The Consumer Financial Protection Bureau's first six months: A predictor of the new agency's growth and expansion
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The Consumer Financial Protection Bureau ("Bureau") has been touted by some as the most powerful federal agency ever created. While definitive proof of such bold statements remains elusive, it is clear that the relatively new and burgeoning Bureau appears poised to have a commanding and dominant role in the consumer financial services industry going forward.

On July 21, 2011, the so-called Designated Transfer Date, the Bureau officially opened its doors and inherited many of its extensive and considerable powers. Six months have since elapsed. With that milestone in the rearview mirror, and the power and sphere of influence of the Bureau growing daily, we pause and look back at what the Bureau accomplished in its relatively short existence. As we will discover, if the first six months establish a trajectory of where this new agency is headed, the sky is the limit.

PRESIDENT OBAMA SEATS A DIRECTOR

At this juncture, no discussion of the Bureau would be complete without reference to the battle over its first director. For months and months after Congress passed the Dodd-Frank Act in July 2010, pundits, politicians, and industry insiders wringed their hands over the speculation that President Obama would nominate the oft-cited architect of the Bureau – Harvard Professor Elizabeth Warren – to be the first director of the Bureau. Warren, however, polarized people into camps for and against her.

Rather than dragging the Bureau into a controversy right out of the box, in September of 2010, Obama appointed Warren to serve in a position than did not require the consent of the Senate, but that nonetheless allowed her to set up the Bureau consistent with her long-term vision for the agency. Obama bestowed her with the title of "Assistant to the President and Special Advisor to the Secretary of the Treasury on the Consumer Financial Protection Bureau," a long but apt designation which Warren held until her departure from the Bureau in September 2011 to begin her bid for a senate seat.

In the summer of 2011, President Obama nominated Richard Cordray to be the first director of the Bureau. Cordray is the former Attorney General of Ohio and has a track record of pursuing claims against the consumer financial services industry. By way of example, as the Ohio Attorney General, Cordray filed a series of lawsuits against certain mortgage servicers asserting numerous claims, including alleged violations of Ohio's unfair or deceptive acts or practices laws.

The Cordray nomination sat dormant in the Senate for months. A group of 44 Republican senators made it clear that they would not approve any nomination – not Cordray, not George Bush, not Ronald Reagan were he still alive – until the Dodd-Frank Act is changed to weaken the agency and the power of its director. In December 2011, the Senate voted on the nomination. The nomination failed. Senate Republicans had ostensibly trumped majority support for Cordray.

Then, in what has been hailed as a defiant and unprecedented move, President Obama used his executive authority to seat Cordray as the top consumer watchdog in the United States during what Republicans term a "pro forma" session (gaveling in a session then out a few moments later) and Democrats call a "gimmick" recess session. Republican senators have predictably vowed to challenge the constitutionality of the appointment. For now and for the foreseeable future (that is, at least until the next full and proper session of Congress ends), Cordray is the new sheriff in town.

FEDERAL NON-DEPOSITORY INSTITUTION SUPERVISION

Wielding his new badge, Bureau Director Corday's first official act was to begin the implementation of a federal non-depository, or "nonbank," supervision program. Under the Dodd-Frank Act, the Bureau has the power to regulate nonbanks, which the Bureau has defined as any "company that offers or provides consumer financial products or services but does not have a bank, thrift, or credit union charter." This action marked the first time in the country's history that such entities would be regulated at the federal level beyond the general oversight of the Federal Trade Commission ("FTC").

Under the new program, the Bureau will oversee nonbank business in particular markets. Right out of the box, the Bureau will begin regulating mortgage companies, payday lenders, and private education lenders. It also has the power to supervise any nonbank that it determines is or will pose a risk to consumers.

In addition, the Bureau may supervise so-called "larger participants" in the consumer financial services industry. Last summer, in anticipation of the implementation of the nonbank program, the Bureau sought comments from the public on who should fall within the definition of "larger participant." At the time, the Bureau tipped its hat as to its view, noting six possible markets for consideration: debt collection, consumer reporting, prepaid cards, debt relief services, consumer credit, and money transmitting. At the moment, we are awaiting the Bureau's initial rule on the definition, which is due no later than June 21, 2012.

SUPERVISION AND EXAMINATION MANUAL 1.0

In October 2011, the Bureau released version 1.0 of its Supervision and Examination Manual ("Manual"). The Manual is a guide to the Bureau's supervision of large banks, thrifts, and credit unions (i.e., those institutions with assets in excess of $10 billion). Further, in conjunction with the new nonbank supervision program, the Manual will serve as a tool for the Bureau to examine other providers of consumer products and services that are not depository institutions.

The Manual is not entirely new. It incorporates procedures developed by the Federal Financial Institutions Examination Council ("FFIEC"), and uses the FFIEC's Uniform Interagency Consumer Compliance Rating System. There are, however, a few new things in the Manual worth pointing out. Importantly, the Manual includes examination procedures for the mortgage servicing industry. The Bureau intends to follow up this version of the Manual with examination procedures for other industries and lines of business.

Equally important is that the Manual effectively dodged the most feared and least understood word in all of Title X of the Dodd-Frank Act: "abusive." Title X of the Dodd-Frank Act gives the Bureau the power to prevent unfair, deceptive, or abusive acts or practices ("UDAAP"). The Dodd-Frank Act defines unfair and abusive, but left deceptive undefined. Borrowing heavily from prior statements by the FTC, the Federal Deposit Insurance Corporation ("FDIC"), and other federal regulators, the Manual goes to some effort to lay out the standards for unfair and deceptive, going so far as to provide some examples of each. But the Manual says precious little about the term "abusive."

CONSTITUENCY BUILDING

While Congress and the President have been battling over just how powerful the Bureau should be and who will be the Bureau's first director, the Bureau has been steadily building its enterprise. And this is not your grandfather's, or even your father's, federal regulator. Just take a look at the Bureau's website (www.consumerfinance.gov). The Bureau has a colorful, interactive, and informative website that is user friendly. Compare that to the websites of other federal agencies who have some responsibility over consumer issues. The Federal Trade Commission's website (www.ftc.gov), for example, is static, seemingly one-dimensional, and difficult to use. Contrast that with the vibrant, intuitive, and inviting look-and-feel of the Bureau's website, a design which begs the question of whether users are really interfacing with the government or some sort of cyber consumer advocate.

The Bureau is taking full advantage of social media, too. It has a Facebook page, which currently has about 13,000 "likes." The Bureau blogs and tweets. And it has its own version of the financial crisis set in the easily accessible and understandable medium of a cartoon. In the cartoon, which can be found on the Bureau's website and on YouTube, the Bureau likens itself to a sort of Batman-like crime fighter who shines a light over the darkness of a Gotham-like city in order to bring to justice the supposed dark underbelly of the consumer financial services industry who issues defective credit products analogized to exploding toasters with bad wiring.

THE BUREAU JOINS WITH OTHER REGULATORS TO REGULATE WHO WILL THEY WILL REGULATE

As a gesture of "clarity and transparency," the Bureau and the Prudential Regulators—the Federal Reserve Board, the FDIC, the Office of the Comptroller of the Currency, and the National Credit Union Administration – jointly addressed agency jurisdiction over the nation's largest banks and credit unions, putting to rest the critical question of which regulator regulates certain financial institutions and when. Because the Dodd-Frank Act is silent on the issue of when and how to determine whether a depository institution has $10 billion in assets and, thus, is considered a large institution under the Act, the Prudential Regulators and the Bureau got together on their own to establish policies and procedures. In order to do so, the agencies needed to determine how to measure the size of financial institutions and when to take that measurement.

With respect to how to measure the size of financial institutions, the group of agencies relied on Section 7(a)(3) of the Federal Deposit Insurance Act, which requires financial institutions to file Call Reports (an account of the condition of the institution, including a disclosure of its total assets) on a quarterly basis. Because this measure is the most common measure of asset size, the agencies determined that it was therefore "appropriate" to use Call Reports to determine size.

With respect to the timing of size measurements, the agencies wanted to avoid undue uncertainty and volatility in identifying a financial institution's primary regulator. In other words, the regulators wanted to stay away from any vagueness or ambiguity in establishing the appropriate regulator for an institution that wavered on the $10 billion "large" institution line. This scenario was avoided by the agencies determining that Call Reports for four consecutive quarters must show $10 billion in assets before changing an institution's status to "large." The FDIC has used this precise method for years which, accordingly, has the added benefit of providing some continuity and certainty to a regulatory regime that is in such an extended state of flux at the moment.

The first measurements were applied retroactively. Notwithstanding a November 2011 announcement, the agencies decided to use Call Reports from June 30, 2011 as the starting place. The agencies rationalized this decision because June 30, 2011 is the closest Call Report date to the date that authority for the federal consumer protection laws was transferred to the Bureau (as noted above, the "Designated Transfer Date" was July 21, 2011).

While it is interesting that this group of federal regulators all got together and determined which regulated entities each of them get to supervise by passing this mandate, what is remarkable is that they did it unabated. The substance of the pronouncement on determining who is "large" may have been non-controversial; the FDIC has basically been doing it this way for years. But should the industry be concerned that the regulators have gathered and made a determination affecting substantive provisions of a governing statute without proper notice and comment? If it turns out to have some precedential effect, the answer is unequivocally "yes."

FLIRTING WITH THE ATTORNEY-CLIENT PRIVILEGE

Federal law (12 U.S.C. § 1828(x)(1)) has long-provided that when a federally chartered institution provides materials covered by the attorney-client privilege to a "Federal banking agency" during an examination, the institution does not waive the privilege. The Bureau is not, however, a "Federal banking agency" for purposes of the statute.

Rather than forego receipt of privileged materials or seek a legislative solution (i.e., to have the Bureau added to the definition of "Federal banking agency"), the Bureau simply concluded that it is, in fact, a "Federal banking agency." The Bureau reasoned that since it inherited supervisory authority from the other federal banking regulators, and such supervision requires access to privileged materials from time to time, the Bureau is therefore entitled to demand the privileged materials of banks, declaring that any production of such materials will not waive the privilege. The potential flaw in this position is that while the Bureau did inherit supervisory authority from the federal banking agencies, it only inherited some – not all. The danger, of course, is that the privilege does not apply to the banks' production and anyone can later request the information in litigation. Did the Bureau move too quickly on this one? Time will tell.

WHERE IS THE BUREAU HEADED?

If the Bureau's past performance is a predictor of its future conduct, we can expect to see more expansion in the months to come. "Expansion of what," you might ask. Pretty much everything.

With Cordray at the helm now, financial services companies should expect an expansion of enforcement activity. Furthermore, with the appointment of Cordray came the statutory power under the Dodd-Frank Act to engage in further rulemaking including, among other things, prescribing disclosure rules and rules addressing reporting requirements for purposes of determining whether the Bureau should be supervising certain nonbanks. Expect more rules overall. As the Attorney General of Ohio, Cordray was also a big proponent of using unfair and deceptive trade practices statutes against financial services companies. While the Bureau's UDAAP powers have sat quietly dormant since the passage of the Dodd-Frank Act, expect a Cordray-led Bureau to use UDAAP aggressively.

One other thing to keep an eye on is the potential for the Bureau to gradually creep up to and maybe even over the line of its statutory authority. Without picking sides on any of the issues, it is clear that the President and the Bureau are not afraid to push the envelope with the agency and its potential powers. This is likely to come to a head at some point, but perhaps not before the Bureau achieves more expansion of its already impressive authority.

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