

The Consumer Financial Protection Bureau: Financial Regulation for the twenty-First Century

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THE CONSUMER FINANCIAL PROTECTION BUREAU: FINANCIAL REGULATION FOR THE TWENTY-FIRST CENTURY*

Leonard J. Kennedy,† Patricia A. McCoy†† & Ethan Bernstein†††

After existing regulatory systems failed to prevent the recent financial crisis, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act, a sweeping reform designed to alleviate the crisis and prevent its recurrence. Out of this Act, the Consumer Financial Protection Bureau was born. This new agency is charged with making markets for consumer financial products and services work for Americans, a task that was previously spread out among seven different federal agencies with varying priorities. This Article describes, with a series of concrete case studies, four key principles that have guided the Bureau as it strives to fulfill Congress's mandate. First, the Bureau has taken a market-based approach that reflects its belief in the power of markets and competition to produce increasingly better outcomes for consumers and responsible providers alike. Second, recognizing that understanding a market well is essential to effective regulation, the Bureau has relied on evidence-based analysis to inform all of its activities. Third, the Bureau has complemented its empirical analysis with input from all segments of the public—including consumers, advocates, and regulated entities. To facilitate the kind of robust public participation that will make for more effective regulation, the Bureau has employed innovative technologies and strong transparency policies. Finally, the Bureau has studied and learned from historic regulatory experiences and has adopted best practices from the public and private sectors. These four principles, and others which cascade from them, define the Bureau's twenty-first century approach to promoting a well-functioning market for consumer financial services and effective consumer protection.

* While every effort has been made at accuracy, this Article should not be relied upon as a legal reference.

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INTRODUCTION: THE CHALLENGE OF BUILDING AN ENDURING
CONSUMER AGENCY

The recent financial crisis, the worst since the Great Depression, was partly the result of federal regulatory failure. The consequences were catastrophic. Congress responded by passing the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), which included the creation of a new regulatory agency charged with ensuring that "all consumers have access to markets for consumer financial products and services" that are "fair, transparent, and competitive."¹ Congress consolidated in this new agency consumer financial

¹ Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act or Dodd-Frank), 12 U.S.C. § 5511(a) (Supp. IV 2010).

protection functions that previously were spread across seven federal agencies and provided the new agency with important new authority and responsibilities for consumer financial protection.

Building this new agency—the Consumer Financial Protection Bureau (CFPB or the Bureau)—has been no small job. As described by Raj Date, the Bureau’s Deputy Director, “What we’re doing is in roughly equal measures a startup and a post-merger integration. And, we are doing both of those things at the same time [that] we are trying to undertake a pretty strategic overhaul over how this basic enterprise, protecting consumer financial services, is done.”²

The Bureau has sought to approach the historic challenge it faces deliberately—with full appreciation for the gravity and difficulty of the work before it. The Bureau strives to be an agency that will help consumer financial markets work by making rules more effective, by consistently and fairly enforcing those rules, and by enabling consumers to take more control of their economic lives. This Article explains how the CFPB has approached building an agency that will achieve these goals.

Through a series of concrete case studies describing the Bureau’s startup activity across a range of functions—from rulemaking and enforcement to consumer education and outreach—this Article shows how the CFPB has begun to give life to its statutory obligations through four core principles: (1) a market-based approach, (2) a focus on evidence-based analysis, (3) a commitment to encouraging and enabling robust public participation through transparency and innovative uses of technology, and (4) a recognition that history and other agencies’ experience can provide invaluable guidance. By following these core principles, the Bureau seeks to achieve its mandate.

Part I of this Article provides a brief background of the CFPB. It describes the crisis that inspired the creation of this new consumer agency as well as the Bureau’s legislative mandate, progress so far, and structure. Part II then elaborates on the four core principles noted above that guide the CFPB’s approach to meeting its statutory responsibilities. Finally, Part III provides four concrete examples of how the agency has employed these core principles in practice. Although these four case studies by no means show the full breadth and depth of the Bureau’s work, they do provide insight into how the Bureau has integrated the principles into its activities.

² Tim Fernholz, *What Startups Can Learn from a Bootstrapping Government Agency*, GOOD (Sept. 7, 2011, 5:30 AM), <http://www.good.is/post/what-startups-can-learn-from-a-bootstrapping-government-agency/>.

I

BORN IN CRISIS: A BRIEF HISTORY OF THE CFPB

A. The Financial Crisis

The Bureau was born out of the worst financial crisis since the Great Depression. The crisis, which pushed the financial system into great distress in September 2008 following the unraveling of Bear Stearns, the conservatorship of Fannie Mae and Freddie Mac, the bankruptcy of Lehman Brothers, and the near collapse of AIG and other firms, had devastating consequences. As a result of the crisis, home values plunged, personal savings fell, millions of people lost their jobs, and millions of consumers defaulted on their mortgages and other loans.³

The damage was not confined to those who became delinquent due to unaffordable loans. The housing market crash sparked by the crisis also harmed homeowners able to pay their mortgages whose home values fell and neighborhoods declined.⁴ Consumers struggled to obtain credit as banks tightened their lending standards. Retirees saw their retirement funds drop precipitously. Workers saw their positions eliminated as employers struggled to make ends meet.⁵ Small businesses suffered greatly as credit contracted and consumer demand fell. Providers of financial services and products saw their earnings fall and share prices plunge. The distress was widespread and severe. Many of the problems sparked by the crisis persist years later, as housing prices remain depressed in many areas and the economy continues to recover.⁶

The fact that many Americans took on loans that they did not understand and ultimately could not afford undoubtedly worsened the crisis. While some borrowers consciously assumed too much debt,

³ See generally FIN. CRISIS INQUIRY COMM'N, THE FINANCIAL CRISIS INQUIRY REPORT: FINAL REPORT OF THE NATIONAL COMMISSION ON THE CAUSES OF THE FINANCIAL AND ECONOMIC CRISIS IN THE UNITED STATES 233–410 (2011) (illustrating in detail the events that led to the financial crisis).

⁴ For an overview of the housing downturn, see JOINT CTR. FOR HOUS. STUDIES OF HARVARD UNIV., THE STATE OF THE NATION'S HOUSING 2011 (2011), available at <http://www.jchs.harvard.edu/research/publications/state-nation's-housing-2011>.

⁵ For a summary of job loss, see News Release, Bureau of Labor Statistics, U.S. Dep't of Labor, Worker Displacement: 2007-2009 (Aug. 26, 2010), available at <http://www.bls.gov/news.release/disp.nr0.htm>.

⁶ See *Economic Outlook and Recent Monetary Policy Actions: Hearing Before the Joint Econ. Comm.*, 112th Cong. 1–2 (Oct. 4, 2011) (statement of Ben S. Bernanke, Chairman, Bd. of Governors of the Fed. Reserve System) [hereinafter *Economic Outlook*], available at <http://www.federalreserve.gov/newsevents/testimony/bernanke20111004a.pdf>.

many others were misled by confusing loans.⁷ The regulatory system prior to Dodd-Frank failed to protect consumers from such abuses.

This failure was not surprising. During the period leading up to the crisis, federal oversight of consumer finance was a patchwork spread out among seven different agencies.⁸ None of these agencies had the jurisdiction and tools necessary to ensure that consumer financial markets functioned well, and important sectors of these markets operated without any meaningful federal oversight.⁹ Moreover, consumer financial protection was not a central task for any of the federal banking agencies, whose principal mission was ensuring the safety and soundness of financial institutions.¹⁰ The fragmentation in regulatory structure made policy coordination difficult.¹¹

This regulatory apparatus was simply not up to the task of responding to new products offered in the midst of the dramatic growth in lending. Some lenders took advantage by issuing increasingly complex credit products that entailed significant hidden costs and risks for consumers.¹² Many consumers struggled to make sense of these ever more complicated products.¹³ Ultimately, the ineffective regulatory system failed to protect the market for consumer financial services and the stability of the U.S. economy. Neither the extent nor the ramifications of this problem were exposed fully until the financial crisis.

B. Creation of the Bureau

In June 2009, President Obama proposed to address these failures by consolidating consumer financial protection responsibility in one agency.¹⁴ Just over one year later, with the passage of the Dodd-

⁷ See generally KATHLEEN C. ENGEL & PATRICIA A. MCCOY, *THE SUBPRIME VIRUS: RECKLESS CREDIT, REGULATORY FAILURE, AND NEXT STEPS* (2011) (providing a detailed account of the issues underlying the subprime mortgage crisis).

⁸ See Designated Transfer Date, 75 Fed. Reg. 57,252, 57,252 (Sept. 20, 2010).

⁹ See Oren Bar-Gill & Elizabeth Warren, *Making Credit Safer*, 157 U. PA. L. REV. 1, 95–97 (2008).

¹⁰ See *id.* at 86–87.

¹¹ Private sector firms similarly face high costs when coordinating among fragmented entities. For this reason, private sector firms integrate functions internally rather than purchasing them on the open market. Private firms may integrate functions when the “transaction cost” created by contracting for such functions on the market becomes too great. For the seminal description of transaction cost economics, see R.H. Coase, *The Nature of the Firm*, 4 *ECONOMICA* 386 (1937). The situation is admittedly somewhat different in the case of government agencies, but the transaction costs of interagency coordination can similarly justify integrating authority within one agency.

¹² For an overview of the survey evidence, see Bar-Gill & Warren, *supra* note 9, at 26–58.

¹³ *Id.* at 11–20.

¹⁴ See U.S. DEP’T OF THE TREASURY, *FINANCIAL REGULATORY REFORM: A NEW FOUNDATION; REBUILDING FINANCIAL SUPERVISION AND REGULATION* 55–62 (2009), available at http://www.treasury.gov/initiatives/Documents/FinalReport_web.pdf (proposing the creation

Frank Act, Congress created the CFPB as an independent agency within the Federal Reserve System to regulate consumer financial products and services. The Bureau assumed responsibilities and authorities from seven other federal agencies on July 21, 2011,¹⁵ and President Obama appointed Richard Cordray as its first Director in January 2012.¹⁶

The Dodd-Frank Act tasks the CFPB with helping consumers obtain the information needed to make informed and responsible financial decisions, protecting consumers from harmful practices and discrimination, eliminating outdated and unnecessary regulations, consistently and evenhandedly enforcing federal consumer financial law to promote fair competition, and increasing market transparency.¹⁷ Congress gave the CFPB six basic tools to achieve these goals: examination and supervision, enforcement, rulemaking, consumer education, collecting and responding to consumer complaints, and researching and monitoring consumer financial markets.¹⁸

In giving the Bureau this broad mandate, Congress gave the Bureau many important authorities and transferred functions relating to consumer financial protection from other agencies to the Bureau.¹⁹ For instance, Congress gave the Bureau authority to take action against unfair, deceptive, and abusive acts and practices in the consumer financial marketplace, including through rulemaking.²⁰ Con-

of a new Consumer Financial Protection Agency); President Barack Obama, Remarks by the President on the Economy at Georgetown University (Apr. 14, 2009), *available at* <http://www.whitehouse.gov/the-press-office/remarks-president-economy-georgetown-university> (announcing financial reform as a “new foundation for growth and prosperity”). This idea was derived from Oren Bar-Gill and Elizabeth Warren’s recommendation for a new federal agency to protect consumers in the financial marketplace. *See* Bar-Gill & Warren, *supra* note 9, at 1–2 (making “a case, supported by both theory and data, for comprehensive safety regulation of consumer credit”).

¹⁵ Designated Transfer Date, 75 Fed. Reg. 57,252, 57,252–53 (Sept. 20, 2010) (setting July 21, 2011 as the date on which “certain authorities will transfer from other agencies to the CFPB, and the CFPB will be able to exercise certain additional, new authorities under the [Consumer Financial Protection] Act and other laws”).

¹⁶ Press Release, The White House, Office of the Press Sec’y, President Obama Announces Recess Appointments to Key Administration Posts (Jan. 4, 2012), *available at* <http://www.whitehouse.gov/the-press-office/2012/01/04/president-obama-announces-recess-appointments-key-administration-posts>.

¹⁷ 12 U.S.C. § 5511(a)–(b) (Supp. IV 2010).

¹⁸ *Id.* § 5511(c).

¹⁹ Pursuant to section 1062 of the Dodd-Frank Act, the Treasury Secretary designated that these functions would transfer to the Bureau on July 21, 2011. *See* Pub. L. No. 111-203, § 1062(c)(1), 124 Stat. 1376, 2040 (codified at 12 U.S.C. § 5582(c)(1)); Designated Transfer Date, 75 Fed. Reg. 57,252–53. The Bureau colloquially refers to this as its “launch date,” even though it was vested with and exercised certain other authorities before that date. *See, e.g., Learn About the Bureau*, CONSUMER FIN. PROT. BUREAU, <http://www.consumerfinance.gov/the-bureau/> (last visited Apr. 7, 2012) (listing the Bureau’s accomplishments as of July 21, 2011).

²⁰ 12 U.S.C. § 5531.

gress also assigned the Bureau the responsibility of supervising certain nonbank firms offering consumer financial products and services,²¹ an important market segment that had previously not been subject to federal supervision. In particular, Congress gave the Bureau the authority to conduct examinations of and require reports from nonbank entities including mortgage originators, brokers, and servicers; private student lenders; payday lenders; “larger participant[s]” in markets for other consumer financial products and services; and other covered entities determined to pose risk to consumers.²² This supervisory authority will enable the Bureau to work with nonbank entities to correct violations and provide redress where appropriate. When necessary, the Bureau may also take legal action to enforce “[f]ederal consumer financial law,”²³ including against nonbank entities. The Dodd-Frank Act also makes the Bureau’s Director a member of the Federal Deposit Insurance Corporation’s Board of Directors,²⁴ the Federal Financial Institutions Examination Council,²⁵ and the Financial Stability Oversight Council.²⁶ By giving the Bureau a seat at these tables, Congress recognized that a consumer-oriented perspective can help preserve the safety and soundness of financial institutions and of the financial system as a whole and that safety and soundness measures can have implications for consumers.

At the same time, Congress also transferred the responsibility for protecting consumers in the financial marketplace from other regulators to the Bureau. Notably, Congress gave the Bureau the authority to supervise certain depository institutions that other regulators historically had supervised for compliance with federal consumer financial law.²⁷ In particular, the Bureau is tasked with supervising banks, thrifts, and credit unions with total assets of over \$10 billion, as well as their affiliates, for compliance with federal consumer financial laws.²⁸ Currently, these large institutions total approximately one hundred. The Bureau will coordinate this supervision with other federal and state bank regulators, who have supervisory authority over these entities, for safety and soundness, among other things.

Congress also transferred to the Bureau the authority to promulgate rules regarding federal consumer financial laws and to enforce

²¹ *Id.* § 5514.

²² *Id.* § 5514(a)(1).

²³ *Id.* §§ 5561–5565. “Federal consumer financial law” is defined in § 5481(14).

²⁴ *Id.* § 1812(a)(1)(B).

²⁵ *Id.* § 3303(a)(4).

²⁶ *Id.* § 5321(b)(1)(D).

²⁷ This includes most, but not all, consumer financial protection laws. *See Id.* § 5481(14).

²⁸ *Id.* § 5515(a)(1).

those laws and regulations against certain entities.²⁹ In particular, the Bureau is now charged with implementing and enforcing the following laws, among others:

- The Truth in Lending Act (TILA),³⁰ which requires that lenders provide clear disclosures to consumers about the costs of a mortgage, credit card, payday loan, or other consumer credit. For example, TILA requires that credit card issuers disclose annual percentage rates (APRs) to allow consumers to compare product choices. In addition, the CARD Act of 2009³¹ amended TILA to prohibit certain credit card practices, improve disclosures, and create other important consumer protections. Congress also gave the Bureau jurisdiction over other laws that amended TILA: the Consumer Leasing Act,³² which covers leases; the Home Ownership and Equity Protection Act,³³ which covers high-cost mortgages; and the Fair Credit Billing Act,³⁴ which provides certain protections regarding billing errors, grace periods, and other matters.
- The Fair Credit Reporting Act (FCRA),³⁵ which governs the behavior of consumer reporting agencies and establishes requirements for entities that use credit reports or furnish information to credit bureaus. FCRA also entitles consumers to obtain a free copy of their credit report once a year from each of the three nationwide credit bureaus.
- The Real Estate Settlement Procedures Act (RESPA),³⁶ which regulates settlement services provided in connection with residential real estate transactions and requires certain disclosures in mortgage transactions.
- The Equal Credit Opportunity Act (ECOA),³⁷ which prohibits discrimination in lending on the basis of race, color, religion, national origin, sex, marital status, or age, or because a person receives public assistance or has exercised a right under certain consumer protection laws.

²⁹ *Id.* §§ 5515, 5564, 5581.

³⁰ Pub. L. No. 90-321, 82 Stat. 146 (1968) (codified as amended at 15 U.S.C. §§ 1601-1667e) (2006)).

³¹ Pub. L. No. 111-24, 123 Stat. 1734 (2009) (codified in scattered sections of 15 and 16 U.S.C.). For more information on the CARD Act, see *infra* note 80.

³² 15 U.S.C. §§ 1667-1667e (2006).

³³ *Id.* § 1639 (2006).

³⁴ *Id.* §§ 1666-1666j (2006).

³⁵ *Id.* §§ 1681-81x (2006) (except with respect to 15 U.S.C. §§ 1681m(e), 1681(w), which discuss identity theft and the disposal of records, respectively).

³⁶ 12 U.S.C. §§ 1831b, 2601-2610, 2614 -2617 (2006).

³⁷ 15 U.S.C. §§ 1691-1691f (2006).

- The Home Mortgage Disclosure Act (HMDA),³⁸ which requires most lenders to disclose certain data about their mortgage lending, in part so that the public can determine whether lenders are serving the needs of their local communities. This data can also be used to identify potentially discriminatory lending practices.
- The Electronic Fund Transfer Act (EFTA),³⁹ which provides a framework to protect consumers engaging in electronic money transfers.
- The Fair Debt Collection Practices Act (FDCPA),⁴⁰ which protects consumers against harassment and other unfair or deceptive practices by debt collectors.
- The Truth in Savings Act (TISA),⁴¹ which requires uniform disclosures of various rates and fees for deposit accounts.
- The privacy provisions of the Gramm-Leach-Bliley Act,⁴² which require financial institutions to provide consumers with privacy notices, including notice of the right to direct the institution not to disclose the consumer's nonpublic personal information to unaffiliated third parties in certain circumstances.
- The SAFE Mortgage Licensing Act,⁴³ which provides for registration and some licensing of mortgage loan originators—meaning brokers and mortgage loan officers—and establishes minimum standards for state registration and licensing of specified originators.
- A provision of the Omnibus Appropriations Act of 2009⁴⁴ that authorizes prohibition of unfair or deceptive acts or practices related to mortgage lending.

In addition, the Bureau is empowered to enforce a number of rules issued by the Federal Trade Commission, including rules regarding telemarketing sales and cooling-off periods for sales made at homes.⁴⁵

³⁸ 12 U.S.C. §§ 2801–2810 (2006).

³⁹ 15 U.S.C. §§ 1693–1693r (2006). The Bureau did not assume authority over section 920 of the Act, 15 U.S.C. § 1693r. *See* 12 U.S.C. § 5481(12)(C).

⁴⁰ 15 U.S.C. §§ 1692–1692p (2006).

⁴¹ 12 U.S.C. §§ 4301–4313 (2006).

⁴² 15 U.S.C. §§ 6802–6809 (2006). The Bureau did not assume authority over § 6805 as it applies to § 6801(b). *See* 12 U.S.C. § 5481(12)(J).

⁴³ 12 U.S.C. §§ 5101–5116 (2006).

⁴⁴ Omnibus Appropriations Act, Pub. L. No. 111-8, § 626, 123 Stat. 524 (2009) (codified as amended in scattered sections of 2, 5, 7, 12, 16, 20, 30, 33, 42, 43, 48 and 50 U.S.C.).

⁴⁵ *See* 12 U.S.C. § 5581(b)(5). The Bureau is authorized to enforce FTC rules including, among other things: Telemarketing Sales Rule, 16 C.F.R. pt. 310 (2011); Use of Pre-notification Negative Option Plans, 16 C.F.R. pt. 425 (2011); Rule Concerning Cooling-Off Period for Sales Made at Homes or at Certain Other Locations, 16 C.F.R. pt. 429 (2011);

C. The Challenge Ahead

The Bureau is focused on using the various tools that Congress gave it to turn the Dodd-Frank Act's vision into reality. In the first eighteen months since the Act's passage, the Bureau designed and built an organization that expanded from a few employees to more than 750 employees by the end of 2011.⁴⁶ The Bureau has attracted highly qualified economists, lawyers, and experts from private industry, government, academia, and nonprofit organizations, and has integrated this talent into cross-disciplinary teams. The Bureau has published empirical studies; issued regulations, including ones on remittances and the Bureau's enforcement procedures; designed a nationwide supervision program; consulted with many stakeholders; and begun accepting credit card- and mortgage-related consumer complaints.⁴⁷

Yet substantial challenges remain. Much of the damage that the 2008 financial crisis inflicted has not yet been repaired. Home prices remain depressed in many areas.⁴⁸ Consumers struggle to access needed credit.⁴⁹ Some lenders remain burdened with troubled assets and potentially significant liabilities.⁵⁰ Problematic lending practices persist, including credit agreements that are difficult to understand and compare.

Preservation of Consumers' Claims and Defenses, 16 C.F.R. pt. 433 (2011); Credit Practices, 16 C.F.R. pt. 444 (2011); Mail or Telephone Order Merchandise, 16 C.F.R. pt. 435 (2011); Disclosure Requirements and Prohibitions Concerning Franchising, 16 C.F.R. pt. 436 (2011); and Disclosure Requirements and Prohibitions Concerning Business Opportunities, 16 C.F.R. pt. 437 (2011).

⁴⁶ See *BD. OF GOVERNORS OF THE FED. RESERVE SYS. & BUREAU OF CONSUMER FIN. PROT. OFFICE OF INSPECTOR GEN. & U.S. DEP'T OF THE TREASURY OFFICE OF INSPECTOR GEN., REVIEW OF CFPB IMPLEMENTATION PLANNING ACTIVITIES 5* (2011) [hereinafter *OFFICES OF INSPECTOR GENERAL*]; *CONSUMER FIN. PROT. BUREAU, SEMI-ANNUAL REPORT OF THE CONSUMER FINANCIAL PROTECTION BUREAU: JULY 21–DECEMBER 31, 2011*, at 6 (2012) [hereinafter *CFPB, SEMI-ANNUAL REPORT*].

⁴⁷ See generally *CONSUMER FIN. PROT. BUREAU, BUILDING THE CFPB: A PROGRESS REPORT* (2011) [hereinafter *CFPB, BUILDING THE CFPB*] (reporting on the employees, projects, and methods employed by the CFPB); *CFPB, SEMI-ANNUAL REPORT*, *supra* note 46 (same). For an evaluation of the Bureau's early activities, see *OFFICES OF INSPECTOR GENERAL*, *supra* note 46, at 2, 6–7 (reporting that the CFPB has (1) "identified and documented implementation activities critical to standing up the agency's functions and necessary to address certain Dodd-Frank Act requirements," (2) "developed and is implementing appropriate plans that support ongoing operations as well as the transfer of employees and functions," and (3) "has completed elements of its implementation plans and is making progress on others, including its overall strategic plan").

⁴⁸ See *Economic Outlook*, *supra* note 6, at 3–4; *BD. OF GOVERNORS OF THE FED. RESERVE SYS., THE U.S. HOUSING MARKET: CURRENT CONDITIONS AND POLICY CONSIDERATIONS 1* (2012).

⁴⁹ See *INT'L MONETARY FUND, GLOBAL FINANCIAL STABILITY REPORT: GRAPPLING WITH CRISIS LEGACIES 29* (2011), available at <http://www.imf.org/external/pubs/ft/gfsr/2011/02/pdf/text.pdf>.

⁵⁰ See *KATALINA BIANCO, A RETROSPECTIVE OF THE TROUBLED ASSET RELIEF PROGRAM* (2011), available at http://www.cch.com/press/news/WhitePaper_TARP.pdf.

Through the Dodd-Frank Act, Congress assigned multiple agencies the responsibility of alleviating these problems and preventing their recurrence.⁵¹ The Bureau has a very important role to play within this broader framework. The Bureau must not only achieve the goals that Congress set for it but do so in a thoughtful and targeted manner.

The United States has faced and successfully addressed similar challenges in the past. To take just a few examples, in 1887, Congress created the Interstate Commerce Commission, an independent agency, to curb the railroads from abusing their market power—and the agency had much success in doing so.⁵² Another independent agency, the Federal Communications Commission (FCC), was created in large part to correct market failures that prevented efficient utilization of the radio frequency spectrum in the growing and increasingly complex radio business.⁵³ Since the 1930s, the FCC has evolved to respond to changes prompted by massive technological innovations in television, satellites, computers, mobile phones, and other technologies. In the wake of the Great Depression and the related stock market crash, Congress created the Securities and Exchange Commission (SEC).⁵⁴ The SEC was charged with ensuring adequate disclosures of material information to buyers and sellers of securities.⁵⁵ The Commission had to develop expertise and to evolve with changes in the financial markets, and investors were safer as a result.⁵⁶

Past financial crises have also led to the creation of successful, independent banking agencies. In response to the bank panics during the Depression, Congress created the Federal Deposit Insurance

⁵¹ See, e.g., Dodd-Frank Act, Pub. L. No. 111-203, §§ 111–112 (codified at 12 U.S.C. § 5321–5322 (Supp. IV 2010)) (establishing the Financial Stability Oversight Council, an entity comprised of representatives from several federal agencies that “will respond to emerging threats to the stability of the United States financial system”); *id.* §§ 941–946 (generally requiring the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Securities and Exchange Commission, the Secretary of Housing and Urban Development, and the Federal Housing Finance Agency jointly to prescribe regulations requiring credit risk retention by securitizers in connection with asset-backed securities involving certain residential mortgage assets and exempting “qualified residential mortgages” as defined by those agencies).

⁵² See Interstate Commerce Act of 1887, Pub. L. No. 49-41, ch. 104, 24 Stat. 379. For a survey of the empirical evidence of the Act’s effects, see generally Thomas W. Gilligan et al., *Regulation and the Theory of Legislative Choice: The Interstate Commerce Act of 1887*, 32 J.L. & ECON. 35 (1989).

⁵³ See Communications Act of 1934, Pub. L. No. 73-416, ch. 652, 48 Stat. 1064 (codified as amended in scattered sections of 47 U.S.C.).

⁵⁴ See Securities Exchange Act of 1934, Pub. L. No. 73-291, ch. 404, 48 Stat. 881 (codified as amended at 15 U.S.C. §§ 78a–78pp).

⁵⁵ See *id.* § 6.

⁵⁶ For a description of the SEC’s evolution, see ANNE M. KHADEMIAN, *THE SEC AND CAPITAL MARKET REGULATION: THE POLITICS OF EXPERTISE* 41 (1992).

Corporation (FDIC), an independent agency tasked with maintaining stability and public confidence in the nation's banking system.⁵⁷ Before the FDIC's creation, the banking system suffered numerous panics and bank runs.⁵⁸ Using its independence and expertise, the FDIC has made substantial changes in the banking system since the 1930s that have increased the confidence of bank depositors. It gave customers of FDIC-insured banks the assurance that their deposits were insured, up to specified limits, by the full faith and credit of the United States, largely preventing bank runs. No customer has ever lost insured funds, and the widespread bank runs of the Great Depression have never recurred.⁵⁹ It is noteworthy that Congress chose to put the bank insurance and resolution functions in a new institution that would largely be devoted to this important task.

Congress acted in this same tradition in the wake of the 2008 financial crisis by creating the CFPB. The Bureau must be an expert, durable, and flexible institution that will adapt over time to address substantial challenges. Part II describes the principles that have guided the Bureau to date as it strives to fulfill this mission.

II

THE CFPB'S APPROACH: MARKET-BASED, EVIDENCE-BASED, OPEN TO PUBLIC INPUT, AND GUIDED BY HISTORY AND OTHER AGENCIES' EXPERIENCE

As the first twenty-first-century consumer protection agency, the CFPB has employed innovative approaches to fulfilling the goals set by Congress. Consistent with its statutory mandate to make markets in financial products and services work better for consumers, the Bureau has maintained its overriding belief in the power of competitive markets. To craft the most effective regulations, the Bureau will strive to make extensive use of empirical evidence and public input. In particular, the Bureau has hired teams of expert researchers to study particular consumer financial markets and household finances generally and has increased opportunities for diverse populations to provide meaningful input by using new technologies and implementing robust transparency policies. Finally, the Bureau has drawn on, and will continue to draw on, other agencies' experiences and best practices in creating processes that will enable it to remain true to these values and to fulfill its mission.

⁵⁷ See Banking Act of 1933, Pub. L. No. 73-66, ch. 89, 48 Stat. 162.

⁵⁸ For an overview of the instability in the banking system prior to creation of the FDIC, see generally ELMUS WICKER, *BANKING PANICS OF THE GILDED AGE* (2000).

⁵⁹ See FED. DEPOSIT INS. CORP., *THE FIRST FIFTY YEARS: A HISTORY OF THE FDIC 1933-1983*, at 4, available at <http://www.fdic.gov/bank/analytical/firstfifty/chapter1.pdf>.

A. A Market-Based Approach

Four decades ago, Professor Alfred E. Kahn remarked that competition was far better than regulation at bringing about “*positively good*” economic performance.⁶⁰ While governmental regulation generally counteracts bad outcomes after the fact, competition can bring about performance that is “efficient, progressive, risk-taking, [and] innovative.”⁶¹ Thus, Kahn argued, regulators should focus on fostering institutions that would exert market-like influence on regulated entities.⁶² These ideas caught the attention of conservatives and liberals alike, prompting deregulation of major sectors of the economy including railroads, trucking, and airlines.⁶³

Like Kahn, the Bureau believes in the power of competition and markets to produce “positively good” outcomes. The experience of the past several years has proven, however, that the credit market is particularly susceptible to market failures, which can produce highly destructive economic and financial results.⁶⁴ These failures restrict the advantages that the market and competitive forces can offer.⁶⁵

Congress assigned the Bureau the important task of addressing these market failures. In particular, Congress directed the Bureau to exercise its authorities to ensure, among other things, that “markets for consumer financial products and services operate transparently and efficiently to facilitate access and innovation.”⁶⁶ Consistent with this core purpose, the Bureau will work to ensure that the markets for consumer financial products and services work properly and have the opportunity to yield “positively good” economic performance.

First, to work properly, the markets in consumer financial products and services must be transparent. But some of these markets have been far from transparent. Many consumers have unwittingly taken on loans with hidden fees, unexpected interest-rate hikes, and other unknown and unaffordable costs or obligations. A core goal of the Bureau will be to improve consumers’ ability to understand the

⁶⁰ 1 ALFRED E. KAHN, *THE ECONOMICS OF REGULATION: PRINCIPLES AND INSTITUTIONS* 18 (1970).

⁶¹ *Id.*

⁶² *See id.*

⁶³ *See* Staggers Rail Act of 1980, Pub. L. No. 96-448, 94 Stat. 1895; Motor Carrier Act of 1980, Pub. L. No. 96-296, 94 Stat. 793; Airline Deregulation Act of 1978, Pub. L. No. 95-504, 92 Stat. 1705; Railroad Revitalization and Regulatory Reform Act of 1976, Pub. L. No. 94-210, 90 Stat. 31.

⁶⁴ For a discussion of why markets in consumer financial products have failed, see generally Bar-Gill & Warren, *supra* note 9, at 10–25.

⁶⁵ In his recent book, Judge Posner concludes that the actions of unregulated actors led to the current crisis and that U.S. financial markets need to be more heavily regulated. *See generally* RICHARD A. POSNER, *A FAILURE OF CAPITALISM: THE CRISIS OF '08 AND THE DESCENT INTO DEPRESSION* (2009).

⁶⁶ 12 U.S.C. § 5511(b)(5) (Supp. IV 2010).

costs and risks of products and to compare products before making their choices.⁶⁷ Bureau initiatives to improve disclosure requirements will play an important role in achieving this goal, as will consumer education and financial literacy programs.

Second, and equally important, competition in the markets should take place on a level playing field. In the past, different levels of federal oversight have applied to different types of firms, even when those firms offered nearly identical consumer financial services or products. The Bureau will work to ensure more consistent oversight across different types of financial service providers, including independent nonbank companies that historically have not been subject to federal supervision.⁶⁸ With the consistent application of consumer protection rules, providers will be able to compete fairly on the basis of price, quality, and service. In this way, the Bureau's activities can benefit not only consumers but also the responsible firms that play by the rules—and our economy as a whole.

Finally, incentives in the market for consumer financial services must be better aligned with positive outcomes.⁶⁹ With the exotic financial securities that proliferated in the years before the financial crisis, loan originators could more easily pass off high-risk loans and thus had fewer effective incentives to make loans only to borrowers capable of repaying them.⁷⁰ The Dodd-Frank Act addresses these incentive problems in a number of provisions, including some that the CFPB is not responsible for implementing, such as those requiring sponsors of asset-backed securities generally to retain a percentage of the credit risk.⁷¹ But the Act also gives the Bureau an important role in realigning incentives in the market. For instance, it will issue regulations to implement new statutory provisions imposing a duty on lenders to determine whether consumers have a reasonable ability to repay mortgages.⁷² Implementing these provisions is a key step in

⁶⁷ See CFPB, BUILDING THE CFPB, *supra* note 47, at 9–14.

⁶⁸ See 12 U.S.C. § 5514.

⁶⁹ For a more in-depth discussion of the Bureau's role in increasing transparency and fairness and realigning incentives, see Raj Date, Special Advisor to the Sec'y of the Treasury for the Consumer Fin. Prot. Bureau, Remarks at the *American Banker's Regulatory Symposium* (Sept. 20, 2011), available at <http://www.consumerfinance.gov/speech/remarks-by-raj-date-at-american-bankers-regulatory-symposium/>.

⁷⁰ See *id.*

⁷¹ See 15 U.S.C. § 780-11 (Supp. IV 2010).

⁷² Pursuant to the Dodd-Frank Act, the Board of Governors of the Federal Reserve System issued a proposed rule on ability-to-repay requirements in May 2011. Regulation Z; Truth in Lending, 76 Fed. Reg. 27,390 (May 11, 2011) (to be codified at 12 C.F.R. pt. 226); see also Dodd-Frank Act, 15 U.S.C. § 1639c(a)(1) (“[N]o creditor may make a residential mortgage loan unless the creditor makes a reasonable and good faith determination . . . [that] the consumer has a reasonable ability to repay the loan . . .”). The authority to finalize this proposed rule transferred to the Bureau on July 21, 2011. See 12 U.S.C. § 5581 (Supp. IV 2010).

preventing recurrence of the market failures that led to the 2008 financial crisis.

By promoting transparency, making competition fair, and counteracting misaligned incentives, the Bureau will help to create well-functioning markets that promise to produce “positively good” market outcomes that benefit both consumers and financial service providers.

B. A Focus on Evidence-Based Analysis

The Bureau’s belief in markets is accompanied by a recognition that it must understand a market well to be able to regulate it effectively. This recognition drives an overarching focus on empirical data throughout the Bureau’s work. The CFPB’s commitment to being a fact-based, pragmatic, and deliberative agency will help it to understand the complicated consumer financial markets for which it has responsibility and, in turn, to promulgate better, smarter, and more effective regulations.

The CFPB’s very structure is designed to make research and market analytics central to its work. The Bureau’s Division of Research, Markets, and Regulations, one of the Bureau’s six major divisions, houses not only the attorneys responsible for managing and executing the Bureau’s authority to prescribe rules but also a research team and several markets teams. Each team is staffed with a combination of professionals from different backgrounds and has the capacity to collect and analyze data necessary to inform the Bureau’s work.

Headed by leading economist Sendhil Mullainathan,⁷³ the economists, social scientists, and data analysts in the Bureau’s Office of Research are dedicated to independent, foundational, and applied research on a variety of consumer financial topics, including individual and household decision making, firm behavior, optimal regulation, and the effectiveness of disclosures. The Office will seek out the best available data for use in research and policy evaluation from existing commercial and government sources and ultimately may develop original datasets through surveys, consumer testing, and collaboration with industry and consumer advocates. The researchers in the Office will also have the opportunity to conduct self-directed research and to publish in their own names where permitted by law, without Bureau approval of the policy content. This will promote

⁷³ See Press Release, Consumer Fin. Prot. Bureau, Treasury Department Announces Senior Leadership Hires for the Consumer Financial Protection Bureau (May 11, 2011), available at <http://www.consumerfinance.gov/pressrelease/treasury-department-announces-senior-leadership-hires-for-the-consumer-financial-protection-bureau/>. Sendhil Mullainathan is a Professor of Economics at Harvard University and recipient of the MacArthur Foundation “genius award.” *Id.*

honest investigation, independent thinking, and open discussion that will support evidence-based—rather than myopic or ideological—policymaking.

While the Office develops and analyzes data on consumer financial markets and household finances, highly seasoned experts on the markets teams monitor the U.S. consumer financial markets for emerging risks and provide empirically based policy analysis in distinct consumer financial markets, including: credit cards and other card-based products; residential mortgages; installment and liquidity lending (e.g., student lending and payday loans); and deposits, debt collection, and credit reporting.

Housing the Research, Markets, and Regulations teams together in one division helps to ensure that the insights of expert researchers, economists, and market practitioners are all reflected in the Bureau's policymaking and rulemaking processes. The research and markets teams are setting the empirical groundwork for developing the Bureau's policy and regulatory priorities and potential rules, helping to measure the effectiveness of existing regulations, and providing ongoing analytical support and market intelligence for active rulemaking. For example, on a day-to-day basis, staff from the research and markets teams, as well as from the Bureau's other divisions, actively participate in meetings with regulatory attorneys to discuss market-related issues and other analyses germane to implementing the federal consumer financial laws. Their participation from inception to completion of the rulemaking process ensures that regulatory decisions are made on the basis of sound market analysis and understanding and, in turn, creates a path for more effective regulations.

Already, the Bureau has published several empirical studies that highlight its commitment to evidence-based regulation. In July 2011, for example, the Bureau released a report that describes the credit-scoring industry, relevant market participants, and the complexity of the credit-scoring process.⁷⁴ This report examines how credit scores are obtained and used as well as how differences between scores provided to creditors and scores provided to consumers could potentially harm consumers. Building on this initial research, the CFPB is now undertaking a substantial data collection and analysis project that will explore the nature, range, and size of variations between the credit scores used by creditors and those sold to consumers in order to shed more light on whether, and the extent to which, these variations are

⁷⁴ See Consumer Fin. Prot. Bureau, *THE IMPACT OF DIFFERENCES BETWEEN CONSUMER- AND CREDITOR-PURCHASED CREDIT SCORES: REPORT TO CONGRESS* (2011), available at http://www.consumerfinance.gov/wp-content/uploads/2011/07/Report_20110719_Credit_Scores.pdf.

harming consumers. This project will provide valuable insight for the development of Bureau policy and potential activity in this area.

The Bureau also published a report on remittance transfers.⁷⁵ The report provides background on the remittance transfer market, including information about consumer demand, providers, products, and consumer behavior.⁷⁶ Drawing in part on this understanding of the remittance transfer market, the Bureau has issued regulations designed to achieve transparency and effective disclosure of exchange rates used for remittance transfers.⁷⁷ The report separately considers whether and how remittance histories can be used to enhance consumers' credit scores.⁷⁸ Going forward, the CFPB will further explore these questions by conducting empirical research into the potential value of remittance transfer data in predicting a consumer's credit repayment behavior.

In addition to collecting and analyzing data on markets and potential problems facing consumers, the Bureau will also conduct retrospective empirical evaluations of existing regulations' impact. To ensure that consumer financial protection laws and regulations protect consumers without unintended adverse consequences,⁷⁹ the CFPB has begun to collect and analyze data on the effectiveness of existing regulations. In particular, in February 2011, as part of a conference on the first anniversary of the CARD Act,⁸⁰ the CFPB surveyed cardholders and the nine largest credit card issuers, representing approximately 90% of the market.⁸¹ The studies revealed that, consistent with the purpose of the CARD Act, the long-standing practice of

⁷⁵ See Consumer Fin. Prot. Bureau, Report on Remittance Transfers: Report to the President, the Senate Committee on Banking, Housing, and Urban Affairs, and the House of Representatives Committee on Financial Services (2011) [hereinafter CFPB, REPORT ON REMITTANCE TRANSFERS], available at http://www.consumerfinance.gov/wp-content/uploads/2011/07/Report_20110720_RemittanceTransfers.pdf.

⁷⁶ See *id.* at 3–11.

⁷⁷ See Electronic Fund Transfers, 77 Fed. Reg. 6194 (Feb. 7, 2012) (to be codified at 12 C.F.R. pt. 1005).

⁷⁸ See CFPB, REPORT ON REMITTANCE TRANSFERS, *supra* note 75, at 25–43.

⁷⁹ Critics of the Dodd-Frank Act have cautioned that the Act could restrict economic growth and limit consumer credit by increasing its cost and decreasing its availability. See, e.g., THE FIN. SERVS. ROUNDTABLE, CUMULATIVE WEIGHT: A COMPILATION OF REPORTS AND PUBLIC STATEMENTS RELATED TO THE CUMULATIVE WEIGHT OF REGULATIONS MANDATED BY THE DODD-FRANK ACT (2011), available at http://www.fsround.org/fsr/publications_and_research/files/cumulativeweightwhitepaper.pdf (summarizing the potential negative impact of Dodd-Frank regulations voiced in various studies and reports).

⁸⁰ The CARD Act aims to improve the readability of credit card statements and to curb credit card companies' practices of raising interest rates on existing accounts, charging excessive or unfair fees, and processing charges that exceed a consumer's credit limit and lead to overlimit fees. See CARD Act of 2009, Pub. L. No. 111-24, 123 Stat. 1734 (codified in scattered sections of 15 and 16 U.S.C.).

⁸¹ See *CARD Act Factsheet*, CONSUMER FIN. PROT. BUREAU (Feb. 22, 2011), <http://www.consumerfinance.gov/credit-cards/credit-card-act/feb2011-factsheet/>.

increasing interest rates on existing cardholder accounts has been dramatically curtailed; the amount of late fees consumers are paying has substantially declined; and overlimit fees have virtually disappeared.⁸² Among cardholders surveyed, 60% felt that, since the CARD Act, their monthly statements had become easier to read and that terms were clearer; yet many still reported uncertainty about their APR or interest paid.⁸³ Significantly, the total amount consumers are paying for their credit cards is no higher, on average, than it was before the CARD Act took effect.⁸⁴

These kinds of fact-based analyses and studies of the consumer financial marketplace will help the CFPB to promulgate more cost-effective and beneficial regulations.

C. Facilitating Robust Public Participation Through Innovative Technologies and Transparency

Empirical analysis alone, however, cannot guarantee the most effective regulation. Getting input from diverse parties—including consumers, advocates, and regulated entities—is also essential. The Bureau has accordingly created systems to increase opportunities for public participation in its work. In particular, the Bureau has employed innovative technologies to make it easy and convenient for members of the public to report their problems and to share their suggestions; the Bureau also has implemented strong transparency policies that will increase public awareness and understanding of the Bureau's activities.⁸⁵ By facilitating robust public participation, the Bureau will benefit from a broad spectrum of viewpoints and experiences and avoid the risk of relying on biased and incomplete information that may favor one segment of industry at the expense of others and the public.⁸⁶

The Bureau is taking full advantage of the opportunities that building an agency from the ground up has given it for integrating innovative technologies into its operations. Even before its launch, the Bureau began reaching out to the public using Internet-based tools. Months ahead of the transfer date, the Bureau unveiled its website, ConsumerFinance.gov. Coinciding with the debut of the website

⁸² *Id.*

⁸³ Synovate, *Consumer Perceptions and Reactions to the CARD Act*, 15–16 (2011), http://www.consumerfinance.gov/wp-content/uploads/2011/01/Synovate_FINAL.pdf.

⁸⁴ See David Silberman, *The Credit CARD Act Turns One*, CONSUMER FIN. PROT. BUREAU (Feb. 22, 2011), <http://www.consumerfinance.gov/the-credit-card-act-turns-one/>.

⁸⁵ See CFPB, BUILDING THE CFPB, *supra* note 47, at 17–18.

⁸⁶ See Marnie Stetson, *Reforming SLAPP Reform: New York's Anti-SLAPP Statute*, 70 N.Y.U. L. REV. 1324, 1359 (1995) (noting that “broadly protected participation rights [can] help ensure a participatory democracy and provide an antidote to special interest capture of the government”).

was the CFPB's "Open for Suggestions" campaign, which solicited public input through multiple outlets, including Twitter, e-mail, and YouTube videos.⁸⁷ The CFPB received hundreds of suggestions and posted video responses to many on its YouTube channel. The Bureau also launched a blog and social media outposts on Twitter, Facebook, Flickr, and YouTube. These channels have been providing a steady stream of information from the public about problems with consumer financial products and suggestions for how to address those problems. The Bureau is analyzing this information so that it can inform its priorities and policymaking.

Of course, innovative uses of social media alone cannot guarantee robust public participation in the Bureau's work. To contribute meaningfully to the Bureau's work, the public must know what the Bureau is planning and doing. Accordingly, the Bureau has implemented strong transparency policies to maximize opportunities for the kind of public input that will help make its rules more efficient and effective.

From the start, Bureau staff met with open-government organizations, which provided valuable input regarding how to build transparency into the makeup of the agency. For example, the Bureau uses its website to provide consistent updates about its work and to solicit public feedback. It has made available the raw data underlying its study on the CARD Act's impact, enabling private parties to conduct their own analyses. Further, as discussed in more detail below, the Bureau has adopted a policy governing *ex parte* communications that balances the need to receive input on proposed rules from consumers, industry, and other interested parties with a commitment to transparency.⁸⁸

D. Learning from History and Borrowing Best Practices from Other Agencies

While embracing twenty-first-century innovations, the Bureau has also studied and learned from historical regulatory experiences and the best practices of the private and public sectors, including those of other federal agencies. To facilitate this learning process, the CFPB has hired staff from many other federal agencies and from the private sector.⁸⁹ These staff members' diverse experiences have proven invaluable in structuring the agency and in consciously developing an institutional culture. The Bureau has also solicited input from leaders in

⁸⁷ See CFPB, BUILDING THE CFPB, *supra* note 47, at 17–18.

⁸⁸ See *infra* notes 136–39 and accompanying text.

⁸⁹ In addition, pursuant to the Dodd-Frank Act, employees from other agencies have transferred to the Bureau. See 12 U.S.C. § 5584 (Supp. IV 2010).

the private sector, government, community groups, academia, and Congress in designing the Bureau's structure.

The Bureau has also learned from other agencies' specific policies and procedures. In drafting rules and policies governing *ex parte* communications, disclosure of agency records and information, and investigation and adjudication of violations of consumer financial laws, the Bureau has used other agencies' rules that have proven effective as models and has adapted those rules to its own mission. Several of these efforts are described in greater detail below.⁹⁰ Similarly, in establishing its pay scale and retirement system, and in organizing its procurement system, the Bureau has modeled its own practices on the best practices of other agencies.

Going forward, the Bureau will continue to learn from others' experiences in its effort to build an effective consumer agency. For example, the Bureau maintains open lines of communication with state attorneys general and banking regulators, who can both provide valuable insight into the landscape in their states and how enforcement could be strengthened.⁹¹ The Bureau has been meeting—and will continue to meet—with representatives from consumer groups and financial institutions to hear their perspectives on the best approaches to supervision, regulation, and other areas of the Bureau's responsibilities. In addition, the Bureau is learning from others in developing financial education materials. It is talking to the Financial Literacy and Education Commission—chaired by the Secretary of Treasury, state and local financial education officials, and other leaders in the field of financial education—to learn what others are doing, what works, and what does not work. Drawing on this knowledge, the Bureau will seek to develop new, more effective financial education materials and, as appropriate, to adapt already-available materials to suit its mission.

III

THE CFPB'S APPROACH IN PRACTICE

A. The "Know Before You Owe" Mortgage Disclosure Project: Relying on Data Analysis and Public Input to Craft a Market-Based Solution to Consumer Confusion in the Mortgage Market

Even before the transfer of rulemaking authority from other agencies that occurred on July 21, 2011, the Bureau started working on its "Know Before You Owe" (KBYO) mortgage initiative, a project intended to fulfill Congress's directive that the Bureau integrate fed-

⁹⁰ See *infra* notes 133–67 and accompanying text.

⁹¹ See CFPB, BUILDING THE CFPB, *supra* note 47, at 29–30.

eral disclosures for mortgage loan transactions.⁹² This project aims to create improved residential⁹³ mortgage disclosure forms that will minimize consumer confusion and enable comparison shopping to produce better functioning mortgage markets. To fulfill this important responsibility, the Bureau has taken an innovative approach that combines rigorous empirical testing with robust public participation. This preparatory work will lead to a proposed rule, expected in mid-2012, which will go through the notice-and-comment process.

The stakes of this project are significant. Mortgage lending is a huge industry affecting tens of millions of Americans. In October 2011, over fifty million U.S. residential mortgages,⁹⁴ representing 46% of households,⁹⁵ were outstanding. These outstanding mortgages totaled roughly \$10.4 trillion⁹⁶ and constituted a majority of consumer credit in the United States.⁹⁷ In 2010 alone, \$1.57 trillion in U.S. mortgage loans were originated.⁹⁸ Yet shopping for and obtaining a mortgage loan remains a complex process that can bewilder many consumers.⁹⁹

Given the prevalence of mortgage loans and the widespread lack of understanding of them before the financial crisis, Congress re-

⁹² See 12 U.S.C. § 5532(f); *Know Before You Owe*, CONSUMER FIN. PROT. BUREAU, <http://www.consumerfinance.gov/knowbeforeyouowe/> (last visited Apr. 9, 2012).

⁹³ Throughout this Article, “residential” is defined as one- to four-family dwellings, as reflected in 12 C.F.R. § 1003.2 (2011).

⁹⁴ See EXPERIAN & OLIVER WYMAN, MARKET INTELLIGENCE REPORT: MORTGAGE REPORT 19 fig.24 (2011) (providing a value of \$50.1 million) (on file with author); *Mortgage Monitor: November 2011 Mortgage Performance Observations*, at 3, LENDER PROCESSING SERVICES (Nov. 2011), <http://www.lpsvcs.com/LPSCorporateInformation/CommunicationCenter/PressResources/Pages/MortgageMonitorArchive.aspx> (follow “Complete Presentation” hyperlink under “Data as of October 2011”) (source can only be obtained online by authorized users) (providing a value of \$51.6 million).

⁹⁵ See *State & County QuickFacts*, U.S. CENSUS BUREAU, <http://quickfacts.census.gov/qfd/states/00000.html> (last updated Jan. 17, 2012).

⁹⁶ *Mortgage Debt Outstanding*, BOARD OF GOVERNORS OF THE FED. RESERVE SYS., <http://www.federalreserve.gov/econresdata/releases/mortoutstand/mortoutstand20110930.htm> (last updated Sept. 30, 2011).

⁹⁷ *Consumer Credit*, BOARD OF GOVERNORS OF THE FED. RESERVE SYS. (Dec. 7, 2011), <http://www.federalreserve.gov/releases/g19/20111207/g19.pdf>.

⁹⁸ INSIDE MORTGAGE FINANCE, TOP 50 MORTGAGE ORIGINATORS IN 2010 (2011), available at http://www.insidemortgagefinance.com/issues/reports/top_mortgage/-1000012416-1.html (available online only for subscribing users).

⁹⁹ See generally Brian K. Bucks & Karen M. Pence, *Do Borrowers Know Their Mortgage Terms?*, 64 J. URBAN ECON. 218, 218, 221–28 (2008) (noting adjustable-rate mortgages have become more complex in recent years); Patricia A. McCoy, *Rethinking Disclosure in a World of Risk-Based Pricing*, 44 HARV. J. LEGIS. 123, 125–27 (2007) (describing the evolution in the mortgage market from average-cost-based to risk-based pricing); Mary Umberger, *Survey Reveals Consumer Confusion on Mortgages*, CHI. TRIB., May 13, 2011, available at http://articles.chicagotribune.com/2011-05-13/classified/sc-cons-0512-umberger-zillow-20110513_1_mortgages-home-loans-rate.

quired the Bureau to prioritize addressing this problem.¹⁰⁰ This mandate follows decades of efforts by Congress and other regulators to promote consumer understanding of mortgage products. In 1968, Congress enacted the Truth in Lending Act (TILA) to “assure a meaningful disclosure of credit terms [including mortgage terms] so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit.”¹⁰¹ The Federal Reserve Board (FRB) promulgated Regulation Z to implement TILA, and both the statute and the rule have been amended many times.¹⁰² After TILA’s enactment, Congress passed the Real Estate Settlement Procedures Act (RESPA) in 1974 to enable “more effective advance disclosure to home buyers and sellers of settlement costs” and to prohibit kickbacks, unearned settlement fees, and various other practices.¹⁰³ Pursuant to RESPA, the Department of Housing and Urban Development (HUD) promulgated rules requiring mortgage brokers and lenders to provide two key disclosures in mortgage loan transactions: a good faith estimate (GFE) disclosure and a final disbursement disclosure (HUD-1) at the closing of the loan.¹⁰⁴

Together, the TILA and RESPA disclosures that most consumers currently receive within three days of applying for a mortgage loan usually total five comprehensive, yet complex and often confusing, pages. The copious amount of information presented on those forms does not, on the whole, appear to be well designed for average consumers to use.¹⁰⁵ Disclosures do not focus on the information consumers may need most, such as total cash needed at closing or the size of the payment shock at each rate reset. Further, some items—such as prepayment penalty disclosures—may simply be too opaque for consumers to understand and compare. Consumers that the Bureau interviewed during its research lamented that they simply “don’t know

¹⁰⁰ See 12 U.S.C. § 5532(f) (Supp. IV 2010). The Dodd-Frank Act requires the Bureau to propose for public comment new model mortgage disclosures and accompanying rules within one year of the Bureau’s launch on July 21, 2011. *Id.*

¹⁰¹ Consumer Credit Protection Act, Pub. L. No. 90-321, § 102, 82 Stat. 146, 146 (1968) (codified as amended in scattered sections of 15 U.S.C.).

¹⁰² THOMAS A. DURKIN & GREGORY ELLIEHAUSEN, TRUTH IN LENDING: THEORY, HISTORY, AND A WAY FORWARD 9 (2011) (stating that “Congress amended TILA in 1970, 1974, 1975, 1976 (twice), 1978, 1980 (major revision), 1981 (twice), 1982, 1984, 1987, 1988 (twice), 1992, 1993, 1994, 1995 (twice), 1996, 1997, 1998, 2005, 2008, and 2009” and that the FRB amended Regulation Z “more than fifty times”).

¹⁰³ 12 U.S.C. § 2601(b)(1) (2006).

¹⁰⁴ See 24 C.F.R. § 3500 (2011).

¹⁰⁵ See FED. TRADE COMM’N, IMPROVING CONSUMER MORTGAGE DISCLOSURES: AN EMPIRICAL ASSESSMENT OF CURRENT AND PROTOTYPE DISCLOSURE FORMS ES-5-10, available at <http://www.ftc.gov/os/2007/06/P025505MortgageDisclosureexecutivesummary.pdf> (finding that current mortgage cost disclosures failed to convey key mortgage costs to many consumers and that borrowers failed to understand key loan terms when viewing the disclosures).

what to do with” these forms. While many experts debated the extent to which disclosure can actually promote informed decision making by consumers,¹⁰⁶ few believed at the end of 2010 that the disclosures consumers were receiving were optimal.¹⁰⁷ Even fewer believe that the research necessary to create optimal forms already exists.¹⁰⁸

Recognizing that the current system did not work, Congress included TILA and RESPA among the statutes for which rulemaking responsibility would transfer to the Bureau and charged the CFPB with combining and improving the TILA and RESPA disclosures that consumers currently receive.¹⁰⁹ To carry out this mandate, the Bureau created the “Know Before You Owe” mortgage initiative, which aims to improve mortgage disclosures to enable consumers to understand the relevant terms of credit being offered and to compare those terms across providers and products. This market-based solution—creating more effective disclosures—seeks to minimize consumer confusion and promote a more effective, transparent, and level consumer financial marketplace.

1. *Establishing Project Objectives*

The CFPB has decided to take a fresh approach to achieve this goal. The Bureau is relying on both empirical testing and extensive public participation throughout the process of developing a new disclosure form. In December 2010, the Treasury Department sponsored a research symposium that brought together academics, lenders, and consumer advocates to discuss how to simplify federal mortgage disclosures. Consumer groups explained that many consumers failed to use current disclosures to assess costs or to compare alternatives because the forms are “complicated and hard to use.” Additionally, “[t]he forms came under even more intense criticism from those who have to fill them out. Mortgage originators, particularly community banks and credit unions that work closely with their customers, described paperwork that was costly to complete and pro-

¹⁰⁶ See, e.g., DURKIN & ELLIEHAUSEN, *supra* note 102, at 53–82 (discussing behavioral research questioning consumers’ ability to make rational financial choices).

¹⁰⁷ See Omri Ben-Shahar & Carl E. Schneider, *The Failure of Mandated Disclosure*, 159 U. PA. L. REV. 647, 705–10 (2011); McCoy, *supra* note 99, at 154; Lauren E. Willis, *Decisionmaking and the Limits of Disclosure: The Problem of Predatory Lending: Price*, 65 MD. L. REV. 707, 741–51 (2006).

¹⁰⁸ See JAMES M. LACKO & JANIS K. PAPPALARDO, IMPROVING CONSUMER MORTGAGE DISCLOSURES: AN EMPIRICAL ASSESSMENT OF CURRENT AND PROTOTYPE DISCLOSURE FORMS; FEDERAL TRADE COMMISSION BUREAU OF ECONOMICS STAFF REPORT 2007, available at <http://www.ftc.gov/os/2007/06/P025505MortgageDisclosureReport.pdf>.

¹⁰⁹ See 12 U.S.C. § 5532(b) (Supp. IV 2010) (granting the Bureau the authority to develop model disclosures and requiring consumer testing validation).

duced little value for borrowers.”¹¹⁰ In short, the forms were not serving anyone well.

Shortly after the December 2010 research symposium, a cross-functional team within the Bureau considered what appeared to be the two fundamental questions implicated in executing Congress’s mandate: (1) What were the objectives of the disclosures? (i.e., what “job” were the disclosures meant to do?¹¹¹); and (2) How could a new form achieve those objectives?

On the first question, the team identified three core objectives. The first objective was to identify what information consumers really needed for comprehension and comparison and to present this information on the combined forms in a manner consumers could understand and use if they wanted to comparison shop. In other words, the objective was to build a disclosure that would ensure that material terms could be easily located and that would enable consumers to compare loans offered by one lender or shop between lenders and make better decisions given the options in the marketplace and their individual goals and preferences.¹¹² The second objective was to ensure that the forms stand out from other loan documents so that consumers could quickly determine what information was most critical to their decision. The third objective was to ensure that any required disclosures actually support better decision making by consumers.

In addressing the second question of how the new disclosure form would achieve these objectives, the Bureau is relying on public participation and empirical testing. Throughout the process, the CFPB has consistently recognized that outcomes can be improved via discussions with others. In particular, the Bureau recognizes the need to consider implementation and operational issues, as well as other matters, early in the process so it can make adjustments and test those adjustments thoroughly. As a result, to facilitate the development of a notice of proposed rulemaking, the CFPB released multiple drafts of the disclosure forms for broad public input much earlier than other regulators typically do. This has created additional complexity in the short run, but has already yielded substantial benefits, such as im-

¹¹⁰ CFPB, BUILDING THE CFPB, *supra* note 47, at 10.

¹¹¹ For a description of job-based strategic analysis, see Clayton M. Christensen et al., *Finding the Right Job for Your Product*, 48 MIT SLOAN MGMT. REV., Spring 2007, at 37–47.

¹¹² Notably, the team identified the goal as enabling comparison. They believed that the disclosure should facilitate shopping, but not force shopping to occur. Any new form would therefore be evaluated based on how well it enables shopping, not on how much shopping actually occurs. Enabling shopping can have a profound effect on the market. Economic theory suggests that a more competitive market does not require every consumer to shop and that the efforts of just a few (or even the potential efforts of just a few) may benefit the entire marketplace. See Alan Schwartz & Louis L. Wilde, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. PA. L. REV. 630, 638 (1979).

provements to language that had confused consumers and more effective graphic designs. As the CFPB moves to next phases of its KBYO project, it looks forward to even more feedback from the public through the notice-and-comment rulemaking process.

2. *Iterative, Collaborative Cycles*

In May 2011, the CFPB publicly launched the “Know Before You Owe” project.¹¹³ The goal was simple: to carry out the statutory mandate to combine two federally required mortgage disclosures into a single, simpler form that makes the costs and risks of the loan clear and allows consumers to comparison shop for the best offer.¹¹⁴ The Bureau sought feedback from other regulators, industry groups, consumer groups, and individual consumers. Unlike most other agencies, the Bureau sought this early feedback from the public through iterative cycles and continuous collaboration as the Bureau conducted its own consumer testing.¹¹⁵ The process adopted was, in its early phases, more similar to best practice new product design¹¹⁶ than traditional rulemaking endeavors. This input provided a valuable supplement to the Bureau’s required public consultation.

Each iterative cycle consisted of the release of a new pair of designs. In each cycle, the Bureau conducted a new phase of qualitative testing, consisting of in-depth, one-on-one interviews with borrowers, lenders, and brokers using well-established methodologies.¹¹⁷ Importantly, the CFPB structured these interviews to test how well consumers and lenders were able to use the forms, not individuals’ preferences between and among the forms.

At the same time that the Bureau was testing each set of forms, it also posted them online with an interactive tool to gather public input about the designs. By recording where users clicked as they reviewed the draft disclosures, this tool allowed the Bureau to compile “heatmaps” showing the areas of the disclosures that attracted the most and least attention.¹¹⁸ In addition, as a useful supplement to the traditional public notice-and-comment process, the CFPB’s interactive tool permitted targeted input on the portions of the design that were under investigation in that cycle. That targeted input allowed Bureau

¹¹³ See Aneesh Chopra, “Know Before You Owe,” THE WHITE HOUSE OFF. OF SCI. & TECH. POL’Y (May 21, 2011, 5:59 PM), <http://www.whitehouse.gov/blog/2011/05/21/know-you-owe>.

¹¹⁴ See CFPB, BUILDING THE CFPB, *supra* note 47, at 10–11.

¹¹⁵ See *id.* at 11.

¹¹⁶ See, e.g., Stefan H. Thomke, *Managing Experimentation in the Design of New Products*, 44 MGMT. SCI. 743, 744–45 (1998).

¹¹⁷ See CFPB, BUILDING THE CFPB, *supra* note 47, at 11.

¹¹⁸ *Mortgage Disclosure Is Heating Up*, CFPB BLOG (June 24, 2011), <http://www.consumerfinance.gov/mortgage-disclosure-is-heating-up/>.

staff to process the feedback quickly, iterate the forms, and then test again in four weeks.

The process fostered robust public participation. The Bureau received over 220,000 unique pageviews for KBYO, resulting in 27,000 comments (roughly half from consumers and half from industry) over the first seven iterative cycles.¹¹⁹ Those comments—combined with the results of the qualitative testing—produced an approach to disclosure that initial testing shows is serving the objectives of minimizing consumer confusion and enabling comparison shopping. Seeking broad-based public input as it conducted consumer testing, rather than having a single public comment period on a full formal proposal, has been central to the development and potential success of the Bureau's proposed form. So far, the draft forms have enjoyed a high level of approval among consumers, lenders, brokers, consumer advocates, and other regulators, as evidenced by the discussions at roundtables held in September 2011. These early results are promising as the effort appears to have helped create an approach to disclosure that better enables consumers to determine whether they can afford a mortgage and whether they can get a better deal somewhere else.

Drawing on this experience, the Bureau expanded its “Know Before You Owe” initiative to include student loans and credit cards. In these initiatives, the Bureau developed prototype forms that aim to make the costs and risks of those financial products easier to understand.¹²⁰ These prototypes are not formal proposals related to consumer disclosure requirements, but are designed simply to promote a conversation about what types of disclosures and information might create better-functioning markets and better-informed consumers. These initiatives promise meaningful benefits. Clarifying student loan offers can help students understand their potential obligations, shop for a better deal, and minimize educational debt service obligations. Similarly, improving credit card agreements can help consumers understand the debts they may take on and empower consumers to make the best decisions for themselves and to avoid costly surprises.

For each initiative, the Bureau drew on available data to develop the prototype forms and invited input from the public, including consumers, advocates, and the financial services industry.¹²¹ For the credit cards initiative, the Bureau also partnered with Pentagon Federal Credit Union, an institution with more than 350,000 credit cardholders, to use its agreement in a pilot test.¹²² The Bureau continues

¹¹⁹ CFPB, SEMI-ANNUAL REPORT, *supra* note 46, at 13–14.

¹²⁰ *Id.* at 13.

¹²¹ *Id.* at 13.

¹²² Press Release, Consumer Fin. Prot. Bureau, Consumer Financial Protection Bureau Aims to Simplify Credit Card Agreements (Dec. 7, 2011), *available at* <http://>

to work with Pentagon Federal and other card issuers who are interested in adopting simplified credit card agreements. By drawing on feedback from consumers and industry alike, the Bureau will develop consumer information documents that can help make markets work better.

B. Office of Servicemember Affairs: Collecting Information to Ensure Effective Education and Outreach

The Bureau has also sought broad public input to build market-based programs to help servicemembers address their financial problems. Finances are of great concern to military personnel and their families, who are too often targeted by unscrupulous lenders.¹²³ Former Undersecretary of Defense for Personnel and Readiness Clifford Stanley reported that finances are the second-largest cause of increasing stress among servicemembers and their families, behind only work and career concerns, and ahead of deployments, health, life events, and war.¹²⁴ Financial concerns not only hurt individual servicemembers but also can compromise national security.¹²⁵ A 2006 Department of Defense report concluded that predatory lending directed at servicemembers “undermines military readiness, harms the morale of troops and their families, and adds to the cost of fielding an all volunteer fighting force.”¹²⁶

To help reduce or eliminate these problems, Congress required the Bureau to establish an Office of Servicemember Affairs that could address the financial issues faced by members of the military.¹²⁷ Among other things, this Office is charged with educating and em-

www.consumerfinance.gov/pressreleases/consumer-financial-protection-bureau-aims-to-simplify-credit-card-agreements/.

¹²³ U.S. DEP’T OF DEFENSE, REPORT ON PREDATORY LENDING PRACTICES DIRECTED AT MEMBERS OF THE ARMED FORCES AND THEIR DEPENDENTS 4 (2006), available at http://www.defense.gov/pubs/pdfs/report_to_congress_final.pdf (“Predatory lending practices are prevalent and target military personnel, either through proximity and prevalence around military installations, or through the use of affinity marketing techniques, particularly on-line.”). See generally Steven M. Graves & Christopher L. Peterson, *Predatory Lending and the Military: The Law and Geography of “Payday” Loans in Military Towns*, 66 OHIO ST. L.J. 653, 709–832 (2005) (providing in-depth empirical evidence and analysis showing that payday lenders target military personnel and their families).

¹²⁴ *Military Saves Week 2011*, U.S. MARINES (Jan. 24, 2011), available at <http://www.marines.mil/news/messages/Pages/MARADMIN057-11.aspx> (last visited Mar. 19, 2012).

¹²⁵ See *id.* (quoting Undersecretary Stanley as saying that “the Department of Defense fully believes that personal financial readiness of our troops and families equates to mission readiness”).

¹²⁶ U.S. DEP’T OF DEFENSE, *supra* note 123, at 9.

¹²⁷ Dodd-Frank Act, 12 U.S.C. § 5493(e) (Supp. IV 2010).

powering servicemembers and their families to make better-informed decisions when choosing financial services and products.¹²⁸

The CFPB's approach to fulfilling this mission has exemplified its commitment to evidence-based programs and its belief in the power of the market. In particular, the Bureau has collected information from diverse sources to shape outreach and education campaigns that will promote servicemembers' ability to understand and analyze the costs and benefits of different financial products and services.¹²⁹ Under the leadership of Holly Petraeus,¹³⁰ the Office has been collecting information from servicemembers, their advocates and counselors, and industry participants about the financial challenges that servicemembers face and the consumer financial products and services marketed to them. The Office has hosted town hall meetings with military families and roundtable discussions with financial readiness program managers and counselors, legal assistance lawyers, chaplains, and other professionals serving the military community.¹³¹ These meetings have educated the Bureau about what financial issues are most significantly affecting servicemembers and about local advocates' best practices for protecting against harmful lending practices. The meetings have also given the Bureau a better understanding of how servicemembers' special circumstances—such as deployments, permanent change-of-station moves, overseas assignments, and relocations—can present unique financial challenges to military families and their creditors. The Bureau is now using the insights gained in these meetings to shape financial education programs for servicemembers.

The Bureau also launched an initiative to collect data on the beneficial financial products that companies offer servicemembers and

¹²⁸ *Id.* § 5493(e)(1)(A). The Office of Servicemember Affairs will also monitor complaints by servicemembers and their families, as well as the responses to those complaints, and coordinate efforts among federal and state agencies regarding consumer financial protection measures for servicemembers and their families. *Id.* § 5493(e)(1)(B)–(C).

¹²⁹ *See, e.g.*, Press Release, Consumer Fin. Prot. Bureau, Consumer Financial Protection Bureau Analyzing Financial Products Tailored to Servicemembers (Sept. 7, 2011), available at <http://www.consumerfinance.gov/pressrelease/consumer-financial-protection-bureau-analyzing-financial-products-tailored-to-servicemembers/>.

¹³⁰ As the wife of General David Petraeus, the mother, sister, daughter, granddaughter, and great-granddaughter of servicemembers, and the former Director of the Better Business Bureau Military Line, Holly Petraeus has a deep understanding of the kinds of financial obstacles that men and women in the armed forces encounter. *See* Press Release, U.S. Dep't of the Treasury, Treasury Department Announces Holly Petraeus to Establish Office of Servicemember Affairs for Consumer Financial Protection Bureau (Jan. 6, 2011), <http://www.treasury.gov/press-center/press-releases/Pages/tg1015.aspx>. This depth of personal and professional experience will greatly promote the programmatic ends of learning from and responding to the needs of the military community.

¹³¹ *See* Elizabeth Warren & Holly Petraeus, *Hearing Directly from Our Servicemembers*, CONSUMER FIN. PROT. BUREAU (Jan. 18, 2011), <http://www.consumerfinance.gov/oped/hearing-directly-from-our-servicemembers/>.

their families. In September, the Bureau published a notice in the Federal Register seeking information on financial products and services offered to servicemembers and their families.¹³² The Bureau received dozens of responses, primarily from financial service providers about products and services tailored to servicemembers' financial needs, accommodations and benefits provided to servicemembers that exceed those required or available under federal law,¹³³ and special assistance offered to distressed homeowners affiliated with the military. The responses show that many companies have offered products and programs tailored to servicemembers, such as short-term, small-dollar loans with interest rates lower than those offered by payday lenders and matching savings programs.¹³⁴

Building on these responses, the Bureau hosted a Financial Fitness Forum that featured panels consisting of servicemembers, representatives from banking and credit union trade associations, and individual financial institutions.¹³⁵ These panelists shared innovative ideas for meeting military customers' unique needs in a way that allows financial institutions to thrive as well.

The Bureau will evaluate the information about these products and programs and, as appropriate, will incorporate it into servicemember education and outreach programs. Better information about what banks, credit unions, and other companies are offering military personnel will ease servicemembers' burdens in choosing the products and services that best meet their needs. The Bureau will also continue to educate financial service providers about other providers' practices as a way to encourage healthy competition. By encouraging service providers to improve their offerings and educating servicemembers about how to select the products best suited to their par-

¹³² Request for Information on Consumer Financial Products and Services Offered to Servicemembers, 76 Fed. Reg. 54,998 (Sept. 6, 2011). The notice also requested information about the financial education opportunities that companies offered servicemembers and about the nature and effectiveness of marketing and communication strategies targeted at servicemembers and their families. *Id.*

¹³³ For example, the Servicemembers Civil Relief Act prevents creditors from charging more than 6% interest on a servicemember's preservice debt during a servicemember's period of military service. 50 U.S.C. app. § 527(a). Some banks reported that they have lowered servicemembers' interest rates to below the statutory maximum. *See, e.g.*, Comment on Notice, Request for Information: Consumer Financial Products and Services Offered to Servicemembers, Docket No. CFPB-2011-0016-0080, REGULATIONS.GOV (Sept. 20, 2011), available at <http://www.regulations.gov/#!documentDetail;D=CFPB-2011-0016-0080>.

¹³⁴ *See* Kate Davidson, *CFPB Plans Financial Boot Camp for Military*, AM. BANKER (Dec. 16, 2011, 4:41 PM), http://www.americanbanker.com/issues/176_243/CFPB-military-service-member-defense-Petraeus-foreclosure-1044975-1.html (available online only for subscribing users).

¹³⁵ Holly Petraeus, *Financial Fitness Forum*, CFPB BLOG (Dec. 16, 2011), <http://www.consumerfinance.gov/financial-fitness-forum/>.

ticular needs, the Bureau aims to make the markets work better for servicemembers.

C. *Ex Parte* Policy: Promoting Transparency and Evidence-Based Decision Making

While rigorous data analysis and collection of input from diverse sources informs the Bureau's initial policymaking and program building, feedback and information provided by interested parties during the notice-and-comment period is also crucial to the Bureau's evidence-based approach to policymaking. Ideas and comments received in response to a proposed rule are critical in shaping the Bureau's ultimate regulations. The primary and preferred means for the Bureau to collect public input regarding proposed rules is through written comments that are posted on the rulemaking docket. But, in some cases, pertinent information may also come through telephone calls, e-mails, face-to-face meetings, and written letters. The Bureau has carefully considered how to handle such informal "*ex parte*" communications during the notice-and-comment process. The policy that the Bureau adopted seeks to accommodate both a commitment to transparency and an openness to information and feedback from various sources to support its evidence-based policymaking.¹³⁶

As a supplement to written comments, *ex parte* communication can be a valuable means for the Bureau to consult with the public and can provide a valuable diversity of perspectives and additional information. Not all parties interested in a rule have the resources or sophistication to file extensive comment letters that effectively convey their viewpoints. Some parties can better explain their perspective in a phone call or meeting. Barring all *ex parte* communication could diminish these groups' ability to be heard.¹³⁷ In some cases, *ex parte* communication can also be an important means for the Bureau to receive information on rulemaking proposals and to obtain clarification on and elaboration of comments filed in rulemaking proceedings. In all instances, *ex parte* communications are intended to supplement and not replace written comments to the rulemaking docket. By allowing these communications, the Bureau facilitates input by many interested parties and ensures that it will have access to

¹³⁶ See *CFPB Policy on Ex Parte Presentations in Rulemaking Proceedings*, CONSUMER FIN. PROT. BUREAU BULL. 11-3, (Aug. 16, 2011) [hereinafter *Ex Parte Presentations*], available at http://www.consumerfinance.gov/wp-content/uploads/2011/08/Bulletin_20110819_ExPartePresentationsRulemakingProceedings.pdf.

¹³⁷ See generally Mark Seidenfeld, *A Civic Republican Justification for the Bureaucratic State*, 105 HARV. L. REV. 1511, 1530 (1992) (noting that the citizenry requires "[b]road rights of access" to administrative agencies and that "[r]epresentatives of all interests potentially affected by a government action must have meaningful opportunities to engage in discussion about the action").

the best available information. This information supplements the empirical data analysis that drives much of the Bureau's work.

At the same time, the Bureau's *ex parte* policy promotes transparency, fairness, and deliberation among parties interested in the rule by requiring disclosure of *ex parte* communications. Under the policy, *ex parte* presentations must be summarized and disclosed on the public docket.¹³⁸ The policy applies to communications that are directed to the merits or outcome of an open rulemaking proceeding—from the publication of a notice of proposed rulemaking or interim final rule until final disposition of the rulemaking.¹³⁹ Through this disclosure, any interested party can see the information that the Bureau has received. This preserves the transparency of the rulemaking process, increases public deliberation, and gives the Bureau access to better quality information and data.

D. Adjudication Rules: Learning from Other Federal Regulators

The Bureau is drawing on the experiences of other regulators in shaping many of its procedures. This Section highlights some of the ways in which the Bureau has gained insight and guidance from the practices of other federal agencies in drafting the rules that will govern its administrative adjudications. Congress vested the Bureau with broad authority to enforce federal consumer financial protection laws in the courts or through administrative adjudications.¹⁴⁰ The Dodd-Frank Act, however, does not detail the administrative adjudication process that the Bureau should utilize but rather requires the Bureau to promulgate rules establishing adjudication procedures.¹⁴¹ In doing so, the Bureau has sought the advice of other regulators and has attempted to learn from their experiences and to adopt their best practices. The Bureau's goal was to establish an administrative process that is both fair and efficient.

Shortly after its launch date in July 2011, the Bureau issued interim final rules governing its adjudication proceedings (Adjudication Rules).¹⁴² The Bureau's Adjudication Rules govern proceedings

¹³⁸ *Ex Parte Presentations*, *supra* note 136, § (d)(1)–(2). The policy explains certain circumstances that do not require disclosure and where the Bureau retains discretion to make modifications as appropriate during particular rulemakings. *Id.* § (e).

¹³⁹ *Id.* § (b)(1)(A).

¹⁴⁰ See Dodd-Frank Act, 12 U.S.C. §§ 5562–5564 (Supp. IV 2010).

¹⁴¹ 12 U.S.C. § 5563(e).

¹⁴² Rules of Practice for Adjudication Proceedings, 76 Fed. Reg. 45,338 (July 28, 2011) (codified at 12 C.F.R. pt. 1081). This discussion refers to the Bureau's interim final rule. After this Article was finalized, but before it was published, the Bureau issued a final rule in response to the comments it received regarding the interim final rule. The reader is encouraged to review the Bureau's final rule for further information regarding the Bureau's efforts to craft a fair and efficient administrative process.

brought under section 1053 of the Dodd-Frank Act,¹⁴³ which authorizes the Bureau to use administrative adjudications to ensure or enforce compliance with the Act, the Bureau's rules, or any other federal law or regulation that the Bureau is authorized to enforce.¹⁴⁴ In drafting the Adjudication Rules, the Bureau carefully considered the rules and procedures of federal banking regulators, the FTC, and the SEC.¹⁴⁵ The Bureau also referred to the Model Adjudication Rules prepared by the Administrative Conference of the United States.¹⁴⁶

In developing the Adjudication Rules, the Bureau aimed to create a process that would both provide for expeditious resolution of claims and guarantee respondents a fair hearing. To achieve these goals, the Bureau looked to the history of administrative proceedings at the FTC and SEC and learned from those agencies' experience.¹⁴⁷ More specifically, in the last twenty years, both the SEC and the FTC have revised their rules to make the adjudicatory process more efficient. In 1990, the SEC created a task force to review its rules and procedures governing administrative proceedings "to identify sources of delay in those proceedings and to recommend steps to make the adjudicatory process more efficient and effective."¹⁴⁸ Drawing on this task force's recommendations, the SEC revised its rules in 1995.¹⁴⁹ The FTC similarly revised its rules in 2008 to improve its adjudicatory process, which had "long been criticized as being too protracted."¹⁵⁰ The FTC's revised rules sought to "strike an appropriate balance between the need for fair process and quality decisionmaking, the desire for efficient and speedy resolution of matters, and the potential costs imposed on the Commission and the parties."¹⁵¹ Studying this history allowed the Bureau to gain a better understanding of the advantages and disadvantages of different procedures.

In drafting its Adjudication Rules, the Bureau adopted these agencies' best practices and sought to improve upon their efforts to streamline proceedings without compromising fairness to the parties. For example, for purposes of its interim final rule, the Bureau decided to adopt the SEC's affirmative disclosure approach to fact dis-

¹⁴³ 12 U.S.C. § 5563.

¹⁴⁴ Rules of Practice for Adjudication Proceedings, 76 Fed. Reg. at 45,338.

¹⁴⁵ See *id.*

¹⁴⁶ *Id.* (citing Michael P. Cox, *The Model Adjudication Rules (MARs)*, 11 T.M. COOLEY L. REV. 75 (1994)).

¹⁴⁷ *Id.*

¹⁴⁸ Rules of Practice, 60 Fed. Reg. 32,738, 32,738 (June 23, 1995).

¹⁴⁹ *Id.*

¹⁵⁰ Rules of Practice, 73 Fed. Reg. 58,832, 58,832-33 (Oct. 7, 2008).

¹⁵¹ *Id.* at 58,833.

covery in administrative adjudications.¹⁵² In particular, the Adjudication Rules generally require the Enforcement Office to make available for inspection and copying by any party documents that the Office obtained from persons not employed by the Bureau during the investigative phase.¹⁵³ The SEC codified a similar practice in 1995 in part to help make proceedings more fair and efficient.¹⁵⁴ By adopting the SEC's basic approach in this regard, the Bureau aims to ensure fairness to respondents while streamlining resolution of administrative proceedings.¹⁵⁵ By requiring the affirmative disclosure of information, the Bureau seeks to ensure that respondents have a full understanding of the factual basis of the charges at an early stage of the proceedings so that they can efficiently determine what defenses to present and whether to seek settlement.¹⁵⁶ At the same time, because this approach reduces the need for traditional fact discovery, it will allow for faster and more efficient resolution of the Bureau's administrative claims, conserving both the Bureau's and respondents' resources.¹⁵⁷ The Bureau's rule also includes exceptions to the affirmative disclosure requirement, largely based on the exceptions contained in the SEC's analogous rule.¹⁵⁸ These exceptions balance "the needs of respondents, the rights of those who have submitted documents, and the [agency's] legitimate interests in maintaining effective law enforcement."¹⁵⁹

The Bureau's Adjudication Rules also adopt certain timelines modeled on the SEC and FTC rules to encourage expeditious resolution of proceedings. Like the SEC's rules, the Bureau's rules require a hearing officer to issue a recommended decision within 300 days of service of the notice of charges.¹⁶⁰ The Adjudication Rules permit hearing officers to request an extension of this 300-day deadline in individual cases but state that the Director will only rarely grant such extensions.¹⁶¹ The Adjudication Rules also follow the SEC's standards governing extensions of time, which are generally disfavored.¹⁶² To

¹⁵² Rules of Practice for Adjudication Proceedings, 76 Fed. Reg. 45,338, 45,344 (July 28, 2011).

¹⁵³ 12 C.F.R. § 1081.206(a)-(b) (2011).

¹⁵⁴ See Rules of Practice, 58 Fed. Reg. 61,732, 61,750 (Nov. 22, 1993).

¹⁵⁵ See Rules of Practice for Adjudication Proceedings, 76 Fed. Reg. at 45,339.

¹⁵⁶ *Id.* at 45,344.

¹⁵⁷ *Id.*

¹⁵⁸ *Id.*; Rules of Practice, 58 Fed. Reg. at 61,750.

¹⁵⁹ Rules of Practice, 58 Fed. Reg. at 61,750.

¹⁶⁰ 12 C.F.R. § 1081.400 (2011) (CFPB rule); 17 C.F.R. § 201.360(a)(2) (2011) (SEC rule).

¹⁶¹ Rules of Practice for Adjudication Proceedings, 76 Fed. Reg. 45,350; 12 C.F.R. § 1081.400.

¹⁶² Rules of Practice for Adjudication Proceedings, 76 Fed. Reg. 45,342; 12 C.F.R. §§ 1081.115, 1081.400. This applies to requests for extensions by the hearing officer and by the parties. If the hearing officer seeks an extension of the 300-day deadline, both the

further facilitate speedy resolution of matters, the Bureau's Adjudication Rules prescribe a rule similar to one of the FTC that requires hearing officers to file their recommended decisions within ninety days after the deadline for filing post-hearing responsive briefs.¹⁶³

In addition, the Bureau followed the SEC's lead in requiring the hearing officer to convene a pretrial conference soon after initiation of proceedings to set a schedule appropriate to the particular proceeding.¹⁶⁴ The rules further require the parties to meet before the conference to discuss the nature and basis of their claims and defenses, the possibilities for a prompt settlement or resolution of the case, and other matters that can or should be addressed at the scheduling conference.¹⁶⁵ In 1995, the SEC amended its rules to make such pretrial conferences mandatory in most instances.¹⁶⁶ The SEC made this change "because such a conference can eliminate unnecessary delay and improve the quality of adjudicative decisionmaking by sharpening the preparation of cases and presentation of issues."¹⁶⁷ By similarly requiring such pretrial conferences to take place shortly after initiation of proceedings, the Bureau expects its rules to offer these same benefits.

In sum, relying on the past experiences of other agencies and their input, the Bureau sought to craft Adjudication Rules that are both fair and efficient. The Bureau recognizes, however, that its work will always benefit from the informed views of interested parties

SEC and CFPB rules require the hearing officer to request an extension at least thirty days before expiration of the applicable time period, allow the parties to file briefs supporting or opposing the extension, and authorize the Commission or the Director, respectively, to grant the extension only if "additional time is necessary or appropriate in the public interest." 12 C.F.R. § 1081.400(b) (CFPB rule); 17 C.F.R. § 201.360(a)(3) (SEC rule). Both the CFPB and the SEC rules provide that parties' requests for extensions of deadlines are "strongly disfavor[ed]." 12 C.F.R. § 1081.115(b) (CFPB rule); 17 C.F.R. § 201.161(b)(1) (SEC rule). The CFPB's rules adopt the SEC's rules requiring the requesting party to make a "strong showing that the denial of the request or motion would substantially prejudice their case" and identify five enumerated factors for the agency to consider in evaluating the request. 12 C.F.R. § 1081.115(b); 17 C.F.R. § 201.161(b)(1).

¹⁶³ Rules of Practice for Adjudication Proceedings, 76 Fed. Reg. 45,350. Compare 12 C.F.R. § 1081.400(a) (CFPB rule providing that "the hearing officer shall file a recommended decision no later than 90 days after the deadline for filing post-hearing responsive briefs"), with 16 C.F.R. § 3.51(a) (2011) (FTC rule providing that "[t]he Administrative Law Judge shall file an initial decision within 70 days after the filing of the last filed initial or reply proposed findings of fact, conclusions of law and order pursuant to [16 C.F.R.] § 3.46, within 85 days of the closing the hearing record pursuant to [16 C.F.R.] § 3.44(c) where the parties have waived the filing of proposed findings, or within 14 days after the granting of a motion for summary decision following a referral of such motion from the Commission").

¹⁶⁴ Rules of Practice for Adjudication Proceedings, 76 Fed. Reg. 45,338, 45,350; 12 C.F.R. § 1081.203.

¹⁶⁵ 12 C.F.R. § 1081.203(a).

¹⁶⁶ Rules of Practice, 60 Fed. Reg. 32,738, 32,741 (June 23, 1995).

¹⁶⁷ *Id.*

outside of the government. Therefore, it requested and has received public comment on its Adjudication Rules and has carefully considered commenters' suggestions in drafting improved final rules.¹⁶⁸

CONCLUSION

Congress created the Bureau to act as a twenty-first-century regulator that would promote a well-functioning market for consumer financial services and effective consumer protection. As the recent financial crisis illustrated, the stakes attached to accomplishing this mission are high, and the task is clearly formidable. The CFPB appreciates the significant scope and depth of this mandate. The Bureau has sought to meet this challenge by making policy decisions in light of the following four principles: (1) a market-based approach; (2) a focus on evidence-based analysis; (3) a commitment to encouraging and enabling robust public participation through transparency and innovative uses of technology; and (4) a recognition that history and other agencies' experience can provide invaluable guidance. This Article described, with several concrete examples, how these principles informed important Bureau decisions during the first eighteen months since Congress passed the Dodd-Frank Act. The Bureau intends to abide by these principles as it continues its work to foster fair, transparent, and competitive markets for consumer financial products and services and to empower consumers to take more control of their financial lives.

¹⁶⁸ See Rules of Practice for Adjudication Proceedings, 76 Fed. Reg. at 45,338.

