Statement of Rachel E. Barkow
Professor of Law
Faculty Director, Center on the Administration of Criminal Law
New York University School of Law

The Proposed Consumer Financial Protection Agency: Implications for Consumers and the FTC

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Mr. Chairman and Members of the Subcommittee: Thank you for inviting me to testify before you regarding the Consumer Financial Protection Agency Act of 2009 (CFPA Act or Act). It is an honor to appear before you to discuss this landmark legislation.

At the center of the Act is the creation of an agency charged with protecting and informing consumers in the increasingly complicated world of financial services and products. The Act itself gives few substantive standards for financial products and services. Instead, it leaves it to the Consumer Financial Protection Agency (CFPA) to set benchmarks for this field. Thus, whether the Act will succeed or fail in its mission "to promote transparency, simplicity, fairness, accountability, and access in the market for consumer financial products or services" will depend entirely on whether the agency it creates succeeds or fails.

My testimony therefore explores the structure and powers of the proposed CFPA to determine if it has been designed in the most effective way to achieve its stated statutory mission. I take no position on the merits of that mission or whether there is a need for a new agency to regulate this field. Rather, my focus is on whether the CFPA has been designed as effectively as it can be to achieve the goals of the legislation.

After reviewing the Act in light of the experience of other agencies charged with protecting consumer interests, I have five recommendations and a note of caution. To briefly summarize, they are as follows (listed in the approximate order of importance):

First, I recommend including a provision that would limit the CFPA's membership to no more than three members of the same political party. Unlike virtually all other legislation that governs multi-member independent agencies, including the Federal Trade Commission (FTC), Securities and Exchange Commission (SEC), and Consumer Products Safety Commission (CPSC), the CFPA Act does not require a political balance among the agency's membership. The absence of such a provision in the CFPA Act could lead to a politically-polarized agency that dramatically changes positions from one extreme to another with each new presidential administration. This is unhealthy for the regulation of any market, and there is no apparent justification for the Act's current design of the CFPA.

Second, although the CFPA has elements that are designed to prevent capture by the industry actors the agency will be regulating, there is room for improvement. Specifically, I propose taking a close look at the Act's consultation requirement. This mandate will inevitably cause delays and legal challenges to the CFPA's regulations, so unless Congress is of the view that these costs are outweighed by the benefits of coordination, I recommend modifying this provision to make clear that consultation is at the discretion of the CFPA and not subject to judicial review.

Third, I advise modifying the statute of limitations provision in the Act to begin running from the time the CFPA discovers a violation, not from the time a violation has occurred.

Fourth, I suggest including a limitation on the ability of CFPA Board members to practice before the CFPA for a period of time after their terms of service on the Board have expired. This restriction would limit the negative effects caused by the revolving door between agencies and the industries they regulate.

Fifth, I recommend giving the CFPA's research unit a mandate to analyze and report on the suppliers of financial services and products and on the regulations imposed on those suppliers by other regulators.

Finally, my last major point is to raise the issue of the relationship between the CFPA and the President. It is unclear from the Act as it is currently written whether the CFPA will be subject to presidential directives and oversight, including review by the Office of Information and Regulatory Affairs (OIRA) in the President's Office of Management and Budget (OMB). I take no position on whether or not the agency should be subject to this type of review. Rather, I highlight the lack of clarity and discuss the implications of having the CFPA be treated like other executive agencies for purposes of presidential oversight.

My statement will proceed in three parts. First, I will offer some lessons from other efforts to create agencies with mandates to protect consumer interests. Many of these agencies fall short in their efforts to protect consumers because they become captured by the industries they are charged with regulating. The experience of these agencies therefore offers some valuable insights in thinking about how to structure the CFPA. Second, and with these lessons in mind, I will turn to the proposed CFPA Act to highlight how the Act could be improved to maximize the CFPA's effectiveness. Third and finally, I will address the question of the CFPA's independence. Although there is language in the Act aiming to make the CFPA an independent agency, it departs from the traditional independent regulatory agency model in several respects that, as currently written, give the President considerable power over the agency's operation.

I. Lessons from Other Agencies: The Threat of Capture

In evaluating the CFPA, it is helpful to look at the experience of other agencies that have been charged with promulgating rules, bringing enforcement actions, and reporting to Congress in an effort to protect consumers. On many occasions agencies with such mandates have stalled in their efforts to regulate because the industries they have been charged with regulating have been far more powerful and well-financed than the consumer interests they have been charged with protecting. This is the well-known phenomenon of agency capture, and it is important to consider some of the causes so that the pitfalls of capture can be avoided or at least limited through agency design.

One sees a familiar story repeat itself when one looks at the history of the many agencies charged with protecting consumers. Even if an agency has a promising beginning of "vigorous and independent regulation," it "often becomes closely identified with and dependent upon the industry it is charged with regulating."[1] Thus, as a leading administrative law scholar has observed, "[i]t has become widely accepted, not only by public interest lawyers, but by academic critics, legislators, judges, and even by some agency members, that the comparative overrepresentation of regulated or client interests in the process of agency decision results in a persistent policy bias in favor of these interests."[2] This is true across many industries, including financial services.[3]

This bias may not be intended – on the contrary, the goal may well be to avoid it at all costs – but several dynamics push in favor of giving regulated interests disproportionate influence with the agency charged with policing them.

First, regulated industries are wealthy and well-organized, especially when compared to consumers. Industry groups are well positioned to monitor agencies closely and challenge any and all agency decisions that will negatively affect them.[4] All else being equal, agencies would prefer not to become mired in legal challenges, so they may seek to work with, rather than against, these organized interests. Although there are some important and influential groups representing consumer interests that may also threaten litigation, these interest groups do not have the funding or resources of industries. Thus, they often cannot monitor and challenge all the potentially negative rules and orders from an agency or marshal the same resources as industry representatives when they do bring a

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[1] Thomas W. Merrill, *Capture Theory and the Courts: 1967-1983*, 72 CHI.-KENT L. REV. 1039, 1060 (1997) (citing the work of MARVER H. BERNSTEIN, REGULATING BUSINESS BY INDEPENDENT COMMISSION 79-94 (1955)).

[2] *See* Richard B. Stewart, *The Reformation of American Administrative Law*, 88 HARV. L. REV. 1669, 1713(1975).

[3] Raj Date, Regulator Unbound: Solving an Old Problem at a New Regulatory Agency 2-5 (July 2, 2009), *available at* http://www.cambridgewinter.org/Cambridge_Winter/Regulator_Unbound_files/regulator%20unbound%20070209.pdf.

[4] Mark Seidenfeld, *Bending the Rules: Flexible Regulation and Constraints on Agency Discretion*, 51 ADMIN. L. REV. 429, 464 (1999).

challenge.[5] As a result, agencies tend to be less likely to worry about satisfying consumer groups than the more powerful regulated industries.

The experience of the CPSC illustrates this phenomenon. The CPSC was created in 1972 to "protect the public against unreasonable risks of injury associated with consumer products."[6] At the time it was established, the CPSC was charged with enforcing statutes that were then administered by other agencies and given new powers as well.[7] The CPSC was heralded as the "most powerful Federal regulatory agency ever created."[8] But it soon became apparent that the CPSC was unable to fulfill its statutory mandate. The major reason is that the CPSC has been chronically underfunded and understaffed relative to its mandate.[9] As a result, the CPSC has been no match for the industry participants it is charged with regulating.

Product manufacturers have used their resource advantage to capitalize on various procedural rules in the Consumer Product Safety Act (CPSA). For instance, Section 7 of the CPSA created what was known as the offeror process, which required the CPSC to solicit and use people from outside the agency to draft its safety standards. The CPSC would put out a notice in the Federal Register describing the need for some standard and inviting people to propose a standard or to offer to develop a standard. After the offeror submitted its proposal, the CPSC could adopt or revise it and then had to seek comments on the resulting standard. In theory, offerors could be consumer groups, standard-setting organizations, other agencies, or industry groups. In reality, the process was dominated by industry. Because submitting a proposal was resource-intensive, consumer groups and standards organizations found the process too burdensome; the process was "affordable only to industry groups with an economic stake in the outcome."[10] Industry representatives did not just dominate the drafting stage, they often controlled the outcomes. Industry representatives brought successful challenges to most of the CPSC's rules in court.[11] Ultimately, Congress viewed the offeror process as a failure and abolished it.

Section 10 of the CPSA, which was designed to give consumers a greater say with the agency, suffered a similar fate. Section 10 established a process whereby interested persons could petition the agency to issue rules and the CPSC would have to respond to those requests with reasons and face de novo judicial review. This framework was enacted with the intent to allow the public to "overturn bureaucratic inertia."[12] In fact,

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[5] Seidenfeld, *supra* note 4, at 464 ("A regulated entity frequently is a large corporation with resources to appeal agency decisions at every level.").
[6] 15 U.S.C. § 2051(b)(1).
[7] Robert S. Adler, *From "Model Agency" to Basket Case – Can the Consumer Product Safety Commission Be Redeemed?*, 41 ADMIN. L. REV. 61, 63 (1989).
[8] Teresa M. Schwartz, *The Consumer Product Safety Commission: A Flawed Product of the Consumer Decade*, 51 GEO. WASH. L. REV. 32, 43-44 (1982) (quoting Swit, *An Overview of Public Law 92-573¸*Proceedings of the Briefing Conference on the Consumer Product Safety Act 7 (1973) (sponsored by the Product Safety Letter, Inc.)).
[9] *See id.* at 44.
[10] *Id.* at 63-64.
[11] *Id.* at 66.
[12] 118 Cong. Rec. 21,854 (1978) (remarks of Sen. Magnuson).

however, the process itself impeded the agency from fulfilling its mandate because the CPSC was overrun with petitions, including from industry participants who had economic incentives to get the agency to pass particular standards. Section 10 was therefore also ultimately revoked in 1981.

The story of the CPSA and the CPSC is thus a cautionary tale of how even well-intended provisions can cut against the ultimate success of a statute. Procedural rights aimed at benefitting consumers and creating better policy can become hijacked by well-financed and well-organized industry representatives.

Agency capture is further exacerbated by the fact that industry groups are also well positioned to contribute to political campaigns and to lobby, which in turn gives them influence with the agency's legislative overseers. For example, Arthur Levitt, the chair of the SEC from 1993-2001, describes the SEC during his tenure as being constantly threatened with budget cuts by the SEC's congressional overseers if it pursued aggressive regulations.[13]

Second, capture is also the result of the well-documented phenomenon of a "revolving door" between agencies and the industries they regulate. While serving on an agency's board, agency heads may also be thinking about their prospects in the private sector when their term at the agency expires. This outlook may make these officials reluctant to impose regulations that an industry views as too aggressive or obtrusive. It may dim an official's job prospects or make that job more difficult if the official has to live with the rules upon leaving the agency.[14]

The effect of the revolving door is often cited as one of the reasons why the SEC has failed to address some pressing problems in the trading industry. For example, although late trading and market timing were widespread and well known, the SEC did not act to regulate the practices and stepped in only after the New York Attorney General (AG) brought an enforcement action under state law. Similarly, it was the New York AG who led the fight to stop investment firm bankers from influencing the reports of firm analysts. Experts on SEC practice have noted that the SEC did not initially address these problems because of a prevailing view among SEC officials that, given the "rapidly revolving door between the SEC and private legal practice," "unless an issue has become high profile, it is best not to rock the boat."[15] The SEC became overpopulated with members who "identified with the market participants they were ostensibly regulating."[16] These pressures may have led the agency to adopt an overly lax view of its enforcement

[13] ARTHUR LEVITT, TAKE ON THE STREET 123, 132 (2002)
[14] JERRY L. MASHAW & DAVID L. HARFST, THE STRUGGLE FOR AUTO SAFETY 16 (1990) (noting that agency officials may take into account "social and business relations and the prospects of further career opportunities in the private sector").
[15] John C. Coffee, Jr., *A Course of Inaction*, LEGAL AFFAIRS 46 (Apr. 2004).
[16] Jonathan R. Macey, *State-Federal Relations Post-Eliot Spitzer*, 70 BROOK. L. REV. 117, 128 (2004).

and regulatory functions, which in turn created a void that was filled by the New York AG's office.[17]

Finally, another key factor that helps to give regulated entities disproportionate influence is their information advantage. For an agency to regulate an industry effectively, it needs to know how the industry works and what it is capable of doing. But that information is often in the exclusive control of the regulated entity.[18]

The factors that push toward agency capture can be minimized in various ways. Although it is not possible to adjust the relative resources of industries and consumers, one way to keep the agency from being overwhelmed by industry challenges is to provide it with the resources it needs to carry out its mandate. Additionally, it is important to ensure that the agency will not face insurmountable procedural obstacles in adopting its rules or be subject to unnecessary challenges regarding the scope of its mandate. Second, the revolving-door phenomenon can be curbed by imposing post-employment restrictions on agency officials. Finally, the agency can be assisted in obtaining information by imposing statutory reporting requirements on regulated entities and giving the agency subpoena power. While there is no perfect or complete solution to agency capture, efforts such as these can mitigate its effects and assist an agency in fulfilling a mandate to protect consumers.

II. Protecting the CFPA from Capture

These lessons serve as a helpful backdrop to analyzing the proposed structure of the CFPA. Although the legislation contains some protections for the agency that will assist it in achieving its statutory mission, there are areas that could be improved.

A. Leveling the Regulatory Playing Field

As noted above, agencies can become hampered in their ability to fulfill their mandates when regulated interests leverage procedural rights under a statute to their advantage. The CFPA Act generally relies on the standard requirements in the Administrative Procedure Act (APA) that apply to most independent and executive agencies. But the Act goes beyond the APA by establishing an additional procedural requirement of consultation before the CFPA can promulgate rules under the Act. That consultation requirement has the potential to bog down the CFPA as it tries to establish regulations for this field.

There is language throughout the Act that requires the CFPA to consult with other agencies before it promulgates rules. For instance, in Sections 1022(b)(2) and

[17] Rachel E. Barkow, *The Prosecutor as Regulatory Agency*, in PROSECUTORS IN THE BOARDROOM: USING CRIMINAL LAW TO REGULATE CORPORATE CONDUCT (Anthony Barkow & Rachel Barkow, eds., NYU Press forthcoming), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1428934.

[18] Stewart, *supra* note 2, at 1714; Seidenfeld, *supra* note 4, at 464. For a discussion of how industry participants used their information advantage to avoid regulation of credit default swaps and possible remedies to this problem in the context of consumer financial products and services, see Date, *supra* note 3, at 6-9.

1031(d), the CFPA is required to "consult with the Federal banking agencies, or other Federal agencies, as appropriate, regarding [or concerning] the consistency of a proposed rule with prudential, market, or systemic objectives administered by such agencies." In Section 1035(c), the agency is again required to consult with Federal banking and other agencies, as well as with "State authorities."

These provisions are likely to make it difficult for the CFPA to promulgate rules in a timely manner. These provisions apply to a large number of agencies because so many agencies regulate related fields. And when consulting each of these agencies, the CFPA is charged with considering all of the prudential, market, and systemic objectives of these other agencies – that is, anything of any importance to the consulted agency. This consultation process is therefore likely to delay the promulgation of CFPA rules. This is especially so because failing to take these provisions seriously will make any rules that the CFPA does pass vulnerable to innumerable legal challenges on the ground that the CFPA did not adequately consider a competing agency's objectives. This is the kind of sweeping substantive standard that allows industry participants to tie up agency rules for years with challenges.[19]

Congress may wish to keep this language to ensure rigorous consultation and coordination, even if that means slowing down the CFPA's regulatory progress. But if Congress is concerned that this provision will create unnecessary litigation, it could likely achieve substantial coordination without subjecting the CFPA to as many challenges if the language were to make clear that it is left to the CFPA's discretion how and when to consult. For example, the section could be modified to state that the agency shall "consult with the federal banking agencies, or other Federal agencies, as the Agency in its judgment deems appropriate . . ." and further clarify that the consultation requirement is not subject to judicial review. Again, however, whether the Act should be modified along these lines depends on Congress's considered judgment as to the relative importance of coordination.

The need for the current consultation requirement may also depend on whether the CFPA is an executive agency for purposes of presidential oversight, as discussed more fully below in Part III. If it is an executive agency for oversight purposes, then OIRA can serve the coordinating function of the Act's consultation provisions and make sure that the CFPA's rules are consistent with other agencies.[20] In other words, with

[19] Section 1038 imposes a similar consultation requirement. It provides that "the CFPA shall, when prescribing any rule under this section, consult and coordinate with Federal banking agencies and the Federal Trade Commission" to, among other things, "ensure that the rules impose substantially similar requirements on covered persons." This requirement lacks the "as appropriate" language, so it is broader than the other provisions in that it seems to be a prerequisite any time the CFPA seeks to prescribe rules on consumer access to information. On the other hand, this provision is narrower than the other consultation provisions because the CFPA need only consult the banking agencies and the FTC. But to the extent this consultation requirement subjects the CFPA to challenges that it fails adequately to take into account the requirements of the banking agencies or the FTC, it, too, subjects CFPA rules to broad challenges.
[20] U.S. Gov't Accountability Office, Report to the Chairman, Committee on Oversight and Government Reform, House of Representatives, Federal Rulemaking: Improvements Needed to Monitoring and Evaluation of Rules Development as Well as to the Transparency of OMB Regulatory Reviews 8 (April

OIRA review, this provision may be largely duplicative and simply serve to delay and impede CFPA regulations.

There is an additional obstacle the Act puts in front of the CFPA when it seeks to bring an enforcement action. Section 1054(g)(1) sets out the statute of limitations for the Act, and it provides that "no action may be brought under this title more than 3 years after the violation to which an action relates." Because violations by sophisticated business interests are often not discovered for years, this provision may hamper the CFPA in its enforcement efforts because the clock starts running from the time of the violation, not from the time when the agency discovers the violation.

In related areas, Congress has been careful to trigger the running of the statute of limitations to the time of discovery. For example, suits brought for violations of the Right to Financial Privacy Act may be brought "within three years from the date on which the violation occurs or the date of discovery of such violation, whichever is later."[21] Similarly, the Federal Deposit Insurance Corporation is allowed to bring suit to recover an underpaid amount on an assessment "until 3 years after the date of discovery of the false or fraudulent statement."[22] Suits for false statements or the omission of material facts with regard to securities sales and suits for false registration statements may be brought "within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence."[23]

Given the sophistication of the suppliers of consumer financial products and instruments, it would seem that there is even greater reason than in these other contexts to allow suit to begin from the time of discovery of the violation. As with suits regarding false statements regarding securities, a provision can be added to the CFPA Act noting that the clock starts running from the time of discovery or after such discovery should have been made by the exercise of reasonable diligence. This would protect the interests of suppliers in case the agency was unreasonably slow in its pursuit of violations, but would also protect consumers when a violation was, despite all reasonable efforts, not discovered for a period of time after the violation itself.

While the consultation requirement and the current statute of limitations provision seem to cut in favor of regulated entities, the Act has other provisions that work as counterweights to capture. One of these is Section 1042, which allows State attorneys general to enforce provisions of the Act. As noted above, attorneys general have served a checking function when the SEC has failed to police an area of industry abuse. Section 1042 would allow State AGs to serve a similar function in the context of the CFPA Act. If the CFPA is unwilling or unable to address a problem with consumer financial products or services, State AGs can provide additional resources to police the Act.

2009) (noting that OIRA is responsible for making sure that "decisions made by one agency do not conflict with the policies or actions taken or planned by another agency").

[21] 12 U.S.C. § 3416.

[22] 12 U.S.C. § 1817(g)(2)(C).

[23] 15 U.S.C. § 77m.

Moreover, because the CFPA retains the right to intervene in these actions, it can ensure that its views are known if it is concerned that the AG's action may lead to bad policy.[24] The Act thus effectively uses AGs as a check on capture while respecting the expert judgment of the CFPA.

The Act also provides in Section 1041(a)(1) that states may continue to regulate the field of consumer financial products and services, as long as state laws are not inconsistent with the CFPA Act. The Act further specifies in various provisions that state laws are not inconsistent with the CFPA Act if the "protection such statute, regulation, order, or interpretation affords consumers is greater than the protection provided under this title, as determined by the Agency."[25] These provisions are likely to generate controversy and litigation, because whether a state law is more or less protective of consumers will not always be clear and may depend on one's view of regulation in general. Thus, whether a state law is preempted may well depend on the regulatory orientation of the CFPA's Board and whether or not it tends to trust market forces more or less. For example, if a majority of the CFPA's Board is of the view that market forces better protect consumers than do regulations, the agency may seek to preempt state laws that regulate industry more heavily than CFPA regulations that do not go as far. The effect of this provision on capture is therefore contingent on the views of the CFPA Board and how much deference courts give those views. This provision will provide a check on industry bias only to the extent the CFPA is an accurate judge of what is more protective of consumers.

B. Stopping the Revolving Door

There is another way in which Congress can give the CFPA greater immunity from capture, and that is to impose limits on the ability of the CFPA Board members to work for the very industry actors they are charged with regulating.

Congress has imposed such limits in other contexts. For example, legislation creating the Public Company Accounting Oversight Board (PCAOB) charges the PCAOB with "establish[ing] ethics rules and standards of conduct for Board members and staff, including a bar on practice before the Board (and the [SEC], with respect to Board-related matters) for 1 year for former members of the Board, and an appropriate period (not to exceed 1 year) for former staff of the Board."[26] The Federal Board of Governors also imposes post-employment restrictions on its members, making them "ineligible during the time they are in office and for two years thereafter to hold any office, position, or employment in any member bank."[27] Members of the Board of the Farm Credit Administration are also ineligible to work for "any institution of the Farm Credit System" while they are in office and for two years thereafter.[28]

[24] *See* Barkow, *supra* note 17, at 25-27.
[25] *See*, *e.g.*, Section 1041(a)(2); Section 5136C(c)(2); Section 5136C(d)(2); and Sections 6(c)(2) and (d)(2)(B).
[26] 15 U.S.C. § 7211(g)(3).
[27] 12 U.S.C. § 242. This restriction does "not apply to a member who has served the full term for which he was appointed." *Id.*
[28] 12 U.S.C. § 2242.

The legislation creating the CPSC does not address Board members' post-service employment but it does place restrictions on who can be named a commissioner in the first place. Specifically, it provides that a person cannot hold the office of a commissioner if he or she is "in the employ of, or holding any official relation to, any person engaged in selling or manufacturing consumer products" or owns "stock or bonds of substantial value in a person so engaged" or "is in any other manner pecuniarily interested in such a person."[29] In addition, CPSC commissioners are also barred from "engaging in any other business, vocation, or employment."[30]

The CFPA Act does not presently contain any pre- or post-employment restrictions on its Board members. Because the Act in Section 1012 seeks Board members with relevant experience "related to consumer financial products or services," pre-employment restrictions like those that apply to the CPSC seem unwise. Many of the most qualified people may well be currently employed in the market for consumer financial products or services or own stock in a company because of prior service. It would be feasible, however, to include post-employment restrictions along the lines of those that apply to the PCAOB, the Board of Governors, and the Members of the Farm Credit Administration. The framework that applies to the PCAOB seems particularly well suited to the CFPA because they govern similar industries. Just as it makes sense to try to limit the revolving door between the PCAOB and the accounting industry, so, too, does it make sense to limit the back-and-forth between the CFPA and those who supply financial products and services. The PCAOB legislation also has the advantage of addressing this phenomenon not just at the Board level, but at the staff level as well.

C. Access to Information

The proposed Act is attentive to the value of information to the agency. It gives the CFPA broad access to information, including allowing the agency to seek reports from covered persons (Section 1022(c)(1)), to access to the reports of other regulators (Section 1022(c)(5)), and to subpoena when necessary (Section 1052). One area where there may room for improvement is in Section 1014(c)(1), which creates a specific research unit within the agency. As currently written, the research unit is charged with researching, analyzing, and reporting on the markets for consumer financial products and services, including areas of alternative products with high growth, and on various aspects of consumer awareness and behavior. While this is valuable research, it would be helpful to the CFPA's functioning if the research unit also conducted research on the supply-side of this market. That is, the research unit could also be charged with investigating advertising and marketing practices by financial service and product suppliers. In addition, the research unit could report on the enforcement and regulatory efforts of others federal agencies and the states in addressing financial services and products. This information can assist the CFPA in determining what company practices currently look like and what regulations are feasible.

[29] 15 U.S.C. § 2053(c).
[30] *Id.*

III. The CFPA as Independent v. Executive Agency

The proposed legislation states in Section 1011 that the CFPA will be "an independent agency." At the same time, the Act makes institutional design choices that make the CFPA more political than most multi-member independent regulatory agencies (including some independent agencies whose functions the CFPA is taking over). In addition, the language of the Act is susceptible to an interpretation that gives the President greater control over the CFPA than over other independent regulatory agencies.

A. Politically Balanced Membership

There are typically two attributes that characterize a multi-member independent regulatory agency and distinguish it from an executive agency. First, unlike the heads of executive agencies who can be removed at will by the President, the members of an independent agency serve fixed terms and are removable only for cause. Second, unlike executive agencies, which are most often headed by a single appointee who shares the President's political goals for that agency, almost all multi-member independent regulatory agencies are balanced in their membership so that the view of no one political party dominates.

The CFPA takes over functions relating to consumer financial protection from several traditional independent agencies that have these characteristics. The Federal Deposit Insurance Corporation (FDIC) is a five-member board, and its authorizing statute provides that no more than three members may be of the same political party.[31] The FTC is also governed by a five-member body, and its authorizing statute similarly insists that no more than three of its commissioners can be members of the same political party.[32] The National Credit Union Administration (NCUA) follows this same model. Of the three members of its board, only two may be members of the same party.[33]

Unlike the legislation establishing these independent agencies, the CFPA Act currently lacks any requirement that seeks to balance the politics on the CFPA's five-member Board. As a result, it is not inconceivable – and perhaps to be expected – that a President would appoint only members of his or her political party. Thus, if a President serves two terms, he or she could create a Board entirely composed of members of his or her political party because each Board member's term will have expired over a period of five years. While Senate confirmation may act as a check on this, it is no guarantee of ideological balance or moderation.

The legislation establishing most multi-member independent agencies insists on party balance for good reason. As a wealth of empirical research demonstrates, a group comprised solely of ideologically like-minded people tends toward extreme

[31] 12 U.S.C. § 1812(a)(2).
[32] 15 U.S.C § 41.
[33] 12 U.S.C. § 1752a(b)(1).

decisionmaking.[34] Liberals and conservatives alike become more liberal and conservative, respectively, when they deliberate only with like-minded people. Thus, as Cass Sunstein has observed, "[a]n independent agency that is all Democratic, or all Republican, might polarize toward an extreme position, likely more extreme than that of the median Democrat or Republican, and possibly more extreme than that of any member standing alone."[35] This kind of polarization is unwise for an agency regulating an area as complicated as consumer financial products and services because it could mean wide fluctuations in policy as presidential administrations change. Indeed, dramatic shifts in positions based on political winds were precisely the evil that independent agencies were designed to combat. When the FTC was created, for instance, the Senate Committee Report emphasized the need "for an administrative board . . . which would have precedent and traditions and a continuous policy and would be free from the effect of such changing incumbency."[36]

A multi-member commission that is politically balanced is beneficial for another reason. As noted above, one of the concerns with agencies that regulate powerful, wealthy industries is that those industries tend to dominate the agency's agenda because they have greater resources to monitor what the agency is doing. But when an agency is composed of members of different parties, it has a built-in monitoring system for interests on both sides because that type of body is more likely to produce a dissent if the agency goes too far in one direction.[37] That dissent, in turn, alerts Congress and the public at large that the agency's decision might merit closer scrutiny.

It is possible that the proposed legislation does not follow this template for multi-member independent regulatory agencies because the CFPA is not just taking over functions from traditional multi-member independent agencies. It is also assuming consumer protection functions from two executive agencies – the Comptroller of the Currency and the Office of Thrift Supervision (OTS) – and the Board of Governors. The Board of Governors is unique among most multi-member independent agencies because it does not have a requirement that its membership be politically balanced.[38] But the

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[34] *See*, *e.g.*, David Schkade, Cass R. Sunstein & Reid Hastie, *What Happened on Deliberation Day?*, 95 CAL. L. REV. 915 (2007) (discussing the results of an experiment that shows that liberals and conservatives become more liberal and conservative, respectively, as a result of deliberation amongst like-minded people); Cass R. Sunstein, David Schkade & Lisa Michelle Ellman, *Ideological Voting on Federal Courts of Appeals: A Preliminary Investigation*, 90 VA. L. REV. 301 (2004) (discussing data that shows that unified groups of three Democrat-appointed or Republican-appointed judges are far more likely to vote in a "liberal" or "conservative" manner, respectively, than Democrat-appointed or Republican-appointed judges who are part of a divided bench); Cass R. Sunstein, *Deliberative Trouble? Why Groups Go to Extremes*, 110 YALE L.J. 71, 74 (2000) ("In brief, group polarization means that members of a deliberating group predictably move toward a more extreme point in the direction indicated by the members' predeliberation tendencies.").

[35] Sunstein, *supra* note 34, at 103.

[36] 51 Cong. Rec. 10376 (1914).

[37] A recent empirical study of the Federal Communications Commission (FCC), for example, found that partisanship accounts for roughly 75 percent of the FCC's non-unanimous decisions. Daniel E. Ho, *Congressional Agency Control: The Impact of Statutory Partisan Requirements on Regulation* 35 (Feb. 12, 2007), *available at* http://dho.stanford.edu/research/partisan.pdf.

[38] The legislation creating the Board of Governors does state, however, that, in "selecting the members of the Board, not more than one of whom shall be selected from any one Federal Reserve district, the

Board of Governors is unique in other respects as well. Its members serve long terms of 14 years, and they have perhaps the most powerful agency positions in the country because of their authority to set monetary policy. Monetary policy cannot, of course, fluctuate in an extreme manner as administrations change because of the deleterious effect it would have on the economy. It is therefore unsurprising that even without a requirement that the Board be politically balanced, it is one of the most stable agencies in government and the most independent. As for the Comptroller of the Currency and OTS, those two agencies in Treasury are not multi-member bodies, so their design does not speak to political balance. More fundamentally, as with the Board of Governors, there is no reason to believe that these agencies were designed with their consumer protection functions, as opposed to their more central regulatory functions, in mind.

The CFPA, in contrast, has as its sole mission the protection of consumers in the market for financial products and services. It therefore most closely resembles agencies such as the FTC, the SEC, and the CPSC in its goals – and the legislation for all of those multi-member agencies insists on political balance to help achieve more stable policy outcomes over time. For the same reasons that Congress opted for political balance on those agencies, it should do so with respect to the CFPA as well.

B. Executive Oversight

It is unclear from the proposed legislation what the intended relationship is between the CFPA and the President. Although the legislation states in Section 1011 that the agency is to be "independent," it immediately adds that the agency will be "in the executive branch." Coupled with the lack of a provision that seeks party balance, the legislation is at least susceptible to an interpretation that it is creating an agency that, while independent in some respects (specifically, giving Board members some protection from removal from office), it is otherwise a traditional executive agency subject to presidential oversight and direction.

That presidential oversight could include subjecting the CFPA to various executive orders that require executive agencies to conduct cost-benefit analysis of proposed regulations and guidance documents, to explain what market failure a proposed regulation addresses, and to submit that analysis to the President's Office of Information and Regulatory Affairs for review.[39] These orders also require agencies to designate a regulatory policy officer (RPO) to oversee compliance with the requirements of the executive orders, and a recent order insists that the RPO be a presidential appointee. As a recent Government Accountability Office (GAO) report documents, the OIRA regime expands the President's influence over an agency's substantive policies, frequently leading to significant and material modifications in the agency's regulations.[40]

President shall have due regard to a fair representation of the financial, agricultural, industrial, and commercial interests, and geographical divisions of the country." 12 U.S.C. § 241.

[39] Executive Order 12866; Executive Order 13422.

[40] GAO Report, *supra* note 20, at 30 (reviewing 12 rules submitted to OIRA and finding that OIRA review led to significant or material changes for eight of them).

The Executive orders currently exempt independent agencies from their purview, but an independent agency for purposes of the orders is defined by the Paperwork Reduction Act.[41] The current CFPA Act does not propose an amendment to the Paperwork Reduction Act to include the CFPA among the list of independent agencies, so it is certainly possible, perhaps likely, that OIRA could conclude that the CFPA is not an independent agency for purposes of its review process, particularly given that the Act specifies that the CFPA is "in the executive branch."

In this regard, it is noteworthy that the statutes creating the independent regulatory agencies listed in the Paperwork Reduction Act do not use the same "independent agency in the executive branch" language that the CFPA Act does. In contrast, that language has been used to describe executive agencies that are subject to presidential oversight. For example, the Act creating the Social Security Administration (SSA) states that it shall be "an independent agency in the executive branch."[42] The SSA, in turn, has complied with executive orders on regulatory review, including the appointment of a regulatory policy officer.[43] Similarly, the Federal Emergency Management Agency has also been characterized as an "independent agency in the Executive Branch,"[44] though it, too, is subject to presidential oversight.[45]

There is, then, a significant possibility that the CFPA Act will subject the CFPA to oversight by the President, including the extensive review of regulations conducted by OIRA.[46] Congress should therefore determine whether it wants the CFPA to be subject to this kind of presidential oversight.

OIRA review has benefits. It helps the President coordinate policies across the Executive branch, and requiring an agency to submit a cost-benefit analysis of a proposed regulation to OIRA can have potentially positive disciplining effects because OIRA brings a fresh set of eyes to the issue. And, in recent years, OIRA review has been

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[41] Executive Order 12866 §3 (including all agencies within its ambit except those "considered to be independent regulatory agencies, as defined in 44 U.S.C. § 3502(10)"). 44 U.S.C. § 3502 has since been amended so that independent regulatory agencies are now defined in § 3502(5).
[42] 42 U.S.C. § 901.
[43] Agency Regulatory Policy Officers (as of June 19, 2008), *available at* http://georgewbush-whitehouse.archives.gov/omb/inforeg/regpol/agency_reg_policy_officers.pdf.
[44] *See* notes following 15 U.S.C. § 2202 (transfer of functions).
[45] *See*, *e.g.*, Interim Final Rule, 66 Fed. Reg. 15968 (noting that a FEMA rule has been reviewed by OMB for compliance with 12866).
[46] There is a constitutional question whether OIRA can exercise oversight over an independent agency. *See* Richard L. Revesz & Michael Livermore, Institute for Policy Integrity, New York University School of Law, Memorandum 5 (Feb. 13, 2009) filed in response to Memorandum from the President of January 30, 2009 concerning Regulatory Review, published at 74 Fed. Reg. 5977 (Feb. 3, 2009), *available at* http://www.reginfo.gov/public/jsp/EO/fedRegReview/Revesz_Livermore.pdf; Robert W. Hahn & Cass R. Sunstein, *A New Executive Order for Improving Federal Regulation? Deeper and Wider Cost-Benefit Analysis*, 150 U. PA. L. REV. 1489, 1534-1537 (2002). To the extent the CFPA Act has language distinguishing it from more traditional independent regulatory agencies, however, that constitutional question may be avoided because a court could conclude that this language signifies Congress's intent that presidential oversight, including OIRA oversight, is acceptable.

relatively expeditious, taking less than a month of additional time.[47] Moreover, because the CFPA members are not removable by the President except for cause, OIRA review would give the President some degree of influence over the CFPA's agenda. Thus, to the extent the President represents a national constituency, that view will be represented before the agency.

But there are costs to OIRA oversight as well. The more susceptible an agency is to presidential oversight, the more likely the agency's policies will shift as new administrations take power. Dramatic shifts hinder business planning and create legal uncertainty, which can be damaging to any market, including the one for financial products and services. In addition, OIRA has traditionally had a deregulatory bias. Although many urge OIRA to take a more aggressive role in policing agency inaction as well,[48] OIRA's history is to the contrary. There remains the risk, then, that OIRA review could put pressure on the CFPA to be less ambitious in its regulatory positions. The potential for OIRA to delay the implementation of regulations in the future is also a possibility.

Congress therefore faces the question of whether it would like presidential oversight in the form of OIRA review for the CFPA or whether it would prefer to insulate the CFPA from this type of supervision. If Congress wishes to make clear that the CFPA is not subject to OIRA review and other presidential directives, it should amend 44 U.S.C § 3502(5) to include the CFPA or otherwise provide in the CFPA Act that the CFPA is to be treated as an independent agency for purposes of presidential executive orders governing agency oversight. If Congress wishes to make clear that the CFPA is subject to presidential oversight, it should amend the CFPA to state this more clearly. I take no position on which path Congress should pursue, but simply flag that, as the Act now stands, it is unclear what the relationship between the President and CFPA will be.

IV. Conclusion

Thank you for allowing me to testify and share my thoughts on this critical piece of legislation. I would be happy to answer any questions that you might have.

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[47] *See* OMB Watch, *OIRA's Role in the Obama Administration Examined*, *available at* http://www.ombwatch.org/node/10115.
[48] *See* Revesz & Livermore, *supra* note 46, at 1-3; Hahn & Sunstein, *supra* note 46, at 1521-1524.