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Chapman Client Alert

October 19, 2016 Current Issues Relevant to Our Clients

Adverse CFPB Ruling By D.C. Circuit

On Tuesday, October 11, the U.S. Court of Appeals for the D.C. Circuit issued an important decision involving the Consumer Financial Protection Bureau (*"CFPB")*. Not only did the Court find that the agency's structure was unconstitutional, it also ruled that the CFPB violated due process, and is subject to the statutes of limitations embodied in the laws it seeks to enforce. The case is *PHH Corp. v. Consumer Financial Protection Bureau*, Case No. 15-1177.

Background. In 2014, the CFPB instituted an administrative enforcement against against PHH, a New Jersey-based mortgage lender, alleging violations of the Real Estate Settlement Procedures Act (*"RESPA"*). The CFPB alleged that despite relying on prior regulatory guidance, which was widespread industry practice, PHH violated Section 8 of RESPA by referring customers to mortgage insurers, who in turn bought reinsurance from one of PHH's affiliates. In the initial administrative enforcement action, the CFPB found PHH had violated RESPA, and imposed a $6.4 million penalty. PHH appealed the decision to the CFPB Director, Richard Cordray, who upon review, increased the penalty by $103 million (primarily related to extending relief beyond RESPA's statute of limitations period). PHH then appealed the $109 million final verdict directly to the Court of Appeals for the D.C. Circuit.

In a hundred-page decision, the Court analyzed three questions: (1) whether the CFPB's structure is constitutional, (2) whether the CFPB properly applied RESPA in finding a violation, and (3) whether the statute of limitations in RESPA applies in administrative actions as well as court proceedings.

Constitutionality of CFPB*.* In considering whether the CFPB was constitutional, the Court noted that unlike all other federal agencies, there is no real "check" on the CFPB's power. The CFPB is not administered by a commission, like the Securities and Exchange Commission or the Federal Communications Commission. Instead, only one individual is in charge. And unlike other agencies that feature a single director, the CFPB's Director can only be removed "for cause." Thus, the Court severed the statute's unconstitutional for-cause provision from the remainder of the Dodd-Frank Act. While the decision allows the CFPB to continue its work, it eliminates the Director's unique independence and subjects him to removal by the President, similar to other federal agencies.

With respect to the other two questions, the Court again agreed with PHH.

CFPB Interpretation Flawed. The Court found that, as PHH argued, Section 8 of RESPA allows captive reinsurance arrangements so long as the amount paid by the mortgage insurer for the reinsurance does not exceed the reasonable market value of the reinsurance, overruling the CFPB's interpretation. In addition, the Court found that the CFPB incorrectly and retroactively applied its own interpretation of the law to PHH, and had departed from the guidance of the Department of Housing and Urban Development (*"HUD"*), the agency previously tasked with interpreting RESPA on this issue. Here, rather than publicly changing the prior guidance relied upon by the industry, the CFPB sought to impress its own views through an enforcement action. The Court was highly critical of this practice.

Due Process Thwarted by CFPB's Enforcement Beyond the Statute of Limitations. Lastly, the CFPB had argued that, under Dodd-Frank, there was no statute of limitations for any CFPB administrative action to enforce any consumer protection law. However, the Court strongly disagreed, and noted that the Dodd-Frank Act incorporates the statutes of limitations in the underlying statutes enforced by the CFPB in administrative proceedings. The Court firmly established the premise that the agency cannot exact more than it could in a court proceeding by ignoring applicable statutes of limitation.

What's Coming? While this is a landmark decision, its long term impact is far from clear. The CFPB has noted that it is considering options for seeking further review of the Court's decision, and also cited the need for its continued oversight in order to carry out its enforcement responsibilities as demonstrated by recent actions taken to protect consumers. However, armed with this new decision, companies will have additional bases to challenge CFPB enforcement actions in the future, particularly if the CFPB ignores prior interpretations in order to advance its own agenda or if its actions, like the statute of limitations issue violates due process considerations. This decision also could influence challenges to other agency actions pending in front of the D.C. Circuit Court, including the challenge to the Federal Communications Commission's order regarding the newest interpretation of the Telephone Consumer Protection Act in *ACA International, et al. v. Federal Communications Commission and United States*, which is set for oral argument on October 19, 2016.

For More Information

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