

PHH v. CFPB: The Impact on the Bureau's Future

February 2, 2018

Financial Services

On Wednesday, January 31, 2017, the D.C. Circuit, sitting *en banc*, issued its long awaited [decision](#) in PHH v. CFPB, holding that the Bureau's structure is constitutional and overruling an earlier decision that would have permitted the President to replace the Bureau's Director at will. The decision also reinstates key parts of the original panel's decision on the Real Estate Settlement Procedures Act (RESPA). This client alert summarizes the decision and discusses its impact on the Bureau's future and its enforcement of RESPA.

Background

The PHH case has a long history, beginning with an enforcement action brought by the CFPB in 2014. Later that year, an administrative law judge found that PHH had violated the anti-kickback provisions of RESPA through a mortgage reinsurance referral arrangement and ordered \$6.4 million in disgorgement. See 12 U.S. Code § 2607. The matter was appealed to CFPB Director Richard Cordray in 2015, who [increased](#) the disgorgement amount to \$109 million. PHH then appealed to the Court of Appeals for the D.C. Circuit.

In October 2016, in a 2-1 decision, a panel of the D.C. Circuit issued a sharp rebuke to the Bureau, with three key holdings. See *PHH Corp. v. Consumer Fin. Prot. Bureau*, 839 F.3d 1 (D.C. Cir. 2016). *First*, the D.C. Circuit panel held that the Bureau was impermissibly applying a new interpretation of RESPA that "makes little sense." The Bureau had argued that the exception for bona fide compensation under section 8(c) did not apply to a tying arrangement between PHH and mortgage insurers, regardless of whether the payments were reasonable market value for the services provided. *Second*, the panel held that the statute of limitations period for Bureau actions is tied to the statute of limitations in the underlying law the Bureau is enforcing, regardless of forum. *Third*, the D.C. Circuit panel held that the Bureau's structure was unconstitutional, a defect it sought to cure by striking down the provision of Dodd-Frank that permits the Bureau Director to be removed only for cause. See 12 U.S.C. § 5491(c)(3).

In November 2016, the Bureau, with the support of the Obama Administration Justice Department, appealed the panel's decision to the full D.C. Circuit. The October 2016 decision was then vacated pending the rehearing *en banc*, and [oral arguments](#) were held in May 2017, focusing almost exclusively on the constitutionality of the Bureau's structure. Notably, the U.S. Department of Justice, now under new leadership, filed an [amicus brief](#) on February 17, 2017 supporting the original ruling.

***En Banc* Decision**

The D.C. Circuit's ruling was issued on January 31, 2018. Circuit Judge Pillard, writing for the 7-3 majority, relies heavily on *Humphrey's Executor*, 295 U.S. 602 (1935). In that case, the Supreme Court found, over eighty years ago, that similar for-cause removal provisions were permissible with regard to Commissioners on the Federal Trade Commission, an independent "consumer-protection financial regulator." Judge Pillard notes that the Supreme Court has "since reaffirmed and built on" the protection of independent agency leadership from at-will removal by the President. More broadly, the majority notes that "[n]othing about the CFPB stands out to give us pause that it—distinct from other financial regulators or independent agencies more generally—is constitutionally defective."

For the majority, the application of precedent to the CFPB is fairly straightforward. In analyzing whether the Dodd-Frank Act's limitation on removal unconstitutionally interferes with the President's Article II powers, the majority reasons that (1) the removal limitation is "wholly ordinary" and "the verbatim protection" that was upheld by *Humphrey's Executor*, and (2) the "CFPB Director's autonomy is consistent with a longstanding tradition of independence for financial regulators." Accordingly, the Court concludes that precedents, particularly *Humphrey's Executor* and *Morrison v. Olson*, 487 U.S. 654 (1988), "stand in the way" of finding the CFPB's leadership structure unconstitutional. The majority opinion also takes issue with PHH's "untenable" distinction between a single-headed agency and a multi-member one when it comes to the removal power, describing PHH's position as a "wholesale attack on independent agencies—whether collectively or individually led—that, if accepted, would broadly transform modern government." Circuit Judge Tatel, in concurrence, succinctly summarized the decision: "PHH is free to ask the Supreme Court to revisit *Humphrey's Executor* and *Morrison*, but that argument has no truck in a circuit court of appeals."

In addition to the agency structure issue, the D.C. Circuit reinstated the three-judge panel's RESPA determinations and remanded the case to the CFPB for decisions consistent with that opinion. Accordingly, though PHH did not prevail on the constitutional arguments, the decision is still a substantial victory that could result in the elimination of all liability.

The dissenting opinions disagreed with the majority, finding the Bureau's structure and power "novel" even among independent agencies, arguing for striking the for-cause removal provision or even invalidating all of Title X of the Dodd-Frank Act, which created the Bureau. One dissenting opinion also found that the Administrative Law Judge who heard the initial case was not appropriately appointed. This issue was not reached by the majority, although a pending Supreme Court case touching on that issue could make it relevant in the future. See *Lucia v. Sec. & Exch. Comm'n*, 868 F.3d 1021 (D.C. Cir. 2017), cert. granted, 2018 WL 386565 (U.S. Jan. 12, 2018) (No. 17-130)

The Future of the CFPB Director

The Supreme Court may never get an opportunity to weigh in on whether the CFPB structure is constitutional. The CFPB may only appeal those issues that it lost—*i.e.*, the statute of limitations question and the RESPA issues. Any further appeal on the constitutional issues may depend on PHH's willingness to continue to litigate a matter in which it has already secured substantial relief.

That said, perhaps the most immediate impact of the PHH decision will be on the nomination and confirmation of a new CFPB Director, now that Director Cordray has resigned. That 5 year position, now open and awaiting a nominee, will continue to cross presidential administrations, burdening new Presidents with powerful Directors who may have sharply different views of the agency and its mission. These Directors could serve for years into a new Administration's term with limited checks on their power and decision-making. Both industry and consumer advocates now have reason to rethink their positions on whether mitigating such conflicts, either through a Commission structure or Presidential authority over the Bureau, would be a wiser course. In the short-run, this decision is likely to add fuel to an already politically-charged confirmation process.

RESPA, Statute of Limitations, and Regulation by Enforcement

The other major impact of the PHH decision is that it reintroduces significant limitations on the Bureau's enforcement authority, both for RESPA matters and more broadly. By reinstating the D.C. Circuit panel's scathing critique of the Bureau's RESPA enforcement, the court has breathed new life into the exceptions under RESPA section 8(c). Under the reinstated opinion, and as industry had long believed, Section 8(c) provides an exception for market-value transactions even when there are referrals between the parties. That decision also restricts the Bureau's enforcement actions to statutory timeframes, another welcome development for regulated entities.

More broadly, the opinion is a call for the Bureau to exercise humility, transparency, and deliberative process when proceeding with controversial or new legal theories. These are the same concerns and goals that Acting Director Mulvaney expressed in his Wall Street Journal op-ed and email to Bureau staff regarding the Bureau's [new mission](#) and goals. Together, this joint call for less regulation by enforcement and more clarity and predictability regarding the Bureau's interpretation of the law signal a new direction for the Bureau in the years ahead.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our Financial Services group:

[Eric Mogilnicki](#)
[Eitan Levisohn](#)

+1 202 662 5584
+1 202 662 5309

emogilnicki@cov.com
elevisohn@cov.com

This information is not intended as legal advice. Readers should seek specific legal advice before acting with regard to the subjects mentioned herein.

Covington & Burling LLP, an international law firm, provides corporate, litigation and regulatory expertise to enable clients to achieve their goals. This communication is intended to bring relevant developments to our clients and other interested colleagues. Please send an email to unsubscribe@cov.com if you do not wish to receive future emails or electronic alerts.