

The CFPB Survived The High Court, But Will All Of Its Rules?

By Jon Hill

Law360 (July 6, 2020, 10:42 PM EDT) -- The U.S. Supreme Court's decision settling the long-standing debate around the constitutionality of the Consumer Financial Protection Bureau's structure may have opened a Pandora's box for pending litigation and past rulemaking.

After the high court held last week that it is unconstitutional for the CFPB director to be shielded from presidential removal, the current occupant of that post, Kathleen Kraninger, posted on Twitter that the decision leaves the agency's rules and regulations intact and "finally brings certainty to the operations of the bureau," which has faced repeated constitutional challenges to its single-director structure over the years.

But financial services attorneys said the *Seila Law v. CFPB* decision raises fresh questions about where the agency goes from here. Not only could the ruling create a new path for enforcement targets to resist agency investigations and lawsuits, it could also give Kraninger a chance to line-edit the CFPB's rulebook, they said.

"If the director chose to, she could be very strategic in saying that this or that rule was not validly passed and refuse to ratify it," said Gregory Lisa, a former CFPB enforcement attorney who is now a partner at Hogan Lovells. "There's a real chance of this being a several-months-long opportunity to do some real rewriting of historical bureau activity. That could be even more impactful than new rulemaking."

Although the Supreme Court deemed the CFPB to be unconstitutionally structured, the justices didn't strike down the entire agency. Instead, they ruled that the agency's flawed design could be fixed just by eliminating the director's tenure protection, lifting the statutory restriction placed on the president's removal power.

"The agency may therefore continue to operate, but its director, in light of our decision, must be removable by the president at will," Chief Justice John Roberts wrote in the majority's opinion.

That tweak may put the CFPB on a solid constitutional footing going forward, but it leaves a cloud hanging over prior agency actions taken when the tenure provision was still in effect. Those actions could be viewed as illegitimate and discarded, much as California law firm *Seila Law LLC* wanted the justices to do with the investigative demand at the heart of its fight with the agency.

The demand was issued in 2017, when the CFPB was helmed by its removal-protected first director,

Richard Cordray. Yet the agency has argued the demand was later "cured" of any constitutional flaw stemming from this removal protection because the demand was allegedly ratified, or reauthorized, by Cordray's temporary successor, Mick Mulvaney, who wasn't removal-protected.

The high court majority stopped short of saying whether the demand remains enforceable, citing "case-specific factual and legal questions" surrounding ratification that hadn't been fully addressed in earlier stages of the case. As a result, the justices said they would leave it to the Ninth Circuit "to consider whether the civil investigative demand was validly ratified."

But the move to remand the case nevertheless "suggests that ratification is a live legal issue," said Eric Mogilnicki, a Covington & Burling LLP financial services partner.

"Although the court doesn't quite say that ratification is required, it does suggest that ratification matters, and if it matters for Seila Law, it matters for a lot of folks in a lot of contexts," Mogilnicki said.

"The Supreme Court may have unwittingly turned the world topsy-turvy, because if it's important that a director who can be terminated [by the president] ratify each and every action of the bureau over the last nine years, then Director Kraninger potentially has enormous authority now to undo much of what former Director Cordray accomplished in his tenure," he added.

The CFPB has so far not staked out comprehensively how Kraninger plans to approach the ratification issue, but there is precedent from Cordray, who faced questions about his legitimacy following his controversial January 2012 recess appointment to the agency's top post.

Once the Senate confirmed him as director in July 2013, Cordray sought to tamp down any doubts about the agency's regulatory and enforcement work by publishing a Federal Register notice affirming that he stood by "any and all actions" he had taken up to that point as "legally authorized and entirely proper."

But attorneys who spoke to Law360 said that Kraninger isn't necessarily obligated to stick up for every last regulation, investigation and ongoing enforcement action.

Kraninger has already shown a willingness to revisit regulations written before her arrival at the agency, most notably backing an effort to rescind payday lending underwriting standards that is poised for completion any day now.

"She could, in the interest of clarity, simply ratify all actions taken by prior directors, but the temptation should be considerable to pick and choose," Mogilnicki said.

Lisa agreed that Kraninger will have flexibility to pursue ratification selectively if she so desires. That could be done actively, such as by stating which specific regulations she is rescinding as unconstitutionally approved, or it could take a more passive form, such as by saying nothing for now and instead waiting for rules to be challenged in court.

But it may be tougher for Kraninger to back away from open enforcement cases, according to Lisa.

"On an enforcement action, I think there's going to be a little more pressure to let that continue, especially if there's been additional activity and investment that she, by implication, has endorsed," Lisa said.

Still, even if Kraninger casts a wide net, attorneys told Law360 to expect litigation over whether ratification is enough to salvage pre-Seila actions from post-Seila challenges or whether that lets the CFPB off the hook too easily for its past unconstitutionality.

"When the prior acts were unauthorized to begin with, I'm not so sure ratification is the fix," said Joann Needleman, leader of Clark Hill PLC's consumer financial services regulatory and compliance practice group. "There has to be a consequence for a bad act."

Needleman, who has been representing clients in CFPB matters, said that while it would be difficult to contest old settlements and long-closed cases, she sees more scope for pushing back in open cases.

"For matters that are still pending that were decided by either Cordray or Kraninger, we now know that [agency] structure was unconstitutional," Needleman said. "I think there's an argument to be made ... I can't believe that ratification is that simple."

To be on the safe side, some attorneys suggested that Kraninger could go one step further than ratification and hit reboot on the CFPB's enforcement docket, reissuing all investigative demands and refiling all pending lawsuits.

Lisa viewed it as unlikely that the CFPB would go that far, but he acknowledged that there "may be some windows for tactical opportunities" in the coming months for companies facing agency investigations or enforcement actions to dispute issues like the validity of tolling agreements signed when the agency had a removal-protected director.

"The key things right now for the bureau's leadership to decide are what they are legally entitled to do, what as a policy and political matter they would like to defend, and what resources they want to use to defend those choices," Lisa said. "No matter what, some part of that decision is going to invoke litigation on the other side, or at least the threat of litigation."

--Editing by Jill Coffey and Michael Watanabe.