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"The Administrative State v. The Constitution: Dodd-Frank At Five Years"

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Chairman Cornyn, Ranking Member Durbin, and distinguished members of the Committee, thank you for inviting me to testify on the constitutionality of the Dodd-Frank Wall Street Reform and Consumer Protection Act and the important watchdog agency created by that legislation: the Consumer Financial Protection Bureau (CFPB). My name is Deepak Gupta. I am the founding principal of Gupta Wessler PLLC, a law firm focusing on appellate and constitutional litigation. I previously served as Senior Counsel at the CFPB, where my duties included defending the new agency and its programs in court and advising its leadership on constitutional issues. My testimony today makes three basic points:

***First*, the constitutional challenges to Dodd-Frank lack merit.** It has been five full years since Dodd-Frank's enactment. In that time, the Act's opponents have invoked every conceivable constitutional principle—from the separation of powers, to the void-for-vagueness doctrine, to procedural due process—in an effort to turn back the clock on financial reform and consumer protection. These efforts have failed before every court to consider them. Tellingly, no reputable financial institution or major trade group has lent its name to the

constitutional challenges to the CFPB. Indeed, not a single amicus brief was filed before the D.C. Circuit in *State National Bank of Big Spring v. Lew*, the most high-profile of the cases. These legal challenges are truly at the fringe. Unfortunately, however, they are emblematic of the unique historical moment in which we live, in which seemingly every major political disagreement—from health care to immigration—is constitutionalized and litigated. Consumer protection, apparently, is no exception.

The principal constitutional arguments against Dodd-Frank, based on the separation of powers, are at odds with at least eighty years of settled precedent. Most are really disguised "non-delegation" arguments—that is, arguments that Congress's delegation of power to an agency (such as the CFPB's authority to regulate unfair lending practices, or the Financial Stability Oversight Council's authority to designate entities as systemically risky) is too vague or broad. But that doctrine hasn't been successfully invoked since 1935—at the height of judicial resistance to the New Deal—and Dodd-Frank's standards are actually more specific than those that have been upheld. As the Supreme Court explained in a 2001 opinion by Justice Scalia, "even in sweeping regulatory schemes [the Court] ha[s] never demanded … a 'determinate criterion'" or "felt qualified to second-guess Congress regarding the permissible degree of policy judgment that can be left to those executing or applying the law."[1]

[1] *Whitman v. American Trucking Ass'ns,* 531 U.S. 457, 474-75 (2001).

The challengers also argue that the President lacks sufficient control over the CFPB because its Director may be removed only for cause.[2] This argument likewise seeks to turn the clock back to before 1935—the year the Supreme Court approved identical for-cause removal protections for FTC commissioners.[3] That precedent applies with full force to CFPB.[4] As the age of the precedents reveal, these arguments are not really attacks on Dodd-Frank or the CFPB so much as attacks on the very foundations of the modern administrative state. In that sense, the title of today's hearing is apt.

Second**, even setting aside constitutional precedent, the basic accountability critiques of the CFPB and Dodd-Frank are misplaced.** To be sure, democratic legitimacy is perhaps the central problem of administrative law, and we should always ask whether the administrative state has become unmoored from our democracy.[5] But the CFPB—which was specifically designed to resist capture by narrow industry interests—is at least as accountable to the public as were the existing prudential banking regulators, from which the CFPB inherited much of its authority over consumer protection. And in several respects, the Bureau is far *more* accountable: Its budget is capped; its rules can be vetoed by a

[2] 12 U.S.C. § 5491(c)(3) ("The President may remove the Director for inefficiency, neglect of duty, or malfeasance in office.").

[3] *Humphrey's Executor v. United States*, 295 U.S. 602, 619, 628, 632 (1935).

[4] *See Morrison v. Olson*, 487 U.S. 654, 692-93 (1988) (approving provision authorizing removal of independent counsel only for "good cause"); *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 130 S. Ct. 3138, 3161 (2010) (concluding that "a single level of good-cause tenure" preserved sufficient presidential oversight).

[5] *See generally* Richard B. Stewart, *The Reformation of American Administrative Law*, 88 HARV. L. REV. 1667, 1678–80 (1975).

committee of other regulators; and it is subject to a special small-business review process by which only EPA and OSHA are similarly constrained. Finally, the CFPB has also gone beyond legal requirements and conventions, using technology and public participation to make itself more directly responsive to the American consumer.

***Third*, the CFPB, Dodd-Frank's crown jewel, has already proven that it is working for American consumers; Congress should resist efforts to gut the agency outside the normal political process.** The CFPB is protecting American consumers. The agency has already returned $10.8 billion dollars for more than 25 million consumers harmed by illegal practices, and has reined in some of the worst abuses in the payday and installment-lending, credit-card, and mortgage industries. Yet the Bureau's opponents are trying to hamstring its efforts and alter its structure to make it less effective—not through the ordinary legislative process but through back-door appropriations riders, absent any debate.

I particularly want to focus the Committee's attention on one area in which the CFPB is working hard to fulfill its statutory mandate to protect consumers, and in which some opponents are trying to use the appropriations process to put up roadblocks: the agency's mandate to study and write rules on the forced arbitration of consumer disputes. As mandated by Congress, the Bureau has produced a 726-page report—the most comprehensive study of consumer arbitration to date—and it shows that forced arbitration clauses embedded in the fine print of consumer contracts grossly favor the financial services industry at the expense of consumers.

Allowing CFBP to continue its important work on arbitration is vital for restoring a fair playing field for consumers and rectifying the extreme imbalance of power between corporate interests and the public.

I. Constitutional Challenges to Dodd-Frank and the CFPB.

The constitutional challenges to the Dodd-Frank Act and the CFPB thus far have recited a similar series of unsuccessful legal arguments. At least four federal courts have rejected these arguments on the merits[6] and at least three others have rejected them on standing grounds.[7]

Rather than fully articulating a specific constitutional violation, these litigants partially construct several constitutional claims in the hopes that a "mosaic" will prevail.[8] These theories, which courts have uniformly rejected, allege that the structure and authority of CFPB or the Financial Stability Oversight Council (FSOC), as well as the Treasury's Orderly Liquidation Authority (OLA), are unconstitutional on separation-of-powers or due-process grounds. To adopt these arguments would be to overturn eighty years of settled precedent and, indeed, the foundations of the New Deal and the modern administrative state.

A. Standing and the Lack of Mainstream Support. Before turning to the merits, however, it is worth saying a brief word about who's behind these

[6] *Consumer Fin. Prot. Bureau v. ITT Educ. Servs., Inc.*, No. 1:14-CV-00292-SEB, 2015 WL 1013508, *11, *13-14, *18, *20 (S.D. Ind. Mar. 6, 2015); *Consumer Fin. Prot. Bureau v. Morgan Drexen, Inc.*, 60 F. Supp. 3d 1082, 1089-92 (C.D. Cal. 2014); *Illinois v. Alta Colleges, Inc.*, 2014 U.S. Dist. LEXIS 123053, *8-13 (N.D. Ill. Sept. 4, 2014); *Illinois v. CMK Investments, Inc.*, 2015 U.S. Dist. LEXIS 84277, *8 (N.D. Ill. June 30, 2015).

[7] *State Nat'l Bank of Big Spring v. Lew*, 958 F. Supp. 2d 127, 136-39, 145 (D.D.C. Aug. 1, 2013); *Morgan Drexen, Inc. v. Consumer Fin. Prot. Bureau*, 979 F. Supp. 2d 104, 121 (D.D.C. 2013), *aff'd*, 785 F.3d 684, 690 (D.C. Cir. 2015).

[8] *ITT Educ. Servs., Inc.* at *11.

challenges. Reputable financial institutions and mainstream trade associations have largely stayed clear of the fray. The highest profile challenge, *State National Bank of Big Spring v. Lew*—filed with great press fanfare in 2012 and billed as "a high-noon showdown between the Obama Administration … and the banking industry"—was brought by a group of transparently politically-oriented plaintiffs, organized through the Competitive Enterprise Institute and represented by one of today's majority witnesses, Ambassador C. Boyden Gray.[9] At a debate about the case, Ambassador Gray publicly admitted that he found it difficult to find any financial institution willing to join the challenge.[10] And, despite D.C.'s booming cottage industry of lawyers representing financial institutions on Dodd-Frank matters, not a single amicus brief was filed in the D.C. Circuit appeal in *Big Spring*.

As I observed on the day the case was filed, one consequence of this lack of mainstream industry support is that the plaintiffs—including the lead plaintiff, the State National Bank of Big Spring, Texas—face serious standing problems.[11] Among other things, Big Spring's total assets are far less than the $10 billion

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[9] Keith Goldberg, *Banking Cases to Watch in 2013*, LAW360, Jan. 1, 2013, http://www.law360.com/articles/397603/banking-cases-to-watch-in-2013.

[10] "The Constitutional Challenge to the Consumer Financial Protection Bureau: A Debate," Georgetown University Law Center, Washington, DC (March 21, 2013) (debate between Deepak Gupta and C. Boyden Gray, sponsored by the Georgetown Center on the Constitution, the Federalist Society, and Consumer Law Society). *See also* C. Boyden Gray, *Congressional Abdication: Delegation Without Detail and Without Waiver*, 36 HARV. J.L. & PUB. POL'Y 41, 47 (2013) ("Finding private plaintiffs has not been easy.").

[11] Carter Dougherty, *U.S. Consumer Bureau Violates Constitution, Lawsuit to Claim*, BLOOMBERG BUSINESS, June 21, 2012, http://www.bloomberg.com/news/articles/2012-06-21/u-s-consumer-bureau-challenged-as-unconstitutional-in-lawsuit.

needed for a bank to be subject to the Bureau's direct enforcement authority.[12] As a result, the Bureau's only power over Big Spring is the power to *recommend* an enforcement action to the bank's actual regulator, the Office of the Comptroller of the Currency (OCC)—a recommendation that the OCC would then be free to reject.[13] Therefore, Big Spring's standing theory either rests upon a sequence of interlinked hypotheticals—the Bureau *might* promulgate a regulation, and further *might* recommend that the OCC bring an enforcement action relating to this regulation, a recommendation the OCC *might* follow—or upon the self-inflicted harm that resulted when Big Spring chose to exit the mortgage market, purportedly based on fear of being subject to an enforcement action.[14] As the district court correctly held, neither of these theories provides a basis for standing.[15]

Nonetheless, the constitutional challenges asserted by Big Spring against the CFPB mirror the claims pursued by the challengers in *Morgan Drexen* and *ITT*, who raised their challenges defensively, in the context of CFPB enforcement actions against them. The CFPB sued ITT for predatory lending to college students who were coerced into taking out private loans to pay for their tuition;[16] it sued Morgan Drexen for tricking consumers into paying thousands of dollars in

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[12] First Am. Compl. at 8, *State Nat'l Bank of Big Spring v. Geithner*, No. 1:12-cv-01032 (D.D.C. Sept. 20, 2012); 12 U.S.C. § 5515.

[13] 12 U.S.C. § 5516.

[14] *See* First Am. Compl. at 17-18, *Nat'l Bank of Big Spring*, No 1:12-cv-01032.

[15] *Nat'l Bank of Big Spring*, 958 F. Supp. 2d at 165.

[16] *See ITT Educ. Servs., Inc.* at *1-5.

illegal fees and misrepresenting its questionable debt-relief and bankruptcy services.[17] In both cases, the courts were therefore able to reject the constitutional arguments on the merits.[18]

In addition, in a pending case before the U.S. District Court in Washington D.C., MetLife, Inc. has brought a constitutional challenge to the FSOC's process for designating financial institutions "systemically important" under Dodd-Frank.[19] In relation to *Big Spring*, what's striking about MetLife's complaint is that it bases standing on the alleged harm incurred by the FSOC's designation.[20] Big Spring, in contrast, asserts that its *lack* of FSOC designation places it at a competitive disadvantage with financial institutions that are designated "systematically important."[21] At the very least, this disagreement among the two sets of plaintiffs regarding whether FSOC-designation is a benefit or a burden cautions against a finding that the lack of designation confers standing.[22]

B. Challenges to the CFPB's Structure and Authority. Although Big Spring also aims to discredit the constitutionality of the OLA and the FSOC, its most extensive criticism is reserved for the CFPB. Weaving together a patchwork of disjointed allegations, Big Spring seeks to establish that, when taken together,

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[17] *Morgan Drexen, Inc. v. Consumer Fin. Prot. Bureau*, 979 F. Supp. 2d 104, 110 (D.D.C. 2013), *aff'd*, 785 F.3d 684 (D.C. Cir. 2015).

[18] *See Id.* at 1089-92; *ITT Educ. Servs., Inc.* at *11, 14, 18, 20.

[19] *See* Compl. at 2, *MetLife, Inc. v. Fin. Stability Oversight Council*, No. 1:15-cv-00045 (Jan. 13, 2015).

[20] *Id.* at 9.

[21] Compl. at 31-33, *Nat'l Bank of Big Spring*, No 1:12-cv-01032.

[22] *See Nat'l Bank of Big Spring*, 958 F. Supp. 2d at 137-138 (noting the "ambiguous consequences of SIFI designation" before rejecting the plaintiff's standing argument).

"the overwhelming uncertainty inherent in the Title X's open-ended grant of power to the CFPB and the lack of checks and balances limiting the CFPB's exercise of that power" render it unconstitutional.[23]

1. Disguised Nondelegation Arguments. Big Spring first argues that the Dodd-Frank Act's failure to place meaningful restrictions on CFPB's authority to define and enforce "unfair, deceptive, or abusive actions or practices" contravenes the separation of powers.[24] Morgan Drexen and ITT made similar arguments, and both district courts rejected them. Noting that the Dodd-Frank Act explicitly restricts "abusive" practices to four circumstances,[25] the *Drexen* court found that the legislative guidance provided by the Act satisfies constitutional requirements because it is "at least as specific as other provisions held to constitute 'intelligible principles.'"[26] The *ITT* court applied a similar line of reasoning when it held that, in the context of the statute, the terms "abusive" and "unfair" are not unconstitutionally vague in violation of the Fifth Amendment's Due Process Clause.[27] Given that the Dodd-Frank Act's use of "unfair" reflects

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[23] Second Am. Compl. at 24, *State Nat'l Bank of Big Spring v. Geithner*, No. 1:12-cv-01032 (D.D.C. Feb. 19, 2013).

[24] First Am. Compl. at 15-22, *Nat'l Bank of Big Spring*, No 1:12-cv-01032.

[25] "The Dodd–Frank Act defines 'abusive' as either 'materially interfer[ing] with the ability of a consumer to understand a term or condition of a consumer financial product or service' or 'tak[ing] unreasonable advantage of—(A) a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service; (B) the inability of the consumer to protect the interests of the consumer in selecting or using a consumer financial product or service; or (C) the reasonable reliance by the consumer on a covered person to act in the interests of the consumer.'" *Morgan Drexen, Inc.*, 60 F. Supp. 3d at 1090 (quoting 12 U.SC. § 5531(d)).

[26] *Morgan Drexen, Inc.*, 60 F. Supp. 3d at 1090 (citing *Yakus v. United States*, 31 U.S. 414, 414, 420, 426-27 (1944); *Am. Power & Light Co. v. S.E.C.*, 329 U.S. 90, 90, 104-06 (1946)).

[27] *ITT Educ. Servs., Inc.* at *18, *20. The Dodd-Frank Act provides detailed definitions for both "unfair" and "abusive" acts or practices, thus constraining the Bureau's power far more than the

language used in the Federal Trade Commission Act (FTCA), regulated entities are sufficiently apprised of what practices are permitted and forbidden under the Act. As used in the FTCA, the phrase "unfair or deceptive acts or practices" has survived constitutional challenges and been subject to refinement and elaboration since the statute's enactment in 1914. Based on this history, a reasonable business entity should be able to infer the types of actions to which the CFPB might object.[28]

These arguments against the constitutionality of the CFPB are a thinly veiled attempt to breathe life into the non-delegation doctrine, which has not formed the basis for a successful constitutional challenge since 1935.[29] The Dodd-Frank Act's delegation of power to CFPB, moreover, is far narrower than other delegations that have been upheld. In 2001, for instance, in an opinion by Justice Scalia, the Supreme Court upheld a provision of the Clean Air Act granting the EPA authority to "set ambient air quality standards … requisite to protect the public health."[30] In so doing, the Court in *Whitman v. American Trucking*

Clean Air Act in *Whitman* constrained the EPA's. *See* 12 U.S.C. § 5531. These statutory definitions, moreover, are expressly couched in terms of limitations on the Bureau's powers, providing "[t]he Bureau shall have no authority" to declare acts unfair or unlawful except in conformity with the Act's standards. *Id.* And the Bureau, drawing on the Dodd-Frank Act and established principles of consumer-protection law, has provided clear guidance on its own definitions of "unfair," "abusive," and "deceptive" practices. *See* CFPB, *Supervision and Examination Manual, Version 2*, at UDAAP 1-UDAAP 10 (2012).

[28] *ITT Educ. Servs., Inc.* at *18

[29] A non-delegation challenge to a federal statute has succeeded only twice in the Nation's history—both times in 1935, at the height of judicial hostility to the New Deal. *See Panama Refining Co. v. Ryan*, 293 U.S. 388 (1935); *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935).

[30] *Whitman*, 531 U.S. at 465 (2001) (citing 42 U.S.C. § 7409(b)(1)). The Court said "requisite" meant "not lower or higher than is necessary" – hardly a precise definition. *Id.*

Associations remarked that "even in sweeping regulatory schemes [it] ha[s] never demanded … a 'determinate criterion'" for the standards set by statutes.[31] Thus, to hold that the CFPB is unconstitutional on non-delegation grounds would not just contradict settled precedent; it would open the door to inestimable constitutional challenges to agency delegations and, in turn, compromise the post-New Deal institutions on which our government and its citizens have come to rely.

2. ***Presidential Removal Power.*** Big Spring next contends that the CFPB's insulation from political control also constitutes a violation of the separation of powers. This argument revolves around the Dodd-Frank Act's alleged contravention of the President's removal power. Although the Dodd-Frank Act only permits the President to remove the Director of the CFPB for cause, courts that have addressed this issue in depth have held that *Humphrey's Executor v. United States*,[32] a 1935 case in which the Supreme Court upheld for-cause removal of Federal Trade Commissioners, controls.[33]

Under this standard, the relevant inquiry is whether limitations on the President's removal power "impede the President's ability to perform his constitutional dut[ies]."[34] The for-cause removal provided for by the Dodd-Frank Act satisfies this standard because the President retains "ample authority to

[31] *Id.* at 475. The Court further explained that it has "'almost never felt qualified to second-guess Congress regarding the permissible degree of policy judgment that can be left to those executing or applying the law.'" *Id.* at 474-75 (citing *Mistretta v. United States*, 488 U.S. 361, 416 (1989) (Scalia, J., dissenting)).

[32] 295 U.S. 602, 626-31 (1935).

[33] *Morgan Drexen, Inc.*, 60 F. Supp. 3d at 1087; *see also ITT Educ. Servs., Inc.* at *8-9.

[34] *Id.* at * 9-11, 13-14 (quoting *Morrison v. Olson*, 487 U.S. 654, 691 (1988)).

assure that the Director is competently leading the CFPB," just as the President's for-cause removal power gives him ample authority to oversee the SEC and FTC—agencies that perform very similar functions.[35] As the district court in *ITT* summarized, "the structure and powers of the Bureau are sufficiently analogous to those of the FTC, SEC, and other regulatory agencies that the question of the constitutionality of CFPB's removal provision is settled by *Humphrey's Executor* and its progeny."[36]

Nor does the Dodd-Frank Act present the same "second layer of insulation" issue presented by the Public Company Accounting Oversight Board. Under the Sarbanes-Oxley Act, the Securities and Exchange Commission (SEC), whose members are removable by the President only for cause, appointed the public accounting board, whose members were likewise removable *by the Commissioners* only for cause.[37] In the 2010 case in which it held that this structure violates the separation of powers, *Free Enterprise v. Public Company Accounting Oversight Board*, the Supreme Court made clear that its holding rested on this "second layer of insulation," which did "not merely add to the Board's independence, but transform[ed] it" into an unconstitutional component of an otherwise constitutional independent agency.[38] Because the Dodd-Frank Act authorizes for-cause removal of the Director of the CFPB, it lacks the second layer of insulation that *Free*

[35] *Morgan Drexen, Inc.*, 60 F. Supp. 3d at 1087.

[36] *ITT Educ. Servs., Inc.* at *14.

[37] *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 130 S. Ct. 3138, 3154 (2010).

[38] *Id.* at 3154.

Enterprise Fund concluded differentiated the accounting board from constitutionally permissible independent agencies.

Professor Neomi Rao—a majority witness at today's hearing and a vehement defender of the presidential removal power—has argued in her scholarship that any limitations placed on the President's removal power are unconstitutional.[39] In the wake of *Free Enterprise Fund*, Rao asserts, there is a consensus in legal scholarship that "every federal entity must be accountable to one of three branches."[40] The CFPB is nominally within the Federal Reserve System, but its Director is directly accountable to the President, and, with the exception of the Act's for-cause provision, the President is entirely unobstructed in exercising his or her authority over the CFPB. Despite advocating for courts to overturn the CFPB's for-cause removal provision as unconstitutional, Rao concedes that her approach marks a dramatic departure from existing precedent and would require courts to overturn *Humphrey's Executor*.[41]

Rao's scholarship also reveals that those who challenge Dodd-Frank's constitutionality do not agree even among themselves. Indeed, the majority's witnesses today advance constitutional theories that are fundamentally incompatible. Although she maintains that the Dodd-Frank Act's removal provision is unconstitutional, Professor Rao acknowledges that the CFPB would be

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[39] Neomi Rao, *Removal: Necessary and Sufficient for Presidential Control*, 65 ALA. L. REV. 1205, 1208 (2014).

[40] *Id.* at 1230-31.

[41] Neomi Rao, *A Modest Proposal: Abolishing Agency Independence in* Free Enterprise Fund v. PCAOB, 79 FORD. L. REV. 2541, 2573-75 (2011).

constitutional without it. She thus concedes that the CFPB's basic structure and functions are otherwise constitutionally sufficient. Professor Rao's interpretation, in other words, forecloses Big Spring's and Ambassador Gray's grab-bag (or "mosaic") approach to establishing the constitutional infirmity of Dodd-Frank and the CFPB. As Professor Rao has noted, "there is no all-things-considered functional test to protect separation of powers," nor is there "any decision in which the Court has invalidated government action on functional separation of powers grounds."[42] Thus, Rao recognizes that the dissatisfaction that both proponents and opponents of the CFPB may find with her views "perhaps highlights the political aspects of the disagreement over how to regulate consumer finance, a disagreement that belongs in the political, not judicial arena."[43] On this last point, at least, Professor Rao and I agree.

Finally, it is worth noting that although some opponents of the Dodd-Frank Act's for-cause removal provision call for replacement of the CFPB's Director with a multi-member commission,[44] that structure might actually dilute the President's removal power. With a single agency head, the President is able to expediently remove incompetent leadership. A commission, on the other hand, presents the President with the issue of first identifying which members are responsible for issues that arise.

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[42] *See* Rao, *Removal*, at 1272.

[43] *Id.* at 1275.

[44] *See, e.g., Morgan Drexen, Inc.*, 60 F. Supp. 3d at 1086.

3. **Remaining Constitutional Objections to the CFPB**. Courts easily dispose of the hodgepodge of remaining constitutional complaints lodged against the CFPB, which include challenges to the deference afforded to CFPB's interpretations of federal consumer financial laws,[45] its funding through the Federal Reserve System, and the appointment of its Deputy Director. In connection with the first challenge, the *Morgan Drexen* and *ITT* courts held that the Dodd-Frank Act "merely prescribes that the Bureau's constructions of organic law in its subject area are to be given deference, in accordance with the well-established principles first enunciated in *Chevron*."[46] Both courts also summarily dismissed objections to the CFPB's exemption from congressional appropriations on the grounds that Congress is permitted to establish agencies with alternative funding structures.[47] Settled doctrine affirms that the Appropriations Clause only prevents the Executive Branch from spending public money without Congress's permission—it doesn't prevent Congress from providing funding in any manner it sees fit.[48] Although no court has decided whether the Director's authority to appoint the Deputy Director is constitutional, the court in *ITT* opined that the CFPB may be considered a "department" under the Court's definition in *Free*

[45] Under the Dodd-Frank Act, the CFPB's interpretations of federal consumer financial law receive the same deference that they would "if the Bureau were the only agency authorized to apply, enforce, and interpret, or administer the provisions of such Federal consumer financial law." 12 U.S.C. § 5512(b)(4)(B).

[46] *ITT Educ. Servs., Inc.* at *12; *see Morgan Drexen, Inc.,* 60 F. Supp. 3d at 1091.

[47] *See Morgan Drexen, Inc.*, 60 F. Supp. 3d at 1091; *ITT Educ. Servs., Inc.* at *12.

[48] *Morgan Drexen, Inc.*, 60 F. Supp. 3d at 1089.

Enterprise Fund, which would allow Congress to bestow the Bureau's Director with the power to appoint inferior officers.[49]

C. The FSOC and the Treasury's Orderly Liquidation. Authority. Big Spring's complaint is comprehensive in its condemnation of the Dodd-Frank Act and incorporates challenges to the Treasury's OLA and the FSOC. With respect to the Orderly Liquidation provision, the complaint alleges that it violates separation of powers principles by providing the Treasury with unbridled discretion to identify companies for liquidation "without either useful statutory guidance or meaningful legislative, executive, or judicial oversight."[50] Moreover, according to Big Spring, the Treasury's procedures infringe companies' Fifth Amendment Rights and the uniformity requirement of Article I, Section 8, Clause 4 by precluding "notice and meaningful opportunity to be heard" and permitting the Treasury to "choose favorites among similarly situated creditors in implementing liquidation."[51]

Big Spring's criticism of the FSOC sounds in a similar register: by offering the FSOC unlimited discretion to designate institutions as "systemically important" and insulating this process from judicial review, the Dodd-Frank Act contravenes the separation of powers.[52] MetLife presents a parallel separation of powers argument in its complaint against the FSOC, which alleges that the Council

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[49] *ITT Educ. Servs., Inc.* at *11. The Constitution provides that Congress may vest the heads of Executive Departments with authority to appoint inferior officers. U.S. Const. Art. II, § 2, cl. 2.

[50] Compl. at 7, *Nat'l Bank of Big Spring*, No 1:12-cv-01032.

[51] *Id.* at 7-8.

[52] *Id.* at 6-7.

"conflat[es] the roles of advocate and adjudicator" by having the same individuals investigate and issue a final decision on eligibility.[53] It then proceeds to assert that the thresholds applied by the FSOC to determine eligibility are unconstitutionally vague in violation of the Fifth Amendment.[54]

These claims, which recall the separation of powers and Fifth Amendment challenges to the CFPB, are also largely disguised non-delegation arguments, and fail for much the same reasons. Furthermore, they are representative of an overarching theme embodied by the plethora of ill-conceived constitutional challenges levied against the CFPB and the Dodd-Frank Act, generally: wariness of the regulatory scheme's novelty. The court in *ITT* emphasized that the Bureau is "no venture into uncharted waters," but a "variation on a theme—the independent regulatory agency with enforcement power—that has been a recurring theme of the modern administrative state."[55] But the Dodd-Frank Act is, in many ways, undeniably innovative. In passing the Act, Congress aimed to prevent another Great Recession by overhauling financial regulation in the United States. By instituting the CFPB, it intended to establish the first agency designed to address regulatory capture. Achievement of these ambitious objectives required Congress to consider agency arrangements that deviated from traditional structures.

[53] Cross-Motion for Summ J. at 67-68, *MetLife v. Fed. Stability Oversight Council*, No. 1:15-cv-45 (RMC) (D.D.C. June 16, 2015).

[54] *Id.* at 67.

[55] *ITT Educ. Servs., Inc.* at *13.

Novelty, however, is not in and of itself an indicator of unconstitutionality. As the *Mistretta* Court noted in upholding the structure of the Sentencing Commission, "constitutional principles of separated powers are not violated … by mere anomaly or innovation."[56] Although it may signal that a court should exercise caution, "generalized assault[s] on the unprecedented nature of the Bureau proceed from the mistaken premise that that which is not specifically approved by precedent is forbidden."[57] By treating the Dodd-Frank Act's originality as a mark against its legality, its opponents compromise the presumption in favor of constitutionality and disincentivize innovation designed to make the government both more effective and responsive. We should be celebrating such innovation, not stifling it.

II. Accountability Critiques of CFPB.

Constitutional challenges aside, the primary attack against CFPB is that it is unaccountable to the public and democratically illegitimate. Critics target the fact that the agency is headed by a single Director rather than by a five-member commission, and that its funding is not subject to the appropriations process overseen by Congress. Alarmist appraisals by opponents such as Todd Zywicki—who describes the agency as combining "vast power and lack of public accountability" in unprecedented ways—are routine.[58]

These criticisms are not new: they echo the same attacks that opponents

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[56] *Mistretta v. United States*, 488 U.S. 361, 385 (1989).

[57] *ITT Educ. Servs., Inc.* at *11.

[58] Todd Zywicki, *Consumer Financial Protection Bureau: Savior or Menace?*, 81 GEORGE WASH. L. REV 856 (2013).

launched five years ago, after Congress created the agency.[59] Several facts show that these criticisms are also flatly unfounded. First, agency accountability was a central goal throughout both the conception and formation of the Bureau, and its structure today reflects fidelity to that priority. Second, the CFPB is accountable in all the ways that the Federal Reserve, the OCC, and the Federal Deposit Insurance Corporation (FDIC) are. Third, in important ways the Bureau's power is more constrained than those of these other regulators. And fourth, over its short existence CFPB has pioneered ways to involve citizens in its decision-making, to ensure its work reflects the challenges and needs of actual consumers, and to keep itself accountable to the public.

A. Accountable to the Public, Resistant to Industry Capture. I agree that the democratic legitimacy of independent agencies is of paramount importance and a central challenge of the administrative state. Ensuring that agencies stay accountable to the public isn't just an academic concern; we saw all-too-recently what can happen when regulators become unmoored from serving the public. As is now widely acknowledged, the 2007 financial crash was the result of gross oversight and neglect on the part of the independent agencies charged with overseeing the financial system. The Federal Reserve failed to stem the flow of toxic mortgages and neglected to read the myriad warning signs that

[59] Rachel E. Barkow, *Insulating Agencies: Avoiding Capture Through Institutional Design*, 89 TEX. L. REV. 15 (2010) 72-75; David Hirschmann, *Consumer Financial Protection Bureau needs more accountability*, POLITICO, Dec. 7, 2011, at http://www.politico.com/news/stories/1211/69992.html

foreshadowed the crisis.[60] The OCC and the Office of Thrift Supervision (OTS), caught up in turf wars, preempted state regulators from reining in abuses and created incentives for a regulatory "race-to-the-bottom."[61] In many ways the failings of these agencies can be traced to a lack of democratic accountability, and to ideological and cultural capture by industry.[62]

The Consumer Financial Protection Bureau was created with these failures in mind. Observing that the existing regulatory framework left consumers entirely exposed to risky and predatory financial products, then-Professor Elizabeth Warren proposed the new agency to fill-in the gap.[63] Critically, the idea was to design an entity with both the authority and the incentives to police the safety of consumer credit products. Acutely aware of how vulnerable regulators remain to industry capture, the agency's supporters drew from scholarship on agency accountability, as well as from the practical lessons of agencies like the Consumer Products Safety Commission, whose structure provided a cautionary tale for how

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[60] As the Financial Crisis Inquiry Commission noted in its final report, "Despite the expressed view of many on Wall Street and in Washington that the crisis could not have been foreseen or avoided, there were warning signs. The tragedy was that they were ignored or discounted." The red flags included "an explosion in risky subprime lending and securitization, an unsustainable rise in housing prices, widespread reports of egregious and predatory lending practices, dramatic increases in household mortgage debt, and exponential growth in financial firms' trading activities, unregulated derivatives, and short-term "repo" lending markets, among many other red flags. Yet there was pervasive permissiveness; little meaningful action was taken to quell the threats in a timely manner." THE FINANCIAL CRISIS INQUIRY COMMISSION REPORT, JAN. 2011, xvii.

[61] *Id.* at xiii.

[62] James Kwak, *Cultural Capture and the Financial Crisis*, in PREVENTING REGULATORY CAPTURE: SPECIAL INTEREST INFLUENCE AND HOW TO LIMIT IT, eds. Daniel Carpenter and David A. Moss, The Tobin Project, 2014.

[63] Elizabeth Warren, *Unsafe at Any Rate*, DEMOCRACY (Summer 2007); Oren Bar Gill and Elizabeth Warren, *Making Credit Safer*, 157 U. PENN. L. REV. 101 (2008).

traditional markers of independence can fall short.[64]

The institutional framework of the CFPB was the focus of intense political debate.[65] Initially proposed as a free-standing cabinet-level agency, CFPB's ultimate form was shaped by extensive negotiations in Congress. Tennessee Senator Bob Corker, a conservative Republican, proposed that the agency be housed within the Federal Reserve, insulating it from the appropriations process.[66] Compromises on both sides yielded the final result.

B. Just as Accountable as Other Financial Regulators. As numerous experts have noted, CFPB is accountable to a host of government processes and bodies. Like other agencies, it is bound by the Administrative Procedures Act (APA), which means that it must inform the public of its proposed rules, offer citizens the opportunity to comment on proposals, and then consider public input when finalizing its rules. It is also subject to the Regulatory Flexibility Act, the Paperwork Reduction Act, and the Congressional Review Act.

Additionally, CFPB's authority is uniquely bound by other regulators. When proposing rules to prohibit unfair, deceptive, or abusive practices, the CFPB is required to consult with federal banking agencies or other regulators to ensure that the rules are in line with "prudential, market, or systemic objectives

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[64] Barkow, *Insulating Agencies*, at 65-71 (identifying various structural features of the CPSC that made it "one of the least politically independent and influential agencies in government").

[65] Sewell Chan, *Dodd Proposes Giving Fed the Task of Consumer Protection*, N.Y. TIMES, Mar. 2, 2010, at B2 ("[A]dvocates, mindful of fierce Republican opposition to a stand-alone agency, have said that they are less concerned about where the entity is housed than the scope of its authority and the independence of its leadership and budget.").

[66] Rich Danker, *Corker stiffs anti-Fed Republicans again*, THE HILL, Mar. 6, 2012.

administered by such agencies."[67] The CFPB is also obligated to consult prudential regulators and other agencies when proposing rules administering federal consumer financial laws.[68] Not only are regulators permitted to object to the rules, their written objections must be included in the rule-making record, along with the Bureau's response to their concerns.[69] No other financial regulator faces these requirements.

An agency head who can only be removed by the president for-cause and an independent funding stream are features that the Bureau shares with the Federal Reserve, the FDIC, and the OCC.[70] Congress gave financial regulators this structure because it recognized that the safety and stability of the financial industry—a sector on which all other businesses depend—was too vital to subject to the vagaries of the political process. That the CFPB, a financial regulator, shares the basic design of other financial regulators is not anomalous.

C. More Accountable Than Other Financial Regulators. In important ways, Congress has placed additional limits on CFPB's authority. Unlike any other financial regulator, the Bureau is subject to the Small Business Regulatory Enforcement Fairness Act (SBREFA), which requires it to give small businesses a preview of new proposals and receive extensive feedback before giving notice to the broader public. The CFPB is also the only financial regulator whose books are

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[67] Dodd-Frank Wall Street Reform and Consumer Protection Act, 12 U.S.C. 5301, §1031(e).

[68] *Id* at §1022(b)(2)(B).

[69] *Id* at, §1022(b)(2)(C).

[70] Restraints on the President's ability to remove the Comptroller of the Currency is unclear and the OCC's organic statute does not address the issue.

annually audited by the Government Accountability Office (GAO).[71] Furthermore, the Bureau is subject to significant oversight by Congress: the CFPB Director must submit reports to and appear in committees in front of both houses of Congress twice a year.[72] Senior CFPB officials have already testified to Congress fifty-five times since the agency's birth four years ago, an average of more than one appearance per month. That must be some kind of record.

Uniquely, CFPB's funding is capped. Unlike other financial regulators, CFPB cannot simply hike fees, increase revenue, and boost its activity levels. Its budget is capped at 12 percent of the Federal Reserve's 2009 operating expenses, with slight adjustment for inflation.[73] No other financial regulator has a budget ceiling written into law.

Lastly, all of the Bureau's regulations are subject to review by the FSOC, a body of cabinet-level and executive-appointed officials. The FSOC can veto any proposed rule on safety and soundness concerns with a two-thirds vote. The voting members of the FSOC consist of the Secretary of the Treasury, the Fed Chairman, the Comptroller of the Currency, the Director of the CFPB, the Chairman of the SEC, the Chairperson of the FDIC, the Chairperson of the Commodities Futures Trading Commission (CFTC), the Director of the Federal Housing Finance Agency (FHFA), the Chairman of the National Credit Union Administration (NCUA), and an independent member who has insurance expertise and who is

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[71] *Id.* at § 1017(a)(5)(B).

[72] *Id.* at § 1016(a).

[73] *Id.* at § 1017(a)(2).

appointed by the President and confirmed by the Senate. I am aware of no other independent agency whose regulations are subject to the veto power of regulators from other agencies.

D. Enhancing Public Participation. Not only is the Bureau as accountable as—and in key regards, even more constrained than—other financial regulators, but it has pioneered new ways to solicit public participation in its decision-making and ensure that its work reflects the actual needs of citizens. Since 2011 it has held over thirty public town halls and field hearings in cities across the country, from Itta Bena, Mississippi to Sioux Falls, South Dakota.[74] Even before its official launch, CFPB initiated an online campaign to seek public input through popular venues like Twitter, Facebook, and YouTube. Through these online channels, the Bureau has collected reams of information about the kinds of difficulties consumers face with various financial products, data that it uses to inform its priorities and policymaking.[75]

The Bureau's "Know Before You Owe" mortgage initiative exemplifies the agency's emphasis on public participation. Charged with the task of simplifying the convoluted information consumers receive under the Truth In Lending Act (TILA) and the Real Estate Settlement Procedures Act (RESPA), CFPB redesigned the forms and conducted in-depth, one-on-one interviews with borrowers, lenders, and

[74] Consumer Financial Protection Bureau, Consumer Financial Protection Bureau: By the Numbers Fact Sheet, July 15, 2015.

[75] Leonard J. Kennedy, Patricia A. McCoy, and Ethan Bernstein, *The Consumer Financial Protection Bureau: Financial Regulation for the Twenty-First Century*, 94 CORN. L. REV. 1140, 1159 (2012).

brokers to understand how well consumers and lenders were able to use various iterations. At the same time that the Bureau was testing each set of forms, it also posted them online with an interactive tool to gather public input about the designs. By recording where users clicked as they reviewed the draft disclosures, this tool allowed the Bureau to compile "heat-maps" showing the areas of the disclosures that attracted the most and least attention. In addition, as a useful supplement to the traditional public notice-and-comment process, the CFPB's interactive tool permitted targeted input on the portions of the design that were under investigation in that cycle. That input allowed Bureau staff to process the feedback quickly, iterate the forms, and then test again in four weeks.[76]

The process fostered extensive public participation. The Bureau received over 220,000 unique page-views for KBYO, resulting in 27,000 comments over the first seven iterative cycles.[77] Seeking wide public input as it conducted consumer testing, rather than having a single public comment period on a formal proposal, has been central to the development and success of the Bureau's proposed form. Initial testing shows that the new disclosures have successfully reduced consumer confusion and are enabling comparison-shopping.[78] Drawing on this experience, the Bureau has expanded its KBYO initiative to cover student loans and credit cards—efforts that will make the costs and risks of these products easier for the public to understand.

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[76] *Id.* at 1166.

[77] CONSUMER FIN. PROT. BUREAU, SEMI-ANNUAL REPORT OF THE CONSUMER FINANCIAL PROTECTION BUREAU: JULY 21-DECEMBER 31, 2011, at 13-14 (2012).

[78] Kennedy et al., *The Consumer Financial Protection Bureau*, at 1161.

The Bureau has also sought out extensive feedback from servicemembers. Under the leadership of Holly Petraeus, the Bureau has hosted numerous town hall meetings and roundtable discussions with military families and their advocates. These meetings have educated the Bureau about the financial products and services most affecting servicemembers, information CFPB is now using to shape financial education programs for servicemembers.[79]

These efforts showcase just some of the ways that CFPB is using its mandate to ensure it stays accountable to the public. Not only are attacks on its accountability unfounded, but the Bureau's efforts to enhance its democratic responsiveness serve as a model that we should encourage other regulators to follow.

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Numerous proposals from Congress now threaten the independence and accountability of the Bureau. The most recent House appropriations bill includes several riders that would, among other things, replace its single director with a five-member commission, subject agency rulemaking to additional compliance requirements, and change its funding source from Federal Reserve transfers to annual appropriations.[80] Most alarmingly, the House appropriations bill would introduce fresh obstacles to the Bureau's ability to review and reform pre-dispute mandatory arbitration—a task Congress charged it with in Dodd-Frank.

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[79] *Id.*, at 1168.

[80] Financial Services and General Government Appropriations Bill, 2016, 114th Cong., 1st sess., 47-51.

Each of these proposals would critically undermine the agency's structure and powers and should be fought off. The Bureau's efficacy and force as a public champion stems from its independence, and the fact that it can carry out its work insulated from the threat of industry retaliation and the partisan vagaries of the appropriations process. Undoing these key protections would be disastrous for American consumers.

III. Progress of CFPB & Arbitration Study.

In its short five years, the Bureau already has had tremendous success championing the rights of the American public. The agency has returned $10.8 billion dollars to more than 25 million consumers harmed by illegal practices—including $14 million that the Bureau won back from the payday lender Cash America for targeting and illegally overcharging members of the military.

The Bureau's victories go beyond numbers: it has also made financial products more transparent and provided consumers with key resources to navigate among different financial options. Most importantly, its mere existence as a public watchdog serves as a powerful deterrent against predatory and exploitative industry practices.

One area in which the CFPB is working hard to protect consumers is forced arbitration. Swaths of consumer contracts today contain mandatory arbitration clauses. These clauses rob consumers of the right to take a company to court, and instead force individuals to settle claims through private arbitrators, usually chosen by the company. Originally sanctioned by Congress as a mechanism for

businesses of equal bargaining power to resolve contractual disputes, arbitration today has morphed into a routine device that companies can use against consumers and workers, parties with vastly unequal bargaining power.[81]

For years public advocates and corporate lawyers debated the effects of mandatory arbitration clauses, with each side issuing competing studies documenting how these clauses either harm or benefit the public. Congress gave the Bureau statutory authority to study the prevalence and effects of these clauses as a way to gather credible data and create a public record on the understudied yet rising use of forced arbitration.[82]

The CFPB undertook the process with methodological rigor and transparency. As a preliminary step, it published a Request for Information that sought comments on the appropriate scope, methods, and data sources for the study, and met with commentators to discuss their concerns. It then published preliminary results from the study in December 2013, and again met with various stakeholders—including industry actors—to hear their feedback.

In March of this year, the Bureau issued its final report.[83] The results were unambiguous: the financial industry uses arbitration clauses widely, these clauses notably suppress consumer complaints, and the tiny fraction of consumers who *do* bring claims fare far worse in arbitration than they would in class actions. Strikingly, *four* consumers with small claims received cash compensation through

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[81] Lina Khan, *Thrown Out of Court*, WASH. MONTHLY, June/July/August 2014.

[82] 12 U.S.C. § 5301(a).

[83] Consumer Financial Protection Bureau, Arbitration Study: Report to Congress, pursuant to Dodd-Frank Wall Street Reform and Consumer Protection Act § 1028(a), March 2015.

arbitration, whereas thirty-four million received compensation through class actions.[84] A case study comparing outcomes for consumers who had been swindled by banks through overdraft fees found that those without arbitration clauses were able collectively to recover hundreds of millions of dollars that were deposited straight to their bank accounts, while those facing enforceable arbitration clauses won back nothing.[85]

The Bureau also found that 50 percent of outstanding credit card loans contain forced arbitration clauses. (Were it not for a 2009 antitrust settlement that required some banks to eliminate temporarily these clauses, this number would be around 94 percent.) Between 85 and 100 percent of contracts with forced arbitration clauses additionally contain class action bans. Consumers, meanwhile, overwhelmingly have no idea: over 90 percent of consumers whose contracts for financial products include forced arbitration clauses were unaware that they could no longer sue. Between 2010 and 2012, only about 410 individual consumers brought arbitration claims against financial services companies.

The study also found that consumers generally fare much worse than companies do a significant percentage of the time: in cases initiated by consumers, arbitrators provided them some relief in around 20 percent of cases; by contrast, arbitrators awarded companies relief in 93 percent of cases that they filed.

[84] The arbitration claims were counted over a two-year period, while the class action claims over a five-year period. Needless to say, this discrepancy does not undermine the force of the disparity between four consumers and thirty-four million consumers.

[85] Consumer Financial Protection Bureau, Arbitration Study, at 39.

Moreover, consumers on average won 12 cents for every dollar that they claimed, whereas corporations on average won 91 cents for every dollar that they claimed.

In sum, the study shows that arbitration is starkly inferior to class actions as a vehicle for consumer relief. The next step for the Bureau is to consider rulemaking informed by this study.

Alarmingly, it's become clear that opponents are now trying to use the appropriations process to obstruct the agency's work. The 2016 House Appropriations Bill contains provisions that would tie the Bureau's authority to continue working on arbitration to a litany of additional requirements—instituting a form of paralysis by analysis.

Allowing CFBP to continue its arbitration work is vital for restoring a fair playing field for consumers and rectifying the gross imbalance of power between corporate interests and the public. Members of Congress should pay special attention to this attack—and fight it.

Thank you again for the opportunity to testify. I am happy to answer any of the Committee's questions.