Statement by

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Subcommittee on the Constitution and Limited Government

"Government Litigation and the Need for Reform"

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Chairman Johnson, Ranking Member Scanlon, and members of the Subcommittee, thank you for the opportunity to discuss the federal government's civil litigation practices and authorities. I am Todd Phillips, Principal with Phillips Policy Consulting. I previously served as an attorney advisor with the Federal Deposit Insurance Corporation and the Administrative Conference of the United States, and as counsel with what was then known as the House Oversight and Government Reform Committee. My policy focus is at the intersection of administrative law and financial regulation.

My testimony today will focus on my concerns regarding two enforcement bills the Judiciary Committee is considering: H.R. 3446, the Sunshine for Regulatory Decrees and Settlements Act of 2023, and H.R. 788, the Stop Settlement Slush Funds Act of 2023. In my view, these bills are solutions in search of problems and could ultimately result in wasteful government spending.

I note at the outset that Article II of the U.S. Constitution places with the executive branch the responsibility to "take Care that the Laws be faithfully executed,"[1] which includes the authority to initiate or end civil litigation under duly enacted statutes pursuant to its officers' prosecutorial discretion.[2] It makes sense for agency officials to have this authority: As the Supreme Court noted in *Heckler v. Chaney*, an agency enforcement decision "often involves a complicated balancing of a number of factors which are peculiarly within its expertise" such that agency officials are "far better equipped" than others "to deal with the many variables involved in the proper ordering of its priorities."[3]

If enacted, these bills would prevent the agency officials who know individual cases inside-and-out from using their expert judgment and prosecutorial discretion to ensure that the government operates efficiently. My time as a congressional staffer taught me to be concerned about waste, fraud, and abuse within the government, and I am concerned that enacting these bills could result in unnecessary waste.

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[1] U.S. Const., Art. II, § 3.

[2] *See* Heckler v. Chaney, 470 U.S. 821, 832 (1985) ("we recognize that an agency's refusal to institute proceedings shares to some extent the characteristics of the decision of a prosecutor in the Executive Branch not to indict -- a decision which has long been regarded as the special province of the Executive Branch.").

[3] *Id*., at 831–32.

H.R. 3446, the Sunshine for Regulatory Decrees and Settlements Act of 2023

This bill would, if enacted, empower opponents of particular regulatory safeguards—both inside and outside the government—to perpetuate unlawful agency inaction.

Congress frequently enacts statutory deadlines for agencies to complete new regulations, yet agencies often fail to complete rulemakings pursuant to those statutory mandates. One example of delayed rulemakings relevant to my work is that which was required by Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.[4] Section 956 required several financial regulatory agencies to jointly enact a rule "prohibit[ing] any types of incentive-based payment arrangement, or any feature of any such arrangement, that the regulators determine encourages inappropriate risks by covered financial institutions…that could lead to material financial loss to the covered financial institution."[5] The agencies published a draft of this rule in 2016 that, if finalized, would have encouraged institutions to engage in prudent risk management practices such that bank executives do not take risky bets that put their firms at significant risk.[6] Further, it would have allowed firms to recover incentive compensation provided for activities that ultimately produced losses.[7]

Congress required that rule be enacted by spring 2011, yet 12 years later it has still not been completed.[8] Earlier this year, the nation faced a banking crisis caused, in part, by insufficient risk management practices, which required two government agencies and the Treasury Secretary to declare the failures of Silicon Valley Bank and Signature Bank systemic risks to the financial system.[9] While this rule, if finalized, may not have fully stopped the activities that led to these losses, it would have permitted the FDIC to recover incentive compensation from top executives from the two institutions, as the FDIC has stepped into the shoes of the institutions and used the rule to engage in clawbacks.[10]

While the failure to enact congressionally mandated regulations left financial markets subject to abuse in this instance, unwritten rules similarly leave the environment and workers unprotected. It also, as the D.C. Circuit Court of Appeals has noted, "saps the public confidence in an agency's ability to discharge its responsibilities and creates uncertainty for the parties, who must incorporate the potential effect of possible agency decisionmaking into future plans."[11] For those and other reasons, the Administrative Procedure Act requires courts "to compel agency action

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[4] Pub. L. No. 111-203 § 956, 124 Stat. 1905 (2010), *codified at* 12 U.S.C. § 5641.
[5] 12 U.S.C. § 5641(b)(2).
[6] *See* Incentive-Based Compensation Arrangements, 81 Fed. Reg. 37669, 37712 (June 10, 2016) ("Incentive-based compensation should support prudent risk-taking").
[7] See *id*., at 37679 ("the proposed rule would require a … covered institution to include clawback provisions in the incentive-based compensation arrangements for senior executive officers and significant risk-takers").
[8] *See* 12 U.S.C. § 5641(b) (requiring the rule within nine months of the statute's enactment, or April 2011).
[9] *See Joint Statement by the Department of the Treasury, Federal Reserve, and FDIC* (Mar. 12, 2023), https://www.fdic.gov/news/press-releases/2023/pr23017.html (announcing that the systemic risk exception under the Federal Deposit Insurance Act was used for the failures of Silicon Valley Bank and Signature Bank).
[10] When resolving a failing bank, the FDIC "'steps into the shoes' of the failed [bank], ... obtaining the rights 'of the insured depository institution' that existed prior to receivership." O'Melveny & Myers v. FDIC, 512 U.S. 79, 86 (1994) (internal citation omitted). Accordingly, if a bank had authority to clawback compensation prior to its failure pursuant to a regulation, the FDIC, as receiver, would have that authority as well.
[11] Potomac Electric Power Co. v. ICC, 702 F.2d 1026, 1034 (D.C. Cir. 1983).

unlawfully withheld or unreasonably delayed."[12] The Supreme Court has held that this authority extends to instances in which an "agency is compelled by law to act within a certain time period."[13] Often, these "deadline lawsuits" are the harmed parties' only available recourse as agencies delay rulemakings by nine years,[14] twelve years,[15] or longer.

Court-ordered and -approved settlement agreements and decrees stemming from these lawsuits have no bearing on the substance of the rules agencies complete. In a 2014 study of Environmental Protection Agency rules issued following settlements in deadline lawsuits, GAO found that "[t]he terms of the settlements in these deadline suits established a schedule to issue a statutorily required rule(s) or to issue a rule(s) …. None of the seven settlements included terms that finalized the substantive outcome of a rule."[16] Similar results were found in a 2017 GAO study of Fish and Wildlife and National Marine Fisheries Services rules, which found that "the settlement agreements did not affect the substantive basis or procedural rulemaking requirements the Services were to follow…."[17] That is, these settlements merely required agencies to finalize regulations by some future date because the agency had violated a congressional directive.

Instead of encouraging the executive branch to comply with statutory requirements, this bill would impose a barrage of duplicative, burdensome, and time-consuming hurdles that apply to settlements and decrees, slowing down the rulemaking process and preventing federal law from being implemented. It would subject any "regulatory" decree or settlement to a lengthy new notice-and-comment process, even though agencies are already required to engage in a notice-and-comment process.[18] It would also permit intervention by any individual who declares they would be affected by the regulatory action in question and include that party in additional court-supervised settlement talks, even though individuals aggrieved by deadline lawsuits' rules may already challenge agencies' rulemaking procedures and rules' substance in pre-enforcement litigation.[19] And, ironically, because of the additional hurdles, this bill would make the reason deadline litigation is brought in the first case—delayed agency action—even worse.

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[12] 5 U.S.C. § 706(1).
[13] Norton v. S. Utah Wilderness Alliance, 542 U.S. 55, 65 (2004)
[14] *See, e.g.*, In re Blue Water Network and Ocean Advocates, 234 F.3d 1305, 1307 (D.C. Cir. 2000) ("order[ing] the Coast Guard to conduct prompt rulemaking" nine years after the statute required it be completed); Pub. Citizen Health Rsch. Grp. v. Chao, 314 F.3d 143, 153 (3d Cir. 2002) **("**We find extreme OSHA's nine-year (and counting) delay since announcing its intention to begin the rulemaking process, even relative to delays other courts have condemned in comparable cases.")**.**
[15] *See, e.g.*, Prometheus Radio Project v. Federal Communications Commission, 824 F.3d 33, 48 (3d Cir. 2016) ("With 12 years having passed…, we conclude that the Commission has had more than enough time to reach a decision on the eligible entity definition.").
[16] U.S. Gov't Accountability Office, GAO-15-34, Environmental Litigation: Impact on Deadline Suites on EPA's Rulemaking Is Limited (2014).
[17] U.S. Gov't Accountability Office, GAO–17–304, Environmental Litigation: Information on Endangered Species Act Deadline Suits (2017).
[18] *See* 5 U.S.C. § 553 (articulating the notice and comment process).
[19] *See* Abbott Lab'ys v. Gardner, 387 U.S. 136, 141 (1967) (explaining that "only upon a showing of 'clear and convincing evidence' of a contrary legislative intent should the courts restrict" pre-enforcement review of agency rules).

Rather than endeavoring to slow down necessary, congressionally mandated rulemakings, Congress should instead be conducting oversight to determine why agencies were violating its mandates in the first instance.

H.R. 788, the Stop Settlement Slush Funds Act of 2023

This bill would place arbitrary limits on how the federal agencies may enter into settlement agreements that arise from enforcement actions brought against companies that have violated federal laws. Its cumulative effect would be to deter agencies from the efficient resolution of civil complaints through settlement agreements.

When government agencies litigate, all parties may find that settlement agreements are the most effective and efficient way of resolving the issues and of improving the lives of affected non-parties. In the aftermath of the 2007-08 financial crisis, for example, the Department of Justice (DOJ) sued large financial institutions that had securitized, packaged, and sold mortgage-backed securities to investors.[20] These institutions had little to no interactions with individual homeowners, but their demand for mortgages to securitize incentivized the origination of a large number of subprime loans.[21] Clearly, homeowners were harmed by these behaviors, but the banks were not the proximate cause of the harm.

In settlement agreements with some of these banks, the DOJ secured "consumer relief" provisions that required remediation of the harms that resulted from the banks' conduct.[22] The settlement with Citigroup, for example, required $2.5 billion in various forms of consumer relief, including principal forgivingness, loan modifications, community reinvestment and stabilization initiatives, foreclosure prevention programs, and affordable housing resources.[23] JPMorgan Chase's settlement required $4 billion in consumer relief.[24]

Importantly, without the ability to enter into settlement agreements that provided remediation to impacted victims, there would have been no guarantee that the banks would have settled. The DOJ could have been forced to trial, wasting time, resources, and taxpayer dollars, and delaying

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[20] *See, e.g.*, DEP'T OF JUSTICE, JPMORGAN CHASE & CO. STATEMENT OF FACTS 6–8 (2013), http://www.justice.gov/iso/opa/resources/9432013111915103199062 2.pdf (describing the activities for which the bank was sued).

[21] *See* FINANCIAL CRISIS INQUIRY COMMISSION, THE FINANCIAL CRISIS INQUIRY REPORT xxiv (2011) ("[E]ach step in the mortgage securitization pipeline depended on the next step to keep demand going. From the speculators who flipped houses to the mortgage brokers who scouted the loans, to the lenders who issued the mortgages, to the financial firms that created the mortgage-backed securities, collateralized debt obligations (CDOs), CDOs squared, and synthetic CDOs: no one in this pipeline of toxic mortgages had enough skin in the game.").

[22] See, e.g., Dep't of Justice, Justice Department, Federal and State Partners Secure Record $7 Billion Global Settlement with Citigroup for Misleading Investors About Securities Containing Toxic Mortgages (July 14, 2014), http://www.justice.gov/opa/pr/justice-department-federal-and-state-partners-secure-record-7-billion-global-settlement.

[23] *Id.*

[24] Dep't of Justice, *Justice Department, Federal and State Partners Secure Record $13 Billion Global Settlement with JPMorgan for Misleading Investors About Securities Containing Toxic Mortgages* (Nov. 19, 2013), https://www.justice.gov/opa/pr/justice-department-federal-and-state-partners-secure-record-13-billion-global-settlement.

timely enforcement of the law and the provision of relief for victims—if they would have received any relief at all.

Financial regulation is not the only area in which such settlements are permitted and appropriate. As witnesses have previously testified before the House Judiciary Committee, the Environmental Protection Agency makes significant use of similar provisions in settlements under the Clean Water Act or the Clean Air Acts.[25]

H.R. 788 would prohibit settlement agreements like those the DOJ entered into with the financial institutions, as the harms to borrowers were not "directly *and* proximately caused by the party making the payment."[26] As the DOJ itself noted about a previous version of this bill, it would "impede the government's ability to address the root causes of violations and establish effective remedies that are effective retrospectively (correcting noncompliance) and prospectively (addressing root causes of noncompliance to prevent recidivism)."[27]

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In sum, these bills are solutions in search of problems and, if enacted, could result in a more inefficient government. They would prevent the agency officers and staff who know individual cases inside-and-out from using their expert discretion to ensure that the government operates as efficiently and effectively as possible. These officials, as I noted before, are "far better equipped" than others "to deal with the many variables involved in the proper ordering of [agency] priorities."[28] Congress should endeavor to conduct oversight, rather than enacting dictates that apply to every agency lawsuit.

Thank you, and I am happy to answer any questions.

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[25] *See* H.R. 5063: Hearing before the H. Subcomm. on Regulatory Reform, Commercial and Antitrust Law, 114 Cong. 43 (2016) (Testimony of David M. Uhlmann) (describing a prosecution under the Clean Water Act that resulted in $1 million in restitution and community service).
[26] H.R.788 § 2(a), 118th Cong.
[27] H. Rept. 114-694 (2016) at 36.
[28] Heckler v. Chaney, 470 U.S. 821, 831–832 (1985).