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Legal Update
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Information Asymmetry: The CFPB Proposes Changes to the Rules Governing Confidential Information

The Consumer Financial Protection Bureau (CFPB) recently proposed changes to its rules governing confidential information. The proposed rules would restrict recipients of civil investigative demands (CIDs) from voluntarily disclosing the receipt of a CID, while at the same time giving the CFPB more leeway to disclose confidential supervisory information to other government agencies. The proposed simultaneous tightening and loosening of restrictions on the disclosure of confidential information can have important implications for parties subject to CFPB enforcement and supervisory jurisdiction, who should consider whether to submit comments, which are due by October 24, 2016.

Confidential Investigative Information—Limitations on Recipients of CIDs

From their inception, the CFPB confidentiality rules governing the treatment of CIDs and CID-related information have been fraught with ambiguity with regard to what limitations, if any, they impose on CID recipients. The rules as originally promulgated and currently in effect generally prohibit *the CFPB* from disclosing any confidential investigatory information—defined to include any information provided to the CFPB in response to a CID, as well as any other information prepared or received by the CFPB in the conduct of enforcement activity.[1] The rules appear intended to protect investigation targets from being tarred by the mere existence of an investigation, which does not equal a finding of wrongdoing. In this respect, the CFPB's practice is modeled on that of the Federal Trade Commission (FTC), which similarly does not disclose pending investigations.

The application of the current confidentiality rules to CID recipients—and specifically whether they purport to prohibit a recipient of a CID from voluntarily disclosing the existence of the CID or other CID-related information—is less clear. On the one hand, the rules define confidential investigative information as including information "prepared by . . . the CFPB . . . in the conduct of an [enforcement] investigation," suggesting that the definition includes the CID itself and not merely information provided by a CID recipient to the CFPB.[2] The rules also provide that "except as required by law," no "person in possession of confidential information" may disclose it.[3] Together, these provisions suggest that a recipient of a CID is prohibited from disclosing the existence of a CID absent a legal obligation to do so.

On the other hand, the current rules appear to be intended to protect subjects of investigations by preventing *the CFPB* from disclosing the existence of an investigation or materials provided to it in response to a CID absent an applicable exception. For example, the preamble to the rules discusses the sensitive nature of information the CFPB obtains and states that the

rules "generally prohibit[] *the Bureau and its employees* from disclosing confidential information."[4] And the rules themselves state that "no current or former employee or contractor or consultant of the CFPB" may disclose "confidential information" except as required by law or authorized by the rules.[5]

Other textual clues, and the CFPB's practice over the past five years, support the conclusion that the current rules authorize voluntary disclosure of the existence of a CID by its recipient. Most importantly, the current rules differentiate between how entities subject to CFPB examination or investigation can handle confidential supervisory information and confidential investigative information, respectively. As the preamble to the current rules explains, they expressly "prohibit[] institutions from further disseminating confidential *supervisory information* they receive [from the CFPB] except in limited circumstances."[6] This approach to handling confidential supervisory information is consistent with that of the prudential regulators. In light of this broad prohibition, and recognizing supervised entities' need to disclose such information in certain circumstances, the rules expressly authorize certain disclosures of confidential supervisory information. Thus, section 1070.42 of the current rules expressly allows a supervised financial institution to disclose confidential supervisory information to its attorneys.[7] The current rules also provide a mechanism by which a supervised financial institution may seek authorization from the CFPB to make additional disclosures of confidential supervisory information.[8] Indeed, the CFPB went so far as to issue a Compliance Bulletin emphasizing that those in possession of confidential supervisory information may not disclose it without such authorization.[9]

There are no parallel disclosure provisions governing confidential investigative information. That is, the current rules do not expressly authorize sharing confidential investigative information with counsel and provide no mechanism by which to seek CFPB permission to otherwise disclose such information. (Nor did the CFPB Bulletin discuss the disclosure of confidential investigative information.) In light of the fact that confidential investigative information is subject to the same general prohibitions on disclosure as confidential supervisory information, this absence can mean one of two things: either CID recipients are absolutely prohibited from disclosing the existence of a CID and other CID-related materials, even to counsel, or the non-disclosure provisions are not intended to apply to recipients of CIDs. Clearly, the first option is untenable. CID recipients regularly disclose CIDs to their counsel and also disclose the existence of CIDs to various business counterparties in a variety of circumstances with the CFPB's knowledge (and even express agreement). This practice strongly suggests that the current rules do not, in fact, prohibit CID recipients from disclosing confidential investigative information but are instead focused on the CFPB's non-disclosure of such information.

Moreover, the CFPB's template CID form itself does not state that disclosure of its existence would violate the CFPB's rules. To the contrary, when the CFPB issues CIDs to third parties who are not the subject of the investigation, the CID's instructions *request*, but do not direct, the recipient to keep the existence of the CID confidential.[10] This provides further support to the conclusion that the rules as currently written are not intended to preclude voluntary disclosure of a CID by its recipient.

Why does this matter? While CID recipients often wish to keep the existence of an investigation confidential, there are circumstances in which a company may wish to voluntarily disclose an investigation's existence. Certainly, a company will want to disclose the CID to its outside counsel to obtain legal advice. A company may wish to disclose a CID to its

insurance carrier in order to obtain coverage for defense costs. Additionally, a company may be contractually obligated or otherwise wish to disclose a CID to counterparties, as the result of a contractual commitment, pending transaction or for another reason.

The CFPB now proposes to clarify the ambiguity in its current rules by expressly prohibiting the disclosure of a CID, or other materials an investigation target prepares in response to an investigation, except in limited circumstances. Specifically, the CFPB proposes to "expand[] the scope of § 1070.42 [the provision authorizing the disclosure of confidential supervisory information in narrow circumstances or with the CFPB's approval] to address its enforcement activities in addition to its supervisory activities."[11] The CFPB makes clear that this proposed change would cover—and generally prevent—the disclosure of "civil investigative demands ('CIDs') [and] notice and opportunity to respond and advise ('NORA') letters."[12]

The CFPB provides no explanation or justification for adopting this approach other than to note that it would impose the same information-sharing regime on confidential investigative information as currently exists for confidential supervisory information.[13] Nor does the CFPB discuss the relative merits of imposing such a non-disclosure regime versus allowing recipients of CIDs to voluntarily disclose them if they wish, or identify any harms that would result from a permissive disclosure regime.

These are all serious issues that warrant careful consideration by the agency rather than the cursory treatment provided in the proposed rules. While the proposed rules would treat confidential investigative information consistent with the agency's treatment of confidential supervisory information—and consistent with the manner in which prudential regulators treat confidential supervisory information—they would be a stark departure from the practice of other law enforcement agencies such as the FTC or the Securities and Exchange Commission (SEC). Neither of those agencies prohibits disclosure of CIDs by recipients. The CFPB's statutory authority to issue CIDs is modeled after that provided to the FTC, and the CFPB's investigation rules are modeled on the rules of both agencies. The decision to align the rules governing confidential investigative information with the practices of the prudential regulators, as opposed to the law enforcement agencies upon whose legal authorities the CFPB's enforcement powers were modeled, represents a sharp departure from past CFPB practice. Particularly in light of the fact that in their long experience the FTC and SEC have not identified a need to prohibit CID recipients from disclosing the existence of a CID, the CFPB's proposal warrants careful scrutiny.

Existing practice also suggests that the CFPB's proposed rules may be unwarranted. The CFPB's current rules provide for the disclosure of CIDs under several circumstances. Because the rules as currently written (and as proposed) authorize disclosure when "required by law,"[14] publicly-traded companies who believe that receipt of a CID or NORA letter constitutes a material event regularly disclose such events in their securities filings. Similarly, the CFPB will publically disclose CIDs when recipients avail themselves of the right to petition to modify or quash a CID.[15] The CFPB's proposal does not identify any harm to its enforcement program that has come from such disclosures. As discussed below, one could envision harm to an agency's enforcement objectives when an investigation's target that is unaware of the investigation becomes informed about it. But even in cases where the CFPB sends CIDs to third parties, it has only requested, and not required, that those parties keep the existence of the investigation confidential. Given the history of the disclosure of CIDs—and therefore the existence of CFPB investigations—and the absence of any identified harm to the CFPB from such disclosures, it is not clear why the CFPB is proposing to limit such disclosures in the future.

Finally, and perhaps most importantly, the proposed rules raise constitutional concerns under the First Amendment. By prohibiting the disclosure of information absent advance permission from the CFPB, the proposed rules appear to impose a prior restraint and a content-based restriction on speech. For example, they would prohibit a CID recipient from publicly criticizing the agency for issuing a CID. Even in the context of National Security Letters issued by the FBI—where the governing statute expressly authorizes the FBI to direct third-party recipients not to disclose receipt of the letter and where the governmental interest in national security is considered paramount—courts have rejected such blanket disclosure prohibitions as unconstitutional.[16] The CFPB's proposal does not address this constitutional issue.

The CFPB should address these important issues and seek comment on them before adopting the limitations it proposes. Interested parties should consider filing comments on this aspect of the proposed rules with the CFPB.

Confidential Supervisory Information—Broader Authority to Disclose

At the same time that the CFPB is seeking to impose limitations on the information that CID recipients can share, it is also proposing to loosen the restrictions on the agency's own sharing of confidential supervisory information. The Dodd-Frank Act expressly authorizes the CFPB to disclose confidential supervisory information to a prudential regulator or other government agency "having jurisdiction over" a CFPB-supervised entity.[17] In its currently-operative rules, the CFPB interpreted this statutory grant of authority as reflecting the limits on the agency's authority to disclose confidential supervisory information to other agencies, and the rules therefore only authorize the CFPB to disclose confidential supervisory information to other agencies that "have jurisdiction over" the party to whom the information relates.[18] The CFPB now proposes to re-interpret this provision of the Dodd-Frank Act to be merely permissive and to not reflect any limitation on the CFPB's authority to disclose confidential supervisory information. According to the CFPB, because Congress did not provide that the CFPB may *only* disclose confidential supervisory information to agencies having jurisdiction over a supervised party, the "better view" is that Congress did not intend the statutory provision to restrict the CFPB's discretion.[19] Accordingly, the CFPB proposes to change its rules to authorize the disclosure of confidential supervisory information to another agency "to the extent that the disclosure of the information is *relevant to* the exercise of the agency's statutory or regulatory authority."[20] This is the same standard applicable to the CFPB's sharing of confidential investigative information.

The proposed rules provide little by way of explanation for why this change is needed. The CFPB says only that sharing confidential supervisory information in situations where such information is "relevant" to the receiving agency's exercise of its authorities will "facilitate the Bureau's purposes and objectives" and "assist the Bureau in implementing and administering federal consumer financial law in a more consistent and effective fashion" by working "together with other agencies having responsibilities related to consumer financial matters."[21] The CFPB does not, however, provide any actual examples of how it might share confidential supervisory information and how such sharing would help advance its "purposes and objectives." The CFPB also states that the "current rule's restrictions have proven overly cumbersome in application, pose unnecessary impediments to cooperating with other agencies, and otherwise risk impairing the Bureau's ability to fulfill its statutory duties."[22] Again, the CFPB provides no concrete examples of how the current limitations, which as noted above are grounded in the statutory language, have impeded cooperation with other agencies.

The CFPB's current rules already authorize it to disclose confidential supervisory information to law enforcement agencies that have "jurisdiction" over supervised entities. The CFPB does note that its policy regarding disclosure of confidential supervisory information to law enforcement agencies, which it announced in January 2012, remains unchanged.[23] Pursuant to that policy, "the Bureau will not routinely share confidential supervisory information with agencies that are not engaged in supervision" and will "share confidential supervisory information with law enforcement agencies, including State Attorneys General, only in very limited circumstances."[24] The proposed rules, therefore, are apparently intended to authorize the CFPB to provide confidential supervisory information to other, unspecified agencies that do not have any jurisdiction over the supervised institution whose information is to be shared. It is not clear with which additional agencies the CFPB proposes to share confidential supervisory information or how the proposed change will assist in the coordination the CFPB describes.

Conclusion

The notice and comment process affords impacted and interested members of the public an opportunity to shape important government regulations such as these. Parties potentially impacted by the CFPB's proposed changes, and others concerned about the implications of these actions, should file comments on the proposed rules by the October 24, 2016 deadline.

For more information about this topic, please contact the author listed below.

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Endnotes

1 12 C.F.R. § 1070.41.

2 12 C.F.R. § 1070.2(h).

3 12 C.F.R. § 1070.41.

4 78 Fed. Reg. 11484, 11484 (Feb. 15, 2013) (emphasis added).

5 12 C.F.R. § 1070.41(a).

6 78 Fed. Reg. at 11493 (emphasis added).

7 12 C.F.R. § 1070.42(b)(2)(i).

8 12 C.F.R. § 1070.42(b)(2)(ii).

9 CFPB Bulletin 2015-01, Treatment of Confidential Supervisory Information (Jan. 27, 2015).

10 *See, e.g.,* CID issued to Kevin Stricklin, attached as Exhibit A to CFPB Petition to Enforce Civil Investigative Demand, *CFPB v. Strickin*, No. 1:14-cv-00578-RDB (D. Md.) ("We ask your *voluntary cooperation* in not disclosing the existence of this CID outside your organization, except to legal counsel, until you have been notified that the investigation has been completed. Premature disclosure could impede the Bureau's investigation and interfere with its enforcement of the law.") (emphasis added).

11 81 Fed. Reg. 58310, 58316 (Aug. 24, 2016).

12 *Id.* NORA letters are the mechanism by which the CFPB informs an investigation target that the staff is considering recommending that charges be instituted. It is similar to a Wells Notice in SEC practice.

13 The CFPB makes this observation by stating that the proposed rules would "provide that recipients of confidential investigative information have the same discretion with respect to disclosing" it as do recipients of confidential supervisory information. *Id.* Such a formulation suggests that under the current rules recipients of confidential investigative information lack discretion to disclose that information. As discussed above, there are strong arguments to conclude that is not the case.

14 12 C.F.R. § 1070.41(a).

15 *See* http://www.consumerfinance.gov/policy-compliance/enforcement/petitions/. The CFPB describes publication of CIDs in such circumstances as part of its commitment to transparency.

16 *See, e.g., Doe v. Mukasey*, 549 F.3d 861, 876-83 (2d Cir. 2008); *In Re National Security Letter*, 930 F. Supp. 2d 1064, 1073-78 (N.D. Cal. 2013). Aggravating the constitutional issues inherent in the CFPB's proposal is the lack of any procedures or standards pursuant to which the CFPB would determine whether to allow disclosure in a particular case.

17 12 U.S.C. § 5512(c)(6)(C)(ii).

[18] 12 C.F.R. § 1070.43(b)(1).

[19] 81 Fed. Reg. at 58317.

[20] *Id.* (emphasis added).

[21] *Id.*

[22] *Id.*

[23] *Id.* at 58318 (citing CFPB Bulletin 12-01 (Jan. 4, 2012)).

[24] CFPB Bulletin 12-01 at 5.