



## Enforcement Alert from Hudson Cook; U.S. Supreme Court Hears Oral Argument on Whether CFPB's Funding Mechanism Is Constitutional

October 4th, 2023 | and [Erik Kosa](#)

On October 3, 2023, the U.S. Supreme Court heard oral argument in *Consumer Financial Protection Bureau v. Community Financial Services Association of America*. At issue is the constitutionality of the CFPB's funding structure, the separation of powers amongst the three branches of government, and the power of administrative agencies to issue regulations affecting broad swaths of the nation's economy. The outcome of the case will turn on the justices' interpretation of Article I, Section 9 of the Constitution, known as the appropriations clause, which provides: "No money shall be drawn from the Treasury, but in Consequence of Appropriations made by Law."

Created by the Dodd-Frank Act, the CFPB has the power to issue rules barring unfair, deceptive, or abusive acts and practices in the consumer financial services industry. The Bureau has an unusual funding structure in that its money comes not from the annual appropriations process in Congress but from the Federal Reserve, which is itself funded outside the congressional appropriations process by the private sector. While the amount of funding the CFPB may receive from the Federal Reserve is capped, it is not set each year by Congress.

### Background

In 2017, the Bureau issued the Payday Lending Rule which, among other things, attempted to reduce insufficient funds fees levied on borrowers by barring covered lenders from trying to withdraw payments from borrower bank accounts after the first two efforts failed. In 2018, two industry groups challenged the CFPB's rule in federal court, arguing that it violated procedural standards set by statute governing how agency rules are made as well as the Constitution's appropriations clause.

A federal district court upheld the rule on both theories, but the U.S. Court of Appeals for the Fifth Circuit disagreed. While the Fifth Circuit found the rule complied with the statutory rules governing how regulations may be promulgated, it held that the Bureau's funding structure is unconstitutional. Importantly, the Fifth Circuit reasoned that because the CFPB could not have issued the Payday Lending Rule without its unconstitutional funding structure, the rule must be struck down. The CFPB appealed to the Supreme Court.

### Legal Theories

There are two competing theories for how the appropriations clause should be read here. The

government's view is that the appropriations clause simply means that no money can be paid out of the Treasury unless it has been appropriated by an act of Congress. The Dodd-Frank legislation is an act of Congress, it authorizes the CFPB to receive funds up to a certain cap, and therefore there is no appropriations clause issue. The industry's view is that a specific "appropriation" is required to authorize any spending. That is, a law that only provides an agency with a funding source and spending authority, but which does not set an amount or duration, unconstitutionally cedes the legislature's fiscal powers to the executive branch.

### Oral Argument

During oral argument, the justices initially focused on Congress's historical actions in structuring executive agency funding outside of the annual appropriations process. The government pointed to early examples of this—the Customs Service established in 1789 with uncapped funding collected from money obtained through its law enforcement duties—as well as numerous modern financial regulators whose funding stands outside the annual process. CFSA's counsel distinguished the Bureau from these examples by noting that it is double insulated because it receives its funding from yet another agency which is itself not subject to annual appropriations: the Federal Reserve.

Much of the argument revolved around practical separation of powers considerations. The justices probed the parties about the upper limit of congressional authority to delegate appropriations functions to the executive branch. The government's position was that so long as Congress specifies the *purpose* to which the money should be put, *i.e.*, that the law somehow articulate that the spending be tied to the agency's duties, and does not attempt to bind future Congresses' hands, the law would be constitutional. CFSA argued that legislation must specify not only the purpose, but also the duration and amount of an agency's funding, emphasizing that the first judgment about how much to spend in a given year cannot be delegated by Congress to an executive branch official. Several justices appeared interested in the interplay between the fact that Congress could pass a new law changing the Bureau's funding structure tomorrow if it wished, and the potential consequences of the Court stepping into the appropriations process itself by dictating what requirements appropriations bills must meet to be constitutional.

Finally, the justices only briefly examined the question of what remedy would be appropriate if the Bureau's funding mechanism is unconstitutional, *i.e.*, whether an unconstitutional funding regime can be severed from the Dodd-Frank Act and addressed in isolation, or it invalidates every Bureau action to date. The government cited the amicus brief submitted by the Mortgage Bankers Association explaining how many entities have relied on CFPB regulations, especially in the housing finance space, which have created safe harbors across a broad range of legal requirements, arguing that any remedy invalidating past Bureau actions would have dramatic practical consequences across a large part of the economy. The justices' questions did not shed light on what remedy would be likely if the Court were to find the funding mechanism unconstitutional.

Based upon the justices' questions, it appears that a majority of the Court is hesitant to strike down the CFPB's funding authority.