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THE FINANCIAL SERVICES INDUSTRY'S MISGUIDED QUEST TO UNDERMINE THE CONSUMER FINANCIAL PROTECTION BUREAU

ARTHUR E. WILMARTH, JR.*

I. Introduction

The preamble to the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank")[1] affirms that one of the statute's primary purposes is "to protect consumers from abusive financial services practices."[2] When President Obama signed Dodd-Frank into law, he declared that the statute would create "the strongest consumer financial protections in history."[3]

In order to implement and enforce Dodd-Frank's new protections for consumers, Congress created the Bureau of Consumer Financial Protection ("CFPB") as an "independent bureau" within the

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On January 4, 2012, after the manuscript for this article was completed, President Obama issued a recess appointment to install Richard Cordray as the first Director of the Bureau of Consumer Financial Protection. David Nakamura & Felicia Sonmez, *Obama defies Senate, puts Cordray in consumer post*, WASH. POST, Jan. 5, 2012, at A01. As discussed *infra* in note 13, Republican members of Congress and some analysts have challenged the validity of Mr. Cordray's appointment. Discussion of that issue is beyond the scope of this article.

1 Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) [hereinafter Dodd-Frank].

2 *Preamble* to Dodd-Frank, *supra* note 1, at 1376.

3 President Barack H. Obama, Remarks on Signing the Dodd-Frank Wall Street Reform and Consumer Protection Act (July 21, 2010), *available at* http://www.whitehouse.gov/the-press-office/remarks-president-signing-dodd-frank-wall-street-reform-and-consumer-protection-act [hereinafter Presidential Dodd-Frank Statement].

Federal Reserve System ("Fed").[4] President Obama explained that CFPB will operate as "a new consumer watchdog with just one job: looking out for people—not big banks, not lenders, not investment houses—looking out for people as they interact with the financial system."[5] Similarly, the Senate committee report on Dodd-Frank explained that CFPB's mission is to "help protect consumers from unfair, deceptive, and abusive acts that so often trap them in unaffordable financial products."[6]

Thus, Congress gave CFPB "the Herculean task of regulating the financial services industry to protect consumers."[7] Congress sought to increase CFPB's "accountability" for that mission by delegating to CFPB the combined authority of seven federal agencies that were previously responsible for protecting consumers of financial services.[8]

Congress determined that a single federal authority dedicated to protecting consumers of financial services was needed in light of "the spectacular failure of the [federal] prudential regulators to protect average American homeowners from risky, unaffordable" mortgages during the housing boom that led to the current financial crisis.[9] As stated in the Senate report, federal banking agencies "routinely sacrificed consumer protection" while adopting policies that promoted the "short-term profitability" of large banks, nonbank mortgage lenders and Wall Street securities firms.[10] The Senate

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[4] Dodd-Frank § 1011(a); *see also* H.R. REP. NO.111-517, at 874 (2010) (Conf. Rep.), *reprinted in* 2010 U.S.C.C.A.N. 722, 730 ("Title X establishes the Bureau of Consumer Financial Protection (Bureau), which will be an independent bureau within the Federal Reserve System.").

[5] Presidential Dodd-Frank Statement, *supra* note 3.

[6] S. REP. NO. 111-176, at 11 (2010).

[7] Rachel E. Barkow, *Insulating Agencies: Avoiding Capture Through Institutional Design*, 89 TEX. L. REV. 15, 18 (2010).

[8] S. REP. NO. 111-176, at 11 (2010).

[9] *Id.* at 15; *see also* H.R. Rep. No. 111-517, at 874 (2010) (Conf. Rep.), *reprinted in* 2010 U.S.C.C.A.N. 722, 730 ("The Bureau will have the authority and accountability to ensure that existing consumer protection laws and regulations are comprehensive, fair, and vigorously enforced.").

[10] Senate Report No. 111-176, at 15-16 (2010) (quoting congressional testimony of Patricia McCoy on Mar. 3, 2009). For additional analysis of failures by federal bank regulators to protect consumers during the housing boom that led to the financial crisis, *see, e.g.,* KATHLEEN ENGEL & PATRICIA A. MCCOY, THE SUBPRIME VIRUS 157-205 (2011); SIMON JOHNSON & JAMES KWAK, 13 BANKERS: THE WALL STREET TAKEOVER AND THE NEXT

report concluded that "it was the failure by the [federal] prudential regulators to give sufficient consideration to consumer protection that helped bring the financial system down."[11]

As explained in Part II of this paper, the financial services industry and most Republican members of Congress vigorously opposed the creation of CFPB. During the debates on Dodd-Frank, industry trade groups and Republican legislators argued that CFPB was likely to impose burdensome regulations that would reduce the availability of credit to consumers. CPFB's opponents also maintained that the consumer protection function should remain with federal banking agencies in order to prevent consumer safeguards from undermining the safety and soundness of financial institutions. Opponents further charged that CFPB would have unprecedented freedom to operate without meaningful checks and balances. Accordingly, they alleged, CFPB would likely become an all-powerful bureaucracy that would stifle innovation and flexibility in consumer financial services.[12]

Republicans failed to stop Congress from authorizing the creation of CFPB in Title X of Dodd-Frank. However, following

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FINANCIAL MELTDOWN 120-32, 141-44 (2010) ("The Federal Reserve sidestepped its consumer protection responsibilities by claiming it lacked jurisdiction. . . . While the Federal Reserve was neglecting to protect consumers, other regulatory agencies were neglecting to ensure the soundness of the banks they supervised," *id.* at 142, 143); Oren Bar-Gill & Elizabeth Warren, *Making Credit Safer*, 157 U. PA. L. REV. 1, 81-95 (2008) ("The problem is deep and systemic. These agencies are designed with a primary mission to protect the safety and soundness of the banking system. This means protecting banks' profitability. Consumer protection is, at best, a lesser priority," *id.* at 90); Adam J. Levitin, *Hydraulic Regulation: Regulating Credit Markets Upstream*, 26 YALE J. ON REG. 143, 151-69 (2009) ("The events of the past year have laid bare the shortcomings of our current system of financial-institution regulation. These shortcomings have played out on two levels: consumer protection and systemic risk," *id.* at 151); Arthur E. Wilmarth, Jr., *The Dodd-Frank Act's Expansion of State Authority to Protect Consumers of Financial Services*, 36 J. Corp. L. 893, 897-919 (2011) ("Federal regulatory inaction and federal preemption encouraged federally-chartered depository institutions and their affiliates to become leading participants in nonprime mortgage lending. Ultimately, the regulatory failures of the FRB, the OCC, and the OTS contributed to defaults and foreclosures on millions of nonprime loans," *id.* at 898).

[11] S. REP. NO. 111-176, at 166 (2010).

[12] Melissa B. Jacoby, *Dodd-Frank, Regulatory Innovation, and the Safety of Consumer Financial Products*, 15 N.C. BANKING INST. 99, 100 (2011).

Dodd-Frank's enactment, the financial services industry and Republican legislators launched a new campaign to weaken CFPB's autonomy and authority. The financial sector gave strong backing to Republican candidates in the 2010 congressional elections. That support helped Republicans to secure control of the House and capture several additional Senate seats.

Shortly after the new Congress convened in January 2011, Republican leaders in the House introduced legislation that would transform CFPB's governance, powers and funding. The House Republican bills proposed (i) to create a five-member bipartisan commission to govern CFPB in place of a single Director, (ii) to grant federal banking agencies an expanded veto power over CFPB's regulations, and (iii) to give Congress complete control over CFPB's budget. At the same time, forty-four Republican Senators declared that they would block confirmation of any Director of CFPB until the President and Democratic leaders in Congress agreed to make the same three changes to CFPB's operations. Republicans again argued that CFPB would be a menacing superagency without meaningful oversight unless the stipulated changes were made. By preventing confirmation of any Director, Republicans significantly limited CFPB's ability to implement its mandate under Dodd-Frank.[13]

[13] On January 4, 2012, President Obama invoked his constitutional power of recess appointment and appointed Richard Cordray as CFPB's first Director. Helene Cooper & Jennifer Steinhauer, *Bucking Senate, Obama Appoints Consumer Chief*, N.Y. TIMES, Jan. 5, 2012, at A1; Laura Litvan & Kathleen Hunter, *Cordray Appointment Signals Obama's Readiness to Campaign Against Congress*, BLOOMBERG, Jan. 5, 2012, http://www.bloomberg.com/news/2012-01-05/obama-s-naming-of-cordray-signals-readiness-for-brawling-election-campaign.html. Republican members of Congress and some analysts challenged the validity of Mr. Cordray's appointment. They maintained that the Senate was not in recess when President Obama issued the appointment. They pointed to the Senate's scheduling of brief pro forma sessions that were explicitly designed to prevent President Obama from making recess appointments. The Obama Administration released an opinion of the Justice Department declaring that the Senate's pro forma sessions did not prevent the President from determining that (i) the Senate was unavailable to act as a body in performing its advise-and-consent function on Presidential appointments and was therefore in recess and (ii) in those circumstances the President could exercise his constitutional authority to make recess appointments. Cheryl Bolen, *Appointments and Nominations: Justice Department Releases Opinion Finding Recess Appointments Lawful*, 98 BNA'S BANKING REPORT

Contrary to the claims advanced by CFPB's opponents, Part III of this paper shows that CFPB's governance, powers and funding are similar to those of other federal financial regulators. CFPB's single-Director model of leadership is similar to the governance structure for the Office of the Comptroller of the Currency ("OCC") and the Federal Housing Finance Agency ("FHFA"). CFPB's regulatory and enforcement powers are comparable to those exercised by OCC, FHFA, the Federal Deposit Insurance Corporation ("FDIC") and the Federal Reserve Board ("FRB"). CFPB's ability to fund its operations without relying on congressional appropriations is, again, comparable to OCC, FHFA, FDIC and FRB. The financial services industry and its legislative allies have strenuously defended the governance structure, authority and independence of OCC and FHFA. Accordingly, it appears that CFPB's opponents are motivated by their opposition to CFPB's consumer protection mission rather than the bureau's structure.

As explained in Part IV, the three changes in CFPB's structure demanded by Republicans would significantly undermine CFPB's autonomy and its ability to fulfill its statutory mandate. Replacing CFPB's Director with a multimember commission would increase the likelihood of infighting and deadlock within CFPB's leadership. Allowing federal financial regulators to veto CFPB's regulations by majority vote on general "safety and soundness" grounds would make it very difficult for CFPB to adopt rules that might reduce the short-term profitability of financial institutions. Requiring CFPB to depend on congressional appropriations for its budget would greatly increase the risk that CFPB would be captured or neutralized by the financial services industry. Financial institutions and their trade associations have used the appropriations process to slash the budgets of the Commodity Futures Trading Commission ("CFTC") and the Securities and Exchange Commission ("SEC"), thereby impairing the ability of both agencies to fulfill their statutory agendas prescribed by Dodd-Frank. In combination, the three changes advocated by Republicans would seriously weaken CFPB's ability to protect consumers. Contrary to the claims of the financial services industry, any weakening of CFPB

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95 (Jan. 17, 2012); Cheryl Bolen, *Appointments and Nominations: White House Asserts Legal Rationale for Presidential Recess Appointments*, 98 BNA'S BANKING REPORT 99 (Jan. 17, 2012). Analysis of the validity of Mr. Cordray's recess appointment as CFPB Director is beyond the scope of this article.

would likely have deleterious effects not only on consumers, but also on the long-term soundness and stability of our financial system.

II. The Financial Services Industry and Its Congressional Allies Strongly Opposed CFPB's Creation and Have Sought to Undermine Its Autonomy and Authority

A. The Industry's Efforts to Prevent the Establishment of CFPB

During 2009 and 2010, financial industry trade groups—including the U.S. Chamber of Commerce and the American Bankers Association—waged an aggressive campaign to defeat the Obama Administration's proposal to establish an independent consumer financial protection agency.[14] From the beginning of the debates over Dodd-Frank, industry associations and their members gave "top priority [to] killing President Obama's proposal,"[15] because they viewed CFPB as an "unneeded, intrusive new agency that would increase the[ir] cost of doing business."[16] The financial services industry urged Congress to leave the responsibility for protecting

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[14] Jacoby, *supra* note 12, at 99 (describing the U.S. Chamber of Commerce's campaign against the creation of a consumer financial protection agency); *see also, e.g.,* Robert G. Kaiser, *The CFPA: How a crusade to protect consumers lost its steam*, WASH. POST, Jan. 31, 2010, at G01 (reporting that "[b]usiness groups – most vociferously the U.S. Chamber of Commerce and the American Bankers Association – have campaigned fiercely" against the proposed new agency); Phil Mattingly & Carter Dougherty, *Senate Republicans Plan to Block Consumer Bureau While Seeking Changes*, BLOOMBERG, May 6, 2011, http://www.bloomberg.com/news/2011-05-05/republican-senators-to-block-consumer-nominee-absent-changes-1-.html ("Banking lobbyists fought the [CFPB] from its inception. . . . The U.S. Chamber of Commerce pledged millions of dollars to 'kill' the bureau, running campaign advertisements and working a grassroots campaign that resulted in more than 200,000 letters designed to sway lawmakers . . . .").

[15] Edmund L. Andrews, *Banks Balk at Agency Meant to Aid Consumers*, N.Y. TIMES, July 1, 2009, at B1; *see also* Johnson & Kwak, *supra* note 10, at 198 (explaining that "[t]he banking lobby and its defenders closed ranks against" the proposed agency); Paul Wiseman et al., *Big Job Looms for New Consumer Protection Agency*, USA TODAY, June 24, 2010, at 1B ("Financial industry lobbyists have fought the new agency through every step of the legislative process.").

[16] Kaiser, *supra* note 14.

consumers of financial services with the federal banking agencies in order to ensure that any new consumer safeguards did not impair the "safety and soundness" of financial institutions.[17]

Republican members of Congress supported the financial services industry by strongly objecting to the creation of any independent consumer financial protection agency and by insisting that the consumer protection function must "remain with federal banking regulators."[18] Republican leaders in the Senate bitterly opposed the proposal by Senator Christopher Dodd (D-CT) to establish an independent CFPB within the Fed. The disagreement over CFPB ultimately prevented any bipartisan agreement on Dodd-Frank's terms.[19]

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[17] Mattingly & Dougherty, *supra* note 14; *see also* R. Christian Bruce, *Regulatory Reform: Summers Urges Speed on Bank Reforms, Says Consumer Protection Agency Essential*, 93 BNA'S BANKING REPORT 506 (Sept. 22, 2009) ("[T]he Consumer Bankers Association, the Financial Services Roundtable, and 23 other business groups said creating a stand-alone consumer protection agency with broad powers 'is not the correct approach.' Instead . . . existing regulatory agencies could be given beefed-up powers.").

[18] Mike Ferullo, *Regulatory Reform: State Attorneys General Make Push For Consumer Financial Protection Agency*, 94 BNA'S BANKING REPORT 309 (Feb. 16, 2010) (quoting argument by Senator Richard Shelby, the ranking Republican member of the Senate Banking Committee, that "consumer protection and safety and soundness regulation . . . must be integrated with each other, not separated from each other"); Kaiser, *supra* note 14 (quoting Senator Shelby's view that an independent agency would be "a folly and dangerous").

[19] *See* Cheyenne Hopkins, *Oversight by House GOP to Shape Rules*, AM. BANKER, Nov. 8, 2010, at 1 ("Of all the parts in the [Dodd-Frank] bill, the GOP objected most strenuously to the creation of a consumer protection agency . . . ."); Stacy Kaper, *Dodd Recounts Battles Over Reg Reform*, AM. BANKER, Aug. 24, 2010, at 1 (reporting that attempts by Senator Dodd to agree on a bipartisan bill with Senator Richard Shelby (R-AL) "broke down" because of Republican "hostility" to CFPB's creation); James Rowley & Lisa Lerer, *Consumer Agency Still 'Elephant' in Room for Finance Debate*, BLOOMBERG, May 3, 2010, http://www.bloomberg.com/news/2010-05-03/consumer-protection-still-elephant-in-room-for-financal-overhaul-debate.html (describing the view of Senator Bob Corker (R-TN) that CFPB's creation was "the most contentious issue" during the Senate's consideration of Dodd-Frank and was "the elephant in the room" that prevented any bipartisan agreement on Dodd-Frank).

After Republicans failed to block CFPB's creation, they introduced an amendment on the Senate floor that would have significantly reduced CFPB's powers and removed its independence. The Republican amendment would have placed the bureau firmly under FDIC's control and would have barred the bureau from examining or regulating depository institutions.[20] That amendment was supported by all but three Republican Senators, but it was defeated by the Democratic majority in the Senate.[21]

During the final Senate debates on Dodd-Frank, Senator Shelby declared that CFPB would impose "massive new regulatory burdens on businesses, large and small" and would "stifle innovation in consumer financial products."[22] Other Republican members of Congress similarly alleged that CFPB would wield vast and unaccountable powers with devastating consequences for American businesses and consumers.[23] Republican legislators warned that CFPB would be likely to adopt rules that could threaten the "safety

[20] Senator Shelby's amendment (S. 3826) would have (i) designated CFPB as a division of FDIC, subject to FDIC's oversight, (ii) required CFPB to obtain FDIC approval before issuing any rule, and (iii) exempted all depository institutions and most nonbank financial institutions from CFPB's jurisdiction. 156 CONG. REC. S3325-26 (daily ed. May 6, 2010) (remarks of Rep. Menendez).

[21] Senator Shelby's amendment failed by a vote of 38-61. All fifty-nine Democratic Senators and two Republican Senators (Charles Grassley and Olympia Snowe) voted against the amendment, while another Republican (Senator Robert Bennett) did not vote. *Id.* at S3327–28 (reporting the roll call vote on S. 3826).

[22] 156 CONG. REC. S5877 (daily ed. July 15, 2010) (remarks of Rep. Shelby).

[23] *See, e.g., id.* at S5884 (remarks of Sen. Kyl, asserting that CFPB "will have latitude to impose its will, with few checks and balances, on American credit providers, all of which will result in more expense, more regulation, higher costs for consumers, and less availability of credit"); *id.* at S5816 (daily ed. July 14, 2010) (remarks of Rep. Bond, declaring that CFPB would be a "new superbureaucracy with unprecedented power" and its "decisions on credit will be driven by the administration's political will and agenda"); *id.* at S3321-22 (daily ed. May 6, 2010) (remarks of Sen. Enzi, claiming that CFPB would become "the single most powerful agency in the Federal Government" and would exercise "unchecked power[,]" thereby creating rules that would be "bad for small businesses and our communities, and . . . bad for individual consumer choices and freedoms"); *see also* Jacoby, *supra* note 142, at 100 n.6, 101 n.9 (quoting similar statements by Republican members of Congress who opposed CFPB's creation).

and soundness" of financial institutions, notwithstanding any objections raised by federal banking agencies.[24] Dodd-Frank passed by substantial margins in both houses of Congress, but only three Republican House members and three Republican Senators voted in favor of the legislation.[25]

B. The Industry's Post-Dodd-Frank Campaign to Weaken CFPB

As soon as Dodd-Frank was passed, the financial services industry and its Republican allies began a new campaign to reduce CFPB's independence and authority. During the midterm elections of 2010, financial institutions and their trade groups gave a significant majority of their political contributions to Republican congressional candidates. The financial services industry's strong backing for Republican candidates in 2010 represented a sharp reversal from the industry's political behavior in 2006 and 2008, when the industry gave a majority of its financial support to Democratic candidates. The financial industry's shift in contributions reflected the industry's

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[24] *See, e.g.,* 156 CONG. REC. S5816 (daily ed. July 14, 2010) (remarks of Sen. Bond) ("Politics will then decide how to allocate credit while operating outside the framework of safety and soundness, thus putting more risk back into the system when we were supposed to be taking risk out of the system."); *id.* at S3868 (daily ed. May 18, 2010) (remarks of Sen. Corker) ("The consumer protection agency has the ability to write rules with no veto authority against the safety and soundness of financial institutions."); *id.* at S3312 (daily ed. May 6, 2010) (remarks of Sen. Shelby) ("Under the Dodd bill, the [CFPB] would issue new rules without considering their impact on safety and soundness of financial institutions.").

[25] Mike Ferrulo, *Regulatory Reform: House Clears Financial Reform Bill Along Party Lines, Senate Action Delayed*, 95 BNA'S BANKING REPORT 5 (July 6, 2010) (reporting that Dodd-Frank passed by a vote of 237-192 in the House, and stating that "[t]hree Republicans voted for the bill and 19 Democrats voted against it."); Mike Ferrulo et al., *Regulatory Reform: Senate Sends Financial Regulatory To White House for President's Signature*, 95 BNA'S BANKING REPORT 90 (July 20, 2010) (reporting that Dodd-Frank passed by a vote of 60-39 in the Senate, and stating that Republican Senators Scott Brown, Susan Collins and Olympia Snowe voted in favor of Dodd-Frank while Senator Russ Feingold "was the sole Democrat in opposition").

anger and frustration over Dodd-Frank's passage and CFPB's creation.[26]

The Republicans secured control of the House and captured several additional seats in the Senate. Following the 2010 elections, Republican congressional leaders announced plans to introduce legislation that would change CFPB's structure and weaken its independence.[27] During the spring of 2011, Republican leaders in the House introduced bills that would (i) establish a multimember board to govern CFPB, (ii) give federal prudential regulators a stronger potential veto over CFPB's rulemaking, and (iii) enable Congress to

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[26] For discussions of the financial services industry's decision to shift its political support from Democrats to Republicans, due to the industry's resentment over Dodd-Frank's passage and CFPB's establishment, see T.W. Farnham & Paul Kane, *Democratic campaign committees losing big Wall Street donors*, WASH. POST, July 6, 2010, at A01("A revolt among big donors on Wall Street is hurting fundraising for the Democrats' two congressional campaign committees, with contributions from the world's financial capital down 65 percent from two years ago."); Stacy Kaper, *Banks Use Election as Payback for Reg Reform*, AM. BANKER, Sept. 7, 2010, at 1 ("Though Democrats scored a big political victory in passing regulatory reform, many are already paying for it as the financial services industry directs more of its contributions toward Republicans and moderates who tried to pare back the revamp."); Brody Mullins & Alicia Mundy, *Corporate Political Giving Swings Toward the GOP*, WALL ST. J., Sept. 21, 2010, at A5 ("Corporations have begun to send a majority of donations from their political action committees to Republican candidates, a reversal from the trend of the past three years."); Robert Schmidt, *Wall Street Banking on Republicans to Push Legislative Goals*, BLOOMBERG, Sept. 14, 2010, http://www.bloomberg.com/news/2010-09-14/wall-street-banking-on-republicans-to-push-legislative-goals.html ("Financial firms . . . for most of this year have been shifting political contributions to Republicans . . . ."); *see also* Kevin Wack, *Big Banks Electing to Give Obama Less Cash*, AM. BANKER, Aug. 30, 2011, at 1 (reporting that "[m]any bankers are still particularly angry about Dodd-Frank, which they view as regulatory overkill").

[27] Clea Benson & Phil Mattingly, *Firms That Fought Dodd-Frank May Profit Under Republican House*, BLOOMBERG, Nov. 2, 2010, http://www.bloomberg.com/news/2010-11-03/companies-that-fought-dodd-frank-may-profit-under-republican-u-s-house.html; Stacy Kaper, *Review 2010/Preview 2011: Redrawing the Battle Lines on Reform*, AM. BANKER, Jan. 3, 2011, at 1; Stacy Kaper, *ELECTIONS 2010: Bachus Plots Agenda, But Faces Leadership Challenge*, AM. BANKER, Nov. 4, 2010, at 4.

control CFPB's budget through the appropriations process.[28] Financial industry trade groups and major banks strongly supported Republican efforts to reduce CFPB's autonomy and authority, and they urged House members to pass the Republican bills.[29]

On July 21, 2011 (the first anniversary of Dodd-Frank's enactment), the House of Representatives passed legislation that would (i) create a five-member commission to oversee CFPB, (ii) suspend all of CFPB's powers until the Senate confirmed a Director of CFPB, and (iii) expand the authority of the Financial Stability Oversight Council ("FSOC") to veto CFPB's regulations.[30] Under

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[28] Kate Davidson, *Subcommittee Approves Bills to Revamp CFPB*, AM. BANKER, May 5, 2011, at 3; Brady Dennis & Ylan Q. Mui, *Fight over consumer bureau about to enter next phase* ,WASH. POST, May 4, 2011, at A17; Mike Ferrulo, *Consumer Protection: GOP Lawmakers Take First Legislative Steps to Restructure New Consumer Bureau*, 96 BNA'S BANKING REPORT 850 (May 10, 2011); Cheyenne Hopkins, *Political Sniping Dominates House Hearing on the CFPB*, AM. BANKER, Apr. 7, 2011, at 3; Jennifer Liberto, *Republicans aim to weaken consumer bureau*, CNN MONEY, Apr. 6, 2011, http://money.cnn.com/2011/04/06/news/economy/republicans_consumer_bureau/index.htm.

[29] *See, e.g.,* Mattingly & Dougherty, *supra* note 14 (reporting that the American Bankers Ass'n, Consumer Bankers Ass'n, Bank of America, Citigroup and Capital One lobbied in support of the Republican-backed House bills to change CFPB); *New consumer agency under fire from GOP, banks*, ASSOCIATED PRESS FIN. WIRE, Mar. 16, 2011 (describing support for Republican legislation among financial industry trade groups); Memo from Floyd Stoner, Exec. Vice President, Am. Bankers Assoc., to Members of the U.S. House of Representatives (July 20, 2011), *available at* http://www.aba.com/NR/rdonlyres/76DCD307-2D7E-48A6-A10F-623175F0AEAD/72899/HouseMemoreCFPBBill072011.pdf (expressing support for Republican legislation to change CFPB); Letter from Richard Hunt, President of the Consumer Bankers Assoc., to Representative Shelley Moore Capito (May 3, 2011).

[30] Kate Davidson & Joe Adler, *As CFPB Takes Flight, GOP Bill Aims to Clip Its Wings*, AM. BANKER, July 22, 2011, at 2 ("The legislation . . . would replace the agency's director with a five-member commission, mak[ing] it easier for other regulators to override its rules and suspend its powers until a permanent leader is in place."); Mike Ferullo, *Consumer Protection: House Approves Legislation to Alter CFPB As Agency Gets Underway: Obama Vows Veto*, 97 BNA'S BANKING REPORT 163 (July 26, 2011) (stating that the House bill (H.R. 1315) passed by a vote of 241-173 and all but one Republican member voted for the bill, while all but ten Democratic members voted against it).

the House bill, a majority of FSOC's members could vote to override any CFPB regulation that they found to be inconsistent with the safe and sound operations of U.S. financial institutions, and CFPB would be barred from participating in any override vote by FSOC.[31] In contrast, as discussed below, Dodd-Frank permits FSOC to veto a CFPB regulation only if two-thirds of FSOC's members (including CFPB) determine that the challenged regulation would threaten the safety and soundness of the entire U.S. banking system or the stability of the entire U.S. financial system.[32] Republicans also sponsored a separate House bill that would make all of CFPB's funding subject to congressional appropriations by 2013.[33]

Republicans in the Senate actively supported the efforts of their House colleagues. On May 5, 2011, Senator Richard Shelby and forty-three other Republican Senators declared that they would block Senate confirmation of any CFPB Director until Congress passed legislation that incorporated the three principal changes included in the House bills.[34] Senator Shelby and his Republican colleagues demanded that Congress establish a multimember board to govern CFPB, give federal banking agencies a "safety-and-soundness check" over CFPB's rules and ensure congressional control over CFPB's budget.[35] The American Bankers Association applauded the

[31] Larry Bivins, *House passes Duffy bill*, GANNETT NEWS SERVICE, July 21, 2011 (available on Lexis).

[32] *See infra* note 1147 and accompanying text.

[33] Thecla Fabian, *Appropriations: Obama Opposes Financial Services Elements Within House Spending Bill as It Nears Floor*, 97 BNA'S BANKING REPORT 112 (July 19, 2011) (describing H.R. 2434, which would "make CFPB's funding subject to the annual appropriations process beginning in fiscal 2013"); Mike Ferrulo, *Consumer Protection: House GOP Seeks Control of CFPB Funding As Agency Readies for July 21 Start Date*, 96 BNA'S BANKING REPORT 1137 (June 21, 2011) (discussing introduction of the measure by House Republicans).

[34] Mike Ferrulo, *Consumer Protection: Republican Senators Vow to Block Nominee For CFPB Without Changes to New Agency*, 96 BNA'S BANKING REPORT 849 (May 10, 2011) (describing letter sent by Republican Senators to President Obama); *see also* Mattingly & Dougherty, *supra* note 14 (reporting that "[t]he structural changes proposed by the senators in their letter echo proposals advancing in the Republican-controlled House").

[35] News Release by Richard Shelby, United States Senator, Alabama, 44 U.S. Sens. To Obama: No Accountability, No Confirmation (May 5, 2011), *available at* http://shelby.senate.gov/public/index.cfm/newsreleases?ID=893bc8b0-2e73-4555-8441-d51e0ccd1d17 (citing to "text of [a] letter to

Republican Senators for insisting on those changes as a precondition for confirming any Director of CFPB.[36]

During the Senate Banking Committee's hearing on July 19, 2011, Senator Shelby again maintained that the CFPB was a "huge new and entirely unaccountable bureaucracy" that lacked any "meaningful congressional oversight."[37] Senator Shelby repeated the Republican demands for fundamental changes in CFPB's governance, funding and authority. Witnesses for the American Bankers Association and the U.S. Chamber of Commerce strongly supported Senator Shelby's position at the hearing.[38] The financial services industry also continued its pattern of giving the great majority of its contributions to Republican leaders in 2011, thereby rewarding Republicans for their vigorous opposition to Dodd-Frank and CFPB.[39]

President Obama, declaring, *inter alia*, that '[t]he present structure of [CFPB] . . . violates basic principles of accountability . . . .'"). Two Republican Senators – Scott Brown of Massachusetts and Lisa Murkowski of Alaska – did not sign Senator Shelby's letter; Mattingly & Dougherty, *supra* note 14.

[36] Mattingly & Dougherty, *supra* note 14 (quoting statement by Frank Keating, head of the American Bankers Association).

[37] Thecla Fabian, *Consumer Protection: Senate Banking Hearing Highlights Continued CFPB Structure, 'Accountability' Stalemate*, 97 BNA'S BANKING REPORT 165 (July 26, 2011) (quoting Senator Shelby's opening statement at a hearing of the Senate Banking Committee on July 19, 2011). In a contemporary op-ed, Senator Shelby denounced the CFPB as "the most powerful yet unaccountable bureaucracy in the federal government." Richard Shelby, *The Danger of an Unaccountable 'Consumer-Protection' Czar*, WALL ST. J., July 21, 2011, at A17. During a Senate committee hearing on September 6, 2011, Senator David Vitter (R-LA) similarly argued that "[t]here's a real danger of the CFPB being a super bureaucracy that does a lot of damage to the economy by overreaching in its attempts to make decisions for consumers." Kate Davidson, *Cordray Hearing Devolves into Partisan Fight Over CFPB Structure*, AM. BANKER, Sept. 7, 2011.

[38] Fabian, *supra* note 37.

[39] Jonathan D. Salant & Lisa Lerer, *Romney Lures Obama Wall Street Donors*, BLOOMBERG, Sept. 27, 2011, http://www.bloomberg.com/news/2011-09-27/romney-lures-obama-wall-street-donors-in-race-for-campaign-cash.html ("Republican presidential hopeful Mitt Romney has raised more than twice as much money from Wall Street as Barack Obama . . . ."); Wack, *supra* note 26 ("In 2008, Barack Obama was the toast of Wall Street. But so far in the 2012 race, the six largest U.S. banks have switched sides in a dramatic way, and are giving far more money to GOP hopeful Mitt

Meanwhile, a contemporaneous poll commissioned by Consumer Reports reported that 74% of respondents favored the creation of CFPB as an independent agency with the sole mission of protecting consumers of financial services. The poll showed that large majorities of Democrats, independents and Republicans supported CFPB and its mission.[40] More than four-fifths of the poll respondents agreed that CFPB's "top priorities" should include "strengthening and enforcing rules against deceptive and unfair practices" by financial institutions and "requiring that mortgage and other documents be easier for consumers to understand."[41]

Nearly three-quarters of the poll's respondents also supported Dodd-Frank as a whole, including a majority of

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Romney than they are to the sitting president. . . . While Obama has touted Dodd-Frank as an achievement of his first term, Romney has criticized the law."); Kevin Wack, *GOP Fundraising Beats Dems'*, AM. BANKER, Aug. 31, 2011, at 3 (reporting that Rep. Spencer Bachus and Sen. Richard Shelby, the Republican leaders on the House and Senate banking committees, had received much larger amounts of campaign contributions in 2011 than their Democratic counterparts, Rep. Barney Frank and Sen. Tim Johnson, and a larger percentage of the Republicans' contributions came from the financial services industry); William Selway & Martin Z. Baum, *Derivatives: Bachus Is Wall Street's Man in Jefferson County*, BLOOMBERG BUSINESSWEEK, May 31 – June 5, 2011, at 32 (observing that Rep. Bachus was a "leading critic of the Dodd-Frank law" and "the third-biggest recipient of donations from financial companies" over the past two decades); Gary Rivlin, *The Billion Dollar Bank Heist: How the financial industry is buying off Washington – and killing reform*, NEWSWEEK, July 18, 2011, at 9 (describing the financial services industry's large contributions to Republican leaders who opposed Dodd-Frank and CFPB, including Rep. Sean Duffy (R-WI), who described CFPB as a "rogue agency" with an "authoritarian structure").

[40] Chris Morran, *Poll: Overwhelming Majority of Voters Want a Strong, Undiluted CFPB*, CONSUMERIST, July 19, 2011 (stating that "83% of Democrats, 73% of independents and 68% of Republicans" expressed support in the poll for a strong CFPB) (Newstex Web Blog available on Lexis).

[41] *New Poll Shows Strong Support for Consumer Financial Protection Bureau*, PR NEWSWIRE, July 20, 2011 (describing press release issued by Consumers Union summarizing the poll's results); *see also* Jim Puzzanghera, *GOVERNMENT: Fight over watchdog continues*, L.A. TIMES, July 21, 2011, at B1 ("Advocacy group Consumers Union on Wednesday released results of a recent poll showing that 74% of respondents supported the new bureau.").

Republican respondents.[42] Given the strong public backing for CFPB and Dodd-Frank, as well as widespread popular hostility toward large financial institutions, Republican leaders evidently concluded that their most prudent course of action would be to push for legislation imposing tight restrictions on CFPB instead of seeking to eliminate the bureau.[43] Representative Barney Frank (D-MA) alleged that the Republican-backed House legislation "is as close as [Republicans] dare come now, because of public opinion, to abolishing the whole agency. . . . They do understand that politically it's not a good idea to be fully straightforward about their intentions, and they'd really like to repeal it."[44]

In October 2011, the Senate Banking Committee approved President Obama's nomination of Richard Cordray as the CFPB's first Director by a party-line vote of 12-10, with all Republican committee members voting against the nomination.[45] Two months

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[42] Kevin Wack, *Why GOP Changed Its Dodd-Frank Strategy*, AM. BANKER, Aug. 1, 2011, at 1 (reporting that "[71%] of the poll's respondents favored Dodd-Frank as a whole, including 60% of Republicans"); *see also* Jonathan Chait, *TRB from Washington: Dithering Heights: Obama shows a new level of passivity on financial reform*, NEW REPUBLIC, July 14, 2011, at 2 (stating that "[p]olls in 2010 showed overwhelming support for strong financial regulation, and what little information has come out since suggests strong anti-Wall Street sentiment remains").

[43] Wack, *supra* note 42; Rivlin, *supra* note 39; *see also* Andrew Edgecliffe-Johnson & Francesco Guerrera, *US public loses faith in business*, FIN. TIMES, Jan. 25, 2011, http://www.ft.com/intl/cms/s/0/c60c01ba-27e5-11e0-8abc-00144feab49a.html#axzz1o5AWnRxq (reporting that "the number of Americans who trust US banks has dropped to a low of 25 per cent, down from 33 per cent a year ago and 71 per cent before the financial crisis"); Richard Burnett, *Consumers unhappy with banks*, ORLANDO SENTINEL, Dec. 23, 2010, at B5; *Americans' anger not easing over banks' practices*, CHARLESTON GAZETTE, Dec. 10, 2010, at P3D.

[44] Davidson & Adler, *supra* note 30 (quoting Rep. Frank). Similarly, Senate Banking Committee chairman Tim Johnson (D-SD) criticized Republican Senators for their "misleading claim of no CFPB accountability" and declared that Republicans were trying to "destroy the Bureau's ability to do its job of protecting American consumers . . . ." Davidson, *supra* note 37.

[45] Kate Davidson, *Senate Panel Approves Nomination for CFPB Director*, AM. BANKER, Oct. 7, 2011; Carter Dougherty, *Consumer Bureau Nomination Goes to Senate*, BLOOMBERG, Oct. 6, 2011, http://www.bloomberg.com/news/2011-10-06/consumer-bureau-nominee-approved-by-senate-banking-committee.html ("Today's 12-10 vote sends the nomination to the full Senate . . . ."); Jessica Wehrman, *Confirmation*

later, forty-five Republican Senators (more than enough to sustain a filibuster) voted to block the Senate's confirmation of Mr. Cordray. At the same time, Senate Republican leaders reaffirmed their intention to prevent confirmation of any nominee for Director until Congress passed legislation to satisfy their demands for changes in CFPB's governance, authority and funding.[46]

By preventing Senate confirmation of any Director, Republicans and the financial services industry greatly reduced CFPB's ability to exercise the powers that Dodd-Frank conferred on CFPB on July 21, 2011. According to a joint legal opinion prepared by the Inspectors General ("IGs") of the Treasury Department and the Fed, CFPB may take the following actions *without* a Senate-confirmed Director: (i) issuing rules, orders and guidance under existing federal consumer financial laws that were enforced by other federal agencies prior to the transfer of their functions to CFPB on July 21, 2011, (ii) enforcing previous orders, agreements and other rulings issued by those agencies under such laws, and (iii) examining depository institutions with assets of more than $10 billion.[47]

Battle: Cordray passes first test, but that may be it, THE COLUMBUS DISPATCH, Oct. 7, 2011, at 1A.

[46] Carter Dougherty, *Senate Republicans Block Cordray for CFPB*, BLOOMBERG, Dec. 8, 2011, http://www.bloomberg.com/news/print/2011-12-08/senate-republicans-block-obama-nominee-cordray-as-head-of-consumer-bureau.html; Kevin Wack, *Senate Republicans Block Cordray Nomination*, AM. BANKER, Dec. 9, 2011. All 52 Democratic Senators and one Republican Senator – Scott Brown (R-MA) – voted in favor of Mr. Cordray's confirmation. *Id*.

[47] In reaching this conclusion, the Inspectors General relied on Section 1066(a) of Dodd-Frank. Section 1066(a) authorizes the Treasury Secretary to perform the functions prescribed under Sections 1061-67 of Dodd-Frank (dealing with the transfer of consumer financial protection functions from other agencies) "until the Director of [CFPB] is confirmed by the Senate." Dodd-Frank § 1066(a). *See* Letter from Eric M. Thorson and Elizabeth A. Coleman to Rep. Spencer Bachus and Rep. Judy Biggert, forwarding "Joint Response by the Inspectors General of the Department of the Treasury and Board of Governors of the Federal Reserve System: Request for Information Regarding the Bureau of Consumer Financial Protection," at 4-6, (Jan. 10, 2011), *available at* http://www.treasury.gov/about/organizational-structure/ig/Documents/OIG-CA%2011004%20Committee%20of%20Financial%20Services%20Response%20CFPB.pdf ("If the Bureau does not have a Senate-confirmed Director by the designated transfer date, the Bureau may continue to operate under the Secretary's section 1066(a) authority.").

However, the Fed and Treasury IGs concluded that CFPB must have a Senate-confirmed Director in order to exercise its other powers under Dodd-Frank, including (1) prescribing rules under new statutory authorities not transferred from other federal agencies, (2) issuing rules and orders prohibiting unfair, deceptive and abusive acts and practices, and (3) supervising nondepository providers of consumer financial services.[48]

Thus, according to the joint opinion of the Fed and Treasury IGs, "[u]ntil the Senate confirms a director, the CFPB cannot oversee non-bank lenders or assume enhanced consumer protection powers mandated under [Dodd-Frank]."[49] Assuming the correctness of that opinion, the absence of a Senate-confirmed Director would prevent CFPB from establishing the type of consumer financial protection regime envisioned by Dodd-Frank—namely, a regime that ensures a "level playing field for all banks and . . . nondepository financial companies" and that "ha[s] enough flexibility to address future problems as they arise."[50] Although CFPB's inability to regulate nonbanks appeared to disadvantage banks, some bankers were prepared to accept an uneven playing field as long as it included a referee (i.e., CFPB) with sharply limited powers.[51]

[48] Letter from Thorson & Coleman, *supra* note 47, at 6-7. *See infra* note 68 and accompanying text (discussing CFPB's authority to supervise and examine nondepository providers of consumer financial services).

[49] Mike Ferrulo, *Consumer Protection: House Approves Legislation to Alter CFPB As Agency Gets Underway; Obama Vows Veto*, 97 BNA'S BANKING REPORT 163, 163 (July 26, 2011); *see also* Kate Davidson, *Leaderless CFPB Not a Blessing for Bankers*, AM. BANKER, July 12, 2011, at 1 (describing limitations on CFPB's authority without a Director).

[50] S. REP. NO. 111-176, at 11 (2010); *see also* Davidson, *supra* note 49, at 1 (quoting Amy Friend, former Senate Banking Committee chief counsel, who explained that "[t]he objective in creating [CFPB] was to have an agency that would focus more on consumer protection than the banking agencies had, and would be able to fully scrutinize larger nonbanks in particular").

[51] *See* Davidson, *supra* note 49, at 1 (stating that "some bankers are secretly gleeful the [CFPB] does not yet have a director"). As discussed *supra* in note 13, President Obama issued a recess appointment in January 2012 to install Richard Cordary as CFPB's first Director. However, the validity of that appointment was disputed by Republican members of Congress, and some observers predicted that adversely affected parties would file lawsuits to challenge Mr. Cordray's future rulemaking and enforcement actions as Director. Maria Aspan, *Cordray Recess Appointment Will 'Weaken' CFPB – Barofsky*, AM. BANKER Jan. 6, 2012, at 1 (quoting Neil Barofsky, former

For example, Andrew Kahr, (founder of Providian, the highly controversial credit card bank), argued in July 2011 that banks should prefer a leaderless CFPB, notwithstanding any concerns about the lack of a "level playing field" with nonbanks.[52] Mr. Kahr argued that "[f]or at least 200 years, banks have benefited from a playing field tilted sharply in [their] favor," and "[t]hat's why nonbanks want to own banks."[53] However, Mr. Kahr warned:

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special inspector general for the Troubled Asset Relief Program, who warned that Mr. Cordray's recess appointment had created "legal uncertainties and litigation that are 'going to weaken the [CFPB]'"); Kate Davidson, *Will Cordray Recess Appointment Cloud CFPB's Future?*, AM. BANKER, Jan. 5, 2012, at 1 (reporting that Mr. Cordray's recess appointment "set the stage for a showdown over the [CFPB's] authority that could take years to resolve").

[52] Andrew Kahr, *Let's Keep the CFPB Leaderless*, AM. BANKER, July 26, 2011, at 6 [hereinafter Kahr, *CFPB Leaderless*]. According to one of his previous op-eds, Mr. Kahr "is a principal in Credit Builders LLC, a financial product development company, and was the founding chief executive of Providian Financial Corp." Andrew Kahr, *It's Official: 'Prepaid' Cards Face Cap*, AM. BANKER, July 6, 2011, at 8 [hereinafter Kahr, *It's Official*]. Mr. Kahr was CEO of Providian from the early 1980s to 1988, and he subsequently served as a consultant to Providian from 1988 to 2000. According to one news account, he was "the genius behind Providian's success" in marketing high-cost credit cards to high-risk borrowers during the 1990s. Sam Zuckerman, *How Providian Misled Card Holders*, SAN FRANCISCO CHRONICLE, May 5, 2002, *available at* http://www.sfgate.com/cgi-bin/article.cgi?file=/c/a/2002/05/05/MN138910.DTL. In 2000, Providian paid $300 million to settle enforcement actions brought by state and federal officials alleging deceptive and predatory lending practices. "Mr. Kahr was not charged with wrongdoing," but his "consulting contract was ended in 2000." *Id.*; *see also* Arthur E. Wilmarth, Jr., *The OCC's Preemption Rules Exceed the Agency's Authority and Present a Serious Threat to the Dual Banking System and Consumer Protection*, 23 ANN. REV. BANKING & FIN. L. 225, 315-16 (2004) (referring to enforcement actions against Providian); *see also* Duncan A. MacDonald, *Comptroller Has Duty to Clean Up Card Pricing Mess*, AM. BANKER, Nov. 21, 2003, at 17 (publishing a letter from a former general counsel of Citigroup's European and North American credit card businesses, who alleged that Providian's "telemarketing and pricing practices . . . bordered on the criminal. For a decade Providian had been well known in the [credit] card industry as the poster child of abusive consumer practices").

[53] Kahr, *CFPB Leaderless*, *supra* note 52, at 6.

> [O]nce a director is confirmed banks will suffer severely. The CFPB will then have the power, under Dodd-Frank, to prohibit 'unfair' practices by banks. (Until the CFPB has a director, no regulator has that power.)
> . . .
> [Consider a scenario in which] the Republicans control both houses of Congress after the 2012 election. We might then hope for some rollback of CFPB authority. Even if there's only one chance in four of that, banks should prefer to avoid promulgation of very costly regulations and enforcement actions based on the CFPB's new powers until that election.[54]

Mr. Kahr added (perhaps in jest), "Let the bad times roll!"[55] In explaining why banks should oppose a Senate-confirmed CFPB Director, Mr. Kahr noted that a CFPB Director would have authority to condemn "unfair" consumer financial products, which could potentially include $39 bank overdraft fees and high-cost "credit protection products" offered by banks.[56] Mr. Kahr pointed out that

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[54] *Id.*

[55] *Id.* In a 1999 memo to a Providian executive, Mr. Kahr observed, "Making people pay for access to credit is a lucrative business wherever it is practiced. . . . The trick is charging a lot, repeatedly, for small doses of incremental credit." Zuckerman, *supra* note 52 (quoting March 1999 memo from Mr. Kahr to Providian Executive Vice President David Alvarez). In a 1998 memo to Providian executives, Mr. Kahr recommended that Providian should not disclose that some of its credit cards lacked any "grace period" before customer payments were due. Instead of a "no grace period" disclosure, Mr. Kahr suggested that Providian should use "one of the numerous ideas for a 'limited' grace period that have been put forward. 'Limited' meaning that the customer responds to (it) as if there were a grace period, but in reality almost no one gets the benefit of it." *Id.* (quoting July 1998 memo from Mr. Kahr to Mr. Alvarez and Dawn Greiner, Providian's head of new product development).

[56] Kahr, *CFPB Leaderless*, *supra* note 52, at 6; *see also infra* notes 606, 111 and accompanying text (discussing CFPB's authority to prohibit "unfair" acts or practices). Mr. Kahr's concern that CFPB might act to regulate overdraft fees was not misplaced. In September 2011, Raj Date, assistant to the Treasury Secretary for administering CFPB, indicated that the bureau would take a "closer look" at overdraft programs. Kate Davidson, *New*

bank regulators permitted profit margins for bank credit protection products that were much higher than the profit margins allowed by state insurance regulators for similar products sold by insurance companies. In Mr. Kahr's view, that differential provided "yet another example of a very unlevel playing field, enormously favorable to banks versus nonbanks."[57] Accordingly, he asked: "Is this the time to activate additional elements of [consumer compliance] regulation that can only render banks less profitable—and perhaps more inclined to take greater risks in order to achieve adequate return?"[58]

III. CFPB's Powers, Governance and Funding Are Similar to Those of Other Financial Regulators

CFPB's powers, governance, and funding are hardly unprecedented among federal financial regulators. CFPB's rulemaking and enforcement authorities resemble those of other federal bank regulators. CFPB's leadership by a single director is similar to the governance structure of OCC and FHFA. CFPB's ability to fund its operations without relying on congressional appropriations is comparable to other financial regulators except for CFTC and SEC. While the financial services industry and its Republican allies have vigorously attacked CFPB's perceived independence, they have strongly defended the autonomy enjoyed by OCC and FHFA, which represent the closest regulatory analogues to CFPB's structure. Thus, it appears that the financial industry and its legislative supporters are primarily opposed to CFPB's expected policy choices, not its structural characteristics.

CFPB Leader Pledges 'Tough' Enforcement Regime, AM. BANKER, Sept. 16, 2011, at 2 (summarizing a speech by Mr. Date on Sept. 15, 2011).

[57] Kahr, *CFPB Leaderless supra* note 52, at 6. For additional analysis of the advantages that banks – especially large banks – enjoy relative to nonbanks because of banks' access to federal safety net subsidies, see Arthur E. Wilmarth, Jr., *Wal-Mart and the Separation of Banking and Commerce*, 39 CONN. L. REV. 1539, 1588-93 (2007); *see also* Arthur E. Wilmarth, Jr., *The Dodd-Frank Act: A Flawed and Inadequate Response to the Too-Big-to-Fail Problem*, 89 OR. L. REV. 951, 957-59, 980-86 (2011) [hereinafter Wilmarth, *Too-Big-to-Fail Problem*] (describing the enormous explicit and implicit subsidies that U.S. and foreign governments provided to "too-big-to-fail" banks during the recent financial crisis).

[58] Kahr, *CFPB Leaderless*, *supra* note 52, at 6.

A. CFPB's Powers, Governance and Funding

Title X of Dodd-Frank, designated as the "Consumer Financial Protection Act of 2010" ("CFP Act"), establishes CFPB as an "independent bureau" within the FRB to "regulate the offering and provision of consumer financial products or services under the Federal consumer financial laws."[59] CFPB's statutory mission is "to implement and . . . enforce Federal consumer financial law consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services [that] are fair, transparent, and competitive."[60] The "[f]ederal consumer financial law[s]" that fall within CFPB's jurisdiction include eighteen previously enacted federal statutes, as well as the "new consumer financial protection mandates prescribed by the [CFP] Act."[61]

Title X provides that CFPB will be administered by a single Director.[62] The President appoints CFPB's Director for a five-year term with the Senate's advice and consent, and the President may remove the Director for "inefficiency, neglect of duty, or malfeasance in office."[63] The Director may issue rules, orders and guidance "to administer and carry out the purposes and objectives of the Federal consumer financial laws, and to prevent evasions

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59 Dodd-Frank § 1011(a); *see generally* Michael B. Mierzewski et al., *The Dodd-Frank Act Establishes the Bureau of Consumer Financial Protection as the Primary Regulator of Consumer Financial Products and Services*, 127 BANKING L. J. 722 (2010) (providing a helpful overview of CFPB's authority under Title X).

60 Dodd–Frank § 1021(a).

61 Mierzewski et al., *supra* note 59, at 724-25; *see also* Dodd-Frank § 1002(14) (defining "Federal consumer financial law" to include Title X of Dodd-Frank, eighteen federal consumer protection statutes that are enumerated in Dodd-Frank § 1002(12), and certain other laws).

62 Dodd-Frank § 1011(b)(1). As previously discussed, President Obama invoked his constitutional power of recess appointment and appointed Richard Cordray as CFPB's first Director in January 2012. However, the validity of that appointment was disputed by Republican members of Congress and some analysts. *See supra* notes 13, 51.

63 *Id.* § 1011(c). The Supreme Court has observed, in the context of a similar removal statute, that the quoted terms "are very broad and . . . could sustain removal of a [federal official] for any number of actual or perceived transgressions." Bowsher v. Synar, 478 U.S. 714, 729 (1986).

thereof."[64] The Director also hires and manages CFPB's employees.[65] CFPB may issue regulations to implement federal consumer financial laws and may also issue rules or orders to prohibit "unfair, deceptive, or abusive acts or practices" (UDAAP) in consumer financial services.[66] CFPB may also issue regulations to ensure that "the features of any consumer financial product or service . . . are fully, accurately, and, effectively disclosed to consumers in a manner that permits consumers to understand the costs, benefits, and risks associated with the product or service."[67]

Further, Title X empowers CFPB to supervise and examine depository institutions with assets of more than $10 billion (and their affiliates) as well as all nondepository providers of consumer financial services.[68] CFPB may pursue a variety of enforcement powers to prevent violations of Title X and CFPB's regulations thereunder, or any of the eighteen federal consumer financial statutes enumerated in Section 1002(12) of Dodd-Frank.[69] CFPB's enforcement authorities include (i) undertaking investigations and performing administrative discovery, (ii) initiating administrative enforcement proceedings, (iii) filing judicial enforcement actions, and (iv) referring criminal charges to the Department of Justice.[70]

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[64] Dodd-Frank § 1022(a).

[65] *Id.* §1013(a).

[66] Dodd-Frank §§ 1022(b), 1031(b).

[67] *Id.* § 1032(a).

[68] Depository institutions with assets of $10 billion or less will be examined by federal banking agencies to assess their compliance with consumer financial protection laws. Mierzewski et al., *supra* note 59, at 731-32. CFPB has authority (i) to obtain reports from smaller depository institutions, (ii) to include one of CFPB's examiners on the examination teams for such depository institutions, and (iii) to provide input to the primary regulators of such institutions with regard to the scope and conduct of examinations, the contents of examination reports and examination ratings. Dodd-Frank, § 1026.

[69] Dodd-Frank, §§ 1002(12), 1031, 1036(a)(1)(B), 1052-1055. CFPB may not bring an administrative enforcement hearing to enforce an enumerated federal consumer financial law to the extent that the law in question specifically limits CFPB's authority to do so. *Id.* § 1053(a)(2).

[70] *Id.* §§ 1052-56; *see* Mierzewski et al., *supra* note 59, at 732-35 (describing CFPB's enforcement powers). CFPB has authority to represent itself in the Supreme Court if it submits a request to the Attorney General and the Attorney General concurs or acquiesces in that request. Dodd-Frank § 1054(e).

CFPB may use administrative or judicial proceedings to obtain a wide range of legal and equitable remedies, including refunds, restitution, damages, cease-and-desist orders, civil money penalties and injunctive relief.[71] CFPB's administrative and judicial enforcement powers are generally similar to those granted to federal banking agencies and the Federal Trade Commission ("FTC").[72] Like the FTC, CFPB is statutorily barred from imposing punitive damages.[73]

Thus, Title X vests CFPB with broadly-defined powers to regulate providers of consumer financial products and services.[74] However, CFPB may not regulate the ability of persons to carry on the businesses of insurance, securities, commodity trading, or managing employee benefit or compensation plans.[75] In addition, sellers of nonfinancial goods and manufactured homes, real estate brokers, auto dealers, attorneys, accountants and tax preparers are not subject to CFPB's jurisdiction unless they engage in offering covered financial products or services.[76]

Title X protects CFPB's autonomy in several ways. Title X prohibits FRB from taking any of the following actions: (i) intervening in any CFPB examination, enforcement action or other proceeding; (ii) appointing, directing or removing any CFPB officer or employee; (iii) combining CFPB or any of its functions with any other FRB unit; (iv) reviewing, approving, or delaying any CFPB

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[71] *Id.* §§ 1053-1055.

[72] *See infra* notes 103-04 (discussing enforcement powers of federal banking agencies); 15 U.S.C. §§ 45, 57b, 57b-1 (2006) (prescribing the FTC's enforcement authorities).

[73] 15 U.S.C. § 57b(b) (prohibiting FTC from assessing punitive damages); Dodd-Frank, § 1055(a)(3) (imposing the same prohibition on CFPB).

[74] *See* Dodd-Frank Act §§ 1002(5), (6), (26) (defining "consumer financial product or service," "covered person," and "service provider"); Mierzewski et al., *supra* note 59, at 726 (describing persons, products and services that are regulated under Title X).

[75] Dodd-Frank § 1027(f)-(i), (m).

[76] *See id.* §§ 1027(a)-(e), 1029 (imposing further restrictions to the CFPB's regulatory authority); H.R. REP. NO. 111-517, at 875 (2010) (Conf. Rep.), *reprinted in* 2010 U.S.C.C.A.N. 722, 731 (discussing exclusions from CFPB's jurisdiction for the above types of firms); S. REP. NO. 111-176, at 160, 169–71 (2010) (same); Mierzewski et al., *supra* note 59, at 727-28 (explaining that the listed exclusions apply "to the extent that the parties are not engaged in offering a consumer financial product or service, or are not separately subject to an enumerated consumer law").

rule or order; or (v) reviewing or approving any legislative recommendations, testimony, or comments of CFPB's Director.[77] Thus, Title X "makes clear that [CFPB] is to function without any interference by [FRB]."[78]

In addition, Title X requires FRB to provide CFPB with annual funding up to a maximum limit of approximately $500 million (to be adjusted for inflation).[79] CFPB's guaranteed funding from FRB is not subject to congressional appropriations.[80] However, if CFPB determines that its guaranteed funding from the FRB is inadequate to carry out its responsibilities, CFPB must seek additional funds from Congress through the appropriations process.[81]

B. Comparing the Powers, Governance and Funding of CFPB and Other Financial Regulators

CFPB's powers are comparable to those of other federal financial regulators. As explained in the Senate report, Dodd-Frank's provisions for CFPB were "modeled on similar statutes governing the [OCC] and the Office of Thrift Supervision [("OTS")], which are located within the Department of Treasury."[82] Dodd-Frank abolished OTS,[83] but OCC continues to function as an autonomous bureau of the Treasury pursuant to the National Bank Act ("NBA").[84]

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[77] Dodd-Frank § 1012(c).
[78] S. REP. NO. 111-176, at 161 (2010).
[79] FRB must provide annual funding to CFPB in an "amount determined by [CFPB's] Director to be reasonably necessary to carry out [CFPB's] authorities" in view of other funding available to CFPB, up to the following maximum limits: "(i) 10% of the Fed's 2009 operating expenses in fiscal year 2011, (ii) 11% of such expenses in fiscal year 2012, and (iii) 12% of such expenses in each subsequent fiscal year, with appropriate increases to reflect future inflation." Dodd-Frank § 1017(a). Dodd-Frank will require FRB to provide approximately $500 million of funding to CFPB in fiscal year 2013 and subsequent years. S. REP. NO. 111-176, at 164 (2010) (graph).
[80] Dodd-Frank § 1017(a)(2)(C).
[81] *Id.* § 1017(e).
[82] S. REP. NO. 111-176, at 161 (2010).
[83] Dodd-Frank § 313. Dodd-Frank transfers the functions of OTS to FDIC, FRB and OCC. *Id.* § 312.
[84] RICHARD SCOTT CARNELL, JONATHAN R. MACEY & GEOFFREY P. MILLER, THE LAW OF BANKING AND FINANCIAL INSTITUTIONS 61-62 (4th ed. 2009).

Under the NBA, OCC is administered by a single official, the Comptroller of the Currency ("Comptroller").[85] Like the CFPB's Director, the OCC's Comptroller is appointed by the President for a five-year term, with the advice and consent of the Senate.[86] The Comptroller's autonomy is similar to that of the CFPB's Director. The Treasury cannot prevent or delay the issuance of any OCC regulation, and the Treasury may not intervene in any matter before the Comptroller (including an agency enforcement action) unless specifically authorized by law.[87]

FHFA is responsible for regulating Fannie Mae ("Fannie"), Freddie Mac ("Freddie") and the Federal Home Loan Banks ("FHLBs").[88] Like the CFPB's Director and the OCC's Comptroller, the FHFA's Director serves as the single head of the agency.[89] The FHFA Director's mode of appointment and term of office are similar to the CFPB's Director and the Comptroller. The President appoints the FHFA's Director for a five-year term with the Senate's advice and consent, but the President may also remove the FHFA's Director "for cause."[90] In contrast to the single-agency-head model of CFPB,

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[85] 12 U.S.C. § 1 (2006).

[86] *Id.* § 2. The President may remove the Comptroller "upon reason[s] to be communicated by him to the Senate." *Id.* As noted above, the President "may remove the Director [of CFPB] for inefficiency, neglect of duty, or malfeasance in office." Dodd-Frank § 1011(c)(3). Thus, the President is not limited with respect to the "reasons" he may invoke to remove the Comptroller. On the other hand, the stated reasons for removal of the CFPB Director appear to provide broad discretion to the President. *See supra* note 63 (quoting Bowsher v. Synar, 478 U.S. 714, 729 (1986)).

[87] 12 U.S.C. §§ 1, 1462a(b)(3).

[88] *Id.* §§ 4511, 4502(20) (establishing FHFA as the agency responsible for regulating Fannie, Freddie and the FHLBs). Fannie, Freddie and the FHLBs are generally referred to as "government-sponsored enterprises" ("GSEs"). CARNELL, MACEY & MILLER, *supra* note 84, at 31, 133.

[89] 12 U.S.C. §§ 4512(a), 4513(a). The FHFA's Director receives advice from the FHFA's Oversight Board "with respect to overall strategies and policies," but the Oversight Board "may not exercise any executive authority" over the FHFA. *Id.* § 4513a(a), (b).

[90] *Id.* § 4512(b). In contrast to the stipulated reasons for removal of the CFPB's Director, the grounds representing "cause" for removal of the FHFA's Director are not specified in the governing statute. *Compare* Dodd-Frank § 1011(c)(3) (providing that "inefficiency, neglect of duty, or malfeasance in office" are permissible reasons for removing the CFPB's Director), *with* 12 U.S.C. § 4512(b)(2) (providing that the FHFA's Director may be removed "for cause" without further specification).

OCC and FHFA, the FDIC and FRB are administered by multi-member boards.[91]

All five of the foregoing financial regulators have substantial budgetary autonomy. OCC, FDIC, and FHFA fund their operations primarily by collecting fees and assessments from the institutions they regulate.[92] FRB finances its operations from the earnings generated by its large portfolio of government securities and other investments.[93] Thus, each of those four agencies is completely independent of congressional appropriations. In contrast, CFPB has substantial but not complete budgetary autonomy. As explained above, the independent funding that CFPB receives from FRB is capped at approximately $500 million, adjusted for future inflation, and CFPB is required to seek a congressional appropriation if it wishes to increase its budget beyond that amount.

In some areas, CFPB's regulatory powers are less extensive than those of FHFA and federal bank regulators. For example, FHFA may serve as conservator or receiver of any of its regulated entities.[94] FHFA has served as conservator for Fannie and Freddie since September 2008.[95] FDIC has similar authority to act as conservator or receiver for any FDIC-insured national or state bank,[96] or as receiver for any financial company whose failure "would have serious effects on financial stability in the United States."[97] CFPB

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[91] CARNELL, MACEY & MILLER, *supra* note 84, at 61-63. Two other federal financial regulators – CFTC and SEC – are similarly administered by multimember commissions. THOMAS LEE HAZEN, THE LAW OF SECURITIES REGULATION § 1.3[1], at 27, § 22.7[1], at 752 n.28 (6th ed. 2009).

[92] CARNELL, MACEY & MILLER, *supra* note 84, at 61-63, 314-18; FEDERAL HOUSING FINANCE AGENCY, REPORT TO CONGRESS 2010, at 106 (2010) [hereinafter FHFA 2010 ANNUAL REPORT], *available at* http://www.fhfa.gov/webfiles/21572/FHFA2010_RepToCongress6_13_11.pdf.

[93] CARNELL, MACEY & MILLER, *supra* note 84, at 62.

[94] 12 U.S.C. § 4617 (2006).

[95] FHFA was appointed as conservator of Fannie and Freddie on September 6, 2008, and it has continued to administer those conservatorships since that time. FHFA 2010 ANNUAL REPORT, *supra* note 92, at 1-8.

[96] CARNELL, MACEY & MILLER, *supra* note 84, at 700-01; 12 U.S.C. § 1821(c).

[97] Dodd-Frank §§ 203(b), 204; *see also* H.R. Rep. No. 111-517, at 865-66 (2010) (Conf. Rep.), reprinted in 2010 U.S.C.C.A.N. 722, 723 (explaining that Title II of Dodd-Frank authorizes the Treasury Secretary to appoint FDIC as receiver of a financial company in order to "mitigate serious adverse effects on financial stability in the United States").

does not have authority to act as conservator or receiver for any provider of consumer financial services.

OCC exercises extensive supervisory powers over the structure and governance of national banks, including the authority to approve or deny applications for new charters, changes in the location of main offices and branches, opening of new branches, conversions into state banks, and mergers and consolidations with other depository institutions.[98] CFPB does not possess comparable supervisory powers over providers of consumer financial services. Unlike CFPB, OCC is a "safety and soundness" regulator, and OCC therefore has prudential authority to regulate national banks with regard to such matters as capital adequacy, asset quality, competence and integrity of management, and adequacy of liquidity.[99] FDIC and FRB have similar powers to regulate the safety and soundness of state banks and bank holding companies.[100] Likewise, FHFA has broad authority to supervise the capital, assets, and liabilities of Fannie, Freddie and the FHLBs for the purpose of promoting their safety and soundness.[101]

In other respects, CFPB's powers are similar to those of other financial regulators. CFPB, OCC, FDIC, FHFA and FRB all have authority to examine financial service providers subject to their respective jurisdictions in order to ensure compliance with applicable laws and regulations.[102] All five regulators also have comprehensive

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[98] *See* 12 U.S.C. §§ 26, 27, 30, 36, 214, 214a, 215, 215a, 215a-1, 1828(c), 1831u (2006) (outlining OCC's powers over the structure and governance of national banks); *see also* CARNELL, MACEY & MILLER, *supra* note 84, at 73-76, 86-89,191-95 (discussing OCC's powers over national banks).

[99] CARNELL, MACEY & MILLER, *supra* note 84, at 61-62, 251-53, 279-93, 627-35; Levitin, *supra* note 10, at 155-58.

[100] CARNELL, MACEY & MILLER, *supra* note 84, at 62-63, 251- 53, 279-93, 455-59, 627-35.

[101] 12 U.S.C.A. §§ 4611-4618, 4622-4624 (2010); *see, e.g., id.* § 4611(a)(1) (mandating that the FHFA's Director must "establish risk-based capital requirements for [Fannie and Freddie] to ensure that [Fannie and Freddie] operate in a safe and sound manner"); *id.* § 4624(a) (requiring the FHFA's Director to "establish criteria governing the portfolio holdings of [Fannie and Freddie], to ensure that the holdings are backed by sufficient capital and consistent with the mission and the safe and sound operations of [Fannie and Freddie]").

[102] For examination powers granted to OCC, FRB, FDIC and FHFA, see 12 U.S.C. §§ 481, 483, 1820, 1844(c), 4517 (2006). For the CFPB Director's powers to conduct examinations of nondepository providers of consumer

enforcement powers, including the authority to issue administrative cease-and-desist orders and civil money penalty orders.[103] However, unlike the other four agencies, CFPB does not have authority to remove or suspend officers and directors of the companies it regulates.[104]

C. Significant Statutory Limits on CFPB's Powers

As noted above, CFPB has broadly-defined powers to regulate providers of consumer financial services.[105] However, Title X of Dodd-Frank imposes several significant limitations on the exercise of those powers. CFPB may not impose any usury limit on consumer credit transactions "unless explicitly authorized by law."[106] Moreover, before it issues any regulation, CFPB must analyze "the potential benefits and costs to consumers and covered [providers of consumer financial services], including the potential reduction of access by consumers to consumer financial products or services resulting from such rule."[107] In particular, CFPB must assess the impact of any proposed rule on consumers in rural areas and depository institutions with assets of less than $10 billion.[108] CFPB

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financial services and large depository institutions with more than $10 billion in assets, see Dodd-Frank §§ 1024(b), 1025(a).

[103] For the authority of OCC, FRB and FDIC to issue administrative cease-and-desist orders and civil money penalty orders, see 12 U.S.C. § 1818(b), 1818(c), 1818(i). For FHFA's power to issue such orders, see *id.* §§ 4581, 4585, 4631, 4632, 4636. For CFPB's authority to issue such orders, see Dodd-Frank §§ 1053, 1055. Unlike the FHFA, FRB and OCC, the FDIC and CFPB may also file court actions to obtain civil remedies against persons subject to their regulation. See 12 U.S.C. § 1819(a)(Fourth) (outlining FDIC's authority to file court suits); Dodd-Frank § 1054 (outlining CFPB's litigation authority). All five agencies may file judicial actions to enforce their administrative orders. *See* Dodd-Frank § 1053(d) (describing CFPB's power to seek judicial enforcement of administrative orders); 12 U.S.C. § 1818(i) (granting similar authority to FDIC, FRB and OCC); *id.* § 4635 (granting similar authority to FHFA).

[104] For the authority of OCC, FRB and FDIC to issue orders removing or suspending officers and directors of regulated institutions, see 12 U.S.C. § 1818(e), 1818(g). For FHFA's power to issue such orders, see *id.* § 4636a.

[105] *See supra* notes 59-81 and accompanying text (outlining CFPB powers to regulate providers of consumer financial services).

[106] Dodd-Frank §1027(o).

[107] *Id.* § 1022(b)(2)(A)(i).

[108] *Id.* § 1022(b)(2)(A)(ii).

must also consider (i) any expected increase in the cost of credit for small businesses that would result from the proposed rule, (ii) any alternatives that would accomplish CFPB's statutory objectives and minimize any such increase in cost, and (iii) the advice and recommendations that CFPB's small business advisory panel submitted with regard to the proposed rule.[109]

Thus, CFPB must take due account of the likely costs and benefits of each new rule, and it must evaluate the impact of each rule on consumers, providers of consumer financial services and small businesses. Title X's requirement of a cost-benefit analysis for each new regulation makes CFPB's rulemakings more vulnerable to judicial challenges and therefore encourages CFPB to adopt incremental rather than far-reaching rules.[110]

Title X also imposes tight restrictions on CFPB's UDAAP authority. CFPB may not issue a rule or order declaring an act or practice to be "unfair" unless the agency has a "reasonable basis to conclude" that (1) the act or practice is likely to cause a "substantial injury to consumers which is not reasonably avoidable by consumers" and (2) that injury is "not outweighed by countervailing benefits to consumers or to competition."[111] Similarly, CFPB may not issue a rule or order declaring an act or practice to be "abusive" unless the act or practice either (a) "materially interferes" with a consumer's ability to understand a financial product or service, or (b) "takes unreasonable advantage" of (i) a consumer's lack of understanding of "the material risks, costs, or conditions" of the product or service, or (ii) the consumer's inability to protect his or her interests in selecting or using that product or service, or (iii) the consumer's reasonable reliance on the provider of that product or service.[112]

Title X allows other federal financial regulators to exert significant influence over CFPB's regulations. CFPB may not adopt any rule (including any UDAAP rule) unless it has previously consulted with federal banking regulators and other appropriate

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[109] *Id.* § 1100G.
[110] *See, e.g.,* Business Roundtable v. SEC, 647 F.3d 1146 (D.C. Cir. 2011) (striking down SEC's proxy access rule (Rule 14a-11) because SEC failed to comply with its statutory obligation to perform an adequate analysis of the potential costs and benefits of the rule, including the rule's impact on "efficiency, competition, and capital formation").
[111] Dodd-Frank § 1031(c).
[112] *Id.* § 1031(d).

federal agencies about the "consistency" of the proposed rule with "prudential, market, or systemic objectives administered by such agencies."[113] If any prudential regulator objects in writing to a proposed CFPB regulation, CFPB must include in its final rulemaking a description of the regulator's objection and CFPB's response to that objection.[114] In addition, any federal agency that is a member of the Financial Stability Oversight Council (FSOC) may petition FSOC to veto any regulation issued by CFPB.[115] After such a petition is filed, FSOC's chairman (the Treasury Secretary) may stay the effectiveness of the challenged CFPB regulation for up to 90 days to allow "appropriate consideration of the petition by [FSOC]."[116]

FSOC may set aside the challenged CFPB regulation, or any provision thereof, if two-thirds of FSOC's members determine that "the regulation or provision would put the safety and soundness of the United States banking system or the stability of the financial system of the United States at risk."[117] CFPB is the only federal financial regulator whose regulations are subject to override by an appellate body composed of heads of other agencies.[118] FSOC's

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[113] *Id.* §§ 1022(b)(2)(B), 1031(e).

[114] *Id.* § 1022(b)(2)(C).

[115] *Id.* § 1023. FSOC has ten voting members, including the heads of nine federal financial agencies – the Treasury Department, CFPB, CFTC, FDIC, FHFA, FRB, National Credit Union Administration, OCC and SEC – and an independent member with insurance experience. FSOC also includes five non-voting members – the Directors of the Federal Insurance Office and the Office of Financial Research, as well as three state officials responsible for regulating banks, insurance companies and securities firms. *Id*. § 111(b).

[116] *Id.* § 1023(c)(1).

[117] *Id.* § 1023(a), (c)(3). Only an "agency represented by a member of [FSOC]" may file a petition to stay or set aside a CFPB regulation. *Id.* § 1023(b)(1). It is not entirely clear from the text of section 1023 whether members of FSOC that are considered nonvoting members under section 111 are nevertheless entitled to vote on petitions to set aside CFPB regulations under section 1023.

[118] *Enhanced Consumer Financial Protection After the Financial Crisis: Hearing Before the S. Comm. on Banking, Hous., & Urban Affairs*, 112th Cong. at 8 (2011) [hereinafter Levitin Testimony] (written testimony of Prof. Adam J. Levitin), *available at* http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.Testimony&Hearing_ID=1980c90b-c8f9-4278-b509-d9de43e8506a&Witness_ID=74b14ea1-b0e7-40f5-8d1c-5de7aea00e5a.

potential veto provides "an unusually strong check on CFPB rulemaking."[119]

As noted above, Title X requires CFPB to consult with federal prudential regulators before issuing any regulation.[120] Accordingly, CFPB would have a strong incentive not to "risk a[n] FSOC rebuke" by adopting a regulation that had provoked a strong objection from another federal regulator during the consultative process.[121] It appears that CFPB's supporters included FSOC's veto power in Title X in order to blunt claims by CFPB's opponents that the bureau's rules could potentially threaten the safety and soundness of the banking industry and the stability of the financial system.[122]

Title X also subjects CFPB to significant oversight by the executive and legislative branches. CFPB must submit semi-annual reports to the President and Congress, and CFPB's Director must testify about those reports at semi-annual hearings before the responsible congressional committees.[123] In addition, CFPB's financial operations are audited each year by the Government Accountability Office ("GAO"), and the audit results are reported to Congress.[124] None of the other federal bank regulators is subject to an annual audit by GAO.[125] Thus, while CFPB's powers are undeniably broad, the agency is constrained by significant statutory limitations, "includ[ing] some unique requirements that other banking regulators do not face. . . ."[126]

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[119] *Id.*
[120] *See supra* notes 113-116 and accompanying text.
[121] Levitin Testimony, *supra* note 118, at 8.
[122] The Senate committee report on Dodd-Frank explained that the FSOC's veto "is designed to ensure that [CFPB's] consumer protection regulations do not put the safety and soundness of the banking system or the stability of the financial system at risk." S. REP. NO. 111-176, at 166 (2010). However, the report added, "The Committee notes that there was no evidence provided during its hearings that consumer protection regulation would put safety and soundness at risk. To the contrary, there has been significant evidence and extensive testimony that the opposite was the case." *Id.*
[123] Dodd-Frank § 1016.
[124] Levitin Testimony, *supra* note 118, at 8 (citing Dodd-Frank § 1017(a)(5)).
[125] *Id.*; Kate Davidson, *Four Big Myths About CFPB and Its Powers*, AM. BANKER, June 3, 2011, at 1.
[126] Davidson*, supra* note 125.

D. CFPB's Opponents Are Motivated by the Bureau's Consumer Protection Mission, Not Its Structure

As shown above, CFPB's powers, governance and funding are comparable to those of two other federal financial regulators—OCC and FHFA.[127] Yet the financial services industry and its legislative allies have strongly championed the single leadership governance model and funding arrangements for OCC and FHFA while condemning CFPB's similar features. The marked contrast between the financial industry's attacks on CFPB and its support for OCC and FHFA reveal that the industry's true reason for opposing CFPB is its consumer protection mandate, not its structure.

OCC is widely viewed as the most committed regulatory champion for the interests of major banks.[128] All of the largest banks operate under national charters, and assessments paid by national banks fund virtually all of OCC's budget. Understandably, given its strong budgetary incentives, OCC has competed strenuously with FRB, FDIC and state regulators to attract and retain the allegiance of large banks.[129] During the past three decades, OCC aggressively

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[127] *See supra* notes 82-1013 and accompanying text (discussing similarities among CFPB, OCC and FHFA).

[128] *See, e.g.,* Simon Johnson, *When Regulators Side With the Industries They Regulate*, ECONOMIX (May 19, 2011, 5:00 AM), http://economix.blogs.nytimes.com/2011/05/19/when-regulators-side-with-the-industry-they-regulate ("Over the last decade, [OCC] repeatedly demonstrated that it was very much on the side of banks."); Stacy Mitchell, *Why Republicans Hate Warren's CFPB But Love Another Bank Regulator*, HUFFINGTON POST, (Mar. 18, 2011, 10:32 AM), http://www. huffingtonpost.com/stacy-mitchell/why-republicans-hate-warr_b_837539.html ("The difference between [CFPB and OCC] is that the OCC sees its mission as protecting, not consumers, but big banks. . . . [OCC] has spent much of the last two decades preempting state laws that big banks don't like."); Joe Nocera, *Letting the Banks Off the Hook,* N.Y. TIMES, Apr. 19, 2011, at A25 ("The O.C.C. is a coddler, a protector, an outright enabler of the institutions it oversees. . . . It has consistently defended the Too Big to Fail banks."); Steven Pearlstein, *The Big Banks' Best Friend in Washington,* WASH. POST, May 27, 2009, at A12 ("[T]he too-big-to-fail crowd has found an unapologetic advocate in John Dugan, the comptroller of the currency.").

[129] ENGEL & MCCOY, *supra* note 10, at 157-61; Bar-Gill & Warren, *supra* note 10, at 91-95; Levitin, *supra* note 10, at 152-58; Wilmarth, *supra* note 52, at 259-65, 274-79, 296-97.

preempted state consumer protection laws and adopted "light touch" regulatory policies that helped national banks to build leading positions in consumer lending markets for residential mortgages and credit cards.[130] OCC also issued dozens of rulings that greatly expanded the permissible activities of national banks in areas such as data processing, derivatives, equipment leasing, insurance sales, real estate investments and securities activities.[131] During the legislative and regulatory deliberations over Dodd-Frank and other responses to the financial crisis, OCC strongly opposed a wide variety of reforms, including reforms that would (i) allow the states to give greater protections to consumers who buy products and services from national banks, (ii) provide improved safeguards for credit card customers, (iii) require national banks to retain a substantial portion of the risk of loans they sell for securitization, and (iv) impose tighter restrictions on compensation for bank executives. In each case, OCC adopted an anti-reform position that was strongly aligned with major banks and their trade associations.[132]

Following the enactment of Dodd-Frank, OCC continued to support anti-reform sentiments expressed by major banks. For

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[130] *See* authorities cited *supra* in note 1259; *see also* ENGEL & MCCOY, *supra* note 10, at 164-73; Wilmarth, *supra* note 10, at 910-19; Wilmarth, *supra* note 52, at 348-56.

[131] *See* CARNELL, MACEY & MILLER, *supra* note 84, at 115-27, 134-36, 153-58 (discussing OCC rulings related to data processing, equipment leasing, insurance sales and securities activities); Michael S. Edwards, *OCC Interprets The National Bank Act to Permit Banks to Own Hotels and Windmills*, 59 ADMIN. L. REV. 435 (2007) (describing OCC rulings that broadened the real estate investment powers of national banks); Saule T. Omarova, *The Quiet Metamorphosis: How Derivatives Changed the "Business of Banking*," 63 U. MIAMI L. REV. 1041 (2009) (reviewing OCC rulings that expanded permissible derivatives activities for national banks).

[132] *See, e.g.,* Joe Adler, *Trade Group Backs Dugan Stand,* AM. BANKER, Feb. 11, 2010, at 2 ("A securitization trade group . . . applauded recent remarks by Comptroller of the Currency John Dugan calling into question 'skin-in-the-game' risk-retention proposals."); Andrew Martin, *Does This Bank Watchdog Have a Bite?*, N.Y. TIMES , Mar. 28, 2010, http://www.nytimes.com/2010/03/28/business/28dugan.html?pagewanted=all (reporting on OCC's opposition to provisions of Dodd-Frank that would increase the applicability of state consumer protection laws to national banks); Gretchen Morgenson, *Credit Cards and Reluctant Regulators*, N.Y. TIMES, Jan. 17, 2010, http://www.nytimes.com/2010/01/17/business/17gret.html?pagewanted=all (reporting on OCC's opposition to stricter regulations for credit cards and executive compensation).

example, Acting Comptroller of the Currency John Walsh called for "modest" increases in capital requirements for systemically important financial institutions ("SIFIs"), while other federal regulators advocated significantly higher capital surcharges for SIFIs.[133] Mr. Walsh also questioned the desirability of other reforms mandated by Dodd-Frank, including the "Volcker rule" that restricts bank trading activities.[134] In a speech delivered on June 21, 2011, Mr. Walsh warned that "in the frenzy of the moment, we can overreact in response to crisis. . . . [W]e are in danger of trying to squeeze too much risk and complexity out of banking. . . ."[135] One news report observed that Mr. Walsh "voiced the frustrations of many bankers" about Dodd-Frank.[136]

Mr. Walsh and OCC created additional controversy by issuing regulations that preserved most of the sweeping preemption

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[133] Donna Borak, *OCC's Walsh Signals U.S. Split Over SIFI Charge,* AM. BANKER, June 21, 2011, at 1 (reporting that Mr. Walsh and OCC favored a "modest" capital surcharge for SIFIs, while other regulators, including FDIC chairman Sheila Bair, supported a much higher capital surcharge for SIFIs).

[134] Binyamin Appelbaum, *Dodd-Frank Backers Clash with Regulator*, N.Y. TIMES, July 23, 2011, at B1 (reporting that, under Mr. Walsh's direction, OCC "is seeking to soften a wide range of [Dodd-Frank's] provisions, in areas ranging from the bread-and-butter of consumer protection to the esoteric details of how much money banks can borrow."); Lindsey White, *OCC's Walsh criticizes 'Volcker rule,' Basel III capital rules*, SNL EUR. FIN. DAILY, June 23, 2011 (available on Lexis) (reporting that Mr. Walsh "has taken aim at the 'Volcker rule' and Basel III capital requirements, suggesting that regulators are overreacting to the abuses of the financial crisis"); Dave Clarke & Jonathan Spicer, *Regulators split on hedging under Vocker rule*, REUTERS, Sept. 21, 2011, http://www.reuters.com/article/2011/09/21/us-financial-regulation-volcker-idUSTRE78K42R20110921 (reporting that OCC "has pushed to give banks more leeway" in their trading operations by championing a broader interpretation of permissible hedging activities under Dodd-Frank's "Volcker rule," while FDIC, CFTC and SEC "have advocated for a tighter interpretation of the law"). For a discussion of debates over the enactment and implementation of the Volcker rule, see Wilmarth, *Too-Big-to-Fail Problem*, *supra* note 57, at 1025-30.

[135] John Walsh, Acting Comptroller of the Currency, Remarks Before the Centre for the Study of Financial Innovation (June 21, 2011), at 3, *available at* http://www.occ.treas.gov/news-issuances/speeches/2011/pub-speech-2011-78.pdf.

[136] Appelbaum, *supra* note 134.

rules that OCC had issued in 2004.[137] National banks and their trade associations warmly endorsed the OCC's revised preemption regulations.[138] However, the OCC's notice of proposed rulemaking for those regulations provoked an unusual public rebuke from Treasury Department General Counsel George Madison. Mr. Madison criticized OCC's proposed regulations for (i) adopting a preemption standard that was more favorable to national banks than the standard mandated by Dodd-Frank, and (ii) advocating the retention of most of the OCC's 2004 blanket preemption rules.[139] Democratic members of Congress strongly criticized Mr. Walsh, and President Obama nominated Thomas Curry, a member of FDIC's

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[137] For discussions of OCC's issuance of revised regulations that preserved most of the broad-scale preemption rules that OCC adopted in 2004, see Rob Blackwell, *"New" OCC Standard Feels Very Familiar*, AM. BANKER, May 16, 2011, at 1; R. Christian Bruce, *Preemption: Experts Debate Impact on OCC Powers If Preemption Proposal Is Pushed Back*, 97 BNA'S BANKING REP. 57 (July 12, 2011); R. Christian Bruce, *Preemption: OCC Finalizes Preemption Rule But Leaves Room for Backtracking*, 97 BNA'S BANKING REP. 157 (July 26, 2011) [hereinafter Bruce, "OCC Preemption Rule"]. The OCC's revised preemption regulations are published at Office of Thrift Supervision Integration; Dodd-Frank Act Implementation, 76 Fed. Reg. 43549 (July 21, 2011).

[138] *See* Blackwell, *supra* note 137 (reporting that "banking industry representatives," including the Financial Services Roundtable, endorsed the OCC's notice of proposed rulemaking); Bruce, "OCC Preemption Rule," *supra* note 137 (reporting that "[n]ational banks cheered the [OCC's final] rules," as did the American Bankers Association); Louise Story, *Dodd-Frank Rekindles Old Debate*, N.Y. TIMES, June 29, 2011, at B1 (reporting that Citibank, JP Morgan Chase, Wells Fargo and the Clearing House Association supported OCC's proposed rules).

[139] Kate Davidson, *Treasury Sharply Criticizes OCC's Preemption Proposal*, AM. BANKER, June 29, 2011, at 1; *see also* Binyamin Appelbaum, *Official from F.D.I.C. Picked to Lead Banking Regulator*, N.Y. TIMES, July 2, 2011, at B3 (reporting that "the Treasury Department took the unprecedented step of submitting a public comment to the [OCC] criticizing its [preemption] proposal for ignoring [Dodd-Frank's] intent"). I have previously argued that Dodd-Frank requires OCC to rescind all of its 2004 blanket preemption rules. Wilmarth, *supra* note 10, at 926-41; Arthur E. Wilmarth, Jr., *VIEWPOINT: OCC's Walsh Gets It Wrong on Preemption*, AM. BANKER, May 19, 2011, at 9; Arthur E. Wilmarth, Jr., *OCC Gets It Wrong on Preemption, Again*, AM. BANKER, July 29, 2011, at 8.

Board of Directors, to become Comptroller of the Currency in place of Mr. Walsh.[140]

Republican members of Congress expressed great concern that the Treasury Department's public criticism of the OCC's preemption proposal might undermine the OCC's policymaking independence. As noted above, OCC's autonomy is protected against interference by the Treasury Department in the same way that CFPB's independence is shielded against infringement by the FRB.[141] In July 2011, Representative Randy Neugebauer (R-TX) launched an investigation of the Treasury Department's decision to submit a public comment letter criticizing the OCC's preemption proposal.[142] He declared that the comment letter "prompted concerns regarding the Treasury Department's influence on OCC rulemaking," and he requested "assurances that the Treasury has permitted the OCC to act independently in the rulemaking for this and all provisions of the Dodd-Frank Act."[143] A few weeks later, Senator Shelby expressed similar concerns about Treasury's comment letter during the Senate Banking Committee's hearing on Mr. Curry's nomination for appointment as Comptroller.[144]

As a matter of principle, the emphatic defense of OCC's autonomy by Representative Neugebauer and Senator Shelby seems at odds with their insistence on stringent external controls over CFPB's budget and rulemaking.[145] Their diametrically opposed

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[140] Appelbaum, *supra* note 134; Appelbaum, *supra* note 139; Meera Louis, *Dodd-Frank May Be Subject of Confirmation Hearing for U.S. Bank Regulators*, BLOOMBERG, July 26, 2011, http://www.bloomberg.com/news/2011-07-26/fdic-occ-nominees-to-face-dodd-frank-queries-from-senate-panel.html; Kevin Wack, *Curry Answers Preemption Questions*, AM. BANKER, July 27, 2011, at 3.

[141] *See supra* notes 77-78, 87 and accompanying text.

[142] R. Christian Bruce, *Preemption: Neugebauer Seeks Records from Treasury, Cites Worries About Interference with OCC*, 97 BNA'S BANKING REP. 67 (July 12, 2011).

[143] *Id.* (quoting letter from Rep. Neugebauer to Treasury Secretary Timothy Geithner).

[144] Wack, *supra* note 140.

[145] *See* Mike Ferullo, *Regulatory Reform: Neugebauer Bill Would Allow Congress to Control Purse Strings of Consumer Agency*, 96 BNA'S BANKING REPORT 285 (Feb. 15, 2011) (describing Representative Neugebauer's demands for congressional control over CFPB's budget); Phil Mattingly & Carter Dougherty, *U.S. Consumer Bureau Funding Would Drop 40 Percent Under Republican Plan*, BLOOMBERG (Feb. 15, 2011, 5:16

attitudes toward OCC and CFPB indicate that Republican leaders are "less concerned about the structural independence of federal financial regulatory agencies and . . . more concerned about whether those agencies issue regulations that support the interests of our largest financial institutions."[146]

One finds the same incongruity in the decade-long campaign by major banks and their legislative allies to create a strong independent regulator for Fannie and Freddie. That campaign culminated in Congress' passage of a statute establishing FHFA in 2008.[147] From 1999 to 2008, a coalition of large lenders and their trade associations (known first as "FM Watch" and later as "FM Policy Focus") lobbied for legislation to rein in Fannie and Freddie. That coalition—which included the Financial Services Roundtable, the Consumer Bankers Association, Bank of America, JP Morgan Chase and Wells Fargo—raised a number of valid points, such as the systemic risks posed by Fannie and Freddie, their implicit government subsidies, their inadequate capital, and the weak supervisory powers granted to their existing regulator, the Office of Federal Housing Enterprise Oversight ("OFHEO"). However, coalition members also had a clear self-interest—namely, to remove or weaken Fannie and Freddie as competitors in markets for originating and securitizing residential mortgages. The lobbyists and

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PM), http://www.bloomberg.com/news/2011-02-15/house-republicans-target-consumer-protection-bureau-funding-in-budget-bill.html ("Neuge-bauer . . . has introduced legislation that would move the CFPB into the Treasury Department from the Fed, a step that would make it subject to the congressional appropriations process.") ; U.S. Fed. News, Rep., *Neugebauer Issues Statement on Bringing Oversight and Accountability to the Consumer Financial Protection Board [sic]*, (Feb. 10, 2011) (available on Lexis) ("Given the significant and perhaps over-regulating powers the CFPB has been given by the Obama Administration, Congress must have a say on the appropriation of taxpayer money funding this agency's operation."); Shelby, *supra* note 37, at 1 (explaining in a Wall Street Journal op-ed why Congress should have extensive oversight powers with respect to CFPB).

[146] Bruce, "OCC Preemption Rule," *supra* note 137, at 57-58 (quoting my comments); *see also* Mattingly & Dougherty, *supra* note 145, at 2 (quoting Rep. Brad Miller, D-NC, who maintained that "[t]he financial industry always hated [CFPB] . . . [a]nd in my experience in Congress, what the financial industry wants, Republicans are usually perfectly willing to do").

[147] Kate Davidson, *Question of Hypocrisy in GOP Assault on the CFPB,* 176 AM. BANKER 43, Mar. 21, 2011, at 1.

legislative allies for FM Watch and FM Policy Focus were mainly Republicans.[148]

As noted above, FHFA is similar to CFPB because it has a single-Director governance model and does not depend on congressional appropriations for its funding.[149] Major banks and their congressional allies helped to pass legislation ensuring that FHFA would be "a strong, independent regulator" with a secure funding source, thereby protecting FHFA against the threat of capture by Fannie and Freddie.[150] The obvious inconsistency between the

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[148] For descriptions of the lobbying campaign by FM Watch and FM Policy Focus, see Charles R. Babcock, *Mortgage Giants Stir Congress*, WASH. POST, June 11, 2003, at E01 ("Rival banking and insurance companies have focused more on what they consider the companies' unfair advantage in cheaper financing stemming from their government ties."); Jeffrey H. Birnbaum, Editorial, *The Man Behind the Byline Isn't Behind the Article. So, Who Is?*, WASH. POST, July 29, 2008, at A15 ("[T]he wide-ranging housing rescue bill was a victory for a coalition of banks and mortgage insurers that has been fighting for nearly a decade to rein in the mortgage finance giants Fannie Mae and Freddie Mac."); Stephanie Fitch & Erin Killian, *Freddie's Enemies*, FORBES, July 7, 2003, at 50 ("FM Watch . . . [was] [f]ounded in 1999 with the idea of keeping Freddie Mac and Fannie Mae honest."); Ed Roberts, *Competitors Want Fannie, Freddie Out of Their Business*, 7 CREDIT UNION J. 24, June 16, 2003, at 1 ("FM Watch has been lobbying Congress for the past few years to rein in the so-called mission creep of Freddie Mac and Fannie Mae . . ."); *Opponents Reload for Fight with the GSEs,* 8 CREDIT UNION J. 50, Dec. 13, 2004, at 12 (explaining how FM Watch hired new lobbyists to strengthen its fight for stronger regulation of Fannie Mae and Freddie Mac); Jeanne Cummings, *Regulation comes to those who wait*, POLITICO.COM (July 9, 2007, 7:41 PM), http://www.politico.com/news/stories/0707/4835.html ("For nearly eight years, the organization of bankers, consumer advocates and financial houses has been pushing for greater scrutiny of mortgage lending giants Fannie Mae and Freddie Mac.").

[149] *See supra* notes 79-81, 92-93 and accompanying text (explaining that CFPB's financial autonomy is not as extensive as FHFA's budgetary independence, because CFPB is assured of receiving approximately $500 million of funding from FRB but would be required to request a congressional appropriation in order to obtain supplemental funding).

[150] H.R. REP. NO. 110-142, at 87 (2007); *see also* Davidson, *supra* note 147, at 1 ("[Barney] Frank said, 'I think you've seen that with my Republican colleagues: many of them liked OFHEO, so they wanted it insulated, and they don't like CFPB, so they want to subject it to further controls.'"); *supra* note 148, *infra* notes 302-08 and accompanying text (explaining that a top priority of FHFA's supporters was to insulate FHFA from political capture

banking industry's support for FHFA and its vehement opposition to CFPB provides further evidence that attacks on CFPB's structure "are not born from a matter of principle, but just because [opponents] don't like the CFPB."[151]

IV. *The Changes to CFPB Demanded by the Financial Services Industry and Its Legislative Allies Would Seriously Impair CFPB's Independence and Effectiveness*

As described above, the financial services industry has enthusiastically supported demands by Republican congressional leaders for fundamental changes in CFPB's governance, powers and funding. Republican-backed legislation would establish a multimember board to govern CFPB, would increase the ability of prudential regulators to veto CFPB's rules on "safety and soundness" grounds, and would require CFPB to obtain its funding through congressional appropriations.[152] As shown below, each of those modifications would significantly impair CFPB's ability to fulfill its statutory mission.

A. CFPB's Director Should Not Be Replaced by a Multimember Commission

House Republicans passed legislation on July 21, 2011, that would create a five-member commission to administer CFPB in place of a single Director.[153] As Adam Levitin has observed, "[t]he scholarly literature on agency design has not achieved any consensus" as to whether single agency heads are superior or inferior to multimember commissions.[154] Administrative law scholars have generally described the two agency structures as offering relatively equal "trade-offs" between (1) greater "efficiency and accountability" within agencies administered by single officials and (2) increased "deliberation and debate" and "compromise" within

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by giving FHFA a secure funding source that would not be subject to congressional control).

[151] Davidson, *supra* note 147, at 1 (quoting Rep. Barney Frank).

[152] *See supra* notes 310-35 and accompanying text.

[153] *See supra* notes 30-31 and accompanying text (discussing House passage of H.R. 1315).

[154] Levitin Testimony, *supra* note 118, at 9.

multimember commissions.[155] In contrast, a 1987 evaluation of the Consumer Product Safety Commission ("CPSC") by the General Accounting Office ("GAO") concluded that the superior administrative effectiveness of a single-director structure would outweigh any potential benefits of collegial decision-making within CPSC's multimember commission.[156]

CPSC was "the inspiration" for CFPB's creation.[157] When Congress enacted legislation establishing CPSC in 1972, the agency's proponents sought to create a powerful agency with a broad mandate to protect consumers from dangerous products.[158] Consumer groups also supported the creation of a five-member commission for CPSC as a means of promoting wider expertise and political independence.[159] However, CPSC is now "widely regarded as one of the least politically independent and influential agencies in government."[160]

Commentators have identified several reasons for CPSC's lackluster record in protecting consumers, including its lack of a secure funding source.[161] GAO concluded in 1987 that CPSC's

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[155] Barkow, *supra* note 7, at 37-38; *see also* Levitin Testimony, *supra* note 118, at 9.

[156] U.S. GEN. ACCOUNTING OFFICE, GAO/T-HRD-87-14, TESTIMONY: ADMINISTRATIVE STRUCTURE OF THE CONSUMER PRODUCT SAFETY COMMISSION 2-6 (1987) [hereinafter 1987 GAO-CPSC Report] (explaining that some CPSC officials supported the agency's multimember commission structure because it encouraged an "exchange of ideas, and a mix of perspectives . . . including diversity of background, areas of expertise, and political considerations . . ." while others criticized CPSC's commission structure for creating serious administrative problems; based on GAO's review of "[a] number of studies, such as those by the Hoover Commission and the Ash Council . . . over the past 50 years on regulatory commissions," GAO determined that "[a]ll of the studies we reviewed found some significant problems with the commission structure" and some studies "recommended replacing the multimember commissions with agencies headed by single administrators."); *see also* Barkow, *supra* note 7, at 65-72 (describing CPSC's administrative shortcomings).

[157] Barkow, *supra* note 7, at 72.

[158] *Id.* at 65.

[159] *Id.* at 66.

[160] *Id.* at 71 (noting that "[i]n its first five years, CPSC issued only one safety standard . . . and only seven safety standards after ten years").

[161] *Id.* at 67-71 (citing studies documenting CPSC's lack of effectiveness and explaining that "[t]he major reason [for CPSC's ineffectiveness] is that the CPSC has been chronically underfunded and understaffed"); *see also*

multimember commission structure was ineffective and should be scrapped in favor of a single director.[162] GAO found that CPSC's leadership lacked stability and direction due to "high turnover" in the commission's membership, squabbles among commissioners over resources, and delays in decision-making.[163] GAO reported that "[s]even of the eight other health and safety regulatory agencies . . . have single administrators," and the unified leadership structure of those agencies appeared to "enhance the decision-making process."[164] However, Congress did not adopt GAO's recommendation to replace CPSC's multimember commission with a single administrator.[165]

Thus, the factors of efficiency, stability, decisiveness and accountability argue in favor of retaining CFPB's single-Director model of governance. Creating a five-member commission would likely produce more delay and less consistency in CFPB's decision-making. Moreover, a five-member commission would expose CFPB to the risk of leadership deadlock whenever a commissioner left office.[166] This threat of institutional paralysis would be heightened if—as provided in the recently passed House bill—no more than three members of the commission could be affiliated with the same political party.[167] Under that structure, the departure of any member

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infra note 293 and accompanying text (discussing CPSC's vulnerability to political influence due to its reliance on congressional appropriations for funding).

[162] 1987 GAO-CPSC Report, *supra* note 156, at 1.

[163] *Id.* at 2.

[164] *Id.* at 5

[165] *Id.* at 6; *see also* Barkow, *supra* note 7, at 71 & n.319 (explaining the GAO's single administrator recommendation and Congress's decision to not change the CFPC structure).

[166] In contrast, CFPB's Deputy Director (when appointed by the Director) would have authority to "serve as acting Director in the absence or unavailability of the Director." Dodd-Frank § 1011(b)(5).

[167] Ferullo, *supra* note 30 (describing H.R. 1315 as passed by the House of Representatives on July 21, 2011 which would result in "five commissioners . . . with no more than three of them allowed to be members of the same political party."); Carter Dougherty & Phil Mattingly, *Warren Says Proposed Consumer Bureau Changes Would Aid Banks*, BLOOMBERG (Apr. 8, 2011, 6:53 PM) http://www.bloomberg.com/news/2011-04-08/warren-says-proposed-consumer-bureau-changes-would-benefit-banks.html (discussing the proposal by House Republicans "to replace the

of the majority would likely produce a commission that was evenly divided on a wide range of policy issues. During the past three decades, the lengthy vetting process for Presidential nominees and prolonged Senate confirmation battles have frequently resulted in persistent vacancies and policy deadlocks at agencies with multimember commissions.[168]

The financial services industry and House Republican leaders appear to recognize the potential shortcomings of multimember commissions, at least for the financial regulatory agencies they support. The industry and its legislative allies have not attempted to establish multimember commissions to replace the single-administrator governance structures at OCC and FHFA. Indeed, the Republican leadership summarily rejected such a proposal during a recent House subcommittee vote on legislation to change CFPB's structure. Representative Brad Miller (D-NC) introduced an amendment that would have authorized a multimember commission for OCC as well as CFPB, but his amendment was ruled "not germane" and out of order by Representative Shelley Moore Capito (R-WV), the subcommittee's chair.[169] It is not intuitively obvious why Representative Miller's OCC amendment was "not

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CFPB director position created by the Dodd-Frank Act with a five-person commission").

[168] *See* Robert Douglas Brownstone, *The National Labor Relations Board at 50: Politicization Creates Crisis*, 52 BROOK. L. REV. 229, 268-69 & 269 n.188 (1986) (reporting that, during 1983-84, "more than 20 decisions were stalled because they were deadlocked at 2-2 and the [National Labor Relations] Board did not have a fifth member"); Carol Skrzycki, *Top Regulatory Posts Remain Unfilled: Dozens of Federal Jobs Are Vacant as Politics Bog Down Appointment Process*, WASH. POST, Aug. 2, 1997, at A01 (reporting that 46 positions were vacant on "boards and commissions of independent regulatory agencies that require Senate confirmation," resulting in policy deadlocks at some agencies); John M. Broder, *Tie Vote Blocks F.C.C. Inquiry On Liquor Ads*, N.Y. TIMES, July 10, 1997, at A20 (reporting that a vacancy on the Federal Communications Commission ("FCC") produced a 2-2 vote that prevented the FCC from proceeding with an investigation of liquor advertising); *see also FTC Still Split On Microsoft: No Antitrust Ruling Issued, But Firm Says Probe Is Continuing*, SEATTLE POST-INTELLIGENCER, July 22, 1993, at A1 (reporting that recusal of a commissioner produced a 2-2 vote that prevented the FTC from issuing an antitrust complaint against Microsoft).

[169] Kate Davidson, *Subcommittee Approves Bills to Revamp CFPB*, 176 AM. BANKER 70, May 5, 2011, at 3.

germane" if Republicans were truly seeking to establish an important principle of administrative law by changing CFPB's governance structure to a multimember commission.

As noted above, a leading argument in favor of the multimember commission governance structure is that it encourages the agency to consider views from persons with a variety of backgrounds and perspectives.[170] However, Dodd-Frank already requires CFPB's Director to consult with a wide range of outside parties before making major policy decisions. First, the Director must seek advice from CFPB's Consumer Advisory Board, whose members will represent many different perspectives and backgrounds.[171] Second, CFPB must consult with other federal financial regulators before adopting any regulation, and CFPB must address any objections raised by those regulators in its notice of final rulemaking.[172] In particular, CFPB must take into account the "consistency" of each proposed regulation with "prudential, market, or systemic objectives administered by such agencies."[173] Third, CFPB must seek the advice of its small business advisory panel regarding the impact of any proposed regulation on the cost of credit for small businesses,[174] and CFPB must also consider the effects of each proposed rule on consumers (especially those in rural areas) and

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[170] *See supra* note 1556 (describing arguments made by some CPSC officials in favor of a multimember commission).

[171] Dodd-Frank § 1014(a) (requiring CFPB's Director to establish a Consumer Advisory Board that will meet at least twice each year. The purpose of that Board is "to advise and consult with [CFPB] in the exercise of its functions under the Federal consumer financial laws, and to provide information on emerging practices in the consumer financial products or services industry"); Dodd-Frank § 1014(b) (instructing CFPB's Director, in selecting the Board's members, to "seek to assemble experts in consumer protection, financial services, community development, fair lending and civil rights, and consumer financial products or services," as well as representatives of depository institutions that provide services to underserved communities and communities affected by high-cost mortgages).

[172] *See supra* notes 113-12014 and accompanying text (discussing CFPB's obligation to consult with other regulators under Dodd-Frank §§ 1022(b)(2), 1031(e)).

[173] Dodd-Frank § 1022(b)(2)(B).

[174] *See supra* note 109 and accompanying text (discussing CFPB's duty to seek the recommendations of its small business advisory panel under Dodd-Frank § 1100G(b)).

smaller depository institutions.[175] Thus, CFPB's Director is already obliged to consider the views of many interested parties before deciding to adopt a regulation. Superimposing a multimember commission on top of CFPB's existing decision-making process would provide few, if any, benefits, and it would impose potentially significant costs on the bureau and the public.

B. The Financial Stability Oversight Council Should Not Be Given an Enhanced Veto Power over CFPB's Regulations

1. The House Legislation Would Enable Prudential Regulators to Block CFPB's Regulations by Invoking "Safety and Soundness" Concerns Affecting Individual Banks

The Republican-sponsored House bill would greatly strengthen FSOC's ability to veto regulations issued by CFPB.[176] Currently, under Dodd-Frank, any agency represented on FSOC may file a petition to set aside a CFPB regulation, and the Treasury Secretary may stay the rule's effectiveness for up to 90 days to facilitate FSOC's consideration of the petition.[177] Dodd-Frank authorizes FSOC's members, by a two-thirds vote, to strike down a CFPB regulation if they determine that the rule "would put the safety and soundness of the United States banking system or the stability of the financial system of the United States at risk."[178]

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[175] *See supra* notes 11007-1120 and accompanying text (discussing CFPB's obligation to perform a cost-benefit analysis for each proposed rule).

[176] *See supra* notes 30-31 and accompanying text (discussing passage of H.R. 1315 by the House on July 21, 2011).

[177] Dodd-Frank § 1023(b)(1)(A), (c) (requiring an agency, before filing a petition to set aside a regulation issued by CFPB, to attempt "in good faith" to work with CFPB in resolving the agency's concerns about the regulation's impact on the safety and soundness of the U.S. banking system or the stability of the U.S. financial system).

[178] *Id.* at § 1023(a); *see supra* notes 115-1167 and accompanying text (discussing FSOC's authority to veto a CFPB regulation). As discussed above, there are ten voting members and five nonvoting members of FSOC. It is not entirely clear from the text of Section 1023 whether FSOC's nonvoting members can vote on whether to set aside a CFPB regulation.

In contrast, under the House bill, a simple majority of FSOC's members could vote to invalidate a CFPB regulation if they determine that the rule would be inconsistent with the safe and sound operations of U.S. financial institutions.[179] Thus, the House bill would remove Dodd-Frank's requirement that a CFPB regulation must have *systemic* adverse effects (as opposed to a negative impact on *individual* institutions) in order to justify FSOC's veto. The House bill would also (i) bar CFPB's Director from voting on any petition to set aside a CFPB regulation, and (ii) delete Dodd-Frank's requirement that FSOC must act expeditiously on any such petition.[180]

Hence, the House bill would enable federal prudential regulators to veto CFPB's regulations by claiming that the challenged rules would impair the "safety and soundness" of individual financial institutions. The House bill would also permit the Treasury Secretary to approve indefinite suspensions of CFPB rules while FSOC considers veto petitions. As a practical matter, federal prudential regulators would be able to block any CFPB rule if they believed that the rule would have an adverse impact on one or more financial institutions that were subjects of regulatory concern. As shown below, prudential regulators would be likely to exercise their veto power to protect the interests of their largest regulated constituents.

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[179] Bivins, *supra* note 31.

[180] *Id.*; Dodd-Frank § 1023(c)(1)(B), (c)(4)(B) (requiring FSOC to act on an agency's petition to set aside a CFPB rule within 45 days after the petition is filed, or within 90 days of that date if the Treasury Secretary has agreed to stay the rule's effectiveness).

2. Prudential Regulators Failed to Protect Consumers or to Ensure the Safety and Soundness of Financial Institutions during the Credit Boom that Led to the Current Financial Crisis

The House bill is based on the unwarranted assumption that protecting consumers frequently injures the safety and soundness of financial institutions. While individual institutions may complain about particular consumer laws, the current financial crisis has demonstrated that appropriate consumer protection is essential to maintain the long-term safety and soundness of our financial system.[181] As the Senate committee report on Dodd-Frank pointed out, "[t]here was no evidence provided during [the committee's] hearings that consumer protection regulation would put safety and soundness [of banks] at risk. To the contrary, there has been significant evidence and extensive testimony that the opposite was the case."[182]

The Senate committee report also explained that "the failure of the federal banking and other regulators to address significant consumer protection issues" during the subprime lending boom proved to be "detrimental to both consumers and the safety and soundness of the banking system."[183] The history of the financial crisis strongly supports the Senate committee's view. As I have described in previous articles, federal regulators allowed large complex financial institutions ("LCFIs") to become "the primary private-sector catalysts for the destructive credit boom that led to the

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[181] *See* Levitin, *supra* note 10, at 152 ("The events of 2007-2008 have also shown that . . . [c]onsumer protection must be seen as an essential component of systemic-risk protection. The failure to protect consumers has systemic externalities."); Heidi Mandanis Schooner, *Consuming Debt: Structuring the Federal Response to Abuses in Consumer Credit*, 18 LOY. CONSUMER L. REV. 43, 62 (2005) ("[A] bank that is involved in predatory lending practices not only harms consumers by charging undisclosed fees, but also may threaten the bank's financial condition by systematically making overly risky loans.").

[182] S. REP. NO. 111-176, at 166 (2010) (quoting the views of two senior former bank regulators – Kevin Jacques and Brad Sabel – who denied the existence of any conflict between consumer protection and safety and soundness regulation).

[183] S. REP. NO. 111-176, at 9.

subprime financial crisis," and LCFIs became "the epicenter of the current global financial mess."[184]

LCFIs provided most of the funding, directly or indirectly, for "almost 10 million subprime and Alt-A mortgage loans between 2003 and 2007, and by 2008 about $2 trillion of such loans were outstanding."[185] LCFIs securitized most of those nonprime loans, and securitization encouraged a steady decline in lending standards between 2003 and 2006.[186] LCFIs believed—mistakenly—that they could successfully transfer the risks of nonprime loans by bundling the loans into mortgage-backed securities ("MBS") and selling the MBS to far-flung investors. LCFIs had powerful incentives to originate (or buy) and securitize nonprime loans because they earned large fees from securitizing the loans and selling the MBS.[187]

Thus, LCFIs financed a huge surge in nonprime lending that helped to generate a massive boom-and-bust cycle in the U.S. housing market.[188] "Housing prices rose rapidly from 2001 to 2005, stopped rising in 2006, and began to fall sharply in 2007."[189] As I have previously explained, LCFIs played a central role in this disastrous credit cycle:

> [B]y 2007, the health of the U.S. economy relied on a massive confidence game—indeed, some might

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[184] Arthur E. Wilmarth, Jr., *The Dark Side of Universal Banking: Financial Conglomerates and the Origins of the Subprime Financial Crisis*, 41 CONN. L. REV. 963, 1046 (2009) [hereinafter Wilmarth, *The Dark Side of Universal Banking*], *quoted in* Wilmarth, *Too-Big-to-Fail Problem*, *supra* note 57, at 977; *see also* Wilmarth, *supra* note 10, at 897-903, 910-19 (describing regulatory actions that contributed to the failures or government bailouts of several leading LCFIs).

[185] Wilmarth, *supra* note 10, at 897; Wilmarth, *The Dark Side of Universal Banking*, *supra* note 184, at 1011-12, 1015-20, 1022-24 (showing that (i) LCFIs were the primary sources of funding, directly or indirectly, for most nonprime mortgages, (ii) about $3.7 trillion of subprime and Alt-A mortgages were originated between 2001 and 2006, and (iii) more than half of the nonprime loans originated between 2003 and 2007 were used to refinance existing loans).

[186] Wilmarth, *The Dark Side of Universal Banking*, *supra* note 184, at 1020-27; Wilmarth, *Too-Big-to-Fail Problem*, *supra* note 57, at 963-67.

[187] Wilmarth, *The Dark Side of Universal Banking*, *supra* note 184, at 995, 1025-26; Wilmarth, *Too-Big-to-Fail Problem*, *supra* note 57, at 971-72.

[188] Wilmarth, *Too-Big-to-Fail Problem supra* note 57, at 963-66, 970-71.

[189] Wilmarth, *The Dark Side of Universal Banking, supra* note 184, at 1024.

> say, a Ponzi scheme—operated by its leading financial institutions. This confidence game, which sustained the credit boom, could continue only as long as investors were willing to keep buying new debt instruments [underwritten by LCFIs] that would enable overstretched borrowers to expand their consumption and service their debts. In the summer of 2007, when investors lost confidence in the ability of subprime borrowers to meet their obligations, the game collapsed and a severe financial crisis began.[190]

The rapid decline in home prices after 2006 triggered an abrupt shutdown in nonprime lending and cut off refinancing options for many borrowers.[191] Borrowers defaulted on their mortgages in rapidly increasing numbers, which led to widespread foreclosures. Lenders foreclosed on five million homes by the end of 2010, and 4 million additional foreclosures are expected to occur in 2011 and 2012.[192]

Accelerating defaults on home mortgages inflicted major losses on holders of MBS and other mortgage-related investments. Cascading losses on mortgage-related investments triggered a flight by investors from risky assets of all kinds, and that "flight to safety" unleashed a systemic financial crisis.[193] The financial crisis caused

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[190] *Id*. at 1008.

[191] *Id.* at 1019-20, 1024.

[192] Wilmarth, *supra* note 10, at 898; *see also* Nick Timiraos, *Home Forecast Calls for Pain*, WALL. ST. J., Sept. 21, 2011, at A1 (reporting that "[o]ne in five Americans with a mortgage owes more than their home is worth, and $7 trillion of homeowners' equity has been lost in the [housing] bust").

[193] *See, e.g.,* Gary Gorton & Andrew Metrick, *Securitized Banking and the Run on the Repo* 6-21 (Yale ICF, Working Paper No. 09-14, 2009), *available at* http://ssrn.com/abstract=1440752 (providing data confirming that the repo market dried up quickly once losses on MBS became apparent); Arvind Krishnamurthy, *How Debt Markets Have Malfunctioned in the Crisis*, 24 J. OF ECON. PERSPECTIVES 3, 4 (2010) ("[losses on MBS] caused debt markets to break down; indeed, fundamental values and market values seemed to diverge across several markets and products that were far removed from the 'toxic' subprime mortgage assets at the root of the crisis."); Lasse Heje Pedersen, *When Everyone Runs for the Exit*, 5 INT'L. J. ON CENT. BANKING 177, 177-81 (2009) (explaining how investors "ran for the exits" after recognizing the risks inherent in mortgage-related investments).

the failures or near-failures of many LCFIs and inflicted severe distress on the U.S. economy.[194] To prevent the onset of a second Great Depression, the U.S. government spent $800 billion on economic stimulus and provided more than $6 trillion of assistance to financial institutions in the form of central bank loans and other government extensions of credit, guarantees, asset purchases and capital infusions.[195] Notwithstanding these extraordinary measures, the U.S. economy is still struggling to escape a prolonged period of slow growth and high unemployment.[196]

By giving prudential regulators an enhanced veto over CFPB's regulations, the House bill would effectively put responsibility for consumer protection back in the hands of the same agencies that failed to protect both consumers and our financial markets during the past decade.[197] The Senate committee report on Dodd-Frank pointed out "the spectacular failure of the prudential regulators" to protect consumers from predatory nonprime mortgages.[198] As the report explained, regulators failed to crack down on mortgages with "exploding" adjustable rates and other abusive features.[199] Instead, "regulators 'routinely sacrificed consumer protection for short-term profitability of banks' . . . and Wall Street investment firms, despite the fact that so many people were raising the alarm about the problems these loans would cause."[200] Moreover, OCC and OTS preempted state anti-predatory lending laws and state enforcement efforts and thereby "actively

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[194] Wilmarth, *The Dark Side of Universal Banking, supra* note 184, at 1027-35, 1044-46; Wilmarth, *Too-Big-to-Fail Problem*, *supra* note 57, at 957-61, 977-81.

[195] Wilmarth, *Too-Big-to-Fail Problem*, *supra* note 57, at 957-59.

[196] *Id.* at 959-61; Kevin J. Lansing, *Gauging the Impact of the Great Recession*, FRBSF ECON. LETTER 2011-21 (July 11, 2011), *available at* http://www.frbsf.org/publications/economics/letter/2011/el2011-21.html; Neil Irwin, *Flat job figures stoke fears of stalled recovery*, WASH. POST, Sept. 3, 2011, at A1 (reporting that the U.S. economy was continuing to grow slowly and was hindered by high unemployment).

[197] *See* Bivins, *supra* note 31 ("It makes no sense to give the same banking regulators who were asleep at the wheel before the last financial crisis more power to second guess the CFPB.") (quoting Pamela Banks, senior policy counsel for Consumers Union); Davidson & Adler, *supra* note 30 (quoting a similar comment by Rep. Barney Frank).

[198] S. REP. NO. 111-176, at 15 (2010).

[199] *Id.*

[200] *Id.* (quoting testimony of Patricia McCoy on Mar. 3, 2009).

created an environment where abusive mortgage lending could flourish without state controls."[201]

Numerous studies have confirmed the Senate committee report's findings concerning the shortcomings of federal prudential regulators.[202] For example, FRB had authority under a 1994 federal statute to adopt rules to prohibit unfair or deceptive lending practices by all types of mortgage lenders.[203] However, notwithstanding proposals for action by FRB staff members and many others, FRB failed to promulgate effective regulations until 2008, a year after the subprime mortgage market collapsed.[204] Similarly, FRB declined to exercise its authority to regulate high-risk mortgage lending by nonbank subsidiaries of bank holding companies until 2007, again despite calls for action by FRB staff members and others.[205]

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[201] *Id.* at 16-17.

[202] *See, e.g.*, ENGEL & MCCOY, *supra* note 10, at 157-205 (describing regulatory failures by FRB, OCC and OTS); JOHNSON & KWAK, *supra* note 10, at 120-32, 141-44 (discussing the shortcomings of federal prudential regulators); Bar-Gill & Warren, *supra* note 10, at 81-95 (same); Levitin, *supra* note 10, at 151-69 (explaining the "failure of the current consumer-protection regime in financial services," *id.* at 151); Wilmarth, *supra* note 10, at 897-919 ("Regulatory inaction and preemption by federal banking agencies played a significant role in allowing abusive nonprime lending to grow and spread during the past decade," *id.* at 897).

[203] *See* Wilmarth, *supra* note 10, at 898-99 (discussing FRB's authority to prohibit unfair or deceptive mortgage lending practices under the Home Ownership and Equity Protection Act).

[204] *Id.* at 899-900; *see also* ENGEL & MCCOY, *supra* note 10, at 195-96 ("When HOEPA passed, Congress instructed the Fed to implement the [prohibition against unfair and deceptive acts and practices in mortgage lending], but Alan Greenspan was dead set against obeying that Congressional mandate so long as he was chairman."); JOHNSON & KWAK, *supra* note 10, at 141-42 (describing the FRB's failure to enforce HOEPA because of Greenspan's opposition); Sudeep Reddy, "Currents: Fed Faces Grilling on Consumer-Protection Lapses," WALL ST. J., Dec. 2, 2009, at A22 (same).

[205] Wilmarth, *supra* note 10, at 900-01; *see also* ENGEL & MCCOY, *supra* note 10, at 198-203 (describing the FRB's failure to regulate mortgage lending by nonbank subsidiaries of bank holding companies, due to Alan Greenspan's belief that such regulation would be counterproductive; JOHNSON & KWAK, *supra* note 10, at 142-43 (same); Binyamin Appelbaum, *As Subprime Crisis Unfolded, Watchdog Fed Didn't Bother Barking*, WASH. POST, Sept. 27, 2009, at A1 (same).

When indisputable evidence of the risks of subprime and Alt-A loans emerged in 2005, FRB, FDIC, OCC and OTS responded not with binding rules, but instead with weak "guidance" that urged banks to follow prudent lending policies. The agencies' guidance encouraged—but did not require—banks to verify each borrower's ability to pay the fully-amortized rate on adjustable-rate mortgages. Federal regulators did not take meaningful steps to ensure compliance with their guidance until after the subprime crisis broke out.[206]

In the absence of effective federal regulation, more than thirty states passed laws to restrain predatory lending practices. However, OCC and OTS quickly issued a series of preemptive rulings that blocked the states from applying those laws to national banks, federal thrifts and their subsidiaries.[207] In combination, federal regulatory inaction and federal preemption helped LCFIs that controlled national banks and federal thrifts to capture the lion's share of the subprime and Alt-A mortgage lending markets during the peak of the housing boom between 2005 and 2007.[208] Several of

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[206] Wilmarth, *supra* note 10, at 901-03, 907-08; *see also* ENGEL & MCCOY, *supra* note 10, at 165-66, 168, 174, 176 (discussing the reliance of federal regulators on weak, nonbinding guidance even after they became aware of significant and growing problems with risky nonprime lending); JOHNSON & KWAK, *supra* note 10, at 143 (same).

[207] Wilmarth, *supra* note 10, at 909-15; *see also* ENGEL & MCCOY, *supra* note 10, at 157-62 (describing the adverse effects of OCC and OTS rules that preempted state consumer protection laws); JOHNSON & KWAK, *supra* note 10, at 143-44 (same); Robert Berner & Brian Grow, *They Warned Us: The Watchdogs Who Saw the Subprime Crisis Coming – and How They Were Thwarted by the Banks and Washington*, BUS. WK., Oct. 20, 2008, at 36 (same).

[208] Wilmarth, *supra* note 10, at 916-19; *see also* ENGEL & MCCOY, *supra* note 10, at 169-71, 176-81, 198-206 (explaining how OCC and OTS preemption helped large national banks and federal thrifts to become leading nonprime lenders); JOHNSON & KWAK, *supra* note 10, at 120-44 (same). Twelve of the fifteen largest subprime lenders in 2006 were subject to regulation by federal banking agencies, and those twelve lenders "controlled 50 percent of the subprime market." ENGEL & MCCOY, *supra* note 10, at 204; *see also id.* at 205 tbl. 10.1 (showing that OTS had jurisdiction over five of the top 15 subprime lenders in 2006, while FDIC had authority over one, FRB over three, and OCC over three).

those federally-supervised LCFIs subsequently failed or required federal assistance to avoid failure.[209]

3. Four Factors Contributed to the Regulatory Failures That Occurred during the Subprime Lending Boom

Why didn't federal regulators stop financial institutions from generating huge volumes of high-risk credit that exploited consumers, risked their own soundness and undermined the stability of the financial markets? At least four factors contributed to this systemic failure of regulation. First, during the credit boom banking agencies focused on near-term profitability as a key indicator of the "safety and soundness" of financial institutions. Federal regulators therefore resisted proposals by consumer groups for tougher federal lending rules, and OCC and OTS preempted state anti-predatory lending laws that threatened to reduce bank profits from originating and securitizing nonprime loans.[210] Banking agencies also declined to take tough enforcement actions to stop speculative lending and capital markets activities as long as banks continued to report large profits, despite misgivings among some regulators about the potential long-term risks of those activities.[211]

Second, regulators competed—both within and across national borders—to attract the allegiance of major financial institutions. Regulatory competition encouraged agencies to follow polices that would please their existing regulated constituents and attract new ones. For example, OCC and OTS issued their

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[209] Wilmarth, *supra* note 10, at 918-19 (citing failures of Washington Mutual and IndyMac, massive federal bailouts of American International Group (AIG) and Citigroup, and federally-assisted emergency acquisitions involving Countrywide, Merrill Lynch, Wachovia and National City); *see also* ENGEL & MCCOY, *supra* note 10, at 169-71, 176-81, 200-03, 221-23 (discussing the same transactions).

[210] ENGEL & MCCOY, *supra* note 10, at 173-76; Bar-Gill & Warren, *supra* note 10, at 90-95; Levitin, *supra* note 10, at 152-57; U.S. Senate, Permanent Subcommittee on Investigations, *Wall Street and the Financial Collapse: Majority and Minority Staff Report* (April 13, 2011) [hereinafter *Senate Wall Street Report*], at 4-5, 224-26.

[211] Frederick Tung & M. Todd Henderson, *Pay for Regulator Performance*, at 25 (Univ. of Chicago Law & Econ. Olin Working Paper No. 574, 2011), *available at* http://hq.ssrn.com/abstract=1916310; Wilmarth, *supra* note 10, at 907 n.100; *Senate Wall Street Report*, *supra* note 210, at 224-26.

preemptive rulings to help persuade state-chartered institutions that they should operate under federal charters as national banks or federal thrifts.[212] OCC and OTS had strong financial incentives to induce depository institutions to operate as national banks or federal thrifts, because assessments paid by those institutions funded virtually all of OCC's and OTS' budgets.[213]

In addition, federal regulators competed amongst themselves to enlarge their stables of regulatory clients. For example, FRB and OCC each sought to attract the patronage of major banks by approving new activities and reducing regulatory requirements.[214] Similarly, OTS persuaded Countrywide to convert from a national bank to a federal thrift in early 2007 by promising that OTS would give Countrywide more favorable supervisory treatment.[215] Thus, efforts by federal agencies to attract the allegiance of large institutions resulted in domestic regulatory arbitrage and lax regulation.[216]

OTS compiled the most egregious record of regulatory laxity, and Congress decided to abolish OTS when it passed Dodd-Frank.[217] For example, OTS granted extraordinary forbearance to

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[212] ENGEL & MCCOY, *supra* note 10, at 157-62; JOHNSON & KWAK, *supra* note 10, at 143-44; Levitin, *supra* note 10, at 163-69; Wilmarth, *supra* note 10, at 910-17.

[213] ENGEL & MCCOY, *supra* note 10, at 159-61; Bar-Gill & Warren, *supra* note 10, at 90-94; Wilmarth, *supra* note 10, at 915-16.

[214] Wilmarth, *supra* note 52, at 265, 265 n.150, 275-77, 277 n.203; *see also supra* notes 128-138 and accompanying text (explaining that OCC has consistently supported the interests of national banks); CARNELL, MACEY & MILLER, *supra* note 84, at 61-67, 466-67, 491-94 (describing competition between OCC and FRB during the 1990s to maintain the loyalty of the largest banks, which could choose between status as national banks or as state Fed member banks); Richard M. Whiting, *The New 'Tri-Partite' Banking System*, 17 BANKING POL'Y REP. (Aspen) No. 7, at 1, 14-15 (April 6, 1998) (observing that "overt rivalry" between OCC and FRB produced "expansive regulatory actions" by both agencies).

[215] ENGEL & MCCOY, *supra* note 10, at 159-60; Levitin, *supra* note 10, at 159-60.

[216] ENGEL & MCCOY, *supra* note 10, at 159-66; Levitin, *supra* note 10, at 155-60.

[217] S. REP. NO. 111-176, at 25-26 (2010); *see also* ENGEL & MCCOY, *supra* note 10, at 174-84 (describing OTS' regulatory failures); Binyamin Appelbaum & Ellen Nakashima, *Banking Regulator Played Advocate Over Enforcer: Agency Let Lenders Grow Out of Control, Then Fail*, WASH. POST, Nov. 23, 2008, at A1 (same).

Washington Mutual ("WaMu"), the biggest federal thrift with $300 billion of assets. WaMu's assessments accounted for about one-seventh of OTS' total revenues, and OTS Director John Reich referred to WaMu in 2007 as "my largest constituent."[218] OTS examiners uncovered "more than 500 serious operational deficiencies" in WaMu's lending and risk management practices between 2004 and 2008.[219] However, OTS continued to rate WaMu as "fundamentally sound" until February 2008, and failed to take any public enforcement action against WaMu prior to its failure in September 2008.[220] A Senate investigation concluded that OTS' forbearance toward WaMu "reflected an OTS culture of deference to bank management, demoralized examiners whose oversight efforts were unsupported by their supervisors, and a narrow regulatory focus that allowed short-term profits to excuse high risk activities and disregarded systemic risk."[221]

Cross-border competition with foreign regulators also encouraged federal banking agencies to bend to the wishes of major banks. Regulators worried that any decision to impose stricter supervision on large U.S. financial institutions would cause those institutions to shift more of their operations to London and other foreign locations that offered "light touch" regulation.[222] Federal

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[218] *Senate Wall Street Report*, *supra* note 210, at 165, 210.
[219] *Id.* at 209.
[220] *Id.* at 161-62, 177, 209-30. In addition, from 2006 to 2008, OTS limited FDIC's ability to examine WaMu and obstructed FDIC's efforts to take more vigorous supervisory measures against WaMu. *Id.* at 196-208.
[221] *Id.* at 209. Federal investigators and commentators strongly criticized OTS for similar regulatory lapses that contributed to the failures of other leading thrifts, including IndyMac and Downey Federal. *Id.* at 233-35; ENGEL & MCCOY, *supra* note 10, at 176-81; Appelbaum & Nakashima, *supra* note 217.
[222] Dariusz Wójcik, *The dark side of NY-LON: Financial centres and the global financial crisis* 7 (Oxford University Sch. of Geography and the Environment Working Papers in Employment, Work and Finance No. 11-12, 2011), *available at* http://ssrn.com/abstract=1890644. For example, AIG Financial Products, which sold massive volumes of credit default swaps that destroyed its parent insurance company, conducted most of its operations in London. *Id.*; ENGEL & MCCOY, *supra* note 10, at 221-23. For discussions of international regulatory arbitrage and its impact on supervisory policies, see VIRAL V. ACHARYA, PAUL WACHTEL & INGO WALTER, *International Alignment of Financial Sector Regulation, in* RESTORING FINANCIAL STABILITY: HOW TO REPAIR A FAILED SYSTEM 365, 366-71 (Viral A.

agencies therefore repeatedly offered regulatory accommodations in an effort to persuade LCFIs to keep more of their assets in the U.S.[223] Thus, international as well as domestic regulatory competition discouraged federal regulators from adopting tougher policies that might have restrained speculative activities during the period leading up to the financial crisis.

Third, during the past three decades, financial regulators and Wall Street officials developed a "confluence of perspectives and opinions" in which "Wall Street's positions became the conventional wisdom in Washington."[224] Regulators maintained continuous contacts with LCFIs through (i) frequent consultations with bank

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Acharya & Matthew Richardson, eds., 2009); HEIDI MANDANIS SCHOONER & MICHAEL W. TAYLOR, GLOBAL BANK REGULATION: PRINCIPLES AND POLICIES 283-84, 292-93 (2010); John C. Coffee & Hillary A. Sale, *Redesigning the SEC: Does the Treasury Have a Better Idea?*, 95 VA. L. REV. 707, 716-17, 721 (2009); Cristie L. Ford, *Macro and Micro Level Effects on Responsive Financial Regulation*, 44 U. BRIT. COLUM. L. REV. (2011) (forthcoming), *available at* http://ssrn.com/abstract=1773098, at 17-18.

[223] Wójcik, *supra* note 222, at 7; Ford, *supra* note 222, at 17-18. During the quarter century leading up to the financial crisis, U.S. banking regulators sought to avoid imposing capital requirements on large U.S. banks that would place them at a competitive disadvantage compared to foreign banks. DANIEL K. TARULLO, BANKING ON BASEL: THE FUTURE OF INTERNATIONAL FINANCIAL REGULATION 45-64, 84-85, 210-14 (2008). For example, in 2004 federal regulators adopted an interagency rule setting a very low capital charge for banks that provided backup lines of credit to their sponsored off-balance-sheet conduits. Wilmarth, *supra* note 10, at 974. In agreeing to that very lenient treatment, regulators noted that a proposed higher capital charge "would put U.S. banks at a competitive disadvantage relative to foreign banks." Risk-Based Capital Guidelines, 44 Fed. Reg. 44908, 44910 (July 28, 2004). U.S. banking agencies were not mistaken in fearing that LCFIs would shift operations and assets to jurisdictions with more accommodating regulatory schemes. A recent study found that, between 1996 and 2007, global banks headquartered in 26 developed countries were significantly more likely to transfer capital to other nations, and to open branches and subsidiaries in those nations, if the destination countries adopted fewer activity restrictions, lower capital requirements, weaker disclosure rules, looser auditing standards and more lenient supervisory policies. Joel F. Houston , Chen Lin & Yue Ma, *Regulatory Arbitrage and International Bank Flows* (Aug. 26, 2011), at 2-5, 17-19, 24-29, *available at* http://ssrn.com/abstract=1525895.

[224] JOHNSON & KWAK, *supra* note 10, at 92-97.

representatives on important regulatory initiatives, and (ii) "dedicated examiner teams" that maintained permanent on-site offices at the largest banks and worked closely with bank managers.[225] Regulators and industry insiders also shared close "social, educational, or experiential ties."[226] In contrast, regulators largely dismissed the views of consumer advocates and other outsiders, who lacked access to confidential supervisory information and frequently did not have specialized expertise related to derivatives and other financial innovations.[227]

The "'revolving door' phenomenon" produced even closer relationships between regulators and industry leaders.[228] LCFIs regularly hired "former agency employees familiar with the inner workings of the regulatory process."[229] Conversely, "as the world of finance became more complicated and more central to the economy," the federal government increasingly relied on Wall Street veterans to

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[225] Saule T. Omarova, *Bankers, Bureaucrats, and Guardians: Toward Tripartism in Financial Services Regulation* (Aug. 14, 2011), at 13, 13 n.49, *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1924546; *see also* Levitin, *supra* note 10, at 159 (describing the presence of permanent teams of examiners at LCFIs).

[226] Ford, *supra* note 222, at 23.

[227] Omarova, *supra* note 225, at 13, 32-33 (describing the "secretive, closed-door nature of the decision-making process involving financial regulators and industry actors"); *see also* Ford, *supra* note 222, at 23 ("Regulators operate within a relatively narrow, insulated, and expertise-based band of human experience, characterized by relationships with sophisticated repeat players. . . . [Regulators] may be cognitively predisposed against 'outsiders' who either lack facility with the dominant jargon or who take issue with assumptions that no one in the industry take[s] issue with"); JOHNSON & KWAK, *supra* note 10, at 94 ("Financial policy took on the trappings of a branch of engineering, in which only those with hands-on experience on the cutting edge of innovation were qualified to comment"); Appelbaum, *supra* note 205 (reporting that FRB officials repeatedly dismissed warnings by consumer advocates about the dangers posed by nonprime mortgage lending).

[228] Omarova, *supra* note 225, at 13; *see* JOHNSON & KWAK, *supra* note 10, at 93-97 ("[M]any senior officials moved back and forth between Wall Street and Washington.").

[229] Omarova, *supra* note 225, at 13; *see* JOHNSON & KWAK, *supra* note 10, at 94-96 (explaining that financial industry officials and regulators developed closer connections as experienced government officials increasingly opted to leave government service and enter the private sector).

fill senior regulatory positions.[230] The continuous movement of senior officials between Wall Street and Washington encouraged regulators "to view their institutional interests or mission as largely congruent with the interests of their regulated industry constituency."[231]

Consequently, the aggressive deregulatory policies pursued by Alan Greenspan during his tenure as FRB chairman between 1987 and 2006 were not an aberration. Rather, Greenspan's policies reflected a widely-shared regulatory "mindset," which included great faith in the ability of financial markets to "self-correct" and great skepticism about the federal government's ability to regulate wisely or effectively.[232] Officials who disagreed with that mindset "were marginalized as people who simply did not understand the bright new world of modern finance."[233]

Fourth, regulators were well aware of the enormous political clout wielded by large financial institutions and their allies. The financial sector (including finance, insurance and real estate firms) spent $5.1 billion on lobbying and campaign contributions between

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[230] JOHNSON & KWAK, *supra* note 10, at 92-95.

[231] Omarova, *supra* note 225, at 13; *see* JOHNSON & KWAK, *supra* note 10, at 93, 95 ("[A]s banking insiders gained power and influence in Washington, the positions they held . . . became orthodoxy inside the Beltway. . . [G]roupthink was a major reason why the federal government deferred to the interests of Wall Street repeatedly in the 1990s and 2000s.").

[232] Wilmarth, *supra* note 10, at 898-906; *see* ENGEL & MCCOY, *supra* note 10, at 167-96 (explaining that regulators adopted a "mindset" in the 1990s and 2000s that favored deregulation and placed great faith in the effectiveness of market discipline); JOHNSON & KWAK, *supra* note 10, at 97-109, 133-43 (same).

[233] JOHNSON & KWAK, *supra* note 10, at 97; *see id.* at 103 (describing how International Monetary Fund ("IMF") chief economist Raghuram Rajan "was met with a torrent of attacks by Greenspan's defenders," including FRB vice chairman Donald Kohn and Treasury Secretary Lawrence Summers, when "Rajan presented a paper [in August 2005] asking in prophetic tones about whether deregulation and innovation had increased rather than decreased risk in the financial system"); *id.* at 7–9, 135–37 (explaining that (i) CFTC chairman Brooksley Born "provoked furious opposition" when the CFTC issued a concept paper in May 1998, proposing a study of whether to strengthen the regulation of over-the-counter derivatives; and (ii) Ms. Born's opponents—including Greenspan, Summers, Treasury Secretary Robert Rubin and SEC chairman Arthur Levitt—persuaded Congress to pass legislation barring the CFTC from acting on its proposal).

1998 and 2008.[234] The financial sector was the "leading contributor to political campaigns" after 1990,[235] and it accounted for 15% of total lobbying expenditures by *all* industry sectors between 1999 and 2006.[236]

The financial sector employed nearly 3,000 registered lobbyists in 2007.[237] In 2008 and 2009, the six largest banks (Bank of America, JP Morgan Chase, Citigroup, Wells Fargo, Goldman Sachs and Morgan Stanley) employed more than 240 lobbyists who previously worked in the Executive Branch or Congress.[238] Financial firms that were heavily involved in political lobbying also engaged in more risky activities. An IMF staff study determined that financial firms that engaged in the most intensive lobbying between 1999 and 2006 also made higher-risk mortgage loans, securitized more of their loans, and suffered above-average losses in their stock market values during the financial crisis.[239]

The financial sector received excellent legislative returns on its huge political investments. A second IMF staff study found that lobbying expenditures by financial firms significantly increased the likelihood of passage for bills favored by the financial services industry and also increased the probability of defeat for bills opposed by the industry.[240] Lobbying by the financial sector helped to produce

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[234] Essential Info. & Consumer Educ. Found., *Sold Out: How Wall Street and Washington Betrayed America* 6, 15-16, 99-101 (Mar. 2009) [hereinafter *Sold Out*], *available at* http://www.wallstreetwatch.org/reports/sold_out.pdf.

[235] JOHNSON & KWAK, *supra* note 10, at 90; *see* Levitin, *supra* note 10, at 160-61 ("The financial-services industry has been the single largest contributor to congressional campaigns since 1990.").

[236] Deniz Igan, Prachi Mishra & Thierry Tressel, *A Fistful of Dollars: Lobbying and the Financial Crisis* 18, 32 (tbl.1a) (IMF Working Paper WP/09/87, Dec. 2009), *available at* http://ssrn.com/abstract=1531520.

[237] *Sold Out*, *supra* note 234, at 15-16, 100-01.

[238] Kevin Connor, *Big Bank Takeover: How Too-Big-to-Fail's Army of Lobbyists Has Captured Washington* (Institute for America's Future, May 2010), *available at* http://www.ourfuture.org/files/documents/big-bank-takeover-final.pdf.

[239] Igan, Mishra & Tressel, *supra* note 236, at 4-6, 19-20, 22, 24-27.

[240] Deniz Igan & Prachi Mishra, *Three's Company: Wall Street, Capitol Hill, and K Street* 4, 15-18 (IMF Working Paper, June 2011), *available at* http://ssrn.com/abstract=1915164. In addition, the lobbying efforts of financial firms enjoyed greater success whenever (i) a member of Congress

a series of landmark political victories between 1994 and 2005, including enactment of (i) interstate banking legislation in 1994,[241] (ii) the Gramm-Leach-Bliley Act ("GLBA") in 1999,[242] (iii) the Commodity Futures Modernization Act ("CFMA") in 2000,[243] and (iv) bankruptcy reform legislation in 2005.[244] In addition to those affirmative victories, the financial services industry successfully blocked passage of more than a dozen bills introduced between 2000 and 2007 that would have imposed tighter restrictions on high-risk mortgage lending.[245]

Federal financial regulators who recommended tougher restraints on financial institutions experienced strong "pushback" from the industry.[246] Regulators' career interests and incentives

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formerly worked in the financial industry or (ii) a financial firm hired a lobbyist who had previously worked for a legislator. *Id.*

[241] *See* Wilmarth, *The Dark Side of Universal Banking*, *supra* note 184 at 1012-13 (describing the significance of Congress' passage of interstate banking legislation, which "made possible the establishment of large nationwide banking organizations"); JOHNSON & KWAK, *supra* note 10, at 89.

[242] For discussions of the importance of GLBA, which repealed key provisions of the Glass-Steagall Act and allowed commercial banks to affiliate with securities firms and insurance companies by forming financial holding companies, see JOHNSON & KWAK, *supra* note 10, at 89, 91-92, 133-34; Wilmarth, *The Dark Side of Universal Banking supra* note 184, at 973-75.

[243] *See* JOHNSON & KWAK, *supra* note 10, at 8-9, 92, 134-37 (describing CFMA, which largely exempted over-the-counter derivatives from federal regulation).

[244] The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") "radically altered the policies underlying consumer bankruptcy . . . , marking a significant shift in favor of creditors," because BAPCA made it much more difficult for consumers to obtain a substantial or complete discharge of their debts in bankruptcy. Ronald J. Mann, *Bankruptcy Reform and the "Sweat Box" of Credit Card Debt*, 2007 U. ILL. L. REV. 375, 376-77; *see* Eugene R. Wedoff, *Major Consumer Bankruptcy Effects of BAPCPA*, 2007 U. ILL. L. REV. 31 (surveying the changes made by BAPCPA to consumer bankruptcy statutes).

[245] Igan, Mishra & Tressel, *supra* note 236, at 17-18, 55-59 (Appendix).

[246] Wilmarth, *supra* note 10, at 907-08; *The Financial Crisis Inquiry Report: Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States* (Jan. 2011) [hereinafter FCIC Report], at 20-22, 172-73, 307; *see also* JOHNSON & KWAK, *supra* note 10, at 7-9, 97, 134-37 (describing how the financial industry successfully

discouraged them from challenging the formidable political power wielded by LCFIs and their allies.[247] Deregulation and forbearance were safer alternatives for regulators, especially during a period of apparently unprecedented prosperity for the financial sector.[248]

4. CFPB Is Likely To Be More Resistant to Regulatory Capture than the Federal Banking Agencies

In view of the financial services industry's success in securing extensive forbearance from federal bank regulators during the past two decades, why should we expect CFPB to be more resistant to industry pressure? There are at least two major reasons for optimism. First, CFPB's unified mission makes it different from most federal banking agencies. As described above, prudential regulators typically gave short shrift to consumer protection and instead focused on increasing the banking industry's "safety and soundness" by adopting policies that promoted higher short-term profits for banks.[249] In contrast, CFPB has a single clear mandate to protect consumers from unfair, deceptive, abusive or discriminatory practices.[250] While Dodd-Frank requires CFPB to consider the potential costs and benefits of its proposed rules, and to respond to safety-and-soundness concerns raised by prudential regulators,

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resisted tougher regulation); Tung & Henderson, *supra* note 211, at 29-30 (explaining that when regulators issued mild warnings about risky lending in 2006, "[t]housands of industry comments poured in objecting to the regulators' intrusion, and the FDIC and other agencies backed off, clarifying that they didn't intend to impose limits"); *Sold Out*, *supra* note 234, at 8, 42-49 (observing that "officials in government who dared to propose stronger protections for investors and consumers consistently met with hostility and defeat").

[247] Tung & Henderson, *supra* note 211, at 28-30.

[248] JOHNSON & KWAK, *supra* note 10, at 7-9, 97, 103-09, 134-43, 151-52; FCIC Report, *supra* note 246, at 173, 307.

[249] *See supra* notes 197-20911 and accompanying text; Bar-Gill & Warren, *supra* note 10, at 90-91 ("These agencies are designed with a primary mission to protect the safety and soundness of the banking system. This means protecting banks' profitability. Consumer protection is, at best, a lesser priority . . . ."); Levitin*, supra* note 10, at 155-56 (explaining that "[r]egulators have permitted profitability-protection to trump consumer protection for all but the most egregious behavior").

[250] Dodd-Frank § 1021(b); S. REP. NO. 111-176, at 11, 164 (2010).

CFPB's consumer protection mission remains paramount. The unambiguous primacy of that mission should motivate CFPB to take its statutory responsibilities seriously.[251]

Second, CFPB's institutional safeguards—including its policymaking autonomy and its assured source of funding[252]—make it substantially more insulated from industry capture compared to OCC, CFTC, SEC and FRB. As shown above, OCC relies for most of its funding on assessments paid by national banks, and OCC could lose significant funding if major national banks converted to state-chartered banks. OCC therefore has powerful budgetary incentives to please its largest regulatory constituents.[253] As discussed in the next section, CFTC and SEC rely on congressional appropriations and are therefore highly vulnerable to budgetary leverage exerted by congressional allies of their regulated constituents.

FRB is not subject to the same type of industry-related budgetary pressures. FRB and the Federal Reserve System ("Fed") as a whole finance their operations by drawing on earnings from the Fed's investment portfolio of Treasury securities and other debt instruments.[254] However, the Fed is subject to significant industry influence due to the unique governance structure for the twelve regional Federal Reserve Banks ("Reserve Banks").[255] Member banks in each Fed district elect three Class A directors and three Class B directors for that district's Reserve Bank, while FRB appoints three Class C directors. In each district, Class B directors and Class C directors vote jointly to select the Reserve Bank's

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[251] Bar-Gill & Warren, *supra* note 10, at 98-100. By maintaining CFPB's single-Director governance structure, Congress would enhance CFPB's accountability to the public for carrying out its consumer protection mission. *See* Levitin Testimony, *supra* note 118, at 11 ("A CFPB Director who . . . fails to do enough to protect consumers cannot deflect blame for his actions.").

[252] *See supra* notes 77-81 and accompanying text (discussing CFPB's autonomy and its guaranteed source of funding from the Fed).

[253] *See supra* notes 128-140, 212-16 and accompanying text.

[254] CARNELL, MACEY & MILLER, *supra* note 84, at 62.

[255] Renee B. Adams, "*Who Directs the Fed?*" 3-5, 10-14 (European Corporate Governance Inst., Working Paper No. 293, 2011), *available at* http://ssrn.com/abstract=1756509 (discussing the structure and responsibilities of the Reserve Banks); U.S. GOV'T ACCOUNTABILITY OFFICE, FED. RES. BANK GOVERNANCE: OPPORTUNITIES EXIST TO BROADEN DIRECTOR RECRUITMENT EFFORTS AND INCREASE TRANSPARENCY , GAO-12-18 , 6-7, 9-16, 41 (2011) [hereinafter GAO Fed Governance Report].

president. Thus, member banks elect two-thirds of the directors of each Reserve Bank, and member banks indirectly exercise (through Class B directors) shared control over the selection of Reserve Bank presidents.[256]

The voting members of the Federal Open Market Committee ("FOMC"), which determines the nation's monetary policy, include FRB's seven governors and five Reserve Bank presidents. The president of the Federal Reserve Bank of New York ("New York Fed") is a permanent FOMC voting member, while four FOMC voting seats rotate among the remaining eleven Reserve Bank presidents. All twelve Reserve Bank presidents are entitled to attend and participate in FOMC meetings.[257] In addition, each Reserve Bank is responsible (under FRB's oversight) for examining and supervising state member banks and bank holding companies headquartered in the Reserve Bank's district.[258] Thus, Reserve Bank presidents play significant roles in the Fed's monetary policy decisions and bank supervisory policies.

At first glance, the Federal Reserve Act appears to call for a diversity of backgrounds among directors of Reserve Banks. Class A directors usually are senior bank executives, but Class B and Class C directors are not allowed to serve as directors, officers or employees of banks, and Class C directors may not own bank stocks.[259] In

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[256] GAO Fed Governance Report, *supra* note 255, at 10-13. Prior to the enactment of Dodd-Frank, Class A directors also voted to elect Reserve Bank presidents, and member banks therefore controlled the selection of presidents through their ability to elect Class A and Class B directors. Dodd-Frank removed the right of Class A directors to vote for Reserve Bank presidents, so that the power to select presidents is now divided equally between Class B directors (elected by member banks) and Class C directors (appointed by FRB). *Id.* at 10, 53; H.R. REP. NO. 111-517, at 876 (2010) (Conf. Rep.), *reprinted in* 2010 U.S.C.C.A.N. 722, 732.

[257] GAO Fed Governance Report, *supra* note 255, at 6-9, 14-16.

[258] *Id.* at 7.

[259] 12 U.S.C. §§ 302, 303, 304 (1977); *see* GAO Fed Governance Report, *supra* note 255, at 10-12 (describing the requirements for Class A, B, and C directors). FRB designates one Class C director as the chairman of the board for each Reserve Bank. Strangely, however, while the Federal Reserve Act prohibits Class C directors from owning bank stocks, the Act requires the chairman to have "tested banking experience." 12 U.S.C. §§ 303, 305 (1977); *see* GAO Fed Governance Report, *supra* note 255, at 10-12 (explaining that the Class C director serving as board chairman must have "tested banking experience").

addition, the Federal Reserve Act provides that Class B and Class C directors should "represent the public . . . with due but not exclusive consideration to the interests of agriculture, commerce, industry, services, labor and consumers."[260]

Notwithstanding the Federal Reserve Act's apparent preference for diversity, the boards of directors of Reserve Banks have typically been dominated by senior executives of major banks, large financial firms and leading nonfinancial corporations that are customers of the biggest banks. A recent study found that "class A [Reserve Bank] directorships are dominated by large banks."[261] The study determined that bank size was the most significant factor in determining whether a particular bank was represented by a Class A director between 1987 and 2009, while factors related to bank performance were much less important.[262] For example, Jamie Dimon, chairman of JP Morgan Chase—the nation's largest bank—serves as a Class A director of the New York Fed.[263]

Similarly, despite their statutorily prescribed role as representatives of the public, Class B and Class C directors have frequently been drawn from the ranks of senior executives of large nonbank financial companies and big nonfinancial corporations that are clients of major banks. For example, Richard Fuld, chairman of Lehman Brothers, served as a Class B director of the New York Fed until shortly before his firm declared bankruptcy in September 2008.[264] During 2008 and 2009, the New York Fed's board of directors also included Jeffrey Immelt, chairman of General Electric (a Class B director), and Stephen Friedman, a director and former

[260] 12 U.S.C. § 302 (1977).
[261] Adams, *supra* note 255, at 21-25.
[262] *Id.*
[263] *See* Jamie Dimon's biography, N.Y. FED, http://www.newyorkfed.org/aboutthefed/orgchart/board/dimon.html (last visited Apr. 17, 2012) (describing Jamie Dimon's experience); Alan Kline, *JP Morgan Chase Overtakes B of A as Largest U.S. Bank*, AM. BANKER, Oct. 19, 2011 (reporting that JP Morgan Chase had become the biggest U.S. bank and had $2.29 trillion of assets as of Sept. 30, 2011, compared to $2.22 trillion of assets for Bank of America).
[264] GAO Fed Governance Report, *supra* note 255, at 35-36; Neil Irwin, *N.Y. Fed Chairman Resigns: Friedman's Role as Goldman Sachs Director Questioned*, WASH. POST, May 8, 2009.

chairman of Goldman Sachs (a Class C director), whom FRB designated as chairman of the board of the New York Fed.[265]

A recent GAO study on Fed governance determined that seventy-three of the Reserve Bank's head office directors serving from 2006 to 2010 were drawn from the banking industry, while only eleven head office directors during that period were representatives of consumers or labor.[266] In addition, Class B and Class C directors of Reserve Banks have included senior executives of major nonfinancial corporations that are customers of the largest banks.[267] Thus, members of Reserve Bank boards of directors have predominantly reflected the views and interests of major banks and their clients and financial counterparties.

Stephen Friedman's service at the New York Fed provided a striking example of the conflicts of interest that have resulted from close linkages between the Fed and top financial executives. After Goldman converted to a bank holding company in September 2008, FRB granted a waiver that allowed Friedman (i) to continue serving as a Class C director and as chairman of the board of the New York Fed and (ii) to retain his ownership of 46,000 shares of Goldman stock. Without the FRB's waiver, Friedman would have been disqualified from serving as a Class C director unless he resigned his Goldman directorship and divested his Goldman stock.[268] Moreover, Friedman purchased 37,000 additional shares of Goldman stock while his waiver request was pending, and during that period the New York Fed directed AIG to pay $14 billion to Goldman,

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[265] GAO Fed Governance Report, *supra* note 255, at 33-34, 35 (fig. 10), 39; Scott Lanman, *Friedman Quits New York Fed on Concern About Goldman Sachs Ties*, BLOOMBERG.COM, May 8, 2009, *available at* http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a68WNA7cKzu8.

[266] GAO Fed Governance Report, *supra* note 255, at 19 (fig. 4), 21.

[267] Orson Aguilar, *Viewpoint: N.Y. Fed Board Move Tone-Deaf On Public Service*, AM. BANKER, Oct. 16, 2009, at 9 (criticizing the appointment of Pfizer's chief executive officer, Jeffrey Kindler, as a Class B director of the New York Fed, because Pfizer relied on loans from Bank of America, Citigroup, Goldman Sachs and JP Morgan Chase to finance its recent merger with Wyeth); Steven Sloan, *As Fed's Role Grows, Doubt Spurs Critics*, AM. BANKER, May 15, 2009, available at http://www.americanbanker.com/issues/174_97/-378660-1.html?zkPrintable=true (reporting that Pepsico's chief executive was a Class B director at the New York Fed, while senior executives of United Parcel Service, Home Depot and Chevron served as Class C directors at other Federal Reserve Banks).

[268] GAO Fed Governance Report, *supra* note 255, at 33-34, 35 (fig. 10).

representing full payment of AIG's obligations to Goldman under credit default swaps ("CDS").[269] In addition, Friedman led the search committee for a new president of the New York Fed after Timothy Geithner left that position to become Treasury Secretary, and the New York Fed ultimately selected William Dudley, Goldman's former chief economist, as its new president.[270] Friedman resigned as a Class C director and as chairman of the New York Fed in May 2009, after his dual role provoked intense controversy and widespread criticism.[271]

A GAO report issued in October 2011 warned that "[h]aving the Class A directors, who represent member banks, and the Class B directors, who are elected by member banks . . . creates an appearance of a conflict of interest."[272] The GAO found that this

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[269] Aaron Lorenzo, *Investigations: House Panel Delving Deeper Into Holdings Of Former New York Fed Chair in Goldman*, 94 BNA BANKING REP. 551 (2010); Letter from the House Comm. on Oversight and Gov't Reform to Ben S. Bernanke, FRB Chairman (Mar. 18, 2010), *available at* http://democrats.oversight.house.gov/images/stories/Correspondence/3-18-10-Honorable_Ben_Bernanke-Chairman_Board_of_Gov-AIG.pdf. [hereinafter House Oversight Letter on Friedman Directorship] After the Fed and the Treasury Department rescued AIG in September 2008, the New York Fed directed AIG to pay off its obligations to CDS counterparties at "100% of face value," a decision that provoked sharp criticism from two government oversight bodies. AIG paid Goldman $14 billion to discharge CDS obligations, and Goldman was the second-largest recipient of CDS payments from AIG. FCIC Report, *supra* note 246, at 376-79 (listing AIG's payments to CDS counterparties, including Goldman, and citing strong criticisms of those payments in two reports issued by the Special Inspector General for the Troubled Asset Relief Program ("SIGTARP") and the Congressional Oversight Panel).

[270] Irwin, *supra* note 264; Lanman, *supra* note 265.

[271] Irwin, *supra* note 264 (reporting that Friedman's service at the New York Fed and FRB's waiver became "Exhibit A for what critics perceive as a too-cozy relationship between the New York Fed, which serves as the central bank's eyes and ears on Wall Street, and the bankers it oversees"); House Oversight Letter on Friedman Directorship, *supra* note 269 (declaring that "Mr. Friedman's dual role at the New York Fed and Goldman, his purchase of Goldman stock in December 2008, and the Federal Reserve's waiver of his conflict of its conflict of interest policy after the fact, raise serious questions about the integrity of the Fed's operations").

[272] GAO Fed Governance Report, *supra* note 255, at 41; *see id.* at 32 (stating that Reserve Bank "directors' affiliations with financial firms . . . continue to pose reputational risks to the Federal Reserve System");

perceived conflict of interest was accentuated during the financial crisis, because "at least 18 former and current Class A, B and C directors from 9 Reserve Banks . . . were affiliated with institutions that used at least one [Fed-administered] emergency program."[273] For example, the New York Fed provided emergency assistance to a major bank and three large financial firms while executives of all four organizations served as directors of the New York Fed.[274]

Researchers have confirmed that banks have received material benefits while their executives served as directors of Reserve Banks. Two academic studies found that banks were significantly more likely to receive capital assistance under the Troubled Asset Relief Program ("TARP") if their executives served as directors of either Reserve Banks or Reserve Bank branches.[275] A third study determined that (i) banks whose executives were elected as Reserve Bank Class A directors between 1990 and 2009 experienced significant abnormal gains in their stock market values, and (ii) banks whose executives served as Reserve Bank directors during that twenty-year period were significantly less likely to fail

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Cheyenne Hopkins, *Crisis or No, Debate Over Reg Reform Splintering*, AM. BANKER, May 21, 2009, at 1 (quoting Senator Shelby's statement during a Senate committee hearing that "[a]n inherent web of conflict is built into the DNA of the Fed as it now exists"); Sloan, *supra* note 267 (quoting Kevin Jacques, a prominent academic, who described the governance structure for Federal Reserve Banks as "really, really clubby").

[273] GAO Fed Governance Report, *supra* note 255, at 39.

[274] Jamie Dimon, chairman of JP Morgan Chase, served as a Class A director of the New York Fed while his bank "participated in various emergency programs and served as one of the clearing banks for emergency lending programs" administered by the New York Fed. *Id.* at 40; Donna Borak, *GAO Fears Conflicts of Interest at Fed*, AM. BANKER, Oct. 20, 2011, at 2. Similarly, as previously noted, executives of three major financial firms served as directors of the New York Fed while their institutions participated in Fed emergency programs. Richard Fuld, chairman of Lehman Brothers, and Jeffrey Immelt, chairman of General Electric, served as Class B directors, while Stephen Friedman, a director and former chairman of Goldman Sachs, served as a Class C director and as chairman of the board. GAO Fed Governance Report, *supra* note 255, at 33-36, 39.

[275] Ran Duchin & Denis Sosyura, *TARP Investments: Financials and Politics* 3-4, 19-20, 31-32, 35 (Ross Sch. of Bus. Working Paper No. 1127, 2010), *available at* http://deepblue.lib.umich.edu/bitstream/2027.42/63451/9/1127_duchin_oct10.pdf; Lei Li, *TARP Funds Distribution and Bank Loan Growth* 3-4, 20 (April 22, 2010), *available at* http://ssrn.com/abstract=1567073.

(compared with other banks), and none of those banks failed after receiving government assistance.[276] The foregoing evidence indicates that large financial institutions have exerted substantial influence on Fed policies through their election of bank executives and client executives as Reserve Bank directors. Thus, despite the Fed's political and financial autonomy, the Fed's governance structure evidently has made it vulnerable to considerable industry influence.

In contrast to OCC and the Fed, FDIC has demonstrated a significantly higher degree of independence from industry influence. Like CFPB, FDIC has a clearly defined mission and an assured source of funding. FDIC views its fundamental purpose as protecting bank depositors and defending the integrity of the Deposit Insurance Fund ("DIF").[277] FDIC also has a guaranteed funding source that is not subject to congressional control or vulnerable to charter competition. FDIC collects risk-adjusted assessments from FDIC-insured institutions, and virtually all banks operate with FDIC insurance.[278]

FDIC has frequently demonstrated its commitment to protecting the DIF as well as its willingness to resist banking industry influence. Over the past three decades, bank representatives have repeatedly criticized the agency for imposing higher capital requirements on banks in order to safeguard the DIF. Critics have mocked FDIC's acronym as standing for "Forever Demanding Increased Capital."[279] During the late 1990s and early 2000s, FDIC

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[276] Adams, *supra* note 255, at 28-39.

[277] DAVID WESSEL, IN FED WE TRUST: BEN BERNANKE'S WAR ON THE GREAT PANIC 219-20 (2009) (stating that FDIC Chairman Sheila Bair was "a fierce and relentless defender of the FDIC fund [during the financial crisis], putting protection of that kitty above all else"); Tom Fox, *How the FDIC got to the top of the heap: The No. 1-ranked agency's leader extols his workers' sense of purpose*, WASH. POST, Nov. 24, 2011, at B4 (quoting Acting FDIC Chairman Martin Gruenberg's view that "[t]he great strength of the [FDIC] is that it has a very clear and understandable mission, and that mission is to insure the deposits that people have in federally insured financial institutions").

[278] CARNELL, MACEY & MILLER, *supra* note 84, at 62-63, 316-18; MICHAEL P. MALLOY, PRINCIPLES OF BANK REGULATION § 1.11 (West Concise Hornbook, 3d ed. 2011).

[279] For examples of this mocking description of FDIC, see *All Things Considered*: "FDIC Chief Earned Rep As a Consumer Advocate," Nat'l Pub. Radio broadcast, June 27, 2011 (transcript available on Lexis) (quoting banking industry consultant Bert Ely's use of the same description); Barbara

fought hard to maintain tougher capital rules for U.S. banks (including leverage capital requirements) during international negotiations over the Basel II capital accord. FDIC also strongly questioned the reliability of Basel II's "advanced internal risk-based" ("A-IRB") method for determining capital requirements. In contrast, the Fed aligned itself with the largest banks in pushing for incorporation of the A-IRB methodology into the Basel II accord.[280] FDIC's deep skepticism about the A-IRB approach proved to be well-founded when LCFIs relied on internal risk-based models "to operate with capital levels that were 'very, very low, . . . unacceptably low' during the period leading up to the financial crisis."[281]

During the crisis, FDIC chairman Sheila Bair disagreed with Fed and Treasury officials on several occasions about the desirability of establishing bailout programs for large troubled financial institutions. For example, FDIC refused to concur with the New York Fed and Treasury in using the "systemic risk exception"

A. Rehm, *Editor at Large: Endgame for Bair Is No Less Audacious*, AM. BANKER, Nov. 18, 2010, at 1 (quoting same description, and reporting that FDIC has consistently been the strongest proponent of tougher capital rules for banks); Joseph F. Sinkey, Jr., *Comment: Issuing Trust-Preferred Too Good a Game to Sit Out*, AM. BANKER, Dec. 21, 1998; Jed Horowitz, *Let 'Em Eat Leverage*, AM. BANKER, Oct. 3, 1990, at 2; Paul M. Horvitz, *The Increase in Capital Standards Will Make Banking Safer*, AM. BANKER, Aug. 24, 1988, at 4 (quoting same description, and observing that "FDIC wants increased capital because bank capital provides a cushion for the insurance system against losses due to bank failures," while "[b]ankers oppose higher capital standards because they fear that higher capital ratios result in a lower return on equity"); *Washington's Financial Cops at a Glance: American Banker Guide to the Regulators*, AM. BANKER, Oct. 21, 1984, at 29 (quoting same description); Paul S. Nadler, *A Conference of Directors in Michigan Shows Banking Communications at Work*, AM. BANKER, Nov. 17, 1980, at 4 (quoting same description, and noting that "bankers and board members agreed that a bank should try to get away with as little capital as possible").

[280] TARULLO, *supra* note 223, at 99-130; Arthur E. Wilmarth, Jr., "*Reforming Financial Regulation to Address the Too-Big-To-Fail Problem*," 35 BROOK. J. INT'L L. 707, 759 n.203 (2010).

[281] Wilmarth, *Too-Big-to-Fail Problem*, *supra* note 57, at 1010 (quoting *Base Camp Basel*, ECONOMIST, Jan 21, 2010, *available at* www.economist. com/node/15328883).

("SRE")[282] to protect WaMu's bondholders when WaMu failed on September 25, 2008. Bair insisted that WaMu's uninsured bondholders, rather than the DIF and taxpayers, should bear the losses caused by WaMu's reckless lending policies.[283] Similarly, FDIC originally resisted proposals by Treasury and the Fed to use the SRE on two subsequent occasions: (i) on September 29, 2008, when federal officials invoked the SRE to protect uninsured creditors (including bondholders) when Wachovia failed, and (ii) in October 2008, when federal officials approved a program to guarantee debt securities issued by FDIC-insured banks. On both occasions, Fed and Treasury officials exerted great pressure to overcome Bair's reluctance to expose the DIF to potential losses by invoking the SRE.[284]

FDIC also demonstrated a much tougher attitude than the Fed and OCC when the largest banks sought to exit the TARP capital assistance program by repurchasing the preferred stock they had sold to Treasury. From November 2009 to June 2011, FDIC tried unsuccessfully to force several major banks (including Bank of America, Wells Fargo and PNC) to issue to investors at least $1 in new common stock for every $2 of TARP preferred stock they repurchased from Treasury. FDIC insisted on the 1-for-2 ratio in order to "increase the quality" of the seven banks' capital structures and limit the risk those banks posed to the DIF.[285] However, OCC pushed for much more lenient terms for the big banks, and FRB took an intermediate position. Over the FDIC's objections, regulators ultimately allowed the banks to repurchase their TARP preferred stock while failing to meet the 1-for-2 ratio advocated by FDIC.[286]

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[282] *Id.* at 1001, 1022-23 (discussing the SRE embodied in 12 U.S.C. § 1823(c)(4)(G), and observing that concurrence among the Treasury, Fed and FDIC is required to invoke the SRE).

[283] WESSEL, *supra* note 277, at 218-21 (explaining that New York Fed President Timothy Geithner argued strongly that the SRE should have been invoked to authorize FDIC to protect bondholders when WaMu failed, but Fed chairman Ben Bernanke agreed with FDIC chairman Bair's position that the SRE should not be used); FCIC Report, *supra* note 246, at 366 (stating that Treasury officials also disagreed with Chairman Bair's position).

[284] WESSEL, *supra* note 277, at 221-23, 232-33; FCIC Report, *supra* note 246, at 366-69.

[285] "Exiting TARP: Repayments by the Largest Financial Institutions," SIGTARP Audit Report 11-005 (Sept. 29, 2011), at 19-30.

[286] *Id*. at 20-63.

Former FRB Vice Chairman Donald Kohn summarized the positions of the three agencies in the following terms: "[W]hile FDIC wanted the 1-for-2 to be met entirely with new common stock, "the OCC was much more relaxed than that, and [FRB] was a little more relaxed than the FDIC."[287] Similarly, FRB Governor Daniel Tarullo explained that "FDIC was understandably concerned about its exposure to institutions through [its debt guarantee program] and the deposit insurance fund, [while] OCC tends to look more narrowly at specific national banks with less of a macro perspective."[288]

In sum, FDIC's clearly-defined mission and its secure source of funding have encouraged the agency to act with more independence from the banking industry, compared to OCC and the Fed. A recent study concluded that, while FDIC made some supervisory mistakes during the subprime lending boom, its overall regulatory record during the subprime lending boom was better than that of OCC and the Fed.[289] The FDIC's greater willingness to resist industry influence indicates that CFPB's unambiguous mission and assured funding should encourage a similarly independent attitude within CFPB.[290]

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[287] *Id.* at 20 (quoting Mr. Kohn's remarks to SIGTARP).
[288] *Id.* (summarizing Mr. Tarullo's statement to SIGTARP).
[289] ENGEL & MCCOY, *supra* note 10, at 157-205; *see id.* at 163 (observing that state banks supervised by FDIC and FRB recorded much lower default rates on their mortgage loans from 2006 to 2008 compared to national banks regulated by OCC and federal thrifts regulated by OTS); *id.* at 184-87 (criticizing FDIC for failing to stop unsound subprime lending by Fremont Investment & Loan and Franklin Bank, but noting that those failures appeared to be "isolated instances," while "the OCC and the OTS were in a state of denial about the grave nature of [national] bank and [federal] thrift involvement in reckless lending and the equally grave nature of their own failure to supervise"); *id.* at 204-05 (showing that FRB, OCC and OTS supervised 11 of the 15 largest subprime lenders in 2006, while FDIC regulated only one of those lenders (Fremont)).
[290] *See* Barkow, *supra* note 7, at 44-45, 77 (concluding that that CFPB's "guaranteed funding stream" from the Fed provides the bureau with significant insulation against industry capture).

C. Requiring CFPB to Depend on Congressional Appropriations for Its Budget Would Make CFPB Vulnerable to Political and Industry Capture

The Republican-sponsored House legislation would remove a crucial guarantee of CFPB's autonomy by giving Congress complete control over CFPB's budget.[291] Any regulatory agency that depends on Congress for its budget is vulnerable to political influence exerted by the regulated industry through the appropriations process.[292] For example, Congress controls CPSC's budget, and since its creation in 1980 the agency has been "chronically underfunded and understaffed. . . . As a result, CPSC has been no match for the industry participants it is charged with regulating."[293]

Except for CFTC and SEC, no federal financial regulator is subject to congressional appropriations.[294] Congress has undermined the effectiveness of CFTC and SEC over the past two decades by frequently failing to provide those agencies with adequate funds.[295]

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[291] *See supra* note 33 and accompanying text (discussing a Republican-backed House bill that would make CFPB's entire budget subject to congressional appropriations).
[292] Barkow, *supra* note 7, at 42-44.
[293] *Id.* at 67; *see also id.* at 42 n.103, 44, 67 (describing CPSC's lack of adequate resources to fulfill its statutory mandate, due to Congress' refusal to increase its budget); Andrew Zajac, *New leadership on U.S. product safety: Obama vows to revitalize ailing CPSC*, CHI. TRIB., May 6, 2009, at C14 (reporting that CPSC had been "underfunded for years" and had only 430 employees in 2009, compared with 978 in 1980; as a result, the "gutted agency became a docile captive of the industry it regulates").
[294] Sean Lengell, *Schumer: Boost SEC's budget to fight fraud*, WASH. TIMES, Sept. 4, 2009, at A09.
[295] Mary Schapiro, Chairman, Sec. & Exchange Comm'n, Speech at the Brodsky Family Lecture at Northwestern Univ. Law School (Nov. 9, 2010) (stating that, when Ms. Schapiro became SEC chairman in January 2009, the SEC was "underfunded and understaffed . . . . We were behind, and falling further behind"), *available at* http://www.sec.gov/news/speech/2010/spch110910mls.htm; *Enhanced Investor Protection After the Financial Crisis: Hearing Before the S. Comm. on Banking, Hous., and Urban Affairs*, 112th Cong. 5, 13 (2011) (statement of Lynn Turner, Former SEC Chief Accountant) (stating that one reason why CFTC and SEC were "ineffective" during the decade leading up to the financial crisis was that both agencies "lacked adequate funding and resources;" in particular, "SEC

After Republicans took control of the House in the 2010 midterm elections, Republican leaders announced plans to delay the implementation of Dodd-Frank's reforms of the derivatives and securities markets by squeezing the budgets of CFTC and SEC.[296] Incoming House majority leader Eric Cantor (R-VA) reportedly said that "denying funds to the SEC and other agencies is 'what the American people are expecting.'"[297]

During 2011, Republicans blocked any significant increases in the CFTC's and SEC's operating budgets.[298] At congressional oversight hearings in December 2011, CFTC chairman Gary Gensler and SEC chairman Mary Schapiro expressed grave doubts about their agencies' ability to adopt and enforce the new regulations required by Dodd-Frank unless Congress approved major increases in their budgets.[299] Republican leaders and the financial services industry did

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was essentially starved by Congress of necessary resources during much of the 1990s," and SEC again lacked adequate funding between 2005 and 2007), *available at* http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.Testimony&Hearing_ID=c7085db2-ae43-471a-aa5c-357f2226a096&Witness_ID=df29c589-0882-4468-b4be-96f53902b567; *Memo to Congress: It's time for SEC to be self-funded*, INVESTMENT NEWS, May 16, 2011, at 0008 (stating that "SEC has been chronically underfunded for years") (available on Lexis); Richard Sansom, *Republicans' return to power threatens CFTC's implementation of Dodd-Frank*, SNL DAILY GAS REPORT, Jan. 12, 2011 (reporting that "CFTC has been underfunded for at least a decade").

[296] Bruce Carton, *How Can Congress Kill Dodd-Frank? By Underfunding It*, COMPLIANCE WEEK, Jan. 2011; Kelsey Snell, *Industry Looks to Derail Dodd-Frank Enforcement*, NAT'L J., Feb. 15, 2011.

[297] Carton, *supra* note 296 (quoting Rep. Cantor).

[298] *Id.*; William D. Cohan, *Republicans Try to Starve Wall Street Watchdog*, BLOOMBERG.COM, Nov. 27, 2011, *available at* http://www.bloomberg.com/news/2011-11-27/republicans-try-to-starve-wall-street-watchdog-william-d-cohan.html; Sansom, *supra* note 295 ; Robert Schmidt et al., *The Great Regulatory Hold-Up*, BLOOMBERG BUSINESS WEEK, Feb. 14-20, 2011, at 24; James B. Stewart, *As a Watchdog Starves, Wall St. Is Tossed a Bone*, N.Y. TIMES, July 16, 2011, at A1; *see* Roger Nayak, *The sticky politics of MF Global's demise*, SNL FINANCIAL SERVICES DAILY, Dec. 7, 2011 (reporting that "some observers feel that tightened budgets have hamstrung the CFTC and the SEC" in their efforts to implement Dodd-Frank, and noting that the agencies had missed 71 of 95 deadlines for adopting rules to carry out Dodd-Frank's reforms of derivatives regulation).

[299] Joe Adler, *MF Global, Gensler Dominate Hearing on Derivatives Rules*, AM. BANKER, Dec. 2, 2011, *available at* http://www.americanbanker.

not disagree with these gloomy assessments of the likely impact of budget stringency on the two agencies.[300] Rather, they seem determined to "defang Dodd-Frank" by "squeezing [CFTC and SEC] through the budget process."[301]

As discussed above, Republican legislators and major banks took a very different position when they pushed for legislation to create FHFA as a new and more powerful regulator for Fannie and Freddie.[302] Republicans and their banking allies insisted that FHFA must have an independent, secure funding source that was *not* subject to congressional appropriations. They pointed out that Fannie and Freddie had frequently used their political clout to persuade Congress to cut OFHEO's budget and thereby undermine OFHEO's enforcement efforts. Representative Richard Baker (R-LA), a leading proponent of legislation to establish FHFA, declared that OFHEO "historically has been impaired" because it "must come to the Congress for its funding."[303] Baker emphasized the importance of

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com/issues/176_232/dodd-frank-act-mfglobal-1044523-1html?zkPrintable=true; Lindsey White, *As regulators face Senate, Gensler grilled over MF Global*, SNL BANK AND THRIFT DAILY, Dec. 7, 2011; *see* Kevin Wack, *Reform Implementation and Budget Crunch Collide*, AM. BANKER, July 22, 2011, at 4 (reporting on congressional testimony by CFTC chairman Gensler and SEC chairman Schapiro that their agencies could not fulfill their responsibilities under Dodd-Frank without significant budget increases).

[300] *See* Snell, *supra* note 296 (reporting that CFTC chairman Gensler's "worries" about his agency's ability to implement Dodd-Frank with a constrained budget "are music to the industry").

[301] *Id.* For other commentators expressing the same view, see, e.g., Carton, *supra* note 296; Cohan, *supra* note 298 (discussing Republican efforts to cut CFTC budget); Stewart, *supra* note 298 (discussing the Republicans' success in cutting SEC's budget by $200 million).

[302] *See supra* notes 147-151 and accompanying text (describing support by Republicans and major banks for establishment of FHFA as a more powerful regulator for Fannie and Freddie).

[303] 151 CONG. REC. H9131 (daily ed. Oct. 26, 2005) (remarks of Rep. Baker). In the following passage, a prominent journalist described how Fannie's supporters in Congress used the appropriations process to hamstring OFHEO's supervisory effort:

> Fannie's allies in Congress . . . made sure that . . . OFHEO, unlike any other [financial] regulator, would be subject to the appropriations process, meaning its funding was at the mercy of politicians – politicians who often

creating "an independently funded regulator, with all the tools a modern regulator should have to oversee vastly complex financial enterprises to protect the American taxpayer from unwarranted losses."[304] The final legislation established FHFA as a "strong, independent regulator" funded by assessments collected from the GSEs, and the legislation stipulated that FHFA would *not* be subject to the appropriations process.[305]

In creating CFPB, Congress drew directly on FHFA's secure funding model. The Senate committee report on Dodd-Frank declared that "the assurance of adequate funding [from the Fed], independent of the Congressional appropriations process, is absolutely essential to the independent operations of any financial regulator."[306] The Senate report pointed out that the need for independent funding of financial regulators

> was a hard learned lesson from the difficulties faced by [OFHEO], which was subject to repeated Congressional pressure because it was forced to go through the annual appropriations process. It is widely acknowledged that this helped limit OFHEO's effectiveness. For that reason, ensuring that OFHEO"s successor agency . . . would not be subject to appropriations was a high priority for the Committee and the Congress in [passing] the Housing and Economic Recovery Act of 2008.[307]

> took their cues from Fannie. Not surprisingly, OFHEO was a notoriously weak regulator.

Bethany McLean, *Fannie Mae's Last Stand*, VANITY FAIR, Feb. 2009, at 51; *see also* Binyamin Appelbaum et al., *How Washington Failed to Rein In Fannie, Freddie: As Profits Grew, Firms Used Their Power to Mask Peril*, WASH. POST, Sept. 14, 2008, at A01 (reporting that OFHEO "was required to get its budget approved by Congress, while agencies that regulated banks set their own budgets. That gave congressional allies [of Fannie Mae and Freddie Mac] an easy way to exert pressure" on OFHEO).

304 151 CONG. REC. H9131 (daily ed. Oct. 26, 2005) (remarks of Rep. Baker).

305 H.R. REP. NO. 110-142, at 87-88, 126-27 (2007).

306 S. REP. NO. 111-176, at 163 (2010).

307 *Id*.

Several Republican leaders who are pushing for legislation to subject CFPB to the appropriations process were strong proponents of secure funding for FHFA.[308] It is therefore very difficult to identify any persuasive rationale for the attempt to remove CFPB's budgetary independence beyond the desire "to undercut an agency [Republican leaders] never liked to begin with."[309]

V. Conclusion

Congress decided to establish CFPB after concluding that federal bank regulators repeatedly failed to protect consumers during the credit boom leading up to the financial crisis. Because of the prudential regulators' systematic failures to protect consumers, Congress vested CFPB with sole responsibility and clear accountability for implementing effective consumer safeguards. Title X of Dodd-Frank authorizes CFPB to issue regulations, conduct investigations and prosecute enforcement proceedings to protect consumers against unfair, deceptive, abusive and discriminatory financial practices. Title X promotes CFPB's independence from political influence by granting CFPB autonomy in its policymaking, rulemaking and enforcement functions and by giving CFPB an assured source of funding from the Fed.

The financial services industry and most Republican members of Congress vehemently opposed CFPB's creation, and they have sought to prevent CFPB from implementing its mandate under Title X. In July 2011, the Republican-controlled House passed legislation that would fundamentally change CFPB's governance, authority and funding. That legislation would seriously undermine CFPB's autonomy and effectiveness by (i) changing CFPB's leadership structure from a single Director to a five-member commission, (ii) giving federal prudential regulators a greatly enhanced veto power over CFPB's rules, and (iii) requiring CFPB to obtain congressional appropriations to fund its operations. Similarly, Republican Senators declared that they would block confirmation of any CFPB Director until the Senate approved legislation making the

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[308] Davidson, *supra* note 147 (noting that Representatives Spencer Bachus (R-AL), Jeb Hensarling (R-TX), Ed Royce (R-CA) and other current Republican House members supported legislation to establish a GSE regulator whose funding would *not* be subject to congressional appropriations).
[309] *Id.*

same three changes. Without a lawfully-appointed Director, there are substantial doubts about CFPB's ability to regulate nondepository providers of financial services and to exercise many of the other powers delegated to CFPB by Title X.

The financial services industry and Republican leaders have justified their campaign against CFPB by claiming that the bureau has unprecedented powers as well as a unique structure that is unaccountable to the political branches. In fact, as shown above, CFPB's structure and powers closely resemble those of other federal financial regulators, particularly FHFA and OCC. Major banks and their legislative supporters strongly supported the creation of FHFA in 2008 and emphasized FHFA's need for sweeping powers and an independent funding source that would *not* be subject to congressional control. Similarly, large banks and Republican leaders have consistently and vigorously defended OCC's authority and autonomy.

Moreover, CFPB is hardly an unaccountable agency. CFPB must consult with a wide variety of outside parties before issuing regulations. Congress has extensive powers to oversee CFPB's operations, and FSOC may review and set aside CFPB's regulations. Accordingly, it seems clear that the financial services industry and its political allies oppose CFPB because of its statutory mission, not its structure.

Large financial firms evidently fear that they cannot exercise the same degree of political influence over CFPB that they have successfully deployed in the past with regard to prudential regulators. In the financial industry's view, CFPB is likely to act independently and conscientiously in carrying out its mandate to protect consumers from predatory financial practices. Congress should want that result. The financial crisis has shown convincingly that a systematic failure to protect consumers will eventually threaten the stability of our financial system as well as our general economy. Congress should therefore preserve CFPB's existing authority and autonomy despite the determined attacks of the financial services industry and its Republican allies.