CFPB is in Existential Crisis — and Covered Parties Have a Unique Opportunity

Due to a decision of a three-judge panel of the U.S. Court of Appeals for the Fifth Circuit striking down the Consumer Financial Protection Bureau's ("CFPB" or "the Bureau") Payday Lending Rule promulgated in 2017 — in a case known as *Community Financial Services Association of America, Limited v. CFPB*[1] — the Bureau's very existence is in peril.

That decision, authored by Judge Cory T. Wilson, held that the lack of congressional control over the CFPB's funding apparatus meant that Congress could not exercise over the Bureau its requisite, and constitutionally endowed, oversight through appropriations. This, said the Fifth Circuit, was repugnant to the Constitution's Appropriations Clause, so it reversed the District Court's contrary determination.[2] And this decision imperiled the structural integrity of various CFPB functions and perhaps of the agency itself.

Some of the key takeaways from this decision are:

- CFPB's funding structure violates the Constitution's Appropriations Clause.
- There was a "linear nexus" between the unconstitutional funding mechanism and the challenged CFPB action — in this case, a rule promulgated by the Bureau.
- That nexus applies to all CFPB actions resultant from the CFPB's funding, including the rules it promulgates, the investigations it conducts, and the decisions it makes.
- Most and perhaps all of the CFPB's actions, rules, investigations, and decisions are in jeopardy.
- Private entities subject to the CFPB might want to deploy this decision expeditiously and strategically.

How the CFPB Operates

Even in the special world of independent agencies, the CFPB is a unique agency with unique powers at its disposal and a specific manner of operation. The Bureau is reposed within the Federal Reserve and its budget comes from the Federal Reserve, not from the usual process of congressional appropriations.[3] Federal law lets the CFPB

[1] 51 F.4th 616 (2022) ["*CFSAA*"].
[2] The Fifth Circuit rejected the plaintiffs' Administrative Procedure Act (APA), non-delegation, and unconstitutional insulation from Presidential removal claims. *See id.* at 623, 626—35. However, their Appropriations Clause claim was successful before the Court of Appeals. The District Court had rejected each of the plaintiffs' claims. *See Cmty. Fin. Servs. Ass'n of Am., Ltd. v. CFPB*, 558 F. Supp. 3d 350 (W.D. Tex. 2021).
[3] 12 U.S.C. § 5491(a).

Director draw up to 12% of the annual budget of the Federal Reserve — without needing to request congressional authorization. This, many would argue, means that Congress retains little direct control over the CFPB, which in turn gets to act with even greater omnipotence than other independent agencies in the federal government. Whereas the latter may be reined in directly and easily through congressional appropriations, the CFPB may not. As a consequence, the CFPB's accountability to Congress — and the perception thereof, in the public's eyes — becomes unconstitutionally diluted and attenuated.

A brief recap of the CFPB's backstory is necessary. Enacted in 2008 in response to a financial crisis, the Consumer Financial Protection Act (Act) was an important piece of legislation. It entrusts the CFPB to implement and enforce federal consumer protection laws so that "all consumers have access to markets for consumer financial products and services" — markets that "are fair, transparent, and competitive."[4] The Bureau retains authority to administer and enforce 18 federal statutes "cover[ing] everything from credit cards and car payments to mortgages and student loans."[5] On top of all this, the Act also forbade "any unfair, deceptive, or abusive act or practice" by certain participants in the consumer-finance industry.[6] As the Supreme Court observed in a 2020 decision enabling the President to fire the CFPB Director at will, "Congress authorized the [Bureau] to implement that broad standard (and the 18 pre-existing statutes placed under the agency's purview) through binding regulations."[7]

Congress also empowered the CFPB Director to "prescribe rules and issue orders and guidance, as may be necessary or appropriate to enable the Bureau to administer and carry out the purposes and objectives of the Federal consumer financial laws, and to prevent evasions thereof."[8] Therefore, the "unfair, deceptive, or abusive acts or practices" that some consumer-finance industry actors commit may be "identif[ied] as unlawful" by the rules the CFPB Director prescribes.[9]

According to the Supreme Court, unsurprisingly the CFPB "wields vast rulemaking, enforcement, and adjudicatory authority over a significant portion of the U.S. economy."[10] "Th[at] agency," the court recently noted, is authorized "to conduct investigations, issue subpoenas and civil investigative demands, initiate administrative adjudications, and prosecute civil actions in federal court."[11]

Specifically, the CFPB "may seek restitution, disgorgement, and injunctive relief, as well as civil penalties of up to $1,000,000 — inflation adjusted — for each day that a violation occurs."[12] And in this case, the Fifth Circuit took care to note: "Unlike nearly every other administrative agency, Congress placed this 'staggering amalgam of legislative, judicial, and executive power in the hands of a single Director' rather than a multimember board or commission."[13]

As the Fifth Circuit further noted, "[w]hile the great majority of executive agencies

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[4] 12 U.S.C. § 5511(a).
[5] *Seila Law LLC v. CFPB*, 140 S. Ct. 2183, 2200 (2020).
[6] 12 U.S.C. § 5536(a)(1)(B).
[7] *Seila Law*, 140 S. Ct. at 2193; *see id.* at 2197 (invalidating 12 U.S.C. § 5491(c)(3)).
[8] 12 U.S.C. § 5512(b)(1).
[9] *Id*. § 5531(b).
[10] *Seila Law*, 140 S. Ct. at 2191.
[11] *Id*. at 2193.
[12] *Id*.
[13] 51 F.4th at 638 (quoting *All Am. Check Cashing*, 33 F.4th 218, 221—22 (5th Cir. 2022) (Jones, J., concurring)).

rely on annual appropriations for funding, the Bureau does not."[14] What happens is that "each year, the Bureau simply requisitions from the Federal Reserve an amount 'determined by the Director to be reasonably necessary to carry out' the Bureau's functions."[15] Congress compels the Federal Reserve to so permit if the CFPB's request stays within 12% of the reserve's "total operating expenses."[16] This means that the money diverted to the CFPB from the reserve's funds, in the Fifth Circuit's words, "reduce amounts that would *otherwise* flow to the general fund of the Treasury, as the Federal Reserve is required to remit surplus funds in excess of a limit set by Congress."[17] It was this funding structure of the CFPB that the Fifth Circuit panel reviewed.

The Fifth Circuit's Decision

The Court of Appeals invalidated, under the Appropriations Clause, what it regarded as the CFPB's "self-actualizing, perpetual funding mechanism."[18] It started out by tracing the history of the power of the purse that the Constitution commits to Congress, one that the Constitution expects will stay with Congress.[19]

This clear and specific allocation was at the heart of the separation of powers so unique to the American Constitution and indeed the American experiment itself. Notably, as far as the Framers were concerned, "Congress's exclusive 'power over the purse' [w]as an indispensable check on 'the overgrown prerogatives of the other branches of the government.'" *Id*. at 636 (quoting THE FEDERALIST NO. 58 (J. Madison)). Since most things require money, the Executive and the Judiciary would have to come to Congress. And Congress in turn would have to turn to the Executive to execute the laws and to protect our national security; and it would need to rely on the courts to interpret the laws.

In addition, said the Court of Appeals, "vesting Congress with control over fiscal matters was the best means of ensuring transparency and accountability to the people."[20] It enabled Congress, the panel invoked James Madison in noting, to "'obtain[] a redress of every grievance, and for carrying into effect every just and salutary measure.'"[21] By controlling the federal purse-strings, Congress could dictate how the public's money was going to be expended. The Executive's activities as well as its priorities — including the things it did not want to do — had to be accountable to Congress. And Congress — specifically, its members — had, in turn, to be cyclically accountable to the electorate. That is why we have elections. And this is how power, under our constitutional system, became a check on power.[22]

The Fifth Circuit appreciated that these purposes crystallized in this framework were effectuated in the Constitution's text itself. As an initial matter, all bills to raise revenue had to "originate in the House of Representatives ...." U.S. Const. art. I, § 7, cl. 1. Next, the constitutional power "[t]o lay and collect Taxes" was "cabined by the Appropriations Clause and its follow-on, the Public Accounts Clause: 'No money shall be

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[14] *Id*. (citing 12 U.S.C. § 5497(a)).
[15] *Id*. (quoting 12 U.S.C. § 5497(a)).
[16] 12 U.S.C. § 5497(a)(1)–(2).
[17] *CFSAA*, 51 F.4th at 638 (citing 12 U.S.C. § 289(a)(3)(B)) (emphasis added).
[18] *Id*.
[19] *See id*. at 635—38.
[20] *Id*.
[21] *Id*. at 636 (quoting THE FEDERALIST NO. 58 (J. Madison)).
[22] *See id*. at 635 (citing *United States v. Cox*, 342 F.2d 167, 190 (5th Cir. 1965) (Wisdom, J., concurring); BARON DE MONTESQUIEU, THE SPIRIT OF THE LAWS bk. XI, ch. IV (1772)).

drawn from the Treasury, but *in Consequence of Appropriations made by Law*; and a regular Statement and Account of the Receipts and Expenditures of all public Money shall be published from time to time.'"[23] It is difficult to miss the Constitution's focus on accountability to the public about how its money is being spent by those who wield the power to do so — at least in the federal government.

In the Fifth Circuit's view, "[t]he Appropriations Clause's 'straightforward and explicit command' ensures Congress's exclusive power over the federal purse."[24] This means that "[a]ny exercise of a power granted by the Constitution to one of the other branches of Government is limited by a valid reservation of congressional control over funds in the Treasury."[25] This instruction just as strongly signals an encumbrance on Congress: The Federal Legislature may not forego "'requir[ing] legislative appropriations prior to expenditure.'"[26] And that principle is key here with respect to how the CFPB funding mechanism operated. The CFPB's drawing of funds from within the Federal Reserve's pool of money liberated the CFPB from having to justify its existence to the people's elected representatives when it was spending the people's money.

The CFPB, reasoned the Court of Appeals, "'receives funding directly from the Federal Reserve, which is itself outside the appropriations process through bank assessments.'"[27] Consequently, "Congress did not merely cede *direct* control over the Bureau's budget by insulating it from annual or other time limited appropriations. It also ceded *indirect* control by providing that the Bureau's self-determined funding be drawn from a source that is itself outside the appropriations process — a double insulation from Congress's purse strings that is 'unprecedented' across the government."[28] What is more, "the Treasury will never regain one red cent of the funds unilaterally drawn by the Bureau."[29]

Indeed, CFPB has "a separate fund, ... the 'Bureau of Consumer Financial Protection Fund,'" which "shall be maintained and established at a Federal [R]eserve bank."[30] This fund is controlled by the CFPB Director, who has access to the money deposited there.[31] In fact, the Act says that "[f]unds obtained by or transferred to the Bureau Fund shall not be construed to be Government funds or appropriated monies."[32] And Congress also said that "funds derived from the Federal Reserve System ... shall not be subject to review by the Committees on Appropriations of the House of Representatives and the Senate."[33] This, in the Fifth Circuit's view, meant that "Congress expressly" — and impermissibly — had "renounced its check 'as a restriction upon the disbursing authority of the Executive department.'"[34]

To the Fifth Circuit's mind, this funding scheme clashed with the common sense underlying the Appropriations Clause. Some might say it "dash[ed]" that Clause's "whole

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[23] *Id*. at 636—37 (quoting U.S. Const. art. I, § 9, cl. 7 (emphasis added)).
[24] *Id*. at 637 (quoting *OPM v. Richmond*, 496 U.S. 414, 424 (1990)).
[25] *Id*. (quoting *Richmond*, 496 U.S. at 425).
[26] *Id*. (quoting Kate Stith, *Congress' Power of the Purse*, 97 YALE L.J. 1343, 1349 (1988)).
[27] *Id*. at 638 (quoting *Seila Law*, 140 S. Ct. at 2194, and citing 12 U.S.C. § 5497(a)).
[28] *Id*. at 638—39 (quoting *All Am. Check Cashing*, 33 F.4th at 225 (Jones, J., concurring)).
[29] *Id*. at 639.
[30] *Id*. at 639 (cleaned up).
[31] *See id.*
[32] 12 U.S.C. § 5497(c)(2).
[33] *Id*. § 5497(a)(2)(C).
[34] *CFSAA*, 51 F.4th at 639 (quoting *Cincinnati Soap*, 301 U.S. at 321).

scheme."[35] Since "the executive is forbidden from unilaterally spending funds, the actual exercise by Congress of its power of the purse is imperative to a functional government."[36] The Appropriations Clause, observed the Court of Appeals, "affirmatively obligates Congress to use that authority 'to maintain the boundaries between the branches and preserve individual liberty from the encroachments of executive power.'"[37]

The Appropriations Clause, according to the Fifth Circuit, "embodies the Framers' objectives of maintaining 'the necessary partition among the several departments,' and ensuring transparency and accountability between the people and their government."[38] The Court of Appeals painstakingly pointed out that the Appropriations Clause's powerful "role as 'a bulwark of the Constitution's separation of powers' has been repeatedly affirmed" by the Supreme Court and prominent lower court judges.[39]

The Fifth Circuit invoked Justice Joseph Story's explanation that the Appropriations Clause "'secure[s] regularity, punctuality, and fidelity, in the disbursements of the public money .... If it were otherwise, the executive would possess an unbounded power over the public purse of the nation; and might apply all its moneyed resources at his pleasure.'"[40] Justice Story had added that "'[t]he power to control and direct the appropriations, constitutes a most useful and salutary check upon profusion and extravagance, as well as upon corrupt influence and public peculation.'"[41] The Appropriations Clause, in the Fifth Circuit's view, "expressly 'was intended as a restriction upon the disbursing authority of the Executive department.'"[42]

The Court of Appeals also noted that the CFPB's "capacious portfolio of authority" exacerbated all these concerns about its funding scheme.[43] The greater and more powerful its functions, the more its funding system is likely to corrupt. After all, the Bureau "'acts as a mini legislature, prosecutor, and court, responsible for creating substantive rules for a wide swath of industries, prosecuting violations, and levying knee-buckling penalties against private citizens.'"[44] In sum, "[a]n expansive executive agency insulated (no, double-insulated) from Congress's purse strings, expressly exempt from budgetary review, and headed by a single Director removable at the President's pleasure is the epitome of the unification of the purse and the sword in the executive — an abomination the Framers warned 'would destroy that division of powers on which political liberty is founded.'"[45]

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[35] *Department of Transportation v. Association of American Railroads*, 575 U.S. 43, 61 (2015) (Alito, J., concurring).
[36] *CFSAA*, 51 F.4th at 637.
[37] *Id*. (quoting *All Am. Check Cashing*, 33 F.4th at 231 (Jones, J., concurring)).
[38] *Id*. (quoting THE FEDERALIST NO. 51 (J. Madison)).
[39] *Id*. (quoting *U.S. Dep't of Navy v. Fed. Lab. Rels. Auth*., 665 F.3d 1339, 1347 (D.C. Cir. 2012) (Kavanaugh, J.); and citing, among other cases, *id*. ("The Appropriations Clause prevents Executive Branch officers from even inadvertently obligating the Government to pay money without statutory authority.") (citations omitted); *Sierra Club v. Trump*, 929 F.3d 670, 704 (9th Cir. 2019) ("The Appropriations Clause is a vital instrument of separation of powers ...."); *United States v. McIntosh*, 833 F.3d 1163, 1175 (9th Cir. 2016) ("The Appropriations Clause plays a critical role in the Constitution's separation of powers among the three branches of government and the checks and balances between them.")).
[40] *Id*. (quoting 2 JOSEPH STORY, COMMENTARIES ON THE CONSTITUTION OF THE UNITED STATES § 1348 (3d ed. 1858) [STORY]).
[41] *Id*. (quoting STORY, *supra*, at § 1348).
[42] *Id*. at 638 (quoting *Cincinnati Soap Co. v. United States*, 301 U.S. 308, 321 (1937)).
[43] *Id*. at 640.
[44] *Id*. (quoting *Seila Law*, 140 S. Ct. at 2202 n.8).
[45] *Id*. (quoting 2 THE WORKS OF ALEXANDER HAMILTON 61 (Henry Cabot Lodge ed., 1904)).

The Fifth Circuit now came to the most immediately impactful part of its decision: the remedy. What redress would cure this Appropriations Clause violation? In order to get the Payday Lending Rule invalidated, plaintiffs had to demonstrate that "the unconstitutional ... [funding] provision inflicted harm."[46] This they could easily do, said the Court of Appeals, since "the funding employed by the Bureau to promulgate the Payday Lending Rule was wholly drawn through the agency's unconstitutional funding scheme."[47] This meant that "there [wa]s a linear nexus between the infirm provision (the Bureau's funding mechanism) and the challenged action (promulgation of the rule)."[48] It is not seriously contestable that "without [the CFPB's] unconstitutional funding, the Bureau lacked any other means to promulgate the rule."[49]

The Payday Lending Rule, accordingly, had to be "rew[ou]nd[]" — and it was vacated by the Fifth Circuit.[50] Judgment was rendered in the plaintiffs' favor.

Benefiting From This Decision

Businesses and other entities currently being pursued, investigated, or in any way subject to the CFPB's bailiwick might consider invoking this Fifth Circuit decision at the earliest possible opportunity. This decision could have pervasive impact because CFPB's funding likely has impact pervading all its actions, enforcement, investigations, rules, and so on. The question will be whether "the Bureau's improper use of unappropriated funds" led to the challenged action.[51] Put differently, could the challenged action have occurred without the CFPB's "improper use of unappropriated funds?"[52] The answer to both questions almost certainly will be no. Refuting this obvious causal link would be difficult, though certainly the Bureau would try to do so. This Fifth Circuit decision is also a shot across the bow against congressional contemplations of devising agency funding mechanisms outside of the normal appropriations process.

The pertinent covered parties are most likely to succeed in the Fifth Circuit, where this decision remains a binding precedent. That said, the federal government has appealed this decision directly to the Supreme Court.[53] Until this panel decision of the Fifth Circuit is disturbed, the CFPB remains — and will remain — in existential crisis. While Congress could reconfigure the Bureau's funding by bringing it in line with traditional appropriations practice, to many that would undermine the very independence of the CFPB, the reason for its unique funding structure in the first place.

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[46] *Id*. at 643.
[47] *Id*.
[48] *Id*.
[49] *Id*.
[50] *Id*.
[51] *CFSAA*, 51 F.4th at 643.
[52] *Id*.
[53] Interestingly, the CFPB chose to avoid asking the full Fifth Circuit, with its entire complement of non-recused judges, to rehear this case en banc. Instead, the Bureau preferred to go straight to the Supreme Court.

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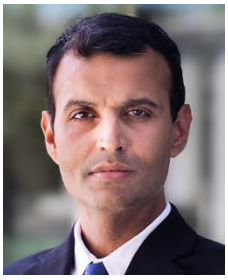

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