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High Court CFPB Review May Determine Fate Of FHFA Too

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Whether the structure of the Consumer Financial Protection Bureau is unconstitutional because the president does not have the statutory right to fire its director without cause now is squarely in front of the U.S. Supreme Court based on its recent acceptance of cert in Seila Law LLC v. CFPB.

How the Supreme Court eventually rules in Seila Law may also decide the fate of the structure of the Federal Housing Finance Agency, which is similar to the CFPB.

If you have ever negotiated an employment agreement or a commercial agreement, you probably are familiar with the concept of termination with cause and without cause. The former generally is reserved for situations where one party breaches a contractual obligation, and the other party wants to terminate the agreement as a result. The latter generally permits either party to terminate the agreement for any reason or no reason, although usually with an advance notice requirement, and sometimes only after the payment of a termination fee.

Termination with or without cause also is addressed in many state labor and employment codes, which often contain a presumption that employees are employed at will. This means that state law essentially permits an employer or an employee to terminate employment at any time, with or without cause or prior notice.

This presumption, however, is subject to certain exceptions such as (1) civil service laws protecting public sector employees, (2) employees represented by unions and covered by a collective bargaining agreement requiring a proper cause for termination, or (3) employment agreements containing contrary provisions.

This backdrop may provide useful context to understand the controversy over whether the sole directors of the FHFA and CFPB may be removed by the president without cause, even though the agencies are structured as independent agencies.

At first blush, the issue seems straightforward. The enabling statute for each of the FHFA and the CFPB has the same language regarding the term and termination of its director. Each provides that the director serves for a term of five years and may continue serving until a successor has been appointed and confirmed.

Each also prohibits the president from removing the director absent “inefficiency, neglect of duty, or malfeasance in office.” In other words, termination of either director without cause is not an option under the enabling statutes. The five-year terms of the directors of both the FHFA and the CFPB have crossed two different administrations, with directors Mel Watt and Richard Cordray, both appointed by former President Barack Obama, remaining in their positions for part of President Donald Trump's administration.

In light of the explicit statutory limitation on termination without cause, last month the U.S. Court of Appeals for the Fifth Circuit, sitting en banc (meaning that all of the judges participated in the opinion), ruled in Collins v. Mnuchin that the FHFA is unconstitutionally structured. It based its decision on the fact that the FHFA director may be removed solely for cause.

Another case, All American Check Cashing Inc. v. CFPB, also is in front of the Fifth Circuit, is challenging the constitutionality of the CFPB in part based on the same arguments.

The crux of the argument in each case is that the inability of the president to remove the applicable director without cause interferes with the president’s exercise of executive power and the president’s constitutionally directed duty to take care that the laws be faithfully executed under Article II of the U.S. Constitution.

If the president has the authority to appoint the directors as part of the exercise of his executive power, why then should the president not be able to remove such directors even if they have done nothing wrong?

Indeed, in the hierarchy of political appointees, it is interesting that the president clearly has the power and authority to fire any Cabinet member without cause, but the president does not have the same authority when it comes to materially smaller agencies. Some have asked why the president cannot fire the director of the FHFA without cause, but the president can fire the attorney general or the secretaries of the U.S. Department of Defense or the U.S Department of the Treasury for any reason or no reason at all.

The short answer is that the enabling statutes for the FHFA and the CFPB, as independent agencies, provide for the distinction based on a Congressional determination that accomplishment of the mission of these independent agencies requires some distance from political interference. The Fifth Circuit rejected this view, finding the FHFA’s enabling statute to be unconstitutional because it impermissibly insulated the director from executive branch oversight.

Not all courts agree that a for-cause removal restriction impedes the president’s ability to perform his constitutional duty to ensure that the laws are faithfully executed. A 1935 Supreme Court case, for example, Humphrey’s Executor v. United States, held that the limited for-cause provision in the structure of the Federal Trade Commission did not violate the separation of powers clause.

The FTC does not have a single director, but instead has a multimember commission comprised of presidentially appointed Democrats and Republicans. The Fifth Circuit in Collins v. Mnuchin, distinguished the two cases, noting that a sole-director structure lacks the checks inherent in the multilateral decision making structure of the FTC.

The 2018 en banc decision of the U.S. Court of Appeals for the D.C. Circuit in PHH Corp. v. CFPB also refused to find a for-cause removal restriction to be unconstitutional. It reversed a prior ruling by a three-judge panel that had held the CFPB's structure unconstitutional.

The initial ruling, authored by then-U.S. Circuit Judge Brett Kavanaugh, concluded that the CFPB's structure was unconstitutional by virtue of its organization as an independent agency with a single director. Instead, the full court concluded that being able to terminate the director for cause is sufficient authority to assure that an official is properly performing his or her statutory responsibilities.

What it really comes down to is what type of insulation from executive oversight is appropriate for a director of an independent agency. Those who oppose for-cause limits on termination argue that the president must have full oversight authority and flexibility to change the team at will.

Those who support for-cause limits on termination argue that such limits on termination do not impermissibly burden the president's Article II powers, and are necessary to provide a degree of independence to ensure the proper functioning of the agency, particularly where Congress deemed such independence necessary to promote stability and confidence in the country's financial system.

Which is it then: insulation from politics or insulation from oversight? And is it only a public policy question that Congress may decide, or ultimately a constitutional question beyond the powers of Congress to dictate?

Particularly fascinating for so-called inside-the-Beltway types, like me, are recent letters CFPB Director Kathleen Kraninger sent to House Speaker Nancy Pelosi, D-Calif., and Senate Majority Leader Mitch McConnell, R-Ky. Kraninger's sentiments also are included in the brief the U.S. Department of Justice filed in Seila Law v. CFPB in response to Seila Law's recent petition to the Supreme Court to review the constitutionality of the for-cause removal provision in the CFPB's enabling statute and reverse a Ninth Circuit decision upholding the structure.

Reversing the CFPB's long-standing position taken in litigation throughout its existence, Kraninger expressed her decision that the CFPB would adopt the DOJ's view that for-cause removal is unconstitutional. She noted that she had directed CFPB attorneys to cease defending the for-cause provisions in the lower courts. It is rare in Washington, D.C., for politically appointed figures to write publicly disclosed letters about the president's right to terminate them at will.

To date, FHFA Director Mark Calabria has not publicly issued similar letters, although the Fifth Circuit in Collins v. Mnuchin stated that the FHFA reversed its prior admission that the agency's structure violates separation ofpowers. The court stated that the FHFA now contends that the agency's structure is constitutional.

The level of direct and indirect executive oversight also differs between the FHFA and the CFPB. For that matter, the level of direct and indirect executive oversight also varies between those two independent agencies that have a sole director and the FTC, which is another independent agency run by multimember commission. Those differences ultimately may or may not matter as a constitutional question. This issue seems headed to the Supreme Court.

While the provision in the enabling statutes' limited for-cause removal may be unconstitutional, both the Fifth Circuit and the administration call for the continuation of the independent agencies. They are not arguing that the prior acts of the independent agencies should be invalidated or that the independent agencies cannot continue to do their day-to-day work.

Rather, the proper remedy for the constitutional violation is to sever the offending provision and leave the remaining statutory provisions intact, according to the decision in Collins v. Mnuchin and the brief filed by the DOJ in the All American Check Cashing case. In this regard, Kraninger's letters asserted that a Supreme Court decision holding the for-cause removal provision to be unconstitutional should not affect the CFPB's ability to remain fully operational and carry on its mission.

But these positions do not definitively resolve the issue about the respective agencies' ability to issue rules and, in the case of the CFPB, enforce federal consumer financial laws, if the enabling statute has a constitutional defect. Whether an independent agency that proclaims itself to be unconstitutional can nevertheless bring enforcement actions is by no means free from doubt, and still is being actively contested. We should expect that those businesses subject to an independent agency's regulation or enforcement will continue to assert this defense in past and future CFPB enforcement actions.

The ultimate irony of the administration's change in position on the constitutionality of the FHFA's and CFPB's leadership structure is that 2021 is just around the corner. While not necessarily true, it is quite possible that both Kraninger and Calabria would lose their jobs based on a without-cause termination if there is a change in administration following the next presidential election.

A "be careful what you wish for" overhang permeates the entire discussion. Not being insulated from politics may seem less desirable when one disagrees with those politics. And the Supreme Court decision in Seila Law v. CFPB is expected to arrive right in the middle of the down stretch of the 2020 presidential campaign.

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Disclosure: Lawyers at Mayer Brown, but not the author, represent clients that have challenged and are challenging the constitutionality of the sole-director structure of the CFPB.