Consumer Finance Monitor (Season 6, Episode 4): How the U.S. Supreme Court Will Decide the Threat to CFPB's Funding and Structure: Part II, with Adam J. White, a Renowned Expert on Separation of Powers and the Appropriations Clause and a Close Follower of the U.S. Supreme Court

Speakers: Alan Kaplinsky, Rich Andreano, John Culhane, Michael Gordon, and Adam White

Alan Kaplinsky:

Welcome to the award-winning Consumer Finance Monitor podcast, where we explore important new developments in the world of consumer financial services, and what they mean for your business, your customers, and the industry. This is a weekly show brought to you by the Consumer Financial Services Group at the Ballard Spahr Law Firm. I'm your host, Alan Kaplinsky, the former practice group leader for 25 years, and now senior counsel of the Consumer Financial Services Group at Ballard Spahr.

I'm very pleased to be moderating today's program. For those of you who want even more information, don't forget about our blog, consumerfinancemonitor.com, shares the same name as our podcast show. We've hosted our blog since 2011, so there's a lot of relevant industry content there. We also regularly host webinars on subjects of interest to those in the industry. To subscribe to our blog or to get on the list for our webinars, please visit us at ballardspahr.com. If you like our podcast, please let us know about it.

Leave us a review on Apple Podcast, Google, or wherever else you obtain your podcasts. Also, please let us know if you have ideas for other topics that we should consider covering, or if you can recommend speakers that we should consider as guests on our show. Well, today is part two of our podcast show. Part one was done a week ago, and the topic, of course, was how the US Supreme Court will decide the threat to the CFPB's funding and structure.

Of course, what we are referring to in the title, is the monumentally important Fifth Circuit opinion that came down several months ago in a case called CFSA versus the CFPB, which amounted to, among other things, a challenge to the funding of the CFPB. The fact that the CFPB is funded not through congressional appropriations, but rather is funded by the Federal Reserve System or the Federal Reserve Board, up to a certain percentage of the Federal Reserve System's budget.

In part one, we featured our very special guest, Adam White, who is back again for part two. Adam is a senior fellow at the American Enterprise Institute, and he's co-director of George Mason University's Gray Center for the Study of the Administrative State. Last year, President Biden appointed him to the Presidential Commission on the Supreme Court of the United States. He also serves on the Administrative Conference of the United States. He is the next chair of the American Bar Association's Administrative Law Section.

We are also joined again today by my three colleagues at Ballard Spahr, Mike Gordon, Rich Andreano and John Culhane. Mike Gordon is an alumnus of the CFPB. He spent many years during the formative period for the CFPB, and he was a special advisor to then Director Richard Cordray. Rich Andreano is the chair of our mortgage banking group at Ballard Spahr. He has particular interest in the impact that this decision could have on the mortgage banking industry. Then finally, let me introduce John Culhane.

John is really an expert in all consumer financial services law. I kid John and other people by saying that he has encyclopedic knowledge of consumer finance law. That means not just the statutes and the regulations, but he knows all the cases, and generally knows the citation in the Federal Reporter for each case, and I kid you not. Without further ado, let's get into our

program today. I'm going to call on Rich, Rich Andreano. First Rich, I don't know if this is the point you're going to make, but I'd like to get your thinking about this severability issue.

Because we had a little colloquy earlier today where we concluded that the severability clause that's in Dodd-Frank, might actually be used here by the Supreme Court. Rich, why don't you start and then like to get the views of my other colleagues.

Rich Andreano:

Yeah. There is a provision, it's almost like Congress envisioned the Fed money not being available or not enough and that the bureau could ask for appropriations, although we think Congress separately could simply outside of that Dodd-Frank provision probably appropriate money. I think the issue would come down to, which we may get a little later, is to get the agreement of Republicans to appropriate funds, what changes to the bureau structure would they insist on? I think that's where it would come down to.

Interestingly, what you would get from the industry, is a strong-arm twist of Congress to make sure the rules stay effective. We saw that in the Seila Law case, where in fact, that we discussed before. That's where the Supreme Court ruled that the for-cause removal provision was unconstitutional and they severed it. Where the industry got worried is Seila Law argued that perhaps the right remedy was to overturn the Consumer Financial Protection Act, which would throw out the bureau and everything with it.

And they were very concerned. The Mortgage Bankers Association, National Association of Home Builders and National Association of Realtors filed an amicus brief with the Supreme Court. They did not address the constitutional question, was the for-cause removal provision constitutional or not? They solely focused on the remedy and said the remedy should simply be limited to severing the for-cause removal provision. Let everything else stand.

They indicated the chaos that would result if all the bureau's rules were thrown out, that lenders would stop making loans, investors would stop buying loans. Consumers couldn't buy or sell homes because no one would make them a loan. They pointed to two rules in particular just to say, this is just two of the rules. One was the Truth in Lending Act, Real Estate Settlement Procedures Act Integrated Disclosure Rule, commonly known as the Trade Rule.

It took the Truth in Lending Act disclosures and the respite disclosures, put them into combined disclosures. Significantly, the bureau with their great exemptive authority, exempted the industry from certain statutory requirements under the rule and modified certain statutory requirements. If you throw that rule out, you're left with a statute and disclosures that don't comply with the statute. The other rule they pointed was the ability to repay rule. The Bedrock Dodd-Frank rule, requiring that mortgage lenders make a reasonable determination that the consumer can repay a loan at the time of consummation of the loan.

Significantly, while the statute gives guidance to the bureau, a lot of the provisions that the industry relies on are provisions solely of regulation based on congressional authority. In particular, the qualified mortgage for loans based on loans being eligible for sale to Fannie and Freddie, is purely a regulatory provision. Billions and billions of dollars were originated under that qualified mortgage safe harbor. If the rule's thrown out, you have billions and billions of dollars of loans that do not comply with the ability to repay statutory provisions.

That's just two rules. It would cascade down. Here you have three major trade associations arguing for a minimalistic remedy. My guess is you'll see those trade associations or even a broader group, file an amicus brief with the Supreme Court making the same arguments in this case. That if they strike down the funding, that there should just be a severance of that provision. But not to throw out the whole validity, and not deem that the lack of funding rendered the rules invalid. Because that would be a very bad result for the industry and for consumers as well. I think you'll see consumer groups and the industry make the same argument.

Alan Kaplinsky:

Yeah, interesting. Strange bedfellows. John, Rich did a really good job of talking about some of the very bad results that might happen in the mortgage area, if the mortgage regs that were adopted early on in the CFPB's life, if they were thrown out. What about the non-mortgage area, John?

John Culhane:

Well, I think in some respects we're in the same place, Alan. There are a lot of rules that the broader consumer financial services industry has structured themselves to operate under and get benefit from. I'm thinking that although there are a lot of maybe individual provisions in Regulation F, the debt collection rule, but debt collectors, if they could pick and choose, would throw tiny pieces out. But the provisions for call frequency, the great support for electronic communications under those rules.

If we throw out the debt collection rule, Regulation F, we're back to real chaos in the collection industry, in terms of what call frequency is permitted, whether texts and emails are subject to the same kinds of limitations as other communications. Another rule that has been very helpful for the industry, are the amendments to Regulation Z that were adopted by the CFPB to accommodate the transition from LIBOR to SOFR. I think we'd really hate to see those rules get thrown out.

There are very extensive rules now for governing remittance transfers. The industry has adopted to those rules. Again, as Rich said with the mortgage rules, there are some provisions there that are actually favorable for the industry. I think that having that thrown out would likewise be problematic. It's a difficult situation, but I think as Rich said, I think probably the trade associations will support having the regulations stay in place.

Ask the Supreme Court not to overturn other regulations, I guess, with the possible exception of the payday loan rule in the case since it hasn't gone into effect.

Alan Kaplinsky:

Yeah. I guess, John, there might be a few industries, sub-industries within the consumer financial services industry, that would probably shed only crocodile tears if the CFPB was eliminated.

But I'm thinking of installment lenders and I don't know, some of the fintech companies that are providing services where there aren't specific regulations that they rely upon.

John Culhane:

Well, yes, certainly the CFPB has proposed an aggressive agenda going forward, yeah.

Alan Kaplinsky:

Right.

John Culhane:

I think there'd be a lot of tears over curtailment of that aggressive agenda, but that may be something that we're going to see through some kind of congressional compromise as to the CFPB going forward.

Alan Kaplinsky:

Yeah. Mike, let me turn to you now because I want you to put on the hat that you wore when you spent five years or so at the CFPB, and there were a number of crises that occurred while you were there. What's the posture of the CFPB now?

I guess there are maybe two postures, what they're saying to the outside world and maybe the discussions that are going on internally, where maybe the look might be a little bit different. But is it business as usual at the bureau?

Michael Gordon:

Certainly publicly, yes, that messaging is loud and clear, and I've heard it from individuals. I think the director is also exuding confidence, and really what choice do they have as an agency on that score? But behind closed doors, I actually think it's not that far off from the public messaging. I would imagine that they would think twice before filing new matters in the Fifth Circuit or initiating new investigations in the Fifth Circuit, but they might go ahead and do it anyway.

We've seen continued activity outside the Fifth Circuit in the enforcement realm. Of course, a flurry of activity for the types of policy guidance and pronouncements that the bureau likes to make these days. We've seen lots of activity on that front, and exams continue and examination work and findings continue. In many ways, it is business as usual and they're continuing to push forward until someone pushes back, and that's not surprising. I think for any agency, I think it's particularly expected for an agency, which takes the aggressive posture that this one does.

Alan Kaplinsky:

Right. Right. Yesterday and the day before, Director Chopra testified before the Senate committee, Financial Services Committee and the House Financial Services Committee. He certainly didn't look like he was quaking in his boots during the hearing. He didn't seem particularly worried about the case. The one thing that I wondered about, but maybe this just isn't in Rohit Chopra's nature, whether he is thinking further down the road that he may have to at some point, this case comes out the wrong way.

He may have to go on bended knee to Congress seeking money for the survival of the CFPB. The more activity that goes on while this case is pending, does he end up, does he run the risk of creating further enemies in Congress? If that's the case, if I were advising him, I might say, "Be a little cautious here during this interim period, because we don't want any of the things that we do in the next several months to come back to haunt us." What's your reaction to that, Mike?

Michael Gordon:

That Rohit probably wouldn't hire you to advise him. Yeah, I think that battle lines have been drawn for quite some time. There's potentially a risk of what you're talking about of some movement politically of people becoming more opposed to the bureau over the next few months, based on the way the bureau behaves than they were before. But that seems marginal to me in the larger calculation.

As you said, I watched Rohit's appearance on the hill this week, and it didn't seem like he was modulating his message or his approach in any way out of that concern or any other concern. They've got an agenda, he feels strongly about it. It involves, I think, in my view, pushing the envelope in certain areas, but they haven't made any public indication that they're going to stop pushing.

Honestly, what I'm saying is I don't think it would make much a difference one way or the other in the final analysis on some legislative compromise how they behave in the next few months.

Alan Kaplinsky:

Right. Right. Let's talk about another topic. Let's say you're handling a case right now, an enforcement case with the CFPB. Is this a good time to get a settlement in the case? If there's a fire sale going on at the bureau while there's this cloud of uncertainty that's hanging over the bureau, would they be more inclined to be a little kinder in the relief that they seek, the civil money penalties that they seek?

Or is it not going to matter to them one way or the other? We have seen a few cases settle since the opinion came down. To me, it struck me that the relief in the civil money penalties didn't seem as Draconian as they sometimes have seemed. Do you think something's going on there, Mike?

Michael Gordon:

Well, I think about this in a couple ways. If you're a litigant on the receiving end of an enforcement matter, you're certainly going to try to drive a harder bargain now before you would settle in light of this constitutional cloud. The bureau, I think, would never admit that they're giving some leeway based on that, but it may very well happen. On the other hand, do you want to be signing an enforcement order that you may never get out from under or be able to reverse, if in fact, the Supreme Court rules against the bureau?

There's an argument for waiting as well. I look back at the recent cases that have been publicly announced or settled since the Fifth Circuit opinion, and I don't see strong indications of the bureau being settling on the cheap right now. Perhaps there was one case with a small specialty funding company that settled and they have to pay back folks who were allegedly harmed to the

tune of $600,000. There was a $1 CMP, which is an odd thing, but it allows the bureau to then let those affected consumers partake of the CMP fund if they're eligible, which they wouldn't if there weren't a penalty assessed.

That number, that $1 number jumped out at me, but I think there's a rationale there, and I'm not sure that that firm is a going concern. The smaller amounts of relief, they could be due to this dynamic or they could have been due to the general circumstances of the case. A couple other cases where CMPs were combined with redress were in the millions, maybe you could argue some of these were on the low end, but I'm not sure. They seemed more or less in the mainstream. It's pretty small, sample size too of cases since the Fifth Circuit decision, so I'm not going to draw that conclusion.

But like I said, what this means, what this decision means for you as an institution, very much depends on your circumstances and where you are. These will be the bureau's exertion of power. If you're in active litigation, it's one thing. If you're in the Fifth Circuit, it's an extreme example. But there are lots of other shades of gray where the bureau may be knocking on your door for an exam, or negotiating around information requests associated with that or some other authority that it has to seek information.

Then finally, there's just general compliance with rulemaking. In that realm, the bureau's not knocking on your door, and you're looking at your compliance obligations as a company. I'm not sure it's a wise thing to consider this case to change your calculation on terms of your compliance obligations, in any sense. Even if there's some theoretical chance that it won't be the CFPB that would enforce them. I think it's wise to, for a lot of reasons, to continue to take the same compliance posture you took prior to this Fifth Circuit decision.

Someone's going to be enforcing these laws. We think it's likely to be the CFPB in some form or another, but the laws aren't going away, even if some of the rules are in question. Of course, in many cases the requirements overlap with state law requirements that you need to follow anyway and state law you'd have. I don't have a lot of clients coming to me saying, "Hey, now we can blow up our compliance program." But there is a range and there is a range of activity. I think each company should think carefully about how this decision might affect what their optionality is.

Alan Kaplinsky:

I'm going to conclude. We're drawing to the end of our webinar. We've got about five minutes left. My final question that I'm going to pose to each of you, is what happens when the dust settles? Supreme Court grants cert, they decide the case, and let's make the assumption that they decide that it's unconstitutional. Commerce gets involved.

If you were to just make a projection of what things are going to look like when all this is said and done, and we've moved on from a discussion of this Fifth Circuit case. I want to start with you, John, first, and then let's go to Rich. Then we'll break it up. I'll go to Adam, and then finally to you, Mike. John, what do you think?

John Culhane:

Well, I think the easy prediction, and I don't want to throw a bunch of things out here, I want to leave room for everybody to discuss this, is we're going to have a five member commission or something similar in charge of the CFPB.

That's going to be, I think, the minimum that the CFPB will be able to escape with and get appropriated funding. I think there are going to be lots of questions about how much and how often. I'd have to think that on the how often, there'll be a fair amount of pressure to have them coming back every year. Let me stop there.

Alan Kaplinsky:

Yeah. Okay. Rich, what do you think?

Rich Andreano:

Yeah. I agree with John on budget, a bipartisan commission. In general, I could see the industry would want some confirmation that the rules are valid rules. They would look to something along those lines, and that'll depend what the Supreme Court does, obviously, if they call into question the legitimacy of the rules.

But if they do, they'd want something to address that. Two particular rules I could see is they probably want the UDAP authority further specified to curtail the extraordinarily broad usage. If I had to pick a specific mortgage rule they would want revisited, it would probably be the servicing rules.

Alan Kaplinsky:

Yeah. The one thing that got alluded to a little bit earlier, and it's really the gravamen of the complaint filed by the Chamber of Commerce against the CFPB.

The industry, I would say, is just about unanimously opposed to the decision by Rohit Chopra to amend the examination manual dealing with the UDAP to encompass or to define the term unfairness to include discrimination.

I have a feeling that's going to be targeted by the industry and by Congress. What do you think, Adam, dust settles? Where are you?

Adam White:

A couple of things. First of all, and we shouldn't discount the possibility the court will affirm the funding structure. If it does, I think what's going to follow from that a few years down the road, the next time that Democrats have unified controlled government, you'll see some talk about giving the SEC and the CFTC a similar funding structure. When the CFPB was first created, the chairs of the SEC and the CFTC both said in hearings and elsewhere, they wanted the same funding structure. Judicial legitimization of the funding structure probably put a wind in those sails.

Now, if the court strikes down the funding structure, I don't anticipate this being the end of the agency at all. In fact, the fact that the appropriations process now is basically done through continuing resolutions and omnibus bills. The showdowns that we see once or twice a year means that it'll probably be easier for an administration to get funding for the CFPB. Because nobody's going to shut down the government over the CFPB, although I suppose those are famous last words, but I don't think they would. To the extent that there is a push for legislative reform of the CFPB, I agree with some of the things that have been said already.

You can see a push for greater specification on UDAP authority, and a push for a multi-member commission structure. Again, that's what then Professor Elizabeth Warren first proposed the CFPB to be, a multi-member commission. Soon after Dodd-Frank's enactment, you did see bills coming out of House Financial Services, Congressman Duffy and Hensarling and others pushing to make the CFPB a multi-member commission like the FTC. It's not hard to imagine those coming back again.

Alan Kaplinsky:

Right. Finally, Mike, I guess I'll give you the last say on our panel.

Michael Gordon:

Yeah. I tend to agree with all the comments we just heard. The only thing I would add to the mix is that it could be a really wild year, because of the brinkmanship that certain parties on the hill may be willing to go to before this is resolved. I think that we're in an interesting time with respect to the lobbying power of the finance services industry. Where because of the mortgage market implications that Rich talked about, they want a quick resolution by Congress that preserves status quo on certain mortgage rules.

But I'm not sure their voice is as strong as it used to be, frankly. On the Republican side of the aisle, there's a very mixed environment in terms of the political pressures. Put that all in with a new House leadership that, I think, is already signaling a willingness to play hardball on certain issues. They may choose to play hardball on this issue, even if industry's uncomfortable with that. I think it'll be a wild process to get there.

But I agree, in the end of the day, the bureau in some form will exist. That form could very well be a commission, and there might be some other tinkering with the bureau's authorities on top of it.

Alan Kaplinsky:

I want to thank Adam White, our very special guest today, and I want to thank my colleagues at Ballard Spahr, Mike Gordon, Rich Andreano and John Culhane. Of course, I want to thank all of our listeners today, who have downloaded our podcast show and who probably, I'm assuming most of you, have already heard part one. But if you haven't, I strongly encourage you to listen to part one, because there is a lot of pithy analysis of the Supreme Court case and predictions as to the outcome by Adam White, our special guest.

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