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The CFPB's early-warning notice: The devil's in the details

Robyn Quattrone, Lauren Randell and Stephen LeBlanc of BuckleySandler LLP say the Consumer Financial Protection Bureau's release of details regarding its early-warning notice is a welcome indication that it will follow the lead of the Securities and Exchange Commission by informing investigation targets of its intent to bring enforcement actions.

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CREDIT REPAIR ORGANIZATIONS ACT

Supreme Court rules consumers must arbitrate credit card disputes

Consumers must arbitrate fee disputes with credit card companies instead of pursuing their Credit Repair Organizations Act claims through lawsuits, the U.S. Supreme Court has ruled, with one justice dissenting.

CompuCredit Corp. et al. v. Greenwood et al., No. 10-CV-948, 2012 WL 43514 (U.S. Jan. 10, 2012).

Justice Antonin Scalia, writing for the court, said the Federal Arbitration Act, 9 U.S.C. § 1, calls for enforcement of the arbitration provision in the plaintiffs' credit card agreement.

This is the case because the Credit Repair Organizations Act, 15 U.S.C. § 1679, which prohibits credit repair businesses from engaging in certain practices, is silent on whether claims brought under it can be heard in an arbitration forum, he said.

Justice Scalia's ruling, joined by Chief Justice John Roberts and Justices Anthony Kennedy, Clarence Thomas, Stephen Breyer and Samuel Alito, reverses a decision of the 9th U.S. Circuit Court of Appeals.

The appellate court held that CROA claims are not subject to arbitration and can be heard in court.

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The CFPB's early-warning notice: The devil's in the details

By Robyn C. Quattrone, Esq., Lauren R. Randell, Esq., and Stephen LeBlanc, Esq.
BuckleySandler LLP

The Consumer Financial Protection Bureau continues to bring its enforcement infrastructure to life, announcing Nov. 7 that in some circumstances it will issue "early-warning notices" to investigation targets before initiating enforcement proceedings.[1] The CFPB's early-warning notice bulletin offers a measure of welcome guidance to the financial services industry regarding at least some of the pre-enforcement procedures that the CFPB will implement.

But with certain details of the early-warning process still unclear, and others potentially troubling, it remains to be seen whether investigation subjects will take advantage of the opportunity to present their views to the enforcement staff prior to the recommendation of formal proceedings.

Most notably, the requirement that "[a]ny factual assertions relied upon or presented in the written statement [to] be made under oath by someone with personal knowledge of such facts" could dissuade targets under investigation from providing submissions because of the potential collateral consequences of swearing under oath to the facts contained in the statement.[2]

The goal of the early-warning notice process, according to Raj Date, special adviser to the secretary of the treasury for the CFPB, is to "strike ... a balance between the goal of fairness to those being investigated and [the CFPB's] mission to protect consumers. ... This process will help [the CFPB] fulfill [its] commitment to transparency in enforcing the law."[3]

As described in the early-warning notice bulletin, before the CFPB's Office of Enforcement recommends that the CFPB commence enforcement proceedings, the office *may* provide investigation subjects notice of its intent to recommend enforcement proceedings and an opportunity to submit a written response to the potential charges.

The bulletin explains that the "primary focus of the written statement in response should be legal and policy matters relevant to the potential enforcement proceedings."[4] Responses are due within 14 days and may not exceed 40 pages. If the Office of Enforcement ultimately recommends enforcement proceedings, the investigation subject's written submission will be included with that recommendation.

The CFPB's announcement of the early-warning notice regime acknowledges that the notice is modeled on similar pre-enforcement procedures from other federal agencies, and most closely parallels the Securities and Exchange Commission's Wells process. Under the Wells process, the SEC's enforcement staff also issues a notice to the target of an SEC investigation that "identif[ies] the specific charges the staff is considering recommending to the commission."[5] The recipient is similarly provided the opportunity to submit a response "arguing why the commission should not bring an action against them."[6]

> The CFPB's early-warning notice process is modeled on similar pre-enforcement procedures from other federal agencies and most closely parallels the Securities and Exchange Commission's Wells process.

Although the CFPB bulletin provides only a skeletal outline of the early-warning notice process, the parallels to the Wells process are many; in light of the many similarities, however, the differences are particularly notable.

At their most basic, both processes share the stated goal of informing investigation subjects of the charges against them and permitting those subjects the opportunity to present their positions and defenses to the agency before an enforcement proceeding is formally commenced. The processes purport to ensure a fuller agency understanding of any enforcement decision and potentially to help resolve regulatory concerns without the need for a formal enforcement action.

The CFPB process is also procedurally similar to the Wells process. Neither agency *requires* a pre-enforcement notice, which leaves the decision of whether to provide notice to the discretion of the agency staff. Both agencies acknowledge that the need for prompt enforcement action may render a notice and submission impractical, such as in proceedings seeking temporary restraining orders or asset freezes to stop ongoing frauds.

Like the SEC, the CFPB will permit unsolicited written statements where notice is not formally provided.[7] Of course, an unsolicited submission presumes that the subject is aware of the investigation, which is often, but not always, the case in the absence of an agency notice.

Another important similarity involves the permitted extrinsic uses of submission materials. Under the SEC's enforcement rules, Wells submissions may be used by the agency "in any action or proceeding that it brings" and may be "discoverable by third parties."[8] The SEC staff is authorized to reject any submission that purports to limit its ability to use it, such as attempts to limit admissibility under the Federal Rules of Evidence.

The CFPB bulletin and the sample early-warning notice attached to it incorporate similar provisions, warning that "[s]ubmissions may be discoverable by third parties in accordance with applicable law" and that "the bureau may use information contained in any submission as an admission, or in any other manner permitted by law, in connection with CFPB enforcement proceedings or otherwise."[9]

This potential for adverse agency or third-party use of submission materials heightens the consequences of a target's decision to participate in the process. And, as with the Wells process, particular care should taken in light of these concerns when deciding the overall approach and strategy and whether to make a CFPB submission.

A positive aspect of the early-warning notice process is that, like the Wells process, submissions will be included with any enforcement recommendation. The SEC's enforcement rules provide that "Wells submissions will be provided to the commission along with any recommendation from the staff for an unsettled action against the recipient of the Wells notice."[10]

This structure increases the potential upside for submitting a Wells response because, if efforts to dissuade staff have failed, a submission will be reviewed by the commissioners before a decision is made to undertake enforcement action, as opposed to the submission simply being considered by the SEC staff conducting the investigation.

Wells submissions therefore have at least the potential to steer both the staff away from recommending enforcement and the commissioners away from adopting an enforcement recommendation.

The CFPB's bulletin includes similar language: "If the Office of Enforcement ultimately recommends the commencement of an enforcement proceeding, the written statement will be included with that recommendation."[11] Whereas the SEC's enforcement manual provides a thorough discussion of the enforcement-recommendation process and the voting procedures governing the commissioners' ultimate decision, however, the CFPB has not yet publicly promulgated rules addressing these facets of its enforcement-decision process.[12]

It at least appears that, as with the SEC's process, the final decision-maker for an enforcement action will have the benefit of the target's submission. CFPB clarification on this issue, in the form of detailed, written rules of practice that explain the internal enforcement recommendation and decision processes, will presumably follow as the CFPB develops its internal enforcement procedures.

While the CFPB appears to have adopted many of the primary aspects of the Wells process, at least one conscious divergence should give subjects of CFPB investigations pause. The CFPB will require "[a]ny factual assertions relied upon or presented in the written statement [to] be made under oath by someone with personal knowledge of such facts."[13] The CFPB's requirement raises the stakes for a target making a submission and underscores the care that must be taken in crafting a proper response.

While the CFPB appears to have adopted many of the primary aspects of the SEC's Wells process, at least one conscious divergence should give subjects of CFPB investigations pause.

The investigation target and potential defendant, and its executives, may be the only people capable of verifying facts under oath, and significant consequences will attach, including potential perjury penalties. Defense counsel and a target entity may well decide against making a submission to avoid even the potential for these consequences.

Additionally, if an individual or executives of the target entity wish to preserve their Fifth Amendment rights against testifying, then the target may be effectively barred from making a submission to the CFPB, particularly because it may share submissions with third parties, including state attorneys general and other governmental authorities. This verification requirement may have the practical impact of lessening the likelihood that submissions will be made to the CFPB, undermining its laudable stated goal.

Important issues also remain unresolved with the early-warning notice process, as compared with more established pre-enforcement notice processes. For instance, it is unknown whether the CFPB's notice process will permit subjects of investigations and recipients of early-warning notices to review the investigative record. Under the Wells process, the SEC staff may, at its discretion, "allow the recipient of the notice to review portions of the investigative file that are not privileged."[14] Permitting the target to review the agency's record allows a better understanding of the circumstances underlying the potential charges against it, and may result in a more informed written submission, a benefit to both the recipient's defense and the agency's decision-making process. Given these benefits, the CFPB should strongly consider permitting file review within the early-warning notice process.

Another uncertainty involves whether the CFPB will permit notice recipients to request meetings with its staff to discuss the investigation and possible enforcement action. The SEC's Wells process allows notice recipients to "request meetings with the staff to discuss the substance of the staff's proposed recommendation to the commission," and in practice, of course, such meetings are frequent and common.[15] Pre-enforcement dialogue benefits both the target of an investigation and the SEC, as each side gains a better understanding of the factual, legal and policy concerns and the dialogue often facilitates a quicker resolution of investigations.

It is also unclear whether the CFPB's notice process will incorporate any of the recent enforcement-related Dodd-Frank amendments to the Wells process. For example, Section 929(U) of Dodd-Frank imposes a deadline of 180 days after issuing a Wells notice for the SEC to bring an enforcement action. Additionally, Section 929(U) provides that within 180 days of completing an onsite compliance examination or inspection, or receiving all requested records, the SEC must request corrective action or notify the target entity that the investigation has concluded. Either of these deadlines may be extended due to factors that in practice have included the complexity of particular investigations.

The addition of these deadlines signals a congressional effort to encourage more expeditious investigation resolution, a goal that is beneficial to regulated industries seeking a measure of certainty. With respect to the SEC, however, these new deadlines have had the effect of limiting previously customary extensions granted to subjects for submitting their Wells responses or limiting opportunities for post-Wells dialogue. Whether similar deadlines will be tied to the CFPB's notice process remains an important but unresolved issue.

The CFPB's early-warning notice announcement provides guidance on the investigation and enforcement procedures of a still-developing enforcement agency, and it signals certain positive steps toward procedural fairness by affording subjects of investigations the opportunity to be heard before an enforcement action commences. Yet this new process includes potentially troubling requirements, namely the factual verification obligation for all submissions and that other significant issues remain unresolved.

Although the CFPB still in its infancy, it is essential that the agency move swiftly to codify additional rules and procedures governing its pre-enforcement notice process so that targets of its investigations in the financial services industry may fully understand, and defend against, potential charges. Publicly available guidance on the CFPB's investigation process, and procedural safeguards facilitating dialogue between the CFPB and potential targets in the financial industry, can only advance the CFPB's stated commitment to "transparency in enforcing the law."[16] WJ

NOTES

[1] *See* Consumer Fin. Prot. Bureau, CFPB Bulletin 2011-04, Early Warning Notice (Nov. 7, 2011).

[2] *Id*.

[3] Press Release, Consumer Fin. Prot. Bureau, Consumer Financial Protection Bureau Plans to Provide Early Warning of Possible Enforcement Actions (Nov. 7, 2011).

[4] CFPB Bulletin 2011-04.

[5] Sec. & Exchange Comm'n, Division of Enforcement, Enforcement Manual, § 2.4.

[6] *Id*.

[7] *Compare* CFPB Bulletin 2011-04 ("Persons involved in an investigation who wish to submit a written statement on their own initiative at any point during an investigation should follow the relevant procedures" for responding to an early warning notice) *with* SEC Rules on Informal and Other Procedures, 17 C.F.R. § 202.5(c) ("Persons who become involved in preliminary or formal investigations may, on their own initiative, submit a written statement to the commission setting forth their interests and position in regard to the subject matter of the investigation.").

[8] SEC Enforcement Manual, § 2.4.

[9] CFPB Bulletin 2011-04.

[10] SEC Enforcement Manual, § 2.4.

[11] CFPB Bulletin 2011-04.

[12] The CFPB's interim final rules relating to investigations are notably vague on these points. *See* 76 F.R. 45173, § 1080.11(a) ("When the facts disclosed by an investigation indicate that an enforcement action is warranted, further proceedings may be instituted in federal or state court or pursuant to the bureau's administrative adjudicatory process.").

[13] CFPB Bulletin 2011-04.

[14] SEC Enforcement Manual, § 2.4.

[15] *Id*.

[16] Press Release, *supra* note 3.

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