PUBLICATION

Consumer Financial Services Reform in Year Two of the Trump Administration

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The publicly traded banking sector increased its market value by almost 30 percent in the first year of the Trump Administration. In part, this was a product of an overall strong performance by the stock market, but it also reflects a market and industry expectation for deregulatory efforts. The Administration delivered at least modest reforms in its first year – rulemakings related to capital, the Volcker Rule, living will extensions, and capital planning and stress testing – but noticeably absent were major changes in the consumer financial services space. Looking at the rest of 2018 and into 2019, it is reasonable to believe that the Administration will make modest deregulatory reforms in the consumer space. While some of these changes may be formal rulemakings, it is more likely that the Administration will rely on agency staffing and litigation priorities to reform the consumer financial services industry, most notably in continued litigation over the constitutional status of the Consumer Financial Protection Bureau (CFPB); resetting enforcement priorities for the CFPB; less aggressive interpretations of current law; tailored regulation of community financial institutions; and a continuation of deregulatory rulemakings in the area of capital.

CFPB Constitutional Litigation

One reason that the Trump Administration may not have delivered much change on the consumer financial services front in year one was the uncertain constitutional status of the CFPB. In 2014, the CFPB issued a $109 million penalty against PHH Corp., a mortgage servicer, for violations of RESPA. PHH sued the CFPB, alleging that its single director removable only for cause structure was unconstitutional, and that it had taken an overly broad reading of RESPA in issuing the penalty.

After several years of court challenges, the U.S. Court of Appeals for the D.C. Circuit vacated the $109 million penalty but upheld the constitutionality of the CFPB's structure. Interestingly, the Trump Administration, acting through the Department of Justice, filed a brief in support of PHH's position that the CFPB was unconstitutionally structured. PHH has not yet petitioned the Supreme Court to review the D.C. Circuit's decision, and the DOJ does not have standing on its own to appeal. PHH may well decide that it has obtained the relief it wanted in this case and move on. If so, challenges to the CFPB's structure are proceeding in federal courts in California, Indiana, and Pennsylvania. Expect the DOJ to continue to support the challengers in these cases, including filing a brief in support of any petition for certiorari to the U.S. Supreme Court.

CFPB Enforcement Priorities

Whatever the outcome of the constitutional wrangling over the CFPB's structure, we should expect its enforcement priorities to change in the coming year. The CFPB was guided by Richard Cordray until last November when, after a lawsuit over who had the power to appoint an acting director, Mick Mulvaney became acting director of the agency. Because Cordray's enforcement priorities differed radically from those of the Trump Administration, the CFPB's enforcement actions actually *increased* in frequency after the inauguration of President Trump in January 2017.

Acting Director Mulvaney has set forth an aggressive agenda for shrinking the scope of the CFPB's mission and reducing its power, including returning unspent funds to the Federal Reserve, recommending that the CFPB be subject to annual Congressional appropriations, and appointing an agency inspector general. Acting

Director Mulvaney has also stated in the CFPB's semi-annual report that the agency intended to focus its efforts on increasing credit opportunities for low-credit borrowers who may not have access to bank credit. Given these statements, we would expect to see a downward trend in enforcement actions, especially those directed towards payday lenders and other non-bank lenders.

CFPB Legal Positions

Similarly, it appears that the CFPB will pursue fewer novel theories of law under its new leadership. The PHH penalty was vacated by the D.C. Circuit, in part, because Director Cordray took an aggressive position on the meaning of certain statutory phrases, a reading of RESPA's statute of limitations, and the CFPB's authority. Acting Director Mulvaney is much less likely to take such novel positions, especially those that have yet to be affirmed by a court or those that might restrict access to credit to low income persons. We would expect that lenders, both bank and non-bank, may rely on settled interpretations of consumer statutes over the next few years, or where settled interpretations may not exist, more industry-friendly interpretations.

Tailored Regulation

It is important to remember that the CFPB is not the only agency with consumer regulatory enforcement jurisdiction. Because the vast majority of banks have less than $10 billion in assets, primary enforcement jurisdiction falls to their primary federal regulator – the Federal Reserve, OCC, or FDIC.

The Dodd-Frank Act created the position of Vice Chairman for Supervision of the Federal Reserve. That position remained unfilled in the Obama Administration. Randal Quarles was appointed to the position by President Trump and assumed office in October of last year. In public comments, Vice Chairman Quarles has announced that the Federal Reserve will make bank examiner training a priority, especially as it relates to tailoring Federal Reserve guidance to banks with less than $10 billion in assets. While Vice Chairman Quarles did not specifically refer to consumer protection laws, the Federal Reserve and other bank regulatory agencies may take a lighter touch to enforcement actions than they have since the financial crisis of 2008 – handling consumer compliance through matters requiring attention in annual reports of examination or memoranda of understanding rather than formal enforcement actions.

Capital Regulation

Finally, while not traditionally thought of as consumer financial regulation, bank capital regulations and deregulatory efforts, both by bank regulators and Congress, have the potential to encourage lending to lower income and higher credit risk customers. The federal bank regulators have proposed a rule that would simplify capital definitions and standards for smaller financial institutions. Further, legislation has passed the Senate and is currently pending in the House of Representatives that would exempt certain financial institutions with less than $10 billion in assets that meet a leverage ratio to be set between eight and ten percent from Basel III risk-weighted capital standards. While such financial institutions must still meet supervisory expectations related to loan quality, changes to capital rules may allow such financial institutions to expand their lending to low- and moderate-income individuals and businesses without damaging their capital ratios.

In sum, banks and other financial institutions should still carefully monitor their compliance with consumer financial regulations, both to protect their customers and the institutions. However, given the actions of Congress and the Trump Administration, it appears that risks related to federal consumer financial services regulation may modestly decrease over the course of the next year.