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GUEST COMMENTARY

HOW *NOEL CANNING* MAY IMPACT THE CFPB, RICHARD CORDRAY, AND CONSUMER FINANCIAL SERVICES

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The District of Columbia U.S. Circuit Court of Appeals has ruled on the highly-anticipated case of *Noel Canning v. NLRB*, in which the legality of President Barack Obama's recess appointments to the National Labor Relations Board were challenged. In light of the D.C. Circuit's decision to invalidate the appointments of three NLRB board members, the validity of Consumer Financial Protection Bureau director Richard Cordray's "recess" appointment has justifiably come into question.

This article analyzes the impact of the *Noel Canning* decision on the Cordray appointment as well as the more challenging issue of how an invalidation of Cordray's appointment would impact the various settlements, enforcement actions, and regulations implemented by the CFPB since Cordray's appointment.

THE RELEVANT STATUTORY BACKGROUND

The CFPB was created by Title X of the Dodd-Frank Wall Street Reform Act. Signed into law on July 21, 2010, Dodd-Frank created the CFPB as an independent agency within the Board of Governors of the Federal Reserve System. Dodd-Frank tasked the CFPB with implementing and enforcing the regulations of consumer financial products and services under federal consumer financial laws. The CFPB, as mandated by Dodd-Frank, is to be headed by a President-appointed and Senate-confirmed director.

In addition to the authorities created under Dodd-Frank — such as the power to supervise non-depository institutions and the power to adopt new rules prohibiting unfair, deceptive, or abusive acts in connection with consumer financial products — the CFPB would be transferred certain authorities from several different federal agencies, including the FDIC, FTC, NCUA, OCC, OTS, and HUD.

The transferred powers consisted of supervisory and enforcement authority over large banks, savings associations, and credit unions. Although the newly-established powers of the CFPB were made dependent upon a director being put in place, the powers transferred to the CFPB from other federal agencies were fully in effect as of July 21, 2011. In fact, a report by two inspectors general of the Treasury Department and Federal Reserve confirmed that Dodd-Frank permits the CFPB to carry out certain powers over depository institutions even without a director, including prescribing rules, issuing orders, and providing guidance where such actions were previously within the authority of the transferor agency.

That said, a director-less CFPB is powerless against non-depository institutions such as auto lenders, credit-card companies, credit reporting agencies, debt collectors, debt managers, mortgage companies, mortgage servicers, payday lenders, and private education lenders.

THE APPOINTMENT

On July 17, 2011, President Barack Obama announced the nomination of former Ohio attorney general and then CFPB enforcement chief Richard Cordray as director of the CFPB. In objection to a perceived lack of congressional oversight of the CFPB's activities as well as a lack of accountability, Senate Republicans refused to confirm any nominee to the position without first instituting several amendments to the agency's structure. Among their con-

cerns, Senate Republicans took issue with the fact that the bureau would be headed by a single director, as opposed to a five-member commission.

On Jan. 4, 2012, a day after Congress had convened the second session of the 112th Congress as required by the Constitution, President Obama invoked the "Recess Appointments Clause" and appointed three individuals to the National Labor Relations Board, as well as Cordray as director of the CFPB.

THE *NOEL CANNING* DECISION

Oddly enough, the decision that thrust the status of Cordray's appointment and all subsequent CFPB conduct up into the air had nothing to do with CFPB.

In *Noel Canning v. NLRB*, Nos. 12-1115 & 12-1153, 2013 WL 276024 (D.C. Cir. 01/25/12), bottler Noel Canning objected to a decision of the NLRB which found it in violation of the National Labor Relations Act. Among other arguments, Noel Canning asserted that the NLRB's decision was made without authority because three of the five members of the board were never validly appointed, and as such, the NLRB never had the necessary quorum.

The D.C. Circuit agreed with Noel Canning, finding that the appointments were, in fact, unconstitutional and invalid. The decision of the court centered on the fact that the appointments were not made while Congress was in "the Recess," and non-recess appointments may only be made "by and with the Advice and Consent of the Senate."

In defense of the appointment, the government argued for an expansive interpretation of "the Recess" to include intra-session breaks of the Senate. Using textual, structural, and historical arguments, the court rejected the government's interpretation. Although the court's interpretation of "the Recess" was sufficient grounds to render the NLRB appointments invalid, the court also found that in order for the President to invoke the Recess Appointments Clause, the vacancy must actually happen or arise during "the Recess" of the Senate. In doing so, the court specifically rejected the government's argument that "happen" should be read as "happen to exist" during the Recess.

THE POTENTIAL IMPACT

As noted earlier, the appointment of Cordray as director of the CFPB occurred simultaneously with the appointment of the three NLRB members invalidated in *Noel Canning*. In light of the fact that CFPB director clearly falls into the category of "Officers of the United States" as that term is used in the Appointments Clause of the Constitution, there does not appear to be any legal basis for differentiating between President Obama's appointment of the NLRB members and his appointment of Cordray.

Therefore, it seems beyond doubt that the same panel of D.C. Circuit judges that decided *Noel Canning* would likewise find the appointment of Cordray to have run afoul of the Appointments Clause. It is still unknown whether the Obama Administration plans to appeal the *Noel Canning* decision, and if it did, a specific outcome is far from predictable.

It should also be noted that President Obama nominated Cordray on Jan. 24th, 2013, as CFPB director. However, this nomination itself would not have any impact on the legality of the conduct taken by the CFPB since the Jan. 4, 2012 "Recess nomination."

Much of the following analysis will be rendered moot if the *Noel Canning* decision is reversed on appeal. However, if the D.C. Circuit's interpretation does stand the legality of a host of CFPB activity would be in flux.

For example, all CFPB actions taken against non-depository institutions are arguably void. As stated earlier, the only authority held by the CFPB prior to the appointment of Cordray was whatever authority was transferred to the CFPB from other federal agencies. The power to prohibit unfair, deceptive, or abusive acts in connection with consumer financial products and services, and the power to supervise non-depository institutions were not among those powers transferred to the CFPB.

There are numerous examples of CFPB activities during the past year that are in legal limbo post-*Noel Canning*:

- The CFPB's recent regulations relating to "qualified mortgages" and mortgage servicing guidelines.
- A CFPB probe into potentially illegal collusion between insurance company AIG and mortgage lender MGIC.
- A CFPB probe into the mortgage-insurance practices of non-depository mortgage servicing companies.
- A joint enforcement action with state attorneys general against Payday Loan Debt Solutions Inc. for unlawful fees.

Other CFPB post-appointment activities appear to be on more solid ground based on the CFPB's pre-director authority over large banks:

- An enforcement action against Discover Financial Services (CFPB jointly with the FDIC).
- An enforcement action against Capital One for deceptive marketing (CFPB jointly with the OCC).
- An enforcement action against American Express for violating consumer protection laws (CFPB jointly with the FDIC).

Although it is too early to speak conclusively about the lawfulness of particular CFPB activities, much of the activity undertaken by the CFPB over the past year could appropriately be described as *ultra vires*. It is obvious that supervisions, enforcements, and regulations of non-banking entities enacted during the subject period would have been outside the scope of the CFPB.

THE CHALLENGE TO THE APPOINTMENT

More interesting is the impact that an invalidation of Cordray's appointment would have on consent orders and settlements made during the period.

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While an argument may be made that such consent orders and settlement agreements were voluntarily entered into, and thus were not *ultra vires*, an argument may also be made that such agreements were made under a false duress placed upon the subject party. Additionally, parties that do not wish to remove themselves from their earlier agreements with the CFPB might consider obtaining a reaffirmation of the terms of the agreement to ensure its validity going forward.

In order to challenge Cordray's appointment in federal court, the plaintiff bringing suit must have standing. In past challenges under the Appointments Clause, courts have looked to whether the plaintiff was directly subject to the government authority they seek to challenge and whether the specific appointment is the source of the government authority. Furthermore, U.S. Supreme Court precedent indicates that judicial review of an Appointments Clause challenge will proceed even where any possible injury is "radically attenuated," and several federal courts have stated that plaintiffs making such a challenge need not show that they would not have suffered their injury if the officials had been properly appointed. In sum, federal standing jurisprudence in Appointments Clause cases appears to be quite liberal.

Given that the newly-created powers provided to the CFPB by Dodd-Frank would not have been available without a director, it appears clear that any CFPB assertion of such a power against a particular entity would provide that particular entity with standing to challenge Cordray's appointment. In fact, the unique relationship created by Dodd-Frank between the scope of the authority of the CFPB and the appointment of a director makes proving the relationship between Cordray's appointment and any challenged CFPB activity all the easier.

What is less clear is whether any party subject to the rules and regulations issued by the CFPB pursuant to its Dodd-Frank powers has standing, regardless of whether they were subject to an enforcement action. However, in light of the Supreme Court's broad interpretation of standing in Appointments Clause cases, it is certainly possible that such a party would be found to have standing to challenge Cordray's appointment.

There is currently at least one active challenge to the appointment of Cordray in federal court. In the case of *State National Bank of Big Spring, et al. v. Geithner* (*Wolin*)*, et al.*, No. 1:12-cv-01032 (D.D.C., *complaint filed* 06/21/12; *amended complaints filed* 09/20/12, 02/13/13), a Texas community bank is challenging the constitutionality of several aspects of the CFPB, including the appointment of Cordray. On Nov. 20, 2012, the government filed a motion to dismiss on the grounds that the plaintiffs lacked standing. As of the most recent amended complaint filed on Feb. 13, 2013, 13 state attorneys general have joined as plaintiffs.

Even assuming that the plaintiffs are found to have standing in the *Big Spring* case, a definitive answer on Cordray's appointment is not likely to come anytime soon. Should the Obama administration decide to challenge the *Noel Canning* decision on appeal and the Supreme Court grants *certiorari*, it will likely quite be quite some time before the Supreme Court comes down with its decision. In fact, it is not rare for Supreme Court decisions to come more than eighteen months after the challenged decision of the Court of Appeals is issued.

THE IMPACT ON CFPB GOING FORWARD

Regardless of how the lack of a CFPB "director" would affect past CFPB conduct, the legal battling will surely impact CFPB regulated non-depository entities going forward. Some of the uncertainties in the wake of *Noel Canning* include the following:

1. Will the CFPB have to cease all in-process examinations of non-depository companies until it gets a validly nominated director?
2. Will any past enforcement action settlements by the CFPB be undone, or will any party to a past settlement demand return of settlement funds paid to the agency?
3. Will any company that produced data to the CFPB in response to a civil investigative demand (CID), seek to claw-back their documents and data until such time as the agency actually establishes exam power over non-depositories?
4. Last month the Senate passed a bill that adds the CFPB to the list of federal banking agencies which may receive privileged information without causing a waiver of the attorney-client privilege as to third-parties. In light of the fact that the agency may have obtained data from non-depository companies during *ultra vires* examinations, is the agency-examination privilege with respect to such data void?
5. If the CFPB's exam privilege is blown, can the CFPB tack-on, or claim another agency's exam privilege, in all cases where other federal regulatory agencies (e.g., the FTC and FDIC) were jointly involved and also obtained the data?
6. Last year, the CFPB entered into information-sharing agreements with state attorneys general and with the Conference of State Bank Regulators in order to coordinate their reach over activities of non-depository institutions. If the CFPB's exam privilege is no longer in play, how will that affect tainted exam data shared with the state regulators pursuant to those agreements?
7. If the Obama administration proceeds forward with an attempt to have Cordray confirmed by the Senate, will the confirmation process devolve into a public cross-examination as to every arguably *ultra vires* exam activity, enforcement action, or utilization of the new authorities provided in the Dodd-Frank Act — going back 18 months?
8. If the CFPB signed a regulatory enforcement settlement against a non-depository entity and such enforcement activity is ultimately found to have been *ultra vires*, then would this destroy the claim preclusion protection that the non-depository institu-

tion bargained for?

9. Will a prolonged stalemate in a Senate confirmation force the CFPB to realign resources and to redeploy folks back to the FTC — which is arguably the only federal regulator over the past 18 months to legally possess (although limited to UDAP) the power to regulate non-depositories?
10. If a stalemate occurs, then what are all the recent hires at the CFPB in the non-depository exam and enforcement group going to do with their time and resources?
11. Is the only certain and quick fix to the CFPB's stalemate problems to concede to Republican demands for a 5-person board and for Financial Stability Oversight Council veto-power and oversight of the CFPB?

While it is too early to fully analyze the impact of the *Noel Canning* decision on the CFPB's post-director conduct, an argument may be made that all CFPB actions taken pursuant to the director-dependent authorities created by Dodd-Frank are invalid and subject to legal challenge.

Regulated entities should be advised, however, that not all powers possessed by the CFPB are dependent upon having a director, and CFPB actions taken pursuant to those transferred powers appear beyond reproach.

The greatest uncertainty lies in between, where regulated entities voluntarily entered into consent orders or settlement agreements in the shadow of regulations and enforcements for which the CFPB may never have had the authority to enact in the first place.

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