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TESTIMONY OF

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SUBCOMMITTEE ON FINANCIAL INSTITUTIONS

of the

COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

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[1] The views expressed in this testimony are my personal views and do not represent the views of Manatt, Phelps & Phillips, LLP, or any other organization with which I am or have been affiliated.

Chairman Barr, Ranking Member Foster, and members of the subcommittee, thank you for the opportunity to testify at today's hearing focused on the consumer protection landscape and the need for reforms to ensure that the regulatory structure protects consumers while providing financial services companies the stability and predictability to invest in innovation, expand access to credit, and reduce costs to consumers.

My name is Bryan Schneider. I am a partner at Manatt, Phelps & Phillips, a multidisciplinary, integrated national professional services firm focused on specific industry sectors, including all aspects of the financial services industry. As an attorney at the firm, my practice focuses primarily on providing regulatory compliance and enforcement advice concerning consumer finance matters.

I previously served as Associate Director for Supervision, Enforcement, and Fair Lending at the Consumer Financial Protection Bureau (CFPB), where I managed the team of professionals responsible for the oversight of the nation's largest depository institutions and the thousands of non-depository companies that provide the many financial services upon which American consumers rely. Prior to that I served as the Secretary of the Illinois Department of Financial and Professional Regulation, the chartering and licensing authority for all financial services companies operating in that State. Before entering public service, I was regulatory counsel to numerous highly regulated entities. I am grateful for the chance to share my views and answer your questions on this important topic. The views that I offer today are my own and not those of my law firm nor any other organization with which I am or have been affiliated.

Informing my positions are a set of fundamental beliefs based on my experiences on both sides of the regulatory divide:

- The overwhelming majority of businesses operating in the consumer financial services sector want to comply with the law and will strive diligently to do so, provided they understand the law and the obligations it imposes.
- American consumers want and need access to a broad and diverse group of options to access credit and the myriad other financial services available in the marketplace.
- Acting through rigorous compliance with the Administrative Procedure Act and related laws is the hallmark of lawful and careful regulation. The announcement of new regulatory requirements through blog postings, a Director's speech, or other sub-regulatory pronouncements calls into question the legitimacy of the agency and creates a situation where regulatory expectations change rapidly according to the vicissitudes of each incoming administration. This whipsawing is precisely what the APA was designed to prevent. When legal standards are changed without the deliberative process called for by the APA, it becomes increasingly difficult for smaller entities to support necessary compliance functions. This leads to a predictable decline in financial services innovation and an increase in the concentration of financial services in large entities.
- Financial regulation needs to be purged of the fantasy of perfection. Systemized modern data collection ensures that every mistake is recorded. This error data is invaluable to compliance professionals within financial services firms as they work to identify the root cause of errors and develop remediation plans to ensure that the mistakes are not repeated. Such data is also essential to regulators as they seek to better understand the marketplace and to develop rulemaking, supervisory, and enforcement strategies. But it is unreasonable to predicate regulatory action on

extremely low levels of noncompliance. Indeed, the CFPB is expressly charged when executing its rulemaking authority to consider the costs and benefits to consumers and service providers.[2] The CFPB should fulfill this mandate by studying and articulating tolerable levels of error that are inherent in any complex process.

- Risk-based supervision is key to the successful oversight of the financial services system. However, because supervision is by necessity a confidential process, some protest that supervision is little more than a way to brush problems under the rug and attempt to convert the supervisory process into a pipeline for enforcement investigation. I disagree entirely. The close relationship between a supervised entity and its regulator creates oversight opportunities that not only allow for the rapid identification of areas that require correction, and an equally fast consumer redress schedule, but also those that actually *prevent* consumer harm before it happens. Supervision requires cooperation between the supervised entity and the regulator that is likely to occur only if the supervised entity has confidence that a supervisory exam is not a civil enforcement investigation by another name. The CFPB should enhance guardrails to protect and enhance the supervisory process. Further, if its periodic publication *Supervisory Highlights* continues, the CFPB should recount instances of appropriate compliance protocols identified through its supervisory work.
- Enforcement is a tool that is essential to the CFPB's mission. I can speak from experience. During my tenure at the CFPB we brought dozens of enforcement actions. Indeed, during 2020 the CFPB initiated the fourth highest number of enforcement actions in its relatively brief history. But enforcement should be

[2] 12 U.S.C. 5512(b)(2)(A)(i)

reserved for situations in which the CFPB has exhausted other available options and has determined that it must proceed against a bad actor whose behavior has caused significant consumer harm and has allowed the entity to operate out-of-compliance to the detriment of its competitors that follow the law. And the aim of enforcement should be focused primarily on stopping the entity from engaging in the prohibited conduct and the prompt and fulsome remediation and redress of all consumer harm. Civil penalties unquestionably play a role in a reasoned enforcement regime, but eye-popping fines just for the sake of grabbing headlines should have no place. Moreover, enforcement should be undertaken only when the entity's actions violate clearly articulated statutory or regulatory requirements. When Congress has given the CFPB broader, less specific authority, such as the prohibitions against unfair, deceptive, or abusive acts or practices (UDAAP), its enforcement activity should proceed in an incremental manner that provides clarity for regulated entities through the careful development of the common law. And prior to a reasoned settling of the law, civil penalties, apart from consumer restitution and redress, should be assessed only when an entity has acted without good faith in complying with its legal obligations.

- In announcing enforcement actions, and indeed in all of its communications, a regulator, especially one with as tall of a bully pulpit as the CFPB, should refrain from gratuitous comments that go beyond the specific allegations of the complaint or facts relevant to the matter under discussion. It is worth calling to mind Rule 3.8 of the American Bar Association's Model Rules of Professional Conduct which instructs that a prosecutor must "except for statements that are necessary to inform

the public of the nature and extent of the prosecutor's action and service a legitimate law enforcement purpose, refrain from making extrajudicial comments that have a substantial likelihood of heightening public condemnation" of the entity that is subject to the legal proceeding. The CFPB is vested with significant power; it does not need to resort to bullying and name calling.

- The CFPB must rigorously abide by its statutory obligation to coordinate with federal and state prudential banking regulators. In establishing the CFPB, Congress was clear that it was to eliminate duplicative examination activity as much as possible. Indeed, Congress explicitly charged the CFPB "to coordinate its supervisory activities with the supervisory activities conducted by prudential regulators" and to use the supervisory reports of prudential regulators "to the fullest extent possible."[3] As bank partnerships with fintech companies increasingly join the consumer financial services marketplace, the CFPB's adherence to its statutory obligation to coordinate with federal banking regulators is perhaps the most straightforward way to create immediate, meaningful regulatory relief. Bank regulators know banks and bank programs. The CFPB should respect their expertise and not discharge its obligation to coordinate its supervisory activity by merely listening to the appropriate prudential regulator and then opening its own new, duplicative examination. Similarly, the CFPB is charged with coordinating its supervisory activities of non-depository institutions with appropriate state regulators.[4] This obligation should not be dismissed as a mere check-the-box

[3] 12 U.S.C. §§ 5514(b)(3) and 5514(b)(4)(A)
[4] 12 U.S.C. § 5514(b)(3)

activity that deprives State regulators the chance to meaningfully engage in the identification of entities to be examined and the scope of such reviews.

- Finally, and perhaps most importantly, the CFPB must respect its role as a regulator and not a policy maker. Even the CFPB's broad UDAAP authority cannot be contorted to achieve the policy goals of the current occupant of the CFPB Director's office apart from appropriately delegated congressional authority. The Supreme Court has been clear that Congress has no authority to delegate rulemaking authority concerning a "major question" to an administrative agency without providing an "intelligible principle" to which it must conform.[5] Recently, the CFPB has been prepared to press seemingly well beyond the grant of its authority by claiming, for example, that its "unfairness" authority allows it to create a regulatory regime concerning alleged discrimination outside of the offering or extension of credit notwithstanding Congress' clearly expressed demarcation of the CFPB's role in combatting discrimination in the financial markets.[6] Similarly, the CFPB has claimed the authority to regulate third-party payment processors that provide services exclusively to businesses and not consumers, despite the clear limitation of its jurisdiction to consumer-purpose financial products and services.[7]

It is difficult to object to the CFPB's statutory mission: "to implement and, where applicable, enforce Federal consumer financial law consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services and that

[5] *West Virginia v. Environmental Protection Agency*, 597 U.S. 697 (2022)
[6] Equal Credit Opportunity Act, 15 U.S.C. §§ 1691 *et seq.*
[7] CFPB Press Release, CFPB Launches Inquiry into Practices that Leave Workers Indebted to Employers (June 9, 2022)

markets for consumer financial products and services are fair, transparent, and competitive."[8] I make no quarrel with that purpose nor with the work of many of my former CFPB colleagues. But because that work occurs within an agency whose very structure seems designed to subvert constitutional principles, it will, in its current form, likely never be able to fulfill its dual mandate of consistent regulation and enforcement coupled with market stability. In my experience, regulators are justifiably concerned about not acting quickly or forcefully enough to protect the constituencies entrusted to them. Mistakes in fulfilling those responsibilities can be readily and painfully visible. But regulators should, in my judgment, be equally concerned about what they do not see if they act without proper care and deliberation. The innovation lost to agency action unmoored to principles of separation of powers and the rule of law can never be accounted for.

The question remains then what changes need to occur so that the CFPB's actions align with the specific mandates and authorities conferred on it by Congress:

- As an initial matter, in the wake of the recent multi-year blizzard of guidances, blog posts, interpretations, manual amendments, and speeches, the CFPB ought to conduct a comprehensive review and rescind or repeal those that fail to comply with the Administrative Procedure Act or that exceed that lawful authority granted to the CFPB in the Consumer Financial Protection Act.
- The arrival of a new Senate-confirmed Director will lead naturally to a review of the size and structure of the organization. Since 2020, the CFPB's annual transfer demand from the Federal Reserve has increased 36% and its headcount has expanded 17%.[9] It is not clear that these dramatic increases are necessary or

[8] 12 U.S.C. § 5511(a)
[9] Financial Report of the Consumer Financial Protection Bureau for Fiscal Year 2024, pages 8-9

sustainable. And it is worth noting that each dollar extracted by the CFPB is one less dollar the Federal Reserve is able to remit to the Treasury for the reduction of our public debt.

- Furthermore, it is not clear that these additional resources have been appropriately allocated. The CFPB is often said to possess four tools – rulemaking, supervision, enforcement, and education. Yet for the most recently completed fiscal year, the CFPB committed a mere 8% of its resources to consumer response and education.[10] American consumers are intelligent and sophisticated. If consumers were armed with thorough educational materials from the CFPB, considerable consumer harm could be *prevented* from occurring, thus reducing the need for other regulatory resources.
- The CFPB should review its staffing and control structure to ensure that supervision and enforcement are two independent tools. The involvement of enforcement staff in the planning or execution of supervisory exams should be prohibited.
- In addition to generally refraining from rude and petulant comments about outside persons and companies, the CFPB should ensure that press releases concerning settlements are reviewed by the affected entity.

However, these internal reforms may not be fully sufficient. The only way to ensure stability across executive administrations is for Congress to act to ensure the agency is accountable to it and the American people:

[10] Id. at 9

- While the Supreme Court has recently held that the CFPB's current funding structure is constitutional, that by no means suggests that it is optimal or even salutary. Indeed, the CFPB's budget is presently subject to no congressional oversight. As a result, it goes without saying, the CFPB's priorities are in no meaningful way subject to the priorities of the American people represented in Congress. Considerable ink has been spilled on just how unusual the CFPB's funding mechanism is within the Federal government, but, speaking as a former State regulator, it is to my eye inconsistent with fundamental principles of separation of powers and ordered liberty. While serving in the government of the State of Illinois, I, like my fellow state regulators in their state Capitols, had to request appropriations for our operations from the Illinois General Assembly. Having your work examined and evaluated by appropriations committees is not something generally welcomed, but it is assuredly the only reliable way for the legislature to ensure that a regulatory agency is tying its activities to the authority granted to it. And despite some occasional messiness, Illinois legislators consistently discharged their duties and provided our agency with the resources necessary to do its work. The same can be expected from Congress.
- Congress should consider the need for the establishment and strengthening of limitations periods concerning both the issuance of Civil Investigative Demands and underlying conduct. Unchecked, the CFPB is free to return in the future to pursuing conduct going back a decade or more.[11]

[11] *E.g., CFPB v. Harbour Portfolio Advisors, LLC*, No. 16-14183. 2017 WL 631914 (E.D. Mich Feb. 16, 2017)

- Congress should evaluate the need to cabin the CFPB's use of its UDAAP authority, especially concerning the untested abusive standard, in situations when the entity has acted in good faith with respect to its compliance obligations.

Thank you, members of the committee, for the chance to speak on these critical issues. It is my hope that through both internal and external reform, the CFPB may yet be positioned to fulfill its mandate to both protect consumers and ensure that they have the innovative products and services that American ingenuity is prepared to deliver.