

Clients & Friends Memo

The Consumer Financial Protection Bureau: The New, Powerful Regulator of Financial Products and Services

March 6, 2012

I. Introduction

The Dodd-Frank Wall Street Reform and Consumer Protection Act (“**Dodd-Frank**”) created the Consumer Financial Protection Bureau (“**CFPB**”) to oversee a broad array of financial products and services. Creation of the CFPB marked the first time in decades that Congress had formed a new federal agency. The political debate over who would lead the new agency initially overshadowed the more significant legal and policy concerns about the manner in which the CFPB was intended to operate. But now, after the procedurally controversial appointment of former Ohio Attorney General Richard Cordray on January 4, 2012, these broader concerns will be tested, both as a matter of governance and very possibly in the courts.

The CFPB has (i) independence from Congressional or Presidential oversight, (ii) centralized power in a single individual, and (iii) a guaranteed budget that is a percentage of the Federal Reserve’s operating expenses. The principal questions this memorandum asks are whether these characteristics of the agency are constitutional or well-advised, particularly in light of the significant powers that the CFPB possesses.

The first sections of this memorandum provide a description of the powers of the CFPB and its structure. Because it is hard to appreciate the agency’s structure in the abstract, we have provided a chart (Appendix A at the end of the memorandum) to highlight the differences between the CFPB’s structure and those of other federal government agencies charged with related tasks. In the next part of the memorandum, we discuss briefly the question of whether the CFPB’s operational procedures are consistent with the requirements of the Constitution. Finally, we turn back to the policy question of whether it is “good government” for Congress to authorize an agency (or, as a practical matter, the single person that is its head) to act with such independence from restraint or oversight from any of the legislative, executive, or judicial branches of the federal government.

The questions raised in this memorandum are not a function of the agency’s goal; that is a separate issue entirely. This memorandum instead primarily addresses the CFPB’s structure within the

government, and while this issue has been discussed since the early drafting stages of the Dodd-Frank Act, it is immediately relevant now that a CFPB director has started the agency's work.¹

II. CFPB Purpose and Jurisdiction

A. Formation of the CFPB

The stated purpose of the CFPB is to implement and enforce federal consumer financial law: to enable all consumers to access the markets for consumer financial products and services while ensuring that these markets are fair, transparent, and competitive.² Previously, these functions were intended to be served, in large measure, by other parts of the government. Pursuant to the Dodd-Frank Act, however, the CFPB assumes to a significant degree the consumer financial protection functions of the following federal agencies: the Federal Reserve Board, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, and the former Office of Thrift Supervision.³ The CFPB also assumes jurisdiction of the Department of Housing and Urban Development (“HUD”) with respect to HUD’s authority pursuant to the Real Estate Settlement Procedures Act, the S.A.F.E. Mortgage Licensing Act, and the Interstate Land Sales Full Disclosure Act.⁴

B. Key Definitions

In addition to the consumer protection functions previously performed in these other agencies, the CFPB also has newly created regulatory and enforcement powers tied to three important principal definitions (and one subsidiary definition):

- 1) “consumer financial product or service,”

¹ See, e.g., *Hearing before the U.S. Senate Comm. on Banking, Housing, and Urban Affairs*, 112th Cong. (Jan. 31, 2012) (summarizing and reviewing the first months of the CFPB’s work), available at http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.LiveStream&Hearing_id=fdc6713a-a47c-4872-ac2d-f201e60cd26b.

² Dodd-Frank Act § 1021(a). Elizabeth Warren, advisor to the President with respect to the agency, explained:

The purpose of the CFPB’s work should be . . . to create a level playing field where both parties to the transaction understand the terms of the deal, where the price and risk of products are clear, and where direct comparisons can be made from one product to another. . . . American families need an agency that is actively monitoring consumer financial markets to ensure that they are fair, transparent, and competitive.

Hearing before the Subcomm. on Fin. Insts. & Consumer Credit, H. Comm. on Fin. Servs., 112th Cong. 3-4, 12 (Mar. 16, 2011) (statement of Elizabeth Warren, Assistant to the President and Special Advisor to the Secretary of the Treasury on the Consumer Financial Protection Bureau) [hereinafter “March 16, 2011 Warren Testimony”], available at <http://financialservices.house.gov/media/pdf/031611warren.pdf>.

³ Dodd-Frank Act § 1061(a)(2)(A), (b)(1)-(4), (b)(6).

⁴ *Id.* § 1061(b)(7).

- 2) “covered person” (and the related subsidiary definition of “service provider”), and
- 3) “federal consumer financial law.”

“**Consumer financial product or service**” is defined in Dodd-Frank as a financial product or service “offered or provided for use by consumers primarily for personal, family, or household purposes.”⁵ This is a very broad concept, including each of the following categories of products or services:⁶

- the extension of credit and servicing of loans,
- brokerage of leases of real or personal property,
- real estate settlement or appraisal services,
- deposit-taking activities or “otherwise acting as a custodian of funds or any financial instrument,”
- prepaid debit cards and other “stored value” instruments,
- check cashing, collection, or guaranty services,
- payment processing or “other financial payment processing,”
- financial advisory services,
- credit reporting services, and
- debt collection.

“**Covered person**” is defined in Dodd-Frank as “any person that engages in offering or providing a consumer financial product or service. . . .”⁷ This term is likewise expansive, expressly including an affiliate of a covered person who “acts as a service provider” to the covered person.⁸ The term “service provider” includes any person that provides a “material service”⁹ to a “covered person” in connection with a consumer financial product or service.

⁵ *Id.* § 1002(5).

⁶ *Id.* § 1002(15)(a)(i).

⁷ *Id.* § 1002(6)(A).

⁸ *Id.* § 1002(6)(B).

⁹ *Id.* § 1002(26). “Material services” involve design, operation, or maintenance of the product and certain processing functions.

Covered persons are subdivided further into three different types:

- large banks and other depository institutions, *i.e.*, those depository institutions with assets greater than \$10 billion,¹⁰
- small banks and other depository institutions, *i.e.*, those depository institutions with assets of \$10 billion or less,¹¹ and
- non-depository institutions that offer or provide consumer financial products or services and which are not expressly excluded by Dodd-Frank or a rule of the CFPB.¹²

The Dodd-Frank Act excludes the following from the definition of covered person: those persons engaged in activities regulated by the Securities and Exchange Commission (“**SEC**”) or state securities commissions or by the Commodity Futures Trading Commission (“**CFTC**”); tax preparers, lawyers, or persons regulated by state insurance regulators or engaged in the business of insurance; employee benefit plans under ERISA or the Internal Revenue Code of 1986; persons regulated by the Farm Credit Administration; and car dealers, merchants, retailers, and other sellers of non-financial goods or services.¹³

However, otherwise excluded individuals and entities nevertheless may be “covered persons” regulated by the CFPB to the extent that they are otherwise engaged in CFPB-regulated activities and are not acting in their excluded capacity. These persons and entities also may be subject to CFPB regulation to the extent they act as service providers to covered persons.¹⁴

Finally, “**federal consumer financial law**” is defined in the Dodd-Frank Act by reference to a long list of federal laws that involve the offering or providing of a consumer financial product or service other than the Federal Trade Commission Act.¹⁵ That is, the Dodd-Frank Act enumerates federal

¹⁰ *Id.* § 1025.

¹¹ *Id.* § 1026.

¹² *Id.* § 1002(5), (15). Consistent with recognizing the enforcement powers of state attorneys general, the Dodd-Frank Act codifies the Supreme Court’s holding in *Cuomo v. Clearing House Ass’n, LLC*, 129 S. Ct. 2710 (2009). With regard to nationally chartered banks, the Act codifies the Supreme Court’s holding in *Barnett Bank of Marion County, N.A. v. Nelson*, 517 U.S. 25 (1996). As such, state banking regulations are preempted as to national banks in three situations: if the state regulations (i) are discriminatory, (ii) “prevent or significantly interfere with the exercise by the national bank of its powers,” or (iii) are expressly preempted. Dodd-Frank Act § 1044.

¹³ Dodd-Frank Act §§ 1027, 1029.

¹⁴ *Id.* § 1027(n). Congress did vest the CFPB with some level of discretion to exercise restraint if it so chooses. The CFPB may exempt from regulation persons, entities, and affiliates that provide consumer financial products or services as the CFPB deems “necessary or appropriate” to carry out its purposes. § 1022(b)(3).

¹⁵ The Dodd-Frank Act § 1002(12) lists the following “enumerated consumer laws,” *id.*, which compose the federal consumer financial law:

(A) the Alternative Mortgage Transaction Parity Act of 1982 (12 U.S.C. § 3801 et seq.);

consumer laws already in existence that now fall within the control of the CFPB. Accordingly, the CFPB has broad authority over dozens of financial acts ranging from the Homeowners Protection Act to the Consumer Leasing Act, the Truth in Lending Act, and sections 502 through 509 of the Gramm-Leach-Bliley Act.

III. Rulemaking Powers

The CFPB may “prescribe rules and issue orders and guidance, as may be necessary or appropriate to enable the Agency to administer . . . enforce, and otherwise implement the provisions of Federal consumer financial law” (as such term is defined in Section II of this memorandum).¹⁶ This rulemaking authority is exclusive to the CFPB,¹⁷ except where it shares rulemaking power with the Federal Trade Commission (“FTC”) under the Federal Trade Commission Act.¹⁸ This expansive rulemaking power includes issuing new rules and guidelines and also revising ones already in existence.¹⁹ With the broad list of federal consumer financial laws within its jurisdiction, the CFPB has the power to rewrite a vast array of regulations.

(B) the Consumer Leasing Act of 1976 (15 U.S.C. § 1667 et seq.);
 (C) the Electronic Fund Transfer Act (15 U.S.C. § 1693 et seq.), except with respect to § 920 of that Act;
 (D) the Equal Credit Opportunity Act (15 U.S.C. § 1691 et seq.);
 (E) the Fair Credit Billing Act (15 U.S.C. § 1666 et seq.);
 (F) the Fair Credit Reporting Act (15 U.S.C. § 1681 et seq.), except with respect to §§ 615(e) and 628 of that Act (15 U.S.C. §§ 1681m(e), 1681w);
 (G) the Home Owners Protection Act of 1998 (12 U.S.C. § 4901 et seq.);
 (H) the Fair Debt Collection Practices Act (15 U.S.C. § 1692 et seq.);
 (I) subsections (b) through (f) of § 43 of the Federal Deposit Insurance Act (12 U.S.C. § 1831t(c)-(f));
 (J) sections 502 through 509 of the Gramm-Leach-Bliley Act (15 U.S.C. §§ 6802-6809), except for § 505 as it applies to § 501(b);
 (K) the Home Mortgage Disclosure Act of 1975 (12 U.S.C. § 2801 et seq.);
 (L) the Home Ownership and Equity Protection Act of 1994 (15 U.S.C. § 1601 note);
 (M) the Real Estate Settlement Procedures Act of 1974 (12 U.S.C. § 2601 et seq.);
 (N) the S.A.F.E. Mortgage Licensing Act of 2008 (12 U.S.C. § 5101 et seq.);
 (O) the Truth in Lending Act (15 U.S.C. § 1601 et seq.);
 (P) the Truth in Savings Act (12 U.S.C. § 4301 et seq.);
 (Q) section 626 of the Omnibus Appropriations Act, 2009 (Public Law 111-8); and
 (R) the Interstate Land Sales Full Disclosure Act (15 U.S.C. § 1701).

Id.

¹⁶ *Id.* § 1022.

¹⁷ *Id.* § 1022 (“Notwithstanding any other provisions of Federal law and except as provided in section 1061(b)(5), to the extent that a provision of Federal consumer financial law authorizes the Bureau and another Federal agency to issue regulations under that provision of law for purposes of assuring compliance with Federal consumer financial law and any regulations thereunder, the Bureau shall have the exclusive authority to prescribe rules subject to those provisions of law.”).

¹⁸ *Id.* § 1061(b)(5)(B). Although the Dodd-Frank Act directs the CFPB and the FTC to cooperate in their rulemaking, it nonetheless raises the possibility of the promulgation and enforcement of conflicting directives.

¹⁹ Professor Elizabeth Warren, who is credited with designing the agency, stated:

Any final rules adopted by the CFPB may be set aside only where the Financial Stability Oversight Council (“FSOC”)²⁰ finds, by two-thirds majority, that the rule would “put the safety and soundness of the United States banking system or the stability of the financial system of the United States at risk.”²¹ This is a high standard indeed; as a practical matter, the FSOC does not have meaningful veto power.

Courts must afford deference to the agency’s determinations regarding the meaning or interpretation of federal consumer financial law as if the CFPB were the only agency authorized to apply, enforce, interpret, or administer that law.²² Accordingly, the CFPB may act contrary to the existing legal precedent and interpretations by other federal agencies, which will create at least some, perhaps substantial, legal uncertainty.²³

IV. Monitoring and Investigating

The Dodd-Frank Act requires the CFPB to monitor consumer risks posed by consumer financial products or services.²⁴ The CFPB also must publicly report its significant findings regarding those risks at least once annually.²⁵ In the course of its monitoring duties, the CFPB may demand and receive access to the confidential reports of other federal agencies, including “reports of examination or financial condition made by a prudential regulator or other Federal agency having jurisdiction over a covered person.”²⁶ Additionally, the CFPB has the power to require covered

It should be the job of the consumer agency to revise and update outdated regulations and useless disclosures as aggressively as it monitors the fine print layered on by lenders. If everything is on the table, including existing government regulations, the goals of transparency and consumer understanding can become a reality.

March 16, 2011 Warren Testimony, *supra* note 2, at 7. In prescribing rules, the Bureau is constrained by certain standards: namely, the Bureau must consider benefits and costs to consumers of a proposed rule including “the potential reduction of access by consumers to consumer financial products or services.” Dodd-Frank Act § 1022(b)(2). Further, the Bureau must consider the impact of a proposed rule on small depository institutions (regulated under § 1026) and rural consumers. *Id.*

²⁰ The Financial Stability Oversight Council was established by Title I of the Dodd-Frank Act for the purpose of serving as an early warning system as to systemic risks to the United States financial system. The Council consists primarily of the heads of various financial regulatory agencies. Dodd-Frank Act § 111.

²¹ *Id.* § 1023.

²² *Id.* § 1022(b)(4)(a)(B).

²³ It is unclear whether the CFPB would in fact choose to disregard legal precedence, particularly if most CFPB staffers were former employees of other banking agencies. On the other hand, the CFPB not only has different leadership, it also may view its principal goals and policies differently than, for example, the banking regulators who are also responsible for the “safety and soundness” of the banking system.

²⁴ *Id.* § 1022(c)(1).

²⁵ *Id.* § 1022(c)(3)(A).

²⁶ *Id.* § 1022(c)(6)(B).

persons and their service providers to give testimony under oath, file reports, or otherwise answer written questions.²⁷

The extent of the CFPB's monitoring and investigative powers varies somewhat depending upon the class of covered person regulated.

Non-Depository Institutions. With respect to non-depository institutions (many of which will be subject to federal supervision for the first time), the CFPB may prescribe rules requiring them to file registration statements concerning the consumer financial products or services they offer.²⁸ Additionally, the CFPB may require certain non-depository institutions to keep records in order to assess compliance with federal consumer law, obtain information about such non-depository institutions' compliance systems, and detect and assess risks to consumers and markets.²⁹ The non-depository institutions subject to these reporting and record-keeping requirements include:

- those providing services in connection with loans secured by real estate,³⁰
- any "larger participant" (to be defined by rule) of a market for other consumer financial products or services,³¹
- any covered person whom the CFPB has a reasonable basis to determine, based on complaints, is or has engaged in conduct that poses risks to consumers with regard to the offering or provision of consumer financial products or services,³²
- any person offering or providing private education loans,³³ and
- any person offering or providing payday loans.³⁴

Large Banks. The CFPB has broad and exclusive authority to monitor the compliance of large banks with federal consumer laws. For depository institutions that have assets exceeding \$10

²⁷ *Id.* § 1022(c)(4)(B)(ii).

²⁸ *Id.* § 1022(c)(7).

²⁹ *Id.* § 1024(b). The Dodd-Frank Act defines "nondepository covered persons" as: those providing services in connection with loans secured by real estate; any "larger participant" (to be defined by rule) of a market for other consumer financial products or services; any covered person whom the CFPB has a reasonable basis to determine, based on complaints, is or has engaged in conduct that poses risks to consumers with regard to the offering or provision of consumer financial products or services; any person offering or providing private education loans; and any person offering or providing payday loans. *Id.* § 1024(a)(1).

³⁰ *Id.* § 1024(a)(1)(A).

³¹ *Id.* § 1024(a)(1)(B).

³² *Id.* § 1024(a)(1)(C).

³³ *Id.* § 1024(a)(1)(D).

³⁴ *Id.* § 1024(a)(1)(E).

billion—including banks, credit unions, and savings associations—the CFPB holds exclusive authority to require the depository institution and its affiliates to file reports and periodically submit to assessment examinations of their compliance with federal consumer law. The CFPB has exclusive authority to investigate and obtain information about these depository institutions' compliance systems, and to detect and assess consumer and market risks posed by them.³⁵ To the extent that prudential (banking) regulators continue to exercise examination authority over large depository institutions, the CFPB is required by Dodd-Frank to coordinate examinations with those of the relevant prudential regulators.³⁶

Small Banks. The CFPB has more limited powers to monitor smaller banks and depository institutions. For those with assets at or below \$10 billion, the prudential regulators retain the primary role to examine. However, the CFPB may require reports from these depository institutions to supplement the implementation of federal consumer protection law.³⁷ The CFPB also has the power to force the prudential regulators to include CFPB examiners “on a sampling basis” in the examinations they perform.³⁸

V. The CFPB's Enforcement Powers and Cooperation with State Attorneys General

The CFPB has at its disposal a broad range of enforcement tools and significant sanction powers, some of which resemble those of other banking agencies.³⁹ The Dodd-Frank Act provides the CFPB with the power to issue subpoenas and civil investigative demands requiring the production of testimony, documents, or objects, or the submission of written reports or written answers to questions.⁴⁰

The CFPB may serve a cease and desist notice on any covered person asserted to have violated applicable federal consumer financial law. The recipient must abide by its terms thirty days after it is served and until the notice is adjudicated at an administrative hearing held by the CFPB or by a court. Such CFPB administrative hearing must be held between thirty and sixty days after service

³⁵ *Id.* § 1025(b).

³⁶ *Id.* § 1025(e).

³⁷ *Id.* § 1026(b).

³⁸ *Id.* § 1026(c).

³⁹ The CFPB's administrative enforcement powers are similar, in some ways, to those held by the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Reserve, and the Office of Thrift Supervision under 12 U.S.C. §1818(i). However, the CFPB's powers differ from those of the Office of Thrift Supervision under 1818(i) in that (i) reformation serves as a remedy; (ii) excess proceeds can be placed into CFPB-designated “financial literacy” programs, rather than remittance to the Treasury general account; (iii) there is no specific requirement that the CFPB must prove that the perpetrator was enriched by the violation; and (iv) the CFPB's penalties may be imposed against non-depository institutions.

⁴⁰ *Id.* § 1052(b), (c).

of the notice.⁴¹ Appeal is permitted to the D.C. circuit or to the federal circuit court of the location of the covered person's principal office.⁴²

The CFPB has the additional power to issue cease and desist notices that are effective immediately upon service. These temporary cease and desist orders may be issued when the CFPB determines that a violation of law "is likely to cause the person to be insolvent or otherwise prejudice the interests of consumers" before the completion of proceedings that would otherwise ordinarily be taken.⁴³ Appeal of the temporary order must be taken within ten days of its service to the federal district court in which the covered person resides or has its principal office or to the district court for the District of Columbia.⁴⁴

In terms of sanctions, the CFPB has the authority to impose substantial penalties on those who violate its rules.⁴⁵ There are, in the words of Dodd-Frank, three tiers of penalties: (i) \$5,000 a day for those who violate a law or rule; (ii) \$25,000 a day for those who "recklessly" violate a law or rule; and (iii) \$1,000,000 a day for those who "knowingly" violate a law or rule.⁴⁶ However, it is not clear that there is any legal distinction among these three tiers of fines. As a general matter, ignorance of the law is not an excuse for a violation—thus, anyone who knowingly acts in a manner or who is deemed to be in violation of law would seem to be subject to the highest tier fine level, and, thus, the lower levels are arguably irrelevant (or, are relevant only at a regulator's discretion).⁴⁷ Additionally, the CFPB is empowered to recoup its, or a state attorney general's, costs in recovering the penalty.⁴⁸ In short, the CFPB has power to fine many firms out of business, a power that inevitably colors any discussion with the accused of the settlement of alleged violations.

In exercising its administrative adjudicative powers, the CFPB has the discretion to fashion any appropriate legal or equitable remedy with respect to a violation of federal consumer financial law. These remedies expressly include rescission, reformation of contracts (a somewhat unusual power), refund of moneys, return of real property, disgorgement, damages, and penalties.⁴⁹

⁴¹ *Id.* § 1053(b).

⁴² *Id.* § 1053(b)(4).

⁴³ *Id.* § 1053(c).

⁴⁴ *Id.*

⁴⁵ For a comparison of the civil money penalty authority conferred on the federal banking agencies, see 12 U.S.C. §1818(i).

⁴⁶ Dodd-Frank Act § 1055.

⁴⁷ *Id.* § 1055(b)(2).

⁴⁸ *Id.*

⁴⁹ *Id.* § 1055. The CFPB is not empowered to award exemplary or punitive damages.

The Dodd-Frank Act contemplates coordinated enforcement action by the CFPB with the states, giving state attorneys general the express power to enforce regulations implemented by the CFPB. Each state's powers include the ability to bring enforcement action against national banks and federal savings associations in any federal district court having jurisdiction and sitting within the state.⁵⁰ In addition to empowering the states to enforce federal regulations, the Dodd-Frank Act preserves state financial regulations to the extent that they are consistent with Dodd-Frank (generally meaning the stricter law governs)⁵¹ and does not preclude states from enacting and enforcing laws that provide consumers protection that is greater than that afforded by federal law, which potentially subjects businesses to 50 sets of differing state laws in addition to federal laws.⁵²

Cooperation with the states in enforcement has been a consistent theme in the public statements of the leadership of the CFPB.⁵³ The CFPB and state attorneys general already have taken significant steps toward cooperative enforcement. In April 2011, the National Association of Attorneys General and the CFPB announced an accord in which they agreed to cooperate in setting priorities, sharing information, conducting investigations, and initiating enforcement, and to do so without regard to corporate forms, charters, or state lines.⁵⁴

On January 4, 2012, during what was characterized by the White House as a Senate recess, the President appointed former Ohio Attorney General Richard Cordray to lead the agency.⁵⁵ CFPB Director Cordray previously held the role of enforcement chief for the CFPB, and he is known for his record of vigorously pursuing enforcement actions against banks, insurers, and brokers. Indeed,

⁵⁰ *Id.* § 1042(a)(2)(B). In addition, the CFPB is required to give a state attorney general notice of planned litigation in that attorney general's state and, where applicable, to any prudential regulator. *Id.* § 1054(d).

⁵¹ *Id.* § 1041(a)(2).

⁵² *Id.*

⁵³ Agenda, 2011 NAAG Presidential Initiative Conference: America's Financial Recovery: Protecting Consumers While We Rebuild (Apr. 10-12, 2011), available at http://www.naag.org/assets/files/pdf/meetings/2011_Presidential-Initiative_Draft-Agenda.pdf. Professor Warren has stated elsewhere that "the attorneys general serve as an early warning system, acting as first responders to activities that harm American families. . . . As a result, they are also natural partners for the consumer bureau." March 16, 2011 Warren Testimony, *supra* note 2, at 33. Similar sentiments have been expressed by Peggy Twohig, the Bureau's Team Leader for Non-Bank Supervision and former Assistant Director for Financial Practices of the Federal Trade Commission's Bureau of Consumer Protection. Ms. Twohig has signaled that a chief priority of her office is to work closely with states in order to carry out the Bureau's goals with respect to non-depository covered persons. *Treasury's Twohig: CFPB Moving Fast*, Nat'l Mortgage News, Aug. 13, 2010.

⁵⁴ Press Release, U.S. Dep't of the Treasury, Consumer Financial Protection Bureau and National Association of Attorneys General Presidential Initiative Working Group Release Joint Statement of Principles (Apr. 11, 2011), available at <http://www.treasury.gov/press-center/press-releases/Pages/tg1134.aspx>.

⁵⁵ David Nakamura and Felicia Sonmez, *Obama Appoints Richard Cordray to Head Consumer Watchdog Bureau*, WASHINGTON POST, Jan. 4, 2012.

he has called the foreclosure practices of some of the nation's largest banks a business model "built on fraud."⁵⁶

Director Cordray has expressed that one of the CFPB's chief enforcement strategies is to actively cooperate with state attorneys general in enforcement of the federal consumer financial law.⁵⁷ He has characterized his former role as enforcement chief for the CFPB as "doing on a 50-state basis the things I cared most about as a state attorney general, with a more robust and a more comprehensive authority."⁵⁸ Recently, on January 31, 2012, Director Cordray appeared before the United States Senate Committee on Banking, Housing, and Urban Affairs to update the Committee on the agency's work during his six weeks as director.⁵⁹

VI. CFPB's Structure and Organization

The structure of the CFPB is set forth in Title X of the Dodd-Frank Act; primarily, in Section 1011.⁶⁰ The CFPB is an independent federal agency housed within the Federal Reserve and entitled to a percentage of the Federal Reserve's operating expenses—guaranteed funding that is not subject to the congressional appropriations process.⁶¹ Although housed within and funded by the Federal Reserve, the Federal Reserve's Board of Governors cannot interfere in the actions and decisions of the agency.⁶² In other words, the CFPB is entirely independent from both Congressional and Federal Reserve oversight and is almost entirely independent from Executive oversight. For example, the President may remove the head of the CFPB only for "inefficiency, neglect of duty or malfeasance of office."

Unlike, for example, the Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC"), the exercise of whose powers are subject to a majority vote of Commissioners who must come from more than one party, the CFPB's consolidated regulatory

⁵⁶ Jean Eaglesham, *Warning Shot on Financial Protection*, Wall St. J., Feb. 9, 2011, available at <http://online.wsj.com/article/SB10001424052748703507804576130370862263258.html>.

⁵⁷ Richard Cordray, Remarks at the National Association of Attorneys General ("NAAG") Spring Meeting (Mar. 8, 2011), available at <http://www.consumerfinance.gov/speech/partnering-the-consumer-financial-protection-bureau-and-state-attorneys-general/>.

⁵⁸ Eaglesham, *supra* note 56.

⁵⁹ *Hearing before the U.S. Senate Comm. on Banking, Housing, and Urban Affairs*, 112th Cong. (Jan. 31, 2012) (summarizing and reviewing the first months of the CFPB's work), available at http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.LiveStream&Hearing_id=fdc6713a-a47c-4872-ac2d-f201e60cd26b.

⁶⁰ Dodd-Frank Act, Title X, 124 Stat. at 1955. For background on the CFPB, see Rachel E. Barkow, *Insulating Agencies: Avoiding Capture through Institutional Design*, 89 Tex. L. Rev. 15 (2010).

⁶¹ Dodd-Frank Act § 1017.

⁶² *Id.* § 1012(c).

powers will be wielded by a single director. The director, removable only for cause and largely free from oversight authority, is appointed by the President and confirmed by the Senate to a five-year term.⁶³

VII. Constitutional Concerns

The operational structure of the CFPB raises at least two constitutional concerns: (i) a potential violation of the doctrine of separation of powers due to the lack of the agency's accountability to other government branches, and (ii) the potential invalidity of Director Cordray's actions given his appointment during what some characterized as a Senate recess. Both of these concerns were voiced by several senators in the recent hearings before the United States Senate Committee on Banking, Housing, and Urban Affairs.⁶⁴

Regarding the first constitutional concern, the CFPB has only limited accountability to the legislative or executive branch and limited checks on its power.⁶⁵ The CFPB is independent of, even though formally housed within, the Federal Reserve,⁶⁶ which itself is an independent agency.⁶⁷ Any regulation or decisions made by the CFPB may be overruled or prevented only by a two-thirds vote of the Financial Stability Oversight Council, and only if a decision of the CFPB would threaten the safety and soundness of the American financial system or the stability of the financial system.⁶⁸ This limited veto power is the only restraint on the CFPB's independence.⁶⁹

⁶³ *Id.* § 1011. The director also has a seat on the new Financial Stability Oversight Council, whose ten voting members include the Secretary of Treasury and Chairman of the Federal Reserve. *Id.* § 111(b)(1). Moreover, the CFPB director is conferred an automatic seat on the board of the Federal Deposit Insurance Corporation. *See id.* § 336.

⁶⁴ *Hearing before the U.S. Senate Comm. on Banking, Housing, and Urban Affairs*, 112th Cong. (Jan. 31, 2012), available at http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.LiveStream&Hearing_id=fdc6713a-a47c-4872-ac2d-f201e60cd26b.

⁶⁵ At the hearing of the House Financial Services Subcommittee on Financial Institutions and Consumer Credit, Representative Spencer Bachus, R-Ala, stated, "My fear is that there are simply no checks and balances. It could easily become a loose cannon." Ruth Mantell, *CFPB's First 100 Days under Microscope at Hearing*, MARKETWATCH, Nov. 2, 2011, available at http://www.marketwatch.com/story/cfpbs-first-100-days-under-microscope-at-hearing-2011-11-02?reflink=MW_news_stmp.

⁶⁶ *Id.* § 1101(a).

⁶⁷ See 12 U.S.C. § 248 (2006) (listing enumerated powers of the Federal Reserve Board); see also Bd. of Governors of the Fed. Reserve Sys., *The Federal Reserve System: Purposes and Functions* 2-3 (5th ed. 2005), available at http://www.federalreserve.gov/pf/pdf/pf_complete.pdf ("The Federal Reserve System is considered an independent central bank because its decisions do not have to be ratified by the President or anyone else in the executive branch of government.").

⁶⁸ Dodd-Frank Act § 1023(c)(3), (4).

⁶⁹ See Daniel F.C. Crowley, J.W. Verret, Todd J. Zywicki, & Moderator: Geoffrey J. Lysaught, *5th Annual Judicial Symposium on Civil Justice Issues: George Mason Judicial Education Program: December 5-7, 2010: Edited Transcripts*:

The CFPB escapes Congressional oversight due to its guaranteed funding. Although the director of the CFPB is required to submit a budget “request” to the Board of the Federal Reserve, that request must be granted if it is for no more than 12% of the Federal Reserve’s operating expenses.⁷⁰

Judicial oversight of the CFPB also is limited. Courts must defer, subject to *Chevron*,⁷¹ to the CFPB’s interpretation of federal consumer law as the exclusive authority to apply, enforce, interpret, or administer the provisions of that law.⁷²

Accordingly, the structure of the CFPB may not comply with the requisite Article II oversight described in the Supreme Court’s decision in *Free Enterprise Fund v. Public Company Accounting Oversight Board*.⁷³ In that opinion, the Court held unconstitutional a particular structure of the Public Company Accounting Oversight Board (“PCAOB”) that was established by the Sarbanes-Oxley Act of 2002.⁷⁴ Under that structure, the President could not remove SEC members without good cause, and those SEC members could not remove PCAOB members without good cause. The result—dual for-cause limitations on the removal of PCAOB members—prevented Presidential oversight of the PCAOB and, therefore, ran afoul of the Constitution’s separation of powers. Similarly, the CFPB’s insular structure (with a director who may be removed only for cause who in turn may appoint other personnel), coupled with its broad interpretive powers and its guaranteed funding, may run afoul of Article II of the Constitution.

Another potential issue is the process by which the current director was appointed. Title X of the Dodd-Frank Act states that the director of the CFPB is to be appointed by the President, by and with the advice and consent of the Senate.⁷⁵ However, President Obama appointed Richard Cordray on January 4, 2012, taking the position that the Senate was then in recess. Although the Department of Justice has opined that the appointment was legal because the Senate was

Perspectives on Dodd-Frank Wall Street Reform and Consumer Protection Act, 7 J.L. Econ. & Pol’y 307, 320 (2010) (Crowley speaking).

⁷⁰ Dodd-Frank Act § 1017(a)(1), (2).

⁷¹ *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984) (“First, always, is the question whether Congress has spoken directly to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court as well as the agency must give effect to the unambiguously expressed intent of Congress. . . . If the Court determines Congress has not directly addressed the precise question at issue, the court does not simply impose its own construction of the statute. . . . Rather, if the statute is silent or ambiguous with respect to the specific question, the issue for the court is whether the agency’s answer is based on a permissible construction of the statute.”).

⁷² Dodd-Frank Act § 1022(b)(4)(a)(B).

⁷³ 130 S. Ct. 3138 (2010).

⁷⁴ Pub. L. No. 107-204, 116 Stat. 745 (2002) (codified at 15, 18, and 28 U.S.C.).

⁷⁵ Dodd-Frank Act § 1011(b)(2).

functionally in recess, others have argued that the Senate was in session at the time of the appointment.⁷⁶ In either case, this appointment therefore might raise legal issues under the Dodd-Frank Act, which contemplated a Senate check on the appointment of the agency's director. Ultimately, recess appointments generally must be approved by the Senate by the end of the next session of Congress to remain valid.⁷⁷

The Dodd-Frank Act confers the Bureau's powers to the Secretary of the Treasury until the Senate confirms the Director, stating that "The Secretary is authorized to perform the functions of the Bureau under this subtitle until the Director of the Bureau is confirmed by the Senate in accordance with section 1011."⁷⁸ The resulting issue is whether Cordray's actions are valid if his appointment is not.⁷⁹ In testifying before the Committee on Banking, Housing, and Urban Affairs of the Senate on January 31, 2012, Director Cordray confidently stated that he did not believe the work of the CFPB to be impacted by the process of his appointment.⁸⁰

These various concerns likely will result in legal challenges to the CFPB. However these constitutional questions may be resolved, certain other policy questions also deserve attention, as set out below.

VIII. Policy Concerns

In addition to the constitutional concerns, there may be policy concerns regarding the CFPB. These result from the agency's single-director structure, its independence from oversight, and the nature of its budget.

Single Director. There are certain concerns inherent to an agency structure headed by a single director. First, a single director may act counterproductively or ineffectively in regard to the agency's mission. In the context of the CFPB, this problem is magnified by the nonexistence of

⁷⁶ Office of Legal Counsel, Department of Justice, *Memorandum Opinion for the Counsel to the President: Lawfulness of Recess Appointments During a Recess of the Senate Notwithstanding Periodic Pro Forma Sessions* (Jan. 6, 2012), available at <http://www.mainjustice.com/wp-admin/documents-databases/75-1-pro-forma-sessions-opinion.pdf>.

⁷⁷ See U.S. CONST. art. II § 2.

⁷⁸ Dodd-Frank Act § 1066(a).

⁷⁹ *Hearing before the U.S. Senate Comm. on Banking, Housing, and Urban Affairs*, 112th Cong. (Jan. 31, 2012) (statement of Senator Johanns R-NE), available at http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.LiveStream&Hearing_id=fdc6713a-a47c-4872-ac2d-f201e60cd26b.

⁸⁰ *Hearing before the U.S. Senate Comm. on Banking, Housing, and Urban Affairs*, 112th Cong. (Jan. 31, 2012) (statement of Richard Cordray, Director, Consumer Financial Protection Bureau), available at http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.LiveStream&Hearing_id=fdc6713a-a47c-4872-ac2d-f201e60cd26b.

many limits or checks and balances, as well the significant amount of regulatory and budgetary power given to a single person under the agency's structure.⁸¹

Independence. The Federal Reserve is given independence as an agency because it is thought that control over the money supply is such a politically thorny issue that it is imprudent to give day-to-day control to the President and Congress. By contrast, the CFPB has authority over more mundane matters, such as payday loans, prompting the question of whether it is really the case that these matters are so problematic for Congress to regulate directly that it cannot do so except through the establishment of an independent agency.

Budget. In 2011, the Federal Reserve's total operating expenses were \$3.4 billion. As the economy remains vulnerable, the Federal Reserve Board may spend significant amounts of money to support the economy. It seems problematic that the CFPB is set to receive 12% of the Federal Reserve's operating expenses beginning in the fiscal year 2013.⁸² The purposes of the Federal Reserve Board and CFPB differ, and a fixed ratio between their budgets appears arbitrary.

IX. Conclusion

Although still in its infancy, the CFPB is a powerful agency that operates in a novel regulatory scheme with little oversight. The CFPB has broad jurisdiction to regulate financial products and services not previously subject to federal regulation and has assumed exclusive jurisdiction over laws previously under the jurisdiction of other regulatory agencies. With such a broad mandate over virtually all of the economy, the CFPB has the potential for being perhaps the most powerful agency exerting domestic economic authority in the federal government. Among the questions that such powers will raise are (i) are the powers constitutional? and (ii) is this how the federal government should work?

⁸¹ The OCC and former OTS both have had a single agency head who did not report to a board. However, these agencies were established as offices of the Treasury Department and, therefore, were subject to the oversight of the Treasury; while the CFPB is not subject to oversight of either the Treasury or the Federal Reserve, whose partial budget it receives. By way of example of the import of potential dissent among the Commissioners of an agency, the decisions of the CFTC have been subject to public and sometimes quite strong disagreement among the Commissioners. Even where there is no obvious dissent, the possibility of dissent may force an exchange of views among the Commissioners that may likely result in a better process than a single-director system.

⁸² The CFPB is entitled to a slightly smaller percentage of the Federal Reserve's operating expenses in the years leading up to the fiscal year 2013.

Appendix A

	CFPB	CFTC	EPA	FDA	Federal Reserve	FTC	OCC	SEC ⁸³
Leadership	1 Director	5 Commissioners	1 Administrator	1 Commissioner	7 Board Members	5 Commissioners	1 Comptroller	5 Commissioners
Term Length	5 years	5 years	no set term; presidentially appointed	no set term; presidentially appointed	14 years (4 years as Chairman or Vice Chairman)	7 years	5 years	5 years
Bipartisan or Geographic Requirements	none	no more than 3 Commissioners from same political party	none	none	no more than one Board Member from each Federal Reserve district	no more than 3 Commissioners from same political party	none	no more than 3 Commissioners from same political party
Budgeting	guaranteed percentage of Federal Reserve's operating expenses	subject to congressional appropriations ⁸⁴	subject to congressional appropriations	subject to congressional appropriations	sets its own budget through internal process	subject to congressional appropriations	from assessments on national banks and savings associations; examination fees; and investment income	subject to congressional appropriations
Primary Jurisdiction	all consumer financial protection functions of several agencies, including FTC, Federal Reserve, and FDIC; ⁸⁵ rulemaking, investigatory, and enforcement power over covered persons offering a consumer financial product or service	administration of Commodity Exchange Act— various rulemaking, investigatory, and enforcement powers over trading of commodity futures	matters of the environment on which Congress passes laws	all food except for meat, poultry, and some egg products; all drugs, biological products, and medical devices; all animal drugs and feed; cosmetics; and medical and consumer products that emit radiation	supervision and regulation of District Reserve Banks, U.S. banking system generally; authority over U.S. monetary policy, including sole authority to change reserve rate and approve Federal Reserve Bank discount rates; consumer protection regulation	various rulemaking, investigatory, and enforcement power over consumer protection (“unfair or deceptive acts or practices”) and antitrust (“unfair methods of competition,” including Sherman and Clayton Act violations) violations	supervision of national banks and their subsidiaries; savings associations and their subsidiaries; federal branches and agencies of foreign banks; and institution-affiliated parties that include officers, directors, and employees, as well as a bank's controlling stockholders, agents, and certain other individuals	administration of the securities laws: various rulemaking, investigatory, and enforcement power over violations of federal securities laws
Scope of Judicial Review	courts defer to Bureau interpretations of federal consumer financial law as if the Bureau were the only agency authorized to administer those provisions	Commission orders must be supported by weight of evidence and must be issued with due notice and reasonable opportunity for hearing ⁸⁶	administrative fact-finding and rulemaking subject to arbitrary and capricious review; judicial review of agency interpretations under <i>Chevron</i>	administrative fact-finding and rulemaking subject to arbitrary and capricious review; judicial review of agency interpretations under <i>Chevron</i>	courts must defer to reasonable interpretations of the Federal Reserve Board subject to <i>Chevron</i> ⁸⁷	Commission findings of fact receive deference equivalent to “substantial evidence” standard; otherwise, no statutory mandate of judicial deference ⁸⁸	courts defer to the OCC subject to <i>Chevron</i> , as set forth in <i>Barnett</i> and <i>Smiley</i> ⁸⁹	Commission findings of fact underlying rules and orders must be supported by substantial evidence; Commission fact-finding and rulemaking subject to arbitrary and capricious review ⁹⁰

⁸³ This chart depicts only the SEC's enforcement and rulemaking authority under the Securities Exchange Act of 1934; it excludes SEC filing requirements and authority under other statutes.

⁸⁴ The Commodities Exchange Act provides: “There are authorized to be appropriated such sums as are necessary to carry out this chapter for each of the fiscal years 2008 through 2013.” 7 U.S.C. § 16(d).

⁸⁵ Other agencies are the National Credit Union Administration, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, and the Department of Housing and Urban Development.

⁸⁶ Furthermore, Commission orders must not violate the Constitution and must be within the Commission's jurisdiction.

	CFPB	CFTC	EPA	FDA	Federal Reserve	FTC	OCC	SEC ⁹³
Cease and Desist Authority	authority to issue cease and desist order, effective after 30 days with opportunity for hearing within 30-60 days, for any violation of a law, rule, or condition imposed in writing by the Bureau; authority to issue temporary cease and desist order, effective upon service, if violation is likely to cause insolvency or prejudice to consumers' interests	authority to issue cease and desist order, after notice and opportunity for hearing, for violation of any provision, rule, regulation, order by a person or contract market; ⁹¹ authority to issue cease and desist order, after notice and opportunity for hearing, if Commission reasonably believes a person is manipulating or attempting to manipulate prices	authority to issue administrative compliance orders	authority to issue cease and desist order	authority to issue cease and desist order, after notice and opportunity for hearing within 30-60 days and effective after 30 days, if reasonable cause to believe unsafe or unsound practice, or violation of law, rule, regulation, condition imposed in writing by Board, or agreement with Board; ⁹² authority to issue temporary cease and desist order, effective upon service, if likely to cause insolvency or significant dissipation of assets or earnings ⁹³	authority to issue cease and desist order, effective 60 days after service or upon completion of appeals and petitions for court review, if reason to believe violation has occurred	authority to issue cease and desist order, after notice and opportunity for hearing within 30-60 days and effective after 30 days, if reasonable cause to believe unsafe or unsound practice, or violation of law, rule, regulation, condition imposed in writing by Board, or agreement with Board; ⁹⁴ authority to issue temporary cease and desist order, effective upon service, if likely to cause insolvency or significant dissipation of assets or earnings ⁹⁵	authority to issue cease and desist order, after notice and opportunity for hearing within 30-60 days, upon Commission finding of violation of any provision, rule, or regulation; ⁹⁶ authority to issue temporary cease and desist order, effective upon service, if violation is likely to result in significant dissipation or conversion of assets, significant harm to investors, or substantial harm to the public interest

⁸⁷ *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984) (“First, always, is the question whether Congress has spoken directly to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court as well as the agency must give effect to the unambiguously expressed intent of Congress. . . . If the Court determines Congress has not directly addressed the precise question at issue, the court does not simply impose its own construction of the statute. . . . Rather, if the statute is silent or ambiguous with respect to the specific question, the issue for the court is whether the agency’s answer is based on a permissible construction of the statute.”).

⁸⁸ One exception is rulemaking on consumer protection, which must be supported by substantial evidence.

⁸⁹ Under Dodd-Frank, preemption determinations are reviewed under the Skidmore standard that considers the thoroughness of the OCC’s consideration, the validity of the OCC’s reasoning, the consistency with the OCC’s other determinations, and any other factors that the court finds persuasive and relevant to its decision.

⁹⁰ Specifically, Commission rules must not be “arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; contrary to constitutional right, power, privilege, or immunity; in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; or without observance of procedure required by law.” 15 U.S.C. § 78y(b)(4).

⁹¹ For contract markets, a cease and desist order may also include a civil penalty of up to \$500,000 per violation.

⁹² Orders also may require that the subject take steps to correct conditions resulting from violations or practices.

⁹³ Specifically, temporary cease and desist orders are permissible if “the violation or threatened violation or the safe or unsound practices or practices . . . is likely to cause insolvency or significant dissipation of assets or earnings of the depository institution, or is likely to weaken the condition of the depository institution or otherwise prejudice the interests of its depositors prior to the completion of the proceedings.” 12 U.S.C. § 1818(c)(1).

⁹⁴ Orders also may require that the subject take steps to correct conditions resulting from violations or practices.

⁹⁵ Specifically, temporary cease and desist orders are permissible if “the violation or threatened violation or the safe or unsound practices or practices . . . is likely to cause insolvency or significant dissipation of assets or earnings of the depository institution, or is likely to weaken the condition of the depository institution or otherwise prejudice the interests of its depositors prior to the completion of the proceedings.” 12 U.S.C. § 1818(c)(1).

⁹⁶ Orders also may require that the subject take steps to effect compliance.

	CFPB	CFTC	EPA	FDA	Federal Reserve	FTC	OCC	SEC ⁹⁷
Other Remedies	fines up to \$1,000,000 plus discretion to fashion any appropriate legal or equitable remedy (aside from exemplary or punitive damages)	authority to seek equitable relief, including injunctive relief, in court; authority to seek civil penalties of up to \$100,000 (or triple monetary gain) per violation or up to \$1,000,000 for manipulation or attempted manipulation	authority to seek civil and criminal penalties, as well as injunctive relief; authority to issue administrative compliance orders	authority to seek civil and criminal penalties; as well as injunctive relief	discretion to fashion appropriate remedies in cease and desist orders, including authority to limit activities of insured institution; authority to seek civil penalties up to \$1,000,000 and restraining orders in court	authority to seek civil penalties and equitable remedies, including injunctive relief, in court; authority to order other remedies that bear reasonable relation to violations, such as divestiture or rescission of a merger	discretion to fashion appropriate remedies in cease and desist orders, including authority to limit activities of insured institution; authority to seek civil penalties up to \$1,000,000 and restraining orders in court	injunctive relief; ⁹⁷ suspension or revocation of broker-dealer and investment advisor registrations; bars from association with the securities industry; civil monetary penalties; disgorgement; censure

⁹⁷ Injunctive relief is available only in civil actions. All other remedies are available in both civil and administrative proceedings.

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