BETTER MARKETS

REPORT

SUMMARY

More Than Ever, the States Have a Vital Role to Play in Investor and Consumer Protection

As Federal Protections Against Financial Fraud and Abuse Are Gutted, the States Help Fill the Void

Federal deregulation is well underway, just as new threats to investors and consumers are emerging. The Trump Administration has undertaken an aggressive campaign to cut back protections for investors and consumers. It is gutting the agencies that oversee the markets, rolling back important rules, and abandoning enforcement actions that hold wrongdoers accountable. At the same time, new threats to investors and consumers are rapidly emerging, from an endless wave of new cryptocurrency investments to an increasing reliance on artificial intelligence (AI) in finance. The result is a perfect financial storm that threatens all Americans.

The states are key to limiting the damage. The states already play a major role in policing securities, banking, and insurance. Now their expertise, resources, and commitment to fair dealing in the financial markets are more important than ever to help compensate for the rapidly shrinking role of the federal agencies. The states can aggressively exercise the considerable regulatory and enforcement authority they already have, and in some areas, they can expand their authority to better protect investors and consumers, as many states are already doing.

The stakes are high. Federal deregulation will inevitably spur a surge in predatory practices among many brokers, advisers, banks, payday lenders, debt collectors, and other financial firms. Without the states at their side, Americans will suffer ever-greater financial losses and economic insecurity. We also know that when state regulators are unable to act because of preemption—when federal law overrides state law—the risk of systemic instability rises, increasing the odds of another financial crisis like the 2008 crash, which destroyed the financial lives of millions of Americans.

Inevitable resistance lies ahead. The states have always faced headwinds in protecting consumers and investors, including budgetary limitations, political pressures within states, and aggressive industry lobbying for deregulation. Also looming is the threat of preemption, which can eliminate or narrow state authority. Notwithstanding these challenges, however, the states must do all they can to protect consumers and investors from fraud and abuse and maintain the integrity and stability of our financial markets. Policymakers, public interest advocates, and the public at large should stand by the states and fully support their critical role in this era of federal deregulation.

In light of all these developments, our report reviews the states' key role in overseeing the securities, banking, and insurance markets. It also highlights some additional steps the states can take to further protect American investors and consumers.

Securities Regulation. The states have been regulating the securities markets for over 100 years, well before the SEC was established. Our report reviews the general scope of the states' authority and then highlights their key role in four specific areas: bringing enforcement actions against a wide variety of misconduct; policing the cryptocurrency market; raising the standards among financial advisers; and helping to curb abuses in the use of pre-dispute mandatory arbitration agreements. Their investor protection and enforcement activities, are now especially vital for two reasons: The SEC is retreating from its role as the cop on the Wall Street beat, while investors face new risks from the explosion in cryptocurrency offerings, the rising use of AI in finance, and the expansion of private or exempt offerings.

Banking. Banks and credit unions, along with a variety of nonbank financial firms, are the bread and butter of Americans' financial lives, providing the necessary staples such as bank accounts, auto loans, mortgage loans, and small business loans. Making sure these institutions treat their customers fairly is therefore vitally important. With the passage of the Dodd-Frank Act in 2010, the states gained significantly broader authority, especially in the regulation of nonbanks and the enforcement of a wide range of consumer protection laws. Our report reviews the states' authority over traditional banks, thrifts, and credit unions, and then highlights the state's expanded authority to bring enforcement actions against nonbanks, which play an increasingly important role in finance. It also cites examples of states writing new rules to protect consumers from abusive practices in the areas of overdraft fees, buy-now-pay-later loans, debt settlement services, and others.

Insurance. Americans rely on insurance products to protect against risks to their lives, homes, personal property, and businesses. However, some insurance products are predominantly investment vehicles, including fixed-indexed annuities (indexed annuities). Those increasingly popular products, often sold as retirement planning instruments, generate huge and essentially guaranteed profits for insurance companies and the agents or "producers" that sell them. Yet they are extremely complex and difficult for investors to understand. Moreover, they can carry huge commissions, lock up savings for years, and offer meager returns by virtue of caps and other features that limit gains. Investors and retirement savers therefore need protection against the intense conflicts of interest that motivate insurance companies and agents to sell them.

Our report details the weaknesses in the current state rules governing the sale of annuities, which are based on a template known as the "Suitability in Annuity Transactions Model Regulation (#275)," drafted by the National Association of Insurance Commissioners or NAIC. Despite the claims of the insurance industry, the rule does little to protect investors from the powerful conflicts of interest that motivate insurance agents to sell annuities. Our report explains that every state can and should adopt a stronger version of the NAIC model rule, one that actually prevents both agents and insurance companies from advising clients to purchase annuities that are not in the clients' best interest.

Better Banks | Better Businesses
Better Jobs | Better Economic Growth
Better Lives | Better Communities

Better Markets is a public interest 501(c)(3) non-profit based in Washington, DC that advocates for greater transparency, accountability, and oversight in the domestic and global capital and commodity markets, to protect the American Dream of homes, jobs, savings, education, a secure retirement, and a rising standard of living.

Better Markets fights for the economic security, opportunity, and prosperity of the American people by working to enact financial reform, to prevent another financial crash and the diversion of trillions of taxpayer dollars to bailing out the financial system.

By being a counterweight to Wall Street's biggest financial firms through the policymaking and rulemaking process, Better Markets is supporting pragmatic rules and a strong banking and financial system that enables stability, growth, and broad-based prosperity. Better Markets also fights to refocus finance on the real economy, empower the buyside and protect investors and consumers.

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