UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

STATE NATIONAL BANK OF BIG SPRING *et al.*, Plaintiffs,	)	
v.	)	Case No. 1:12-cv-01032 (ESH)
JACOB J. LEW, in his official capacity as United States Secretary of the Treasury and *ex officio* Chairman of the Financial Stability Oversight Council, *et al.*,	)	Judge: Hon. Ellen S. Huvelle
Defendants.	)	

PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT

Pursuant to Federal Rule of Civil Procedure 56, Plaintiffs State National Bank of Big Spring, the 60 Plus Association, Inc., and the Competitive Enterprise Institute hereby respectfully move for summary judgment, including a declaration that the Consumer Financial Protection Bureau (CFPB) is unconstitutional, the January 2012 recess appointment of Richard Cordray was unconstitutional, and all CFPB regulations promulgated during the time of Cordray's illegal appointment and that impact plaintiffs are invalid and cannot be enforced against plaintiffs.

The grounds supporting this Motion are set forth in the accompanying Statement of Undisputed Material Facts and Memorandum of Points and Authorities in Support of Plaintiffs' Motion for Summary Judgment.

Dated: November 6, 2015

Respectfully submitted,

/s/ Gregory Jacob

Gregory Jacob (D.C. Bar 474639)
O'MELVENY & MYERS LLP
1625 I St. NW
Washington, D.C. 20006

(202) 383-5110
(202) 383-5413 (fax)
gjacob@omm.com

C. Boyden Gray (D.C. Bar 122663)
Adam J. White (D.C. Bar 502007)
BOYDEN GRAY & ASSOCIATES P.L.L.C.
1627 I St. NW, Suite 950
Washington, D.C. 20006
(202) 955-0620
(202) 955-0621 (fax)
adam@boydengrayassociates.com

Counsel for Plaintiffs State National Bank of Big Spring, the 60 Plus Association, Inc., and the Competitive Enterprise Institute

Sam Kazman (D.C. Bar 946376)
Hans Bader (D.C. Bar. 466545)
COMPETITIVE ENTERPRISE INSTITUTE
1899 L St. NW, Floor 12
Washington, D.C. 20036
(202) 331-1010
(202) 331-0640 (fax)
skazman@cei.org

Co-counsel for Plaintiff
Competitive Enterprise Institute

Certificate of Service

I, Gregory Jacob, hereby certify that on November 6, 2015, I electronically filed the foregoing through the CM/ECF system, which will send a notice of electronic filing to counsel for the Defendants.

/s/ Gregory Jacob

Gregory Jacob
O'Melveny & Myers, LLP
1625 Eye St., NW
Washington, DC 20006
Telephone: (202) 383-5300
Facsimile: (202) 383-5414
Email: gjacob@omm.com

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MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT

GREGORY JACOB
Counsel of Record
O'MELVENY & MYERS LLP
1625 I St. NW
Washington, DC 20006
(202) 383-5300
gjacob@omm.com

C. BOYDEN GRAY
ADAM J. WHITE
BOYDEN GRAY & ASSOCIATES
1627 I Street NW, Suite 950
Washington, DC 20006
(202) 955-0620
adam@boydengrayassociates.com

Counsel for Plaintiffs State National Bank of Big Spring, the Competitive Enterprise Institute, and the 60 Plus Association

SAM KAZMAN
HANS BADER
COMPETITIVE ENTERPRISE INSTITUTE
1899 L St. NW, Floor 12
Washington, DC 20036
(202) 331-1010

Co-Counsel for Plaintiffs Competitive Enterprise Institute

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INTRODUCTION

The Consumer Financial Protection Bureau ("CFPB") was designed to be—and operates as—a government unto itself. It is vested with sweeping executive authority to make and enforce rules that affect virtually every sector of the U.S. economy. This authority is entrusted to a single individual, the Director, who serves a five-year term that is longer than the President's. Yet the Director does not answer to the President, who is prohibited from removing him from office except for cause. Indeed, the Director stands above the President, as by statute the Director's view of consumer financial protection law prevails over the President's if the two disagree.

Further, unlike the President, who is checked in the exercise of his executive authority by his dependence on congressional appropriations to fund the government that he runs, the CFPB is exempted from Congress's power of the purse and accompanying congressional oversight. Indeed, the CFPB has been created as an entirely self-perpetuating entity, empowered to appropriate hundreds of millions of dollars annually from the Federal Reserve System for its own use, without approval or review from the legislative or executive branches. Nor did Congress stop at freeing the CFPB from external restraints; in the asserted interest of fostering energy and independence, Congress also eschewed the creation of any internal checks or balances within the CFPB, such as those that are afforded by a deliberative multi-member commission structure.

The Constitution does not permit the creation of such an entity. Rather, to protect individual liberty, the Constitution mandates a separation of powers that imposes checks, balances, and accountability on the exercise of governmental authority. In creating the

CFPB, however, Congress deliberately nullified these checks and balances in pursuit of a particular vision of expediency, efficiency, and the perceived virtues of having an *un*accountable agency placed in charge of enforcing consumer financial protection law. Whatever the merits of this policy objective, the Constitution does not permit the amalgamation of such sweeping and unchecked authority in a single executive entity. Certain features of the CFPB viewed in isolation may or may not be constitutionally permissible, but the combination cannot be reconciled with the text or structure of the Constitution. Fidelity to the Constitution requires that the CFPB be invalidated.

The CFPB's constitutional infirmities were significantly exacerbated between January 4, 2011 and July 16, 2013, during which period the CFPB's substantial executive authority was illegally exercised by Richard Cordray, an individual who was not legally serving as the CFPB's Director. The rules that Cordray promulgated during that period must be invalidated not only because the CFPB is unconstitutional, but also for the separate reason that they were promulgated by an individual who was not the Director of the CFPB.

BACKGROUND

I. THE PLAINTIFFS

State National Bank ("SNB" or "the Bank") is a community bank that has served Big Spring, Texas and other communities for over a century. The Competitive Enterprise Institute ("CEI") is a nonprofit organization dedicated to advancing the principles of individual liberty, limited government, and free enterprise. Towards those ends, CEI engages in research, education, and advocacy efforts involving a broad range of regulatory, trade, and legal issues. The 60 Plus Association is a non-profit, non-partisan seniors advocacy group devoted to advancing free markets.

In *State National Bank of Big Spring v. Lew*, 795 F.3d 48 (D.C. Cir. 2015), the D.C. Circuit held that "[t]here is no doubt that the Bank is regulated by the Bureau," and "therefore has standing to challenge the constitutionality of the Bureau." *Id*. at 53. It further held that "[f]or the same reasons that the Bank has standing to challenge the constitutionality of the Bureau, the Bank has standing to challenge Director Cordray's recess appointment." *Id*. at 54.

II. THE CFPB

The CFPB was created in 2010 by Title X of the Dodd-Frank Act.[1] Dodd-Frank vested the CFPB with exclusive jurisdiction to administer eighteen "Federal consumer financial law[s]" previously administered by myriad other agencies. 12 U.S.C. §§ 5481(12), (14), 5511. And Dodd-Frank further vested the CFPB with newly created authority to regulate or prosecute "unfair, deceptive, or abusive" consumer lending practices. *Id.* § 5531(a).

The CFPB is an "independent bureau" within the Federal Reserve System. *Id.* § 5491(a); *see also* 44 U.S.C. § 3502(5) (designating the CFPB as an "independent regulatory agency," and thus excluding it from E.O. 12866's process for regulatory review by the Office of Management and Budget). Yet the CFPB is not answerable to the Federal Reserve, as the Federal Reserve cannot intervene in any CFPB matter or

[1] Formally, the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

proceeding or appoint or remove any CFPB employee. *See* 12 U.S.C. § 5492(c). And the CFPB's Director enjoys the "defining hallmark of an independent agency": the President cannot remove him except "for inefficiency, neglect of duty, or malfeasance in office." 12 U.S.C. § 5491(c)(3); Rachel E. Barkow, *Insulating Agencies: Avoiding Capture Through Institutional Design*, 89 Tex. L. Rev. 15, 16 (2010) ("defining hallmark"). Moreover, the Director serves longer than a full presidential term, being accorded a minimum term of five years, and the authority to hold over in office indefinitely until the Senate affirmatively confirms a successor (or the President makes a genuine recess appointment). 12 U.S.C. § 5491(c)(1)-(2).

The CFPB is also entirely independent from Congress's power of the purse. Instead of relying on congressional appropriations to fund its activities, the CFPB is statutorily entitled to claim about $600 million annually from the Federal Reserve System.[2] Congress is prohibited even from attempting to "*review*" the CFPB's non-appropriated budget. *See* 12 U.S.C. § 5497(a)(2)(C) (emphasis added).

Dodd-Frank takes yet further steps to empower the CFPB Director to act without restraint or accountability. Eschewing the traditional, bipartisan "independent

[2] Specifically, the CFPB is entitled to up to 12 percent of the Federal Reserve's operating expenses. 12 U.S.C. § 5497(a). According to the CFPB, this amounts to $539 million in 2015 and $605.5 million in 2016. CFPB, *The CFPB Strategic Plan, Budget, and Performance Plan and Report* 21 (Feb. 2015), http://files.consumerfinance.gov/f/201502_cfpb_report_strategic-plan-budget-and-performance-plan_FY2014-2016.pdf.

commission" model, in which several commissioners check and balance each other,[3] the Act vests the agency's power in a single director. 12 U.S.C. § 5491(b)(1).

III. THE RECESS APPOINTMENT OF RICHARD CORDRAY

The President nominated Cordray to serve as the Director of the CFPB on July 18, 2011.[4] The Senate never consented to that nomination. Nevertheless, the President appointed Cordray to the position on January 4, 2012,[5] under the purported authority of the Recess Appointments Clause. The same day, the President unilaterally appointed three members to the National Labor Relations Board ("NLRB"), also under the purported authority of the Recess Appointments Clause. The Senate, however, was not in recess at the time. 157 Cong. Rec. S883–S8784 (daily ed. Dec. 17, 2011). To the contrary, it was in the midst of a three-day break between pro forma sessions. *Id*.

The NLRB recess appointments were challenged in court. In *NLRB v. Noel Canning*, the Supreme Court unanimously held that the President lacked the constitutional authority to recess appoint the NLRB members because the Senate was not

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[3] *See* Kirti Datla & Richard L. Revesz, *Deconstructing Independent Agencies (and Executive Agencies)*, 98 Cornell L. Rev. 769, 794 (2013) (describing benefits of independent commissions' multimember structure).

[4] Nikki Sutton, *President Obama Nominates Richard Cordray to Lead Consumer Financial Protection Bureau* (July 18, 2011, 3:55 PM), https://www.whitehouse.gov/blog/2011/07/18/president-obama-nominates-richard-cordray-lead-consumer-financial-protection-bureau.

[5] Press Release, White House, President Obama Announces Recess Appointments to Key Administration Posts (Jan. 4, 2012), http://www.whitehouse.gov/the-press-office/2012/01/04/president-obama-announces-recessappointments- key-administration-posts.

in recess on January 4, 2012, but was instead on a three-day break. 134 S. Ct. at 2550, 2556–57, 2573–78 (2014). For that reason, the Court invalidated the NLRB recess appointments as unconstitutional. *Id.* at 2557, 2578.

Prior to the Supreme Court's decision in *Noel Canning*, on January 24, 2013, the President re-nominated Cordray to serve as Director of the CFPB—the position in which he had purported to serve as a recess appointee since January 4, 2012. The Senate confirmed Cordray on July 16, 2013. 159 Cong. Rec. S5704–05 (daily ed. July 16, 2013).

During the period of Cordray's alleged recess appointment—that is, between January 4, 2012, and July 16, 2013—Cordray exercised final decision-making authority concerning numerous CFPB rulemakings. Many of those rulemakings impact plaintiffs, particularly SNB. The regulations that most directly impact SNB are the Electronic Fund Transfers Rule (Regulation E), 77 Fed. Reg. 6193 (Feb. 7, 2012), 77 Fed. Reg. 50,243 (Aug. 20, 2012), and 78 Fed. Reg. 30,661 (May 22, 2013); the Mortgage Servicing Rules Under the Real Estate Settlement Procedures Act (Regulation X), 78 Fed. Reg. 10,696 (Feb. 14, 2013); the Escrow Requirements Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 4725 (Jan. 22, 2013); the Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 6407 (Jan. 30, 2013); and the Integrated Mortgage Disclosures Under the Real Estate Settlement Procedures Act (Regulation X) and the Truth In Lending Act (Regulation Z), 77 Fed. Reg. 51,115 (Aug. 23, 2012) (NPRM, finalized Dec. 31, 2013, 78 Fed. Reg. 79,730).

The impacts of these rules are described in Plaintiffs' Statement of Undisputed Material Facts, filed herewith.

On August 30, 2013, Cordray published a one-paragraph "notice" in the Federal Register, "[t]o avoid any possible uncertainty" about the validity of the CFPB's actions taken during the period of his recess appointment. The notice purported to "affirm and ratify any and all actions" Cordray took on behalf of the CFPB during that time. 78 Fed. Reg. 53,734 (Aug. 30, 2013).

SUMMARY OF ARGUMENT

In a constitutional system that separates power among the legislative, executive, and judicial branches, "independent" agencies exist as a limited exception to that fundamental structural rule. The President has general power to "keep [agency heads] accountable" by "removing them from office, if necessary." *Free Enter. Fund v. Public Co. Accounting Oversight Bd.*, 561 U. S. 477, 483 (2010) (citing *Myers v. United States*, 272 U.S 52 (1926)). But Congress "can, *under certain circumstances*, create independent agencies" run by officers removable only for good cause. *Id.* (emphasis added) (citing *Humphrey's Ex'r v. United States*, 295 U.S. 602 (1935)).

Notably, the courts have not allowed this limited exception to swallow the general rule that checks, balances, and accountability are necessary elements of governance under our constitutional structure. In *Free Enterprise Fund*, the Supreme Court stressed that *Humphrey's Executor* represents the outermost limit on agency independence. 561 U.S. at 514 ("While we have sustained in certain cases limits on the President's removal power, the act before us imposes a new type of restriction[.]"). Thus, the Sarbanes-Oxley

Act violated the Constitution by creating an agency with two layers of independence from the President.

The Dodd-Frank Act crosses the constitutional line yet again—not by giving an independent regulatory agency an unprecedented double layer of insulation from the President, but rather by giving it an unprecedented double lack of accountability to the political branches. The CFPB has broad executive regulatory and enforcement powers, yet it has been structured to remove ***all*** meaningful executive, legislative, and internal checks. As a result, the CFPB is far more unaccountable and unchecked than the FTC of *Humphrey's Executor*.

Our constitutional system of government does not permit Congress to create self-perpetuating entities with broad powers to regulate and enforce that exist outside of, and are unanswerable to, both the executive and legislative branches. *See, e.g.*, Federalist No. 9 (Hamilton) ("The regular distribution of power into distinct departments [and] the introduction of legislative balances and checks …. are means, and powerful means, by which the excellences of republican government may be retained and its imperfections lessened or avoided."); *Free Enter. Fund*, 561 U.S. at 499. Yet the Dodd-Frank Act vests the CFPB with vast executive authority, exempts it from accountability to the political branches, provides no mitigating internal checks and balances, and allows it to make and execute law on its own *indefinitely* without further involvement or oversight by Congress or the President.

Congress evidently saw the CFPB's structural "independence" as a salutary feature that it hoped would make it more energetic and effective. But the libertyprotecting value of checks, balances, oversight, and accountability cannot be sacrificed at the altar of expediency. *Bowsher v. Synar*, 478 U.S. 714, 736 (1986) ("Convenience and efficiency are not the primary objectives—or the hallmarks—of democratic government."); *Free Enter. Fund*, 561 U.S. at 498 (separation of powers violations are not saved by perceived need for "technical competence" and "apolitical expertise" (quotations omitted)). Nor is the CFPB saved by the fact that Congress and the President jointly participated in its creation, as "[n]either Congress nor the Executive can agree to waive" the Constitution's "structural protection." *Freytag v. Comm'r*, 501 U.S. 868, 880 (1991); *Free Enter. Fund*, 561 U.S. at 498.

The Government may attempt to defend the CFPB with a piecemeal approach: pointing to a single structural feature of the CPFB (e.g., for-cause removal protection), and citing cases in which the courts have endorsed that specific feature, in isolation. Neither this Court nor the Supreme Court has ever blessed the unprecedented combination of sweeping executive powers and stripped-away constitutional restraints that is embodied in the CFPB, however. That combination must be viewed by this Court *as a whole*, and when so viewed it cannot be reconciled with the constitutionally required separation of powers. *Ass'n of Am. R.R. v. DOT*, 721 F.3d 666, 673 (D.C. Cir. 2013) ("just because two structural features raise no constitutional concerns independently does not mean Congress may combine them in a single statute"), *rev'd on other grounds*, 136 S. Ct. 1225 (2015); *Free Enter. Fund*, 561 U.S. at 496 ("This novel structure does not merely add to the Board's independence, but transforms it."). The CFPB is unconstitutionally constituted, and Title X of the Dodd-Frank Act must be declared invalid.

In addition, plaintiffs seek redress for the multiple occasions between January 2011 and July 2013 when the CFPB's rulemaking authority was illegally exercised by Richard Cordray, an individual who was not then legally serving as the CFPB's Director. The illegality of Cordray's January 2011 recess appointment is definitively established by the Supreme Court's decision in *Noel Canning*. During the roughly eighteen months that Cordray was illegally exercising the CFPB's various authorities, he promulgated several rules that harm plaintiffs. Although Cordray later attempted to retroactively bless his illegal actions through a statement published in the Federal Register, no doctrine permits rules that were illegally promulgated in violation of statutory requirements to be rendered legal through such a notice. The rules in question must accordingly be invalidated—not only because the agency that promulgated them is unconstitutional, but also for the independent reason that they were promulgated by an individual who was not the Director of the CFPB, in violation of statutory requirements.

ARGUMENT

I. CONGRESS VESTED THE DIRECTOR OF THE CFPB WITH BROAD EXECUTIVE AUTHORITY, BUT PLACED HIM OUTSIDE THE PRESIDENT'S OVERSIGHT AND CONTROL

A. The CFPB has expansive executive authority.

The Dodd-Frank Act vests the CFPB with broad authority to exercise executive power in its designated domain. The CFPB has the power to "establish the general policies of the [CFPB] with respect to *all executive and administrative functions*," including "implementing the Federal consumer financial laws through rules, orders, guidance, interpretations, statements of policy, examinations, and enforcement actions"; deciding on the appropriate "use and expenditure of funds" for those purposes; "coordinat[ing] and oversee[ing] the operation of all administrative, enforcement, and research activities of the [CFPB];" and "performing such other functions as may be authorized or required by law." 12 U.S.C. § 5492(a)(4), (9), (10), (11) (emphasis added). Among these broad powers, Dodd-Frank grants the CFPB exclusive jurisdiction to administer eighteen "Federal consumer financial law[s]" previously administered by other agencies, 12 U.S.C. §§ 5481(12) & (14), 5511, and further vests the CFPB with newly created authority to regulate and prosecute "unfair, deceptive, or abusive" consumer lending practices. *Id.* § 5531(a). In sum, the core purpose of the CFPB is "to implement and, where applicable, enforce Federal consumer financial law," *id.* § 5511(a)—that is, to "take Care that the [Federal consumer financial laws] be faithfully executed," *see* U.S. Const. Art. II, § 4, cl. 4—a clear executive responsibility.

B. The CFPB executes the law but does not answer to, and is not restrained by, the President.

"But where, in all this, is the role for oversight by an elected President?" *Free Enter. Fund*, 561 U.S. at 499. Because the CFPB performs a role constitutionally committed to the executive branch, it must remain ultimately accountable to the President as the Chief Executive. *See* U.S. Const. Art. II, § 1, cl. 1; *see also Free Enter. Fund*, 561 U.S. at 484. Yet the Congress and the President that enacted the Dodd-Frank Act took pains to ensure this was not the case. The CFPB and its Director have been thoroughly insulated from future Presidents' control.

In its day-to-day operations, the CFPB operates entirely outside the President's sphere of influence. The Director of the CFPB is not required to coordinate with any other executive branch official regarding "legislative recommendations, or testimony or comments on legislation." 12 U.S.C. § 5492(c)(4). Likewise, the Director is independent from the President's financial oversight. Though he must provide the Director of the Office of Management and Budget ("OMB") copies of certain financial reports, he has no "obligation … to consult with or obtain the consent or approval of the Director of the [OMB] with respect to any report, plan, forecast, or other information," and the OMB lacks "any jurisdiction or oversight over the affairs or operations of the [CFPB]." *Id.* § 5497(a)(4)(E).

Most significantly, the Director of the CFPB is protected from removal and, as a result, from ultimate accountability to the Chief Executive. Once appointed, the Director serves a five-year term and can be removed only for "inefficiency, neglect of duty, or malfeasance in office." *Id.* § 5491(c)(3). This term can extend indefinitely, until the Senate affirmatively confirms his successor (or the President makes a genuine recess appointment). *Id.* § 5491(c)(2). The Director therefore cannot be removed by the President merely for failing to execute the law in a manner inconsistent with the President's policies and directives. *See Free Enter. Fund*, 561 U.S. at 496. And if the President and the Director disagree in the field of consumer finance, by statute the Director's view prevails. *See* 12 U.S.C. § 5512(b)(4).

In effect, the Dodd-Frank Act establishes the Director as a mini-President of consumer finance, vested with sweeping executive authority within his prescribed domain, yet entirely unaccountable in its exercise to the Chief Executive (or to the Congress). This structure cannot be reconciled with the constitutionally prescribed separation of powers, as explained by the Supreme Court in *Free Enterprise Fund*, 561 U.S. 477, and in what the Court there described as its "landmark" decision in *Myers v. United States*, 272 U.S. 52 (1926). Those cases establish that the President's constitutional responsibilities require that he have the authority to remove appointed executive officers, and that only "under certain circumstances" can even "limited restrictions" be imposed on the removal power, *Free Enter. Fund*, 561 U.S. at 483, 495. These holdings recognize that the removal power is "perhaps *the* key means" that the President has for "appointing, overseeing, and controlling those who execute the laws.'" *Id.* at 501 (quoting 1 Annals of Cong. 463 (1789)). After all, "[t]he President cannot 'take Care that the Laws be faithfully executed' if he cannot oversee the faithfulness of the officers who execute them." *Free Enter. Fund*, 561 U.S. at 484. And the Constitution "requires that a President chosen by the entire Nation oversee the execution of the laws." *Id.* at 499.

Yet as is discussed in more detail below, none of the "certain circumstances" the courts have deemed sufficient to warrant even "limited restrictions" being imposed on the removal power are present in the CFPB. Its executive authority is not minor or narrow. It has no internal checks and balances. And it is accorded a perpetual funding supply outside the appropriations process that exempts it from Congress's power of the purse.

This combination of features has produced a "novel structure [that] does not merely add to the [CFPB's] independence, but transforms it." *Id.* at 496.

If for-cause removal restrictions can be applied to the Director of an agency with the powers and structural features of the CFPB, then *Myers* must be entirely overruled, and nothing prevents Congress from imposing similar removal restrictions on the head of every Department of the government. At minimum, *Myers* must be understood to establish that the Constitution guarantees the President authority to remove at will any executive official that exercises the powers of a Department head. *Myers*, 272 U.S. at 133–35 (noting that the heads of the "executive departments"—also known as "cabinet ministers"—are designed to "aid [the President] in the performance of the great duties of his office," especially in ensuring that he "take care that the laws be faithfully executed" (quotation omitted)); *id*. at 176 (declaring invalid the Tenure of Office Act of 1867, which restricted the President's ability to remove Cabinet Secretaries and other executive officers). And in *Free Enterprise Fund*, the Court reaffirmed this central holding of *Myers*, holding that "the separation-of-powers principle guarantees the President the authority to dismiss certain Executive Branch officials at will." *Free Enter. Fund*, 561 U.S. at 516 (citing *Myers*, 272 U.S. at 52). The Court elaborated, "[s]ince 1789, the Constitution has been understood to empower the President to keep [executive] officers accountable—by removing them from office, if necessary." *Id.* at 483 (citing *Myers*, 272 U.S. at 52).

What, then, differentiates the Director of the CFPB from a Cabinet-level official? Cabinet Secretaries cannot be distinguished from the Director on the ground that they are "purely executive," but that because of his role in making rules and adjudicating disputes the Director is not. *Cf. Humphrey's Ex'r*, 295 U.S. at 630-32 (distinguishing *Myers* on the ground that it involved "purely executive officials"). Many Cabinet Secretaries perform the very same kind of rulemaking and adjudicative functions that the Director does.[6] And the Director's authorities are by no means limited to rulemaking and adjudication. *Cf. Humphrey's Ex'r*, 295 U.S. at 628 (finding FTC acted "as a legislative or as a judicial aid" rather than an eye or arm of the executive). The Director's powers simply cannot be meaningfully distinguished from those of formally recognized Department heads. *See Decatur v. Paulding*, 39 U.S. 497, 515 (1840) ("The head of an executive department of the government, in the administration of the various and important concerns of his office, is continually required to exercise judgment and discretion. He must exercise his judgment in expounding the laws and resolutions of Congress, under which he is from time to time required to act.").

True, Congress has slapped the "independent" label on the CFPB. But the Constitution does not permit Congress to talismanically invoke the word "independent" to transform any agency—no matter how broad and wide its law-executing authority—from an arm of the executive into an unaccountable bureaucratic entity. *Humphrey's*

[6] *See, e.g.*, *Bowen v. Yuckert*, 482 U.S. 137, 153 (1987) ("[T]he Secretary decides more than 2 million claims for disability benefits each year, of which more than 200,000 are reviewed by administrative law judges."); *DiCenso v. Cisneros*, 96 F.3d 1004 (7th Cir. 1996) (HUD secretary adjudication of hostile housing environment sexual harassment); *Beavers v. Sec'y of HEW*, 577 F.2d 383, 386 (6th Cir. 1978) ("[T]he Secretary is entrusted with the duty of making all findings of fact . . . the statutorily-mandated deference to findings of fact runs in favor of the Secretary, not the administrative law judge….").

Executor did not remotely sanction such a result. Nor does Congress's apparent hope that unaccountability would render the CFPB more energetic and efficient alter the analysis. "[C]onvenience and efficiency are not the primary objectives—or the hallmarks—of democratic government," and the "fact that a given law or procedure is efficient, convenient, and useful in facilitating functions of government, standing alone, will not save it if it is contrary to the Constitution." *Free Enter. Fund*, 561 U.S. at 499 (alteration in original) (quoting *Bowsher*, 478 U.S. at 736).

C. The CFPB is unlike other executive entities approved by the courts.

This case is materially unlike others in which the Supreme Court has upheld restrictions on the President's removal power. In *Morrison v. Olson*, the Supreme Court upheld a statute that insulated a special "independent counsel" from Presidential oversight and removal, but it did so because the independent counsel had "limited jurisdiction and tenure and lack[ed] policymaking or significant administrative authority." 487 U.S. 654, 691, 696 (1988). Because the independent counsel had limited enforcement powers and no policy-setting role, the Court did not think that restrictions on the President's ability to remove him "unduly intefer[ed] with the role of the Executive Branch." *Id.* at 693.

Likewise, in *Humphrey's Executor v. United States*, the Court upheld a for-cause removal requirement on members of the Federal Trade Commission ("FTC") in substantial part because the Commission was statutorily created as a "nonpartisan" entity and had almost no role in setting executive policy. 295 U.S. at 624.[7] The FTC was structured to ensure a degree of political impartiality: By statute, no more than three of the FTC's five commissioners could come from the same political party. *Id.* at 611, 624. And the FTC commissioners were intended to act primarily "as a legislative or … judicial aid[]," using their expertise to carry out predominately ministerial and adjudicative tasks, rather than functioning as "arm[s] or … eye[s] of the executive." *Id.* at 628.[8] Because the FTC ultimately served "as a means of carrying into operation legislative and judicial powers" and ultimately acted "as an agency of the legislative and judicial departments," Congress could impose a good-cause removal requirement to preserve some of the agency's independence from the President.

D. Congress failed to create any mitigating internal checks and balances within the CFPB.

By design, the CFPB was created with *no* mitigating internal checks and balances. By placing a single Director at its head—beholden to no one, charged with running a self-perpetuating executive agency with vast enforcement authority, and able to act

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[7] *Humphrey's Executor*'s continued validity has been called into question by the reasoning of *Free Enterprise Fund*, and plaintiffs here preserve the argument that it should be overruled.

[8] The current FTC has been accorded additional executive powers that go beyond the quasi-legislative and quasi-judicial functions that were identified by the Supreme Court in *Humphrey's Executor* as the basis for the Court's passing muster on the FTC's for cause removal. The impact of those additional features on the FTC's constitutionality has not yet been considered by the courts. In any event, today's FTC is subject to a variety of checks and balances that do not constrain the CFPB—most notably, appropriation by Congress.

unilaterally and without need to deliberate or persuade—Congress has exacerbated the underlying separation of powers violation.

The Supreme Court has on several occasions favorably cited multi-member commission structures as providing useful checks, balances, and accountability. In *Humphrey's Executor*, the Supreme Court upheld for-cause removal with respect to the FTC in part because the Commission was expressly created as a "non-partisan" entity; by statute, no more than three of the five commissioners serving on the Commission could come from the same political party. 295 U.S. 602, 611, 624 (1935). Similarly, in *A.L.A. Schechter Poultry Corp. v. United States*, in striking down an impermissible delegation of authority, the Supreme Court expressly distinguished other grants of power to multi-member commissions, including the FTC, the Interstate Commerce Commission, and the Radio Commission. 295 U.S. 495 (1935).

Much has been written on the benefits of multi-member bodies relative to sole directorships. For example, one scholar (later an FTC commissioner himself) has explained that a single directorship prevents "the agency from enjoying the benefits of deliberation which produces more informed judgments about the direction of regulatory policy." Joshua D. Wright, *The Antitrust/Consumer Protection Paradox: The Two Policies at War With Each Other*, 121 Yale L.J. 2216, 2260 (2012). "[M]ultimember structures," on the other hand, foster collegiality and thereby "the potential for exposure to a variety of views and improved decisionmaking." *Id*. Others have explained that "collective governance can constrain overconfidence or cognitive errors by providing critical assessments and viewpoints of proposals," and "can also constrain shirking, selfdealing, and capture by providing multilateral monitoring and raising the number of people who need to be corrupted for improper action to occur." Todd Zywicki, *The Consumer Financial Protection Bureau: Savior or Menace?*, 81 Geo. Wash L. Rev. 856, 897–98 (2013). The bipartisan multimember commission structure has thus been the standard one for independent agencies for over 125 years. *See* Ronald J. Krotoszynski, Jr. et al., *Partisan Balance Requirements in the Age of New Formalism*, 90 Notre Dame L. Rev. 941, 962–983 (2015) (explaining that discussion regarding whether to have a bipartisan commission structure is often devoid from agencies' legislative histories, because it was assumed that such a structure would be used).

E. The Executive must defer to the CFPB.

The Dodd-Frank Act further insulates the CFPB from the President's control by elevating the CFPB's interpretation of consumer financial laws above that of all other executive agencies charged with enforcing those laws.[9] Specifically, the statute provides that "the deference that a court affords to the Bureau with respect to a determination by the Bureau regarding the meaning or interpretation of any provision of a Federal consumer financial law shall be applied as if the Bureau were the only agency authorized to apply, enforce, interpret, or administer the provisions of such Federal consumer financial law." 12 U.S.C. § 5512(b)(4)(B). This provision further diminishes the

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[9] Title X of the Dodd-Frank Act divides federal supervisory and enforcement responsibilities for consumer financial law between the federal banking regulators, who supervise and enforce consumer financial laws for banks whose assets are less than or equal to $10 billion, and the CFPB, which is the primary supervisor and enforcement authority for banks whose assets exceed $10 billion. *See* 12 U.S.C. §§ 5514, 5515, 5516.

President's authority to interpret and execute the consumer financial laws, and indeed places the President in a position of subservience to the CFPB, by requiring the heads of those financial regulatory agencies that are subject to removal at will by the President (*e.g.*, the Comptroller of the Currency—*see* 12 U.S.C. § 2) to defer to the CFPB Director—over whom the President has no control—rather than to the President.

II. THE CFPB ENJOYS "FULL INDEPENDENCE" FROM CONGRESS

A. The Dodd-Frank Act frees the CFPB from Congress's "power of the purse."

The CFPB is not funded by appropriations. Instead, the Dodd-Frank Act gives the CFPB a perpetual, annual entitlement to hundreds of millions of dollars from the Federal Reserve. 12 U.S.C. § 5497(a). Indeed, the Dodd-Frank Act goes so far as to expressly prohibit Congress even from attempting to "*review*" the CFPB's automatically funded budget. *See id.* § 5497(a)(2)(C) (emphasis added).

The President and Congress included this provision in the Dodd-Frank Act in order to free the CFPB from congressional oversight. S. Rep. No. 111-176, at 163 (2010)). They characterized this as a salutary feature, viewing such funding as "absolutely essential" to ensuring the agency's "independent operations"—independent, that is, from future Congresses. S. Rep. No. 111-176, at 163. But the D.C. Circuit, the Supreme Court, and the Framers would characterize it quite differently.

B. The Constitution's "power of the purse" is Congress's most powerful tool for overseeing and holding accountable agencies exercising federal law.

The Constitution entrusts taxpayers' money to Congress, requiring that "[n]o Money shall be drawn from the Treasury, but in Consequence of Appropriations made by Law." U.S. Const. art. I, § 9, cl. 7. As the D.C. Circuit recognizes, the Constitution commits that power and responsibility to Congress for a very specific reason: "The Framers placed the power of the purse in the Congress in large part because the British experience taught that the appropriations power was a tool with which the legislature could resist 'the overgrown prerogatives of the other branches of government.'" *Noel Canning v. NLRB*, 705 F.3d 490, 510 (D.C. Cir. 2013), *aff'd*, 134 S. Ct. 2250 (2014).

On this point, the Framers were emphatic. James Madison stressed that "[t]his power over the purse may, in fact, be regarded as the most complete and effectual weapon with which any constitution can arm the immediate representatives of the people, for obtaining a redress of every grievance, . . . for carrying into effect every just and salutary measure," and for "reducing . . . all the overgrown prerogatives of the other branches of the government." Federalist No. 58 (Madison). Alexander Hamilton was all the more blunt: "[T]hat power which holds the purse-strings absolutely, must rule." 1 *Works of Alexander Hamilton* 218–19 (Henry Cabot Lodge, ed., 1904) (Letter to James Duane).[10] Thus, while the Executive Branch "holds the sword," Congress "prescribes the

[10] *See also* 2 *Works of Alexander Hamilton* 8–9 (Address to New York Ratification Convention) ("Will any man who entertains a wish for the safety of his country trust the sword and the purse with a single Assembly, organized on principles so defective?"); *id.* at 61 ("Neither [the Legislative Branch] nor the [Executive Branch] shall have both [the

rules by which the duties and rights of every citizen are to be regulated" and, to that end, also "commands the purse." Federalist No. 78 (Hamilton).

The earliest major constitutional commentators, too, reiterated the importance of Congress's power of the purse as both a check against the other parts of government and a means of accountability between Congress and the Executive to the People. "The power to control, and direct the appropriations," wrote Joseph Story, "constitutes a most useful and salutary check upon profusion and extravagance, as well as upon corrupt influence and public peculation." 3 Joseph Story, *Commentaries on the Constitution* § 1342 (1833); *see also* 1 St. George Tucker, *Blackstone's Commentaries*, Appx., p. 362 (1803) ("All the expenses of government being paid by the people, it is the right of the people . . . to be actually consulted upon the disposal of the money which they have brought into the treasury . . . .").

Modern Congresses have recognized the significance of their "power of the purse," not merely as an end in itself, but as a means for ensuring that the other parts of government conduct their work in a manner consistent with the law, the public interest, and the public will. "The appropriations process is the *most potent form* of congressional oversight, particularly with regard to the federal regulatory agencies." S. Comm. on Gov't Operations, 95th Cong. 1st Sess., 2 *Study on Federal Regulatory Agencies* 42 (1977) (emphasis added); *see also* 1 GAO, *Principles of Federal Appropriations Law*, pp.

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power of the purse and the sword]; because this would destroy that division of powers on which political liberty is founded, and would furnish one body with all the means of tyranny. But when the purse is lodged in one branch, and the sword in another, there can be no danger.").

1-4 to 1-5 (3d ed. 2004) ("The Appropriations Clause has been described as 'the most important single curb in the Constitution on Presidential power.' . . . [T]he congressional power of the purse reflects the fundamental proposition that a federal agency is dependent on Congress for its funding."). Congress's continued recognition of the fundamental significance of its "power of the purse" is most recently evidenced by the House of Representatives' decision to file a federal lawsuit to prevent the executive branch from undertaking activities beyond the limits of Congress's appropriations—or, in this court's words, "to preserve its power of the purse and to maintain constitutional equilibrium between the Executive and the Legislature." *U.S. House of Representatives v. Burwell*, --- F. Supp. 3d ----, 2015 WL 5294762, at *1 (D.D.C. Sept. 9, 2015).

Myriad legal scholars have highlighted the fact that the power of the purse is the foundation for "most of the oversight that Congress exercises over administration." *See, e.g.*, Arthur W. Macmahon, *Congressional Oversight of Administration: The Power of the Purse I*, 58 Pol. Sci. Q. 161, 173 (1943).[11] Congress has relied on "limitations riders"

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[11] *See also, e.g.*, Kate Stith, *Congress' Power of the Purse*, 97 Yale L.J. 1343, 1360 (1988) ("Appropriations limitations constrain every government action and activity and, assuming general compliance with legislative prescriptions, constitute a low-cost vehicle for effective legislative control over executive activity."); Jack M. Beermann, *Congressional Administration*, 43 San Diego L. Rev. 61, 84 (2006) ("One way in which Congress has supervised agencies with great particularity, both formally and informally, is through the appropriations process"); Kirti Datla & Richard L. Revesz, *Deconstructing Independent Agencies (and Executive Agencies)*, 98 Cornell L. Rev. 769, 816 (2013) ("Congress primarily exerts influence over agency heads . . . through the power of the purse. Thus '[an] agency has an incentive to shade its policy choice toward the legislature's ideal point to take advantage of that inducement.'" (second alteration in original) (quoting Randall L. Calvert *et al.*, *A Theory of Political Control and Agency Discretion*, 33 Am. J. Pol. Sci. 588, 602 (1989)); Joseph Cooper & Ann Cooper, *The*

since at least the 1870s to rein in the executive branch and agencies. Neal E. Devins, *Regulation of Government Agencies Through Limitation Riders*, 1987 Duke L.J. 456, 462 (1987); *see also* Jason A. MacDonald, *Congressional Power over Executive Branch Policy Making: Limitations on Bureaucratic Regulations, 1989-2009*, 43 Pres. Studies Q. 523 (2013). But appropriations are all the more "critical to governing in an era characterized by large delegation to the executive branch." Jason A. MacDonald, *Limitation Riders and Congressional Influence Over Bureaucratic Policy Decisions*, 104 Am. Pol. Sci. Rev. 766, 781 (2010); *see also id.* ("[L]imitation riders provide Congress with much more influence . . . over the substance of regulations about which members of Congress, and their constituencies, care for political and policy reasons.").

And Congress's "power of the purse" is all the more important with respect to the independent regulatory agencies not subject to direct presidential oversight: "The most constant and effective control which Congress can exercise over an independent regulatory commission is financial control. . . . Viewed broadly, the financial control exercised by Congress over the [independent] commissions is a necessary and desirable form of supervision." Robert E. Cushman, *The Independent Regulatory Commissions* 674–75 (1972). For example, the FCC policy change at the center of *FCC v. Fox*, the Supreme Court's landmark case on agency discretion to change policies, was itself "spurred by significant political pressure from Congress," via "the congressional

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Legislative Veto & the Constitution, 30 Geo. Wash. L. Rev. 467, 491 (1961) ("Congress constantly uses the appropriations bills to control and supervise executive decision-making with regard to both policy and operations.").

committees responsible for oversight and appropriations with respect to the relevant agency." *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 523 & nn.4–5 (2009) (plurality op.).

The Supreme Court and D.C. Circuit share this appreciation of the power of the purse. The Appropriations Clause is nothing less than "a bulwark of the Constitution's separation of powers among the three branches of the National Government," a power that is "particularly important as a restraint on Executive Branch officers." *U.S. Dep't of Navy v. FLRA*, 665 F.3d 1339, 1347 (D.C. Cir. 2012); *see also Office of Personnel Mgmt. v. Richmond*, 496 U.S. 414, 425 (1990) ("Any 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."); *United States v. Richardson*, 418 U.S. 166, 178 n.11 (1974) ("The ultimate weapon of enforcement available to Congress [to rein in an rogue agency] would, of course, be the 'power of the purse.'").

Indeed, in *Free Enterprise Fund*, the majority and dissent *both* stressed the power of the purse's paramount importance—and each side invoked it in support of its own broader constitutional argument. Justice Breyer, writing for the four dissenting justices, downplayed the practical importance of "for cause" removal by pointing out that even when the President can threaten to remove officers, that influence is dwarfed by Congress's *fiscal* influence: "the decision as to who controls the agency's budget requests and funding, the relationships between one agency or department and another, as well as more purely political factors (including Congress' ability to assert influence) are more likely to affect the President's power to get something done." *Free Enter. Fund*, 561 U.S.

at 524 (Breyer, J., dissenting). Replying to that argument, the Court's majority did not downplay the power of the purse; rather, it stressed that the sheer potency of this core legislative power—Congress's "plenary control over the salary, duties, and even existence of executive offices"—is the very reason why the President must retain full power to act as a counterweight against Congress's influence. *Id.* at 500.

The courts' recognition of these principles is more than merely theoretical; the principles undergird other doctrines respecting the Constitution's separation of powers. In decisions denying standing to private parties challenging government policies, for example, the Supreme Court and D.C. Circuit have stressed that recourse is better found in the purse-strings of Congress. Thus, when the Supreme Court dismissed a suit challenging Vietnam-era military surveillance of American civilians, it stressed that the task of monitoring "the wisdom and soundness of Executive action" is "a role [that] is appropriate for the Congress acting through its committees and the 'power of the purse'; it is not the role of the judiciary . . . ." *Laird v. Tatum*, 408 U.S. 1, 15 (1972); *see also Allen v. Wright*, 468 U.S. 737, 760 (1984) (quoting *Laird* in denying standing to lawsuit against federal government to change tax-exemption policy). More recently, when the D.C. Circuit denied judicial review to those challenging federal regulators' decision not to modify auto safety standards, it pointed the challengers to Congress: "[t]o the extent Congress is concerned about Executive under-regulation or under-enforcement of statutes, it also may exercise its oversight role and power of the purse." *Pub. Citizen v. NHTSA*, 489 F.3d 1279, 1295 (D.C. Cir. 2007).

Indeed, the D.C. Circuit's prohibition against individual congressmen bringing suit to restrain agencies reflects the fact that Congress ordinarily has its constitutional "power of the purse" at hand to rein in the agency. *Harrington v. Bush*, 553 F.2d 190, 213 (D.C. Cir. 1977) ("The abuse of delegated authority does not invade the lawmaking power of Congress or appellant; all the traditional alternatives related to the 'power of the purse' remain intact.").

Moreover, even when the specific question of Congress's "power of the purse" is not expressly invoked, it still can serve to silently undergird significant doctrines involving the separation of powers. In *Humphrey's Executor* itself, for example, the Supreme Court justified the FTC's independence from the President on the basis that Congress remained the agency's "master." 295 U.S. at 630; *see also id.* (describing the FTC as "wholly disconnected from the executive department" but "an agency of the legislative . . . department[]"). Freed from Congress's power of the purse, the FTC would have been no such agent, and Congress no such master. *Cf. Fox*, 556 U.S. at 523 ("The independent agencies are sheltered not from politics but from the President, and it has often been observed that their freedom from presidential oversight (and protection) has simply been replaced by increased subservience to congressional direction.").

C. The CFPB has demonstrated that Congress cannot meaningfully oversee and restrain an agency without the power of the purse.

Given that the Appropriations Power is a bulwark of Congress's legislative oversight authority, scholars have come to recognize that an agency's protection against the President's removal authority is not the only form of "independence" that an agency may enjoy. Protection against Congress's power of the purse is another: if an agency can rely upon "an independent funding source," then an independent agency "is insulated from Congress as well as the President." Rachel E. Barkow, *Insulating Agencies: Avoiding Capture Through Institutional Design*, 89 Tex. L. Rev. 15, 44 (2010); *see also id.* at 43 ("To be sure, the power of the purse is one of the key ways in which democratic accountability is served.").[12]

The CFPB proves the theory as a matter of fact. The Dodd-Frank Act's framers gave the CFPB a permanent source of non-congressional funding for the express goal of ensuring the agency's full independence from future Congresses. And the CFPB does not hesitate to assert this independence, in both word and deed. The CFPB recognizes that its legal entitlement to hundreds of millions of dollars in "funding outside the congressional appropriations process" ensures its "full independence" from Congress. *Consumer Financial Protection Bureau Strategic Plan: FY 2013-FY 2017* 36 (Apr. 2013), http://files.consumerfinance.gov/f/strategic-plan.pdf. As such, while the CFPB may sometimes agree to appear before congressional committees, submit reports to Congress, or undergo GAO audits, the agency faces no serious consequences for refusing to respond meaningfully to Congress's attempts to conduct oversight regarding the agency's regulatory and enforcement activities.

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[12] *See also* Charles Kruly, *Self-Funding and Agency Independence*, 81 Geo. Wash. L. Rev. 1733 (2013); Note, *Independence, Congressional Weakness, and the Importance of Appointment: The Impact of Combining Budgetary Autonomy with Removal Protection*, 125 Harv. L. Rev. 1822 (2012); Kirti Datla & Richard L. Revesz, *Deconstructing Independent Agencies (and Executive Agencies)*, 98 Cornell L. Rev. 769, 782–83 (2013) (reiterating Barkow's focus on budgetary autonomy).

Congressmen and Senators can write letters to the CFPB, complaining that the agency is "wholly unresponsive to our requests for additional budget information,"[13] or that the agency "has yet to explain its basis for" controversial policies.[14] At hearings, Congress can criticize the agency's failure to answer questions about its secret "data gathering activities," and "deman[d] to know why the agency's director . . . and his staff have not yet answered roughly 200 questions sent to the agency."[15] Congress can do all of those things, but without the power of the purse its ability to secure answers to its questions, let alone to guide the agency's policies, is severely limited.

This dynamic was fully on display at a hearing earlier this year, at which a Congresswoman asked CFPB Director Cordray for information as to who at the agency was directing renovation projects costing hundreds of millions of dollars. The Director declined to answer her question; instead, he asked her bluntly, "*why does that matter to*

[13] Letter from Rep. Randy Neugebauer, Chairman, H.R. Comm. on Fin. Servs., Subcomm. on Oversight and Investigations, *et al*. to Richard Cordray, Director of the CFPB, at 1 (May 2, 2012), http://www.aba.com/aba/documents/winnews/CFPB_OversightMemo_050212.pdf.

[14] Letter from Sen. Rob Portman, *et al*. to Richard Cordray, Director of the CFPB, at 1 (Oct. 30, 2013), http://www.portman.senate.gov/public/index.cfm/files/serve?File_id=ad73c8d1-39c6-4c4f-80da-c13c57013b12.

[15] Rachel Witkowski, *Lawmakers Fume Over Unanswered Questions to CFPB*, Am. Banker (Sept. 12, 2013), http://www.americanbanker.com/issues/178_177/ lawmakers-fume-over-unanswered-questions-to-cfpb-1062015-1.html. A year later, an investigation by the GAO revealed that the CFPB had collected information regarding over 10 million individuals' credit reports, 29 million active mortgage loans, and up to 75 million credit card accounts. GAO, *Consumer Financial Protection Bureau: Some Privacy and Security Procedures for Data Collections Should Continue Being Enhanced* 15–16 (Sept. 14, 2014), http://www.gao.gov/assets/670/666000.pdf. The GAO further concluded that the "CFPB lacks written procedures and documentation needed to address privacy risks and better ensure ongoing compliance with requirements." *Id.* at 37 (capitalization modified).

you?" *See* U.S. House of Representatives, Committee on Financial Services, "Committee Pushes for Accountability and Transparency at the CFPB" (Mar. 6, 2015) (emphasis added), http://financialservices.house.gov/blog/?postid=398780.[16]

The loss of Congress's constitutional power over the CFPB is not ameliorated by the fact that a previous Congress passed the statute eliminating Congress's power of the purse. After all, an individual Congress, like an individual President, "might find advantages in tying [its] own hands." *Free Enter. Fund*, 561 U.S. at 497; *see also* James Q. Wilson, *Bureaucracy* 239 (1989) ("[P]oliticians have good reasons to tie their own hands. But once tied, they cannot easily be untied."). But just as "the separation of powers does not depend on the views of individual Presidents," *Free Enter. Fund*, 561 U.S. at 497, nor does it depend on the views of an individual Congress. And therefore, just as a single President "cannot . . . choose to bind his successors by diminishing their powers," *id.*, nor can a single Congress choose to bind its successors by diminishing theirs.

Whatever flexibility Congress may have in effecting appropriations, the perpetual nature of § 5497(a)'s massive funding stream—amounting to more than $600 million in 2016, enough to fund the entire operations of an agency that cannot meaningfully be distinguished from an executive Department—is uniquely constitutionally problematic. And make no mistake: having granted the CFPB perpetual authority to self-appropriate its funding from a source outside the Treasury, a future Congress cannot simply restore

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[16] Video of the exchange is available at https://www.youtube.com/ watch?v=5IxSfJ638cs.

its constitutionally prescribed oversight role. Even if both houses of Congress were to pass a bill that eliminated § 5497(a) and required the CFPB to seek all of its future funding from Congress, that bill could be vetoed by the President. *See* U.S. Const. Art. I, § 7. The Dodd-Frank Congress having abdicated its power of the purse check on executive authority, and rendered the CFPB entirely self-sustaining, a successor Congress cannot simply cannot take its constitutionally prescribed authority back. The Constitution cannot be read to permit the Dodd Frank Congress to strip successor Congresses of their core power of the purse authority in this manner.

III. CORDRAY'S RECESS APPOINTMENT WAS ILLEGAL, AND REGULATIONS HE PROMULGATED WHILE ILLEGALLY SERVING ARE INVALID

A. *Noel Canning* definitively establishes that Cordray's purported recess appointment was unconstitutional.

Nothing differentiates Cordray's recess appointment from the NLRB recess appointments that the Supreme Court invalidated in *Noel Canning*. The President appointed Cordray on the same day as the three NLRB members, and using the same process. And the position to which Cordray was appointed—Director of the CFPB—was of equal or greater executive stature.

The Constitution requires that all principal Officers of the United States be appointed to their posts by the President "with the Advice and Consent of the Senate." U.S. Const. Art. II, § 2, cl. 2. The Director of the CFPB exercises significant executive authority, and does not answer to any other appointed executive official. He thus acts as a principal Officer of the United States, *see Edmond v. United States*, 520 U.S. 651, 663

(1997) (principal officers are those whose work is not directed or supervised at some level by other appointed officers), and his appointment is subject to the requirements of the Appointments Clause.

B. All rules promulgated by Cordray during his illegal appointment are invalid.

All of the regulations challenged by plaintiffs were published under Cordray's signature, either as final rules or as notices of proposed rulemaking, at a time that neither Cordray nor anyone else was legally serving as Director of the CFPB. Because each of these acts of publication, as well as the agency actions underlying them (such as consideration of comments and compilation of the administrative record) was legally invalid, the rules themselves must be held to be illegal and without effect. *See* 5 U.S.C. § 553 (requiring publication of notice of proposed rule, consideration of comments, and publication of final rule); 5 U.S.C. § 706(2) (courts should "hold unlawful and set aside agency action" taken "without observance of procedure required by law"); *Sierra Club v. E.P.A.*, 699 F.3d 530, 531 (D.C. Cir. 2012) (vacating and remanding a rulemaking action taken by the agency "[b]ecause EPA issued the [rulemaking] Determination without providing notice and opportunity for comment" consistent with the requirements of 5 U.S.C. § 553).[17]

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[17] The involvement of CFPB staff in the rulemakings in no way saves them. By statute, all of the CFPB's rulemaking authorities are vested in a legally appointed Director or his delegee. 12 U.S.C. §§ 5492(b), 5512(b)(1). The Director could not have had any valid delegees prior to July 2013, since there was no constitutionally appointed Director who could delegate the Director's authorities. "The head of the agency is generally the final rulemaking authority." 1 Charles H. Koch, Jr. & Richard Murphy, *Administrative Law*

C. Cordray's nominal "ratification" does not cure his actions' unlawfulness.

After Cordray was finally appointed CFPB Director with Senate advice and consent in July 2013, he issued a proclamation "[t]o address any possible uncertainty" about the validity of the CFPB's actions taken during his recess appointment. Published in the Federal Register, the notice purported to "affirm and ratify any and all actions" Cordray took on behalf of the CFPB before his reappointment on July 16, 2013. 78 Fed. Reg. 53,734 (Aug. 30, 2013). That proclamation did not—and could not—have the alchemic effect he hoped it would with respect to past invalid rulemakings.

To start, Cordray's purported "ratification" was not an independently valid rulemaking. Under the Administrative Procedure Act ("APA"), to engage in rulemaking an agency must publish notice of the proposed rule and give interested persons at least 30 days to submit "written data, views, or arguments" regarding the proposal. 5 U.S.C. § 553(b)–(d). Cordray did not follow this notice-and-comment procedure with respect to the "notice of ratification." *See* 78 Fed. Reg. 53,734. He simply published the notice.

Second, to the extent the notice was an attempt to retroactively ratify previously invalid rulemakings, such ratification was likewise ineffective. It is black letter law that ratification of a past action can be effective only when the purported ratifier possessed the legal authority take the action both when it was originally taken, and at the time of ratification. *See Fed. Election Comm'n v. NRA Political Victory Fund*, 513 U.S. 88, 98

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and Practice § 4:42 (3d ed. 2015). "While the staff may make recommendations, the decision-making authority rest[s] in the top of the agency hierarchy" *Id.* at 4:42[3].

(1994) ("[I]t is essential that the party ratifying should be able not merely to do the act ratified at the time the act was done, but also at the time the ratification was made."). This rule is grounded in a fundamental principle of agency law: "[A] person may not ratify an act which he or she could not have originally authorized." 3 Am. Jur. 2d *Agency* § 177 (2014); *see also W. Nat'l Bank of N.Y. v. Armstrong*, 152 U.S. 346, 352 (1894) ("[A] ratification, to be efficacious, must be made by a party who had power to do the act in the first place."); *Franklin Sav. Ass'n v. Director of Office of Thrift Supervision*, 740 F. Supp. 1535, 1539 (D. Kan. 1990) ("[F]or a ratification to be effective, the ratifying person or entity must have had authority to do the underlying act both at the time of the original act and at the time of ratification.").

Cordray's ratification fails because he lacked the authority to exercise the CFPB's rulemaking powers at the time the challenged regulations were initially proposed and enacted. The only individuals authorized to exercise the CFPB's rulemaking authority between January 4, 2012 and July 16, 2013 were a constitutionally appointed Bureau Director or his delegee, or (with respect to certain rules) the Treasury Secretary. *See* 12 U.S.C. § 5491(b)(1) (naming the Director head of the CFPB); *id.* § 5586(a) [Needs to be separate citation and not an id.] (authorizing the Treasury Secretary to exercise certain CFPB authorities until a Director is appointed and confirmed). Cordray was neither of these things prior to his July 2013 reappointment.

As an illegally appointed Director from January 4, 2012 until July 16, 2013, Cordray lacked the authority to exercise the CFPB's executive powers during that time, including its power to propose and approve regulations. *See Noel Canning*, 134 S. Ct. at

2574, 2557–58, 2578 (intra-session appointments were constitutionally invalid and thus improperly appointed NLRB members could not act as executive officers); *see also Noel Canning v. NLRB*, 705 F.3d 490, 514 (D.C. Cir. 2013) (because appointments were constitutionally invalid, NLRB "had no quorum, and its order [was] void"). And of course Cordray never served as Treasury Secretary. Because Cordray lacked the power "to do the act[s] ratified" at the time the actions were taken—namely, propose and authorize regulations on the CFPB's behalf during the period of his unconstitutional appointment—he cannot legally ratify those past actions. *NRA Political Victory Fund*, 513 U.S. at 98.[18]

D. The CFPB's invalidly enacted regulations cannot be rescued by the de facto officer doctrine or harmless error analysis.

Courts have at times applied two narrow rules to affirm agency actions by improperly appointed officers: the de facto officer doctrine and harmless error analysis. Neither can save Cordray's rulemaking actions in this case, because the challenged rulemakings were infected with a structural constitutional error.

The de facto officer doctrine may "confer[] validity upon acts performed by a person acting under the color of official title even though it is later discovered that the legality of that person's appointment or election to office is deficient." *Ryder v. United States*, 515 U.S. 177, 180 (1995). But as the Supreme Court has recently held, this doctrine does not apply in cases where the officer's authority to act is challenged because

[18] Cordray can no more "ratify" regulations promulgated by an unlawfully appointed "Director" than he can "ratify" regulations promulgated by anyone else purporting to issue regulations in the CFPB's name without a lawful appointment to the office.

he was unconstitutionally appointed to his post—for if it did, the "rule would create a disincentive to raise Appointments Clause challenges." *Id.* at 182–83; *see also Nguyen v. United States*, 539 U.S. 69 (2003) (refusing to apply de facto officer doctrine to uphold actions of an appellate panel where one of the panel members was not properly appointed pursuant to Article III). In cases post-dating *Ryder*, the D.C. Circuit and other courts consequently have not applied the doctrine where the constitutionality of an officer's appointment is at issue. *SW Gen., Inc. v. NLRB*, 796 F.3d 67, 81 (D.C. Cir. 2015) ("In its most recent cases . . . the Supreme Court has limited the doctrine, declining to apply it when reviewing Appointments Clause challenges and important statutory defects to an adjudicator's authority." (citation omitted)).[19]

Moreover, even if the de facto officer doctrine could be applied to Appointments Clause challenges, the D.C. Circuit has held it does not apply in any event where two conditions are satisfied. First, the challenger "must bring his action at or around the time that the challenged government action is taken." *Andrade v. Lauer*, 729 F.2d 1475, 1499 (D.C. Cir. 1984). Second, "the agency or department involved [must have] reasonable

[19] *See also Silver v. U.S. Postal Serv.*, 951 F.2d 1033, 1036 n.2 (noting that "[t]he continued vitality of the de facto officer doctrine is in serious doubt" after "the Supreme Court entertained collateral challenges based on the Appointments Clause without ever mentioning … the de facto officer doctrine"). *Cf. Intercollegiate Broad. Sys. Inc. v. Copyright Royalty Bd.* ("*Intercollegiate Broad. Sys., Inc. I*"), 684 F.3d 1332, 1333 (D.C. Cir. 2012) (vacating and remanding the Board's decision "[b]ecause of the Appointments Clause violation at the time of decision" without considering whether the Board members were de facto officers). Although the Supreme Court in *Buckley v. Valeo* accorded de facto validity to the actions of the Federal Election Commission despite finding an Appointments Clause violation, *see* 424 U.S. 1, 142 (1976), the Court in *Ryder* limited *Buckley*'s holding to its facts, *Ryder*, 515 U.S. at 183–84.

notice under all the circumstances of the claimed defect in the official's title to office." *Id.* Where those two conditions are met, the doctrine does not apply because allowing a legal challenge to proceed "adequately protect[s] citizens' reliance on past government actions and the government's ability to take effective and final action." *Id.*

Here, both requirements are satisfied. Plaintiffs filed suit challenging Cordray's authority to enact certain regulations on behalf of the CFPB just six months after Cordray's unconstitutional appointment. *See* ECF No. 1. And the CFPB had ample notice that Cordray's purported recess appointment could be constitutionally defective — from this lawsuit, from the *Noel Canning* litigation, and from widespread publicity of its questionable constitutional character. *See SW Gen., Inc.*, 796 F.3d at 82 ("[T]he notice requirement is satisfied if the agency learns of the defect from *any* source, not only the petitioner."); *Andrade v. Regnery*, 824 F.2d 1253, 1256 (D.C. Cir. 1987) ("The filing of the underlying suit ... in and of itself notified the government of appellants' ... challenge."). Indeed, just one day after Cordray was initially named CFPB Director, newspaper pieces already decried his recess appointment as unconstitutional. *See, e.g.*, Edwin Meese III and Todd Gaziano, *Obama's Recess Appointments Are Unconstitutional*, The Washington Post (Jan. 5, 2012).[20] The CFPB thus had ample opportunity to "remedy any defects … either before it permit[ted Cordray] to act or shortly thereafter." *SW Gen., Inc.*, 796 F.3d at 82 (internal quotation marks omitted).

[20] *Available at* https://www.washingtonpost.com/opinions/obamas-recess-appointments-are-unconstitutional/2012/01/05/gIQAnWRfdP_story.html.

For similar reasons, the Court should reject any claim that the regulations are valid because their promulgation during Cordray's unconstitutional tenure was harmless error. "[S]eparation of powers"—an interest the Appointments Clause protects— "is a *structural safeguard* rather than a remedy to be applied only when specific harm, or risk of specific harm, can be identified." *Landry v. FDIC*, 204 F.3d 1125, 1131 (D.C. Cir. 2000); *see also SW Gen., Inc.*, 796 F.3d at 80 (noting that the Appointments Clause requirements are "structural safeguard[s] intended to curb Executive abuses of the appointment power and to promote a judicious choice of persons for filling the offices of the union." (internal quotation marks omitted)). For this reason, courts must assume that structural errors are harmful, "even where any possible injury is radically attenuated." *Id*. at 1130–32 (harmless error analysis could not apply to save an unconstitutionally appointed administrative law judge's involvement in recommending a decision to the FDIC). Indeed, applying the harmless error doctrine to Appointments Clause violations would effectively render it optional, rather than a mandatory safeguard.[21]

[21] The presence of an uncured structural constitutional error in this case distinguishes it from others in which the D.C. Circuit concluded that the harmless error doctrine saved agency actions. *See, e.g.*, *Doolin Sec. Sav. Bank, F.S.B. v. Office of Thrift Supervision*, 139 F.3d 203, 211–12 (D.C. Cir. 1998) (concluding that issue of a notice of charges by an officer whose appointment was statutorily improper was rendered harmless when a properly appointed official considered the charges de novo and found sufficient evidence to conclude that the bank had committed the noticed violations); *Fed. Elec. Comm'n v. Legi-Tech, Inc.*, 75 F.3d 704 (D.C. Cir. 1996) (finding that ratification by a constitutionally composed council of prior adjudication decisions rendered by an unconstitutionally composed council were adequate to cure the constitutional violation); *see also Intercollegiate Broad. Sys., Inc. II*, 796 F.3d at 120–21 (noting that "review by a properly appointed body can be insufficient to cure an Appointments Clause violation" including when "a statute expressly requires" the decision-maker to follow a particular

Because Cordray's recess appointment violated the Appointments Clause, any rulemaking actions Cordray took while illegally serving are tainted with structural constitutional error. *See id.* Accordingly, they cannot be saved by harmless error analysis and must be declared invalid.

CONCLUSION

This Court should hold that the CFPB unconstitutionally violates the separation of powers, that Richard Cordray's January 4, 2011 recess appointment was unconstitutional, and that the challenged regulations are invalid and cannot be enforced against plaintiffs.

Respectfully submitted.

GREGORY JACOB
Counsel of Record
O'MELVENY & MYERS LLP
1625 I St. NW
Washington, DC 20006
(202) 383-5300
gjacob@omm.com

C. BOYDEN GRAY
ADAM J. WHITE
BOYDEN GRAY & ASSOCIATES
1627 I Street NW, Suite 950
Washington, DC 20006
(202) 955-0620
adam@boydengrayassociates.com

Counsel for Plaintiffs State National Bank of Big Spring, the Competitive Enterprise Institute, and the 60 Plus Association

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procedure). To the extent any of these decisions present circumstances similar to this case, their reasoning has been abandoned by subsequent decisions holding that structural constitutional errors cannot be considered harmless. *See Landry*, 204 F.3d at 1131; *see also SW Gen., Inc.*, 796 F.3d at 79–80 (noting that harmless error analysis seems ill-suited to cases involving structural constitutional errors); *Intercollegiate Broad. Sys., Inc. I*, 684 F.3d at 1342 (vacating and remanding the Board's decision without considering whether any error was harmless because the Board was unconstitutionally structured in violation of the Appointments Clause at the time it acted).

SAM KAZMAN
HANS BADER
COMPETITIVE ENTERPRISE INSTITUTE
1899 L St. NW, Floor 12
Washington, DC 20036
(202) 331-1010

Co-Counsel for Plaintiffs
Competitive Enterprise Institute

November 6, 2015

CERTIFICATE OF SERVICE

I certify that on this 6th day of November 2015, I electronically filed the foregoing brief with the Court. I further certify that on this 6th day of November 2015, I served the foregoing brief on all counsel of record through the Court's CM/ECF system.

/s/ Gregory F. Jacob
Gregory F. Jacob
O'MELVENY & MYERS LLP
1625 Eye Street NW
Washington, D.C. 20006
Telephone: (202) 383-5300

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

STATE NATIONAL BANK OF BIG SPRING *et al.*, Plaintiffs, v. JACOB J. LEW, in his official capacity as United States Secretary of the Treasury and *ex officio* Chairman of the Financial Stability Oversight Council 1500 Pennsylvania Avenue, NW Washington, DC 20220, et al., Defendants.	Case No. 1:12-cv-01032 (ESH) Judge: Hon. Ellen S. Huvelle

STATEMENT OF MATERIAL FACTS NOT IN DISPUTE IN SUPPORT OF PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT

Pursuant to L. Cv. R. 7(h)(1), and in support of its Motion for Summary Judgment Against the Consumer Financial Protection Bureau ("CFPB" or "Bureau"), plaintiffs State National Bank of Big Spring ("the Bank") and Competitive Enterprise Institute submit the following material facts as to which there is no genuine dispute:

CFPB's Statutory Powers

1. The CFPB was created in 2010 by Title X of the Dodd-Frank Act ("Dodd-Frank"). *See* Pub. L. No. 111-203, 124 Stat. 1376 (2010).

2. Dodd-Frank vested the CFPB with exclusive jurisdiction to administer eighteen "Federal consumer financial law[s]" previously administered by myriad other agencies. 12 U.S.C. §§ 5481(12), (14), 5511.

3. The CFPB has the power to "establish the general policies of the [CFPB] with respect to all executive and administrative functions," including "implementing the

Federal consumer financial laws through rules, orders, guidance, interpretations, statements of policy, examinations, and enforcement actions"; deciding on the appropriate "use and expenditure of funds" for those purposes; "coordinat[ing] and oversee[ing] the operation of all administrative, enforcement, and research activities of the [CFPB];" and "performing such other functions as may be authorized or required by law." 12 U.S.C. § 5492(a)(4), (9), (10), (11).

4. Dodd-Frank further vested the CFPB with newly created authority to regulate or prosecute "unfair, deceptive, or abusive" consumer lending practices. *Id.* § 5531(a).

5. The CFPB is an "independent bureau" within the Federal Reserve System. *Id.* § 5491(a); *see also* 44 U.S.C. § 3502(5).

6. The Federal Reserve cannot intervene in any CFPB matter or proceeding or appoint or remove any CFPB employee. *See* 12 U.S.C. § 5492(c).

7. The CFPB's Director ("Director") cannot be removed by the President except "for inefficiency, neglect of duty, or malfeasance in office." 12 U.S.C. § 5491(c)(3).

8. The Director is accorded a minimum term of five years, and the authority to hold over in office indefinitely until a successor is confirmed. 12 U.S.C. § 5491(c)(1)-(2).

9. Instead of relying on congressional appropriations to fund its activities, the CFPB is statutorily entitled to claim about $600 million annually from the Federal Reserve System. Specifically, the CFPB is entitled to up to 12 percent of Federal Reserve's operating expenses. 12 U.S.C. § 5497(a).

10. According to the CFPB, this is estimated to be $539 million in the fiscal year ending Oct. 31, 2015 and $605.5 million in the fiscal year ending Oct. 31, 2016. CFPB, *The CFPB Strategic Plan, Budget, and Performance Plan and Report* 21 (Feb. 2015),

http://files.consumerfinance.gov/f/201502_cfpb_report_strategic-plan-budget-and-performance-plan_FY2014-2016.pdf.

11. Congress is prohibited even from attempting to "review" the CFPB's non-appropriated budget. *See* 12 U.S.C. § 5497(a)(2)(C).

12. The CFPB recognizes that its legal entitlement to hundreds of millions of dollars in "funding outside the congressional appropriations process" ensures its "full independence" from Congress. *Consumer Financial Protection Bureau Strategic Plan*: *FY 2013-FY 2017* 36 (Apr. 2013), http://files.consumerfinance.gov/f/strategic-plan.pdf.

13. At a hearing earlier this year, a Congresswoman asked CFPB Director Cordray for information as to who at the agency was directing renovation projects costing hundreds of millions of dollars. The Director declined to answer her question; instead, he asked her bluntly, "*why does that matter to you?*" *See* U.S. House of Representatives, Committee on Financial Services, "Committee Pushes for Accountability and Transparency at the CFPB" (Mar. 6, 2015) (emphasis added), http://financialservices.house.gov/blog/?postid=398780. Video of the exchange is available at https://www.youtube.com/watch?v=5IxSfJ638cs.

14. Eschewing the traditional, bipartisan "independent commission" model, in which several commissioners check and balance each other, the Act vests the agency's power in a single director. *See* 12 U.S.C. § 5491(b)(1).

15. The bipartisan multimember commission structure has thus been the standard one for independent agencies for over 125 years. *See* Ronald J. Krotoszynski, Jr. et al., *Partisan Balance Requirements in the Age of New Formalism*, 90 Notre Dame L. Rev. 941, 962–983 (2015) (explaining that discussion regarding whether to have a bipartisan commission structure is

often devoid from agencies' legislative histories, because it was assumed that such a structure would be used).

16. The Director of the CFPB is not required to coordinate with any other executive branch official regarding "legislative recommendations, or testimony or comments on legislation." 12 U.S.C. § 5492(c)(4).

17. Though he must provide the Director of the Office of Management and Budget ("OMB") copies of certain financial reports, the Director of the CFPB has no "obligation … to consult with or obtain the consent or approval of the Director of the [OMB] with respect to any report, plan, forecast, or other information," and the OMB lacks "any jurisdiction or oversight over the affairs or operations of the [CFPB]." *Id.* § 5497(a)(4)(E).

The Recess Appointment of Richard Cordray

18. The President nominated Richard Cordray to serve as the Director on July 18, 2011. Nikki Sutton, *President Obama Nominates Richard Cordray to Lead Consumer Financial Protection Bureau*, (July 18, 2011; 3:55 PM) https://www.whitehouse.gov/blog/2011/07/18/president-obama-nominates-richard-cordray-lead-consumer-financial-protection-bureau (July 18, 2011).

19. Because the Senate never consented to that nomination, the President appointed Cordray to the position on January 4, 2012, under the purported authority of the Recess Appointments Clause. Press Release, White House, President Obama Announces Recess Appointments to Key Administration Posts (Jan. 4, 2012) http://www.whitehouse.gov/the-press-office/2012/01/04/president-obama-announces-recessappointments- key-administration-posts.

20. In his speech announcing Cordray's "recess" appointment, the President stressed that he was installing Cordray without Senate confirmation not because of Senate delay per se, but rather because the Senate had made clear its intent not to confirm Cordray's nomination. As the President explained to the audience (near Cordray's hometown), "I refuse to take no for an answer." Press Release, White House, Remarks by the President on the Economy (Jan. 4, 2012), https://www.whitehouse.gov/the-press-office/2012/01/04/remarks-president-economy.

21. The same day, the President unilaterally appointed three members to the National Labor Relations Board ("NLRB"), also under the purported authority of the Recess Appointments Clause. *See NLRB v. Noel Canning*, 134 S. Ct. 2550 (2014).

22. The Senate, however, was not in recess at the time. 157 Cong. Rec. S 8783-84 (daily ed. Dec. 17, 2011).

23. To the contrary, the Senate was in the midst of a three-day break between pro forma sessions. *Id.*

24. The NLRB recess appointments were subsequently challenged in court. In *NLRB v. Noel Canning*, the Supreme Court unanimously held that the President lacked the constitutional authority to recess appoint the NLRB members because the Senate was not in recess on January 4, 2012, but was instead on a three-day break. 134 S. Ct. at 2550, 2556–57, 2573–78.

25. For that reason, the Court declared the NLRB recess appointments invalid. *Id.* at 2557, 2578.

26. Prior to the Supreme Court's *Noel Canning* decision, on January 24, 2013, the President re-nominated Cordray to serve as Director of the CFPB—the position in which he had purported to serve as a recess appointee since January 4, 2012.

27. The Senate confirmed Cordray to serve as Director of the CFPB on July 16, 2013. 159 Cong. Rec. S5704–05 (daily ed. July 16, 2013). This occurred after the Senate majority leader had threatened to change Senate filibuster rules. *See, e.g.*, Jim Puzzanghera, *Senate Clears Way For Cordray Confirmation as Consumer Bureau Chief*, L.A. Times, July 16, 2013 (noting that Cordray's original appointment, without lacking Senate confirmation, had "left a legal cloud over the bureau").

28. During the period of Cordray's alleged recess appointment—that is, between January 4, 2012, and July 16, 2013—Cordray exercised final decision-making authority concerning numerous CFPB rulemakings that impact plaintiffs, particularly SNB. Those rules include the Electronic Fund Transfers Rule (Regulation E), 77 Fed. Reg. 6193 (Feb. 7, 2012), 77 Fed. Reg. 50243 (Aug. 20, 2012), and 78 Fed. Reg. 30,661 (May 22, 2013) ("Remittance Rule"); the Mortgage Servicing Rules Under the Real Estate Settlement Procedures Act (Regulation X), 78 Fed. Reg. 10,695 (Feb. 14, 2013) ("Mortgage Servicing Rule"); the Escrow Requirements Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 4725 (Jan. 22, 2013) ("Escrow Rule"); the Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 6407 (Jan. 30, 2013) ("ATR/QM Rule"); the Integrated Mortgage Disclosures Under the Real Estate Settlement Procedures Act (Regulation X) and the Truth In Lending Act (Regulation Z), 77 Fed. Reg. 51,115 (Aug. 23, 2012) (NPRM, finalized Dec. 31, 2013, 78 Fed. Reg. 79,730) ("TRID Rule").

29. On August 30, 2013 Cordray published a statement in the Federal Register "[t]o address any possible uncertainty" about the validity of the CFPB's actions taken during the period of his recess appointment. The notice purported to "affirm and ratify any and all actions" Cordray took on behalf of the CFPB during the time. 78 Fed. Reg. 53734 (Aug. 30, 2013).

Plaintiffs had predicted to this Court a month earlier that Cordray might attempt such a tactic. *See* Private Plaintiffs' Supplemental Br. at 6 (July 19, 2013) [Doc. 38].

Plaintiffs

30. State National Bank ("SNB" or "the Bank") is a community bank that has served Big Spring, Texas and other communities for over a century.

31. The Competitive Enterprise Institute ("CEI") is a nonprofit organization dedicated to advancing the principles of individual liberty, limited government, and free enterprise.

32. The 60 Plus Association is a non-profit, non-partisan seniors advocacy group devoted to advancing free markets.

The Impact on State National Bank of Big Spring

33. The regulatory and enforcement authority conferred on and exercised by the Consumer Financial Protection Bureau (the "Bureau" or "CFPB") under the Dodd-Frank Act has required the Bank to incur significant legal compliance costs. Exhibit 1, Declaration of Jim R. Purcell ¶¶ 4-10 [Dkt #27-2] ("First Purcell Decl.").

34. The Remittance Rule imposed new disclosure requirements on institutions, such as the Bank, that offer international remittance transfers. Although the Remittance Rule offers a safe harbor exemption, the Bank must incur costs to ensure that it properly complies with the terms of that safe harbor. Ex. 1 ¶¶ 18-20; *State Nat. Bank of Big Spring v. Lew*, 795 F.3d 48, 53 (D.C. Cir. 2015).

35. Concerned that the Bureau would take enforcement actions against mortgage lenders for "abusive acts," even though the Bureau had not clearly defined that term, and due to the anticipated cost of complying with the CFPB's new mortgage regulations, the Bank stopped making consumer mortgage loans in the last quarter of 2010. Ex. 1 ¶¶ 21-31.

36. The Mortgage Servicing Rule imposed new restrictions on the Bank's ability to service the mortgage loans it currently holds, which it issued before exiting the market. 78 Fed. Reg. 10,695, 10,876 (Feb. 14, 2013) (codified at 12 C.F.R. §§ 1024.30(b), 1024.31 – 1024.37, 1024.41(j)). For example, the rule draws out the process by which the Bank may seek to recover on a defaulted mortgage loan. Ex. 1 ¶¶ 35-37.

37. The Escrow Rule imposes new requirements on institutions that make certain types of mortgage loans. For example, creditors "may not extend a higher-priced mortgage loan secured by a first lien on a consumer's principal dwelling unless an escrow account is established before consummation . . .." 78 Fed. Reg. 4725, 4753 (Jan. 22, 2013) (codified at 12 C.F.R. § 1026.35(a),(b)). Before exiting the mortgage market, the Bank offered several loans that would be "higher-priced mortgage loans" under the Escrow Rule. Ex. 1 ¶ 25. The Bank is exempted from the Escrow Rule only if it operates predominantly in rural or underserved areas. If the Bank reentered the mortgage market, it would necessarily incur costs to ensure that it properly complies with the terms of that exemption. Exhibit 3, Declaration of Jim R. Purcell ¶¶ 16-17 ("Third Purcell Decl."). If it does not incur these costs, it would either have to forgo the profit associated with making "higher-priced mortgage loans" or it would have to incur the costs associated with establishing such escrow accounts.

38. The ATR/QM Rule imposes new requirements on mortgage lenders. As background, the Dodd-Frank Act (a) requires lenders to assess a borrower's ability to repay before issuing a mortgage loan, and (b) states that a lender is presumed to have adequately assessed the ability to repay if it issues a "qualified mortgage." 15 U.S.C. § 1639c(a)(1), (b). The ATR/QM Rule implements and elaborates on this statute.

39. The ATR/QM Rule states that balloon mortgages issued by the Bank would be qualified mortgages only if the Bank issues mortgages predominantly in rural or underserved areas. 78 Fed. Reg. 6408, 6588 (Jan. 30, 2013) (codified at 12 C.F.R. § 1026.43(f)). A later amendment allows the Bank to issue qualified balloon mortgages regardless of whether it operates predominantly in rural or underserved areas, but this is a temporary exemption that expires in 2016. 78 Fed. Reg. 35429, 35503 (Jun. 12, 2013) (codified at 12 C.F.R. § 1026.43(e)(6)). Before exiting the mortgage market, the Bank made balloon mortgages. Ex. 3 ¶ 12. If the Bank reenters the market in 2016, it would incur costs to ensure that it operates predominantly in rural or underserved areas. Ex. 3 ¶ 16-17. If it does not incur these costs, it would have to either forgo the profit associated with balloon mortgages, or it would have to incur the increased litigation risk associated with issuing such mortgages.

40. In addition, the ATR/QM states that the Bank's mortgages will only be given a "rebuttable presumption" of compliance with the ability to repay requirement when the loan's interest rate exceeds the Average Prime Offer Rate ("APOR") by 3.5 percentage points – even if the loan otherwise satisfies the requirements for a qualified mortgage. 78 Fed. Reg. 6408, 6584, 6586 (Jan. 30, 2013), amended by 78 Fed. Reg. 35429, 35503 (June 12, 2013) (codified at 12 C.F.R. § 1026.43(b)(4), (e)(1)). The Bureau could have written a rule under which such mortgages conclusively satisfy the ability to repay requirements, but it chose not to. 78 Fed. Reg. 6408, 6506-14 (Jan. 30, 2013). The Bank previously made mortgages with an interest rate that exceeded the APOR by 3.5 percentage points. Exhibit 2, Second Decl. of Jim R. Purcell ¶ 10 [Dkt #35] ("Second Purcell Decl."). If the Bank reenters the mortgage market, it would either have to forgo the profit associated with making such loans, or it would have to incur the increased litigation risk associated with making such loans.

41. The TRID Rule mandates that certain documents be provided to the borrower of a mortgage loan. In the preamble to the rule, the CFPB acknowledges that it could have exempted construction-only mortgage loans from the TRID Rule, but it chose not to. 78 Fed. Reg. 79,730, 79,789-92 (Dec. 31, 2013). Ex. 3 ¶ 6. Although the Bank exited the mortgage lending market in 2010, the Bank continued to make short-term construction-only loans because they were exempt from many of the Bureau's regulations. Ex. 3 ¶ 7. The Bank will now either have to stop making construction-only loans, or it will incur additional costs to comply with the TRID Rule. Ex. 3 ¶ 9-11.

Respectfully submitted.

GREGORY JACOB
Counsel of Record
O'MELVENY & MYERS LLP
1625 I St. NW
Washington, DC 20006
(202) 383-5300
gjacob@omm.com

C. BOYDEN GRAY
ADAM J. WHITE
BOYDEN GRAY & ASSOCIATES
1627 I Street NW, Suite 950
Washington, DC 20006
(202) 955-0620
adam@boydengrayassociates.com

Counsel for Plaintiffs State National Bank of Big Spring, the Competitive Enterprise Institute, and the 60 Plus Association

SAM KAZMAN
HANS BADER
COMPETITIVE ENTERPRISE INSTITUTE
1899 L St. NW, Floor 12
Washington, DC 20036
(202) 331-1010

Co-Counsel for Plaintiffs Competitive Enterprise Institute

November 6, 2015

EXHIBIT 1

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

STATE NATIONAL BANK OF BIG SPRING *et al.*, Plaintiffs, v. TIMOTHY GEITHNER, in his official capacity as United States Secretary of the Treasury and *ex officio* Chairman of the Financial Stability Oversight Council, *et al.*, Defendants.	Case No. 1:12-cv-01032 (ESH) Judge: Hon. Ellen S. Huvelle

DECLARATION OF JIM R. PURCELL

In Accordance with 28 U.S.C. § 1746, I, Jim R. Purcell, declare as follows, under the pains and penalties of perjury:

1. I am the Chairman of the Board and CEO of the State National Bank of Big Spring in Big Spring, Texas ("the Bank"). I have served as CEO since 1988 and became Chairman of the Board in 2012.

2. I served as President of the Bank from 1988 to 2012.

3. I am familiar with the Bank's legal compliance practices, remittance services, and mortgage lending.

Compliance Practices

4. The regulatory and enforcement authority conferred on and exercised by the Consumer Financial Protection Bureau (the "Bureau" or "CFPB") under the Dodd-Frank Act has required the Bank to incur significant legal compliance costs.

5. In the year 2012, for example, the Bank incurred $231,000 in compliance costs.

That includes costs for compliance personnel (including an outside auditor), compliance software, and compliance education.

6. In particular, the Bank's annual compliance costs in 2012 included over $2,500 to send a representative to the Texas Bankers Association Compliance School. That training covered, among other things, the Bureau's regulations governing electronic funds transfers and mortgage disclosures.

7. In addition, after the Dodd-Frank Act was passed, the Bank determined that it needed to stay informed of the regulatory requirements that would be adopted by the CFPB and other agencies under the Act. The Bureau's authority to enforce its views of "unfair, deceptive, or abusive" practices ex post facto further made it necessary to stay abreast of its interpretations, announcements, and enforcement actions. For this reason the Bank began to subscribe to a service from the Texas Bankers Association, the Compliance Alliance, that keeps the Bank informed of the activities and pronouncements of Government agencies that regulate the Bank, including the Bureau, as well as their impact on the Bank. Attached to this declaration are true and correct copies of marketing materials the Bank received from the Compliance Alliance to induce the Bank to subscribe to its service, which specifically note that the service is necessary because of the Dodd-Frank Act and CFPB. The Bank found these materials persuasive.

8. The Bank used the Compliance Alliance service to aid in its understanding of the CFPB's rules governing international remittance transfers, mortgage disclosures, and ability-to-pay requirements, as well as to stay abreast of Bureau interpretations and enforcement actions. Attached to this declaration are true and correct copies of materials the Bank has received from the Compliance Alliance.

9. The Compliance Alliance subscription costs the Bank $9,900 annually. The

original subscription price was $12,000, but so many institutions signed up for the service that the Compliance Alliance was able to lower its fees. The Compliance Alliance now has customer banks in 18 States and is sponsored by 16 state banking associations.

10. The Bank also responded to the Dodd-Frank Act by subscribing to the compliance service TriNovus, paying $2,340 for a one-year subscription in 2011.

Remittance Transfers

11. Until May 22, 2012, the Bank offered international remittance transfers to consumers and businesses that requested them. The Bank regularly offered more than 25 transfers a year and has offered up to 70 transfers a year.

12. From May 1, 2011 to April 30, 2012, for example, the Bank offered 18 international consumer remittance transfers and 8 mixed use transfers.

13. On February 7, 2012, the CFPB published a rule governing the provision of international remittance transfers. Electronic Fund Transfers, 77 Fed. Reg. 6194 (Feb. 7, 2012) (to be codified at 12 C.F.R. pt. 1005) ("the Remittance Rule").

14. The 18 international consumer remittance transfers the Bank offered from May 2011-2012 are covered by the Remittance Rule. For the 8 mixed-use transfers offered during that period, the Bank does not have the details necessary to determine whether they would be covered by the Rule.

15. On May 22, 2012, the Bank determined that it would not be able to comply with the requirements of the Bureau's Remittance Rule and still offer international consumer remittance transfers at a profit.

16. On June 21, 2012, the Bank filed this suit.

17. On August 20, 2012, the Bureau revised the Remittance Rule to include a safe

harbor exemption for providers that perform 100 or fewer international consumer remittance transfers per calendar year. Electronic Fund Transfers, 77 Fed. Reg. 50244 (Aug. 20, 2012).

18. On November 27, 2012, in response to the Bureau's revision of the Remittance Rule, the Bank adopted an exception to its policy barring international consumer remittance transfers under which the Bank may offer those transfers but will never perform more than 99 such transfers in any given year. The Bank did so in order to fall within the Remittance Rule exception for banks performing under 100 international consumer remittance transfers annually.

19. But for the Remittance Rule, the Bank would offer an international consumer remittance transfer to any customer that requested it, even if the Bank exceeded 100 transfers each year.

20. The Bureau's Remittance Rule has caused the Bank financial harm. The Bank lost income on the international consumer remittance transfers it declined to offer after the adoption of the original Rule. In addition, the revised Remittance Rule limits the Bank's opportunity to expand that transfer business in the future. The Rule therefore has placed the Bank at a competitive disadvantage vis-à-vis other (typically larger) banks that can afford to offer remittances under the Rule without limitation, a service expected of a lending institution from its existing and prospective customers.

Mortgage Lending

21. In addition to authorizing the CFPB to regulate remittance transfers, the Dodd-Frank Act prohibits unfair, deceptive, and abusive consumer financial practices and authorizes the Bureau to identify what those practices entail and to take or recommend enforcement against institutions that engage in such practices. 12 U.S.C. § 5531(a)-(b).

22. The Director of the Bureau, Richard Cordray, has acknowledged the abstract

nature of the term "abusive," explaining in a January 24, 2012 hearing before a subcommittee of the U.S. House Committee on Oversight and Government Reform, that it is "a little bit of a puzzle because it is a new term" and is "not something [the Bureaus is] likely to be able to define in the abstract. Probably not useful to try to define a term like that in the abstract; we are going to have to see what kind of situations may arise where that would seem to fit the bill under the prongs."

23. Government officials have repeatedly stated that the Bureau's enforcement efforts will focus on mortgage lending practices. President Obama stated that the Bureau would "crack down on the abusive practice of unscrupulous mortgage lenders" on September 17, 2010. In March 2012, Director Cordray reiterated the Bureau's intention to "address the origination of mortgages, including loan originator compensation and the origination of high-priced mortgages."

24. Up until the last quarter of 2010, the Bank offered consumers several types of mortgages, including mortgages with five-year balloon payments and "character loans," which are loans based on the borrower's known character in addition to estimates of the borrower's ability to repay.

25. Before leaving the market, the Bank offered several loans at interest rates that were at least 1.5% higher than the Average Prime Offer Rate, as calculated with reference to the "Average Prime Offer Rates – Fixed" listed at http://www.ffiec.gov/ratespread/aportables.htm. Had it continued to offer consumer mortgage loans, it would have expected many of them to be of this character.

26. Based on statements Government officials made after the enactment of Dodd-Frank concerning the Bureau's authority over mortgage practices and the limits the Bureau could

impose on those practices, the Bank became concerned that the Bureau might retroactively deem its mortgage loans abusive. The Bank is a local, community bank, and it operates under different internal guidelines than other financial institutions. For example, the Bank's charter specifically provides that the Bank will serve the community, and the Bank therefore focuses on serving the needs of the community. The Bank does not sell its loans. As a result, the Bank has offered mortgages to its customers, based on its knowledge of their character and circumstances, that other institutions have been (and still today would likely be) unwilling to provide. The Bank would continue this practice of serving the community if it were to reenter the mortgage market.

27. For example, if the Bank were approached by a young couple whose income alone did not suggest ability to repay under traditional standards, but the Bank knew the parents of the couple were members of the community who themselves would be willing and able to pay for the mortgage, even if they were not themselves on the note, the Bank would be willing and able to offer that couple the mortgage. But the Bank would be concerned that the Bureau, looking at only the figures directly involved in such a loan, and not the unique circumstances the Bank evaluates as a community banker making that loan, would deem it abusive.

28. As another example, the Bank in the past made a loan with a 50% debt-to-income ratio to a borrower because the Bank had engaged in past transactions with the customer and knew that the customer—a single head-of-household whose credit had been negatively impacted by a previous relationship—would repay the obligations the customer incurred, even if the customer's former spouse had not.

29. When the Bank became concerned that it could not safely offer mortgages consistent with the Bureau's authority under the Dodd-Frank Act, the Bank expressed its concerns to officials at its prudential regulator, the Office of the Comptroller of the Currency (the

"OCC"). The OCC provided the Bank with no reassurance that it could remain in the market without fear of prosecution under the Bank's then-current practices.

30. In the last quarter of 2010, the Bank decided to exit the consumer mortgage business and determined that it would no longer offer any consumer mortgage loans. The Bank did so due to fear that those loans would be subject to enforcement action under the Dodd-Frank Act because they might be deemed to violate the prohibition against unfair, deceptive, and abusive practices.

31. The Bank also recognized that if it attempted to stay in the consumer mortgage market, it would have to incur significant additional costs to comply with proposed regulations governing mortgage loans, and thus would not be able to offer them in the cost-effective manner to which it was previously accustomed.

32. For example, if the Bank were to reenter the mortgage market and offer the terms it previously provided on consumer mortgage loans, many of the mortgages would constitute higher-priced covered transactions under the Bureau's new regulations. That means the loans would not fall within the safe harbor created by the Bureau pursuant to which the Bank could not be held liable to the borrower or to the Government on the theory that it did not adequately consider the borrower's ability to repay. The Bureau's regulations providing the Bank with only a rebuttable presumption of an adequate investigation, but otherwise leaving it subject to the costs of litigation, would require the Bank to reconsider whether it could offer the customer the loan at all and would impose an additional risk factor that would affect the costs and structure of the loan if the Bank were to offer it.

33. The Bank's inability to offer mortgages has harmed it financially in a number of ways. First, the Bank's mortgage business was regularly profitable. It was one of the best and

most prudent ways to invest and earn a return on the Bank's deposits and also one of the best ways for the Bank to reinvest in the community. The Bank's alternative use of funds is not as profitable.

34. Moreover, the Bank can no longer offer the full array of mortgage services existing and prospective customers expect of a lending institution, putting the Bank at a competitive disadvantage.

35. Finally, the Bureau's new rules governing mortgage foreclosure increase the Bank's costs of doing business. On January 17, 2013, the Bureau issued a rule that governs, among other things, the mortgage loan foreclosure process. *See* Mortgage Servicing Rules under the Real Estate Settlement Procedures Act (Regulation X) (Jan. 17, 2013), *available at* http://www.consumerfinance.gov/regulations/2013-real-estate-settlement-procedures-act-regulation-x-and-truth-in-lending-act-regulation-z-mortgage-servicing-final-rules/. Under this rule, "[a] small servicer shall not make the first notice or filing required by applicable law for any judicial or non-judicial foreclosure process unless a borrower's mortgage loan obligation is more than 120 days delinquent." *Id.* at 696 (to be codified at 12 CFR §1024.41(j)).

36. Although the Bank no longer makes new consumer mortgage loans, it still holds several such loans from previous years that have yet to be satisfied. Under Texas law, the Bank could initiate foreclosure proceedings on such a loan, should the borrower default, if the borrower did not cure that default within 20 days of a letter notifying him of the delinquency. *See* Tex. Prop. Code Ann. § 51.002(a), (b), (d) (West 2012). After those 20 days expired, the Bank could post a foreclosure notice at the courthouse, file the notice with the county clerk, and notify the borrower of the foreclosure sale, which could be held as soon as 21 days thereafter. *Id.* Even if the Bank does not intend to actually foreclose on a defaulted borrower, posting a

foreclosure notice at the courthouse soon after a default can be a useful tool to induce such a borrower to get current on their payments—but the Bank is now prohibited by the Bureau's new rule from doing so for 120 days. The Bureau's new rule will increase the Bank's costs by drawing out the process by which the Bank may seek to recover on a defaulted loan.

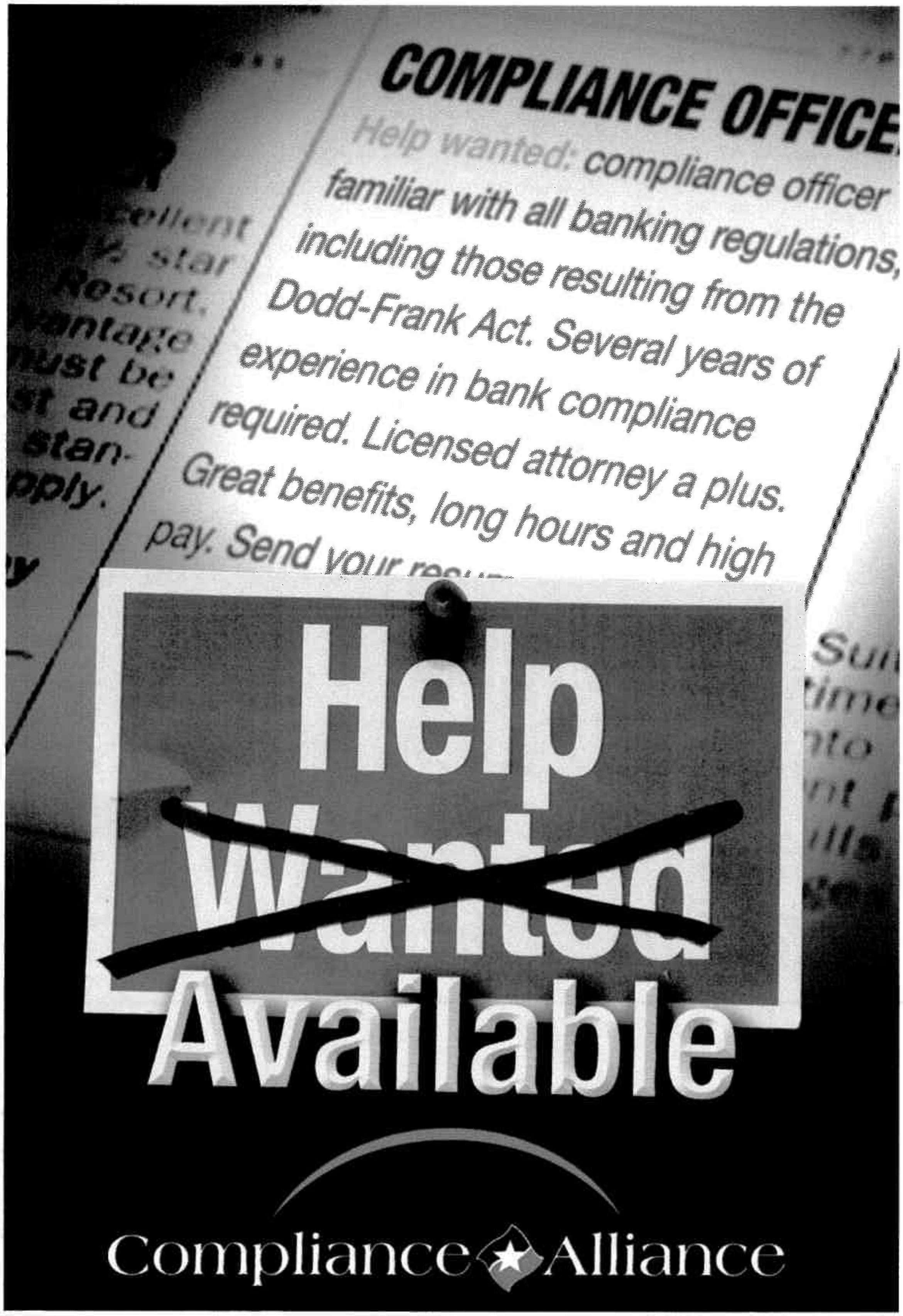
37. Any new loans the Bank would make would also be subject to the Bureau's foreclosure limitations.

38. But for the Bureau, its rules, and its enforcement authority, the Bank would reenter the consumer mortgage and remittance markets without limitation.

I declare under penalty of perjury that the foregoing is true and correct.

Executed on February 12, 2013, at Big Spring, Texas.

Jim R. Purcell


COMPLIANCE OFFICE
Help wanted: compliance officer
familiar with all banking regulations,
including those resulting from the
Dodd-Frank Act. Several years of
experience in bank compliance
required. Licensed attorney a plus.
Great benefits, long hours and high
pay. Send your
Help
~~Wanted~~
Available
Compliance Alliance

Compliance Alliance

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Drowning in a sea
of regulations?
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A SUBSIDIARY OF THE TEXAS BANKERS ASSOCIATION

The Industry – Ready or Not – *It's Coming…*

- You have undoubtedly heard and read much about the compliance and operational impacts of the Dodd-Frank Act.
- The Dodd-Frank Act will have a significant and costly effect on traditional banks.
- Banks should pay close attention to the rules, regulations and statements that come from the newly created CFPB and other regulatory banking agencies.
- Each of these new compliance mandates will affect consumer financial products and services and enterprise risk management throughout the bank.

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Survey Says…

- Survey results indicated that banks plan to hire or redirect one or more FTEs to handle compliance needs
- Average salary for a compliance officer is $62,000 plus benefits (Based on TBA Salary Survey)

Research Says…

TBA is a member-driven Association that strives to meet our members' needs. When we saw the insurmountable compliance burden grow for our members, we set out to help our members navigate through the complexity of the compliance maze.

- **Held a Compliance Focus Group meeting in 2010, comprised of 16 banking compliance personnel from TBA member banks across the state to explore ways to ease the compliance and regulatory burdens on banks.**
- **Surveyed our TBA Board of Directors to get feedback on their plans to adapt to the compliance and operational impacts of the Dodd-Frank Act.**

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What we found…

Compliance Focus Group

Focus Group Findings:

- Understaffed. Bank employees spreading compliance duties across departments to accommodate the load
- Hard to track. Bankers' need for a simple calendar to track all things compliance and the mandatory effective dates
- Mundane tasks. There is an enormous amount of tedious tasks related to taking a new regulation from introduction to policy
- Trusted source. There are other compliance website resources out there, but can they be trusted?
- One location. Other compliance websites may have one or two beneficial resource tools, but there is not one site that offers it all, which creates multiple and time consuming web searches. There is a need for a one-stop, up-to-date and trusted website
- Full Capacity. Compliance staff are already overloaded with the current level of regulations – How will they survive the 200+ coming?
- Extra Set of Hands. Compliance staff repeatedly reported the need for an extra set of hands. Hiring is one option, but leveraging the expertise and economies of scale with a trusted and knowledgeable third party will be more economical and free up existing staff's time to take on more.

What we do…

Compliance Alliance Benefits:

- Cliff Notes on New Regulations (White Papers)
- Policy Templates
- Procedures
- Processes
- Action Plans
- Lending Matrices
- Compliance Hotline

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What we do…

Compliance Alliance Benefits:

- Cheat Sheets
- Checklists
- Worksheets
- Compliance Calendar
- Risk Assessment Tools
- Tracking Tools
- Review of Advertising and Marketing
- Review of Website

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What we do…

Compliance Alliance Benefits:

- Evaluate new products to ensure compliance
- Review Disclosures
- Training Tools
- Statutes
- Regulations
- Rules
- Interpretations
- Compliance Webinars
- Compliance Newsletter

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What we do…

Compliance Alliance Benefits:

- Forms
- Notices
- Website
- Notification of changes, updates, and news
- FAQs
- And more to come…

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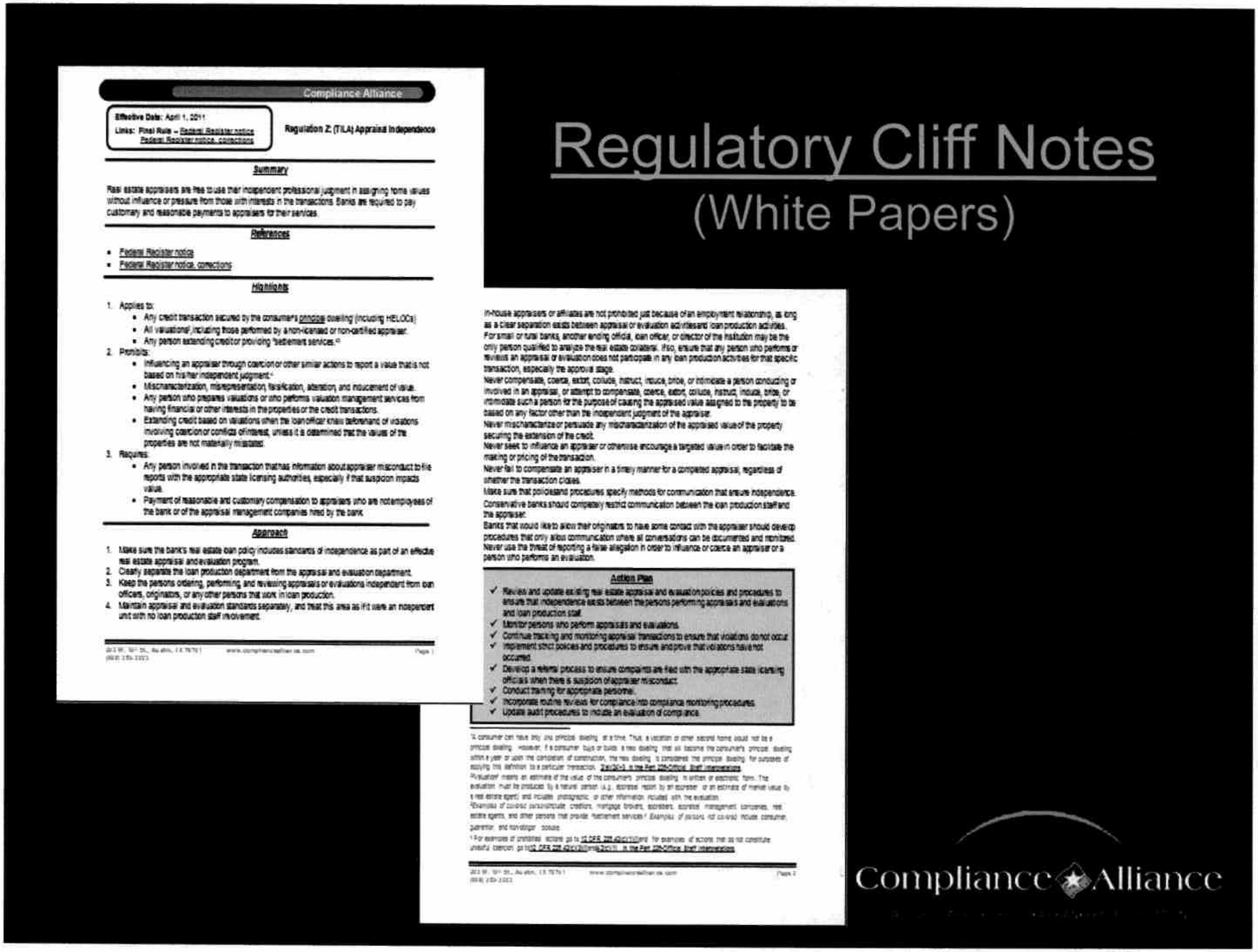

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Effective Date: April 1, 2011
Links: Final Rule – Federal Register notice
Federal Register notice, corrections

Regulation Z (TILA) Appraisal Independence

Summary

Real estate appraisers are free to use their independent professional judgment in assigning home values without influence or pressure from those with interests in the transactions. Banks are required to pay customary and reasonable payments to appraisers for their services.

References

- Federal Register notice
- Federal Register notice, corrections

Highlights

1. Applies to:
   - Any credit transaction secured by the consumer's principal dwelling (including HELOCs)
   - All valuations, including those performed by a non-licensed or non-certified appraiser.
   - Any person extending credit or providing "settlement services."
2. Prohibits:
   - Influencing an appraiser through coercion or other similar actions to report a value that is not based on his/her independent judgment.
   - Mischaracterization, misrepresentation, falsification, alteration, and inducement of value.
   - Any person who prepares valuations or who performs valuation management services from having financial or other interests in the properties or the credit transactions.
   - Extending credit based on valuations when the loan officer knew beforehand of violations involving coercion or conflicts of interest, unless it is determined that the values of the properties are not materially misstated.
3. Requires:
   - Any person involved in the transaction that has information about appraiser misconduct to file reports with the appropriate state licensing authorities, especially if that suspicion impacts value.
   - Payment of reasonable and customary compensation to appraisers who are not employees of the bank or of the appraisal management companies hired by the bank.

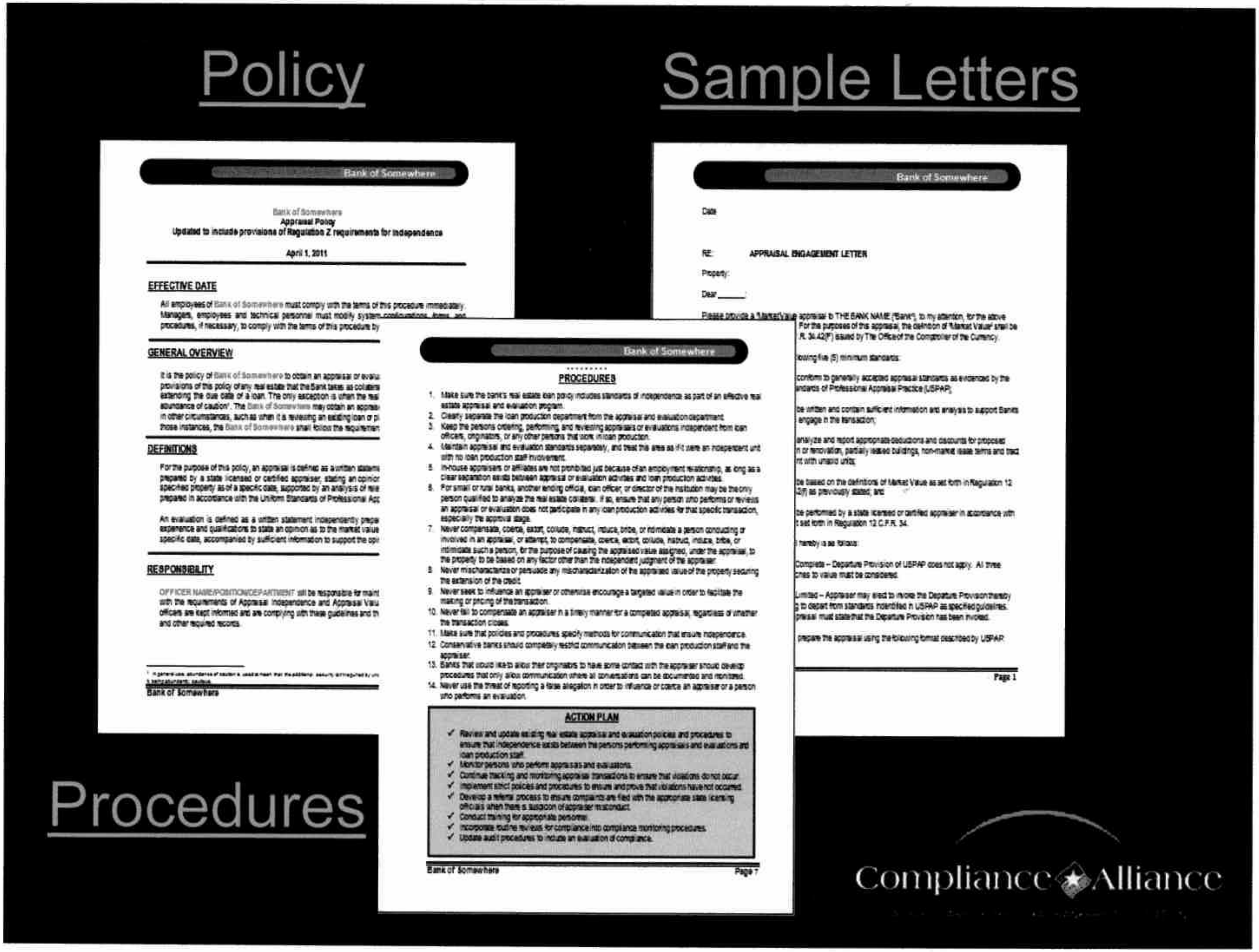
Approach

1. Make sure the bank's real estate loan policy includes standards of independence as part of an effective real estate appraisal and evaluation program.
2. Clearly separate the loan production department from the appraisal and evaluation department.
3. Keep the persons ordering, performing, and reviewing appraisals or evaluations independent from loan officers, originators, or any other persons that work in loan production.
4. Maintain appraisal and evaluation standards separately, and treat this area as if it were an independent unit with no loan production staff involvement.

In-house appraisers or affiliates are not prohibited just because of an employment relationship, as long as a clear separation exists between appraisal or evaluation activities and loan production activities.
For small or rural banks, another lending official, loan officer, or director of the institution may be the only person qualified to analyze the real estate collateral. If so, ensure that any person who performs or reviews an appraisal or evaluation does not participate in any loan production activities for that specific transaction, especially the approval stage.
Never compensate, coerce, extort, collude, instruct, induce, bribe, or intimidate a person conducting or involved in an appraisal, or attempt to compensate, coerce, extort, collude, instruct, induce, bribe, or intimidate such a person for the purpose of causing the appraised value assigned to the property to be based on any factor other than the independent judgment of the appraiser.
Never mischaracterize or persuade any mischaracterization of the appraised value of the property securing the extension of the credit.
Never seek to influence an appraiser or otherwise encourage a targeted value in order to facilitate the making or pricing of the transaction.
Never fail to compensate an appraiser in a timely manner for a completed appraisal, regardless of whether the transaction closes.
Make sure that policies and procedures specify methods for communication that ensure independence.
Conservative banks should completely restrict communication between the loan production staff and the appraiser.
Banks that would like to allow their originators to have some contact with the appraiser should develop procedures that only allow communication where all conversations can be documented and monitored.
Never use the threat of reporting a false allegation in order to influence or coerce an appraiser or a person who performs an evaluation.

Action Plan

- ✓ Review and update existing real estate appraisal and evaluation policies and procedures to ensure that independence exists between the persons performing appraisals and evaluations and loan production staff.
- ✓ Monitor persons who perform appraisals and evaluations.
- ✓ Continue tracking and monitoring appraisal transactions to ensure that violations do not occur.
- ✓ Implement strict policies and procedures to ensure and prove that violations have not occurred.
- ✓ Develop a referral process to ensure complaints are filed with the appropriate state licensing officials when there is suspicion of appraiser misconduct.
- ✓ Conduct training for appropriate personnel.
- ✓ Incorporate routine reviews for compliance into compliance monitoring procedures.
- ✓ Update audit procedures to include an evaluation of compliance.


Policy
Sample Letters
Procedures
Bank of Somewhere
Bank of Somewhere
Appraisal Policy
Updated to include provisions of Regulation Z requirements for independence
April 1, 2011
EFFECTIVE DATE
GENERAL OVERVIEW
DEFINITIONS
RESPONSIBILITY
APPRAISAL ENGAGEMENT LETTER
PROCEDURES
ACTION PLAN
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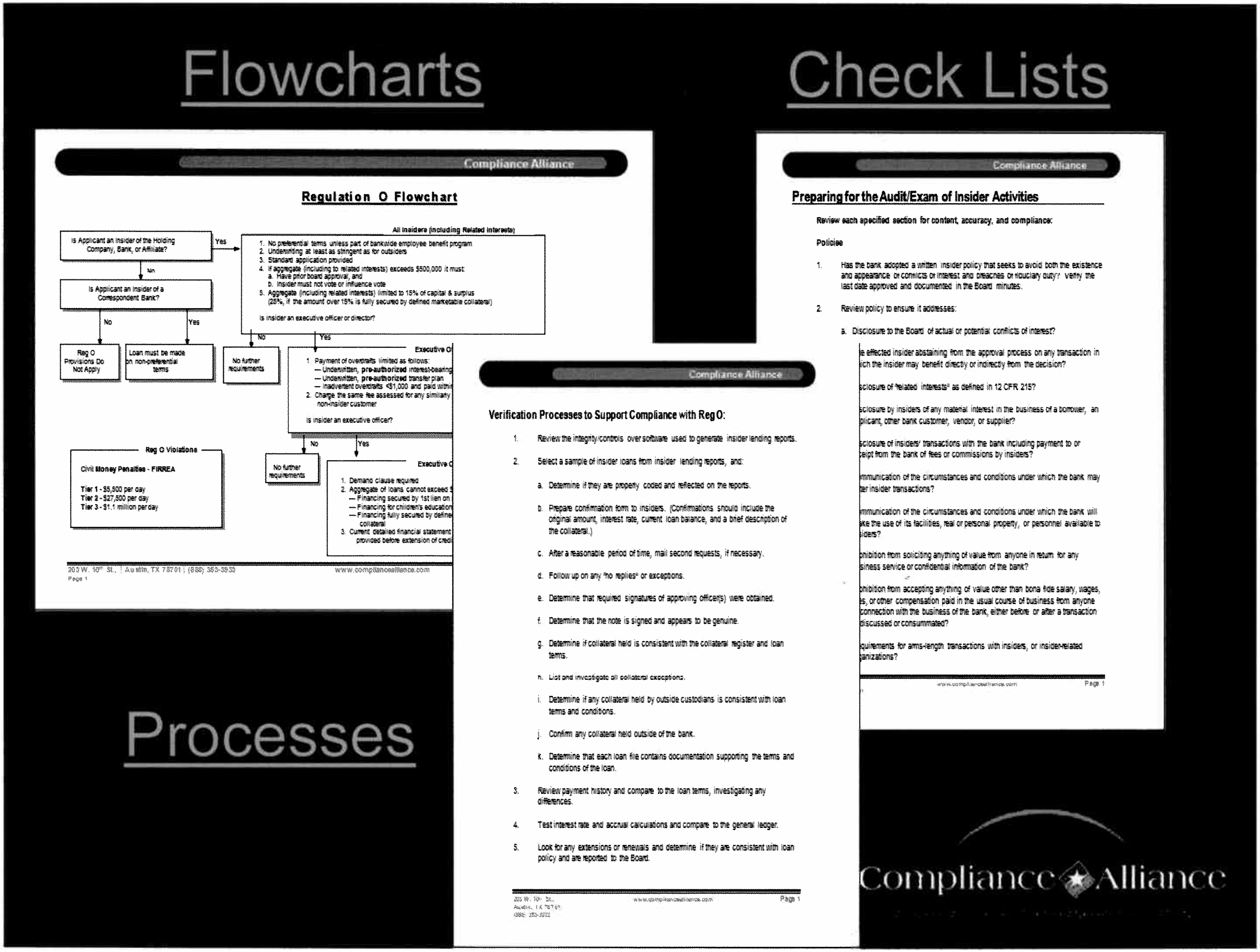
Flowcharts
Check Lists
Processes
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Regulation O Flowchart
Is Applicant an Insider of the Holding Company, Bank, or Affiliate?
Yes
No
Is Applicant an Insider of a Correspondent Bank?
No
Yes
Reg O Provisions Do Not Apply
Loan must be made on non-preferential terms
All Insiders (including Related Interests)
1. No preferential terms unless part of bankwide employee benefit program
2. Underwriting at least as stringent as for outsiders
3. Standard application provided
4. If aggregate (including to related interests) exceeds $500,000 it must:
a. Have prior board approval, and
b. Insider must not vote or influence vote
5. Aggregate (including related interests) limited to 15% of capital & surplus (25%, if the amount over 15% is fully secured by defined marketable collateral)
Is insider an executive officer or director?
No
Yes
No further requirements
1. Payment of overdrafts limited as follows:
— Unwritten, pre-authorized interest-bearing
— Unwritten, pre-authorized transfer plan
— Inadvertent overdrafts <$1,000 and paid within
2. Charge the same fee assessed for any similarly non-insider customer
Is insider an executive officer?
No
Yes
No further requirements
1. Demand clause required
2. Aggregate of loans cannot exceed
— Financing secured by 1st lien on
— Financing for children's education
— Financing fully secured by defined collateral
3. Current detailed financial statement provided before extension of credit
Reg O Violations
Civil Money Penalties - FIRREA
Tier 1 - $5,500 per day
Tier 2 - $27,500 per day
Tier 3 - $1.1 million per day
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Page 1
Preparing for the Audit/Exam of Insider Activities
Review each specified section for content, accuracy, and compliance:
Policies
1. Has the bank adopted a written insider policy that seeks to avoid both the existence and appearance of conflicts of interest and breaches of fiduciary duty? Verify the last date approved and documented in the Board minutes.
2. Review policy to ensure it addresses:
a. Disclosure to the Board of actual or potential conflicts of interest?
Page 1
Verification Processes to Support Compliance with Reg O:
1. Review the integrity/controls over software used to generate insider lending reports.
2. Select a sample of insider loans from insider lending reports, and:
a. Determine if they are properly coded and reflected on the reports.
b. Prepare confirmation form to insiders. (Confirmations should include the original amount, interest rate, current loan balance, and a brief description of the collateral.)
c. After a reasonable period of time, mail second requests, if necessary.
d. Follow up on any "no replies" or exceptions.
e. Determine that required signatures of approving officer(s) were obtained.
f. Determine that the note is signed and appears to be genuine.
g. Determine if collateral held is consistent with the collateral register and loan terms.
h. List and investigate all collateral exceptions.
i. Determine if any collateral held by outside custodians is consistent with loan terms and conditions.
j. Confirm any collateral held outside of the bank.
k. Determine that each loan file contains documentation supporting the terms and conditions of the loan.
3. Review payment history and compare to the loan terms, investigating any differences.
4. Test interest rate and accrual calculations and compare to the general ledger.
5. Look for any extensions or renewals and determine if they are consistent with loan policy and are reported to the Board.
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Another Training Tool

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Regulatory Policy & Training Requirements and Penalties

Regulation	Policies **	Training	Penalties for non compliance
Regulation B, Equal Credit Opportunity Act	Expected	Strongly Recommended For New Account and Loan Personnel	• FIRREA Penalties Civil liability: • Actual damages • Punitive damages: a. $10,000 in individual cases, b. the lesser of $500,000 or 1% of the creditor's net worth in class action suits • Attorney's fees
Regulation C, Home Mortgage Disclosure Act	Expected	Recommended Regularly For New Account and Loan Personnel (Consumer Compliance Handbook Examination Manual p 122)	• FIRREA Penalties
Regulation D, Reserve Requirements of Depository Institutions	Expected	Recommended Regularly For New Account Personnel	• FIRREA Penalties: Civil penalties are available; Federal Reserve may waive penalties exempt for gross negligence or willful noncompliance
Regulation E, Electronic Fund Transfer Act	Expected	Recommended Regularly For Teller and New Account Personnel (Consumer Compliance Handbook Examination Manual pg 25)	• FIRREA Penalties Civil liability: • Actual damages • Court costs and attorney's fees Criminal liability: • Fines up to $5,000 and/or imprisonment of up to one year for knowingly giving false information • Fines up to $10,000 and/or imprisonment for 10 years for forgery, counterfeiting, and stealing debit devices
Flood Insurance Flood Disaster Protection Act	Expected 12 CFR 208.25	Recommended Regularly For New Account and Loan Personnel 12 CFR 208.25	• FIRREA Penalties Statutory penalties: • $385 per violation • Up to $125,000 per lender per, calendar year Potential of negligence liability if lender does not comply with the act and the borrower's property is damaged or destroyed
Regulation M, Consumer Leasing			- FIRREA Penalties Civil liability: • Actual damages • Court costs, attorney's fees • Statutory damages ($100 to $1,000) • Class Actions ($500,000 or 1% of the creditor's net worth, whichever is less) Criminal liability

Risk Assessment Tools

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Fair Lending Risk Assessments

Directions: In this Assessment, summarize the factors supporting the Level of Risk, the Aggregate Level, and the Direction by checking Low, Moderate, or High ... , or High boxes in the Totals Box below to determine your bank's overall

Quantity of Risk

High	L	M	H	Comments
...able volume of consumer ...ld be discouraging to				
...products offered (e.g., sub-...ortgages, etc). Prime and ... offered appear similar.				
...licy exceptions/overrides.				
...ows a high level of subjective ...actors.				
...ities among approval/denial ... basis groups.				
...ithdrawn/incomplete ...ohibited basis groups.				
... in lending patterns identified ...e.				

...alliance.com Page 1

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Overall Compliance Risk Assessments

Directions:
In this Assessment, summarize the factors supporting the Level of Risk, the Aggregate Level, and the Direction by checking Low, Moderate, or High for each category. Then, total the number of check marks for each of the Low, Moderate, or High boxes in the Totals Box below to determine your bank's overall risk. Please be sure to also note comments regarding your bank's status for each category.

QUANTITY OF COMPLIANCE RISK INDICATORS

LOW	MODERATE	HIGH	L	M	H	COMMENTS
Violations or noncompliance issues are insignificant, as measured by their number or seriousness.	The frequency or severity of violations or noncompliance is reasonable.	Violations or noncompliance expose the company to significant impairment of reputation, value, earnings, or business opportunity.				
The institution has a good record of compliance. The bank has a strong control structure that has proven effective. Compliance management systems are sound and minimize the likelihood of excessive or serious future violations or noncompliance.	The institution has a satisfactory record of compliance. Compliance management systems are adequate to avoid significant or frequent violations or noncompliance.	The institution has an unsatisfactory record of compliance. Compliance management systems are deficient and reflect an inadequate commitment to risk management.				
Management fully understands all aspects of compliance risk and exhibits a clear commitment to compliance. The commitment is communicated throughout the institution.	Management reasonably understands the key aspects of compliance risk. Its commitment to compliance is reasonable and satisfactorily communicated.	Management does not understand, or has chosen to ignore, key aspects of compliance risk. The importance of compliance is not emphasized or communicated throughout the organization.				

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Cheatsheets

Quick Reference Info Chart for Corporate Accounts	
STYLE OF ACCOUNT AND OWNERSHIP OF FUNDS	The account should be styled in the legal name of the entity¹. For example: • Food Market, Inc. • Food Market, Corporation • Food Market, Inc., DBA Sunset Produce (assumed name certificate required)
TAXPAYER IDENTIFICATION NUMBER (TIN) REQUIREMENTS	EIN is required, and SSNs are never permissible. Certification of the EIN is provided by the officer of the corporation.
DOCUMENTATION	The following documentation should be obtained at the time the account is opened: 1. Signature card signed by those persons authorized to sign on the account; 2. EIN certification signed by one of the officers of the corporation; 3. Certificate of Corporate Resolution (TX)²; 4. Certified copy of Certificate of Formation (or Articles of Incorporation if formed before January 1, 2006), and Certificate of Filing (TX); 5. Certificate of Authority for foreign corporations (TX); 6. Assumed name certificate if applicable (TX, CIP).
INFORMATION	The following CIP information is required: 1. Name of corporation; 2. Address of corporation; 3. EIN; and 4. Corporate Resolution. **Tip:** Find or verify proof of corporation's legal existence and assumed name documentation on the Texas Secretary of State's (SOS's) website, http://www.sos.state.tx.us/. **Tip:** Obtain the name and address of the corporation's registered agent.³ This can be found on the SOS's website. **Tip:** To add/remove signers a financial institution will need a new corporate resolution and a new signature card. **FDIC Corporate Accounts Coverage Limits:** ✓ $ 250,000 per corporation

¹Legal name of the entity includes the form of organization.
² (TX) means under Texas law.
³A registered agent may be a business or individual designated to receive service of process when a business entity is a party in a legal action such as a lawsuit or summons.

Quick Reference Info Chart for Revocable Living Trust Accounts	
STYLE OF ACCOUNT AND OWNERSHIP OF FUNDS	*The account should be styled either in the name of the trust or in the name(s) of the trustee(s).* For example: • John Doe Revocable Living Trust, John Doe, Trustee; or • Doe Family Trust, John Doe, Trustee *The funds in the trust account are owned by the grantor. Trustees just manage the trust.*
TAXPAYER IDENTIFICATION NUMBER (TIN) REQUIREMENTS	Either the grantor's SSN (trustee must have grantor sign the SSN certification), or EIN certified by the trustee.
DOCUMENTATION	***Documents should be obtained at the time a deposit account is opened.*** Documents include: 1. Signature card signed only by the trustee(s); 2. TIN (SSN) or EIN certification; 3. Trust Authorization and Agreement; and 4. A copy of the trust agreement, or certificate of trust (affidavit). ***The certificate of trust should include*** (sample model): 1. Trust date; 2. Names of trustee and successor trustees, if any; 3. Name and address of each beneficiary; 4. Powers granted to the trustee; and 5. Indemnification¹ of the bank.
INFORMATION	***The following CIP information is required from the grantor(s) at the time the deposit account is opened:*** 1. Name; 2. Date of birth; 3. Physical address of residence; 4. Appropriate TIN; and 5. Proof of trust indicate. ***FDIC Coverage Limits:*** ✓ $ 250,000 for each named beneficiary, or the total amount allocated to each beneficiary, whichever is greater. ✓ Trustees, co-trustees, and successor trustees are not relevant.

¹ Under Texas Statute, the indemnification should specify that, "The bank is not liable for administering the account as provided by the certificate of trust, even if the certificate of trust is contrary to the terms of the trust agreement, unless the bank has actual knowledge of the terms of the trust agreement."

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Loan Matrix

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CHARACTERISTICS OF LOAN REQUEST				REG B		FCRA	REG C	REG Z							RESPA					REG AA	REG H
TYPE OF SECURITY	USE OF SECURITY	USE OF PROCEEDS	INS. DISC.	WRITTEN APP.	NOTICE OF RIGHT TO RECEIVE COPY OF APPRAISAL	NOTICE TO HOME LOAN APPLICANT	(GOV. MON. INFO) HMDA	HOME EQUITY BROCHURE & PROGRAM DISC.	ARM BOOKLET & PROGRAM DISC.	HOEPA (NA if purchase)	HPML CHECK LIST	EARLY TIL DISC.	TIL DISC.	RIGHT TO RESCIND	BUYING YOUR HOME BOOKLET	GOOD FAITH ESTIMATE	MTG. SERV. DISC. (1ST LIENS ONLY)	HUD-1 OR HUD-1A	INITIAL ESCROW STMT. (if escrow)	NOTICE TO CO-SIGNER	FLOOD CHECK
Consumer goods, raw land, unsecured	Consumer use	Purchase	X	Personal									X							X	
		Refinance	X	Personal									X							X	
		Equity	X	Personal									X							X	
	Business use	Purchase, refi, equity		CAA*																	
Residential dwelling of 1-4 families, or a mobile home (less than 25 acres)	Primary Residence	Purchase	X	URLA	X	X	X		X**		X	X	X		X*	X*	X*	X*	If Escrow	X	X
		Refinance	X	URLA	X	X	X		X**	X	X	X	X	X		X*	X*	X*	If Escrow	X	X
		Home Improvement	X	URLA	X	X	X		X**	X	X	X	X	X		X*	If 1st lien	X*	If Escrow	X	X
		Bridge to Purchase		Home Equity	X	X						X	X	X						X	X
		Home Equity (non-HMDA)	X	Home Equity	X	X			X**	X	X	X	X	X		X*	If 1st lien	X*	If Escrow	X	X
		HELOC (open end)(& 2nd home)	X	Home Equity	X	X		X						X						X	X
		Business or Ag		CAA*	X	XX	If HMDA														X
	Rental House	Purchase, refi, improvement		CAA*	X	XX	X														X
		Home Equity-consumer	X	Home Equity	X	X			X**			X	X			X*	If 1st lien	X*	If Escrow	X	X
		Home Equity-business		CAA*	X	XX															X
	Secondary or other residence	Purchase, refi, improvement	X	URLA	X	X	X					X	X		X*	X*	X*	X*	If Escrow	X	X
		Home Equity	X	Home Equity	X	X						X	X			X*	If 1st lien	X*	If Escrow	X	X
Residential dwelling of 1-4 families, or a mobile home (25 acres or more)	Primary Residence	Purchase	X	URLA	X	X	X		X**		X	X	X							X	X
		Refinance	X	URLA	X	X	X		X**	X	X	X	X	X						X	X
		Home Improvement	X	URLA	X	X	X		X**	X	X	X	X	X						X	X
		Home Equity (non-HMDA)	X	Home Equity	X	X			X**	X	X	X	X	X						X	X
		HELOC (open end)	X	Home Equity	X	X		X						X						X	X
		Business or Ag		CAA*	X	XX	If HMDA														X
Raw Land	Primary Residence	Construction to Permanent	X	URLA	X	X	X		X**		X	X	X		X*	X*	X*	X*	If Escrow	X	X

Current Compliance Alliance Staff Experience

- One Attorney with 18 Years Banking Experience
- One Attorney with 9 Years Banking Experience
- One Compliance Specialist with 13 years at OCC and 14 years of Compliance and Auditing Experience
- One Compliance Specialist with 25 years of Bank Compliance Experience

Compliance Alliance

We listened to you…
and designed
a bank compliance company
for bankers by bankers.

Compliance Alliance

Compliance Alliance Pricing

Three Year Contract – signed by 08/15/11	Three Year Contract – signed after 08/15/11	One Year Contract
$12,000/ yr.	**$15,000/ yr.**	**$18,000/ yr.**

Compliance Alliance

Join Compliance Alliance

- **Due to the vast interest and demand for service, Compliance Alliance will start servicing banks based on the order of sign-up.**

- To join, please contact us at:

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  compliancealliance@texasbankers.com

Compliance Alliance

CFPB Issues Rule To Protect Consumers From Irresponsible Mortgage Lending

01/10/13

CFPB Issues Rule to Protect Consumers from Irresponsible Mortgage Lending

Today the Consumer Financial Protection Bureau (CFPB) adopted a new rule that will protect consumers from irresponsible mortgage lending by requiring lenders to ensure prospective buyers have the ability to repay their mortgage. The rule also protects borrowers from risky lending practices such as "no doc" and "interest only" features that contributed to many homeowners ending up in delinquency and foreclosure after the 2008 housing collapse.

"When consumers sit down at the closing table, they shouldn't be set up to fail with mortgages they can't afford," said CFPB Director Richard Cordray. "Our Ability-to-Repay rule protects borrowers from the kinds of risky lending practices that resulted in so many families losing their homes. This common-sense rule ensures responsible borrowers get responsible loans."

Leading up to the mortgage crisis, certain lenders originated mortgages to consumers without considering their ability to repay the loans. The gradual deterioration in underwriting standards led to dramatic increases in mortgage delinquencies and rates of foreclosures. What followed was the collapse of the housing market in 2008 and the subsequent financial crisis. The 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act created broad-based changes to how creditors make loans and included new ability-to-repay requirements, which the CFPB is charged with implementing. Read more.

Read Other news

CFPB Launches Inquiry On Campus Financial Products

01/31/13

CFPB Launches Inquiry on Campus Financial Products

The Consumer Financial Protection Bureau (CFPB) announced that it is launching an inquiry into the impact of financial products marketed to students through colleges and universities. The CFPB intends to use the information gathered to determine whether these arrangements are in the best interest of students.

"We have seen many colleges establish relationships with financial institutions to offer banking services to their students," said CFPB Director Richard Cordray. "The Bureau wants to find out whether students using college-endorsed banking products are getting a good deal."

The Credit CARD Act of 2009 (CARD Act) restricted financial institutions from using certain types of marketing practices on college campuses. The CARD Act also made agreements between credit card issuers and institutions of higher education subject to public disclosure. However, less is known about arrangements regarding other products marketed to students. To better understand the market, the CFPB is publishing today a Notice and Request for Information on the topic of campus financial products. Campus financial products include student identification cards that double as debit cards, cards used to access scholarships and student loans, and school-affiliated bank accounts. Read more.

Read Other news

Compliance Alliance

April 10, 2012

Email to a friend

REMEMBER CONSUMER COMPLAINTS WHEN REVIEWING YOUR OVERDRAFT PROGRAM

In the wake of the comment period ending for overdrafts, we wanted to address an important component to remember when reviewing your overdraft program, whether it is automated or ad hoc.

If you have been out in the trenches you know that customers seem to have shorter fuses these days. Aggravation and stress levels seem higher than normal. Right in the middle of the aggravation, the regulatory agencies are going to make sure the stakes for keeping our customers happy have never been higher, especially now that the new Consumer Financial Protection Bureau has "gone live."

One of the first icons that any visitor to the Consumer Financial Protection Bureau's home page sees is a reddish box labeled "Submit a credit card complaint." That is just the first complaint reporting function the Bureau plans.

"The Dodd-Frank Act directs the CFPB to facilitate the collection and monitoring of and response to consumer complaints regarding certain financial products and services. These complaints and consumers' inquiries will help the CFPB identify areas of concern and will help the CFPB in its supervision and other responsibilities."

How the Bureau will handle complaints remains to be seen. But bank regulators have already stepped up their own attention to consumer complaints, both those filed with the agencies and those made to banks directly. New channels for complaints, ranging from tweets on Twitter and demonstrative videos on YouTube to angry blogs and more, underscore that consumer dissatisfaction with their financial services providers have entered a new age.

The message to remember is ... Don't wait for Washington to come to you. Before you get a visit from the regulators or the Department of Justice, your bank should have a process in place to address consumer complaints. The complaints that are coming in should be being used as an early warning system to protect customers and the bank from an unintentional problem. It is important to note that anything the customers are telling the banks, good or bad, can be used to "control our destiny." Don't wait for the Consumer Financial Protection Bureau or other regulatory agencies to notify the bank that they have received numerous complaints about your overdraft checking program.

Complaints represent an opportunity to spot weaknesses, places where the bank needs to improve processes, procedures, or, where those are correct, communication with consumers so they understand what is going on. Regulators' exam procedures now stress not only that examiners review a bank's complaints management process, but weigh how well the bank is dealing with what its systems track.

The Federal Reserve exam manual procedure states: "Determine whether the bank reviews consumer complaints to identify potential compliance problems and negative trends that have the potential to be unfair or deceptive. Determine whether the bank reviews concentrations of complaints about the same product or about bank conduct in order to identify potential areas of concern."

It is not unusual for consumers, when first sending a letter of complaint, for instance, to ramp things up immediately. They not only write to the bank, but carbon copy all banking regulators.

A strong complaint management system will give a bank an overview of six critical factors:

1. Overall volume of complaints.

2. Number of open complaints at a given time, versus resolved complaints.

3. Number of complaints open for a given length of time.

4. Number of complaints where the issue involved has resulted in regulatory violations.

5. Concentrations of complaints tied to a specified area of the bank.

6. The number of complaints arising from a specific source among the bank's operations.

In some areas of banking compliance and regulation, a "dispute" and a "complaint" are not the same thing (for example: electronic funds transfer transactions). Don't confuse disputes with complaints, but don't let a dispute go unresolved and turn into a complaint.

Complaints have always been a serious matter, but they have grown more critical to a bank's compliance record because banking regulators are playing hard ball these days.

When regulators see multiple complaints that all fall into the same area, they may regard this as a pattern or practice of behavior by the bank.

Complaints can wind up as exam issues and be written into the formal report as a "matter requiring attention," and it has been reported that examiners may follow up independently of formal visits to determine how the bank is following up on complaints.

It is important to note that patterns that indicate systemic issues may result in regulatory referrals to the Department of Justice, and even morph into "UDAAP" under the Dodd-Frank Act. (UDAP stood for "Unfair or Deceptive Acts and Practices," while UDAAP underscores the expansion of the standard to "Unfair Deceptive and Abusive Acts and Practices.")

That being said, the banks should not assume they have done something wrong just because a complaint has been received, but if the bank was in the wrong, self-identification will weigh in the bank's favor when regulators examine the bank's complaint record and its impact on overall compliance issues.

The goals of a complaint handling system range from tracking them so they are dealt with to providing an appropriate overview to various levels of bank leadership.

One of the regulators' key interests when reviewing complaint handling systems is whether senior management and the board are given "meaningful data" on customer complaints. Only reporting numbers is not enough. We recommend that complaint reports include the following elements:

• Summaries of significant items,

• Status of complaints,

• Age of pending complaints awaiting resolution,

• Lines of business and bank regions impacted by complaints,

• Regulations impacted by complaints,

• Trends in complaints, and

• Opportunities for improvement.

Once this information is received and reported, the bank can use this information to improve the affected product or line of business.

Compliance Alliance, Inc.
Phone: 888-353-3933 | Feedback

Compliance Alliance

May 30, 2012

Email to a friend

THE CFPB TAKES AIM AT CURTAILING RULES FOR MORTGAGES

I am sure you have heard the news regarding one of the CFPB's latest proposals, specifically regarding flat fee compensation instead of origination fees being tied to a loan amount. On May 8, 2012, the Consumer Financial Protection Bureau (CFPB) said it plans to propose tighter mortgage lending regulations that would limit the ability of banks to charge specified transaction fees to consumers when they buy a house.

If you recall, on March 9, 2012, the CFPB announced that they will propose residential mortgage loan origination (MLO) rules this summer with a goal of adopting the final rules by January 2013. According to the CFPB, these rules will make it easier for consumers to understand mortgage costs and compare loans in order to get the best deal.

Director Richard Cordray stated that "Mortgages today often come with so many different types of fees and points that it can be hard to compare offers. We want to bring greater transparency to the market so consumers can clearly see their options and choose the loan that is right for them."

The CFPB is considering proposals that would:

- Require an interest-rate reduction when consumers elect to pay discount points;
- Require lenders to offer consumers a no-discount-point loan option;
- Ban origination charges that vary with the size of the loan;
- Implement federal standards for qualification of loan originators; and
- Reconfirm the prohibition on paying steering incentives to mortgage loan originators.

The CFPB also has plans to convene a Small Business Review Panel that will meet with a group of representatives of the small financial services providers that would be directly affected by the proposals under consideration.

In my opinion, the most concerning proposals issued by the CFPB are the complete ban on dual compensation of loan origination, the potential flat charge per loan originated, regardless of size, and the limitations on upfront payments of discount points, origination points, or fees. While the CFPB may create some exemptions related to the points and fees provision if it finds that doing so would be "in the interest of consumers and in the public interest," the Bureau believes generally that points and fees present the possibility of consumer confusion. Thus, by providing

no exemptions, lenders would be forced to offer no-point, no-fee loans and to recover their administrative costs through the rate over time, rather than through upfront payments.

The CFPB's lack of forethought as to the overall effect these types of bans will have on the consumers ability to actually availability of consumer credit and the mortgage industry as a whole is disturbing.

Similarly, with regard to the licensing requirements, the CFPB's suggestion of one size fits all, namely, that licensing requirements will be the same for all originators (e.g., banks, thrifts, mortgage brokers, nonprofit organizations), will likely increase problems in implementation and effectiveness. These types of ultimatums, invariably, will cause small businesses to struggle, given the increased regulatory burdens and limitations. Further, the availability of consumer credit to borrowers seeking smaller mortgages may decrease if banks are not able to seek some sort of guaranteed compensation for the risk they incur to offer credit to many of their customers.

These proposals will be reviewed by the public and a small-business panel to be convened by the consumer bureau. This panel is a requirement of Dodd-Frank, as a way of trying to limit the effect of new regulations on small businesses.

After taking comments, the bureau will formally propose the rules this summer and, after another round of comments, hopes to make them permanent by January.

Please take the time to write a comment letter addressing these concerns.

Compliance Alliance, Inc.
Phone: 888-353-3933 | Feedback

EXHIBIT 2

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

STATE NATIONAL BANK OF BIG SPRING *et al.*, Plaintiffs, v. JACOB J. LEW, in his official capacity as United States Secretary of the Treasury and ex officio Chairman of the Financial Stability Oversight Council 1500 Pennsylvania Avenue, NW Washington, DC 20220, *et al*., Defendants.	Case No. 1:12-cv-01032 (ESH) Judge: Hon. Ellen S. Huvelle

SECOND DECLARATION OF JIM R. PURCELL

In Accordance with 28 U.S.C. § 1746, I, Jim R. Purcell, declare as follows, under the pains and penalties of perjury:

1. I am the Chairman of the Board and CEO of the State National Bank of Big Spring in Big Spring, Texas ("the Bank"). I have served as CEO since 1988 and became Chairman of the Board in 2012.

2. I served as President of the Bank from 1988 to 2012.

3. I am familiar with the Bank's depository and lending practices.

Lending Practices

4. The Bank makes a wide variety of agricultural loans, including loans for equipment, livestock, operating costs, commodities, and real estate. By total amount, approximately 37% of the Bank's outstanding loans are agricultural loans.

5. The Bank also makes automobile loans, including loans for new and used vehicle

purchases, with payback periods of up to 60 months. The bank also makes personal loans that are secured by vehicles.

6. As of May 31, 2012, the Bank held 165 outstanding agricultural loans. As of January 31, 2013, the Bank held 129 outstanding agricultural loans. As of May 31, 2013, the Bank held 159 outstanding agricultural loans.

7. As of May 31, 2012, the Bank held 236 outstanding business loans. As of January 31, 2013, the Bank held 220 outstanding business loans. As of May 31, 2013, the Bank held 204 outstanding business loans.

8. As of May 31, 2012, the Bank held 579 outstanding consumer loans. As of January 31, 2013, the Bank held 560 outstanding consumer loans. As of May 31, 2013, the Bank held 530 outstanding consumer loans.

9. As of May 31, 2012, the Bank held 209 outstanding automobile loans. As of January 31, 2013, the Bank held 199 outstanding automobile loans. As of May 31, 2013, the Bank held 207 outstanding automobile loans.

10. As of May 31, 2013, three of the outstanding mortgage loans held by the Bank exceeded the prime offered rate by more than 3.5%.

11. According to publicly available information, GE Capital and its subsidiaries offer numerous loans in the agricultural sector, including in markets that are served by the Bank. For example, GE Capital and/or its subsidiaries provide financing for purchases from McCoy's, which offers "Farm and Ranch Outfitt[ing]" supplies. *See* https://www.mccoys.com/mccoys-credit (visited June 13, 2013). McCoy's has stores in Midland and Odessa, TX; Odessa is 62 miles from Big Spring, and Midland is 40 miles from Big Spring. *See* www.mccoys.com/why-mccoys/store-locator?state=TX (visited June 13, 2013). To provide another example, Bobcat is a

Case 1:12-cv-01032-ESH Document 33-1 Filed 06/06/13 Page 3 of 4

manufacturer of agricultural equipment that has a dealer in Odessa, TX. *See* bobcat.know-where.com/bobcat/cgi/selection?option=&mapid=US&lang=en&design=default&country=&region_name=&regionSelect=US%2CWorld&addr=&city=big+spring&state=TX%2CUS&zip=&province=&postalcode= (visited June 13, 2013). Bobcat provides financing both to its dealers and to consumers through GE Capital. *See* http://www.gecapital.com/en/our-customers/bobcat.html (visited June 13, 2013).

12. The Bank has previously used the foreclosure-notice-posting process provided for in Tex. Prop. Code Ann. § 51.002(a), (b), (d) (West 2012).

Depository Practices

13. The Bank competes with a wide variety of bank and non-bank financial institutions for deposits. For example, during the financial crisis, the Bank's deposits increased by approximately $75 million between March 2007 and December 2010, a 45% total increase in deposits, primarily because depositors/investors perceived other investment alternatives during that time as bearing significantly increased risk. In deciding where to invest/deposit money, an investor/depositor typically considers the promised return on the investment (as reflected, for example, by a promised interest rate), discounted by the risk that the investment will be lost. The Bank faces increased competition when its competitors either (1) promise higher returns on investments/deposits, including higher interest rates, ***or*** (2) offer less risky investment/deposit opportunities.

14. As of May 31, 2012, the Bank had 162 depository accounts that exceed the $250,000 FDIC insurance threshold. As of January 31, 2013, the Bank had 186 depository accounts that exceed the $250,000 FDIC insurance threshold. As of May 31, 2013, the Bank had 181 depository accounts that exceed the $250,000 FDIC insurance threshold.

15. As of May 31, 2012, the Bank offered .05% interest on amounts deposited in checking accounts, .15% interest on amounts deposited in money market or savings accounts, and .25% interest on 6 Month CDs. Those interest rates remained unchanged as of January 31, 2013, and as of May 31, 2013. These rates reflect competitive market conditions.

16. As of May 31, 2012, the Bank offered .50% interest on amounts deposited on 1 Year CDs. Those interest rates dropped to .40% as of January 31, 2013, and remained at .40% as of May 31, 2013. These rates reflect competitive market conditions.

17. According to publicly available information on www.gecapitalinvestdirect.com, GE Capital offers GE Interest Plus accounts that, as of June 13, 2013, pay as much as 1.10% interest. GE Capital markets these accounts as direct competitors of bank deposit accounts, stating that potential investors/depositors should "[c]onsider this investment if you are comfortable investing in the corporate debt of GE Capital, want your cash to earn a higher rate of return than many FDIC-insured deposit accounts, and want easy access to your investment through check writing, electronic transfers and wires." Customers can apply for these accounts and fund them online through the GE Capital website from anywhere in the United States, including the geographic areas in which the Bank does its business. The investment/deposit opportunities offered by GE Capital are natural competitors with the investment/deposit opportunities provided by the Bank.

I declare under penalty of perjury that the foregoing is true and correct.

Executed on June 13, 2013, at Big Spring, Texas.

Jim R. Purcell

EXHIBIT 3

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

STATE NATIONAL BANK OF BIG SPRING *et al.*, Plaintiffs, v. JACOB J. LEW, in his official capacity as United States Secretary of the Treasury and *ex officio* Chairman of the Financial Stability Oversight Council 1500 Pennsylvania Avenue, NW Washington, DC 20220, et al., Defendants.	Case No. 1:12-cv-01032 (ESH) Judge: Hon. Ellen S. Huvelle

DECLARATION OF JIM R. PURCELL

In Accordance with 28 U.S.C. § 1746, I, Jim R. Purcell, declare as follows, under the pains and penalties of perjury:

1. I am the Chairman of the Board and CEO of the State National Bank of Big Spring in Big Spring, Texas ("the Bank"). I have served as CEO since 1988 and became Chairman of the Board in 2012.

2. I served as President of the Bank from 1988 to 2012.

3. I am familiar with the Bank's legal compliance practices, remittance services, and mortgage lending.

Construction-Only Loans and the Integrated Mortgage Disclosures Regulation

4. On August 23, 2012, the Consumer Financial Protection Bureau ("CFPB" or "Bureau") published, in the Federal Register, a Proposed Rule With Request For Public Comment titled, "Integrated Mortgage Disclosures Under the Real Estate Settlement Procedures Act (Regulation X) and the Truth In Lending Act (Regulation Z)." 77 FR 51115 (Aug. 23,

2012) ("Proposed TRID Rule").

5. The CFPB published the final version of the Proposed TRID Rule in the Federal Register on December 31, 2013. 78 FR 79730 (Dec. 31, 2013) ("Final TRID Rule").

6. In the preamble to the Final TRID Rule, the CFPB states that in response to the Proposed TRID Rule, numerous comments asked for "construction-only loans and bridge loans [to] be exempt because their unique characteristics make them ill-suited for RESPA disclosures." 78 FR 79791 (Dec. 31, 2013). The CFPB "considered the comments received regarding the applicability of the integrated disclosures to . . . construction-only loans" and chose to subject such loans to the Final TRID Rule. 78 FR 79792 (Dec. 31, 2013).

7. In calendar years 2013 and 2014, the Bank issued construction-only mortgage loans made primarily for personal, family, or household purposes.

8. The Final TRID Rule prescribes new documents that must be provided to the borrower of such construction-only loans.

9. Before the Final TRID Rule became effective, the Bank generally did not use an outside vendor to prepare the documents that must be provided to the borrower of a construction-only loan. The bank prepared these documents in-house. In rare cases where the loan was unusually complicated, the Bank paid an attorney a flat fee of $250 to prepare the documents.

10. The Bank's is unable to cost-effectively generate the new documents that must be provided to borrowers of construction-only loans under the Final TRID Rule. As a result, the bank must hire a vendor to prepare such documents, at a cost of $375 per loan application.

11. The need to comply with the new requirements imposed by the Final TRID Rule also slows down the loan approval process, and requires additional time by Bank employees for each such loan approval.

Balloon mortgages

12. In calendar years through 2010, the Bank issued mortgage loans made primarily for personal, family, or household purposes, which had a balloon payment ("Balloon Mortgages").

Exemptions to Banks That Operate Predominantly in Rural Areas

13. The CFPB provides exemptions from certain mortgage regulations to Banks that issue mortgages predominantly in rural or underserved counties and meet other requirements. For example, such banks "can originate Qualified Mortgages with balloon payments even though balloon payments are otherwise not allowed with Qualified Mortgages." They are also "not required to establish escrow accounts for higher-priced mortgages." Consumer Financial Protection Bureau, *CFPB Finalizes Rule to Facilitate Access to Credit in Rural and Underserved Areas* (Sep. 21, 2015), http://www.consumerfinance.gov/newsroom/cfpb-finalizes-rule-to-facilitate-access-to-credit-in-rural-and-underserved-areas/ (last visited Oct. 30, 2015).

14. The Bank currently cannot qualify for the above two exemptions because it issues mortgages predominantly in Howard County, TX, which is not included in the CFPB's 2015 list of rural or underserved counties. Consumer Financial Protection Bureau, *Final lists of rural and rural or underserved counties for use in 2015* (Oct. 27, 2014), http://www.consumerfinance.gov/blog/final-list-of-rural-or-underserved-counties-for-use-in-2015/ (last visited Oct. 30, 2015).

15. The above two exemptions and the methodology used by the CFPB to identify rural and underserved counties appear in regulations that the CFPB issued before July 17, 2013. See Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 FR 6407, 6588 (Jan. 30, 2013) (12 C.F.R. §1026.43, which allows banks that

operate predominantly in rural or underserved areas to issue Qualified Balloon Mortgages); Escrow Requirements Under the Truth in Lending Act (Regulation Z), 78 FR 4725, 4756 (Jan. 22, 2013) (12 C.F.R. §1026.35(b)(2)(iii), which exempts banks that operate predominantly in rural or underserved areas from the escrow requirement, and 12 C.F.R. §1026.35(b)(2)(iv), which states the methodology the CFPB will use to identify rural or underserved counties, e.g. stating that "the Bureau classifies a county as 'rural' if the USDA-ERS categorizes the county under UIC 4, 6, 7, 8, 9, 10, 11, or 12.").

16. On Sep. 21, 2015, the CFPB issued a Final Rule that allows banks to qualify for the above exemptions if they issue mortgages predominantly in rural census blocks, and meet other requirements.

17. The Bank is not aware of a list, published by the CFPB, of Howard County's rural census blocks. Assuming such a list were published, to benefit from the above two exemptions the Bank would need to examine the list before making each new mortgage, identify the applicable rural census block, and count its mortgages by census block type so as to ensure it makes mortgages predominantly in rural census blocks.

I declare under penalty of perjury that the foregoing is true and correct.

Executed on November 4, 2015 at Big Spring, Texas.

Jim R. Purcell

Jim R. Purcell

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

STATE NATIONAL BANK OF BIG SPRING *et al.*,	)	
Plaintiffs,	)	
v.	)	Case No. 1:12-cv-01032 (ESH)
JACOB J. LEW, in his official capacity as United States Secretary of the Treasury and *ex officio* Chairman of the Financial Stability Oversight Council, *et al.*,	)	Judge: Hon. Ellen S. Huvelle
Defendants.	)	

[PROPOSED] ORDER

Upon consideration of Plaintiffs' Motion for Summary Judgment, it is hereby ORDERED that the motion is granted.

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HONORABLE ELLEN S. HUVELLE
U.S. District Court Judge