

# Consumer Finance Monitor (Season 6, Episode 39): Federal Court Rules CFPB Cannot Use UDAAP Authority to Regulate Discrimination: A Close Look at the Decision and its Implications

Speakers: Alan Kaplinsky and Rich Andreano

Alan Kaplinsky:

Welcome to the award-winning Consumer Finance Monitor podcast, where we explore important new developments in the world of consumer financial services and what they mean for your business, your customers, and the industry. This is a weekly podcast show brought to you by the Consumer Financial Services Group at the Ballard Spahr Law Firm. I'm your host, Alan Kaplinsky, the former practice group leader for 25 years and now senior counsel of the Consumer Financial Services Group at Ballard Spahr, and I'm very pleased to be moderating today's program. For those of you who want more information, don't forget about our blog, [consumerfinancemonitor.com](http://consumerfinancemonitor.com). We've hosted the blog since 2011 when the CFPB became operational. So, there is a lot of relevant industry content there, particularly on the topic we're going to be talking about today. We have blogged about it from the very beginning and it's a blow-by-blow description of all the events leading up to what we're going to be focusing on today.

We also regularly host webinars on subjects of interest to those in the industry. So, to subscribe to our blog or to get on the list for our webinars, please visit us at [ballardspa.com](http://ballardspa.com), and if you like our podcast, please let us know about that. Leave us a review on Apple Podcasts, Google Play, Spotify, or wherever you obtain your podcasts. Also, please let us know if you have ideas for any other topic that we should consider covering or speakers that we should consider as guests on our show. So, let me tell you a little bit about the topic we're going to talk about today and then I will introduce our guest and we will dive into it. So, let's roll back the calendar to March 2022, a very important event occurred in March and during that month.

Consistent with our expectations that the CFPB under Director Chopra's leadership would take an expansive view of its statutory authorities, the CFPB announced its intention to use its authority to prohibit unfair, deceptive, or abusive acts or practices, the so-called UDAAP authority, and in particular the unfairness prong of the UDAAP statutory authority to target discriminatory conduct, even in instances where the fair lending laws, most importantly, the equal credit opportunity, may not apply. Specifically, the CFPB directed its examiners to apply the unfairness standard to any conduct considered to be discriminatory, such as in connection with denying somebody access to a checking account or access to any deposit account.

So, that is a very high level overview of what we're going to be talking about today, and I can't think of anybody more qualified to talk about this subject than Rich Andreano, my good colleague. Rich is the Practice Group Leader of the Mortgage Banking Group at Ballard Spahr and he's a member of the Consumer Financial Services Group. He's devoted over 35 years of practice to mortgage banking and consumer finance law. He advises mortgage and settlement service industries on regulatory compliance and related matters, which also assists clients with the implementation of the CFPB's small business loan data collection and reporting rule, the so-called 1071 rule. Pertinent to the topic we're going to be talking about today, I would say that Rich is one of our leading experts in the area of fair lending law, Equal Credit Opportunity Act, the Fair Housing Act, etc. So, Rich, a very warm welcome to you.

Rich Andreano:

Thank you very much, Alan. Glad to be here.

Alan Kaplinsky:

Okay. Let's get into this very interesting topic. So, I just said a couple of few words about the topic we're going to be talking about today. But tell us more specifically, what changes did the CFPB make in 2022 to its UDAAP exam manual?

Rich Andreano:

Yes. Prior to March 2022, the exam manual, which is not that long in general, talked about UDAAP in a general concept and had no mention of the concept of discrimination. In March, what the bureau did was insert the concept of discrimination as being covered by UDAAP. In particular, the unfairness prong. Now, under the UDAAP principle, something is unfair if it causes or is likely to cause substantial injury to consumers, the injury's not reasonably avoidable by consumers, and the injury's not outweighed by countervailing benefits to consumers or to competition, and that's the same definition that the FTC applies under section five of the Federal Trade Commission Act.

In the view of the bureau, discrimination is unfair and consumers cannot reasonably avoid it. Thus, it instructed examiners when reviewing companies and exams to look at their policies and procedures to see if they have addressed discrimination as to the offering of any consumer financial product or service, as you mentioned, Alan, could even be a deposit account, which is not within the reach of existing congressional fair lending laws, and also in assessing whether to offer new products and services, did the institution assess the risk of discrimination? So, it was really embedding discrimination concepts into any financial services product or service, and that's a very bold move because the bureau went way beyond the boundaries of anti-discrimination laws as defined by Congress.

Alan Kaplinsky:

Yeah. And interesting, Rich, isn't it, at least interesting to me, that they made this very big change by changing their exam manual? Technically speaking, the exam manual only applies to banks and non-banks that they supervise. Doesn't technically apply to anybody else. Why do you think they did it that way? Do you have any idea?

Rich Andreano:

What we found is Director Chopra in general prefers making statements through circulars, through exam manuals, through bulletins, and not actually adopting rules. They view the rulemaking process as being slow and cumbersome, so he'll just issue edicts as he did here. I know you and I both viewed this as in the first place, it's a rule. You can't just adjust your exam manual to expand the concept of UDAAP to discrimination. But this is consistent with the CFPB. They very much push their authority and they do it through informal measures, not through formal notice and comment rulemaking.

Alan Kaplinsky:

Right. Right. So, are you saying, Rich, that this, what they did in March of 2022, that that was the first time the CFPB had ever stated that the unfairness prong of UDAAP encompassed discrimination?

Rich Andreano:

Well, to the industry, this was new. But according to the bureau, this was not new. We'll get into in a little bit the lawsuit that was filed against the bureau on this issue. In its briefing, the bureau asserted that this isn't a new theory. Even without the exam manual update, we could have challenged discriminatory practices under UDAAP. That was a surprise to us because that exam manual change we thought was the first time the bureau had had ever mentioned it. But in its view, this was not a new theory.

Alan Kaplinsky:

So, tell us how, from a practical standpoint, and we're not up to the lawsuit yet, we're going to get into that in a few minutes, how did the changes that were made to the exam manual differ from fair lending and the discrimination prohibited by the Equal Credit Opportunity Act?

Rich Andreano:

Right. The bureau does have authority to enforce a ECOA, and that applies exclusively to credit, both to consumer credit and business credit. But that's the boundary. So, for instance, it doesn't apply to deposit products or other non-credit products, whereas the bureau's position under UDAAP is any consumer financial product or services is covered by UDAAP and thus

subject to assessments based on discrimination. So, it was a tremendous expansion of the boundaries of fair lending laws drawn by Congress. There's also the Fair Housing Act, which applies more to housing related credit and other housing related services. That's in the purview of the Department of Housing and Urban Development and Department of Justice. So, this was the bureau looking at ECOA and just saying, "No, that's not broad enough. I want to reach discrimination as to anything I can touch, and so I'll use UDAAP to do that." It would significantly, that position, expand the scope of anti-discrimination laws beyond what we think Congress ever envisioned.

Alan Kaplinsky:

Tell us, there's one other thing that I thought was very significant. Under the Equal Credit Opportunity Act, as you pointed out, deals with credit, consumer credit, business credit, but it only protects certain classes. It doesn't protect everybody. So, can you tell, it bears repeating, I think, for our audience, who's protected by ECOA and what changes were made by the exam manual in terms of what additional protected classes have been added?

Rich Andreano:

Yes. ECOA's very specific. It first was adopted to address discrimination based on gender because this was back in the '70s. It was very difficult for a single woman to get credit at all and also very difficult for a married woman to get credit on her own. The bank would ask, "No, you have to have your husband as a co-applicant or co-signer." Then it was expanded to include also age, race, ethnicity as well, and a few certain other matters, but very specific. The bureau's action has no such boundaries. It could address any basis of discrimination whatsoever. Now, the gender base has been interpreted based on Supreme Court decisions to apply to also sexual orientation or preference. So, that's not specifically set forth in the act, but is interpreted that way consistent with some Supreme Court authority. But here, the bureau, any basis it thinks up, it could determine as a prohibited basis of discrimination, so well beyond the neat categories that Congress has defined.

Alan Kaplinsky:

Yeah. Well, just provides some examples of kinds of things that at least theoretically could be encompassed by the exam manual.

Rich Andreano:

What you look at sometimes is state laws often go beyond where EOA or the Fair Housing Act particularly goes. For instance, they might include veteran status, that you can't discriminate someone on the basis that they are or are not a veteran of the services. Now, if a state wants to do that under its authority, that's perfectly fine. Congress has chosen not to go there. So, for the bureau to basically say, "We could reach discrimination on the basis of whether or not you are a veteran," or really any other basis that they think up is quite extraordinary.

Alan Kaplinsky:

Yeah. Well, the thing I always think of, Rich, and I'm very familiar with this practice, a lot of community banks around the country, they only want to do business with people who live within their local community. They don't want to do business with people who live in the other 49 states, and sometimes they only want to do business with people who live within a certain defined area, a county or places where they have branch offices. So, I guess that's a kind of geographic discrimination not covered by ECOA, but it seems like it could be covered by this change to the exam manual.

Rich Andreano:

Potentially, even though when you read Dodd-Frank, what clearly comes through is they wanted to protect the community banks and make sure that Dodd-Frank wasn't too onerous on them, and that the relationship banking approach seemed to be something Congress approved of and was not responsible for the crisis that resulted in Dodd-Frank. So, here, you have Congress favoring a model of banking that the bureau potentially could attack under this UDAAP theory.

Alan Kaplinsky:

Yeah. So, let me ask you this. There's been a lot of, I guess you could say, pushback by consumer advocacy groups. I'm thinking in particular Professor Sovern at University of Maryland, formerly at St. John's, who said, "This is nonsense. The industry, of course, discrimination is unfair, right?" Everybody would say if you were to go up to the man in the street and you'd say, "Is it unfair to discriminate against somebody based on anything, race, gender, etc., etc.?" the answer I think would undoubtedly be, "Of course it's unfair to do that." Right? So, how do you respond to that, Rich?

Rich Andreano:

Yeah, and it is. Without question, discrimination is unfair. The issue, though, is not whether discrimination as a generic concept is unfair. The issue is really whether you can take general UDAAP principles and apply them to expand discrimination beyond specific laws adopted by Congress. Important underlying principle here, what sets us apart from many countries is we're governed by the Constitution. People when they take oath, they don't give oath to the President of the United States. They give an oath to the Constitution and we live by the rule of law. That is a very important concept. So, the principle there, though, is also we follow laws, we're governed by laws, and laws should be applied as intended by the legislature. Now, let's take the bureau's view, which has a certain basic attraction that, well, discrimination is unfair, so we can use UDAAP to get at discrimination.

Following that, though, the bureau can expand its authority wherever it wants to go. Let's take an example. One could also argue that a company with excessive market power could use that power to be unfair to consumers. Using the bureau's theory could then say, "Well, because of that, I can use UDAAP to enforce basic antitrust principles." Now, I think anyone would look at that and say, "Well, no. Congress has authorized only specific agencies under specific acts to exercise antitrust principles. We never meant for the bureau to do that under UDAAP." The application of UDAAP to discrimination is exactly the same thing. Now, I get it. Maybe Congress has not expanded discrimination laws as broadly as would be proper, but that's purview of Congress, which is the legislative body. It's not the purview of the CFPB, which is an executive agency.

Alan Kaplinsky:

Right. So, how did the industry, the banking and the consumer finance industry, react to what the CFPB had done? I know that we immediately wrote a highly critical blog. I remember when we did it, and we basically said, "This is never going to stand up. It's going to be challenged, be thrown out." I guess you could say there was a hue and a cry.

Rich Andreano:

Yeah. Shock and then anger were the initial reactions, and a group of trade associations, including the US Chamber of Commerce, American Bankers, and others, first tried to address this in a diplomatic way with the bureau. They actually wrote a whitepaper and submitted that to the bureau and engaged with the bureau really explaining that Congress and Dodd-Frank was relatively specific. It treated discrimination in UDAAP as separate concepts. In other words, if you look at Dodd-Frank, it's pretty clear Congress never intended for UDAAP to cover discrimination. It viewed discrimination as a separate concept that it had specific laws that it authorized the bureau to address, but the CFPB was unmoved by that in treaty by the trade association. So, they left the associations no choice but to file a lawsuit, and as is common nowadays, that lawsuit was filed in a federal district court in Texas, which has been very favorable to challenges against the bureau.

Alan Kaplinsky:

Right. So, that's a nice segue, Rich, into a discussion of that lawsuit. So, the Chamber of Commerce, American Bankers Association, Consumer Bankers Association. I guess there were some other trade associations.

Rich Andreano:

Typically a local one in Texas, which becomes very important in the case.

Alan Kaplinsky:

Yes. Absolutely. Maybe, was there an individual bank too, or were they all trade associations?

Rich Andreano:

Unlike other suits where they involved individual, I think this was all trade associations.

Alan Kaplinsky:

Anyway, what were the claims? You're right, it got filed in the Eastern District of Texas, got assigned to a judge, a pretty young judge, looking into his background recently, who's only been on the bench for three years, appointed by former President Trump. Certainly, if you look at his background, I would say a conservative leaning judge for sure. What claims did the plaintiffs make in that lawsuit?

Rich Andreano:

Well, there were four claims made by the plaintiffs. Importantly, this court sits in the Fifth Circuit and earlier this year, the Fifth Circuit ruled that the CFPB funding structure is unconstitutional as violating the Appropriations Clause. The Supreme Court has decided to hear that case based on petitions by parties in that case and very soon, we will hear all arguments, October 3rd. Then since this is a very significant case, usually the Supreme Court waits to the end of its term to release opinions in significant cases, which would be June 2024. So, that was one claim. But there were three other claims, all of which I think were appropriate claims to bring. One, the very basic one is bureau, you don't have the statutory authority under Dodd-Frank to use your UDAAP power to reach discrimination. Congress has specifically authorized when you could reach discrimination, and they did not do so here.

Next, Administrative Procedure Act claim, these changes were arbitrary and capricious, which is a basis to strike down an agency action, be it a rule or an informal action like this. Then finally, as we thought, this is a rulemaking, so even if you had authority to do this, which we don't think you do, the only way you could do this is through notice and comment rulemaking under the Administrative Procedure Act. So, what they did, they asked the court, "Please rule in favor on all our claims. Please enjoin and set aside this manual update." But they also, specifically for their members of the trade associations that were plaintiffs, asked for an injunction preventing the bureau from pursuing this theory that you could use UDAAP to address discrimination against any of their members.

Alan Kaplinsky:

Well, in fact, just to clarify something, you're quite right. They did seek injunctive relief that would only benefit their members. But their primary argument was to seek injunctive relief that would protect anybody who was covered by this rule.

Rich Andreano:

Yes. Oh, yeah. The court, what they did is while seeking the injunction that would prevent the bureau from enforcing this theory against their members, they basically wanted the exam manual set aside. So, basically a ruling that it's vacated, it doesn't exist anymore.

Alan Kaplinsky:

Right right. Procedurally, as I understand it, the opinion that was decided by the court came up in the context of cross motions for summary judgment. What I can't understand, at least from my review of the docket and the filings, why do you suppose the CFPB didn't just say to this judge, "Let's put this case on ice, pending the outcome in the Supreme Court of the CFSA vs. CFPB case"? Why do you suppose the CFPB was in such a big hurry to get a decision in federal court in Texas from a conservative judge?

Rich Andreano:

That is a puzzling issue. I could see why the bureau may have wanted to pursue this theory, but I would've thought another forum would be more favorable for getting a positive ruling because I just didn't see the CFPB winning on this. Now, perhaps they really believed in their position and thought they could win, knowing they would have to lose on the Appropriations Clause claim because the court had to rule based on the Fifth Circuit that it had no discretion there. But it looked like they were trying to get the court to say, "No, this is something the bureau could do," and I just don't think that was anything this court was ever going to rule. Perhaps a court in another jurisdiction might have, and that's why I thought this was peculiar that the bureau really moved forward and wanted a ruling.

Alan Kaplinsky:

Yeah. Now, the bureau asserted a bunch of defenses at the beginning, which seemed to be maybe technical defenses, but unlikely to work, like, am I right, lack of standing of the trade associations?

Rich Andreano:

Lack of standing. One of the ones, the bureau generally, I think, in this case, acted in a peculiar manner in general. One, it asserted sovereign immunity, said, "Yeah, well, you can't sue the federal government," which you mean I can never challenge any rulemaking or other action by an entity? It was kind of silly and the court easily backhanded that saying, "No, this is a final agency action under the Administrative Procedure Act, which has an exemption that permits the government to be sued for final agency action." So, the court relatively easy backhanded that claim.

The standing one, the Plaintiff Trade Association said, "Our members are being injured by this action because they're expending funds now to comply with this guidance that we think is illegal." Oddly, apparently the bureau introduced no evidence to refute that claim. So, the court said, "Well, based on their assertions, bureau, that you didn't object to, they have standing. I'm going to deny your claim." Then strangely, and this is where we made reference to one particular Chamber of Commerce member that was added to this suit as a plaintiff, the bureau said, "Venue's not proper. This isn't the right court," and the court said, "No. Longview Chamber of Commerce is one of the plaintiffs and it's a resident of the jurisdiction of this court. So, venue is proper." So, very peculiar claims. I'm not sure why the bureau made any of them because it was very unlikely to win.

Alan Kaplinsky:

Then the other thing that I sort of chuckled about, Rich, was as the judge started dealing with the various defenses that the CFPB had put up, they said, and the CFPB never argued that this court should defer to the changes in the exam manual, and then they said, and therefore they've waived their deference argument.

Rich Andreano:

Exactly. They said under the Supreme Court case in Chevron, where although that principle is going to be addressed by the Supreme Court also this term, but it's a basic principle that if a law is ambiguous, then the agency has some discretion to interpret that, although the interpretation must be reasonable. But that deference can be forfeited, and apparently the court believes the bureau forfeited that deference because it didn't make the argument. Again, peculiar activity by the bureau in this case.

Alan Kaplinsky:

Yeah. Yeah. Almost seems like the litigators from the CFPB or whoever was litigating the case, they were not at the top of their game. At least that's my reaction to what I read. So, let's now talk about the opinion. The opinion came down, I think it was on late Friday, September 8th, and I happened to be attending a American Power Association Committee on Consumer Financial Services Committee meeting in Chicago. The lawyer from the American Bankers Association who was managing the litigation was there, and I was sitting in the lobby and he came by me. It almost looked like he just won the multi-billion dollar

lottery. He was literally walking on air. So, I then over the weekend spent my time writing the blog. So, let's talk about what the court did on the merits, getting beyond these procedural defenses that the CFPB raised.

Rich Andreano:

Now, interestingly in this, because we were sitting, this court was sitting in the Fifth Circuit, which had ruled that CFPB's funding structure violated the Appropriations Clause, the bureau actually conceded that if the court reached that argument, it had to rule for the plaintiffs, given the fifth Circuit binding precedent. But they preserved their argument that we think the Fifth Circuit is wrong. But the court said, "Yeah, I'm granting summary judgment to the plaintiffs on the Appropriations Clause claim because I have to based on the Fifth Circuit precedent." Now, the court noted that ordinarily, that ruling would've disposed of the case, and so it normally wouldn't have proceeded onto the three other claims. But they said there's a compelling reason to do so here. That compelling reason is the Supreme Court is going to decide the Appropriations Clause issue. It may well rule that the CFPB's funding structure it's constitutional, which then would throw out my ruling here on the Appropriations Clause. So, I need to address at least one of the other substantive claims made by the plaintiffs.

Alan Kaplinsky:

Do you recall whether the CFPB opposed that? Did they just want the judge just to rule on the constitutional issue and just let it go at that?

Rich Andreano:

As I recall, it conceded the position on the Appropriations Clause, but I can't remember if it said don't decide any of the other issues if you rule on the Appropriations Clause issue.

Alan Kaplinsky:

Yeah, It seems to me, again, if I were litigating for the CFPB, I would say, "Well, Judge, again, let's stay the remainder of the case. Let's leave the rest of it open. Let's see what happens, and you can deal with that after the Supreme Court rules." But they didn't and the judge seemed like he was anxious to get to the other issues. So, tell us, what did he say about the other issues?

Rich Andreano:

What he decided was to decide only one of them, and that was the statutory authority, which became very important in here because what the court determined that this issue presented the major questions doctrine, although the court referred to it as the major questions canon, and basically, that comes down from Supreme Court rulings, and the basis of it is that courts will presume that Congress does not delegate to executive agencies issues of major political or economic significance. In other words, that's the purview of Congress to adopt laws then directing agencies how to implement these major policies as specified by Congress and not leaving these matters to the discretion of an agency, and they say, "Look, whether the bureau has authority to police the financial services industry for discrimination against any group on any protected basis that the bureau deems proper is a question of major economic and political significance, and also, such agency authority would've significant political implications, both with regard to state and federal power."

So, it really said, "I'm going to apply the major questions doctrine here," and then quoted from the recent Supreme Court case in *West Virginia vs. EPA*, which is a case where the court most recently applied that doctrine to strike down an action by the EPA. What the quote was that something more than a merely plausible textual basis for the agency action is necessary. The agency instead must point to clear congressional authorization for the power it claims. One phrase describing this that I often like and refer to is that Congress does not hide elephants in mouse holes. When it wants to give broad authority to an agency, it does so very clearly with a clear grant of authority and not in vague, unclear terms.

So, the court believe here, look, Congress has very specifically addressed what conduct is prohibited by anti-discrimination laws, and the bureau's authority to prohibit discrimination based on desperate impact under UDAAP is something that Congress rarely authorizes. So, in other words, it said, "Look, I'm looking at this. The bureau has a really high burden to argue

that Congress conferred sweeping anti-discrimination authority without defining what are the protected classes or defenses, without using the words discrimination or disparate impact, and while separately giving the bureau under other laws authority to police discrimination," and said, "The bureau doesn't meet that bar. It doesn't have the statute authority authority to do what it tried to do."

Alan Kaplinsky:

Yeah. Let's now turn to the question of remedies. What did the court do?

Rich Andreano:

Yeah, and this is one we puzzled over ourselves and then reasoned the way to the explanation. The court first vacated the exam manual update, meaning it's as if it never existed. But even though it did that, it then went and enjoying the bureau from pursuing this theory in the supervisory or enforcement context against any members of the plaintiff trade associations. That's what we scratched our head about going, "Why did it need to do that if the manual update no longer exists?" There was a reason. As we noted before, the bureau in its briefing of the case was of the view that, oh, this isn't a new theory applying UDAAP to discrimination. We could have done that even without this exam manual update. We were only clarifying in the exam manual that this theory exists. So, the plaintiffs specifically didn't want the bureau even without the exam manual to argue this theory against any of its members. So, they specifically asked for that injunction.

Alan Kaplinsky:

Yeah. In a way, the CFPB sort of got hoist on their own petard because in their briefing, they were the ones that went out of the way to diminish the significance of the exam manual changes and they said, because in their zeal to show that this is not something new, this idea of unfairness equals discrimination, and they said the exam manual update, that's just talks about what the examiners are going to look at, specifically the procedure that they're going to follow, etc., etc. But the law here emanates from the UDAAP provision itself in Dodd-Frank and that scared the hell out of the plaintiffs in the case thinking that simply vacating the exam manual, that might not be enough. They might still feel they could go after members of our associations quite apart from the changes to the exam manual based on UDAAP itself.

Rich Andreano:

That's correct. So, in theory, could the bureau still say that even without the exam manual, we could apply this theory to parties who are not members of those plaintiff trade associations? Theoretically, it could. I think the court's reasoning though is quite good and I think will have some influence on other courts, should that issue come up either in this context or in other major questions contexts.

Alan Kaplinsky:

Right. So, anyway, that's what the court did. Let me ask you the next question. What do you think the CFPB does now? Do they drop this case? Do they appeal to the Fifth Circuit? It almost feels like you're going into the lion's den, right, if you're the CFPB. What do you think?

Rich Andreano:

Yeah. Using a football term, an appeal to the Fifth Circuit would be a Hail Mary. It's just, they're not going to get a favorable ruling in that court. Again, the district court's decision is very well reasoned and to us makes perfect sense, and I don't think they'd get any other result than what the district court ruled. They perhaps might even get language that's even harsher. If I were them, I would stand down on the matter, wait to see what the Supreme Court does on the Appropriations Clause issue, and then go from there. I don't think pursuing this at this point is the right thing.



Alan Kaplinsky:

Do you think it's necessary for non-members of the trade associations to do what they have been doing in connection with the rule, the 1071 rule and the litigation challenging that? I'm referring to the small business data collection rule. There, it's similar situation in that the injunction was limited just to the plaintiffs and their members, and we have seen almost an avalanche of other trade associations seeking to intervene, CFPB is allowing them to intervene, and then filing their own motions for preliminary injunction. Do you think we're going to witness that here?

Rich Andreano:

This is different. In the case with the 1071 rule, that was an actual adopted rule that institutions need to start work on complying. Now, what the plaintiff members of the trade association in that case got was an extension because what the court said, for as long as this stays in effect, that period of time will delay the implementation date, assuming the bureau is ultimately allowed to impose that rule based on the Appropriations Clause issue or however that gets resolved. This is something where we don't have an actual rule that will go into effect. It would take additional CFPB affirmative action against someone who is not a member of one of these associations to enforce the UDAAP claim. So, I don't think the argument is compelling to seek to intervene. But certainly, if someone's facing this claim from the bureau, at that point, I would probably seek to intervene to get them to stop pursuing that action.

Alan Kaplinsky:

I had heard, I can't confirm this, Rich, that sometime after the changes to the exam manual were made, up to a current date, the CFPB had issued CIDs to several institutions. I don't know who they are, and even if I did, I wouldn't mention any names. But they were seeking to enforce the changes to the exam manual. What do they do now? You think they just do nothing? They just wait, wait it out?

Rich Andreano:

Yeah. I think if I'm looking at that sort of a CID, if the bureau still intends to pursue it, then I think I'm intervening in the case at that point to get protection to have them from pursuing that action. If the bureau indicates it's standing down on the issue, then I think we wait. You'd wait and see what happens.

Alan Kaplinsky:

Yeah. Yeah. Yeah. I agree with you. I think that is exactly what's going to happen. Now, let me ask you, I know you're more of a regulatory lawyer and not a litigator, but I know that you talk to the litigators very frequently in our consumer finance group. Would the CFPB be able to, let's say, bring an enforcement action somewhere in the Second Circuit against a company that it thinks has violated its view of what UDAAP encompasses, namely that encompasses discrimination, and seek a ruling from a different judge who may be more favorably inclined toward the views of the CFPB? We do know, for example, the Second Circuit has issued a ruling saying that it disagrees with the Fifth Circuit about the funding issue. How do you view that? Do you think that is something that they could do and do you think it's something that they're likely to do, or do you think they will keep their powder dry, so to speak?

Rich Andreano:

We ran this issue by our colleague, Burt Rublin, who said, no, he thinks the Texas Court ruling doesn't preclude the bureau from pursuing this action. In other words, there's no collateral estoppel. A very good example is the Second Circuit where the Fifth Circuit had ruled that the CFPB's funding was unconstitutional, the matter was being litigated in the Second Circuit, and the Second Circuit didn't find itself estopped from deciding the issue, and it did, and it disagreed with the Fifth Circuit. So, certainly, the bureau could go into another jurisdiction, such as the Second Circuit, and enforce this position. Whether it will be an interesting question because I think it would immediately face a legal challenge, and again, the court's reasoning is quite good. I'm not sure it would get a different outcome.

Alan Kaplinsky:

Yeah. Sure. Sure. So, let's talk about some of your other observations you have about this case or the takeaways from the opinion and what happened here.

Rich Andreano:

Yeah. The Appropriations Clause ruling, really, that's going to be the Supreme Court. So, the Supreme Court will have the final judicial say on that issue, and depending on how it rules, particularly if it rules the funding's unconstitutional, it's then going to be handed to Congress to come up with a legislative solution. So, that part of the ruling is going to be resolved by other means. The statutory authority part of the ruling, I think, is the most significant because it addresses the major question doctrine, which is relevant not only to the bureau, but any other federal agency in trying to assert broad authority when Congress has given a maybe not so clear authorization. I think that has more significance. For instance, as we noted earlier, the FTC also has unfair and deceptive actor practice authority under section five of the Federal Trade Commission Act. Will this ruling cause the FTC not to try to assert that unfairness covers discrimination?

Alan Kaplinsky:

Am I right, Rich, they've already asserted that, right?

Rich Andreano:

Yeah. They haven't been quite aggressive as the bureau, but they asserted that position. That position now obviously is in question. So, do they back off from that position or do they go full speed ahead in trying to assert the position? That will be an interesting factor to watch what they do. Also, UDAAP can apply to almost anything, and the bureau apparently thinks it does. For instance, it's also opined that it could use its UDAAP authority to address data security issues, even though the Federal Trade Commission Act actually has the data security authority under Gramm-Leach. So, will the industry now be more inclined to push back on the bureau when it makes broad assertions?

That may well be the case because again, it's a well-reasoned decision and I think one I could easily see other courts going to with similarly broad expressions of bureau authority. The real interesting issue as to the bureau's UDAAP authority in general is let's say the Supreme Court does find their funding structure to be unconstitutional, and then the matters before Congress. As I say, at that point, it's where the horse-trading begins. It's to address the measure legislatively. What other actions regarding the CFPB might members of Congress want to agree to fund the CFPB going forward? One thing I think that very much may be looked at is reigning in the bureau's UDAAP authority. That is something that does concern a lot of members of Congress. So, I could see future legislative action there not to give them authority to pursue discrimination, but to in fact restrict their authority under UDAAP.

Alan Kaplinsky:

Right. Right, and there are some other regulations that will probably get promulgated before year end. There are a couple of registries that the CFPB has proposed that I think they're likely to finalize. Do you think that's vulnerable as a result of this opinion?

Rich Andreano:

I think so. Dodd-Frank does have the concept of a registry that the bureau can require registration, but I'm not so sure Congress envisioned this contract clause registry or administrative order registry that would impose significant burdens on registrants both to implement and then to annually update. I don't get it that Congress thought that that's what was granting the CFPB the power to do, so I would expect them, although I think it's likely they're going to adopt these registries, I think it's then very likely that both registry requirements will be challenged in court and the major questions doctrine will be front and center.

Alan Kaplinsky:

And the lawsuit will probably be filed in federal court in Texas.

Rich Andreano:

In Texas. Yes. I would put odds on that. Exactly.

Alan Kaplinsky:

There are other rule makings, I think, that aren't at least subject to the same precise kind of a challenge, namely, I think before the end of the year, the CFPB will finalize its credit card late fee, the changes to that regulation. That's been very controversial because in the proposal, they proposed to create a safe harbor of \$8, and they did that with essentially no data supporting that, or if they have data, they haven't shared it with anybody.

So, I've had clients ask, will that get thrown out? Well, certainly the funding, the constitutional issue is the same. That will apply. But in the credit card late fee litigation, at the credit card late fee reg, the source of the authority isn't UDAAP. It comes from the Card Act, which is a different part of the Dodd-Frank Act. Same thing with the open banking regulation. There is a separate provision in Dodd-Frank giving the CFPB, at least theoretically, the power to issue a regulation dealing with open banking. So, I guess it's sort of a mixed bag. The constitutional issue will apply to anything that they do. But you have to take a close look at the statutory authority to figure out whether it's vulnerable. Someone also asked me, what is the effect of anything on the Townsend redlining case? Maybe you could just tell people very briefly what that case is about.

Rich Andreano:

Sure. This is a case where the bureau filed ... It was first time ever a redlining complaint was filed against a non-bank mortgage company, Townstone Financial, as they wouldn't settle. So, the bureau went and sued them, and the theory was it was brought under ECOA, that ECOA applies to pre-application activity, particularly Reg B. Not ECOA. ECOA refers to applicants. Reg B also refers to discouraging prospective applicants. On that theory, the bureau brought a redlining claim saying that by not lending in particular areas, not marketing in particular areas and such, you're discouraging people in those areas from applying. A district court in Illinois looked at it and said, "No, ECOA's clear. It only applies to applicant's. Bureau, you cannot use ECOA to bring a redlining claim." Bureau, I would've advised against this, decided to appeal to the Seventh Circuit, which will hear the issue. We think the correct ruling is that ECOA does not apply to pre-application activity. The court may read this decision, but I think it's we're going to decide it on the four corners of ECOA is can you read that statute as written, which only uses the word applicant and not prospective applicant or potential applicant or anything like that.

Alan Kaplinsky:

Am I right that the claim, well, this is a lawsuit brought by DOJ or the CFPB?

Rich Andreano:

Just the CFPB. Yeah. The bureau had referred the matter to DOJ, and the DOJ is the Fair Housing Act. The Fair Housing Act has much more conducive language to bring a redlining claim. But the DOJ just said, "This case isn't worth pursuing. Why are you pursuing this case, bureau? We're not going to take it up."

Alan Kaplinsky:

Right. They didn't, interestingly enough, Rich. Am I right that their entire case is predicated on ECOA? They didn't bring a UDAAP claim, right?

Rich Andreano:

No. No, although one thing we surmised is because of this case, did the bureau come out with its UDAAP position realizing it risked losing the ECOA claim, and that way it could attack red lining as a UDAAP theory?

Alan Kaplinsky:

Well, and I guess I would say to the CFPB, well, you've said that UDAAP encompasses discrimination, that that's existed forever, ever since the enactment of UDAAP and Dodd-Frank, and for the FTC Act, it goes back even further. If it's such a well established principle, why in the world did you not include account in the complaint dealing with UDAAP?

Rich Andreano:

Yep. Very interesting. It's purely ECOA, and so the odds are that this one way or another will end up going up to the Supreme Court, and I don't think the bureau will like what the Supreme Court does with the issue.

Alan Kaplinsky:

Yeah. That's another good bet. So, CFPB is getting slapped around a lot, Rich. They seem to be losing a lot of major issues, the 1071 case, this case. They're not doing so well in court. Do you see them going into more a shell or do you think that they just can't do it, it's just not the nature of A CFPB as led by Rohit Chopra, that his attitude seems to be, "Bring it on, industry. I'm going to do what I want to do. You file lawsuit. I love your lawsuits. We'll go to court"? Is that going to change?

Rich Andreano:

Yeah. I think using a military phrase and knowing Director Chopra probably said, "Damn the torpedoes. Full speed ahead." I don't think this will affect him one bit. He's going to do what he wants and if you want to sue him, sue him. They'll then fight it in court, they shrug off losses, and keep going.

Alan Kaplinsky:

Yeah. Even though, at some point, he gets an adverse ruling in the Supreme Court, he may have to go hat in hand to Congress, and this is not, I think, helping him politically.

Rich Andreano:

No. No. I think their aggressiveness will certainly, I think, influence the Supreme Court in the Appropriations Clause case because I think that court, the conservatives in that court clearly don't like the concept of unbounded regulators doing things beyond the authority granted by Congress or beyond the direction of the President. So, the thinking is they're going to use this opportunity to reign in what they probably perceive as regulatory overreach by saying their funding is unconstitutional. So, this ruling will force them, as you said, to go hat in hand to Congress every year to seek an annual appropriation.

Alan Kaplinsky:

Okay. Well, we've reached the end of our program today, Rich. First of all, let me thank you very much for taking the time to share your thoughts about this case, and I will tell our audience we will be continuing to follow all developments related to this. So, you need to only consult our blog. So, thank you again, Rich.

Rich Andreano:

You're quite welcome.

Alan Kaplinsky:

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