UNITED STATES OF AMERICA

Before the

BUREAU OF CONSUMER FINANCIAL PROTECTION

ADMINISTRATIVE PROCEEDING
File No. 2015-CFPB-0029

In the Matter of:	)	
INTEGRITY ADVANCE, LLC, and JAMES R. CARNES	)	**ORDER DIRECTING A REMAND TO THE BUREAU'S ADMINISTRATIVE LAW JUDGE**

On July 10, 2018, Acting Director Mick Mulvaney directed the parties to file a Joint Statement regarding further proceedings in this matter. The parties submitted that Statement on August 13, 2018, and they agreed that *Lucia v. SEC*, 138 S. Ct. 2044 (2018), applies to this matter, and that, pursuant to *Lucia*, the Administrative Law Judge (ALJ) who presided over the hearing was not constitutionally appointed. However, the parties disagreed on other points. Respondents argued that all the claims in the Bureau's notice of charges are time-barred, that they are outside the Bureau's authority, and that all charges against them should be dismissed. Enforcement counsel urged that the matter be remanded so that the Bureau's ALJ could address the issues raised by Respondents.

In the Joint Statement, Respondents raised two issues as to which Acting Director Mulvaney wanted further briefing. On September 2, 2018, he signed an Order directing the parties to address the following issues:

> 1) If a new hearing is to be held in this matter before an administrative law judge, must the Bureau also file a new Notice of Charges?
> 2) Does the Bureau's current administrative law judge satisfy the requirement in *Lucia v. SEC*, 138 S. Ct. 2044 (2018), that an

> administrative law judge be appointed by the President, a court of law, or the head of a department?

Both parties have now addressed these issues. After carefully considering their arguments, I conclude that, consistent with *Lucia v. SEC* and the Bureau's Rules of Practice for Adjudication Proceedings, this matter may be remanded to the Bureau's ALJ without issuing a new notice of charges. I also conclude that the Bureau's ALJ was appointed in a manner consistent with the Appointment's Clause of the Constitution. Accordingly, I will remand this matter to the Bureau's ALJ for a new hearing and recommended decision in accordance with the Bureau's Rules of Practice for Adjudication Proceedings, 12 C.F.R. Part 1081.[1]

Background

This proceeding commenced when the Bureau's Enforcement counsel filed its notice of charges with the Bureau's Office of Administrative Adjudication on November 18, 2015. Doc. 1. The notice named as respondents Integrity Advance, LLC, and its chief executive officer, James R. Carnes. The notice contained seven counts, which alleged violations of the Truth in Lending Act, the Electronic Fund Transfer Act, and the Consumer Financial Protection Act. When the notice of charges was issued, the Bureau did not have its own administrative law judge. Accordingly, on November 19, the matter was transferred to the Administrative Law Judge Office of the United States Coast Guard for adjudication. Doc. 8.[2] This assignment was made pursuant to an interagency agreement under which the Coast Guard had agreed to provide administrative law judge services to the Bureau. *Id.* The chief administrative law judge of the Coast Guard then assigned the matter to Coast Guard ALJ Parlen McKenna for adjudication. That adjudication was to be conducted pursuant to the Bureau's Rules of Practice for Adjudication Proceedings. *Id.*

Judge McKenna oversaw discovery by the parties. He also addressed three dispositive motions: He denied a motion to dismiss submitted by Respondents.

---

[1] The Bureau's rules use the term "hearing officer," but "hearing officer" is defined as "an administrative law judge or any other person duly authorized to preside at a hearing." 12 C.F.R. § 1081.103. Because the proceeding in this matter was conducted by an administrative law judge, I will use the term administrative law judge or ALJ in this Order.

[2] Documents filed in this adjudicative proceeding are referred to as "Doc. xx."

Doc. 75. He granted in part and denied in part a motion for summary disposition submitted by Enforcement counsel. Doc. 111 (granting the Bureau summary disposition with respect to five counts of the notice of charges). And he denied a motion for summary disposition submitted by Respondents. *Id*.

In July 2016, Judge McKenna conducted three days of hearings. Docs. 150-152. He then issued his Recommended Decision on September 27, 2016. Doc. 176. After making findings of fact, Judge McKenna reached his conclusions of law, and held that Enforcement counsel had established the violations alleged in six of the counts of the notice of charges. (The parties agreed by stipulation to withdraw the remaining count. Doc. 133.) He then addressed the appropriate sanctions. He recommended an award of restitution of approximately $38 million, and a civil penalty of $5.4 million. He also recommended two injunctive provisions.

Both Respondents and Enforcement counsel appealed the Recommended Decision. Docs. 177, 178. They submitted briefs, and, on January 11, 2017, presented oral argument in support of their appeals before the Bureau's Director. They also submitted post-argument supplemental briefs. Docs. 202, 203. In support of several of the arguments in their appeal, Respondents relied on the panel opinion in *PHH Corp. v. CFPB*, 839 F.3d 1 (D.C Cir. 2016). In particular, they argued that a three-year statute of limitations applied to the alleged violations of the Consumer Financial Protection Act. Also, based on Judge Randolph's concurrence in *PHH*, they argued that Judge McKenna was an inferior officer who was not appointed in accordance with the Appointments Clause of the Constitution. However, on February 17, 2017, the D.C. Circuit granted the Bureau's petition to rehear *PHH* en banc, and vacated the panel's opinion. As a result, on March 30, 2017, the Director issued an order holding resolution of Respondents' appeal in abeyance pending the en banc review.

On January 31, 2018, the en banc D.C. Circuit issued its decision in *PHH*, 881 F.3d 75 (D.C. Cir. 2018). Although the court reversed some parts of the panel's decision, it reinstated the portion on which Respondents based their statute of limitations argument. *Id*. at 83. The court declined to resolve whether administrative law judges who preside at trials of the Bureau's administrative proceedings are inferior officers who must be appointed pursuant to the Appointments Clause. However, while the D.C. Circuit was reconsidering the decision in *PHH*, the Supreme Court had granted certiorari in *Lucia v. SEC* to address the status of administrative law judges in connection with an administrative adjudication conducted by the Securities and Exchange

Commission. Accordingly, Acting Director Mulvaney issued an order holding this matter in abeyance until the Court issued its decision in *Lucia*. Doc. 210.

On June 21, 2018, the Supreme Court held that the SEC's ALJ who presided over its administrative trial was an officer of the United States, not an employee, and that he had not been appointed in a manner consistent with the Constitution's Appointments Clause, such as by the head of a department of the United States. *Lucia v. SEC*, 138 S. Ct. 2044 (2018). The Court further held that the appropriate remedy was a new hearing before an ALJ who had been properly appointed.

On July 10, 2018, Acting Director Mulvaney directed the parties to file a Joint Statement addressing the applicability to this proceeding of the D.C. Circuit's en banc decision in *PHH* and the Supreme Court's decision in *Lucia*. He also requested the parties to indicate whether there was any possibility that the matter could be resolved through settlement. The parties submitted the Joint Statement on August 13, 2018. Doc. 212. They agreed that settlement was unlikely, that *Lucia* applies to this matter, and that Judge McKenna had not been constitutionally appointed. But they disagreed as to how the remedy in *Lucia* should be applied in this proceeding, and as to the impact of the en banc decision in *PHH.* Respondents argued that there should be no additional proceedings, that the matter should be dismissed because they were not covered persons subject to the Bureau's authority, and that their conduct occurred outside the statute of limitations. They also argued that, if there were to be a new proceeding, the Bureau would have to file a new notice of charges. Further, they argued that the Bureau's current ALJ, Christine Kirby, could not conduct the proceeding because, even if she was appointed by Director Cordray (and they questioned whether she was), he was not the head of a department. Enforcement counsel urged that the matter be remanded to the Bureau's ALJ and that it be left to her to resolve the issues raised by Respondents.

After reviewing the Joint Statement, Acting Director Mulvaney concluded that he needed additional briefing regarding two issues:

1) If a new hearing is to be held in this matter before an administrative law judge, must the Bureau also file a new Notice of Charges?

2) Does the Bureau's current administrative law judge satisfy the requirement in *Lucia v. SEC*, 138 S. Ct. 2044 (2018), that an administrative law judge be appointed by the President, a court of law, or the head of a department?

That briefing has now been completed.

Analysis

Respondents urge that, before I address the two issues as to which Acting Director Mulvaney sought briefing, I should "dismiss[] this matter as outside the scope of the Bureau's jurisdiction and time-barred" because a dismissal on these grounds at this time would further the interests of "constitutional avoidance and judicial economy." Doc. 214 at 3. I decline to consider these arguments at this stage because a constitutionally appointed ALJ has not yet addressed them.

Under the Bureau's rules, dispositive issues like these are to be addressed first by the administrative law judge. 12 C.F.R. §1081.212(h). While Judge McKenna considered these matters (and rejected Respondents' arguments) in his Order Denying Motion to Dismiss, Doc. 75, Judge McKenna's appointment was inconsistent with the Appointments Clause. And as the Court explained in *Lucia*, the appropriate remedy for an Appointments Clause violation is a new hearing by a properly-appointed ALJ who has not previously adjudicated the issues. 138 S. Ct. at 2055. Consistent with the Bureau's rules and *Lucia*, I believe it is appropriate for these issues to be raised before, and addressed by, a constitutionally appointed ALJ in the first instance.

1. Notice of charges

The first question raised in the Order of September 2 is whether, if there is to be a new hearing in this matter before a properly appointed ALJ, the Bureau must also file a new notice of charges. Respondents contend that a new notice of charges is necessary. They cite Bureau rule 1081.203(d), 12 C.F.R. §1081.203(d), to support their contention that "a lawfully-appointed hearing officer is a pre-requisite for filing the Notice of Charges." Doc. 241 at 6. They also note that the Bureau's rules require the ALJ to issue a recommended decision within 300 days after the filing of the notice of charges. Thus, they argue that "Enforcement Counsel never properly brought an action because the Bureau lacked the legal authority to pursue an adjudication, since it could not bring the proceeding before a properly appointed hearing officer." *Id.* at 7.

Enforcement counsel argue that no new notice of charges is necessary. They cite numerous cases, including *Lucia*, where courts held that officials had been appointed in violation of the Appointments Clause, and point out that, in none of those cases did the court require the filing of new charges. Doc. 215 at 4-6. They also note that, in SEC cases that were originally heard by improperly appointed ALJs, new proceedings have begun before properly appointed ALJs but new

charges have not been filed. They argue that nothing in the Bureau's rules suggests that a new notice of charges is necessary. They cite rules 1081.200(a) and 1081.105(a), 12 C.F.R. §§ 1081.200(a), 1081.105(a), and claim that "it is the filing of a notice of charges that initiates a case, and only later is a hearing officer assigned." Doc. 215 at 6. Finally, they cite Bureau rule 1081.105(d), 12 C.F.R. § 1081.105(d), which contemplates the unavailability of the ALJ, and note that nothing in the rules "suggest[s] that such unavailability would render the proceeding itself (or the notice of charges) fatally defective." Doc. 215 at 7.

I conclude that no new notice of charges is necessary here. The Bureau's rules provide that an administrative adjudication proceeding is commenced "by filing of a notice of charges by the Bureau." 12 C.F.R. § 1081.200(a). Pursuant to this rule, the notice of charges is filed by "the Bureau," not by the ALJ. A separate rule, rule 1081.105(a), provides for the assignment of the ALJ: "In the event that more than one hearing officer is available to the Bureau for the conduct of proceedings under this part, the presiding hearing officer shall be designated by the chief hearing officer, who shall notify the parties of the hearing officer designated." 12 C.F.R. § 1081.105(a). Thus, once the ALJ has been selected, the ALJ shall notify *the parties* of her selection. But there are no parties until a proceeding has been commenced. So the Bureau's rules contemplate that the ALJ is not selected until after a notice of charges has been filed, and that is what occurred in this proceeding: The notice of charges was filed by the Bureau on November 18, 2015, Doc. 1, and the ALJ was not designated until the following day, Doc. 8.[3]

Respondents argue that, because Judge McKenna was unconstitutionally appointed, the Bureau could not validly complete the hearing in this matter within 300 days, as required by the Bureau's rules, 12 C.F.R. § 1081.400(a). Because the proceeding could not be finished within that time, Respondents contend that the proceeding was not properly commenced. At the time the Bureau commenced its action against Respondents, it had no reason to believe that the ALJ had not been properly appointed. Indeed, in *Landry v. FDIC*, 204 F.3d 1125 (D.C. Cir. 2000), the D.C. Circuit held that ALJs were not inferior officers. In any event, Respondents misunderstand rule 1081.400(a). That rule is a direction to the ALJ, and its purpose is to promote expeditious resolution of adjudicative hearings. It is

[3] Respondents are mistaken that Bureau rule 1081.203(d), 12 C.F.R. § 1081.203(d), "firmly establish[es] that the availability of a lawfully-appointed hearing officer is a pre-requisite for filing the Notice of Charges…." *See* Doc. 216 at 3. That rule addresses the timing of the scheduling conference and the scheduling order, not the filing of the notice of charges.

not a limit on the Bureau. Nor does it create any right for Respondents. This is particularly so here, where Judge McKenna did issue a timely recommended decision, where his recommended order has never taken effect, and where the additional delay that has resulted from the appeal process has not prejudiced Respondents.

Accordingly, this proceeding may go forward based on the notice of charges issued on November 18, 2015.

2. Appointment of the Bureau's ALJ

The second question raised in the Order of September 2 is whether the Bureau's current ALJ, Christine Kirby, was appointed in a manner that satisfies the requirements of *Lucia*. Respondents raise two arguments. First, they contend that the Bureau has identified no records indicating that either Acting Director Mulvaney, or the Bureau's former Director, Richard Cordray, appointed Judge Kirby. Accordingly, Respondents assume that Judge Kirby was hired by the Office of Personnel Management, not appointed in accordance with the Appointments Clause. Second, they contend that, even if Judge Kirby had been appointed by the Bureau's Director, her appointment would nonetheless be defective. They note that, under the Appointments Clause, the appointment of an inferior officer, such as an ALJ, must be vested in "the President alone, in the Courts of Law, or in the Heads of Departments." Because Judge Kirby was not appointed by the President or the courts of law, her appointment is valid only if she were appointed by the head of a department. Respondents argue that the Bureau is not a department. They cite *Free Enterprise Fund v. Public Company Accounting Oversight Board*, 561 U.S. 477, 511 (2010), which holds that a department must be a freestanding component of the executive branch. Because the Bureau "is established in the Federal Reserve System," 12 U.S.C. § 5491(a), they contend that the Bureau is "contained within the Federal Reserve System," and therefore it is not a freestanding component of the executive branch, so it cannot be a department. Thus, Respondents argue that even if the Bureau's Director appointed Judge Kirby, that appointment is not valid because the Bureau's Director is not the head of a department.

Enforcement counsel argue that they "understand[]" that former Director Cordray appointed Judge Kirby, but that even if he did not, I could appoint her now, thereby satisfying the requirements of the Appointments Clause. Enforcement counsel also argue that, even if, pursuant to the Consumer Financial Protection Act (CFPA), the Bureau "is established in the Federal Reserve System," this does not

mean that the Bureau is subordinate to, or contained within, another component of the Executive Branch. According to Enforcement counsel, although the Federal Reserve *Board* is an agency, and thus a component of the Executive Branch, the Federal Reserve *System* is not. Enforcement counsel argue that the Federal Reserve System "is a collection of distinct entities, including the Board of Governors of the Federal Reserve System, the Federal Reserve banks, and every national bank, among other entities." It has "no authorities, let alone authority it can exercise over the Bureau." The Board of Governors is an agency, but, pursuant to various provisions of the CFPA, the Bureau is not subordinate to it. Enforcement counsel contend that if the Bureau were not a department, then the Bureau's Director would be unable to appoint not only ALJs, but also other senior Bureau officials who are inferior officers (such as, perhaps, the Bureau's Deputy Director).

First, I have reviewed the relevant documents and determined that, on January 5, 2016, former Director Cordray signed a Decision Memorandum authorizing the appointment of Judge Kirby.

Second, I conclude that the Bureau is a department and that Director Cordray was, at the time of Judge Kirby's appointment, the head of a department. A "department" is "a freestanding component of the Executive Branch, not subordinate to or contained within any other such component." *Free Enterprise*, 561 U.S. at 511. The "other such component[s]" that the Court was talking about are entities "'in which a class of duties are allotted to a particular person.'" *Id.* quoting 1 N. Webster, *American Dictionary of the English Language*, (1828) (1995 facsimile ed.). Pursuant to the CFPA, the Bureau is an "Executive agency," that is "independent" and "established in the Federal Reserve System." 12 U.S.C. § 5491(a). The Federal Reserve System is distinct from the Board of Governors of the Federal Reserve System (*i.e.*, the Federal Reserve Board). The Federal Reserve Board, like the Bureau, is within the Federal Reserve System and it, and its Director, are assigned duties that it must carry out. Thus, the Federal Reserve Board is a department. But the Bureau is not subordinate to, or contained within, the Federal Reserve Board. *See*, *e.g.*, 12 U.S.C. § 5492(c) (describing the Bureau's autonomy from the Federal Reserve Board). Instead, the Bureau is established in the Federal Reserve System. But the Federal Reserve System, unlike the Federal Reserve Board, is not an entity as to which duties have been allotted. Instead, it is an umbrella over several components, each of which has assigned duties. The components of the Federal Reserve System include the Federal Reserve Board, the

Federal Open Market Committee, and the Federal Reserve Banks.[4] And it also includes the Bureau. Because the Federal Reserve System is not a department, the Bureau is not contained within a department.[5] Therefore, the Bureau is a department, and Director Cordray's appointment of Judge Kirby was valid.

* * * * *

For the reasons set forth above, I ORDER that this matter be remanded to the Bureau's Administrative Law Judge, Christine Kirby, for a new hearing and recommended decision in accordance with Part 1081 of the Bureau's Rules, 12 C.F.R. Part 1081. Further, I direct that Judge Kirby give no weight to, nor presume the correctness of, any prior opinions, orders, or rulings issued by Judge McKenna. Further, Judge Kirby should seek submissions from the parties regarding the conduct of further proceedings.

SO ORDERED this 28th day of May, 2019.

Kathleen L. Kraninger
Director
Bureau of Consumer Financial Protection

[4] https://www.federalreserve.gov/aboutthefed/structure-federal-reserve-system.htm. If the Federal Reserve System were a department, then, presumably, none of its components, including the Federal Reserve Board, would be a department, and they would all be precluded from appointing inferior officers.

[5] Respondents contend that, because the Bureau obtains its funding from the Federal Reserve System, 12 U.S.C. § 54976(a), it is "monetarily 'contained within' the Federal Reserve System." *See* Doc. 216 at 7. But the Bureau's source of funding is irrelevant to the analysis here. What matters is that the Federal Reserve System is not a component of the Executive Branch to which duties have been allotted.

CERTIFICATE OF SERVICE

I hereby certify that I have served a true and correct copy of the *Order Directing a Remand to the Bureau's Administrative Law Judge* upon the following parties and entities in Administrative Proceeding 2015-CFPB-0029 as indicated in the manner described below:

Via Electronic Mail to Representatives for Consumer Financial Protection Bureau
Alusheyi J. Wheeler, Esq.
1700 G Street, NW
Washington, DC 20552
alusheyi.wheeler@cfpb.gov

Deborah Morris, Esq., Email: deborah.morris@cfpb.gov
Craig A. Cowie, Esq., Email: craig.cowie@cfpb.gov
Wendy J. Weinberg, Esq., Email: wendy.weinberg@cfpb.gov
Vivian Chum, Esq., Email: vivian.chum@cfpb.gov

Via Electronic Mail to Representatives for Respondent
Allyson B. Baker, Esq.
Venable LLP
600 Massachusetts Ave., NW
Washington, D.C., 20001
abbaker@venable.com

Hilary S. Profita, Esq., Email: hsprofita@venable.com
Peter S. Frechette, Esq., Email: psfrechette@venable.com
JP Boyd, Esq., Email: jpboyd@venable.com

Jameelah Morgan
Digitally signed by Jameelah Morgan
Date: 2019.05.29 11:30:48 -04'00'

Jameelah Morgan
Docket Clerk
Office of Administrative Adjudication
Bureau of Consumer Financial Protection

Signed and dated on this 29th day of May, 2019 at Washington, D.C.