NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

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Remarks to the Exchequer Club
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15 minutes, Q&A to follow

Good Afternoon. Thank you, Wayne [Abernathy, Chancellor of the Club] for that introduction. Thank you, Exchequer Club for having me here again. I am pleased to be here with all of you today, on this beautiful June day. I was last here in January 2017, two days before the Inauguration, and a lot has happened since that time. In preparing my remarks for today, I can say with ease that I had a very long list of possible topics. It has certainly been a busy 18 months, and my agency, the NYS Department of Financial Services is in the midst of a host of bad federal actions that have hurt ordinary people.

As Superintendent of DFS since early 2016, I lead an agency with 1,400 employees and have a vast mandate in state-based regulation, enforcement and consumer protection. At DFS we regulate and

supervise the activities of nearly 1,500 banking and nondepository institutions with assets of more than $2.6 trillion and more than 1,400 insurance companies with assets of more than $4.3 trillion. As New York is the financial capital of the world with a long and proud history of robust consumer protections, DFS has a leadership role in all periods of time, and one can say particularly when the federal government is aiming in a different direction as has been the case over the past 18 months.

When I spoke here last, I discussed the importance of state-based regulation and, specifically, the then proposed federal "fintech" charter. I made clear my opposition to such a charter. Two lawsuits later, the charter has not happened, though I understand Comptroller Otting will soon be announcing his view. We certainly hope he will decline to move forward and choose litigation, rather than accept the OCC's lack of authority in the non-depository space and respect the states' regulation of and consumer protections in this area.

Our work on "fintech" reflects our support for our state-chartered banking system and of the growth of innovative nondepositories, with a

focus on ensuring a level playing field where everyone conducting the same types of activities – both our depository community banks and our nondepository online lenders -- complies with the same rules.

"Fintech" is simply an abbreviation of the term financial technology – which alone does not encompass any particular industry or sector. Certain kinds of fintech can be utilized quite effectively (when used responsibly) to bring banking services to hard-to-reach consumers. When done right, this is a very good thing. Fintech can enable an institution to underwrite transactions more quickly by allowing for the real-time evaluation of data points – provided that the underwriting is done right and with regard for risk and consumer protection. And, data collection must vigilantly protect consumers from misuse of their data and cyber threats. We do not want another Equifax.

There are those who argue that the mere utilization of financial technology alone somehow grants them an exemption from the rules that banks and other financial institutions follow to manage risk and protect consumers. I have been highly vocal on myriad fronts in my opposition to this view, which would permit any company that calls itself a fintech

to engage in a form of regulatory arbitrage, either with no regulator or in a so-called sandbox. A sandbox is where toddlers play. Adults play by rules and if you engage in banking activities, that means you are responsibly regulated in order to protect the customers. Period.

Today, in fact, I wanted to discuss other areas where the federal government is damaging markets and undermining important consumer protections. It seems that, every day, we at DFS are responding to federal attacks on our markets and our values. We remain ever vigilant and ever watchful. As New York's regulator, DFS will always be prepared to respond to whatever comes our way, and to fill any voids, as we faithfully execute our mission in service to New York's markets and consumers.

Today, we are on the frontlines of an ongoing battle that is essentially federalist in nature. New York is proudly both the financial capital of the world <u>and</u> the progressive capital of the nation. Right now, in this time of federal abandonment of values, New York is fighting back. And we will win.

One of the many brilliant aspects of our federalist system is that the states are empowered to respond in this way. In my role as a state regulator, I have the occasion to work within the historical principles of federalism -- a helpful lens through which I view and calibrate current events. And as a history buff, I would like to use the example of Alexis de Tocqueville.

de Tocqueville was an astute observer of American life and political ascendancy. He understood that whatever else it was designed to do, a federal system should offer government a division of labor. He admired the decentralized nature of the United States government because, among other virtues, it enabled its national government to focus on primary public obligations ("a small number of objects," he stressed, "sufficiently prominent to attract its attention"), leaving what he called society's countless "secondary affairs" to lower levels of administration.[1] Such a multi-layered system, far from being a by-

[1] https://www.brookings.edu/research/why-federalism-matters/

product of federalism, was its *raison d'etre*, allowing the central government to order its priorities efficiently.

In my role as new York's banking regulator, I am very aware of the ways in which our federalist dual banking system led to state-initiated innovations over the course of early American history, which (by the way) furthers my view of the importance of state regulation of fintechs. Over the course of history, there have been many attempts to nationalize banking, and each effort has been met with resistance by the states, and also spurned state (not federal) innovation. For example, in order to stay competitive in response to increasingly restrictive federal actions seeking to hinder state banking, it was New York that responded by pioneering such innovations as the insurance of paper currency, so-called 'free chartering' of banks by any qualified group of citizens – which was a precursor to deposit insurance – and the creation of a central clearing house the collective strength of which enabled the state, and ultimately the nation, to weather many of the world's most severe financial crises. The result was a sorting of roles, and as de Tocqueville would say, of 'sufficiently prominent objects' and functions into state

and federal banking systems, and regulatory structures evolved to follow suit.

Thanks to our federalist system, states can – and I say must – provide greater protections to their residents than federal law does, particularly at times like now when the federal government is rolling back important protections for our people. Thankfully, the Founders created a structure that understood this, and recognized the importance of states filling the void. On this same track, as Justice William Brennan cautioned in 1977, "[t]he legal revolution which has brought federal law to the fore must not be allowed to inhibit the independent protective force of state law – for without it, the full realization of our liberties cannot be guaranteed." These principles are critically important today – because consumers rely on their state representatives to protect them. And we have many examples of this happening right now.

Turning first to health insurance, in New York and in other states, we fully supported the Affordable Care Act (also known as Obamacare) and took great care to implement it fully and completely unlike in other states that spent way too much energy challenging this important law.

As a result, in New York we cut the uninsured rate in half, from 10 percent to 5 percent, and slashed individual premiums as well. We have worked hard to build – and very much still maintain -- a robust health insurance market in New York.

But this Federal administration, from Day One, has been on a dangerous path to destroy this important legislation and thereby destroy the principle that affordable, comprehensive health care is a right of every American, not simply a privilege just for those with employers who provide them good coverage.

While the Trump administration failed to repeal, and then to "repeal and replace" the ACA, they are taking actions every day that damage our markets, create market instability, increase rates and lower benefits. I can speak for many hours on this topic, but let me mention just three recent actions that we strongly oppose:

First, are so-called short-term health plans, which I accurately call "skimpy" plans. Short-term plans are intended to carry people over from one plan to the next. But, HHS has proposed a rule changing the up to three months duration of these plans to 364 days. Yes, that is one

day short of a year. 364 days is not "short-term" – rather it is a transparent effort to undermine the ACA's individual market and an end-run around the requirement of essential health benefits. This is because short-term plans are not required to cover essential health benefits and they permit discrimination in coverage and rates. If this regulation is allowed, healthy people will buy these plans for 364 days because they are cheaper – and let me tell you, with health insurance, you get what you pay for – close to nothing. But if this happens, the individual EHB market will see higher premiums. This proposal is – simply put – a way to discriminate based on age, gender and pre-existing conditions.

New York will not permit these plans. Short-term plans must be short-term and they must provide EHB. In New York, we will continue to require EHBs and prohibit discrimination based on age, gender and pre-existing conditions. That is why I did a regulation last year mandating EHBs and prohibiting discrimination in New York regardless of federal action. Our federalist system fully permits states to provide these greater protections.

Second, the federal tax bill included a repeal of the penalty for the individual mandate. This change will drive healthy and young people out of the market, raising rates and jeopardizing health care for everyone else. The CBO has estimated that this will cost over 10 percent in additional premiums. In New York, the insurers have proposed about 12 percent in increases for 2019 based solely on the Trump administration's repeal of the mandate penalty. This constitutes half of the overall rate requests. Without this addition, the requested rate requests are very manageable. And our small group rate requests are single digits. I stress that these are the insurers' requests. We have a good prior approval law in New York. We will look at the data very carefully. We will not allow federal fear-mongering to cause excessive rate increases. There was no market based reason for the federal government to eliminate the individual mandate penalty – it was purely a political move and it will hurt markets across the country. But we will not allow it to hurt New York.

Third, HHS has proposed regulations regarding contraceptive and abortion coverage, which we also strongly oppose. The constant attacks

on women's health care are stunningly regressive – not to mention the attacks that led to the #MeToo movement. These HHS regulations provide that your employer can refuse to cover reproductive health services based on <u>your</u> <u>employer's</u> "conscience." We are not talking here about churches or other true religious organizations. This regulation says that <u>any</u> employer can impose his "conscience" on his women employees. In New York, we have made clear that women are entitled by state law to insurance coverage of contraceptives and medically necessary abortions without co-pays and deductibles. And while an employer may seek a religious exemption in New York, to do so the employer must be a religious organization <u>and</u> the insurer must still provide the coverage directly to the insured. An employer should not stand in the middle of a woman and her doctor. This has <u>nothing</u> to do with the employment relationship and it should not be allowed.

That's a summary of just a few bad proposals coming from this Administration in the health insurance space. Make no mistake about it, the Trump administration owns the premium increases you are reading about, and they own the reduced benefits and unstable insurance markets

that exist today. They have done everything possible to destabilize the markets. In New York, we will not let their efforts succeed. We have a robust market with strong consumer protections – thanks to federalism and New York law.

Another aspect of federally-created instability that DFS has contended with this past year are the many changes to the Consumer Financial Protection Bureau made by the new Acting Director. The Bureau's importance is obvious when considered within the context of the financial crisis that – like DFS - precipitated its creation and which reshaped the lives of millions of Americans. The financial crisis wiped out nearly $11 trillion in household wealth, sent U.S. GDP tumbling, and caused a huge drop in employment. The savings and retirement accounts of many millions of Americans were emptied out and, after the housing bubble burst, millions also lost their homes to foreclosure.

While many states, including New York, have vigorously enforced their laws and regulations protecting consumers and markets, prior to 2011, no single federal agency had an exclusive focus on consumer financial protection. There was a clear consensus after the crisis that our

financial system needed better enforcement of laws and regulations at the federal level to protect consumers. That is why Congress created the CFPB. Since its creation in 2011, until the recent halt in new actions, the Bureau had produced impressive results—an estimated one in ten Americans have received some kind of relief or reimbursement from the Bureau's work. It is simply wrong that the Bureau is now turning away from actively enforcing federal consumer financial laws. The new leadership is turning its back on ordinary people, and must have amnesia about the financial crisis.

In addition to its investigative and enforcement actions, the CFPB also previously engaged in rulemaking that aided the implementation and enforcement of federal consumer financial laws. That brings me to the Payday Lending Rule. We should not move backwards on this important work. DFS, through its own work on payday lending, knows that payday lenders charge interest rates far higher than state interest rate caps, and too often engage in predatory tactics that harm struggling borrowers. Restrictions on usurious payday and car title loans, like those found in New York and 14 other states that ban payday lending,

prevent borrowers from paying unaffordable finance fees and help them maintain their ability to make ends meet.

The CFPB's Payday Lending Rule provides common sense protections for borrowers in all states while preserving their access to the credit markets. In finalizing the Rule, the Bureau reviewed more than one million comments, conducted extensive outreach, and learned about the payday industry through its examinations. DFS supports the existing Rule and opposes any changes that would weaken the safeguards the Rule provides. Too many borrowers have already fallen victim to usurious lenders to now abandon the well-researched, fair, and sensible provisions of the Payday Rule.

Student lending is another area in which changes at the federal level can only be viewed as a huge step backwards. The recent announcement by the CFPB's Acting Director that the Office of Students and the Student Loan Ombudsman would be subsumed by the Office of Financial Education is a marked shift. The Bureau appears ready to reduce student lending examinations, investigations, and enforcement, where it had previously been quite active. This is another

blow to hardworking Americans, reversing years of positive work protecting students from loan servicers and predatory debt collectors that engage in unfair, deceptive, and abusive practices. .

In addition, Secretary DeVos of the U.S. Department of Education issued guidance in March 2018 stating the erroneous position that only the federal government may oversee student loan servicers. As courts have already held, states retain the ability to stop illegal practices in the student loan industry to protect students and student debt holders within their own borders. DFS has received and mediated numerous consumer complaints about the student loan servicing and debt collection industries, and has identified many fraudulent and abusive practices. The states have no choice but to fill this void, too. Otherwise, student borrowers are left vulnerable to fraudulent and abusive practices.

Let me now turn to another topic where federal and state regulators are active and thus far are <u>not</u> in conflict: crypto-currency. I welcome the recent involvement of other regulators in this space, though I note that DFS started looking into virtual currency in 2013, long before it was on the radar for most of the financial services world. At the time,

Bitcoin was fluctuating around $100. One concern DFS had at the time was that startups - like the Mt. Gox exchange operating in Japan - had deficient operations that put customer funds at risk. Another concern was that these then unregulated small businesses were not respecting anti-money laundering laws. DFS recognized early on that standards needed to be set that would help improve operations and safety, and allow for responsible innovation – yet another example of state innovation in a federalist system.

DFS held public hearings on virtual currency in January 2014, and invited companies to submit proposals for chartering a virtual currency exchange, as the problems at Mt. Gox - then handling 70% of Bitcoin exchanges - continued to spiral out of control. DFS issued a proposed Virtual Currency Regulation in 2014, and made its Bitcoin license final in June 2015. Companies that have since received licenses from DFS include the largest virtual currency exchanges in the United States and in Japan.

Virtual currency remains a novel and far from stable area of activity. Its suitability as a payment system remains to be seen. But,

while it has presented a challenge to traditional financial services, it has spurred innovation. And DFS has helped set the standards through our application and examination processes to ensure that customer protection is taken seriously, and that cybersecurity and AML standards are respected. As Superintendent, I have taken this task seriously, by moving forward on license issuance and new product applications and by encouraging a legally compliant industry.

As with other so-called fintechs, there are those who resist regulation in this space in the name of innovation. They, too, are wrong. We cannot dispute that the crypto-currency space has its risks – and I believe firmly that we cannot allow these risks to be unregulated until we learn the consequences at some later date. By setting standards early on, New York and other states have made it possible for both startups and traditional financial service providers to pursue innovation in this area - as well as in areas of traditional finance where innovation had slowed down. Indeed, regulatory standards help insure that the competition among new entrants is not a race to the bottom - where services that seem cheap or convenient turn out to hide fatal flaws -

flaws like those that led to hacking, massive losses, and eventually the bankruptcy of Mt. Gox.

Strong standards are important to our markets and our consumers, as well as the companies that want to be best in class in providing financial services. The regulatory structure that we created for virtual currency has helped our licensed companies attract greater interest from customers, investors, and potential financial services partners seeking to pursue further innovation, while protecting market integrity by stringent standards applicable to all law-abiding business enterprises.

I think de Tocqueville would approve of strong crypto standards and the interplay between regulatory agencies in this space with their distinct roles and functions. States like New York have traditionally regulated money transmitters, and crypto-currency falls consistently under that regulation. The Securities and Exchange Commission (SEC) regulates public companies, and, therefore, initial coin offerings, or ICOs, fall under its purview. The Commodity Futures Trading Commission (CFTC) is on the lookout for disruptive trading,

particularly in the futures market that it regulates. This is how it should be. There is certainly no need for a federal crypto-fintech charter.

Elsewhere, we should not allow a dual system to result in insidious efforts to make end runs around state or federal regulators, depending on who is in control. With respect to banking the practice of regulatory arbitrage, , is when banks seek to relocate their regulatory oversight out of a certain jurisdiction to one where the regulator is perceived to be more favorable, at a given point of time.

Of course, promoting the New York State charter is part of my job as DFS Superintendent in a competitive, federalist, dual banking system. But no regulator should allow the threat of a charter flip to cause him or her to forget that we are charged with enforcing the law. No financial institution should be permitted to avoid responsibility for its illegal conduct by trading enforcement regimes through a conversion from a state-licensed entity to a federally licensed entity, or vice versa. What goes around, comes around, too. And a charter flip cannot give the institution a pardon by the federal government for past misconduct.

On the insurance side of my house, the arbitrage issue is less dramatic as it presents as an intra-state problem. An insurer, seeking to avoid one state's robust reserve requirements, could look to other states for relief. Those other states may appear to be more friendly to industry, but the ability to forum shop and select jurisdictions that permit insurers to back policy liabilities with low quality assets threatens the solvency of the insurance industry on the whole and the entire state-based insurance regulatory system.

Overall, New York industry benefits from our ability to steer clear of some of the insurance industry's biggest problems. The proof is in the pudding: where there has been exposure to us in New York State, New York subsidiaries and affiliates are in much better financial condition than the affiliated companies in other states. This is a fact.

And before I conclude, a few words about the efforts to roll back Dodd-Frank. Here, too, I could spend hours on this topic, but I want to mention a few points today:

First, our community banks are vitally important to communities across the country. But, relief given to large banks is not in service to

the community banks and only adds risk to our system and creates, once again, "too big to fail" institutions.

Second, the Volcker rule is a well-considered rule that protects against risky investments and holdings. We should not be rolling it back, on the claim that we have a good economy today. We had a robust economy in 2006 before the crash. We stress test for the bad times, because that is when capital and reserves are most needed, otherwise people will be harmed. Reducing capital or reserves in the good times, allowing for increased profit-making and risky investments, is a recipe we have seen baked before. It seems the federal government has chosen this risky path which will harm ordinary Americans if allowed to progress.

Third, leverage ratios are just as important as risk-based capital. We should not eliminate or reduce our requirements in these areas. Capital and liquidity are both necessary at appropriate levels. Again, we should not forget the lessons of 2007-2008.

In closing, in the year and a half that has passed since my last time addressing this group, we have seen the importance of sound and stable state-based regulation as a bulwark against federal instability and attacks, regulatory arbitrage or another yet-to-be revealed threat. The importance, effectiveness (and sheer brilliance) of our federalist system has increased in equal measure. I will add that we are also witnessing the importance of our third branch of government – the independent judiciary. We must keep it that way.

Our Founders created a democracy, with checks and balances, including our Federalist system that permits the states to provide greater protections when needed. Our Founders did not create an executive dictatorship. In my office in downtown Manhattan, I am privileged to witness every day, outside my window at DFS, the Statue of Liberty – Lady Liberty – lighting the way away from dictatorship and oppression to democracy and opportunity. She reminds me every day of the privilege that I have as an American and as a New Yorker, because my grandparents – with not a penny in their pockets – came through New York's harbor for the opportunities this country can provide. We cannot

forget this history. We all want our children and grandchildren to have a better life. So do the people seeking to come to this country from other places today. Negativity and fear mongering is not the path forward. Rolling back health care protections, financial consumer protections and increasing risk in the financial sector is not in service of the American dream that our neighbors share. The additional profit made at the expense of our struggling neighbors is the wrong path. We have seen this before. We should not go backwards.

Let's move forward instead, together, and in doing so let us bring others along with us.

Thank you.