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New Lawsuit Attacks Constitutionality and Authority of the CFPB and FSOC

The Competitive Enterprise Institute (CEI), one of the organizations that filed briefs supporting the recent challenge to the Affordable Care Act, has now brought a constitutional challenge seeking to block two major President Obama initiatives born out of the Dodd-Frank Act of 2010. CEI, a Washington, D.C. nonprofit, has joined forces with a small-town Texas bank and an advocacy organization for seniors to ask a federal court to find that the Consumer Financial Protection Board (CFPB) and Financial Stability Oversight Council (FSOC) violate the checks and balances system of the U.S. Constitution. They also contend that the recess appointment of Richard Cordray as CFPB Director was an unconstitutional evasion of the Senate confirmation prerogative.

The complaint, filed June 21, 2012 in the District Court for the District of Columbia (*State Nat. Bank of Big Spring v. Geithner*, 1:12-cv-01032-ESH (available at <http://cei.org/legal-briefs/state-national-bank-big-spring-et-al-v-geithner-et-al>), alleges harm to the plaintiffs from new regulations under Dodd-Frank. The Bank of Big Spring alleges that: onerous new CFPB rules have driven it out of the international wire-transfer business; that its consumer mortgage activity has been shut down under the chill of Dodd-Frank's vague proscriptions against "unfair, deceptive, or abusive" practices; and that the FSOC, when it designates certain entities as "too big to fail," will unfairly disadvantage smaller institutions perceived as higher-risk. The Bank of Big Spring could have standing issues because, due to its size, it may not be subject to direct CFPB scrutiny. However, as asserted by the CFPB, the scope of its powers could certainly cover certain lines of business operated by the Bank of Big Spring.

If the plaintiffs can withstand a challenge to their standing, constitutional questions will come to the forefront. The plaintiffs contend that the CFPB and FSOC are overly insulated from political accountability, contrary to the checks and balances provided by the Constitution. The CEI previously advanced similar arguments in a landmark case in which the Supreme Court of the United States struck down a provision of the Sarbanes-Oxley Act requiring the President to delegate certain executive powers to a supervisory body. See *Free Enterprise Fund v. Public Co. Accounting Oversight Bd.*, 130 S. Ct. 3138 (2010) (available at <http://www.supremecourt.gov/opinions/09pdf/08-861.pdf>). In that case, plaintiffs argued that Congress had created an executive office too far removed from accountability to the President, the Accounting Oversight Board. The Board was to be supervised by the SEC, which could, however, remove members only for cause. The President had no authority to fire the Board members himself; they were insulated by a layer of bureaucracy. Therefore, the Court determined the provisions of Sarbanes-Oxley creating the Board were unconstitutional as an encroachment on the President's power to hold executive-branch officials accountable.

Plaintiffs also seek to overturn the standard for Executive removal of agency officials. According to the complaint, the Director of the CFPB cannot be removed at the pleasure of the President but only for "inefficiency, neglect of duty, or malfeasance in office." This

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longstanding standard has been considered constitutional for purposes of executive delegation, and was not altered by *Free Enterprise Fund*. In addition, plaintiffs allege that other checks and balances are lacking. Congress cannot rein in the CFPB's power using its funding authority because the Director can unilaterally appropriate funding from the Federal Reserve's operating budget. Judicial review of the CFPB is limited by a provision of Dodd-Frank requiring courts to show deference under the *Chevron* standard. *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 387 (1984) ([available at http://www.law.cornell.edu/supct/html/historics/USSC_CR_0467_0837_ZS.html](http://www.law.cornell.edu/supct/html/historics/USSC_CR_0467_0837_ZS.html)). In sum, the plaintiffs argue that the CFPB enjoys unconstrained power that goes beyond what the Constitution allows.

In a similar vein, the complaint alleges that the current autonomy given to the Financial Stability Oversight Council, a multi-agency body set up to forestall future financial crashes, is unconstitutional. The FSOC will designate certain banks for special status and heightened oversight because of their size and importance to the financial system. The plaintiffs allege that this structure impermissibly delegates executive functions to persons outside the authority of the President: state insurance and banking officials will choose several members of the fifteen-member Council. The complaint concedes that these officials will have no vote, but points out that they will be able to "participate in its deliberations and proceedings." In addition, the complaint charges that the lack of judicial review for FSOC determinations violates the Constitution's system of checks and balances.

The remaining count in the complaint alleges irregularity in President Obama's appointment of Richard Cordray as the first full-fledged Director of the CFPB. Plaintiffs allege this appointment, carried out while the Senate asserted itself still to be in session, may not have qualified as a "recess appointment" under the precedents for such appointments. The relief sought here is an injunction against Cordray alone – but removing him as Director would also hobble the Bureau because of the statutory requirement for the Director's involvement in many of its activities.

The complaint in *Big Spring Bank* asks the federal courts to go far beyond the 2010 *Free Enterprise* decision, and find the delegation of executive power to the CFPB and FSOC improper. The case also provides an opportunity to litigate President Obama's installation of Cordray under a disputed interpretation of the rules for recess appointments. If the complaint survives initial attacks — including an almost certain attack on standing — it will be an important case to watch and, though unusual but not unprecedented, other interested parties (including banks and trade associations) may want to consider filing amicus briefs.

