NO. 13-56484

**UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT**

CONSUMER FINANCIAL PROTECTION BUREAU,
Plaintiff-Appellee,

v.

CHANCE E. GORDON,
Defendant-Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA

No. CV12-06147
(Honorable Percy Anderson, United States District Judge)

BRIEF OF AMICUS CURIAE CATO INSTITUTE IN SUPPORT OF DEFENDANT-APPELLANT AND REHEARING *EN BANC*

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CORPORATE DISCLOSURE STATEMENT

Amicus curiae Cato Institute states that it has no parent companies, subsidiaries, or affiliates, and that it does not issue shares to the public.

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INTRODUCTION AND INTEREST OF AMICUS CURIAE

Amicus curiae Cato Institute ("Cato") was established in 1977 as a nonpartisan public policy research foundation dedicated to advancing the principles of individual liberty, free markets, and limited government. Cato's Center for Constitutional Studies was established in 1989 to help restore the principles of limited constitutional government that are the foundation of liberty. Toward those ends, Cato publishes books and studies, conducts conferences and forums, publishes the annual *Cato Supreme Court Review*, and files amicus briefs.

Cato is interested in this case because it poses a significant challenge to the vitality of the Appointments Clause, a bulwark of individual liberty and check on the unbridled exercise of executive power without Congressional oversight. Cato agrees with Defendant-Appellant that the possibility of future "ratification" cannot justify the present *ultra vires* exercise of executive power by an agency head not duly appointed in accordance with the Appointments Clause.

More generally, Cato has devoted considerable attention—through its sponsorship of scholarship, public debate, and testimony before Congress—to the Consumer Financial Protection Bureau's structure and functions, as well as Congressional oversight of its activities. *See*, *e.g.*, Mark Calabria, "The CFPB: Problem or Solution?" Mortgage Orb (Aug. 17, 2012) (discussing greater need for Congressional oversight of Bureau's functions) (available at http://bit.ly/29tbkAY); Testimony of Mark Calabria before the Committee on Financial Services, Subcommittee on Oversight and Investigations (Dec. 16, 2015) (discussing Fourth Amendment implications for Bureau's data collection activities) (available at http://bit.ly/29B94qy).

The questions at issue here are not limited to the facts of this dispute. A constitutional challenge to the CFPB is pending before the U.S. Court of Appeals for the District of Columbia Circuit. *See PHH Corp. v. CFPB*, No. 15-1177 (whether

CFPB's structure violates the U.S. Constitution's separation of power principles). Earlier this year, that Court *sua sponte* ordered briefing at oral argument as to whether an independent agency headed by a single person violates Article II as interpreted in *Free Enter. Fund v. PCAOB*, 561 U.S. 477 (2010). There, as in this case, the aggregation of wide-ranging powers in a single head of agency looms large in the Court's deliberations.

Finally, as the dissent in this case noted, the President's responsibility to "take Care that the Laws be faithfully executed" is jeopardized by the extra-constitutional exercise of enforcement powers by an agency of the Executive Branch. *CFPB v. Gordon*, 819 F.3d 1179, 1198 (9th Cir. 2016) (Ikuta, J., dissenting) (citing U.S. Const. art. II, § 3). This is an issue of considerable moment in the highest court of our land.[1]

SUMMARY OF ARGUMENT

This case presents two questions of constitutional significance: First, whether the Consumer Financial Protection Bureau (the "Bureau") was vested with Article III standing to "commence a civil action" against Appellant Chance Gordon, notwithstanding the undisputed fact that its Director was not properly appointed by the President at any point during the pendency of the enforcement proceedings in the district court. Second, whether Mr. Cordray's *post hoc* "ratification" cured retroactively his admitted lack of executive authority under the Appointments Clause.

The Court of Appeals answered both questions in the affirmative. It held that the Bureau had Article III standing because "Congress authorized the CFPB

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[1] No party counsel authored any portion of this brief. No party, party counsel, or person other than Cato or its counsel paid for this brief's preparation or submission. All parties have consented to the filing of this brief.

to bring actions in federal court to enforce certain consumer protection statutes and regulations." *CFPB v. Gordon*, 819 F.3d 1179, 1188 (9th Cir. 2016). And "[b]ecause the CFPB had the authority to bring the action at the time Gordon was charged, Cordray's August 2013 ratification, done after he was properly appointed as Director, resolves any Appointments Clause deficiencies." *Id.* at 1192.

The centerpiece of the majority's decision, and its fundamental flaw, rests on the *ipse dixit* that the Bureau may exercise executive authority to bring a civil enforcement action because the Bureau is part of the Executive Branch. This is wrong as a matter of constitutional law, and at odds with the statute creating the CFPB's enforcement regime—a statute which vests a properly appointed Director, not a headless agency of the Executive Branch, with that power. *See* 12 U.S.C. § 5491(b)(1)–(2).

The dissent rejected the majority's Article III analysis, noting that "without the Executive's power to 'take Care that the Laws be faithfully executed,' U.S. Const. Art. II, § 3, no one could claim the Executive's unique Article III standing." *Gordon*, 819 F.3d at 1198 (Ikuta, J., dissenting). That responsibility imposes on the President that he act "faithfully"—literally, in good faith. This means, at minimum, that the use of the Executive Branch's prosecutorial power must comport with standing requirements, separation of powers principles and Congress's clear statutory intent to demarcate the authority and functions of the Director of the Bureau. When the departure from the law is used to accomplish ends rejected by Congress; when the Executive Branch bypasses a statute by relying on a claim of authority withheld by Congress, this is evidence, not of the use of enforcement authority as an "exercise of judgment," but of a violation of constitutional and statutory duties—to respect the structural boundaries created under the Appointments Clause and legislation codifying that separation of powers. That is the issue presented here.

ARGUMENT

I. The Appointments Clause Represents One of the Few Checks on the Bureau's Immense and Largely Unaccountable Power.

The Director's powers are considerable, a point vividly demonstrated by the actions of the CFPB throughout the underlying enforcement proceedings. It obtained, without notice to defendants, an immediate appointment of a temporary receiver and an *ex parte* asset freeze order. Appellant's Excerpts of Record ("ER") 0018 (ECF No. 180). Shortly thereafter, the Bureau settled with some related defendants, all business partners of Gordon. That settlement included a cooperation provision that (among other things) required the settling defendants to testify against Gordon upon "request" by the Bureau. Stipulated Final Judgment and Order for Permanent Injunction and Settlement of Claims as to Defendants Abraham Michael Pessar, Division One Investment and Loan, Inc., and Processing Division L.L.C. at 12, *Consumer Financial Protection Bureau v. Chance Gordon*, No 12-6147 (C.D. Cal. Jan. 25, 2013) (ECF No. 98-1). Summary judgment was entered against Gordon, as was a permanent injunction. ER 0003, 0021, 0025 (ECF Nos. 180, 188). That order stopped short of the Bureau's proposed remedy, which would have compelled Gordon to submit periodic compliance notices to the Bureau for the next 15 years and permanently ban him from engaging in any business relating to mortgage assistance or debt relief service. The Court imposed monetary penalties, based on the retroactive imposition of damages calculated for a time period before the remedial regulation (Regulation O) was in effect. The majority vacated this portion of the order; in all other respects, the Court affirmed the district court's judgment. *Gordon*, 819 F.3d at 1198.

The extent of the Bureau's power is matched only by its insulation from democratic accountability. The CFPB is an independent bureau housed within the Board of Governors of the Federal Reserve, itself an independent regulatory agency.

12 U.S.C. § 5491(a). The CFPB was deliberately designed to be a highly independent agency. It is not subject to congressional restraints via the appropriations process. *Id.* § 5497(a)(2)(A). It has a unitary directorship, rather than a bipartisan committee structure typical in other independent regulatory agencies, such as the SEC. *Id.* § 5491(b)(2). The Director serves a fixed term of five years. *Id.* § 5491(c)(1). He may be removed by the President only for cause. *Id.* § 5491(c)(3). The accretion of powers in one officer is unprecedented.

Given these powers (and the near total lack of oversight by the President or Congress in the exercise of that authority), one of the few meaningful checks on arbitrary CFPB action is the requirement of Senate consent to the Director's appointment. *See* 12 U.S.C. § 5491(b)(2).

II. Congress Did Not Authorize the Bureau to Bring an Enforcement Action Without a Duly Appointed, Senate-Confirmed Director.

The majority brushes aside this constitutional check, concluding that Appointments Clause questions are "'nonjurisdictional,' even though they implicate core separation of powers principles." *Gordon*, 819 F.3d at 1189. To the extent the defects as to his appointment have any relevance to either the Bureau's Article III standing or the Director's enforcement authority, the majority makes short work of these concerns: Because "Congress authorized the CFPB to bring the action in question," when Mr. Cordray arrogated to himself the authority to ratify his own extra-constitutional conduct, he "resolve[d] any Appointments Clause deficiencies." *Id.* at 1192.

This is pure bootstrapping, albeit an instance that renders Mr. Cordray's plenary self-absolution of all prior, *ultra vires* acts (acts he deemed "entirely proper") little more than a superfluous exercise in constitutional etiquette. The lack of a properly appointed Officer, in the majority's view, amounts to a technical foot-fault (at most), so much so that ratification served no purpose other than to

vitiate any argument as to whether the constitutional error was harmless (assuming one occurred at all). *Gordon*, 819 F.3d at 1192, n.6.

Nearly two decades ago, Congress rejected the notion that the Appointments Clause was a mere vestigial inconvenience. It did so in direct response to *Doolin Sec. Sav. Bank, F.S.B. v. Office of Thrift Supervision*, 139 F.3d 203, 212–13 (D.C. Cir. 1998). There, an unlawfully appointed "acting director" of OTS initiated an agency enforcement action against a bank. The Court of Appeals held that the subsequent ratification by a lawfully appointed OTS director rendered the *ultra vires* action "harmless." *Id.* at 213–14. Congress denounced the result in *Doolin* as "undermin[ing] the constitutional requirement of advice and consent"; if any subsequent acting official or anyone else can ratify the actions of a person who served unlawfully, "then no consequence will derive from an illegal acting designation." S. Rep. No. 105-250, at 8 (1998). In *Doolin*, the successor OTS director ratified his predecessor's actions. Here, there is not even a pretense of separation between the action to be ratified and the person doing the ratification, since both the unlawful act and the allegedly cleansing ratification were performed by the same person.

Advice and consent is "more than a matter of etiquette or protocol"; it is a "structural safeguard[ ]" intended to "curb Executive abuses of the appointment power" and to "promote a judicious choice of persons for filling the offices of the union." *Edmond v. United States*, 520 U.S. 651, 659 (1997) (internal quotation marks and alterations omitted). It is a "basic constitutional protection[ ] designed in part for the benefit of litigants." *Ryder v. United States*, 515 U.S. 177, 182 (1995) (quoting *Glidden Co. v. Zdanok*, 370 U.S. 530, 536 (1962)). And it is a statutory bulwark in the CFPB's enabling legislation, one that imposes certain checks on the Bureau's newly created enforcement powers.

A. The Bureau Lacked Authority to Exercise Its Newly Enacted Powers Without a Duly Appointed Director.

The Dodd-Frank Act gave the Bureau sweeping new powers to define "unfair, deceptive, or abusive act[s] or practice[s]," (12 U.S.C. § 5511(b)(2) (Supp. 2011)), and then try to hold liable "covered person[s]" allegedly engaged in those Bureau-defined "unfair" practices. *Id.* § 5564(a). These new powers are in addition to the agency's purview over consumer laws transferred to it from other agencies. *Id.* § 5481(14).

But the Bureau's authority to "commence a civil action" is neither unlimited nor undifferentiated. When Dodd-Frank created the Bureau on July 21, 2010, it did not vest enforcement powers upon inception in the agency *qua* agency, or enable the exercise of ***any*** such powers by the Director before he or she was validly appointed. Instead, Dodd-Frank granted limited, interim authority to the Secretary of the Treasury to perform certain functions transferred from other agencies. These do ***not*** include enforcement powers unique to the Bureau, created by Dodd-Frank. *See* Memorandum from Inspectors Gen. of the Treasury Dep't and the Fed. Reserve, to Spencer Bachus, Republican Chairman of the House Fin. Serv. Comm. (Jan. 10, 2011) ("OIG Memo") at 6–7 (explaining that "[t]he Secretary is not permitted to perform certain newly established Bureau authorities if there is no confirmed Director by the designated transfer date").[2] Therefore, only a Director properly

[2] Available at http://bit.ly/29kpHci (describing the limits of the acting Director's authority). Gordon brought the OIG Memo to the district court's attention. ER 0175, 0199–0200 (ECF Nos. 139, 140). The district court, concluding that the citation to this report "falls well short of providing the Court with a reasoned and supported argument concerning the CFPB's authority to prosecute this action," held that Gordon waived the argument under the Appointments Clause. ER 0023–24 (ECF No. 180). While the majority addressed the issue, its opinion (like that of the district court) does not engage in any

appointed in accordance with 12 U.S.C. § 5491 can initiate the enforcement procedure at issue here.

The fundamental elements of the Bureau's authority are bounded by this statutory scheme, which not only transfers to the Secretary certain consumer financial protection functions heretofore vested in other agencies, but *limits* the powers the Bureau may exercise until the Director is duly appointed. Thus, "until the Director of the Bureau is confirmed by the Senate in accordance with [12 U.S.C.] § 5491," "[t]he Secretary is authorized to perform the functions of the Bureau under this part." 12 U.S.C. § 5586(a) ("Interim Authority of the Secretary"). Section 5491 establishes the Bureau, and the position of the Director, who "shall be appointed the President, by and with the advice and consent of the Senate." 12 U.S.C. § 5491(b)(2).

This "part" of the statute is subtitle F, which transfers to the Bureau "all authority to prescribe rules or issue orders or guidelines pursuant to any Federal consumer financial law" vested in (*e.g.*) HUD, the FDIC, and the Office of Thrift Supervision, 12 U.S.C. § 5581(b), and "primary enforcement authority of consumer financial laws and regulations over larger depositories." 12 U.S.C. § 5581(c)(2). The "enumerated consumer laws" over which the Bureau would exercise rulemaking authority comprise eighteen federal laws already in place prior to Dodd-Frank's enactment. These include the Truth in Lending Act ("TILA") and the Real Estate Settlement Procedures Act ("RESPA"). As stated, the Secretary—***not the Director***—is authorized to perform these functions until such time as the Director is duly appointed. 12 U.S.C. § 5586(a).

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substantive consideration of the issues raised by the Inspector General. *Gordon*, 819 F.3d at 1190–91, n.5.

The following is fairly clear from this scheme: *First*, the "Interim authority of the Secretary" under § 5586(a) "does not authorize the Secretary to exercise the full panoply of the Bureau's powers. Rather, the scope of the Secretary's powers under [§ 5586(a)] is limited to 'the functions of the Bureau under this [part F].'" David H. Carpenter, *Limitations on the Secretary of the Treasury's Authority to Exercise the Powers of the Bureau of Consumer Financial Protection*, Congressional Research Service, at 3 (May 11, 2011).

Second, the Secretary's "Interim authority" under § 5586(a) does "not expire ***until a Director is appointed***." *Id.* (emphasis in original).

Third, the powers vested in the Secretary do not include "the Bureau's 'newly established' powers – *i.e*., the enhanced consumer protection authorities that were not provided by law to federal regulators before the Dodd-Frank Act." *Id*. at 5. These "newly established" powers include those on which the Bureau based its complaint against Gordon.

In sum, this scheme of transferring authority reposed the Bureau's power in the Secretary—and only the Secretary—until the Director was appointed. Further, the Bureau's newly created powers were not reposed in the Secretary—and, therefore, could not be exercised by the Director—until he was confirmed pursuant to Dodd-Frank's constitutional appointment procedures.It is undisputed that Mr. Cordray's Recess Appointment on January 4, 2012 violated Article II. The Bureau did not have a Director until the Senate confirmed Mr. Cordray on July 16, 2013. Until then, the Bureau had no legal authority to initiate the enforcement proceedings it filed against Gordon. No one had that authority until a constitutionally valid appointment was made. Given Congress's carefully delineated allocation (and limitation) of the Bureau's power, it cannot be said (as the majority concluded) that the CFPB "had the authority to bring the action at the time Gordon was charged." *Gordon*, 819 F.3d at 1192.

B. Mr. Cordray's Ratification Could Not Authorize the Bureau's Exercise of Its Newly Created Powers Before the Time Prescribed by Congress.

The statute authorizing the creation of the CFPB is clear: the Bureau can only act through a Director "appointed by the President, by and with the advice and consent of the Senate." 12 U.S.C. § 5491(b)(1)–(2). The CFPB cannot act except through its agents, who, tasked with "conducting civil litigation in the Courts of the United States for vindicating public rights," must be duly appointed "Officers of the United States' within the language of [the Appointments Clause]." *Buckley v. Valeo*, 424 U.S. 1, 140 (1976).

The majority interprets the CFPB's enforcement actions to be valid as long as there is a duly appointed Director *eventually*. But "[t]here is no support in the Constitution … for the proposition that the cumbersomeness and delays often encountered in complying with explicit Constitutional standards may be avoided." *I.N.S. v. Chadha*, 462 U.S. 919, 958–59 (1983).

Mr. Cordray's ratification cannot cure the Bureau's unsanctioned prosecution. Even under the "less stringent" requirements for ratification relied on by the majority (*Gordon*, 819 F.3d at 1191), "whether an action taken by an agent is illegal is not treated as a question of the principal's capacity." Restatement (Third) of Agency § 4.04 cmt. b. In other words, the question of whether Mr. Cordray acted in excess of his delegated authority is separate from whether the enforcement action the Bureau undertook was lawful (and Cato believes that it was not). Ratification is not legislation. Putting aside whether Mr. Cordray's ratification could cure his own incapacity to sue in the Bureau's name, only Congress could authorize the Bureau's use of its newly created enforcement powers without first having a Senate-confirmed Director in place.

C. Mr. Cordray Cannot Ratify the Bureau's Past Conduct Because it Would Prejudice Gordon's Rights.

The law has long recognized that "[t]he intervening rights of third persons cannot be defeated by [ ] ratification." *Cook v. Tullis*, 18 Wall. 332, 338 (1874).The Supreme Court explained this principle in an analogous case, *FEC v. NRA Political Victory Fund*, 513 U.S. 88 (1994). The FEC had brought an enforcement action against a political action committee and prevailed in the district court. The Court of Appeals for the D.C. Circuit reversed. Without obtaining the statutorily mandated authorization from the Solicitor General, the FEC filed a petition for *certiorari*. *Id.* at 90. Months after the deadline to file for *certiorari* had passed, the Solicitor General attempted to ratify the FEC's unauthorized petition. *Id.* at 90–91. The Court rejected this attempted "after-the-fact" authorization, holding that the late authorization could not relate back to the FEC's original unauthorized filing so as to make it timely. *Id.* at 99. According to the Supreme Court, permitting such retroactive authorization of untimely petitions would confer on the Solicitor General unilateral power to extend statutory period deadlines indefinitely.*Id.*

The majority's holding here confers on Mr. Cordray power analogous to that rejected in *FEC*, the power to unilaterally accelerate the CFPB's permissible exercise of its newly created enforcement powers by eighteen months, in contravention of an express statutory limitation. But for this ratification, the Bureau could not have leveraged these powers against Gordon, let alone induced his alleged co-conspirators to turn "state's evidence" (albeit in exchange for a suspension of a $10 million judgment, later executed against Gordon). No fair-minded person can say to Gordon under these circumstances, "no harm, no foul."

Harm is presumed and unquestionably present. A litigant "is not required to show that he has received less favorable treatment than he would have if the agency were lawfully constituted and otherwise authorized to discharge its functions."

Comm. for Monetary Reform v. Bd. of Governors of Fed. Reserve Sys., 766 F.2d 538, 543 (D.C. Cir. 1985) (internal citation omitted); *see also Andrade v. Lauer*, 729 F.2d 1475, 1496 (D.C. Cir.1984) (noting that litigants could "rarely or never" show that "if the government had operated in accord with [the Constitution], it would not have taken adverse action against them").

One need not speculate as to whether Mr. Cordray—had he not been installed via improper recess appointment—would have withdrawn his name, in favor of a nominee potentially more palatable to those who opposed his nomination. Nor must the Court conjecture as to whether his successor would have been as aggressive in the prosecution of Gordon and his co-defendants. Instead, litigants need only demonstrate that they have been "directly subject to the authority of the agency" that engaged in unauthorized activity. *Comm. for Monetary Reform*, 766 F.2d at 543. It is beyond dispute that Gordon was subjected to that power. Whether or not the enforcement machinery of the Bureau could have kicked into gear (and Cato maintains it could not), the irreducible fact is that Gordon was subjected to the unconstitutional exercise of that enforcement power, with irrevocable consequences.

The question of whether the CFPB can wipe away "any initial Article II deficiencies" should be considered *en banc* by this Court, along with the flaws in the majority's conclusion that ratification can retroactively imbue an invalidly appointed Director with the Executive's unique Article III standing. *E.g.*, *Gordon*, 819 F.3d at 1203 ("Because Article III standing must exist at the time a complaint is filed, Richard Cordray's August 30, 2013, ratification could not retroactively cure the district court's lack of jurisdiction.") (Ikuta, J., dissenting).

CONCLUSION

Amicus Curiae Cato respectfully requests that the Court grant rehearing *en banc*.

Dated: July 7, 2016

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation of Fed. R. App. P. 29(d) because it contains 3,519 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type-style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word 2013 in 14-point Times New Roman font.

Dated: July 7, 2016

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CERTIFICATE OF SERVICE

I hereby certify that I electronically filed the forgoing with the Clerk of Court for the United States Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system on July 7, 2016. I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

Dated: July 7, 2016

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