CRS Reports & Analysis

Legal Sidebar

D.C. Circuit Rules Consumer Financial Protection Bureau's Structure is Unconstitutional

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This is the first of a series of Sidebars focusing on a recent decision by the U.S. Court of Appeals for the D.C. Circuit, which held unconstitutional a provision of the Dodd-Frank Act barring the President from removing the Director of the Consumer Financial Protection Bureau (CFPB) except "for cause." This Sidebar summarizes the basics of the case and immediate consequences for the CFPB. Subsequent Sidebars will explore the broader implications of the decision.

A recent decision by the U.S. Court of Appeals for the D.C. Circuit (D.C. Circuit) recognized constitutional limitations on Congress's ability to insulate so-called "independent agencies" from presidential control. Broadly speaking, these are agencies empowered to enforce federal laws whose heads are not removable by the President at will, but only "for cause," which is often defined to require the termination be for "inefficiency, neglect of duty, or malfeasance in office." In practice, this means that Presidents have not removed independent agency heads because of political disagreements. On October 11, 2016, in *PHH Corp. v. CFPB*, a three-judge panel of the D.C. Circuit invalidated a provision of the Dodd-Frank Wall Street Reform and Consumer Financial Protection Act that insulated the Director of the CFPB from removal by the President except "for cause," but provided for a limited remedy. Specifically, the Court invalidated the "for cause" removal restriction for the Director of the CFPB, allowing the President to more freely remove the Director from his service.

Congress created the CFPB through the Dodd-Frank Act, a law that generally consolidated and expanded federal regulation of consumer financial products. The agency is statutorily authorized to issue regulations and bring enforcement actions and impose penalties against individuals found to violate a variety of statutes and CFPB rules. Supporters of the CFPB's structure argue that its independence permits the agency to adopt policies free from political pressures, while opponents criticize the lack of accountability that follows from this insulation from presidential control. Here, the D.C. Circuit was asked to review the CFPB Director's partial affirmation of an administrative ruling that a mortgage lender, PHH, violated the Real Estate Settlement Procedures Act (a previous Sidebar described PHH's constitutional arguments in more depth). All three judges on the circuit panel agreed that the CFPB's decision was inconsistent with the relevant governing statute, and agreed to vacate the order on those grounds. In addition, two of the three judges held that "for cause" removal protection for an independent agency headed by a single director, rather than a multi-member commission or board, violated the Constitution's separation of powers.

The majority opinion in *PHH Corp.*, written by Judge Brett Kavanaugh, focused on two primary themes: (1) a purported lack of a historical analog for the structure of the CFPB, and (2) at least in the court's view, an absence of accountability for the Director's actions. The court began by observing that the Constitution's separation of powers necessitates that the executive power, in particular, be entrusted in a President who is held accountable by the people — a constitutional feature that prevents Congress from allowing unaccountable officials to enforce the law. Judge Kavanaugh relied on the Supreme Court's 1926 decision in *Myers v. United States*, which he described as "recogniz[ing] the President's Article II authority to supervise, direct, and remove at will subordinate officers in the Executive Branch." Of course, Judge Kavanaugh continued, the Supreme Court's subsequent 1935 decision in *Humphrey's Executor v. United States* upheld Congress's power to create an independent agency headed by *multi-member expert boards* whose members are removable by the President only for cause. Judge Kavanaugh appeared to read *Humphrey's Executor* as a somewhat limited exception to the general rule endorsed in *Myers* that executive branch officers must be accountable to the

President. Judge Kavanaugh concluded that because the absence of presidential supervision "pose[s] a significant threat to individual liberty," independent agencies have historically been headed by multi-member bodies, rather than by one individual, as those members can serve as a "check" on one another. In other words, traditional executive agency heads are accountable to the President, while independent agency boards or commissions are accountable to each other. Both structures are constitutionally permissible under the reasoning of *Humphrey's Executor* and *Myers*.

Therefore, the crucial question for the D.C. Circuit was whether the Supreme Court's precedent in *Humphrey's Executor*, upholding "for cause" removal protections for multi-member independent agency boards or commissions, extended to the CFPB's single-Director structure. The D.C. Circuit panel concluded it did not. Given the lack of a clear answer in the Constitution's text, the court reasoned that historical practice and tradition could be persuasive on the matter. The circuit court found that the CFPB's structure was a "gross departure from settled historical practice." The court dismissed the relevance of those agencies cited as having a similar structure to the CFPB – for example, the Social Security Administration and the Office of Special Counsel – characterizing these agencies as "anomalies" because, among other things, they lacked "deep historical roots."

Importantly, the panel distinguished a Supreme Court opinion which affirmed the constitutionality of a single-headed independent entity in the executive branch. In the 1998 case of *Morrison v. Olson*, the Supreme Court upheld removal protections for an independent counsel that exercised prosecutorial authority in particular cases. The D.C. Circuit concluded that this precedent did not support the constitutionality of the CFPB because the Supreme Court's opinion did not explicitly examine the status of an independent agency headed by a single director and the independent counsel "had only a limited jurisdiction for particular defined investigations." Further, the court reasoned that the "independent counsel experiment ended with nearly universal consensus that the experiment had been a mistake" and the dissenting opinion of Justice Scalia in that case – challenging the independent counsel statute as unconstitutional – had been correct.

Second, the court, looking to the original purpose behind constitutional separation of powers, emphasized that the CFPB's structure threatened individual liberty. According to the court, "the multi-member structure of independent agencies acts as a critical substitute check on the excesses" of other members, which helps "prevent arbitrary decisionmaking and abuse of power." Because the CFPB Director could only be removed by the President for reasons specified by statute, the Director was not truly accountable to the President. And without the presence of a multi-member board to check his power, the circuit panel reasoned, the CFPB Director operated with immense unilateral power unconstrained by others. Given the lack of historical precedent for the CFPB and the "threat to individual liberty posed" by its structure, the D.C. Circuit concluded that Constitution did not allow for a single-headed independent agency.

However, in order to remedy the constitutional violation, the court did not block the CFPB from exercising its authority under the Dodd-Frank Act, but instead invalidated and severed only the statutory provision that protected the Director from removal by the President. The effect of the decision is to leave the CFPB's substantive authority in place, but render the Director subject to removal by the President at any time and for any reason. In other words, the decision does not eliminate the CFPB's powers, but instead transforms the CFPB from an independent agency – with a director who may be removed by the President only in limited circumstances – into an executive branch agency whose Director serves at the pleasure of the President.

The constitutional aspects of the opinion are unlikely to have a major impact on the immediate operations of the CFPB. The effects of the decision may be felt more substantially upon the arrival of a new President. As specified in the Dodd-Frank Act, the Director serves a term of five years, and current Director Richard Cordray's term is set to expire in July 2018. Before the D.C. Circuit's opinion, a new President faced with a CFPB Director whose tenure overlaps into his or her term in office could not remove the Director except for cause. Following the court's opinion, however, the Director may be replaced by a new President in the same manner as the heads of other traditional executive agencies. Given the importance of the decision for the separation of powers and the structure of federal government agencies, the decision is expected to be appealed for rehearing en banc by the full D.C. Circuit and potentially to the Supreme Court.