

## Reconsidering CFPB V. PHH

*Law360, New York (February 17, 2017, 8:45 AM EST) --*

The tortuous path of the Consumer Financial Protection Bureau's enforcement action against PHH Corporation took another twist this week, as the U.S. Court of Appeals granted the CFPB's petition for rehearing and vacated a panel opinion that sharply criticized the agency and found its structure unconstitutional. If the court had declined to act, President Donald Trump would have had a clear path to firing CFPB Director Richard Cordray. Instead, the court's action creates fresh uncertainty about the scope and shape of the president's authority over the CFPB. That uncertainty will not be resolved for many months to come.

### CFPB v. PHH

This long journey began as a 2014 enforcement proceeding against PHH for alleged violations of the Real Estate Settlement Procedures Act relating to captive mortgage reinsurance arrangements. The first turning point in the case was the bureau's decision to pursue the action in an administrative proceeding, rather than court. This choice meant that an administrative law judge — rather than a court — would hear the bureau's claims. The bureau did quite well before the ALJ, who ruled against PHH and ordered \$6.4 million in disgorgement.

The bureau's decision to proceed administratively also meant that Cordray — rather than a court — would hear the appeal of that initial decision. The bureau also proved quite effective before its director, who ruled against PHH and ordered \$109 million in disgorgement. In doing so, he made a series of rulings relating to RESPA, including that the RESPA statute of limitations did not apply in administrative proceedings.

Undeterred, PHH appealed Cordray's decision to the D.C. Circuit. There, the bureau faced a panel of three judges appointed by Republican presidents, including Judge Brett Kavanaugh, a longstanding critic of independent agencies. The result was a sharp turn away from Cordray's decision. The court of appeals panel fully and forcefully disagreed with the director's interpretations of RESPA and, more importantly, ruled that the bureau's very structure was unconstitutional.

The CFPB responded with a petition asking the court of appeals to reconsider the case en banc. Such petitions are rarely granted, but today's action means that the panel's opinion is vacated, and the full court of appeals will hear the appeal. The court specifically asked the parties to brief three issues:



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- Is the CFPB’s structure as a single-director independent agency consistent with Article II of the U.S. Constitution and, if not, is the proper remedy to sever the for-cause provision of the statute?
- May the court appropriately avoid deciding that constitutional question, given the panel’s ruling on the statutory issues in this case?
- If the court ruled in *Lucia v. U.S. Securities and Exchange Commission* — another case in which it granted reconsideration — that administrative law judges are inferior officers rather than employees, what is the appropriate disposition of this case?

Each of these issues provides some insight into the court’s thinking and the potential stakes of the appeal.

### **Constitutional Issues**

The panel’s now-vacated opinion featured a long, vigorous analysis of the constitutionality of the single-director independent agency structure. In brief, the court found that the combination of a single director and the requirement that the director be fired only for cause meant that “other than the president, the director of the CFPB is the single most powerful official in the entire United States Government.” This power “threatens the individual liberty protected by the Constitution’s separation of power.” The remedy, according to the court, was to strike from the Dodd-Frank Act the language limiting the president to terminating the director only for “inefficiency, neglect of duty or malfeasance.”

This constitutional issue is the first raised by the court’s order, and it seems likely that it was crucial to the court’s decision to rehear the case. While the RESPA issues that underlie the enforcement cases are important — particularly to PHH and others who engaged in the relevant captive reinsurance practices — it is difficult to see why the full court would wish to engage on a relatively narrow statutory issue. In contrast, the issue of whether Congress may create independent agencies with a single director may be of broad, lasting significance. It will also be of immediate significance to the handful of such agencies already in existence, such as the Federal Housing Finance Agency.

The court’s direction on the constitutional question also raises a question of remedy. The panel selected a fairly modest remedy — the severing of the small portion of the Dodd-Frank Act that limited the president’s authority to terminate the CFPB director. However, the court’s direction that the parties brief the remedy issue suggests that the court may consider more Draconian approaches.

### **Avoiding the Constitutional Issues**

While the constitutional issue may have caught the attention of the court, it may be that some judges would prefer to avoid it entirely. In a partial dissent from the panel opinion, Judge Karen LeCraft Henderson argued that the court should have confined itself to its RESPA analysis, as “normally the court will not decide a constitutional question if there is some other ground upon which to dispose of the case.” To the majority’s contention that resolving only the RESPA issues would merely send PHH back to a new proceeding, Judge Henderson notes that PHH asked only that the prior order be vacated.

The potential that the PHH case turns out to be only about RESPA may vex those who had hoped the case would serve as a springboard to the removal of the current CFPB director. The constitutional issue

in PHH has also been raised in a host of other enforcement matters. In fact, in *CFPB v. D and D Marketing et. al.*, a federal district court in California has already found the PHH panel opinion “most persuasive” and adopted its holding on the constitutionality of the bureau’s structure. However, every month without finality on this issue will bring Cordray a month closer to the end of his term in July 2018. If the single-director structure is deemed unconstitutional after that date, the first director to be terminated without cause could be Cordray’s successor.

### **Administrative Law Judge Issue**

On the same day as it ordered reconsideration in PHH, the court of appeals separately ordered reconsideration of *Lucia v. SEC*, a case involving the constitutionality of the appointments of SEC administrative law judges. *Lucia* raises the issue of whether ALJs are inferior officers under the Constitution. If they are, then there are constitutional limits to the ways in which they may be appointed. Because the CFPB borrowed an SEC ALJ for the PHH hearing, any infirmity in SEC appointments might also apply in PHH.

The court asked for briefing on the appropriate disposition of the PHH case if it decides in *Lucia* that SEC ALJs were not properly appointed. That briefing will likely include arguments about whether the court should reach the constitutional issues relating to the CFPB’s structure if the underlying hearing is vacated due to an appointments issue.

### **What’s Next?**

There has been considerable speculation on the fate of Cordray under Trump, with leaders in both parties expressing strong views about whether he should be terminated. The decision of the D.C. Circuit to reconsider whether the president may fire the director without cause may dampen that debate for the time being. However, the president still has the option, under the Dodd-Frank Act, to fire the director for “inefficiency, neglect of duty or malfeasance.” In addition, he could seek to fire Cordray without cause, and rely upon the reasoning of the panel opinion in PHH. As noted above, a court in California has found that opinion persuasive, and adopted its reasoning. Trump could do the same.

The Trump U.S. Department of Justice will also have to decide whether and how to participate in this case. The bureau has the authority to represent itself before the courts of appeals, but the court requested the views of the United States before it evaluated the petition for rehearing, and may expect or request such briefing on the merits. In December the Obama Department of Justice supported reconsideration, arguing that the panel applied the wrong constitutional test to the agency’s structure. The Trump administration may be less supportive of the bureau and more interested in urging the court to maximize the president’s authority.

During the months the petition has been pending, the CFPB has been moving full speed ahead. Those efforts have included cases — such as last week’s allegation that RD Legal Funding LLC and others had bilked 9/11 first responders out of compensation for their injuries — that burnish the reputation and record of the bureau and its director. That positive momentum may be stalled if more controversial initiatives — such as arbitration and payday lending rules — are rolled out in the months ahead. Such regulations would be subject to review by Congress under the Congressional Review Act, and so may draw attention to the bureau and its director on Capitol Hill.

Meanwhile, PHH is not going to be resolved any time soon. Oral argument is scheduled for May 24, 2017. However, a final opinion may be delayed by several factors, including the slower pace of decisions

during the summer months; the logistics of decision-making and the review of drafts by an en banc court; and the added complexity of the court's interest in coordinating this case with *Lucia v. SEC*. If the president is willing to wait for a decision in this matter, less than a year of Cordray's term will be left.

In a final irony, it bears noting that nothing that happens in *CFPB v. PHH* can prevent Cordray from leading the CFPB for more than five years. Opposition to his nomination in the Senate led to his recess appointment in January 2012 — more than five years ago. His term would be over if he had been confirmed at that time. However, because it took the Senate until July 2013 to confirm his nomination, he may serve until July 2018.

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