

CORPORATE COUNSEL

The Long Arm of the CFPB

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Today is the fifth birthday of the Consumer Financial Protection Bureau (CFPB), and it is critical to understand the evolving breadth of the new agency's investigatory powers—especially as it has recently been testing the limits of its jurisdiction in 2016. The most elucidating developments regarding the CFPB's enforcement investigation authority unfolded in three cases decided this past spring.

Background on Civil Investigative Demands

Section 1052 of the CFPB's enabling statute, Title X of the Dodd-Frank Wall Street Reform and Consumer Financial Protection Act of 2010, authorizes the agency to conduct investigations and administrative discovery. Under Dodd-Frank, it may issue a civil investigative demand (CID) to "any person" whenever the CFPB believes that the person "may be in possession, custody, or control of any documentary material or tangible things, or may have any information, relevant to a violation." The rule relating to investigations prescribes procedures under Section 1052. While the rule contains a protocol by which a CID recipient can petition to set aside the CID, the adjudicator of such a petition is the CFPB's own director, Richard Cordray. 12 C.F.R. § 1080.6(3)(4); see also Joseph T. Lynyak III and Rebecca Tierney, "Dealing with the Civil Investigative Demands from the CFPB," *The Banking Law Journal*, at 777 (2013). In deciding a petition, Cordray is bound by Dodd-Frank, which sets forth a low standard in that the CID may be issued to "any person" who has information "relevant to a violation." Rarely would Cordray decide to quash a CID issued by his own staff attorneys. Of the 22 instances in which parties have petitioned to set aside or modify a CID as of when this article went to press, fifteen petitions have been decided, and all were denied.

Facing poor odds of setting aside or modifying CIDs, recipients have also pursued the more passive strategy of simply not responding. If a CID recipient does not comply fully with a CID, the regulation authorizes Cordray, the assistant director of the office of enforcement or the general counsel to initiate "appropriate action," including by filing enforcement actions to compel compliance in federal district court and, where a court order has been violated, by seeking civil contempt. Although the CFPB attained successful outcomes in motions to compel CID compliance in the past, the events of early 2016 reveal a changing tide.

Recent Cases

In the Matter of Westgate Resorts Ltd., the CFPB propounded 27 interrogatories and nine requests for documents in an investigation commenced by the its office of enforcement. Westgate complied with several demands, but did not respond fully to requests for consumer complaints related to the offering or sale of timeshares and for the identity of anyone who worked for Westgate after August 2012, except for "greeters." Instead, Westgate raised several arguments in its petition to set aside or modify the CID, including most notably the argument that the probing of these topics went beyond the scope of the CFPB's authority to investigate certain industries. According to Westgate, the marketing and sales of timeshares were outside the bureau's enforcement authority under Section 1027 of Dodd-Frank, which contains exemptions for sellers of nonfinancial goods and for real estate brokerage activities.

In his ruling in March, Cordray denied the petition, but did not disagree with Westgate's argument that its activities are exempt from the CFPB's enforcement authority. In sidestepping that issue, Cordray reasoned that it is irrelevant that Dodd-Frank exempted merchants or real estate brokerage services because the power to enforce is not coextensive with the power to investigate. This is because, as discussed above, Dodd-Frank authorizes the CFPB to issue CIDs to "any person" who may have information "relevant to a violation," regardless of whether that person is in a category of industries subject to its enforcement authority. Cordray invoked case precedents dealing with the subpoena power of the Securities Exchange Commission and the Federal Trade Commission, which have long held that subpoenas could be enforced even against entities outside those agencies' jurisdiction. Accordingly, the petition was denied.

One month before the *Westgate* ruling, Cordray had reached a similar result *In the Matter of J.G. Wentworth LLC*. In that investigation, the CFPB had propounded 14 document requests, seven interrogatories and two requests for written reports seeking information about structured-settlement transactions and other services provided by J.G. Wentworth. The company petitioned the CFPB to set aside the CID for several reasons, including because J.G. Wentworth was not a "covered person" under Dodd-Frank and was thus not properly within the CFPB's jurisdiction to enforce the federal prohibition of unfair, deceptive and abusive acts or practices (UDAAP). A "covered person" is "any person that engages in offering or providing a consumer financial product or service." The federal prohibition of UDAAP applies only to "covered persons" or service providers. In his ruling in February, Cordray denied the petition, again emphasizing that Dodd-Frank authorizes the CFPB to issue CIDs to "any person" who may have information "relevant to a violation." In addition, he explained that J.G. Wentworth may eventually be revealed later in the investigation to be within the definition of a "covered person"—depending on the company's activities—and that, in any event, "fact-based arguments about whether [an entity] is subject to or has complied with substantive provisions of [Dodd-Frank] are not defense to the enforcement of a CID." On June 7, after J.G. Wentworth had informed the CFPB that it would no longer produce documents or information, the agency filed a federal district court action in Philadelphia to enforce the CID. The case is pending. As a practical matter, Cordray's position in both cases means that a party can be required to comply with CIDs even if such party is not a "covered person" under Dodd-Frank. This position is consistent with the CFPB's regulation, which distinguishes the power to gather evidence from the power to bring an enforcement action.

This extensive investigative authority, however, was curtailed recently by a federal district judge. *In the Matter of Accrediting Council for Independent Colleges and Schools (ACICS)*,

the CFPB had sought oral testimony regarding ACICS's policies, practices and procedures for accrediting for-profit colleges and two interrogatories (including the identity of the colleges accredited by ACICS and the individuals who conducted the accreditation). Unsurprisingly, on October 8, 2015, Cordray denied the petition. After ACICS explained that it was unable to discuss complying with the CID, the CFPB filed a petition to enforce it in federal court in the District of Columbia.

On April 21, U.S. District Judge Richard J. Leon—in a matter of first impression—denied the request to compel compliance and dismissed the matter. Leon reasoned that the CFPB's investigative authority must be tethered to its overall UDAAP authority. After explaining the nature of the CFPB's power to prevent UDAAP applies to, among other things, a "covered person," Leon emphasized that "[t]o facilitate this purpose, the CFPB may issue CIDs to 'any person [believed to] be in possession, custody, or control of any documentary material [].'" Because the bureau's CID explicitly said in the "Statement of Purpose" section that it sought to investigate the accreditation process of for-profit schools – and the accreditation process is unrelated to the financial aid decisions of the schools it accredits – the judge determined that the purpose was to explore areas that are not within the jurisdiction of the CFPB and was impermissible. Leon explained, "Although it is understandable that new agencies like the CFPB will struggle to establish the exact parameters of their authority, they must be especially prudent before choosing to plow headlong into fields not clearly ceded to them by Congress." The case is currently on appeal to the D.C. Circuit.

Implications of Recent Developments

In reconciling these three cases, it may be that Dodd-Frank's distinction between "any person" and "covered person" permits the CFPB to issue CIDs to third parties (i.e., not those that are the subject of a CFPB investigation). Thus, it may issue CIDs to a third party in the course of an investigation of an entity that is subject to the CFPB's enforcement authority without overstepping its jurisdiction. If the CID issued to ACICS had fallen into that category, it seems unlikely that the court would have ruled against the CFPB.

A tension unresolved by the court, however, is whether CIDs may be issued to investigate an entity that is not a "covered person" but is suspected to be facilitating the violations committed by covered persons, which is itself an illegal act under the "aiding and abetting" provision in Section 1036(a)(3) of Dodd-Frank, which applies generically to "any person." In *ACICS*, the CFPB revealed a possible interest in investigating the accreditation process as a means to facilitate the business of for-profit colleges, including education loans. Yet, the clear implication of Leon's decision is that because the accreditation process is outside of its jurisdiction, the CID was impermissible regardless of the CFPB's theory related to how the accreditation process may "aid and abet" potential violations by lenders or student loan servicers. It remains to be seen how the D.C. Circuit will react.

Regardless, the cases foreshadow future disputes regarding the manner in which CFPB can investigate non-covered persons who are suspected to be "aiding and abetting" others—a theory which the CFPB has deployed broadly and frequently in consent orders. The final outcome of these issues also hinges on whether courts will recognize that a distinct policy exists—given the specific Dodd-Frank limitation to enforce consumer protection laws against "covered persons"—to distinguish CIDs from the administrative subpoenas of other agencies (like the SEC and FTC), thereby warranting a higher standard for the CFPB than otherwise exists for federal agencies.

In that sense, these cases strike at the heart of the CFPB, and not just at its investigatory powers. We should expect increased litigation over the bureau's CID authority. As the CFPB enters its next phase of development, industry participants must not only take heed of recent court developments, they should also scrutinize carefully how any CID is drafted, and develop robust strategies to capitalize on the judicially determined limits of its authority.

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