UNITED STATES OF AMERICA
Before the
CONSUMER FINANCIAL PROTECTION BUREAU

ADMINISTRATIVE PROCEEDING File No. 2015-CFPB-0029	)
In the matter of:	) ORAL ARGUMENT REQUESTED
INTEGRITY ADVANCE, LLC and JAMES R. CARNES	)

RESPONDENTS' REPLY BRIEF IN SUPPORT OF THEIR
<u>MOTION TO DISMISS THE NOTICE OF CHARGES</u>

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The Bureau ignores the fact that the Consumer Financial Protection Act ("CFPA"), Supreme Court precedent, and the Constitution prevent it from bringing this case. Indeed, the Bureau does not try to defend its basis for jurisdiction here. The CFPB also asserts, incorrectly, that no statutes of limitations apply to any of its claims. Finally, the Bureau fails to plead a Truth in Lending ("TILA") claim. The Court should dismiss the Notice of Charges in its entirety.[1]

ARGUMENT

I. The Bureau Has Never Had Enforcement Authority As To Respondents

The Bureau has no authority to pursue this action.[2] Instead of addressing this fact, the Bureau mischaracterizes Respondents' argument, which is summarized as follows:

- Section 1066 of the CFPA provides (to the Secretary of the Treasury) *only* authority over the transferred functions of the Bureau, until a Director is lawfully appointed. 12 U.S.C. § 5586. The Inspectors General of two federal agencies—the Department of Treasury, which exercised statutory authority in the absence of a confirmed Director and the Federal Reserve, which now houses the Bureau—noted this in a response to a Congressional query. *See* Respondents' Memorandum in Support of Motion to Dismiss 6–8 [hereinafter "Mem."]. The Bureau ignores the plain language of Section 1066 and the Inspectors General response.

- In *NLRB v. Noel Canning*, 134 S. Ct. 2550, 2577–78 (2014), the Supreme Court held that the nature of Director Cordray's recess appointment was unconstitutional. Thus, the Bureau could not assume any newly-created authorities under the CFPA, including the authority to regulate and enforce the laws as to nonbanks, before there was a lawfully-appointed Director, which happened on July 16, 2013. The Bureau ignores Supreme Court precedent.

- Director Cordray's August 27, 2013 ratification cannot cure the Bureau's lack of authority as to nonbanks. Indeed, it is well-established law that "a ratifying party must have the legal authority to perform the act 'at the time the ratification was made.'" Mem. at 12 (quoting

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[1] The Bureau concedes that "Counts III, IV, and VII are limited to deceptive or unfair acts and practices that occurred on or after July 21, 2011." Opp'n at 14; s*ee also* Notice ¶¶ 62–77, 88–94. Although, the Court should dismiss the CFPA claims in their entirety due to a lack of jurisdiction, in the alternative, Respondents request that the Court dismiss these counts as to conduct that predates July 21, 2011 and require that the Bureau re-plead its Notice to this effect.

[2] Respondents' argument here is especially discrete. Indeed, this case is likely one of the few cases where nonbanks that are the subject of an enforcement action ceased all conduct that would have qualified them as "covered persons" prior to the vesting of the Bureau's nonbank authority.

FEC v. NRA Political Victory Fund, 513 U.S. 88, 98 (1994). Respondents were not "covered persons" in August 2013. Here, too, the Bureau ignores Supreme Court precedent.

- Respondents are not currently covered persons, and have never engaged in any "covered person" conduct at a time when the Bureau had authority to regulate or enforce the law as to nonbanks. The Bureau responds that it now has nonbank authority and that this suffices. The Bureau ignores the CFPA's plain language, Supreme Court precedent and the Constitution.

A. The Bureau Has Only Ever Had The Authority Vested In It By The CFPA

"[A]n agency's power is no greater than that delegated to it by Congress." *Lyng v. Payne*, 476 U.S. 926, 937 (1986) (noting that an agency's exercise of authority must conform to Congressional intent). The CFPA is clear that two specific conditions must be met before the Bureau could have assumed any authority as to nonbanks. First, the statute's effective date of July 21, 2011 must have passed, *and* second, the Bureau must have had a lawfully-appointed Director who had taken office. *See* 12 U.S.C. §§ 5491(b), 5586. In a mere footnote, the Bureau states that it "disagrees" that its authority as to nonbanks took effect only once a Director was lawfully appointed. Opp'n at 5 n.4.[3] It, of course, cites no law to support this position. Non-transfer authorities—including those concerning nonbanks—were not vested with the Bureau until there was a lawfully-appointed Director. The CFPA's July 21, 2011 effective date does not, on its own, confer nonbank jurisdiction.

[3] While the Bureau's argument here ignores this legal issue, the agency's conduct in January 2012 conceded the limitations of Section 1066. For example, on January 5, 2012, one day after his recess appointment, Director Cordray stated that "[o]ne of the difficulties we faced up to now was that, w*ithout a director, we were unable to address all the problems we were created to tackle* . . . ." Prepared Remarks by Richard Cordray, Director of the Consumer Financial Protection Bureau at The Brookings Institution, Washington, D.C., (Jan. 5, 2012), *available at* http://www.consumerfinance.gov/newsroom/remarks-by-richard-cordray-at-the-brookings-institution/ (emphasis added). Also on January 5, 2012, the Bureau began its supervisory program for nonbanks, stating that it "*now ha[d] the authority to oversee nonbanks*." Press Release, CFPB Launches Nonbank Supervision Program ("Effective Immediately") (Jan. 5, 2012) (emphasis added), http://www.consumerfinance.gov/blog/the-cfpb-launches-its-nonbank-supervision-program/.

The statutory and the Constitutional framework for delegating authority to a government agency requires that a statute be effective and also that an Officer of the United States assume the statutory authority before that authority can be lawfully applied. *See Buckley v. Valeo*, 424 U.S. 1, 124–41 (1976), *superseded by statute*, *on other grounds*. Indeed, the "Constitution does not leave to speculation who is to administer the laws enacted by Congress; the President, it says, 'shall take Care that the Laws be faithfully executed,' . . . personally and through officers whom he appoints." *Printz v. United States*, 521 U.S. 898, 922 (1997).

The Bureau ignores the Appointments Clause and the CFPA. In fact, taken to its logical extreme, the Bureau's argument eviscerates the Appointments Clause. Adopting the Bureau's position means that it makes no difference whether Director Cordray was appointed on July 21, 2011 or July 16, 2013 (or, indeed, on November 17, 2016, a day before the Bureau filed the present case). But the Appointments Clause is not a mere "frivolous" concern for "etiquette or protocol." *Buckley*, 424 U.S. at 125. Section 1066 of the CFPA mandates that there be a lawfully-appointed Director in order for the agency's full powers and authorities to be effective. Before July 16, 2013, there was no individual who had been appointed according to the Appointments Clause, as necessary, to carry out the agency's full authorities.

The CFPA is also clear that Bureau Director is a "principal officer" who is "selected by the President with the advice and consent of the Senate." *Id.* at 132; *see also* 12 U.S.C. § 5491(b). This is because the CFPA creates specific agency authorities that are "substantial powers" and "may be discharged only by persons who are 'Officers of the United States' within the language" of the Appointments Clause. *Printz*, 521 U.S. at 922–23, s*ee also Edmond v. United States*, 520 U.S. 651, 662 (1997). In other words, the Bureau's full authorities could not be assumed until a Director had been lawfully appointed. To ignore this requirement is to undermine the separation of powers balance between the Congress and the Executive Branch. This would "permit an agency to expand its power in the face of a congressional limitation on its jurisdiction," which in turn would effectively "grant to the agency power to override Congress" and the role of the President in appointing officers of the United States. *La. Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 374–75 (1986). The Bureau's argument that it can bring this case regardless of whether or when there was a lawfully-appointed Director in place is wrong as a matter of law.

The Bureau's other argument that its lack of jurisdiction does not matter because the Bureau now has the authority to pursue enforcement actions against nonbanks is equally wrong. Here, the Bureau's arguments rely only on mischaracterizations of Respondents' legally correct arguments. First, contrary to the Bureau's contention, Respondents never argue that the Bureau may take enforcement actions only against *ongoing* illegal activity or that a requisite for a CFPA claim is that a party be a current "covered person." Rather, Respondents assert that, as a matter of law, an entity or person must have been engaged in conduct that meets the definition of covered person "*at some point in time when the Bureau had authority as to that conduct*." Mem. at 16. The Bureau does not contest Respondents' actual point, because it cannot.

Second, the Bureau mischaracterizes Respondents' arguments about the plain language of the "covered person" definition.[4] The Bureau conflates the present tense definition of "covered person," with a provision in the CFPA that governs the agency's cease and desist authority, which has nothing to do with this matter.[5] Here, the CFPB's apparent logic also

[4] The Bureau cites two cases, Opp'n at 9 n.7, that do not contradict Respondents. Neither case is relevant. *McNeill v. United States* stands for the proposition that criminal defendants are sentenced under statutes as written at the time of their conviction. 131 S. Ct. 2218, 2223 (2011). *Rajabi v. Attorney General* holds that an *expressly retroactive* antiterrorism law applies retroactively, despite the use of a present-tense verb. 555 F. App'x 251, 256 (3d Cir. 2014) (unpublished).

[5] It bears pointing out that the language quoted by the CFPB regarding conduct that a "covered person" has "engaged in" stems from its authority to bring a *cease and desist* proceeding under 12

undermines core principles of due process as the Bureau seeks to apply legal consequences to an actor over which it never had authority and also contradicts well-established principles that counsel against the retroactive application of the law. Indeed, the Bureau acknowledges these principles when it concedes that its UDAAP claims reach only conduct that happened on or after July 21, 2011. Respondents have never engaged in conduct over which the Bureau has had authority. And, on and after July 16, 2013 when Director Cordray was confirmed, Respondents were not "covered persons." The Notice should be dismissed in its entirety, and, if nothing else, the Court should dismiss Counts II, III, IV, VI, and VII, the Bureau's CFPA claims.

II. The Bureau Misstates The Applicable Statute Of Limitations Provisions

The Bureau asserts that its claims are not subject to any statutes of limitations because the agency is pursuing an administrative case and not one in federal district court. The Bureau seeks the widest remedies without the accompanying limitations. The CFPB has complete and sole discretion when deciding whether to bring a case in its administrative forum or in federal court. *See* Opp'n at 12. And, unlike any other agency whose case law it cites, the Bureau may seek the same remedies in either forum. *Id.*; 12 U.S.C. § 5565. Statutes of limitations must be consistently applied; it should not matter where the CFPB chooses to pursue litigation.

A. The Bureau's CFPA Claims Are Time-Barred And Must Be Dismissed

Section 1054 of the CFPA "directly sets a time limit" for the bringing of CFPA claims; thus, the Bureau erroneously relies on cases that address "borrowed" time limits. *See* Opp'n at 11 (quoting *Alden Mgmt. Servs. Inc. v. Chao*, 532 F.3d 578, 582 (7th Cir. 2008) (discussing a time limitation "borrowed" from another statute); *Intercounty Const. Corp. v. Walter*, 422 U.S. 1,

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U.S.C. § 5563(b)–*not* its authority to bring an administrative adjudication action under § 5563(a). Here, the Bureau's citation to its cease and desist authority is bewildering. The Notice does not indicate that the Bureau seeks a cease and desist order (which typically applies to forestall prospective conduct or provide an immediate remedy for violations).

4 (1975) (discussing the effect of an amended limitation on an unrelated limiting provision).[6] Specifically, the CFPA states that "no *action*" may be brought for a violation after three years from the date of discovery. 12 U.S.C. § 5564.

The term "action" in the CFPA must be read to refer to any enforcement action taken by the Bureau, not only those brought in district court, as the Bureau contends. Indeed, if the Court adopts the Bureau's "action" argument, then the Bureau has no authority to pursue the UDAAP claims in this case or any other administrative litigation. Section 1031, which is called "Prohibiting Unfair, Deceptive, or Abusive Acts or Practices," specifically provides that "[t]he Bureau may take any *action* authorized under part E [Enforcement Powers] to prevent a covered person or service provider from committing or engaging in an unfair, deceptive, or abusive act or practice under Federal law . . ." *Id.* § 5531 (emphasis added); *see also* Notice ¶ 70 (citing § 5531(a)). It follows that if "action" means only federal district court litigation, then the CFPA does not authorize the Bureau's UDAAP claims in this case. The CFPA's plain language also states that the Bureau may only seek to recover "costs in connection with prosecuting [an] *action*." 12 U.S.C. § 5565(b) (emphasis added). Similarly, if the Court adopts the Bureau's "action" argument, then the Bureau cannot seek to recover any costs here.

The Bureau's arguments, of course, are contradictory and also counter well-established canons of statutory construction. It is well-established that "[a] term appearing in several places

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[6] The Bureau also relies on other inapposite cases. *See* Opp'n at 11 n.9. For example, the Bureau cites *Rentacolor, Inc. et al.*, No. 9163, 1984 WL 56583 (F.T.C. Apr. 16, 1984), for the holding that "no statute of limitations attach[] to" the Federal Trade Commission's administrative proceedings. Opp'n at 11. But the FTC's administrative proceedings are different from the proceeding here. For example, when it proceeds administratively, the FTC is not able to obtain civil money penalties, and if the FTC seeks monetary redress, the FTC can only obtain that remedy from district court *after* disposition of an administrative action or by proceeding in district court in the first instance. It follows logically that the statute of limitations that applies to the FTC in district court would not apply in its administrative forum. In contrast, the Bureau is able to obtain monetary relief and civil money penalties in this administrative forum, without also proceeding in district court.

in a statutory text is generally read the same way each time it appears." *Ratzlaf v. United States*, 510 U.S. 135, 143 (1994).[7] Thus, the word "action" either applies to the administrative forum, or the Bureau has no authority here to pursue a UDAAP claim or to recover costs. The Bureau cannot have it both ways.

The Bureau further relies erroneously on *PHH Corp., et al.*, File No. 2014-CFPB-0002, Decision of the Director (Jan. 29, 2014), even though that case only concerns the Real Estate Settlement Procedures Act ("RESPA"). Indeed, the ALJ's statute of limitations holding in that case applies only to RESPA's statute of limitations (12 U.S.C. § 2614). *See PHH Corp., et al.*, Order Denying Motion to Dismiss 8–9 & n.2 (Mar. 13, 2014).[8] The Bureau also relies incorrectly on *BP America Production Co. v. Burton*, 549 U.S. 84 (2006). In *Burton,* the question about the word "action" arose in the context of a statute that uses the phrase "right of action" in close proximity to the terms "complaint" and "money damages." *See id.* at 91, 95. In fact, the *Burton* court relied heavily on the use of the word "complaint" which specifically initiates a lawsuit filed in court, as opposed to a notice of charges. *See id*. at 91–92. It follows that the *Burton* Court held that the word "action" in that case referred to civil lawsuits filed in federal district court. The CFPA has no such language and the term "action" is used throughout the CFPA but never in the phrase "right of action." *See id.* at 91 (discussing 28 U.S.C. § 2415).[9]

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[7] Moreover, Sections 1054(a) and (f) specifically use the term "civil action" and not just the word "action" to refer to district court litigation. *See* 12 U.S.C. § 5564(a) ("If any person violates a Federal consumer financial law, the Bureau may . . . commence a *civil action* . . . ."); *Id.* § 5564(f) ("Any *civil action* brought under this title may be brought in a United States district court . . . .") (emphasis added).

[8] Since the question of whether the CFPA's statute of limitations applies to claims brought under the *CFPA itself* was not before the court in *PHH Corp.*, any statements on this point are merely dicta.

[9] A broader use of the term "action" is not without precedent in the Supreme Court. *See, e.g.*, *Alexander v. Sandoval*, 532 U.S. 275, 289 (2001) (referring to an agency's decision to terminate funding to a program for regulatory violations as an "enforcement *action*") (emphasis added).

The Bureau attempts to extend *Burton* to a different statute with plainly different language to justify a tortured reading of the CFPA.

The CFPB also ignores clear case law providing that the date of discovery means the date when an agency was likely to have known of the conduct at issue through reasonable due diligence. *See Gabelli v. SEC*, 133 S. Ct. 1216, 1221 (2013). If "date of discovery" means when the Bureau completes an investigation or even when a Notice of Opportunity to Response and Advise ("NORA") response is filed, as the Bureau asserts, then the Bureau could always delay the running of the statute of limitations. Such an outcome, of course, would fail to provide requisite notice to would-be defendants about whether and for what they might face potential liability. The Supreme Court has emphasized the vital "importance of time limits on penalty actions," recalling Chief Justice Marshall's words that it "'would be utterly repugnant to the genius of our laws' if actions for penalties could 'be brought at any distance of time.'" *Gabelli*, 133 S. Ct. at 1223 (quoting *Adams v. Woods*, 2 Cranch 336, 342, 2 L.Ed. 297 (1805)). "Statutes of limitations . . . represent a pervasive legislative judgment that it is unjust to fail to put the adversary on notice to defend within a specified period of time and that 'the right to be free of stale claims in time comes to prevail over the right to prosecute them.'" *United States v. Kubrick*, 444 U.S. 111, 117 (1979) (citations omitted).[10] The Bureau's argument undermines the CFPA's express statute of limitations provision, and its CFPA claims are time-barred.

[10] Principles of fairness, notice, and due process are central to the concept of statutes of limitations. *See Burnett v. N.Y. Cen. RR. Co.*, 380 U.S. 424, 428 (1965) (a statute of limitations is "primarily designed to assure fairness to defendants"); *Armada De La Republica Arg. v. Yorkington P'ship*, 1995 U.S. Dist. LEXIS 1317, 1995 WL 46394, at *18 (D.D.C. Jan. 27, 1995) (stating that it is "clear that the issue of fairness should be the animating consideration in any statute of limitations inquiry"); *Robinson-Smith v. Gov't Employees Ins. Co.*, 424 F. Supp. 2d 117, 121 (D.D.C. 2006) (same). Indeed, it is axiomatic that statutes of limitations exist in part to ensure that defendants have due process and fair notice. A different outcome would "[l]eave defendants exposed to Government enforcement action . . . for an additional uncertain period into the future. Repose would hinge on

B. The TILA And EFTA Claims Are Also Time-Barred And Must Be Dismissed

The Bureau's own administrative precedent indicates that "the CFPB must follow the statute of limitations of the statute it is enforcing." *3D Resorts-Blugrass, LLC*, File No. 2013-CFPB-0002, Order on Aff. Def. (Jul. 12, 2013). Further, TILA's (and by extension, EFTA's) one-year statute of limitations have already been applied to the Bureau. The court in *ITT* held that TILA's one-year statute of limitations applies to the Bureau's enforcement actions in federal court, and EFTA has the same limiting language as TILA. *CFPB v. ITT Educ. Servs., Inc.*, No. 1:14-cv-00292-SEB-TAB, 2015 WL 1013508, *33 (S.D. Ind. Mar. 6, 2015); *see also* Mem. at 20.

In dicta, the *ITT* court indicated that the result might be different in the administrative forum *of the prudential banking regulators* (a key factor that the Bureau's brief conveniently elides, *see* Opp'n at 14). *See ITT*, 2015 WL 1013508 at *33. But the prudential banking regulators cannot even pursue enforcement cases in federal district court. Moreover, the *ITT* court's dicta specifically cites guidance from the Office of the Comptroller of the Currency ("OCC") concerning that agency's authority to pursue administrative cease and desist actions, which is not relevant here. *See id.* The Bureau's TILA and EFTA claims are time-barred and should be dismissed.

III. The Bureau Fails To State A TILA Claim

Integrity Advance's TILA disclosures complied with Regulation Z's technical requirements and accurately reflected the terms of the legal obligation. A renewal that extends the term of a loan after consummation and associated renewal fee is not required to be included in the disclosures. *See* 12 C.F.R. §§ 1026.17(c), (e). The Bureau ignores TILA's regulatory framework (which does not require creditors to assume that post-consummation renewals and

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speculation about what the Government knew, when it knew it, and when it should have known it." *See Gabelli*, 133 S. Ct. at 1223.

extensions of short-term loans will occur when making TILA disclosures). The Bureau asks the Court to hold, as a matter of law, that a single-installment loan is really a multi-installment loan if the contract contains a renewal provision that automatically applies if the consumer does not pay off the loan by its original contractual due date. This is inconsistent with Regulation Z's treatment of post-disclosure events and must be dismissed accordingly. *See id.* § 1026.17(e).

The Bureau's attempt to limit Section 1026.17(e) ignores Regulation Z's regulatory framework. *See* Opp'n at 18. Sections 1026.17(e) and 1026.20 must be read together to determine when changes to a loan require additional disclosures in addition to those made in the initial Truth in Lending disclosures. *See* 12 C.F.R. § 1027.20. In essence, Regulation Z distinguishes between changes that constitute new loans (disclosure required), and changes that merely update the terms of the existing loan (disclosure not required). The renewal provision in Integrity Advance's contracts falls under this latter exclusion.

The Bureau nevertheless insists that Integrity Advance should have included renewals and renewal fees in its TILA disclosures because the contracts automatically renewed if a customer did not choose a payment option. Relying on a single decision that did not consider Section 1027.17(e) of Regulation Z, *FTC v. AMG Servs*., 29 F. Supp. 3d. 1338 (D. Nev. 2014), the CFPB contends that, "as a matter of law" disclosing the APR, finance charge, and total payments based on a single payment when a loan contained an automatic rollover violated TILA. Opp'n at 17. The CFPB's reliance on this case is misplaced. Had the *AMG* court properly considered § 1026.17(e), it likely would have reached a different conclusion about the technical TILA claim, because an extension of loan terms is a post-consummation change and not part of the original loan contract. The Bureau fails to state a TILA claim.

CONCLUSION

For the foregoing reasons, the Court should dismiss the Notice of Charges.

Dated: January 25, 2016

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CERTIFICATION OF SERVICE

I hereby certify that on the 25th day of January 2016, I caused a copy of the foregoing Answer to be filed by electronic transmission (e-mail) with the U.S. Coast Guard Hearing Docket Clerk (aljdocketcenter@uscg.mil), Curtis Renoe (Curtis.e.renoe@uscg.mil) and Administrative Law Judge Parlen L. McKenna (cindy.j.melendres@uscg.mil), and served by electronic mail on the following parties who have consented to electronic service:

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