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CFPB's Watchful Eye To Sharpen In Coming Months

By **Allison Grande**

Law360, New York (August 15, 2011) -- Despite opening without a confirmed director and limited enforcement power, the new Consumer Financial Protection Bureau has already begun to cast a more watchful eye on common financial practices, a move that will permanently change the way banks and other institutions are regulated, attorneys say.

The new bureau, which opened for business on July 21, brings under one roof consumer financial protection authorities that were previously spread among seven federal agencies, with the CFPB becoming responsible for the Real Estate Settlement Procedures Act, the Truth in Lending Act, the Home Mortgage Disclosure Act and more than a dozen other consumer financial laws.

“If you look at their enforcement power, it's breathtaking what they can do to the 71,000 different business entities that they are going to have potential jurisdiction over,” Pepper Hamilton LLP financial services practice group chair Richard Eckman said, adding that this enforcement potential makes industry players “very nervous.”

Established under Title X of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the CFPB is tasked with regulating a wide array of financial institutions — including banks, nonbank lenders, brokers and loan modification companies — in order to ensure that disclosures are clear, risks are visible, and consumers are not subjected to predatory lending and other unfair or deceptive practices.

To achieve these objectives, the CFPB has said that it plans to eliminate outdated, unnecessary or overly burdensome regulations and promote transparency in financial products and services.

This overhaul of outdated rules could ultimately prove beneficial for companies by providing more certainty about how the agency intends to enforce these statutes, Troutman Sanders LLP financial services litigation group co-leader John Lynch added.

Under a unique enforcement regime, state attorneys general will act as the agency’s authority outside of its walls, with the power to bring legal actions on behalf of the agency against any institution that violates federal consumer financial law.

At the outset, the agency's powers will be limited to enforcing the existing consumer protection statutes and regulating banks that already fall under the guise of federal regulation. The bureau will make new rules and begin regulating certain nonbank firms that provide student, payday and mortgage loans when it has a permanent director in place.

President Barack Obama nominated former Ohio Attorney General Richard Cordray to lead the agency on July 18, but his confirmation process could be stalled by congressional concerns about allowing a single director instead of a board of commissioners to run the nascent agency.

Dykema Gossett PLLC financial industry group director Richard Gottlieb pointed out that the agency has “already been effectively functioning for quite some time.”

In early July, the CFPB issued a guidance advising the 111 depository institutions that have total assets exceeding $10 billion — the only institutions the agency can regulate until it has a permanent director — to plan for an agency review of their products and services. The examiners will seek to determine whether the institutions are complying with consumer rules throughout their life cycle, which includes development, marketing, sales and management, the CFPB said.

Large financial institutions should not expect these examinations to die out, the CFPB said in its guidance, adding that it plans to conduct periodic examinations for most of the banks that it regulates. It also plans to implement a year-round supervision program for the largest and most complex banks in the country.

The examinations are intended to assess each institution’s ability to detect, prevent and remedy violations that may harm consumers; evaluate an institution’s policies and practices for compliance with the consumer financial protection laws and regulations; and provide the basis for potential enforcement actions.

The CFPB has also reached out to small financial institutions like community banks and credit unions to tell them that it plans to pay close attention to the potential impact of any proposed policy initiative on small financial services providers, in an effort to ensure that both large and small depository and nondepository institutions play fair.

The CFPB is required to afford this measure of protection under the Small Business Fairness and Regulatory Transparency, or “Speed Bump,” Amendment of Dodd-Frank.

This kind of insurance is especially important for smaller institutions that are not as well equipped as larger institutions to deal with the cost of implementing the changes brought by the new bureau and may not have been subject to such focused regulatory scrutiny in the past, Mayer Brown LLP partner Jeffrey Taft said.

However, the agency will not be so willing to consider such consequences when examining and regulating larger institutions, according to experts.

“Before the creation of the bureau, regulation was a more evenhanded approach of examiners looking at whether what the banks were doing was reasonable,” Eckman said. “This new process doesn’t have the safety and soundness [of the banks] at the forefront, and might make banks more prone to fight the agency’s conclusions.”

The agency has already released reports on how the Credit Card Accountability Responsibility and Disclosure Act of 2009 has affected supply, demand and pricing in the credit card marketplace in light of the recession and its aftermath; on the variation in credit scores sold by certain consumer reporting agencies; and on the use of remittance histories for credit scores.

And a prelaunch initiative, started in May, to combine RESPA and TILA mortgage disclosures into a single, simpler form that makes the costs and risks of the loan clearer, has already garnered more than 18,000 comments.

Simpson Thacher & Bartlett LLP partner Stacie McGinn noted that the final version of Dodd-Frank attempted to strike a compromise by creating some power on the part of prudential regulators to object to CFPB regulations that they believe might negatively impact the safety and soundness of the banking system.

But this measure, which only provides veto rights to these entities collectively in the context of rulemaking, is unlikely to be used much in practice, McGinn added.

When the agency receives its full enforcement power, it is expected to issue more proposed amendments to clarify existing statutes and to reshape payday lending, robo-signing and other potentially deceptive financial practices. Such moves could stifle innovation among both large and small financial institutions, according to experts.

“In the guise of protecting consumers, the agency has to be careful that it does not kill ingenuity that could lead to better choices for consumers,” Gottlieb said. “You don't want to see a situation where the bureau so decimates entrepreneurship and creativity in consumer lending that there is no competition and consumers have no choices.”

The uncertainty that comes along with the launch of a new agency might also make financial institutions weary about “rolling out new programs until the regulatory regime plays out,” Taft added.

But McGinn remains optimistic that the agency can realize its dual mandate to protect consumers while ensuring access to financial products and services without stifling “the great strides” of the industry in creating innovative products and services.

“At the end of the day, you would hope that in carrying out its consumer protection mission, the agency will acknowledge the benefits that consumers receive from these products and services and will not stifle industry innovation in the process,” McGinn said.

While waiting for the bureau to gain its full powers and make its mark on the industry, companies should begin to adjust to the new enforcement power they will face by becoming familiar with state attorneys general who have the ability to bring legal action against them.

“A lot of companies haven't had to deal with attorneys general before, but now it will be increasingly important for these companies to have relationships with the more active attorneys generals in certain states who may be bringing these enforcement actions,” Lynch said.

Eckman recommended that financial institutions use consumer focus groups to get feedback about how their products are being perceived in order to comply with the standards that promise to be enforced by the new regulator.

“Before, financial institutions would read the regulations and prepare product disclosures that comply with those regulations,” Eckman said. “But now the bureau is going to want them to make sure that their products are also simple and clearly transparent as well, so these institutions are going to need to be much more proactive about finding out how their products are being perceived by consumers.”

--Editing by Andrew Park.

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