

The Department of the Treasury Proposes Consumer Financial Protection Agency Act of 2009

On June 30, 2009, the Department of the Treasury sent to Congress a draft of the Consumer Financial Protection Agency Act of 2009 (the “Act”), a bill aimed at establishing a new federal agency for the regulation of consumer financial products and services.¹ The proposed federal agency, the Consumer Financial Protection Agency (the “CFPA”), would be solely responsible for oversight and monitoring of such products and services, and would seek to ensure that:

- consumers have, understand, and can use the information they need to make responsible decisions about consumer financial products or services;
- consumers are protected from abuse, unfairness, deception, and discrimination;
- markets for consumer financial products or services operate fairly and efficiently with ample room for sustainable growth and innovation; and
- traditionally underserved consumers and communities have access to financial services.

If enacted, the Treasury proposal would significantly alter the existing regulatory framework. Certain key changes that would result from the implementation of the Act are summarized below.

I. Changes in the Regulatory Structure

The New Federal Regulatory Landscape

The CFPA would be an “independent agency in the executive branch” run by a five-member Board. Four of those members would be presidential appointees, and the fifth would be the Director of the National Bank Supervisor.² The President would choose one of the five Board members to serve as Director.

Treasury’s proposal would significantly alter the complex regulatory framework currently in place by consolidating the consumer financial protection functions of several existing agencies³ into the CFPA. All lawsuits and rules (including proposed rules and rules not yet effective) of the existing agencies would remain in effect, and certain personnel from those agencies would join the CFPA. The suggested window for consolidation is between six and eighteen months after the passage of the Act.

Importantly, the CFPA’s sweeping jurisdiction would not derogate from the present authority of the Department of Justice, the Securities and Exchange Commission (“SEC”), or the Commodity Futures Trading Commission (“CFTC”). The proposal envisions collaboration in rulemaking among the CFPA, SEC and CFTC, but the CFPA is designed to complement its peer agencies, not compete with them for authority.

¹ Consumer Financial Protection Agency Act of 2009, available at <http://www.financialstability.gov/docs/CFPA-Act.pdf>.

² The Obama Administration has proposed the creation of a National Bank Supervisor, a separate agency within Treasury that would “oversee all federally-chartered banks.” See Financial Regulatory Reform A New Foundation: Rebuilding Financial Supervision and Regulation, available at http://www.financialstability.gov/docs/regs/FinalReport_web.pdf.

³ The agencies referred to are the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, the Director of the Office of Thrift Supervision, the Federal Deposit Insurance Corporation, the Federal Trade Commission, and the National Credit Union Administration.

Federal-State Relations

The goal of the Act is not uniformity, but the establishment of a minimum level of protection for consumers at the federal level. The Act takes care to preserve state laws that impose consumer financial protection regulation which is more stringent than federal regulation in the same field. States are also encouraged to announce their own standards “to deter and detect unfair, deceptive, abusive, fraudulent or illegal transactions in the provision of consumer financial products or services.” Moreover, states are invited to participate in enforcement of federal rules. State attorneys general would be expressly authorized to pursue civil actions on behalf of their citizens in federal court to secure relief for violations of the Act or of rules issued under it.

II. Scope and Nature of CFPA’s Oversight Powers

Covered Persons: The Scope of CFPA Oversight

Under the Act, the CFPA’s oversight powers apply only to certain “covered persons.” The Act defines “covered person” as a person who engages in “financial activity” in connection with providing a “consumer financial product or service” — i.e., providing such a product or service that is to be used primarily for personal or household purposes. Twelve specific “financial activities” are enumerated in the Act, among which are deposit-taking activities, the extension of credit and servicing of loans, check-guaranty services, and acting as a financial adviser.⁴ Investment advisers not already regulated by the CFTC or SEC are covered persons under the Act. The Act also includes a catchall provision, allowing regulation of “financial activity” not listed.

The Act specifically excludes certain persons from the scope of its authority. Section 1022(f) provides that the CFPA has no power to enforce the Act against persons already regulated by the SEC or CFTC. In addition, the CFPA lacks authority to prescribe rules applicable to attorneys or trustees acting in their professional capacities under Section 1037(c). Similarly, most of those engaging in the insurance business are not considered covered persons.⁵

Rulemaking & Information Gathering: The Oversight Powers of the CFPA

The oversight power of the CFPA is twofold, involving both rulemaking and information gathering. Section 1022(b) broadly authorizes the CFPA to “prescribe rules and issue orders and guidance as may be necessary or appropriate to enable it to administer and carry out the purposes and objectives” of the Act and the “enumerated consumer laws.”⁶ Several provisions authorize more specific exercises of the rulemaking power.

⁴ For a complete list, see Section 1002(18).

⁵ Section 1002(18)(O) provides that “the Agency shall not define engaging in the business of insurance as a financial activity (other than with respect to credit insurance, mortgage insurance, or title insurance . . .).”

⁶ Section 1002(16) refers to “enumerated consumer laws,” which include the Alternative Mortgage Transaction Parity Act (12 U.S.C. § 3801 *et seq.*), the Community Reinvestment Act (12 U.S.C. § 2901 *et seq.*), the Consumer Leasing Act (15 U.S.C. § 1667 *et seq.*), the Electronic Funds Transfer Act (15 U.S.C. § 1693 *et seq.*), the Equal Credit Opportunity Act (15 U.S.C. § 1691 *et seq.*), the Fair Credit Billing Act (15 U.S.C. § 1666-1666j), portions of the Fair Credit Reporting Act (15 U.S.C. §§ 1681m(e), 1681s-3, 1681w), the Fair Debt Collection Practices Act (15 U.S.C. § 1692 *et seq.*), portions of the Federal Deposit Insurance Act (12 U.S.C. § 1831t(c)-(f)), portions of the Gramm-Leach-Bliley Act (15 U.S.C. § 6802-09), the Home Mortgage Disclosure Act (12 U.S.C. § 2801 *et seq.*), the Home Ownership and Equity Protection Act (15 U.S.C. § 1639), the Real Estate Settlement Procedures Act (12 U.S.C. § 2601-10), the S.A.F.E. Mortgage Licensing Act (12 U.S.C. §§ 5101-16), the Truth in Lending Act (15 U.S.C. § 1601 *et seq.*), and the Truth in Savings Act (12 U.S.C. § 4301 *et seq.*).

The CFPA may, for example:

- prohibit or impose conditions on binding arbitration provisions in contracts between covered persons and consumers (Section 1025);
- prescribe rules to prevent a person from committing or engaging in an unfair, deceptive, or abusive act (Section 1031);
- require covered persons to make disclosures and communications to consumers (Section 1032);
- prescribe rules and issue orders and guidance regarding sales practices to ensure that risks, costs, and benefits of consumer financial products or services are fully and accurately represented (Section 1033); and
- impose duties on covered persons in dealing directly with consumers that are appropriate or necessary to ensure fair dealing (Section 1037).

There are, however, limitations on these authorities. For example, no rule prohibiting an “unfair” practice under Section 1031 may issue unless “the act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers” and that such injury outweighs “countervailing benefits to consumers or to competition.” Likewise, required disclosures under Section 1032 must pass a balancing test for reasonableness.

The second aspect of the oversight power is information gathering, which is intended to ensure that covered persons are complying with the CFPA’s rules, orders and guidance. Section 1022(c) authorizes the CFPA to periodically examine or require reports from covered persons. Section 1052 grants the CFPA subpoena power, as well as the authority to issue “civil investigative demands,” which if not promptly complied with, can be enforced in federal court. In reports, the CFPA may require that covered persons disclose information about compliance systems or procedures, as well as “matters related to the provision of consumer financial products or services.” This notwithstanding, the CFPA must, “to the fullest extent possible,” rely on reports previously filed with federal agencies. To promote efficiency, the Act grants the CFPA access to reports of other regulators, as well as granting other regulators access to CFPA reports.

“Standard” or “Plain-Vanilla” Products

Section 1036 favors products with straightforward terms. It defines “standard consumer financial products or services” as those that:

- are or can be readily offered by covered persons that offer or seek to offer alternative consumer financial products or services;
- are transparent to consumers in their terms and features;
- pose lower risks to consumers;
- facilitate comparisons with and assessment of the benefits and costs of alternative consumer financial products or services; and
- contain the features defined by the CFPA for the product or service.

Under the Act, the CFPA may require covered persons to offer consumers a “meaningful opportunity to decline” a “standard” or “plain-vanilla” product or service before offering an “alternative” product or service. Although the definition of these “standard” products or services is quite broad, it very probably excludes adjustable rate

mortgages, complex derivatives, and similar non-standard financial products which have drawn much criticism for contributing to the current financial crises.

Enforcement

Section 1039 of the Act makes it unlawful for any individual to “advertise, market, offer, sell, enforce, or attempt to enforce, any term, agreement, change in terms, fee or charge in connection with a consumer financial product or service” not in conformity with the Act or with a rule or order issued by the CFPA. The CFPA will be authorized to enforce this provision through both its own hearings and adjudications and litigation. The Act enumerates several types of potential relief that a violation of the Act might justify.⁷ These include, but are not limited to, civil penalties. Under Section 1018(c)(1), all civil penalties that the CFPA obtains under the Act or the enumerated consumer laws are to be deposited into a victims relief fund, and ultimately paid out to consumers.

In addition, the Act extends whistleblower protection to employees and authorized representatives of covered persons.⁸ Claims of wrongful termination or discrimination are to be adjudicated before the CFPA, subject to judicial review.

III. Role of the CFPA as a Monitoring Agency

Section 1024(a)(1) requires the CFPA to “monitor for risks to consumers in the provision of consumer financial products or services, including developments in markets for such products or services.” It is authorized to do so through a variety of sources, including examinations of and reports from covered persons, and consumer complaints. It must publish at least one report annually of its significant findings.

The Act also imposes new recordkeeping requirements on banks and lending institutions. Section 1071 requires banks to keep records of all deposits and to organize those records according to the “geo-code” of the depositor’s address. Additionally, Section 1072 requires lending institutions to make note, when lending to small business, whether the business is “women- or minority-owned.” All such data is to be submitted annually to federal regulators in accordance with CFPA rules.

IV. Conclusion

If adopted by Congress, Treasury’s proposal would revolutionize the regulation of consumer financial products and services. The Act would consolidate the consumer protection functions of existing federal agencies in the CFPA, whose mandate would include new rulemaking and information gathering powers. The Act, as one piece of Treasury’s wide-reaching proposal to overhaul the American financial regulatory framework, is in harmony with the current political mood. Nevertheless, Congress has yet to adopt this proposed Act in part or in whole, and it remains to be seen to what extent Treasury’s vision will be realized.

⁷ Under Section 1055, such relief includes, but need not be limited to, rescission or reformation of contracts, refund of moneys or return of real property, restitution, compensation for unjust enrichment, payment of damages, public notification regarding the violation, limits on activities or functions, and civil money penalties. Exemplary or punitive damages are not available.

⁸ Section 1057 provides that “[n]o person shall terminate or in any other way discriminate against, or cause to be terminated or discriminated against, any employee or any authorized representative of employees by reason of the fact that such employee or representative has provided information to the Agency, filed, instituted or caused to be filed or instituted any proceeding [under the Act or ‘enumerated consumer laws’] or has testified or is about to testify in any proceeding resulting from the administration or enforcement of the provisions of this title.”

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Jon Mark at 212.701.3100 or jmark@cahill.com; or Ted B. Lacey at 212.701.3669 or tlacey@cahill.com.

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