ways across markets to attract consumers and make profits.¹⁰ Therefore, the government tends to consider similar policy interventions and factors when regulating these markets.

Mainstream economic theory asserts that competitive free markets generally lead to efficient distributions of goods and services to maximize value for society.¹¹ Under this theory, each market moves toward an efficient price, at which the supply of goods produced by firms and amount of goods demanded by consumers equal one another. If consumers demand credit products, then banks or other lenders should want to provide these products to consumers if they can make a profit. Without major barriers for new lenders to enter the market, more lenders should start providing credit to consumers, until the price is no longer excessively profitable to lenders. At this point, the market is at equilibrium, at its efficient outcome for society. If these conditions hold, policy interventions cannot improve on the financial decisions that consumers make based on their unique situations and preferences. For this reason, some policymakers are hesitant to disrupt free markets, on the theory that prices determined by market forces lead to efficient outcomes without intervention.

The life-cycle model is a prevalent economic hypothesis that assumes households usually want to keep consumption levels and their lifestyles stable over time.¹² For example, severely reducing a household's consumption one month may be more painful for a household than the pleasure of a much higher household consumption level in another month. Therefore, households save and invest during their careers in order to afford a stable income across their lives, including retirement. This model suggests that wealth increases as households' age, which generally fits

¹⁰ For more on how firms price consumer loans, see CRS In Focus IF10993, *Consumer Credit Markets and Loan Pricing: The Basics*, by Darryl E. Getter.

¹¹ N. Gregory Mankiw, "Chapter 7," in *Principles of Microeconomics*, 7th ed. (South-Western College Pub, 2014).

¹² Franco Modigliani, "The Life Cycle Hypothesis of Saving, the Demand for Wealth and the Supply of Capital," *Social Research*, vol. 33, no. 2 (Summer 1966), pp. 160-217.

household data in the United States.¹³ However, income and wealth inequality continues to exist after controlling for household age, suggesting that age is not the only important factor.¹⁴

There are also circumstances where the life-cycle model fails to correspond to household behavior in the United States. A recent National Bureau of Economic Research (NBER) working paper on behavioral household finance identifies three facts about U.S. household balance sheets.¹⁵ First, income and consumption move together very closely, unlike the stable consumption that the life-cycle would predict. Second, U.S. households on average tend to have low levels of *liquid* wealth, such as money in a savings account, and a high incidence of credit card borrowing. Third, most U.S. households have much of their wealth in *illiquid* assets, such as home equity. These patterns might fit the life-cycle model if borrowing money is inexpensive and *illiquid* assets have higher returns than *liquid* assets. However, these assumptions might not apply to all households and other explanations might fit these patterns better.¹⁶ Generally, these three facts are important background to better understand consumer behavior in financial markets. These facts suggest why many U.S. households depend on access to affordable credit and robust consumer financial markets, both for short-term needs and for building wealth over time.

In these theoretical frameworks, “market failures” occur when a free market is inefficient due to departures from the standard economic framework, which includes assumptions about perfect information and perfect competition. Market failures can reduce economic efficiency and consumer welfare. In these cases, government policy can potentially correct market failures to bring the market to a more efficient outcome, maximizing social welfare. Yet, policymakers often find it challenging to determine whether a policy intervention will help or harm a particular market from reaching its efficient outcome.

The following sections discuss two specific departures from the conditions associated with economic efficiency—imperfect information and behavioral biases. These market failures are important to understand consumer credit markets.

Imperfect Information

Imperfect information, or information asymmetry, is when one party in a transaction (e.g., a firm) has more accurate or more detailed information than the other party (e.g., a consumer). This imbalance can result in inefficient outcomes.¹⁷ For example, ideally consumers in a mortgage market will shop around among lenders for the best interest rate, fees, and other terms for their own personal situations. Yet, it can be time-consuming to acquire better information, for example, to seek out information from a variety of different lenders to compare loan terms. Consumers might also be willing to spend more to save time or to have a better experience closing their

¹³ Neil Bhutta et al., *Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances*, Board of Governors of the Federal Reserve System, Federal Reserve Bulletin, vol. 106, no. 5, September 2020, p. 11, at <https://www.federalreserve.gov/publications/files/scf20.pdf>.

¹⁴ For more information on income and wealth inequality, see Neil Bhutta et al., *Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances*.

¹⁵ John Beshears et al., *Behavioral Household Finance*, National Bureau of Economic Research (NBER), Working Paper no. 24854, July 2018, p. 4.

¹⁶ For example, behavioral science research suggests that human decisionmakers tend to have biases in rather predictable patterns, which could explain some of these patterns. For more information, see the “Behavioral Biases in Consumer Decisionmaking” section of this report.

¹⁷ George Akerlof, “The Market for Lemons: Quality Uncertainty and the Market Mechanism,” *Quarterly Journal of Economics*, vol. 84, no. 3 (1970), pp. 488-500; and Michael Rothschild and Joseph Stiglitz, “Equilibrium in Competitive Insurance Markets: An Essay on the Economics of Imperfect Information,” *Quarterly Journal of Economics*, vol. 90, no. 4 (November 1976), pp. 629-649.

mortgage. However, if information asymmetry exists—for example, if interest and fee costs are hidden, confusing, or difficult to obtain—some consumers might choose a mortgage loan that is not optimal based on the criteria they deem to be important. In this case, the mortgage market will not lead to efficient societal outcomes, possibly costing some consumers more for a loan than is necessary and dissuading some consumers who otherwise would from entering the market. Information asymmetries occur in the opposite way as well. Often, lenders might not have accurate or detailed information about a consumer, making it hard for them to estimate a consumer’s likelihood of default on a loan. For this reason, systems like the credit reporting industry developed, to give lenders more information about a consumer and make the markets for consumer credit more efficient. For more information on the credit reporting industry, see the section of this report titled “Credit Reporting, Credit Bureaus, and Credit Scoring.”

Behavioral Biases in Consumer Decisionmaking

Behavioral research suggests that humans tend to have biases in rather predictable patterns.¹⁸ This research suggests that the human brain has evolved to quickly make judgments in bounded rational ways, using heuristics—or mental shortcuts—to make decisions. These heuristics generally help people make appropriate decisions quickly and easily, but sometimes, they can result in choices that make the decisionmaker worse off financially. Within consumer finance markets, a few of these biases tend to be particularly important:

- **Choice Architecture**—Research suggests that how financial decisions are framed can affect consumer decisionmaking. Framing can affect consumer decisions in many ways. For example, people can be *anchored* by an initial number, even if it is different from their next choice.¹⁹ In one illustration of this concept, researchers had subjects spin a wheel of fortune with numbers between zero and 100, then asked them the percentage of African countries in the United Nations. The random number generated in the first stage subconsciously affected subjects’ guesses in the second stage, even though they were not related. Another example of a decisionmaking bias is *defaults*.²⁰ For example, employees are more likely to be enrolled in a 401(K) plan by employer defaults than if they actively need to make a choice.²¹ A third example of a framing bias is *loss aversion*, the idea that people tend to respond more strongly to potential losses than gains.²² Therefore, when choices are framed as a potential loss, such as “an opportunity you don’t want to miss,” consumers respond more strongly than they do to potential benefits.

¹⁸ Daniel Kahneman, *Thinking Fast and Slow* (Location: Farrar, Straus and Giroux, 2011); and Dan Ariely, *Predictably Irrational: The Hidden Forces that Shape our Decisions* (Location: Harper, 2008).

¹⁹ Amos Tversky and Daniel Kahneman, “Judgment under Uncertainty: Heuristics and Biases,” *Science*, vol. 185, no. 4157 (September 27, 1974), pp. 1124-1131.

²⁰ Richard Thaler and Cass Sunstein, *Nudge: Improving Decisions about Health, Wealth, and Happiness* (Location: Penguin Books, 2008).

²¹ Brigitte C. Madrian and Dennis F. Shea, “The Power of Suggestion: Inertia in 401(K) Participation and Savings Behavior,” *Quarterly Journal of Economics*, vol. 116, no. 4 (November 2001), pp. 1149-1187.

²² Amos Tversky and Daniel Kahneman, “Loss Aversion in Riskless Choice: A Reference-Dependent Model,” *The Quarterly Journal of Economics*, vol. 106, no. 4 (November 1991), pp. 1039-1061; Kungl. Vetenskapsakademien: The Royal Swedish Academy of Sciences, *Foundations of Behavioral and Experimental Economics: Daniel Kahneman and Vernon Smith*, Advanced Information on the Prize in Economic Sciences 2002, December 17, 2002, pp. 15-19, at <https://www.nobelprize.org/uploads/2018/06/advanced-economicsciences2002.pdf>.

- **Present Bias and Scarcity**—When people tend to put more value on having something now, rather than in the future, even when there is a large benefit for waiting, this behavior is called *present bias*.²³ In addition, even when people decide they should do something difficult, such as saving for the future or choosing a retirement plan, self-control and procrastination may prevent them from following through on their intentions.²⁴ These human biases might lead consumers to make financial decisions that are not optimal.²⁵ Furthermore, a *scarcity mindset* can make optimal decisionmaking more difficult.²⁶ Difficult decisions, such as managing finances, require cognitive bandwidth. When under extreme stress, such as living in poverty, people may tunnel their vision, focusing on immediate needs (e.g., paying current bills), rather than prioritizing based on the big picture (e.g., increasing ones' future income). Self-control might also be a limited resource for humans, where the more self-control a person needs to exert over a day, the harder it is to maintain.²⁷ These limitations to human cognitive functioning can sometimes lead consumers to make flawed financial decisions.
- **Budgeting Biases (Mental accounting)**—Often, households use mental accounts, amounts of money mentally allocated in advance for different purposes, to make consumption decisions.²⁸ For example, a household may have a monthly budget for food, clothing, and entertainment. Even though money is fungible, many households act as if spending in one category does not affect spending in another category.²⁹ This categorization is an intuitive and simple way of thinking about a budget. Although this thinking reduces cognitive effort, it can also lead to predictable biases. For example, research suggests that people have trouble forecasting unusual or infrequent expenses.³⁰ For this reason, these expenses are generally not fully accounted for in the mental budget, leading to overspending.

Although consumers might not be aware of these biases when making financial decisions, they are important because firms can take advantage of them to attract consumers. For

²³ Richard Thaler, "Some Empirical Evidence on Dynamic Inconsistency," *Economic Letters*, vol. 8 (1981), pp. 201-207.

²⁴ Kungl. Vetenskapsakademien: The Royal Swedish Academy of Sciences, *Richard H. Thaler: Integrating Economics with Psychology*, Scientific Background on the Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel 2017, October 3, 2017, pp. 10-14, at <https://www.nobelprize.org/uploads/2018/06/advanced-economicsciences2017-1.pdf>.

²⁵ H.M. Shefrin and Richard Thaler, "An Economic Theory of Self-Control," *Journal of Political Economy*, vol. 89, no. 2 (April 1981), pp. 392-406.

²⁶ Sendhil Mullainathan and Eldar Shafir, *Scarcity: Why Having Too Little Means So Much* (Henry Holt and Company, 2013).

²⁷ Mark Muraven and Roy F. Baumeister, "Self-Regulation and Depletion of Limited Resources: Does Self-Control Resemble a Muscle?" *Psychological Bulletin*, vol. 126, no. 2 (2000), pp. 247-259.

²⁸ Richard Thaler, "Mental Accounting and Consumer Choice," *Marketing Science*, vol. 4, no. 3, Summer, 1985, pp. 199-214; Richard Thaler, "Mental Accounting Matters," *Journal of Behavioral Decision Making*, July 19, 1999; C. Yiwei Zhang and Abigail B. Sussman, "Perspectives on Mental Accounting: An Exploration of Budgeting and Investing," *Financial Planning Review*, vol. 1, no. 1011 (2018).

²⁹ Kungl. Vetenskapsakademien: The Royal Swedish Academy of Sciences, *Richard H. Thaler: Integrating Economics with Psychology*, Scientific Background on the Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel 2017, October 3, 2017, pp. 7-10, at <https://www.nobelprize.org/uploads/2018/06/advanced-economicsciences2017-1.pdf>.

³⁰ Abigail B. Sussman and Adam L. Alter, "The Exception Is the Rule: Underestimating and Overspending on Exceptional Expenses," *Journal of Consumer Research*, December 2012.

example, choice architecture biases might influence how marketing materials are developed, emphasizing certain terms to make a financial product seem more desirable to consumers. In addition, product features may be developed to take advantage of people's present bias, scarcity mindset, or mental accounting mistakes.

Common Policy Interventions and Considerations

In response to market failures, such as information asymmetry and behavioral biases, the government uses policy interventions ideally to bring consumer markets to a more efficient market outcome. Three types of policy interventions are common in consumer finance:

- **Standardized Consumer Disclosures**—Financial products can be complex and difficult for consumers to fully understand. Mandated consumer disclosures are a common policy intervention in consumer financial markets, generally intended to give consumers more information about the costs and terms before they take out a new financial product, thus reducing asymmetric information market failures. Standardized disclosures can also help consumers shop for the best terms, because all financial product terms are required to be disclosed in the same way. Lastly, because disclosure structure and formatting are often standardized, mandated consumer disclosures also can take into account choice architecture biases. Laws that mandate consumer disclosures in financial markets include the Truth in Lending Act (TILA),³¹ which requires standardized disclosures for certain consumer credit products, and the Truth in Savings Act,³² which requires standardized disclosures for certain bank accounts.
- **Unfair, Deceptive, or Abusive Practices or Acts**—Consumers seeking loans or financial services could be vulnerable because some consumers may lack financial knowledge or be susceptible to biases described in the above section. For this reason, certain consumer protection laws prohibit unfair, deceptive, or abusive acts or practices in consumer financial markets.³³ These acts and practices can include both individual firm conduct and product features.³⁴
- **Fair Lending**—Fair lending laws prohibit discrimination in credit transactions based upon certain borrower characteristics, such as sex, race, religion, and age. These laws historically have been interpreted to prohibit both intentional discrimination and *disparate impact* discrimination, in which a facially neutral business decision has a discriminatory effect on a protected class.³⁵ Federal fair

³¹ P.L. 90-321; 15 U.S.C. §1601.

³² P.L. 102-242; 12 U.S.C. §4301.

³³ P.L. 111-203, §1031; CFPB, “Prohibition of Unfair, Deceptive, or Abusive Acts or Practices in the Collection of Consumer Debts,” bulletin 2013-07, July 10, 2013, at <https://www.consumerfinance.gov/policy-compliance/guidance/supervisory-guidance/bulletin-prohibition-practices-collection-consumer-debts/>.

³⁴ For more information on the trade-offs relating to product feature regulation, see John Campbell, *Restoring Rational Choice: The Challenge of Consumer Financial Regulation*, NBER, Working Paper no. 22025, February 2016, pp. 29-37.

³⁵ The Supreme Court's reasoning in a June 2015 decision involving the Fair Housing Act, another federal antidiscrimination law, has sparked debate about whether disparate impact claims are permissible under the Equal Credit Opportunity Act. For background on disparate impact claims, see CRS Report R44203, *Disparate Impact Claims Under the Fair Housing Act*, by David H. Carpenter. For more information on the Fair Housing Act, see CRS Report 95-710, *The Fair Housing Act (FHA): A Legal Overview*, by David H. Carpenter.

lending laws in consumer financial markets include the Equal Credit Opportunity Act (ECOA),³⁶ the Fair Housing Act (FHA),³⁷ and the Home Mortgage Disclosure Act (HMDA).³⁸

Policy Considerations

The market effects of new laws or regulations are important considerations. Does the policy on average lead the market closer or further from its efficient market outcome? In consumer financial markets, both households and firms may react to new policy. Without thinking through all of its potential impacts, a policy can also have unintended effects, and perhaps fail to reach policymakers' objectives.

From a consumer perspective, new policy formulations should consider the policy's effect on consumer decisionmaking, the impact on household well-being over time, and whether these effects might vary across the population. For example, a new disclosure policy might improve consumer comprehension, but not consumer decisionmaking, thus failing to affect the market as intended. In other cases, a subset of consumers may be susceptible to a deceptive practice. If a new policy eliminates that deceptive practice in the market, the policy may only affect that subset of consumers who were susceptible, rather than the whole consumer population.

From a firm's perspective, new policy formulation should consider both the cost for firms to implement the policy as well as its impact on the competitiveness of the market, both within and outside of the regulated market. Another important consideration is the policy's impact on consumer prices and financial product availability. For example, complying with a new regulation might require a firm to bear costs. This might force lenders to raise prices or lenders who cannot bear the additional costs may leave the market. Higher prices and less choice may result in consumers seeking other credit products outside of the market, or reduce consumers' ability to access credit.

Consumer Financial Protection Bureau (CFPB)

Most experts agree that an important factor in the 2008 financial crisis was a housing bubble, which led lenders to relax their underwriting standards (or the process by which a lender determines whether a borrower is creditworthy), which in some cases, led to consumer protection abuses.³⁹ In response, the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) established the CFPB to implement and enforce federal consumer financial law while ensuring consumers can access financial products and services.⁴⁰ The CFPB's statutory purpose is to enable markets for consumer financial services and products to be fair, transparent, and competitive.⁴¹ Dodd-Frank consolidated certain consumer finance-related responsibilities in the CFPB previously held by other regulators and created new authorities unique to the CFPB.⁴²

³⁶ 15 U.S.C. §1691.

³⁷ 42 U.S.C. §3601. For more information, see CRS Report R44557, *The Fair Housing Act: HUD Oversight, Programs, and Activities*, by Libby Perl.

³⁸ 12 U.S.C. §2801.

³⁹ Financial Crisis Inquiry Commission, *Financial Crisis Inquiry Report: Final Report of the Nation Commission on the Causes of the Financial and Economic Crisis in the United States*, January 2011, p. xxiii & 418, at http://fcic-static.law.stanford.edu/cdn_media/fcic-reports/fcic_final_report_full.pdf.

⁴⁰ P.L. 111-203.

⁴¹ 12 U.S.C. §5511.

⁴² For more information on the CFPB, see CRS In Focus IF10031, *Introduction to Financial Services: The Consumer*

The act also directed the CFPB to develop and implement financial education initiatives, collect consumer complaints, and conduct consumer finance research.

The CFPB generally has regulatory authority over providers of an array of consumer financial products and services, including deposit taking, mortgages, credit cards and other extensions of credit, loan servicing, consumer reporting data collection, and consumer debt collection. The authorities that the CFPB may exercise and the breadth of products, services, and entities that fall within its jurisdiction are considerable, but Dodd-Frank imposes some important exceptions to and limitations on those powers.⁴³ The CFPB's authorities fall into three broad categories: *rulemaking*, writing regulations to implement laws under its jurisdiction; *supervision*, the power to examine and impose reporting requirements on financial institutions; and *enforcement* of various consumer protection laws and regulations.

The CFPB is authorized to prescribe regulations to implement 19 federal consumer protection laws that largely predated Dodd-Frank.⁴⁴ These *enumerated consumer laws* govern a broad and diverse set of consumer financial services and generally apply to any entity engaged in the business of offering those services. Dodd-Frank also provided CFPB new power to issue rules declaring certain acts or practices associated with consumer financial products and services to be unlawful because they are unfair, deceptive, or abusive. Other aspects of the CFPB's regulatory power—particularly the scope of its supervisory and enforcement authority—vary depending on a number of factors, including an institution's size and whether it holds a bank charter.

The CFPB is headed by a director appointed by the President with the advice and consent of the Senate for a five-year term. It is located within the Federal Reserve System (Fed), although the Fed does not influence the CFPB's budget or personnel decisions. The Fed also cannot veto a rule issued by the CFPB, but the Financial Stability Oversight Council, of which the Fed Chairman is a member, can overturn a CFPB rule with the vote of two-thirds of its members.⁴⁵ The CFPB is funded through the earnings of the Fed, rather than through the typical appropriations process. The CFPB requests monetary transfers from the Fed with a cap on the amount of these transfers

Financial Protection Bureau (CFPB), by Cheryl R. Cooper and David H. Carpenter.

⁴³ Dodd-Frank exempts some industries from the CFPB's regulatory jurisdiction. The CFPB generally does not have rulemaking, supervisory, or enforcement authority over automobile dealers; merchants, retailers, and sellers of nonfinancial goods and services; real estate brokers; real estate agents; sellers of manufactured and mobile homes; income tax preparers; insurance companies; or accountants. Certain business practices of these entities, however, could trigger CFPB regulatory authority, such as if they engage in an activity governed by an enumerated consumer law.

⁴⁴ The enumerated consumer laws are: the Alternative Mortgage Transaction Parity Act, 12 U.S.C. §§3801 et seq.; the Consumer Leasing Act of 1976, 15 U.S.C. §§1667 et seq.; the Electronic Funds Transfer Act, 15 U.S.C. §§1693 et seq., except with respect to section 920; the Equal Credit Opportunity Act, 15 U.S.C. §§1691 et seq.; the Fair Credit Billing Act, 15 U.S.C. §§1666 et seq.; the Fair Credit Reporting Act, 15 U.S.C. §§1681 et seq., except with respect to sections 1681m(e) and 1681w; the Homeowners Protection Act of 1998, 12 U.S.C. §§4901 et seq.; the Fair Debt Collection Practices Act, 15 U.S.C. §§1692 et seq.; subsections (b) through (f) of section 43 of the Federal Deposit Insurance Act, 12 U.S.C. §§ 1831t(c)-(f); sections 502 through 509 of the Gramm-Leach-Bliley Act, 15 U.S.C. §§6802-6809, except for section 6805 as it applies to section 6801(b); the Home Mortgage Disclosure Act of 1975, 12 U.S.C. §§2801 et seq.; the Home Ownership and Equity Protection Act of 1994, 15 U.S.C. §1639; the Real Estate Settlement Procedures Act of 1974, 12 U.S.C. §§2601 et seq.; the S.A.F.E. Mortgage Licensing Act of 2008, 12 U.S.C. §§5101 et seq.; the Truth in Lending Act (TILA), 15 U.S.C. §§1601 et seq.; the Truth in Savings Act, 12 U.S.C. §§4301 et seq.; section 626 of the Omnibus Appropriations Act, 2009, P.L. 111-8 §626; the Interstate Land Sales Full Disclosure Act, 15 U.S.C. §§1701 et seq.; and many provisions of the Mortgage Reform and Anti-Predatory Lending Act, Dodd-Frank Act Title XIV, Subtitles A, B, C, and E, and §§1471, 1472, 1475, and 1476.

⁴⁵ The Financial Stability Oversight Council (FSOC) is a collaborative body that brings together the expertise of federal financial regulators, a presidentially appointed independent insurance expert, and representatives of state financial regulators. For more information on FSOC, see CRS Report R45052, *Financial Stability Oversight Council (FSOC): Structure and Activities*, by Marc Labonte.

based on a formula set in statute. For FY2020, the CFPB's \$580 million budget was below its \$696 million cap.⁴⁶

Overview of Major Consumer Finance Markets

The following sections examine specific issues within major consumer debt markets: mortgage lending, student loans, automobile loans, credit cards and payments, payday loans and other credit alternative financial products, and checking accounts and substitutes. The markets discussed are under the jurisdiction of the CFPB, and sometimes other regulators as well. Each section briefly describes the financial product, recent market developments, and selected policy issues that may lead each market away from its efficient price or outcomes. These sections focus on the consumer and household perspective as well as consumer protection policy issues in each market.

Mortgage Lending Market

A mortgage loan is a loan collateralized by a house and its land.⁴⁷ Generally, consumers use these loans to purchase a new home or refinance an existing one. These types of mortgages are often called first liens, because if a consumer defaults on the loan, the lender is typically the first in line to be compensated through the proceeds of a home foreclosure. First-lien mortgage loans are usually installment loans, in which the consumer pays off the loan in monthly installments over 15 years or 30 years. Most mortgage loans in the United States have a fixed interest rate and fixed installment amount over the course of the loan, affected by the consumer's credit score and market conditions.⁴⁸

Households buying a new home and taking out a mortgage loan to purchase it generally cannot borrow for the full cost of the house's value. To limit the risk to the lender, borrowers are typically required to make a down payment, the difference between the house's value and the mortgage loan. If the down payment is less than 20% of the home's value, the borrower is often required to pay for additional insurance.

In addition to first-lien purchase mortgages, a consumer may choose to take out a home equity line of credit (often referred to as HELOC) or a smaller installment mortgage loan, which often is a second lien. A second lien means that the lender is second in line, after the first lien holder, to be compensated if the consumer defaults and the home is foreclosed upon. These loans are underwritten using the value of the home, but can be used for a variety of different purposes either related to the home or not. For example, second mortgages can be used to renovate the home, pay for college, or consolidate credit card debts.

Mortgage loans are by far the largest consumer credit market in the United States, and homes are a large part of most households' wealth. According to the Fed, more than \$9 trillion of mortgage debt is currently outstanding,⁴⁹ and more than \$20 trillion in real estate equity is owned by

⁴⁶ CFPB, *Fiscal Year 2020: Annual Performance Plan and Report, and Budget Overview*, February 2020, pp. 7, 15, at https://files.consumerfinance.gov/f/documents/cfpb_performance-plan-and-report_fy20.pdf.

⁴⁷ For more information on the U.S. mortgage market, see CRS Report R42995, *An Overview of the Housing Finance System in the United States*, by N. Eric Weiss and Katie Jones; and CRS Report R45710, *Housing Issues in the 116th Congress*, coordinated by Katie Jones.

⁴⁸ Some mortgages have variable interest rates and installments that are not fixed, such as balloon payments.

⁴⁹ Federal Reserve Bank of New York, Center for Microeconomic Data, *Quarterly Report on Household Debt and Credit*, at <https://www.newyorkfed.org/microeconomics/databank.html>.

households.⁵⁰ As of the third quarter of 2020, 67.4% of U.S. households owned their home.⁵¹ Many people view homeownership as an important way to build wealth over time, both through price appreciation and home equity by paying down their mortgage. Nevertheless, because home prices can fluctuate over time, this investment can be risky, especially if the home owner only stays in the home for a short time. Although homeownership has certain benefits, such as tax benefits like the mortgage interest tax deduction,⁵² it also imposes costs on the household, such as mortgage loan closing costs and home maintenance.

As noted above, most experts believe that a housing price bubble was a central cause of the 2008 financial crisis. In response, Dodd-Frank reformed the mortgage market by attempting to strengthen mortgage underwriting standards, to reduce the risk that consumers' default on their mortgages, even if house prices fluctuated in the future. Dodd-Frank also directed the CFPB to update federal mortgage disclosure forms (called the combined TILA/RESPA form)⁵³ and improve standards for mortgage servicing (a company who manages mortgage loans after the loan is originated).⁵⁴

During and after the financial crisis, mortgage lenders tightened underwriting standards, making it harder for consumers to qualify for a loan.⁵⁵ Although most borrowers with good credit scores continued to qualify for mortgage credit, other borrowers in weaker financial positions found it more difficult to obtain a mortgage.⁵⁶ As the economy has recovered from the Great Recession, concerns exist about whether new consumer compliance regulation in the mortgage market has struck the right balance between prudent mortgage underwriting and access to credit for potential borrowers to build wealth.⁵⁷ Certain features of mortgages during the mortgage boom that were considered to be particularly risky, such as teaser interest rates and loans with little or no income verification, are now uncommon in the mortgage market.⁵⁸ However, research suggests that the regulation of underwriting standards may have caused lenders to prefer certain borrowers, such as those with lower debt-to-income ratios.⁵⁹

Mortgage shopping is another policy issue in this market. Consumers do not tend to shop among lenders for more advantageous mortgage interest rates, even though large price differences exist

⁵⁰ Federal Reserve Board, *B.101: Balance Sheet of Households and Nonprofit Organizations: Households; Owners' Equity in Real Estate*, Q2 2020, at <https://www.federalreserve.gov/apps/fof/DisplayTable.aspx?t=b.101>.

⁵¹ Census Bureau, *Quarterly Residential Vacancies and Homeownership, Third Quarter 2020*, CB20-153, October 27, 2020, p. 1, at <https://www.census.gov/housing/hvs/files/current/hvspread.pdf>.

⁵² For more information, see CRS Report R46429, *An Economic Analysis of the Mortgage Interest Deduction*, by Mark P. Keightley.

⁵³ RESPA stands for Real Estate Settlement Procedures Act (12 U.S.C. §§2601-2617).

⁵⁴ Mortgage servicing activities may include collecting consumer mortgage payments, payment of taxes and insurance from borrower escrow accounts, and modifying or supporting the foreclosure process on mortgages when they default. For more information, see CRS Insight IN11377, *Mortgage Servicing Rights and Selected Market Developments*, by Darryl E. Getter.

⁵⁵ Bing Bai, Laurie Goodman, and Jun Zhu, *Housing and Housing Finance*, Urban Institute, Urban Wire: The Blog of the Urban Institute, January 27, 2016, at <https://www.urban.org/urban-wire/tight-credit-standards-prevented-52-million-mortgages-between-2009-and-2014>.

⁵⁶ Bing Bai, Laurie Goodman, and Jun Zhu, *Housing and Housing Finance*.

⁵⁷ For example, one notable mortgage underwriting regulation implemented after the financial crisis is the Qualified Mortgage (QM) rule. For more information, CRS In Focus IF11413, *The Qualified Mortgage (QM) Rule and the QM Patch*, by Darryl E. Getter.

⁵⁸ CFPB, *Ability-to-Repay and Qualified Mortgage Rule Assessment Report*, January 2019, p. 9, at https://files.consumerfinance.gov/f/documents/cfpb_ability-to-repay-qualified-mortgage_assessment-report.pdf.

⁵⁹ CFPB, *Ability-to-Repay and Qualified Mortgage Rule Assessment Report*, p. 10.

in the market. According to the CFPB, nearly half of all borrowers only seriously consider one lender or broker before taking out a mortgage.⁶⁰ Given the range of interest rates available to a consumer at any given time, the CFPB estimates that a consumer could save thousands of dollars on a mortgage by shopping for the best interest rates.⁶¹

More recently, the COVID-19 pandemic has impacted the mortgage market. Many consumers who would likely have experienced difficulty repaying their mortgage loans received *loan forbearance*.⁶² Loan forbearance plans can prevent a consumer from becoming delinquent, giving the consumer time to repay the debts owed rather than potentially experiencing adverse consequences, such as credit score declines or foreclosure.⁶³ As previously mentioned, the CARES Act established consumer rights to be granted forbearance for federally backed mortgages for up to a year. The CARES Act's consumer protections and financial institutions' loan forbearance programs arguably helped avoid sharp increases in loan delinquencies by making it possible for many loans to receive forbearance during the spring and summer of 2020.⁶⁴ However, when these programs expire, some consumers may fall delinquent on their loans, impacting the mortgage market. In addition, during the second and third quarters of 2020, mortgage debt balances increased as interest rates reached historic lows, causing more mortgage refinances and other mortgage finance activity.⁶⁵

Student Loans

Student loans allow students and their families to pay for postsecondary education expenses while they are enrolled in school.⁶⁶ Education is an investment intended to allow students to earn higher incomes after they complete school and throughout the rest of their careers. In general, student loans are paid back in installments—for example, a fixed payment every month for 10 years. Student loan debt has doubled in the past decade.⁶⁷ Since 2010, student loan debt has been the second-largest category of consumer debt, after mortgage debt.⁶⁸ In academic year 2018-2019, the

⁶⁰ CFPB, *Consumers' Mortgage Shopping Experience: A First Look at Results from the National Survey of Mortgage Borrowers*, January 2015, p. 10, at https://files.consumerfinance.gov/f/201501_cfpb_consumers-mortgage-shopping-experience.pdf.

⁶¹ CFPB, *Consumers' Mortgage Shopping Experiences*, p. 8.

⁶² For more information on consumer loan forbearance during the COVID-19 pandemic, including CARES Act rights to forbearance, regulatory guidance, and impacts on consumers and financial institutions, see CRS Report R46356, *COVID-19: Consumer Loan Forbearance and Other Relief Options*, coordinated by Cheryl R. Cooper; and CRS Insight IN11359, *COVID-19: Financial Relief and Assistance Resources for Consumers*, by Maura Mullins and Jennifer Teefy.

⁶³ Loans in forbearance are not classified as delinquent, although they may be driven by similar underlying circumstances for the borrower.

⁶⁴ For more information about consumer debt during the pandemic, see CRS Report R46578, *COVID-19: Household Debt During the Pandemic*, coordinated by Cheryl R. Cooper.

⁶⁵ Andrew F. Haughwout et al., *A Monthly Peek into Americans' Credit During the COVID-19 Pandemic*, Federal Reserve Bank of New York, Liberty Street Economics, August 6, 2020, at <https://libertystreeteconomics.newyorkfed.org/2020/08/a-monthly-peek-into-americans-credit-during-the-covid-19-pandemic.html>.

⁶⁶ For more information on federal student loan debt, see CRS In Focus IF10158, *A Snapshot of Federal Student Loan Debt*, by David P. Smole.

⁶⁷ Federal Reserve Bank of New York, *Quarterly Report on Household Debt and Credit*.

⁶⁸ Federal Reserve Bank of New York, *Quarterly Report on Household Debt and Credit*.

average amount of student loan debt for a bachelor's degree recipient who borrowed funds to complete her degree was \$28,800.⁶⁹

Unlike other consumer financial markets, most student loans are originated and owned by the federal government. In general, these federal loans are accessible to large portions of the postsecondary student population and their families with limited underwriting of their creditworthiness, estimated future income, or other estimates of their ability to repay the loan. The Department of Education (ED) manages most of the federal student loan programs.⁷⁰ Congress sets interest rates and other loan terms and conditions in statute each year. ED contracts out student loan servicing, sets servicing standards in these contracts, and enforces these servicing standards. The CFPB is the primary regulator for private student loan lending and servicing and has also asserted a role in ensuring compliance with consumer protection laws related to the servicing of federal student loans.⁷¹

From a regulatory perspective, policymakers continue to debate what role the CFPB should play in the federal student loan industry. Consumer groups advocate for more active CFPB enforcement of consumer protection standards in federal student loan servicing. However, because ED already assumes a significant role in how its contractors service federal student loans—and taxpayers are responsible for additional servicing costs and default risk for nonpayment—some have questioned the need for the CFPB to regulate in the same space.

A major concern in the student loan market is whether students are able to manage their debt after graduation. Moreover, unlike other consumer debts, student loans are generally not dischargeable during a bankruptcy proceeding except in limited circumstances.⁷² These concerns have led to efforts to make loan repayment terms more flexible. For example, some federal student loan borrowers now have the option to choose income-driven repayment plans, under which a borrower's monthly loan payments are based on a percentage of the borrower's discretionary income. Loan forgiveness programs have also been developed and expanded in recent years, especially for borrowers in public service occupations. ED manages several of the student loan forgiveness and repayment loan programs.⁷³ Reports suggest issues in the implementation of these programs that make it difficult for borrowers to know their options, understand the process, and qualify for forgiveness or repayment loan programs.⁷⁴

Questions have also arisen regarding student loan availability and whether loans should be limited to certain types of educational programs that enable their students to gain quality employment and successfully pay back their loans.⁷⁵ Many students make school choice and

⁶⁹ College Board, *Trends in College Pricing and Student Aid 2020*, Trends in Higher Education Series, 2020, p. 4, at <https://trends.collegeboard.org/sites/default/files/2018-trends-in-student-aid.pdf>.

⁷⁰ For more information on federal student loan programs, see CRS Report R44845, *Administration of the William D. Ford Federal Direct Loan Program*, by Alexandra Hegji.

⁷¹ 12 C.F.R. §1090.106.

⁷² For more information on student loans and bankruptcy, see CRS Report R45113, *Bankruptcy and Student Loans*, by Kevin M. Lewis; and CRS Legal Sidebar LSB10192, *How Hard Should it be to Discharge a Student Loan in Bankruptcy?* by Kevin M. Lewis.

⁷³ For more information, see CRS Report R43571, *Federal Student Loan Forgiveness and Loan Repayment Programs*, coordinated by Alexandra Hegji.

⁷⁴ For more information, see CRS Report R45389, *The Public Service Loan Forgiveness Program: Selected Issues*, by Alexandra Hegji; and CFPB, *Annual Report of the CFPB Student Loan Ombudsman*, October 2017, at https://files.consumerfinance.gov/f/documents/cfpb_annual-report_student-loan-ombudsman_2017.pdf.

⁷⁵ Stephanie Riegg Cellini and Nicholas Turner, "Gainfully Employed? Assessing the Employment and Earnings of For-Profit College Students Using Administrative Data," *Journal of Human Resources*, vol. 54, no. 2 (Spring 2019),

curriculum decisions at a young age, when they might not have much experience making financial decisions.⁷⁶ In addition, information on program quality and student employment outcomes after graduation is limited. These information asymmetry problems can make it difficult for students to make good financial decisions for their future career.⁷⁷ Questions also exist about the extent to which student loan access causes tuition prices to rise.⁷⁸ For example, if access to student loans makes it easier for schools to raise tuition, then it might lead to some students being worse off.⁷⁹ Some question whether the availability of student loans might harm the larger economy. For example, researchers debate the effect of student loan debt on future macroeconomic performance, including effects on career choice, family formation, home ownership, and retirement savings.⁸⁰

More recently, the COVID-19 pandemic has impacted the student loan market. As previously mentioned, Section 3513 of the CARES Act suspended all payments due and interest accrual for all loans made under the Direct Loan program and the Federal Family Education Loan program held by the Department of Education through September 30, 2020. Since the expiration of this law, the Trump Administration has administratively set the federal student loan interest rate to zero, and borrowers have not been required to make payments due on their loans, currently through January 2020.⁸¹ These policies have likely helped some consumers who might have had trouble paying their federal student loans during the COVID-19 pandemic. However, when these programs expire, some consumers may fall delinquent on their student loans.

Automobile Loans

An automobile (auto) loan allows a consumer to finance the cost of a new or used car.⁸² Auto loans are usually structured as installment loans, in which a consumer pays a fixed amount of money each month for a predetermined time period, frequently three to seven years. Lenders

pp. 342-370; Tiffany Chou, Adam Looney, and Tara Watson, *Measuring Loan Outcomes at Postsecondary Institutions: Cohort Repayment Rates as an Indicator of Student Success and Institutional Accountability*, NBER, Working Paper no. 23118, February 2017.

⁷⁶ Student loan borrowers may face difficulties in understanding their loan terms and conditions. For more information see U.S. Financial Literacy and Education Commission, *Best Practices for Financial Literacy and Education at Institutions of Higher Education*, 2019, at <https://home.treasury.gov/system/files/136/Best-Practices-for-Financial-Literacy-and-Education-at-Institutions-of-Higher-Education2019.pdf>.

⁷⁷ Justine Hastings, Christopher A. Neilson, and Seth D. Zimmerman, *The Effects of Earnings Disclosure on College Enrollment Decisions*, NBER, Working Paper no. 21300, February 2018.

⁷⁸ For more information, see CRS Report R43692, *Overview of the Relationship between Federal Student Aid and Increases in College Prices*, by Adam Stoll, David H. Bradley, and Shannon M. Mahan.

⁷⁹ David O. Lucca, Taylor Nadauld, and Karen Shen, *Credit Supply and the Rise in College Tuition: Evidence from the Expansion in Federal Student Aid Programs*, Federal Reserve Bank of New York, Staff Report no. 733, February 2017; Stephanie Riegg Cellini and Claudia Goldin, “Does Federal Student Aid Raise Tuition? New Evidence on For-Profit Colleges,” *American Economic Journal: Economic Policy*, vol. 6, no. 4 (November 2014), pp. 174-206.

⁸⁰ Some examples of this literature include: Marco Di Maggio, Ankit Kalda, and Vincent Yao, *Second Chance: Life without Student Debt*, NBER, Working Paper no. 25810, May 2019; Katharine G. Abraham et al., *Behavioral Effects of Student Loan Repayment Plan Options on Borrowers’ Career Decisions: Theory and Experimental Evidence*, NBER, Working Paper no. 24804, July 2018; and Holger M. Mueller and Constantine Yannelis, *Students in Distress: Labor Market Shocks, Student Loan Default, and Federal Insurance Programs*, NBER, Working Paper no. 23284, March 2017.

⁸¹ For more information about federal student loan debt relief in the context of COVID-19, see CRS Report R46314, *Federal Student Loan Debt Relief in the Context of COVID-19*, by Alexandra Hegji.

⁸² For more information on the auto lending market, see CRS In Focus IF11192, *The Automobile Lending Market and Policy Issues*, by Cheryl R. Cooper.

often require consumers to make a down payment to obtain the loan. Auto loans are secured by the automobile, so if a consumer cannot pay the loan, the lender can repossess the car to recoup the loan's cost.

Auto loans are the third-largest consumer credit market. At the end of 2020, 114 million consumers—roughly 45% American adults—had an auto loan, and auto loan debt outstanding totaled almost \$1.4 trillion.⁸³ According to the CFPB, terms of auto loans have increased recently. In 2009, 26% of auto loans originated were for six or more years, whereas in 2017, these loans constituted 42% of originations.⁸⁴ This trend may be due in part to rising vehicle costs⁸⁵ and consumers keeping their cars longer.⁸⁶

Reportedly, most auto loans are arranged at the auto dealership where the car is purchased, referred to as the indirect auto financing market.⁸⁷ Indirect auto financing involves the auto dealer forwarding information about the prospective borrower to one or more lenders to solicit potential financing offers.⁸⁸ The dealer is often compensated for originating the loan through a discretionary markup, which is the difference between the lender's interest rate and the rate a consumer is charged. The lender may cap the possible size of the dealer markup (e.g., 2.5%) to limit the loan from becoming too susceptible to default. Auto dealers and consumers can negotiate the loan's interest rate within this range, and therefore indirectly determine how much to compensate the auto dealer for the convenience of arranging the loan.⁸⁹

Alternatively, consumers can go directly to a bank, credit union, or other lender for an auto loan before making their purchases, avoiding the dealer markup cost.⁹⁰ Consumers may prefer arranging auto financing through an auto dealer or directly through a lender, depending on their

⁸³ Federal Reserve Bank of New York, Center for Microeconomic Data, *Quarterly Report of Household Debt and Credit*, 2020:Q3, November 2020, Underlying Data Appendix p.3-4, at <https://www.newyorkfed.org/microeconomics/databank.html>.

⁸⁴ Kenneth P. Brevoort et al., "Growth in Longer-Term Auto," CFPB, *Quarterly Consumer Credit Trends*, November 2017, p. 4, at https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_consumer-credit-trends_longer-term-auto-loans_2017Q2.pdf.

⁸⁵ David Pan, "Used-Car Prices Hit a 13-Year High as More Late-Model Cars Come Off Lease," *USA Today*, June 19, 2018, at <https://www.usatoday.com/story/money/cars/2018/06/15/used-cars-price-hit-record-high/700362002/>.

Adrienne Roberts, "Used-Car Sales Boom as New Cars Get Too Pricey for Many," *Wall Street Journal*, September 23, 2018, at <https://www.wsj.com/articles/used-car-sales-boom-as-new-cars-get-too-pricey-for-many-1537700401>.

⁸⁶ "Make Your Car Last 200,000 Miles; How to Go the Distance and Save Tens of Thousands of Dollars," *Consumer Reports*, November 6, 2018, at <https://www.consumerreports.org/car-repair-maintenance/make-your-car-last-200-000-miles/>.

⁸⁷ CFPB, *Consumer Voices on Automobile Financing*, June 2016, p. 6, at https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201606_cfpb_consumer-voices-on-automobile-financing.pdf.

⁸⁸ CFPB, "What is the Difference Between Dealer-Arranged and Bank Financing?" November 16, 2016, at <https://www.consumerfinance.gov/ask-cfpb/what-is-the-difference-between-dealer-arranged-and-bank-financing-en-759/>.

⁸⁹ CFPB, "What is the Difference Between Dealer-Arranged and Bank Financing?"

⁹⁰ Some auto dealerships extend credit themselves, called "Buy Here, Pay Here," commonly marketing to consumers with subprime or no credit history. These dealers do not work on behalf of other lenders, but keep the loans on their books. These loans tend to have higher interest rates and be more expensive for consumers. For more information see CFPB, "What is a "No Credit Check" or "Buy Here, Pay Here" Auto Loan?" June 8, 2016, at <https://www.consumerfinance.gov/ask-cfpb/what-is-a-no-credit-check-or-buy-here-pay-here-auto-loan-en-887/>.

If a consumer cannot pay cash for a new or used car, the consumer also has the option to lease the car. In a leasing arrangement, the consumer pays for the right to drive the car for a fixed period of time, often three years. Unlike an auto loan, the consumer does not own the car. Leasing arrangements are not considered consumer loans and, therefore, are not regulated like auto loans.

preferences regarding convenience, cost, and other factors. In either case, the lender usually owns the loan and can service it itself or through a third-party company.⁹¹

In the indirect auto financing market, the dealer markup arrangement can incentivize the auto dealer to negotiate—and profit from—a higher interest rate with the consumer. The auto dealer may also choose the lender who compensates it the most—for example, the lender that allows the largest markup, rather than the lender offering the best terms for the consumer. Although other consumer credit markets include markups, it is less common for bank or credit union lenders to allow an outside broker in the transaction discretion as to the amount of the markup. For example, while the Real Estate Settlement Procedures Act⁹² restricts such practices in the mortgage market, after reports of mortgage brokers steering customers to more expensive loans due to “kickbacks”—unearned fees for a referral—in the lead-up to the financial crisis, Congress in 2010 took actions to further restrict these practices.⁹³

The information asymmetry in the indirect auto finance market sometimes can lead to higher prices for consumers. Consumers are not always aware that they can negotiate on loan terms when obtaining dealer-arranged financing.⁹⁴ For this reason, many consumers do not shop for auto loans.⁹⁵ Consumers’ lack of awareness—combined with auto dealers’ discretion on markups—may leave them vulnerable to bad actors, making the auto loan market uncompetitive.

The CFPB oversees consumer protection compliance for auto lenders, but not for auto dealers’ typical activities. Dodd-Frank states that “the Bureau may not exercise any [authority] over a motor vehicle dealer that is predominantly engaged in the sale and servicing of motor vehicles, the leasing and servicing of motor vehicles, or both.”⁹⁶ The scope of this exclusion continues to be debated, given the key role auto dealers play in the auto lending market.

In 2013, the CFPB issued a controversial bulletin providing guidance to indirect auto lenders on how to comply with the Equal Credit Opportunity Act (ECOA).⁹⁷ This guidance generally stated that indirect auto lenders should impose controls on or revise and monitor dealer markups to ensure they do not result in disparate impact based on race or other protected classes. From 2013 to 2016, the CFPB, in coordination with the Department of Justice, issued consent orders to settle enforcement actions against American Honda Finance Corporation, Toyota Motor Credit Corporation, Fifth Third Bank, and Ally Financial & Ally Bank for ECOA violations in indirect auto lending markets.⁹⁸ The CFPB generally alleged that these institutions violated ECOA by

⁹¹ CFPB, “What is the Difference Between Dealer-Arranged and Bank Financing?” at <https://www.consumerfinance.gov/ask-cfpb/what-is-the-difference-between-dealer-arranged-and-bank-financing-en-759/>.

⁹² 12 U.S.C. §§2601-2617.

⁹³ P.L. 111-203, §1403.

⁹⁴ CFPB, *Consumer Voices on Automobile Financing*, June 2016, p. 17, at https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201606_cfpb_consumer-voices-on-automobile-financing.pdf.

⁹⁵ CFPB, *Consumer Voices on Automobile Financing*, pp. 17, 22.

⁹⁶ P.L. 111-203, §1029; 12 U.S.C. §5519.

⁹⁷ CFPB, *Indirect Auto Lending and Compliance with the Equal Credit Opportunity Act*, CFPB Bulletin 2013-02, March 21, 2013, at https://files.consumerfinance.gov/f/201303_cfpb_march_-Auto-Finance-Bulletin.pdf.

⁹⁸ CFPB, *CFPB and DOJ Reach Resolution with Honda to Address Discriminatory Auto Loan Pricing*, July 14, 2015, at <https://www.consumerfinance.gov/about-us/newsroom/cfpb-and-doj-reach-resolution-with-honda-to-address-discriminatory-auto-loan-pricing/>; *CFPB and DOJ Reach Resolution With Toyota Motor Credit To Address Loan Pricing Policies With Discriminatory Effects*, February 2, 2016, at <https://www.consumerfinance.gov/about-us/newsroom/cfpb-and-doj-reach-resolution-with-toyota-motor-credit-to-address-loan-pricing-policies-with-discriminatory-effects/>; CFPB, *CFPB Takes Action Against Fifth Third Bank for Auto-Lending Discrimination and Illegal Credit Card Practices*, September 28, 2015, at <https://www.consumerfinance.gov/about-us/newsroom/cfpb->

permitting their dealers to charge markups that resulted in disparate impacts on the basis of race and ethnicity. Auto lenders generally do not collect information on the race or ethnicity of borrowers. In the absence of direct evidence, the CFPB used a new proxy methodology, a statistical method developed for estimating race and ethnicity using geography and surname-based information.⁹⁹ Although this method may not be able to flawlessly identify race or ethnicity for an individual, aggregate, company-wide estimates of disparate impacts are much more precise. In general, these institutions did not admit or deny the allegations as part of the consent orders but, among other things, paid monetary penalties and agreed to limit their markups to reduce these alleged disparities.

The CFPB's indirect auto lender guidance and the resulting enforcement actions were the subject of significant attention and debate. For example, some expressed the view that the guidance went beyond what ECOA and the Dodd-Frank Act require of auto lenders, while others considered it an important step toward addressing discrimination.¹⁰⁰ In 2018, Congress rescinded the guidance pursuant to the Congressional Review Act.¹⁰¹ Nevertheless, some observers argue that discrimination in auto lending markups continues to be an area of concern.¹⁰²

More recently, the economic impacts of the COVID-19 pandemic have caused some consumers to experience difficulty repaying their auto loans. In response, many financial institutions voluntarily offered loan forbearance and other financial relief options for affected consumers. According to the CFPB, auto loans receiving payment assistance increased from about 1.5% in February 2020 to about 3% in June 2020.¹⁰³ During the pandemic, credit standards for auto loans have tightened and demand for cars has gone down.¹⁰⁴ Yet, despite these negative impacts on the auto lending market, some industry observers are optimistic about future industry growth after concerns about the COVID-19 pandemic dissipate and macroeconomic conditions improve.¹⁰⁵

takes-action-against-fifth-third-bank-for-auto-lending-discrimination-and-illegal-credit-card-practices/; CFPB, *CFPB and DOJ Order Ally to Pay \$80 Million to Consumers Harmed by Discriminatory Auto Loan Pricing*, December 20, 2013, at <https://www.consumerfinance.gov/about-us/newsroom/cfpb-and-doj-order-ally-to-pay-80-million-to-consumers-harmed-by-discriminatory-auto-loan-pricing/>.

⁹⁹ CFPB, *Using Publicly Available Information to Proxy for Unidentified Race and Ethnicity: A Methodology and Assessment*, 2014, at https://files.consumerfinance.gov/f/201409_cfpb_report_proxy-methodology.pdf.

¹⁰⁰ Neil Haggerty, "Trump Makes Repeal of CFPB Auto Lending Rule Official," *American Banker*, May 21, 2018.

¹⁰¹ P.L. 104-121.

¹⁰² U.S. Congress, House Committee on Financial Services, Subcommittee on Oversight and Investigations, *Examining Discrimination in the Automobile Loan and Insurance Industries*, 116th Cong., 1st sess., May 1, 2019.

¹⁰³ The CFPB calculates payment assistance "as an account being reported with a zero scheduled payment due despite a positive balance." The CFPB notes that "the variation in the incidence of consumer assistance reported... may have as much to do with how furnishers in each market report to the [credit bureaus] as it does with the incidence of actual assistance." Ryan Sandler and Judith Ricks, *Household Debt and Credit*, August 2020, pp. 13-15. Other sources calculate estimates differently than the CFPB, and report different percentages. For example, Transunion creates a broader metric called "accounts in hardship," which includes loans "affected by natural/declared disaster, accounts reported as in forbearance, accounts reported as deferred or payment due amount removal, or freezing of account status and/or past due amount." Transunion reports 7.2% of auto accounts in hardship in June 2020. See Transunion, *Monthly Industry Snapshot: Financial Services*, at <https://www.transunion.com/monthly-industry-snapshot-fs>.

¹⁰⁴ According to the Federal Reserve's senior loan officer survey in the summer and fall of 2020, banks tightened credit standards for all types of household lending, including auto loans, see Board of Governors of the Federal Reserve System, *Senior Loan Officer Opinion Survey on Bank Lending Practices*, July and October 2020, at <https://www.federalreserve.gov/data/sloos.htm>; Anthony Gambardella, *Auto Leasing, Loans & Sales Financing in the US*, IBIS World, US Industry (NAICS) Report 52222, September 2020.

¹⁰⁵ Anthony Gambardella, *Auto Leasing, Loans & Sales Financing in the US*, IBIS World, US Industry (NAICS) Report 52222, September 2020.

Credit Cards and Payments

Retail payment services allow consumers to pay merchants for goods and services without cash, sometimes called a payment *transaction*.¹⁰⁶ Consumers can use these services to pay bills, make person-to-person payments, or withdraw cash. These services can be found in many consumer financial products, including credit, debit, and prepaid cards and checking accounts. Given the rise of internet shopping, retail payment services have become especially critical for consumers to be able to make daily purchases. The most common methods of payment are debit cards, credit cards, and cash, respectively.¹⁰⁷ Debit and prepaid cards generally are associated with a funded account from which the consumer draws money to pay for transactions. In contrast, credit cards allow a consumer to pay for transactions using credit.

According to the CFPB, at the end of 2018, just under 170 million consumers, roughly two-thirds of the U.S. adult population, had a credit card.¹⁰⁸ Credit cards provide consumers with unsecured revolving credit, meaning the loan is not secured with any collateral if the consumer defaults (and thus, the lender has no recourse to seize any property connected to the loan in case of consumer default). In some cases, credit cards are used for payment transaction convenience and paid in full each month without incurring interest. These types of users are sometimes called *transactors*. In other cases, credit card users borrow money up to a *credit limit* and make only a *minimum payment* (generally a small portion of the outstanding balance) on the debt each month, incurring interest on the unpaid balance. These types of credit card users are called *revolvers*. In 2018, average percentage rates for general purpose credit cards were just under 18%.¹⁰⁹ Although a consumer can move between transacting and revolving, consumers tend to show persistent payment behavior.¹¹⁰ According to a Fed survey, roughly half of consumers transact and half revolve.¹¹¹

Credit cards are valuable to consumers in part because they are flexible—both the amount borrowed and the amount paid can vary each month according to the consumer’s needs. For example, if a household experiences a financial shock, such as unemployment or a car or house repair, the household can use credit cards to borrow money quickly and easily, which the household can then pay back when it is able. Credit cards can also be used to smooth consumption over time, which may be particularly valuable to households with tight budgets.¹¹²

¹⁰⁶ For more information on consumer payment services, see CRS Report R43364, *Recent Trends in Consumer Retail Payment Services Delivered by Depository Institutions*, by Darryl E. Getter; and CRS Report R45927, *U.S. Payment System Policy Issues: Faster Payments and Innovation*, by Cheryl R. Cooper, Marc Labonte, and David W. Perkins.

¹⁰⁷ Kevin Foster, Claire Greene, and Joanna Stavins, *The 2019 Survey of Consumer Payment Choice: Summary Results*, Federal Reserve Bank of Atlanta, Research Data Reports, No. 20-3, 2020, p. 12, at <https://www.frbatlanta.org/banking-and-payments/consumer-payments/survey-of-consumer-payment-choice/2019-survey>.

¹⁰⁸ CFPB, *The Consumer Credit Card Market*, August 2019, p. 33, at <https://www.consumerfinance.gov/data-research/research-reports/the-consumer-credit-market-2019/>.

¹⁰⁹ CFPB, *The Consumer Credit Card Market*, August 2019, p. 55.

¹¹⁰ Benjamin J. Keys and Jialan Wang, “Minimum Payments and Debt Paydown in Consumer Credit Cards,” *Journal of Financial Economics*, 2018, pp. 528-548; and Daniel Grodzicki and Sergei Kulaev, *Data Point: Credit Card Revolvers*, CFPB, Office of Research, July 2019, pp. 8-10, at <https://www.consumerfinance.gov/data-research/research-reports/data-point-credit-card-revolvers/>.

¹¹¹ Federal Reserve Board, *Report on the Economic Well-Being of U.S. Households in 2019*, Featuring Supplemental Data from April 2020, May 2020, p. 29, at <https://www.federalreserve.gov/newsevents/pressreleases/other20200514a.htm>.

¹¹² Daryl Collins et al., *Portfolios of the Poor: How the World’s Poor Live on \$2 a Day* (Princeton, NJ: Princeton University Press, 2009), Chapter 3 & 7.

However, credit cards also are structured in a way that can take advantage of many consumer decisionmaking biases, which can result in households incurring debt. For example, mental accounting biases can lead to overspending, and credit cards allow households to overspend easily, perhaps without even realizing it until their monthly bill is due. Research suggests that the half of credit card holders who are persistently in credit card debt are likely to be present biased and have little liquid savings.¹¹³

The type of information disclosed in a typical credit card statement may play an important role in how revolving consumers repay credit card debt. Research suggests that many people are anchored by the minimum payment amounts included in each statement, which bias their decisions about how much to pay each month.¹¹⁴ Specifically, the research suggests these consumers are either paying the minimum payment or employing heuristics to pay near the minimum (e.g., twice the minimum or \$20 above the minimum).¹¹⁵ This cue may unconsciously influence consumers to make a lower payment than they otherwise would.

For these reasons, the Credit Card Accountability Responsibility and Disclosure Act of 2009 (CARD Act) established new disclosure requirements for credit cards.¹¹⁶ The CARD Act changed the periodic disclosure credit card companies are required to make to consumers to include information on how long it will take to pay off a consumer's debt if the consumer makes only the minimum payment. The disclosure also now includes the amount a consumer would have to pay to repay the debt in three years and how much interest the consumer would save by paying the debt off in three years compared with the minimum payment. These changes in the disclosure requirements were intended to nudge consumers to pay more on their credit cards each month, but research suggests that the changes did not have as big of an effect on consumer payment behavior as intended, in part because online portals—which have become a popular method of credit card payment—are not required to contain these disclosures.¹¹⁷

More recently, the economic impacts of the COVID-19 pandemic have caused some consumers to experience difficulty repaying their credit cards. In response, many financial institutions voluntarily offered loan forbearance and other financial relief options for affected consumers. According to the CFPB, credit card loans in forbearance increased from about 1.5% in February 2020 to about 3.5% in June 2020.¹¹⁸ In addition, evidence suggests that credit card markets may

¹¹³ Scott Fulford and Scott Schuh, *Credit Card Utilization and Consumption Over the Life Cycle and Business Cycle*, Federal Reserve Bank of Boston, Research Department Working Paper, no. 17-14 (2017), pp. 4-5.

¹¹⁴ Benjamin Keys and Jialan Wang, "Minimum Payments and Debt Paydown in Consumer Credit Cards," *Journal of Financial Economics*, vol. 131, no. 3 (March 2019), pp. 528-548.

¹¹⁵ Benjamin Keys and Jialan Wang, "Minimum Payments and Debt Paydown in Consumer Credit Cards," pp. 528-548.

¹¹⁶ P.L. 111-24. For more information on the CARD Act, see CRS Report R43364, *Recent Trends in Consumer Retail Payment Services Delivered by Depository Institutions*, by Darryl E. Getter, p. 3.

¹¹⁷ CFPB, *CARD Act Report: A Review of the Impact of the CARD Act on the Consumer Credit Card Market*, October 1, 2013, pp. 66-68, at https://files.consumerfinance.gov/f/201309_cfpb_card-act-report.pdf; and Glenn B. Canner and Gregory Elliehausen, *Consumer Experiences with Credit Cards*, Board of Governors of the Federal Reserve System, Federal Reserve Bulletin, December 2013, p. 20, at <https://www.federalreserve.gov/pubs/bulletin/2013/pdf/consumer-experiences-with-credit-cards-201312.pdf>.

¹¹⁸ The CFPB calculates payment assistance "as an account being reported with a zero scheduled payment due despite a positive balance." The CFPB notes that "the variation in the incidence of consumer assistance reported... may have as much to do with how furnishers in each market report to the [credit bureaus] as it does with the incidence of actual assistance." Ryan Sandler and Judith Ricks, *Household Debt and Credit*, August 2020, pp. 13-15. Other sources calculate estimates differently than the CFPB, and report different percentages. For example, Transunion creates a broader metric called "accounts in hardship," which includes loans "affected by natural/declared disaster, accounts reported as in forbearance, accounts reported as deferred or payment due amount removal, or freezing of account status

have tightened during the pandemic. Notably, credit card balances declined sharply during the second quarter by about \$76 billion, the largest quarterly decline on record.¹¹⁹ The CFPB finds credit card balance declines “across all groups, including consumers residing in both high- and low-income census tracts,” possibly due to a decline in consumer spending.¹²⁰ Although evidence suggests limited reductions in credit card limits, the COVID-19 pandemic has also likely led to more credit card account closures and fewer credit-limit increases.¹²¹ If limited access to credit continues, it could make it more difficult for consumers to make large purchases, harming the economic recovery.

Payday and Other Credit Alternative Financial Products¹²²

When consumers face financial shocks, such as unemployment or a car repair, sometimes they need credit to manage the unforeseen event. One option a consumer may access is a short-term, small-dollar loan, which tends to be outstanding for a short period of time and for a small amount of money, generally less than \$1,000. Banks and credit unions sometimes provide these types of loans through cash advances or checking account overdraft programs. Many consumers, often those with a low credit score or no credit history, also turn to alternative financial products from a nonbank institution to provide credit when needed. Alternative financial products include payday loans, pawn shop loans, auto title loans, and other types of products from nonbank providers. According to the Federal Deposit Insurance Corporation (FDIC), in 2019, 4.8% used a credit alternative financial service in the past year.¹²³ Households that did not use bank credit in the past year are more likely to be lower-income and a racial or ethnic minority compared to the general U.S. population.¹²⁴

Perhaps the best known of these products are payday loans, which have been the subject of significant regulatory, congressional, and media attention. Payday loans are structured as short-term advances that allow consumers to access cash before they receive a paycheck. These loans are designed to be paid back on a consumer’s next payday. Payday loans are offered through storefront locations or online for a set fee. The underwriting of these loans is minimal, with consumers required to provide little more than a paystub and checking account information to take out a loan. Rather than paying off the loan entirely when it is due, many consumers roll over

and/or past due amount.” Transunion reports 3.6% of credit card loans in hardship in June 2020. See Transunion, *Monthly Industry Snapshot: Financial Services*, at <https://www.transunion.com/monthly-industry-snapshot-fs>.

¹¹⁹ Federal Reserve Bank of New York, *Household Debt and Credit (Based on New York Fed Consumer Credit Panel)*, Center for Microeconomic Data, Q3 2020, at <https://www.newyorkfed.org/microeconomics/hhdc/background.html>.

¹²⁰ Ryan Sandler and Judith Ricks, *The Early Effects of the COVID-19 Pandemic on Consumer Credit*, CFPB, CFPB Office of Research Special Issue Brief, August 2020, p. 3, at <https://www.consumerfinance.gov/data-research/research-reports/special-issue-brief-early-effects-covid-19-pandemic-on-consumer-credit/>.

¹²¹ Ryan Sandler and Judith Ricks, “Household Debt and Credit,” August 2020, p. 3; and Larry Santucci, “How Has the COVID-19 Pandemic Affected the Supply of Consumer Credit? A Preliminary Look at the U.S. Credit Card Market,” Federal Reserve Bank of Philadelphia, Consumer Finance Institute Special Report, August 2020, p. 3, at <https://www.philadelphiafed.org/consumer-finance/consumer-credit/how-has-the-covid-19-pandemic-affected-the-supply-of-consumer-credit>.

¹²² For more background on short-term, small-dollar loans, see CRS Report R44868, *Short-Term, Small-Dollar Lending: Policy Issues and Implications*, by Darryl E. Getter. For more background on financial inclusion and credit access policy issues, see CRS Report R45979, *Financial Inclusion and Credit Access Policy Issues*, by Cheryl R. Cooper.

¹²³ Mark Kutzbach et al., *How America Banks: Household Use of Banking and Financial Services, 2019 FDIC Survey*, FDIC, October 2020, p. 8, at <https://www.fdic.gov/analysis/household-survey/2019execsum.pdf>.

¹²⁴ Mark Kutzbach et al., 2019 *FDIC Survey*, p. 8.

or renew these loans.¹²⁵ Sequences of continuous roll overs may result in consumers being in debt for an extended period. Because consumers generally pay a fee for each new loan, payday loans can become expensive.

In 2010, the Dodd-Frank Act authorized the CFPB to oversee payday lenders for the first time at the federal level,¹²⁶ but prohibited the CFPB from imposing an interest rate limit on any type of credit, including payday loans.¹²⁷ As of July 2020, 18 states and the District of Columbia either ban or limit the interest rates on these loans.¹²⁸

In the payday market, policy disagreements tend to center on balancing access to credit with consumer protection. The academic research is mixed in terms of payday loans' effect on consumer well-being.¹²⁹ When consumers have emergencies, short-term, small-dollar credit can help them make ends meet. Payday loans' product features, such as the option to roll over, can allow consumers to pay back their loan flexibly, but also can play into cognitive biases, including present biases and scarcity tunnel vision. Some consumers pay off payday loans quickly, but a sizable minority are in debt for a long period of time—a CFPB study found 36% of new payday loan sequences were repaid fully without rollovers, while 15% of sequences extended for 10 or more loans.¹³⁰

In October 2017, during the leadership of then-Director Richard Cordray,¹³¹ the CFPB finalized a rule covering payday and other small-dollar, short-term loans.¹³² The 2017 rule asserts that it is “an unfair and abusive practice” for a lender to make certain types of short-term, small-dollar loans “without reasonably determining that consumers have the ability to repay the loans.” The rule would have mandated underwriting provisions for short-term, small-dollar loans unless made with certain features. In July 2020, the CFPB under Trump-appointed Director Kathy Kraninger issued a final rule that rescinds the mandatory underwriting provisions before the 2017 final rule went into effect.¹³³ The 2020 rule would leave unchanged other parts of the 2017 rule, such as other payment provisions relating to protections for consumers paying back these loans.

Given the concerns about consumer harm from payday and other small-dollar, short-term loans, some financial institutions are interested in exploring other loan models that try to give consumers access to credit for short-term needs at a lower-cost and with an easier repayment process. For this reason, prudential regulators, such as the Office of the Comptroller of the Currency (OCC) and the FDIC, have encouraged banks to offer small-dollar credit products to

¹²⁵ According to CFPB research, 64% of payday loans in their sample were rolled over after the initial loan. For more information, see Kathleen Burke et al., *CFPB Data Point: Payday Lending*, CFPB's Office of Research, March 2014, pp. 10-11, at https://files.consumerfinance.gov/f/201403_cfpb_report_payday-lending.pdf.

¹²⁶ P.L. 111-203, §1023.

¹²⁷ P.L. 111-203, §1027.

¹²⁸ According to CFPB, “Payday, Vehicle Title, and Certain High-Cost Installment Loans,” 85 *Federal Register* 44382, July 22, 2020, p. 44383.

¹²⁹ According to CFPB, “Payday, Vehicle Title, and Certain High-Cost Installment Loans,” 84 *Federal Register* 4252, February 14, 2019, pp. 4292-4294; and CFPB, “Payday, Vehicle Title, and Certain High-Cost Installment Loans,” 82 *Federal Register* 54472, November 17, 2017, pp. 54842-54846.

¹³⁰ Kathleen Burke et al., *CFPB Data Point: Payday Lending*, CFPB's Office of Research, March 2014, pp. 10-11, at https://files.consumerfinance.gov/f/201403_cfpb_report_payday-lending.pdf.

¹³¹ Director Cordray was appointed by President Obama.

¹³² 12 C.F.R. §§1041.1-1041.14.

¹³³ For more information, see CRS Insight IN11059, *CFPB Finalizes New Payday Lending Rule, Reversing Prior Regulation*, by Cheryl R. Cooper.

consumers.¹³⁴ However, it is unclear whether these different types of products can improve outcomes for consumers compared to payday loans, given that the population of consumers these products would target and those consumers' biases concerning money management are likely similar.¹³⁵

Checking Accounts and Substitutes

Checking accounts allow consumers to deposit money and make payments, for example, using bill pay and paper checks. Frequently, a checking account includes access to a debit card, to increase a consumer's ability to make payment transactions through the account. Checking accounts are generally provided by a bank or credit union, and consumers' deposits are government insured (up to a certain amount) against the institution's failure.¹³⁶

In the past decade or so, the availability of free or low-cost checking accounts has reportedly diminished, and fees associated with checking accounts have grown.¹³⁷ The most common fees that checking account consumers incur are overdraft and non-sufficient fund fees.¹³⁸ Consumers can incur an overdraft when they transact below their account balance, and the bank or credit union covers the negative balance for the consumer for a fee. In general, negative balance episodes are short in duration. According to the CFPB, half of all episodes last three or fewer days, and more than three-quarters last a week or less.¹³⁹

Overdraft services can help consumers pay bills on time. However, overdraft fees can be costly, particularly for consumers who are inattentive or tend to overspend due to tight budgets and mental accounting biases.¹⁴⁰ CFPB research suggests that a small number of checking account holders incur most overdraft fees, with 8.3% of consumers overdrafting more than 10 times per year and accounting for 73.7% of overdraft fees.¹⁴¹ According to the CFPB, these frequent overdrafters tend to be more credit constrained, have lower credit scores, and are less likely to have a general-purpose credit card than the general U.S. population.¹⁴²

In 2009, a provision of the CARD Act required consumers to affirmatively opt in for overdraft coverage of ATM withdrawals and nonrecurring debit card transactions.¹⁴³ Since this requirement

¹³⁴ Board of Governors of the Federal Reserve System, FDIC, National Credit Union Administration, Office of the Comptroller of the Currency, *Interagency Lending Principles for Offering Responsible Small-Dollar Loans*, May 2020, at <https://www.occ.gov/news-issuances/news-releases/2020/nr-ia-2020-65a.pdf>.

¹³⁵ For example, deposit advance products, small-dollar loans that some banks used to provide with checking accounts, showed similar outcomes to payday loans. See CFPB, *Payday Loans and Deposit Advance Products: A White Paper of Initial Data Findings*, April 24, 2013, pp. 43-45, at https://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf.

¹³⁶ For more information on checking accounts, see CRS Report R43364, *Recent Trends in Consumer Retail Payment Services Delivered by Depository Institutions*, by Darryl E. Getter.

¹³⁷ CFPB, *Study of Overdraft Programs: A white paper of initial data findings*, June 2013, pp. 15-17, at https://files.consumerfinance.gov/f/201306_cfpb_whitepaper_overdraft-practices.pdf.

¹³⁸ Trevor Bakker et al., *Data Point: Checking Account Overdraft*, CFPB, July 2014, p. 5, at https://files.consumerfinance.gov/f/201407_cfpb_report_data-point_overdrafts.pdf.

¹³⁹ Trevor Bakker et al., *Data Point: Checking Account Overdraft*, p. 22.

¹⁴⁰ For more background on overdraft services, see CRS In Focus IF11460, *Overdraft: Payment Service or Small-Dollar Credit?* by Andrew P. Scott.

¹⁴¹ Trevor Bakker et al., *Data Point: Checking Account Overdraft*, p. 11.

¹⁴² David Low et al., *Data Point: Frequent Overdrafters*, CFPB, August 2017, p. 5, at https://files.consumerfinance.gov/f/documents/201708_cfpb_data-point_frequent-overdrafters.pdf.

¹⁴³ The opt-in rules do not cover checks or automatic bill payments.

was implemented, opt-in rates have tended to vary by bank, from single-digit percentages to more than 40% within particular institutions.¹⁴⁴ Frequent overdrafters who opt in to overdraft services seem to have similar characteristics to those who do not opt in, but tend to pay more in fees.¹⁴⁵ Given this research, consumer advocates have raised concerns about whether overdraft programs are sufficiently transparent and whether consumers receive sufficient disclosures regarding these programs. Advocates have also questioned how financial institution practices influence the opt-in decision.¹⁴⁶

Overdrafts may be caused by the lapse of time between payment authorization, account settlement, and when funds are available to the consumer.¹⁴⁷ Because of these time lapses in the payments system, some consumers may not realize no funds are available when they overdraft their account.¹⁴⁸ For this reason, some argue that a faster payment system or other financial planning products may help consumers keep better track of their balances, preventing overdrafts.¹⁴⁹

Overdraft fees may lead to involuntary checking account closures, leaving some households without access to a bank account. According to the FDIC, in 2019, 5.4% of households were *unbanked*, meaning that no one in the household had a checking or savings account from an insured institution.¹⁵⁰ Unbanked households tend to have lower incomes and are more likely to be racial or ethnic minorities than the general U.S. population.¹⁵¹ The main reasons households cite for not having a bank account include insufficient account funds, not trusting banks, privacy concerns, and high account fees.¹⁵² Moreover, in 2019, 17.2% households used nonbank financial transaction services outside of the banking system, such as money orders or check cashing services.¹⁵³ Certain observers contend that financial outcomes for the unbanked and underbanked would be improved if banks—which may be a more stable source of relatively inexpensive financial services relative to certain alternatives—were more active in serving these customers. For this reason, policymakers and observers will likely continue to explore ways to make banking more accessible to a greater portion of the population.¹⁵⁴ However, it may be expensive for banks to serve these customers—for example, they might have low balance accounts. At least some of these consumers may be served better by alternative financial providers if their products are less expensive or if they provide more customer service than banks.

¹⁴⁴ CFPB, *Study of Overdraft Programs: A white paper of initial data findings*, June 2013, p. 5, at https://files.consumerfinance.gov/f/201306_cfpb_whitepaper_overdraft-practices.pdf.

¹⁴⁵ David Low et al., *Data Point: Frequent Overdrafters*, pp. 30-35.

¹⁴⁶ CFPB, *Study of Overdraft Programs: A white paper of initial data findings*, pp. 17-18.

¹⁴⁷ For more information on how the payment system can cause overdrafts, see CFPB *Study of Overdraft Programs: A white paper of initial data findings*, pp. 42-48.

¹⁴⁸ CFPB, *Study of Overdraft Programs: A white paper of initial data findings*, pp. 42-48.

¹⁴⁹ CFPB, *Consumer Insights on Managing Spending*, February 2017, pp. 19-25, at https://www.consumerfinance.gov/documents/2664/201702_cfpb_Consumer-Insights-on-Managing-Spending.pdf. For more information on faster payment system policy issues, see CRS Report R45927, *U.S. Payment System Policy Issues: Faster Payments and Innovation*, by Cheryl R. Cooper, Marc Labonte, and David W. Perkins.

¹⁵⁰ Mark Kutzbach et al., *How America Banks: Household Use of Banking and Financial Services, 2019 FDIC Survey*, FDIC, October 2020, p. 1, at <https://www.fdic.gov/analysis/household-survey/2019execsum.pdf>.

¹⁵¹ Mark Kutzbach et al., 2019 *FDIC Survey*, p. 1.

¹⁵² Mark Kutzbach et al., 2019 *FDIC Survey*, p. 3.

¹⁵³ Mark Kutzbach et al., 2019 *FDIC Survey*, p. 6.

¹⁵⁴ For more information on access to bank account policy issues, see CRS In Focus IF11631, *Financial Inclusion: Access to Bank Accounts*, by Cheryl R. Cooper.

General-purpose prepaid cards may be considered an alternative to a traditional checking account, and they can be obtained through a bank, at retail stores, or online. These cards can be used in payment networks, such as Visa and MasterCard. General purpose, reloadable prepaid cards generally have features similar to debit and checking accounts, such as the ability to pay bills electronically, get cash at an ATM, make purchases at stores or online, and receive direct deposits. However, unlike checking accounts, prepaid card funds are not always federally insured against an institution's failure. Prepaid cards often have a monthly maintenance fee and other particular service fees, such as for using an ATM or reloading cash. Some banks offer prepaid cards, yet unbanked consumers are much more likely to use a prepaid card from a store or website that is not a bank.¹⁵⁵

Overview of Consumer Finance Market Support Systems

Although each consumer credit market is unique, certain common aspects of the consumer credit system facilitate the pricing of credit offers and the resolution of delinquencies and defaults for most consumer credit markets. This section discusses two of what this report will refer to as market support systems: the consumer credit reporting system (which helps lenders price consumer loans) and the debt collection market (which helps lenders to collect upon consumer default). Notably, in both these market support systems, consumers do not have the ability to choose the financial institution or entity with whom they engage, and therefore are unable to take their business elsewhere if issues arise. For this reason, when consumer abuses occur in these markets, consumer protection laws and regulations may be particularly important. According to the CFPB, credit reporting and debt collection are the consumer finance markets with by far the most complaints, together accounting for 65% of the total complaints the agency received in 2019 (44% and 21%, respectively).¹⁵⁶

Credit Reporting, Credit Bureaus, and Credit Scoring¹⁵⁷

The consumer data industry collects information on consumers, such as financial payment history data, to predict their future financial product performance.¹⁵⁸ This industry includes financial firms who report on consumers' payment behaviors, credit bureaus who collect and store this information, and credit scoring companies that use this data to develop algorithms to predict consumers' future payment behaviors. The three largest credit bureaus—Equifax, Experian, and TransUnion—provide credit reports nationwide.¹⁵⁹ The consumer data industry is important because it significantly affects consumer access to financial products or opportunities. For

¹⁵⁵ For more information on prepaid cards, see CRS Report R43364, *Recent Trends in Consumer Retail Payment Services Delivered by Depository Institutions*, by Darryl E. Getter.

¹⁵⁶ CFPB, *Consumer Response Annual Report: January 1 – December 31, 2019*, March 2020, p. 9, at <https://www.consumerfinance.gov/data-research/research-reports/2019-consumer-response-annual-report/>.

¹⁵⁷ For more information on the consumer data industry, see CRS Report R44125, *Consumer Credit Reporting, Credit Bureaus, Credit Scoring, and Related Policy Issues*, by Cheryl R. Cooper and Darryl E. Getter.

¹⁵⁸ The consumer data industry is also used outside of consumer credit markets, for example, for pricing insurance, renting an apartment, and screening potential employees.

¹⁵⁹ For a list of consumer reporting agencies, see CFPB, "List of Consumer Reporting Agencies," at <https://www.consumerfinance.gov/consumer-tools/credit-reports-and-scores/consumer-reporting-companies/companies-list/>.

example, negative or derogatory information on a credit report, such as information stating that a consumer has paid late or defaulted on a loan, may influence a lender to deny a consumer access to credit.

The main statute regulating the credit reporting industry is the Fair Credit Reporting Act (FCRA),¹⁶⁰ enacted in 1970. The FCRA requires “that consumer reporting agencies adopt reasonable procedures for meeting the needs of commerce for consumer credit ... in a manner which is fair and equitable to the consumer, with regard to the confidentiality, accuracy, relevancy, and proper utilization of such information.”¹⁶¹ Among other things, the FCRA establishes permissible uses of credit reports and imposes certain responsibilities on those who collect, furnish, and use the information contained in consumers’ credit reports.

The FCRA also includes consumer protection provisions. Under the FCRA, a lender must advise a consumer when the lender has used their information from a credit reporting agency (CRA) in taking an adverse action (generally a denial of credit) against the consumer.¹⁶² That information must be disclosed free of charge. Consumers have a right to one free credit report every year (from each of the three largest nationwide credit reporting providers) even in the absence of an adverse action (e.g., credit denial). Consumers also have the right to dispute inaccurate or incomplete information in their reports. After a consumer alerts a CRA of such a discrepancy, the CRA must investigate and correct errors, usually within 30 days. The FCRA also limits the length of time negative information may remain on credit reports. Negative debt collection information typically stays on credit reports for 7 years, even if the consumer pays in full for the item in collection; information about a personal bankruptcy stays on a credit report for a maximum of 10 years.¹⁶³

The CFPB has rulemaking and enforcement authorities over all CRAs in connection with certain consumer protection laws, including the FCRA; it also has supervisory authority, or the authority to conduct examinations, over the larger CRAs. In July 2012, the CFPB announced that it would supervise CRAs with \$7 million or more in annual receipts, which included 30 firms representing approximately 94% of the market.¹⁶⁴

Inaccurate or disputed consumer data within the credit bureaus’ data reports is an ongoing concern in this market. Inaccurate information in a credit report may limit a consumer’s access to credit in some cases or increase the costs to the consumer of obtaining credit in others. In response to this concern, the CFPB has encouraged credit bureaus and financial institutions to improve data accuracy in credit reporting. In 2017, the CFPB released a report of its supervisory work in the credit reporting system.¹⁶⁵ The report discusses the CFPB’s efforts to work with credit bureaus and financial institutions to improve credit reporting in three specific areas: data accuracy, dispute handling and resolution, and furnisher reporting. As the report describes, credit bureaus and financial firms have developed data governance and quality control programs to

¹⁶⁰ 15 U.S.C. §1681.

¹⁶¹ 15 U.S.C. §1681.

¹⁶² See Federal Trade Commission (FTC), *A Summary of your Rights Under the Fair Credit Reporting Act*, at <https://www.consumer.ftc.gov/articles/pdf-0096-fair-credit-reporting-act.pdf>.

¹⁶³ CFPB, “How Long does Negative Information Remain on My Credit Report?” Ask CFPB, August 4, 2016, at <https://www.consumerfinance.gov/ask-cfpb/how-long-does-negative-information-remain-on-my-credit-report-en-323/>.

¹⁶⁴ CFPB, “CFPB to Supervise Credit Reporting,” press release, July 16, 2012, at <http://www.consumerfinance.gov/newsroom/consumer-financial-protection-bureau-to-supervise-credit-reporting/>.

¹⁶⁵ CFPB, *Supervisory Highlights Consumer Reporting Special Edition*, Issue 14, winter 2017, at https://files.consumerfinance.gov/f/documents/201703_cfpb_Supervisory-Highlights-Consumer-Reporting-Special-Edition.pdf.

monitor data accuracy through working with the CFPB. In addition, the CFPB has encouraged credit bureaus to improve their dispute and resolution processes, including making them easier and more informative for consumers.¹⁶⁶

When credit reporting disputes arise, consumers sometimes find it difficult to advocate for themselves because they are not aware of their rights and how to exercise them. According to a CFPB report, some consumers are confused about what credit reports and scores are, find it challenging to obtain credit reports and scores, and struggle to understand the contents of their credit reports.¹⁶⁷ The CFPB provides financial education resources on its website to help educate consumers about their rights regarding consumer reporting. The credit bureaus' websites also provide information about how to dispute inaccurate information, and consumers can contact the credit bureaus by phone or mail. However, debates continue regarding whether these efforts are enough to ensure that consumers can effectively advocate for themselves.

Some consumers may have trouble accessing the credit reporting system.¹⁶⁸ The CFPB estimates that credit scores cannot be generated for approximately 20% of the U.S. population due to their limited credit histories.¹⁶⁹ Many of these consumers are young. For example, the CFPB estimated that 40% of these consumers are under 25 years old.¹⁷⁰ Moreover, a disproportionate share of these consumers are black or Hispanic.¹⁷¹ Consumers without a credit record have trouble accessing credit, but without access to credit, a consumer cannot establish a credit record. In general, there are two ways that policymakers tend to consider approaching this issue; either by (1) expanding uptake of financial products reported in the current system, or (2) expanding the types of information in the credit reporting system using alternative data.¹⁷²

More recently, the economic impacts of the COVID-19 pandemic have caused some consumers to experience difficulty repaying their loans, potentially impacting their credit reports. Section 4021 of the CARES Act protects the credit histories of consumers with forbearance agreements. It requires furnishers during the COVID-19 pandemic covered period to report to the credit bureaus that consumers are current on their credit obligations if they enter into an agreement to defer, forbear, modify, make partial payments, or get any other assistance on their loan payments from a financial institution and fulfill those requirements, provided they were current before this

¹⁶⁶ The credit bureaus' efforts to make disputes easier and more informative for consumers include (1) online portals to submit disputes and upload supporting documentation; (2) improvements to their call center scripts and training regarding solicitation of relevant information from consumers with disputes; (3) no longer requiring that consumers obtain or purchase a recent consumer report before investigations; and (4) notice to consumers of dispute results, including investigation results. CFPB, *Supervisory Highlights Consumer Reporting Special Edition*, Winter 2017, pp. 9-11.

¹⁶⁷ CFPB, *Consumer Voices on Credit Reports and Scores*, February 2015, at https://files.consumerfinance.gov/f/201502_cfpb_report_consumer-voices-on-credit-reports-and-scores.pdf.

¹⁶⁸ For more information on credit access policy issues, see CRS Report R45979, *Financial Inclusion and Credit Access Policy Issues*, by Cheryl R. Cooper.

¹⁶⁹ See Kenneth P. Brevoort, Philipp Grimm, and Michelle Kambara, *Data Point: Credit Invisibles*, CFPB, May 2015, p. 6, at http://files.consumerfinance.gov/f/201505_cfpb_data-point-credit-invisibles.pdf.

¹⁷⁰ Brevoort, Grimm, and Kambara, *Data Point: Credit Invisibles*, p. 14.

¹⁷¹ Brevoort, Grimm, and Kambara, *Data Point: Credit Invisibles*, pp. 16-23.

¹⁷² Alternative data generally refers to information used to determine a consumer's creditworthiness that the national consumer reporting agencies—Equifax, Experian, and TransUnion—do not traditionally use to calculate a credit score. These reporting agencies generally create consumer reports containing historical information about repayment on credit products such as mortgages, student loans, credit cards, and auto loans. Credit applications, bankruptcies, and debts in collection also are regularly included. For more information, see CRS In Focus IF11630, *Alternative Data in Financial Services*, by Cheryl R. Cooper.

period.¹⁷³ Although the CARES Act protects the credit histories of consumers with forbearance agreements, some consumers may still experience harm to their credit record because lenders can choose whether to enter into an assistance agreement for many types of consumer loans.

Debt Collection and Bankruptcy¹⁷⁴

When a consumer defaults on a debt, a third-party debt collector often collects the debt obligation rather than the lender to whom the debt is originally owed. These debt collectors by contract receive a share of the amount collected on behalf of the original lender or buy the debt obligation in full.¹⁷⁵ In general, a robust debt collection market allows lenders to recoup their losses to the maximum extent possible after a consumer defaults on a loan, generally making consumer credit and other related markets more efficient. When lenders can effectively recoup their losses, they may be more willing to lend to consumers at lower initial loan costs, leading to more access to credit for consumers.

Many Americans experience debt collection. According to a CFPB survey, about one-third of consumers with a credit bureau file reported being contacted in the last year by at least one creditor or collector trying to collect on one or more debts.¹⁷⁶ Consumers with lower incomes and non-prime credit scores were more likely to report experience with debt collection than consumers with higher incomes and prime credit scores.¹⁷⁷ In 2019, debt from unpaid loans or other financial services accounted for close to 40% of debt collection revenue.¹⁷⁸ The other over 60% of debt collection revenue includes medical,¹⁷⁹ telecom, utility and other retail debt.

¹⁷³ If the consumer was delinquent before the covered period, then the furnisher should maintain the delinquent status unless the consumer brings the account or obligation current. The covered period starts on January 31, 2020, and extends to the later of 120 days after enactment or 120 days after the national emergency declared by the President on March 13, 2020, terminates. For more information, see CFPB, *Statement on Supervisory and Enforcement Practices Regarding the Fair Credit Reporting Act and Regulation V in Light of the CARES Act*, April 1, 2020, at https://files.consumerfinance.gov/f/documents/cfpb_credit-reporting-policy-statement_cares-act_2020-04.pdf.

¹⁷⁴ For more information on the debt collection market and related policy issues, see CRS Report R46477, *The Debt Collection Market and Selected Policy Issues*, by Cheryl R. Cooper.

¹⁷⁵ CFPB, *Fair Debt Collection Practices Act*, March 2020, pp. 8-10, at <https://www.consumerfinance.gov/data-research/research-reports/fair-debt-collection-practices-act-annual-report-2020/>.

¹⁷⁶ CFPB, *Consumer Experiences with Debt Collection: Findings from the CFPB's Survey of Consumer Views on Debt*, January 2017, p. 5, at https://files.consumerfinance.gov/f/documents/201701_cfpb_Debt-Collection-Survey-Report.pdf.

¹⁷⁷ CFPB, *Consumer Experiences with Debt Collection*, pp. 15-16.

¹⁷⁸ Rohan Jaura, *Debt Collection Agencies in the US*, IBIS World, Industry Report 56144, December 2019, p. 16.

¹⁷⁹ Medical debt collection raises specific policy issues related to inconsistent billing and reporting practices. According to the CFPB study, consumers are unlikely to know how much various medical services cost in advance, particularly those associated with accidents and emergencies. See CFPB, *Consumer Credit Reports: A Study of Medical and Non-Medical Collections*, December 2014, at http://files.consumerfinance.gov/f/201412_cfpb_reports_consumer-credit-medical-and-non-medical-collections.pdf. People often have difficulty understanding co-pays and health insurance deductibles. To address some of these concerns, on December 31, 2014, the Internal Revenue Service (IRS) announced a final rule requiring the separation of billing and collection policies of nonprofit hospitals. See Department of the Treasury, Internal Revenue Service, *New Requirements for 501(c)(3) Hospitals Under the Affordable Care Act*, at <https://www.irs.gov/charities-non-profits/charitable-organizations/requirements-for-501c3-hospitals-under-the-affordable-care-act-section-501r>. Under the rule, hospitals that have or are pursuing tax-exempt status are required to make reasonable efforts to determine whether their patients are eligible for financial assistance before engaging in “extraordinary collection actions,” which may include turning a debt over to a collection agency, thus creating a medical tradeline, or garnishing wages. In short, tax-exempt hospitals must allow patients 120 days from the date of the first billing statement to pay the obligation before initiating collection procedures. See Department of the Treasury, Internal Revenue Service, *New Requirements for 501(c)(3) Hospitals Under the Affordable Care Act*, at <https://www.irs.gov/charities-non-profits/charitable-organizations/requirements-for-501c3-hospitals-under-the->

The Fair Debt Collection Practices Act (FDCPA) is the primary federal statute regulating the consumer debt collection market.¹⁸⁰ Congress passed the FDCPA in 1977 to “eliminate abusive debt collection practices by debt collectors.”¹⁸¹ The law generally applies only to debt collectors, not the original creditors.¹⁸² It prohibits debt collectors from engaging in certain types of conduct when seeking to collect certain debts from consumers, such as engaging in harassment or abuse¹⁸³ or making false or misleading representations.¹⁸⁴ The FDCPA limits when and how a debt collector communicates with a consumer, such as limits on communications at “unusual time[s] or place[s],”¹⁸⁵ and grants consumers the right to dispute¹⁸⁶ or stop certain communications about an alleged debt.¹⁸⁷ Moreover, the FDCPA requires that a debt collector must send a consumer a validation notice, which is to disclose certain information about the debt to the consumer, within five days of the initial communication.¹⁸⁸ In 2010, the Dodd-Frank Act granted the CFPB authority over the FDCPA and became the first federal agency to be able to write regulations to implement the FDCPA.¹⁸⁹ It also grants the CFPB authority over those who collect debt related to a consumer financial product service, as defined in the Dodd-Frank Act.

In general, debt collectors expect that they will collect only a fraction of the face value of any particular debt, knowing that some consumers will never pay back their debt in full. Therefore, when a third-party debt collector contacts a consumer, both parties can negotiate the amount and payment schedule of the debt.¹⁹⁰ If a consumer does not settle her debt, the debt owner often has several options, such as seizing the collateral for secured loans (e.g., car, home),¹⁹¹ or garnishing a consumer’s wages after obtaining a court order. According to CFPB research, “the cost of filing a claim plays a large role in litigation decisions and varies significantly across jurisdictions based on differences in factors such as filing fees and what types of collections claims can be brought in

affordable-care-act-section-501r. The IRS rule only impacts nonprofit hospitals, but, on September 15, 2017, the three major credit reporting agencies—Experian, Equifax, and TransUnion—established a 180-day (6 month) waiting period before posting a medical collection of any type on a consumer credit report. See Experian, “Medical Debt and Your Credit Score: Here’s What You Need to Know,” press release, August 8, 2017, at <https://www.experian.com/blogs/ask-experian/medical-debt-and-your-credit-score/>.

¹⁸⁰ 15 U.S.C. §1692a. The law only includes consumer debts “primarily for personal, family, or household purposes.”

¹⁸¹ 15 U.S.C. §1692.

¹⁸² 15 U.S.C. §1692a. The FDCPA can apply to a creditor collecting its own debts using a different name. Some creditors audit their debt collectors in terms of compliance with federal and state law. For more information on auditing practices of debt collectors, see CFPB, *Study of Third-Party Debt Collection Operations*, pp. 20-21.

¹⁸³ 15 U.S.C. §1692d.

¹⁸⁴ 15 U.S.C. §1692e.

¹⁸⁵ 15 U.S.C. §1692c(a)(1).

¹⁸⁶ 15 U.S.C. §1692g(b).

¹⁸⁷ 15 U.S.C. §1692c(c). For exceptions to this rule, see 15 U.S.C. §1692c(c)(1)-(3).

¹⁸⁸ 15 U.S.C. §1692g(a).

¹⁸⁹ See P.L. 111-203, §1002 and §1011. For more information on the CFPB’s authorities, see CRS In Focus IF10031, *Introduction to Financial Services: The Consumer Financial Protection Bureau (CFPB)*, by Cheryl R. Cooper and David H. Carpenter.

¹⁹⁰ CFPB, “What is the Best Way to Negotiate a Settlement With a Debt Collector?” March 29, 2019, at <https://www.consumerfinance.gov/ask-cfpb/what-is-the-best-way-to-negotiate-a-settlement-with-a-debt-collector-en-1447/>.

¹⁹¹ Legal processes are in place to seize collateral for secured loans, such as foreclosure or car repossession.

small claims court.”¹⁹² More than half of filed suits lead to default judgments in favor of the debt owner, often because consumers fail to appear in court.¹⁹³

Consumers who cannot pay their debts may seek relief through the federal bankruptcy process, which is generally governed by the Bankruptcy Code.¹⁹⁴ In general, the bankruptcy process allows a consumer to enter a court-administered proceeding by which the consumer can “discharge” certain debts and thus obtain a “fresh start.” However, consumers may face negative repercussions by choosing bankruptcy, for example, a lower credit score and reduced access to credit for several years afterward. In 2005, Congress enacted the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA), in response to what some perceived as a high number of consumer bankruptcy filings.¹⁹⁵ BAPCPA made numerous amendments to the Bankruptcy Code. One change was to impose a “means test” to determine when consumers have the financial ability to pay their debts in installments over several years, rather than receiving more immediate relief from their debts.¹⁹⁶

In late 2020, the CFPB announced two final rules intended to regulate the debt collection market.¹⁹⁷ These CFPB regulations, among other things, seek to clarify appropriate communication tactics for debt collectors and what information debt collectors should be required to disclose to consumers. One of these regulations generally limits debt collector phone calls to seven times in a seven-day period and would prohibit debt collectors from making calls within a week after speaking by phone to a consumer. It also allows debt collectors to use newer technologies, such as emails or text messages, to communicate with consumers, requiring a reasonable and simple method for a consumer to opt out of these types of messages if they choose. Congress continues to debate whether these communication limits adequately protect consumers from predatory behavior.¹⁹⁸ Other ongoing policy issues relating to debt collection include the treatment of medical debt by debt collectors and debts incorrectly attributed to consumers or for incorrect amounts.

¹⁹² CFPB, *Study of Third-Party Debt Collection Operations*, p. 18.

¹⁹³ CFPB, *Study of Third-Party Debt Collection Operations*, p. 18.

¹⁹⁴ 11 U.S.C. §§101-1532. For more information on the bankruptcy process, see CRS Report R45137, *Bankruptcy Basics: A Primer*, by Kevin M. Lewis.

¹⁹⁵ P.L. 109-8.

¹⁹⁶ 11 U.S.C. §707(b) provides:

After notice and a hearing, the court, on its own motion or on a motion by the United States trustee, trustee (or bankruptcy administrator, if any), or any party in interest, may dismiss a case filed by an individual debtor under this chapter whose debts are primarily consumer debts, or, with the debtor’s consent, convert such a case to a case under chapter 11 or 13 of this title, if it finds that the granting of relief would be an abuse of the provisions of this chapter.

¹⁹⁷ CFPB, “Debt Collection Practices (Regulation F),” 85 *Federal Register* 76734, November 30, 2020; and CFPB, *Consumer Financial Protection Bureau Issues Final Rule on Consumer Disclosures Related to Debt Collection*, December 18, 2020, at <https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-issues-final-rule-on-consumer-disclosures-related-to-debt-collection/>.

¹⁹⁸ Representative Maxine Waters, Chairwoman of the House Financial Services Committee, “Waters Statement on the CFPB’s Weak Debt Collection Proposal,” press release, May 7, 2019, at <https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=403726>; and Representative Maxine Waters, Chairwoman of the House Financial Services Committee, “Waters Provides Recommendations to President -Elect Biden on Trump Actions to Reverse,” press release, December 4, 2020, at <https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=403726>.

Conclusion

For all of the consumer financial markets described in this report, the societal goal is that each market will create a transparent and competitive price that leads to an efficient market outcome. As described earlier in the report, government policy can potentially correct market failures, such as information asymmetries or behavioral biases, to bring the market to a more efficient outcome, maximizing social welfare. Yet, government policy can lead to unintended consequences as well. Policy changes will typically impose costs and benefits, but these effects can be difficult to calculate in advance of a new law or regulation. It is often challenging to determine whether a policy intervention will help or harm the market from reaching a more efficient outcome.

Author Information

Cheryl R. Cooper
Analyst in Financial Economics

Disclaimer

This document was prepared by the Congressional Research Service (CRS). CRS serves as nonpartisan shared staff to congressional committees and Members of Congress. It operates solely at the behest of and under the direction of Congress. Information in a CRS Report should not be relied upon for purposes other than public understanding of information that has been provided by CRS to Members of Congress in connection with CRS's institutional role. CRS Reports, as a work of the United States Government, are not subject to copyright protection in the United States. Any CRS Report may be reproduced and distributed in its entirety without permission from CRS. However, as a CRS Report may include copyrighted images or material from a third party, you may need to obtain the permission of the copyright holder if you wish to copy or otherwise use copyrighted material.