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CROSS-PRACTICE CLIENT ALERT: LITIGATION & PUBLIC POLICY

THE CFPB: NEW DIRECTOR, NEW POWERS, NEW THREATS-POLITICAL AND JUDICIAL

Last week, the Senate held its first hearing on the Consumer Financial Protection Bureau (CFPB) following President Obama's controversial recess appointment of former Ohio Attorney General Richard Cordray to lead the CFPB. The Senate Banking Committee met to review the First Semi-Annual Report of the CFPB, which discussed the CFPB's near term goals and stated that the CFPB will "intensify" the pace of its efforts to "make consumer financial markets work better" over the next six months. Although Senator Roger Wicker (R-MS) called for a Republican boycott of the hearing, several Republicans, including Ranking Member Richard Shelby (R-AL), attended the hearing to reiterate their legal concerns and questions resulting from the appointment of Mr. Cordray and the CFPB's attempt to wield powers reserved for a Bureau with a Senate-confirmed Director in place.

Much of the appointment's controversy has focused on whether a recess appointment meets the requirements necessary for the CFPB to enjoy its full range of powers granted under the Dodd-Frank Act. In a report released last year, the Inspectors General of the Federal Reserve and Treasury Department explained that the Dodd-Frank Act authorizes the Secretary of the Treasury to execute the pre-existing powers transferred to the CFPB (not newly established powers) until a Senate-confirmed Director is in place. However, the CFPB cannot exercise its new authority to prohibit certain "unfair, deceptive, or abusive acts or practices," and cannot supervise the activities of non-depository institutions (e.g., payday lenders, mortgage lenders, and student loan lenders), until a Director is "confirmed by the Senate." Because of the Senate-confirmation requirement, there is uncertainty whether a recess appointment of the Director allows the CFPB to exercise the new consumer protection and non-bank regulatory powers authorized by Dodd-Frank.

Someone almost certainly will challenge the CFPB's exercise of the new powers that depend on the appointment of a Senate-confirmed Director. The most likely challengers will be one of the newly-regulated nonbank financial institutions, but might also include a trade association, or a Member of Congress. A court may entertain an action by a newly-regulated nonbank financial institution that can prove it is (or imminently will be) injured by a CFPB regulation or enforcement action. There is also the possibility that Mr. Cordray's appointment will be overturned due to challenges to other recess appointments made by President Obama at the same time. In the last few weeks, at least three groups have challenged the President's recess appointments to the National Labor Relations Board, arguing that the appointments, "brazenly violate constitutionally established separation of powers." If these challenges succeed, Mr. Cordray's appointment will likely be overturned as well. If they fail, it may be more difficult for interested parties to argue successfully that Mr. Cordray's appointment was unconstitutional.

Regardless, since President Obama's announcement, the CFPB has wasted no time in moving forward with plans to regulate nonbank financial institutions and crack down on "abusive practices." In his first speech after his recess appointment, Director Cordray noted, "now, with a Director, the CFPB can exercise its full authorities – with respect to both banks and nonbanks – to help those markets operate fairly, transparently, and competitively." The CFPB has also already issued a press release launching its nonbank supervision program. In the release, the CFPB states that "effective immediately, the CFPB has authority to oversee nonbank financial businesses, regardless of size, in certain markets: mortgage companies; payday lenders; and private education lenders." It also notes that, "the CFPB may supervise any nonbank that it has a reason to determine is engaging or has engaged in conduct that poses risks to consumers with regard to consumer financial products or services," and states that, "the CFPB will be publishing rules setting out procedural guidelines for implementation of this provision."

Going forward, barring legal challenges to the agency, those institutions that now fall under the CFPB's jurisdiction should expect to see a rulemaking procedure similar to that found at other agencies. The Dodd-Frank Act requires that the CFPB, like other banking agencies, "consider" the costs and benefits of a rulemaking (though the CFPB does not have to prepare a detailed cost-benefit analysis). The CFPB is also subject to the Administrative Procedures Act, and therefore must provide notice and an opportunity to comment to the public on all proposed rules. Further, the CFPB must evaluate the potential impact of a rule on small businesses and give small businesses a preview of new proposals before it gives notice to the broader public.

Newly regulated entities should consider the CFPB's Supervision and Examination Manual(the Manual), issued on October 13, 2011. The Manual explains how the CFPB will supervise and examine consumer financial service providers, including both depository and non-depository institutions. The three-part Manual describes the CFPB's compliance and supervision process and its examination procedures, and provides templates for reporting risk assessments, examination results, and supervision plans. Among other topics, it includes sections on the CFPB's authority to prevent regulated entities from engaging in "unfair, deceptive, or abusive acts or practices." However, although the Manual applies to non-depository institutions, it is likely that the agency will soon release additional examination procedures specific to the new industries falling under its jurisdiction.