2014

A Spotlight on Shadow Banking: The CFPB Finalizes Procedures to Supervise Risky Nonbanks

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Available at: http://scholarship.law.unc.edu/ncbi/vol18/iss2/5
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I. INTRODUCTION

Captain Steve Zissou\(^1\) assembled his crew of oceanographic explorers into the crowded confines of his deep-sea research vessel for one purpose: to find the mysterious shark that ate his friend. Zissou, an experienced and pompous seaman, had convinced investors to bankroll his expedition in exchange for documentary footage of the rare "jaguar shark." After spending weeks in unchartered waters with no sign of the elusive predator, Zissou faced a mutiny from novice crewmembers who began to doubt the existence of the shark altogether and urged the overzealous Zissou to abandon the mission. In the final leg of the journey, however, Zissou steered his crew into the depths of the ocean, powered up his spotlight, and fixed his eyes upon the jaguar shark he had finally discovered.

It is difficult to see what lies in the shadows, and prior to 2008, federal regulators shied away from the shadow banking industry\(^2\) that had abused consumer trust with impunity.\(^3\) In response, Congress created the Consumer Financial Protection Bureau (CFPB) in the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank).\(^4\) In doing so, Congress effectively sent the CFPB into unchartered waters with a spotlight to illuminate the predatory conduct

1. Steve Zissou is a character in THE LIFE AQUATIC (Touchstone Pictures 2004), on which the Introduction to this Note is based.
2. "Shadow banking" has been defined as "a diverse set of institutions and markets that, collectively, carry out traditional banking functions [] but do so outside, or in ways only loosely linked to, the traditional system of regulated depository institutions." Ben S. Bernanke, Chairman, Fed. Reserve Sys., Some Reflections on the Crisis and the Policy Response at the Russell Sage Foundation and the Century Foundation Conference on "Rethinking Finance" (Apr. 13, 2012) (transcript available at http://www.federalreserve.gov/newsevents/speech/bernanke20120413a.htm).
that contributed to the financial crisis.

On July 3, 2013, the CFPB issued a final procedural rule (Final Rule) to establish supervisory authority over certain risky nonbanks and address unfair, deceptive, and abusive acts or practices in the shadow banking system. This Note will argue that the Final Rule offers a practical, hands-off approach to consumer protection in markets for consumer financial products and services while considering the rights of nonbanks that have only recently found themselves in arms reach of CFPB jurisdiction. This Note will proceed in four parts. Part II will explain the CFPB’s purpose and the scope of its nonbank supervision program. Part III will provide an overview of the Final Rule. Part IV will discuss the major criticisms of the Final Rule and its justification within the context of the CFPB’s objectives. Part V will conclude by discussing the consequences to nonbanks and challenges ahead for the CFPB.

II. THE CFPB: PURPOSE, RULEMAKING AUTHORITY, AND SUPERVISION

A. Purpose: Leveling the Playing Field

In response to the 2008 financial crisis, Congress established the CFPB to regulate consumer financial products and services more effectively. Bank regulators have the safety and soundness of financial institutions as their primary concern, but “this approach judges a bank’s conduct toward consumers by its effect on the bank, not

7. See infra Part II.
8. See infra Part III.
9. See infra Part IV.
10. See infra Part V.
on consumers." Consumer protection was something of an afterthought. Nonbank providers of consumer financial products and services were subject to little or no oversight, and no federal agency had supervision and examination authority over these institutions. Fragmented jurisdiction prevented regulators from engaging in meaningful oversight of consumer financial products and services offered by both banks and nonbanks.

The Federal Trade Commission (FTC), for example, traditionally had jurisdiction over nonbank financial institutions, but

13. Id.
16. Creating a Consumer Financial Protection Agency: A Cornerstone of America's New Economic Foundation: Hearing Before the S. Comm. on Banking, Hous., and Urban Affairs, 111th Cong. 151 (2009) [hereinafter Creating a Consumer Financial Protection Agency] (responses to written questions of Sen. David Vitter from Michael S. Barr, Assistant Secretary for Financial Institutions, Department of the Treasury) (“[T]he Administration’s goal was for there to be a [f]ederal agency with the mission of consumer protection. In the consumer financial products and services area, this agency is lacking; in the nonbank sector, no [f]ederal agency has supervision and examination authority, regardless of the mission, and in the banking sector, five different agencies share this responsibility but each has safety and soundness as its primary mission. The Securities and Exchange Commission (SEC), on the other hand, does have its mission the protection of retail investors . . . . but needs additional authorities . . . to provide the broader and more effective oversight that is needed . . . .”).
17. See id.
18. Id. at 28 (testimony of Michael S. Barr, Assistant Secretary for Financial Institutions, Department of the Treasury) (describing the structural deficiencies within the
as a law enforcement agency it was not structurally designed to supervise the nonbank sector. Unlike federal bank regulators, the FTC lacked supervisory authority over nonbanks and could only act through an enforcement action once a violation had occurred. The FTC did not conduct regular examinations of nonbanks, as state regulators were the primary supervising entities. The level of supervision was not as rigorous as that for depository institutions and varied considerably from state to state.

As a new consumer watchdog, the CFPB was established to prevent unfair, deceptive, and abusive financial services practices and to level the playing field between depository and non-depository institutions that offer consumer financial products and services. Through consistent enforcement of federal consumer financial laws, the CFPB’s goal is to ensure that consumers have access to financial products in fair, transparent, and competitive markets.

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19. Id. ("I think that [the FTC] has not had the tools to [regulate financial products]. It is structurally not set up to supervise or examine the nonbank sector. It can only act long after the fact with enforcement when it is too late—and that is just not enough.").


21. Id.

22. Id. at 8; see also Improving Federal Consumer Protection in Financial Services—Consumer and Industry Perspectives: Hearing Before the H. Comm. on Fin. Servs., 112th Cong. 13 (2007) (statement of James C. Sivon, Barnett, Sivon & Natter PC) ("During the recent problems in the mortgage market, lenders of all types engaged in questionable practices. The institutions that have gone bankrupt because of their practices were State licensed and supervised. This suggests that State supervisory resources were inadequate or not adequately utilized.").


24. S. REP. No. 111-176, at 11 (2010) (describing the CFPB’s goal to establish “a basic, minimum federal level playing field” for all banks, as well as nonbanks that were largely unregulated prior to Dodd-Frank); see also Implementing Wall Street Reform: Enhancing Bank Supervision and Reducing Systematic Risk: Hearing Before S. Comm. on Banking, Hous. and Urban Affairs, 112th Cong. 68 (2012) (prepared statement of Richard Cordray, Director, Consumer Financial Protection Bureau).

25. 12 U.S.C. § 5511(a) (2012) (explaining the CFPB’s purpose 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 markets for consumer financial products and services are fair, transparent,
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operates under a mandate to supervise an array of bank and nonbank institutions, prescribe rules to carry out its objectives, and draw from a variety of tools at its disposal to level the playing field.26

B. Scope of Supervisory Authority: Nonbank Supervision Program

Dodd-Frank grants the CFPB supervisory authority over certain bank and nonbank institutions.27 Supervision allows the CFPB to assess compliance with the requirements of federal consumer financial law, obtain information about the activities and compliance systems of those entities, and assess risks to customers of financial products and services.28 It also permits the CFPB to request reports and conduct examinations of nonbank institutions on a periodic basis.29

With respect to banks, the CFPB may only supervise banks and credit unions with more than $10 billion in assets.30 Banks with $10 billion or less in assets are still subject to CFPB regulations, but the prudential banking regulators remain the primary supervisory and enforcement powers.31 Banking regulators examine those institutions to determine compliance with CFPB rules that implement consumer financial laws.32

With respect to nonbanks, the CFPB has supervisory authority over certain nonbank "covered persons," defined as any entity that "engages in offering or providing a consumer financial product or service."33 The CFPB may regulate nonbank entities that offer consumer financial products or services within three specific categories: private education lenders; payday lenders; and entities that provide...
mortgage-related services, such as mortgage origination, brokerage, mortgage servicing, mortgage modification, and foreclosure relief activities.\textsuperscript{34} The CFPB may also supervise large participants\textsuperscript{35} of consumer debt collection,\textsuperscript{36} consumer reporting,\textsuperscript{37} and student loan servicing markets.\textsuperscript{38}

In addition to its authority to supervise certain types of institutions, the CFPB may supervise nonbanks based on their conduct. Section 5514(a)(1)(C) of Dodd-Frank grants the CFPB authority over any nonbank covered person that

the Bureau has \textit{reasonable cause to determine}, by order, after notice to the covered person and a reasonable opportunity for such covered person to respond, based on [consumer complaints] or information from other sources, that such covered person is engaging, or has engaged, in conduct that poses risks to consumers with regard to the offering or provision of consumer financial products or services.\textsuperscript{39}

Nonbank covered persons described in this section are not classified based on institutional design or function, but rather by the risk associated with the offering of a specific product or service.\textsuperscript{40} Although they are not identified with particularity, these potentially risky nonbanks may nevertheless be subject to CFPB supervision and

\textsuperscript{34} Id. § 5514(a)(1)(A)-(E) (providing a list of "covered persons" subject to CFPB authority and defining "mortgage companies" to include originators, brokers, servicers, and loan modification or foreclosure relief services); \textit{see also} Peggy Twohig & Steve Antonakes, \textit{The CFPB launches its nonbank supervision program}, CFPB BLOG (Jan. 5, 2012), http://www.consumerfinance.gov/blog/the-cfpb-launches-its-nonbank-supervision-program/ (last visited Feb. 8, 2014) (providing an overview of "covered persons" within section 5514 of Dodd-Frank); CARPENTER, supra note 20, at 13-17 (same).

\textsuperscript{35} \textit{See} Defining Larger Participants of Certain Consumer Financial Product and Service Markets, 12 C.F.R. §§ 1090.104-105 (2013) (defining "larger participants" within the consumer reporting market and the consumer debt collection market).

\textsuperscript{36} Id. § 1090.104(a).

\textsuperscript{37} Id. § 1090.105(a).


\textsuperscript{40} \textit{See id.}
The discretion afforded by § 5514(a)(1)(C) provides the CFPB with the latitude to evolve with the markets. Where thousands of nonbank institutions comprise a significant portion of the financial services industry, creating meaningful oversight through legislation requires a proactive approach to address risky practices that would otherwise remain in the shadows. Dodd-Frank empowers the CFPB to regulate consumer financial products or services that were not on the market when the legislation was enacted, but may nevertheless pose serious risks to consumers in future markets. Creating an agency that only had the authority to address the problems of the past would have been shortsighted.

III. THE FINAL RULE: BRINGING RISKY NONBANKS UNDER CFPB SUPERVISION

A. The CFPB's Rulemaking Authority and Goals for Consistency and Transparency

The CFPB wields broad rulemaking powers and

41. See Kevin L. Petrasic & Amanda M. Jabour, Knowing When, Where and How to Draw the Line Presents Significant Challenges for the CFPB's Nonbank Supervision Program, BNA BANKING REPORT, Sept. 11, 2012 (discussing industry concerns over the broad scope of CFPB authority over nonbank financial institutions).

42. See S. Rep. No. 111-176, at 11 (2010) (noting that "[t]he CFPB will have enough flexibility to address future problems as they arise" rather than prescribing authority limited to problems, such as mortgages, that were only readily identifiable in hindsight); Carpenter, supra note 20, at 16 (explaining that, flowing from its discretion to supervise nonbanks based on risk determination, the CFPB has "the latitude to evolve with the markets ... making it possible to regulate entities that offer consumer financial products or services that were not in the marketplace when the Dodd-Frank Act was signed into law"); Consumer Fin. Prot. Bureau, Strategic Plan FY 2013 – FY 2017 4 (2013), available at http://www.consumerfinance.gov/strategic-plan/#goal1 (describing the structure of the CFPB within the context of its goal to "prevent financial harm to consumers while promoting good practices that benefit them").

43. See S. Rep. No. 111-176, at 13 ("This month, the [CFPB] launched the first federal nonbank supervision program, one of the central new authorities provided by the Dodd-Frank Act. There are thousands of nonbank providers of financial products and services that make up a significant portion of the consumer financial marketplace and affect millions of Americans each year.").

44. See id. at 11 ("Experience has shown that consumer protections must adapt to new practices and new industries.").

45. Carpenter, supra note 20, at 16.

Dodd-Frank generally authorizes the CFPB to administer, enforce, and implement federal consumer financial laws. Under 12 U.S.C. § 5512(b)(1), the CFPB may prescribe rules and issue orders and guidance wherever necessary or appropriate for it to carry out its purposes and objectives. To the extent that the CFPB’s rulemaking authority conflicts with that of another federal agency under a specific provision of federal consumer financial law, the CFPB has exclusive authority to prescribe rules pursuant to such provisions.

In addition to its general rulemaking power, the CFPB has specific authority under 12 U.S.C. § 5514(b)(7)(A) to write rules that facilitate its nonbank supervision program. Although the Final Rule was not necessary to implement § 5514(a)(1)(C), the statutory language within § 5514(b)(7)(A) indicates that Congress expected the CFPB to issue rules that would appropriately develop a robust nonbank supervision program. The CFPB issued the Final Rule with two primary goals in mind. First, to create a consistent process applicable to all affected nonbanks, echoing its larger goal of consistent enforcement of federal consumer financial laws. Second, to provide transparency and guidance to nonbanks regarding the procedures the CFPB intends to use prior to supervision.

48. Id. § 5512(a).
49. Id. § 5512(b)(1). In issuing its rules, however, the CFPB must consider the costs and benefits to, and impact on, both nonbanks and consumers—particularly those consumers in rural areas. See id. § 5512(b)(2)(A).
50. Id. § 5512(b)(4).
51. Id. § 5514(b)(7)(A).
53. See 12 U.S.C. § 5514(b)(7)(A) (2012) (“The Bureau shall prescribe rules to facilitate supervision of persons described in subsection (a)(1) and assessment and detection of risks to consumers.”) (emphasis added); see also Petrasic & Jabour, supra note 41 (“The ability to regulate the previously unregulated is what distinguishes and defines the agency’s unprecedented powers, authority[,] and ability to formulate and execute consumer financial protection policy on a nationwide basis.”).
54. Final Rule, 78 Fed. Reg. at 40352 (explaining that, through Final Rule, the CFPB sought to “establish a consent procedure applicable to all affected entities for bringing a nonbank covered person under the Bureau’s supervisory authority pursuant to 12 U.S.C. 5514(a)(1)(C) . . .”).
55. Id. (explaining the CFPB’s goal of providing transparency to potentially affected nonbanks under 12 U.S.C. § 5514(a)(1)(C), as well as to the public).
B. An Overview of the Procedure

1. Issuing a Notice of Reasonable Cause

The process begins with the CFPB issuing a Notice of Reasonable Cause (Notice) to a nonbank target. The Notice informs the nonbank that the CFPB “may have reasonable cause to determine that the respondent is a nonbank covered person that is engaging, or has engaged, in conduct that poses risks to consumers with regard to the offering or provision of consumer financial products or services.” The Notice is based on consumer complaints or information from other sources, which may include, for example, judicial opinions and administrative decisions. The Notice itself includes a description of the basis for the assertion, a statement informing the nonbank respondent of its rights under the Final Rule, and a summary of the documents and other items that the official initiating the proceeding relied on in issuing a Notice. The Notice and all subsequent proceedings prior to examination will be confidential.

2. A Nonbank’s Response to the Notice

Once the Notice is served on the nonbank target, it has thirty days to file a written response to the CFPB setting forth its basis for...
objection to the Notice, if any. The written response must include "all documents, records, or other evidence a respondent wishes to use to support the arguments or assertions set forth in the response." 

Along with a written response, a respondent nonbank may also request to present a supplemental oral response in support of its position. However, the CFPB Associate Director may impose limitations on the oral response including, but not limited to, establishing a time frame for the presentation and limiting the subjects that may be addressed. Discovery is not permitted and no witnesses may be called to testify in connection with either the written response or the supplemental oral response.

In responding to a Notice, waiver provisions apply in three circumstances. First, a nonbank respondent’s failure to raise an argument or rely on a document in its response will constitute a waiver of the right to do so in future proceedings. Second, a failure to request a supplemental oral response will also constitute a waiver of the opportunity to do so. Third, if a nonbank respondent fails to file a written response within the thirty-day time frame, it waives the right to respond to the Notice and subsequently authorizes the CFPB to continue to the next step of the proceedings.

3. Voluntary Consent to the CFPB’s Authority

A respondent has the option to voluntarily consent to the CFPB’s supervisory authority and forego the right to contest its designation as a nonbank covered person. A consent agreement form is provided to the respondent in the Notice, but it does not provide the respondent with an opportunity to bargain for specific terms. Rather,

63. Id.
65. Id.
66. Id.
67. Id.
68. Id.
70. Id.
71. Id.
72. See id. (describing the process by which a nonbank may voluntarily consent to CFPB supervision, which involves completing and executing a consent agreement form provided to a nonbank respondent with a Notice issued by the CFPB).
a respondent who signs the consent agreement thereby agrees to be placed under the CFPB’s supervision for an unspecified time period without the option for a petition to terminate the order. Additionally, if a respondent decides to enter into the consent agreement, he subsequently waives any right to judicial review of the agreement.

4. Recommended Determination by the Associate Director

If the respondent does not voluntarily consent to the CFPB’s supervision, the Associate Director will then make a recommended determination to the Director as to whether there is reasonable cause for the CFPB to determine that the respondent is a nonbank covered person that is engaging, or has engaged in, risky conduct. The recommended determination will include either a proposed decision and order that would subject a respondent to the CFPB’s supervision if adopted by the Director, or a proposed notification that a respondent should not be subjected to the CFPB’s supervisory authority based on the proceedings. If the latter is appropriate, it does not bar the CFPB from issuing another Notice, even on the same grounds.

5. Determination by the Director

Within forty-five days of receiving the recommended determination, the CFPB Director will make a determination that either adopts, modifies, or rejects the recommended determination. The Director must either issue a decision and order subjecting the nonbank

73. See id. at 40379 (noting that a nonbank respondent that voluntarily consents to CFPB supervision will not be eligible for a petition of termination of supervision and allowing a nonbank to file a petition to terminate supervision “no sooner than two years after issuance of an order and no more frequently than annually thereafter” where a nonbank has not voluntarily consented to supervision) (emphasis added).
75. Id. at 40378 (describing the contents of the Associate Director’s Recommended Determination to be submitted to the Director).
76. Id.
77. See id. (“A proposed notification that a respondent should not be subjected to the Bureau’s supervisory authority . . . shall have no precedential effect and shall not prevent the issuance of another Notice of Reasonable Cause pursuant to either section 1091.102, or the procedures set forth in section 1091.111, at any time, or from issuance of a decision and order based on another Notice recommending that a respondent be subject to the Bureau’s authority pursuant to either of those sections.”).
78. Id. (describing the process for reaching a Determination).
respondent to the CFPB’s supervisory authority, or a notification to the contrary.\textsuperscript{79} Within his determination, the Director must include the basis for the decision and a statement that the CFPB has reasonable cause to determine that the respondent is a nonbank covered person that is engaging, or has engaged, in conduct that poses risk to consumers.\textsuperscript{80}

6. Examination and Post-Determination Termination

If a nonbank covered person is determined to be subject to the CFPB’s supervision, the CFPB may request reports and conduct examinations periodically to assess compliance with federal consumer financial laws; to obtain information about the institution’s activities, procedures, and compliance systems; and to detect and assess risks to consumers of consumer financial products and services.\textsuperscript{81} While a nonbank may petition to terminate the order, it may do so no sooner than two years after the order is issued, and no more frequently than once annually thereafter.\textsuperscript{82}

7. Option for Civil Action or Administrative Adjudication

The CFPB may, at its own discretion, decide to forego the informal process just described and seek an order to bring the nonbank under its supervision through a civil action or administrative adjudication.\textsuperscript{83} If the CFPB elects to proceed in this manner, it must still provide notice to the nonbank and allow for an opportunity to respond, but it will not be required to adhere to the process previously


\textsuperscript{80} See id. (providing that any decision and order issued by the Director must also include “[a] statement that the Director adopts the Associate Director’s proposed decision and order without revision as the Director’s decision and order, or that the Director rejects or modifies the Associate Director’s proposed Determination for reasons set forth by the Director . . . ”); see also id. (content requirements for Determination).


\textsuperscript{82} Final Rule, 78 Fed. Reg. at 40379 (“Any person subject to an order issued pursuant to [section] 1091.109(a)(1) may, no sooner than two years after issuance of such an order and no more frequently than annually thereafter, petition the Director for termination of the order.”).

\textsuperscript{83} Id. (“Nothing in this part shall be construed to limit the relief the CFPB may seek in any civil action or administrative adjudication, including but not limited to, seeking an order to have a person deemed subject to the CFPB’s supervisory authority under 12 U.S.C. 5514, including for the reasons set forth in 12 U.S.C. 5514(a)(1)(C).”).
A nonbank may also agree to enter into a consent order in connection with an adjudication proceeding or civil action, but the CFPB has the discretion to accept or reject such a request.\footnote{85}

IV. REACTION TO THE FINAL RULE

The CFPB has drawn criticism from those in the financial services industry who are concerned over the Final Rule’s potentially broad implications.\footnote{86} Standing alone, the Final Rule provides considerable latitude to the CFPB to supervise nonbank financial institutions, and viewed collectively with the CFPB’s other nonbank supervisory powers, “we see an agency with unprecedented and unparalleled power to oversee the operations of nonbank financial firms.”\footnote{87} In conjunction with its supervisory power over large bank consumer financial operations, the CFPB’s nonbank powers effectively enable it to establish a national policy for consumer financial protection.\footnote{88}

Nonbanks are concerned with the regulatory burdens imposed upon those subject to CFPB supervision, the uncertainty of CFPB action, and the disproportional impact that cost of compliance will have on smaller institutions.\footnote{89} Along these same lines, critics urge that even

\footnote{84. \textit{Id.} (“If the Bureau proceeds pursuant to paragraph (a) of this section, the provisions of [sections] 1091.101 through 1091.110, and [sections] 1091.113 through 1091.115 will be inapplicable to such proceeding.”).}

\footnote{85. \textit{Id.}}

\footnote{86. See, e.g., Daniel P. Weitzel \& Douglas P. Faucette, \textit{CFPB Establishes Procedures Relating to Supervisory Authority Over Certain Nonbanks}, LOCKE LORD QUICK STUDY (July 12, 2013), available at http://www.lockelord.com/files/Publication/8a274803-9115-44fe-a602-103efd66bbbb/Preview/PublicationAttachment/c71e927b-74bb-40cb-98aa-16fe874556de/bankregtran_2013-07_11th_CFPBRegulates_Weitzel.pdf (predicting that the market impact of the Final Rule will be “broad and deep” and is likely to create a heightened degree of uncertainty in the marketplace).}

\footnote{87. Petracic \& Jabour, \textit{supra} note 41.}

\footnote{88. Id.}

\footnote{89. See \textit{Open For Business: The Impact of the CFPB on Small Business: Hearing Before the Subcomm. on Investigations, Oversight and Regulations of the H. Comm. on Small Bus.}, 112th Cong. 6 (2011) [hereinafter \textit{Open For Business}] (testimony of Daniel Fleming, President, Fleming Leasing, Alexandria, Va.) (explaining that small businesses anticipate having to hire clerks to comply with data collection requirements, which is a significant investment for many smaller institutions); see also Letter from Stuart K. Pratt, President and CEO, Consumer Data Indus. Ass’n, to Monica Jackson, Admin. Specialist, Consumer Fin. Prot. Bureau (July 24, 2012) (“Preparation costs alone are significant, even if an exam does not occur . . . . Regardless of whether a rule setting standards for supervision imposes ‘substantive conduct requirements,’ it continues to be the case that any covered
that the mere threat of CFPB supervision could have a chilling effect on the industry and stifle innovation within the market for consumer financial products and services.\textsuperscript{90} In addition to such potential repercussions, nonbanks question whether the Final Rule provides them with a reasonable opportunity to respond, or whether unbridled CFPB discretion makes supervision imminent.\textsuperscript{91}

\textit{A. Major Criticisms of the Final Rule}

1. A Subjective Standard for Risk Determination

The public comments that the CFPB received in connection with the Final Rule express concern over the standard it intends to use for risk determination.\textsuperscript{92} Because the CFPB may only supervise nonbanks that it has reasonable cause to determine pose risks to consumers, nonbanks are understandably anxious for guidance as to what qualifies as “risk.”\textsuperscript{93} This concern is further justified by the fact that most of the nonbank institutions subject to the Final Rule were previously unregulated and have a limited understanding of their responsibilities and expectations under Dodd-Frank.\textsuperscript{94}

As one commenter noted, consumer financial products and
services are inherently risky. Personal loans, mortgages, auto-financing, and other similar products all pose some degree of risk to the consumer, and perhaps no transaction involving a consumer financial product or service is risk-free. Commenters contend that Congress could not have intended risk in this broad sense to be the standard for a reasonable cause determination. Therefore, they urged the CFPB to define “risk” in a manner that would provide clear guidance as to the type of conduct that would subject a nonbank to supervision.

2. Unverified Complaints and Information May Lead to a Notice that is a “False Alarm”

The Final Rule contains no provision that requires the CFPB to verify the validity and accuracy of the information it receives from consumer complaints and other sources before issuing a Notice. Without a vetting mechanism for neutralizing fraudulent or baseless complaints, nonbank proponents argue that the complaint system may be subject to abuse by advocacy groups, competitors, “confused consumers,” and even bloggers who have no intention of using the system for its designated purpose. The same could also be said for

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95. Letter from Bill Himpler, Exec. Vice President, Am. Fin. Servs. Ass’n, to Monica Jackson, Admin. Specialist, Consumer Fin. Prot. Bureau (July 24, 2012); see also Pratt, supra note 89.
96. Himpler, supra note 95.
97. Pratt, supra note 89.
98. Himpler, supra note 95.
100. See id. at 40358-59 (declining to revise the Proposed Rule to require the CFPB to verify complaints or to identify information from “other sources” that provide the basis of a Notice); see also id. at 40376 (describing the contents of a Notice).
101. See CONSUMER FINANCIAL PROTECTION BUREAU, CONSUMER RESPONSE: A SNAPSHOT OF COMPLAINTS RECEIVED (2012), http://files.consumerfinance.gov/f/201206_cfpb_snapshot_complaints-received.pdf (explaining “Consumer Confusion” as it applies to the market for financial products and services and suggesting that nonbanks will not be penalized for consumer confusion).
102. See, e.g., Himpler, supra note 95; Letter from Wendy Harp-Lewis, Chief Compliance Officer, Vice President Corp. Legal, Intelispend Prepaid Solutions, to Monica Jackson, Admin. Specialist, Consumer Fin. Prot. Bureau (July 18, 2012); Letter from Louis S. Freedman, President, Nat’l Ass’n of Retail Collection Attorneys, to Monica Jackson, Admin. Specialist, Consumer Fin. Prot. Bureau (July 24, 2012); Letter from Kirsten Trusko, President and Exec. Dir., The Network Branded Prepaid Card Ass’n, to Monica Jackson, Admin. Specialist, Consumer Fin. Prot. Bureau (July 20, 2012); Letter from David C. Jones, President, Ass’n of Indep. Consumer Credit Counseling Agencies, to Monica Jackson, Admin. Specialist, Consumer Fin. Prot. Bureau (July 24, 2012).
“information from other sources” where it may be difficult to verify the accuracy and context of the information given the range of sources the CFPB may consider.\(^\text{103}\)

Additionally, critics claim there are no stops in place to prevent the CFPB from basing a Notice on complaints that have already been resolved by the nonbank institution.\(^\text{104}\) Where a substantial number of complaints alleging major transgressions and consumer risks may be sufficient to trigger a Notice, critics urge that there should be a substantial effort to verify the accuracy of such information or that the information be provided to a nonbank target before the CFPB uses such information as a basis for asserting its supervisory authority.\(^\text{105}\) Otherwise, as critics point out, it would be difficult for a nonbank to object to a Notice where it does not know why its conduct has been classified as risky.\(^\text{106}\)

Furthermore, critics argue that consumer complaints may not be an accurate gauge of the financial industry’s compliance level with consumer protection laws.\(^\text{107}\) It may be the case that the CFPB issues a Notice even where a nonbank has taken steps to disclose risks in its financial products or services without having violated any law or regulation.\(^\text{108}\) The very nature of complaints, which are often derogatory, aggressive, and without proper context, poses an inherent risk of the CFPB issuing Notices that are merely “false alarms.”\(^\text{109}\) In this regard, examining the number of complaints against a nonbank exacerbates the threat. For example, 100 complaints against a small

\(^{103}\) See, e.g., Himpler, supra note 95. It is worth mentioning, however, that other federal agencies (OCC, FRB, FDIC, OTS, NCAU, and FTC) published a final rule to enhance the accuracy and integrity of information furnished to consumer reporting agencies under § 312 of the Fair and Accurate Credit Transactions Act. They found that the percentage of frivolous or irrelevant disputes could range from 25 percent to 94 percent. See 74 Fed. Reg. 31484 (2009) (codified at scattered sections throughout Code of Federal Regulations).

\(^{104}\) See, e.g., Harp-Lewis, supra note 102.

\(^{105}\) See, e.g., Himpler, supra note 95; Trusko, supra note 102 (expressing concern over presumption of guilt in the proceedings based on inaccurate information collected by the CFPB); Jones, supra note 102; Letter from Eric D. Harris, MoneyGram, to Monica Jackson, Admin. Specialist, Consumer Fin. Prot. Bureau (July 24, 2012).

\(^{106}\) Beato & Jed Wulfekotte, supra note 92.

\(^{107}\) Id.

\(^{108}\) Id.

nonbank could have much more significance than the same number of complaints against a larger entity. Similarly, 100 complaints about lawfully permissible debt collection should be distinguished from 100 complaints of actual wrongdoing. Commenters agree that if the complaints are not furnished to a nonbank target, then a more comprehensive evaluation of the complaints seems in order to allow respondents an opportunity to develop an appropriate response.

The nature of the CFPB’s complaint system may also prove problematic for a nonbank filing a response to a Notice. When an institution makes its written response to the allegations, it must set forth all of its arguments and present all documents and evidence on which it plans to base its contentions. Otherwise, a nonbank waives the right to rely on an argument or document in future proceedings. Yet the CFPB may be requesting a response based on an enormous amount of material that has to be reviewed, compiled, and delivered in a relatively short timeframe. When only a summary of the CFPB’s information is available to a nonbank, critics are concerned that the summary may lack specific details that would otherwise allow for a comprehensive response. A nonbank may be inclined to submit more information than necessary to respond to the CFPB’s Notice, or it may fail to include an important piece of evidence addressing a specific document that was only included in summary fashion. Institutions may ultimately find themselves under the CFPB’s supervision because a document not included in a written response could have demonstrated that supervision was unnecessary.

In a similar vein, the Final Rule’s waiver provisions heighten the concerns expressed over the complaint system. The CFPB notes that the waiver provision helps ensure that it is aware of all relevant

111. Id.
112. Himpler, supra note 95; Harris, supra note 105.
114. Id.
115. Trusko, supra note 102 (expressing concern over substantive matters to be addressed within twenty-day time frame). But see Final Rule, 78 Fed. Reg. at 40363 (amending the time period for a response from twenty days to thirty days).
116. See Trusko, supra note 102.
issues that a respondent wishes to rely upon at the earliest opportunity before reaching a determination. While it may be inefficient to have a respondent submit evidence to the CFPB on a rolling basis, it may be effective to consider additional evidence arising after a nonbank's response before both sides expend resources pursuant a Notice that is merely a "false alarm."  

3. An Inadequate Opportunity to Respond Through the Informal Proceedings

Nonbanks are concerned that the informal nature of the proceedings will not afford them an adequate opportunity to respond. Accordingly, some would prefer an option for formal adjudication under the Final Rule. If the CFPB has the authority to bring a civil action against a nonbank respondent, critics argue, then nonbanks should also have the option for formal adjudication. Moreover, without the option to conduct discovery or call witnesses to support its position in a written or supplemental oral response, a nonbank may view formal adjudication as a worthwhile cost to provide greater procedural protections in an effort to avoid supervision.

Beyond the potential expenses incurred in examination, preparation costs alone may be significant—especially for smaller institutions. Considering the staffing and resource constraints within smaller nonbanks, the informal process may impose a substantial burden on companies who may be unaware that they are within the boundaries of the CFPB's supervisory authority and are less likely to have counsel capable of responding to a Notice within the requisite timeframe. Moreover, it seems unclear what types of reports and

119. The Final Rule does not specifically address whether the CFPB may consider additional information it receives in reaching a Determination after a nonbank has filed a response. See id. at 40378 (describing the process that the Associate Director and the Director will use to reach a Determination).
120. See, e.g., Nat'l Indep. Auto. Dealers Ass'n, supra note 91.
121. Harp-Lewis, supra note 102; Trusko, supra note 102.
122. Harp-Lewis, supra note 102.
124. Pratt, supra note 89.
125. Himpler, supra note 95.
examinations will be required for a nonbank supervised by the CFPB, and the difficulty in predicting its obligations may impose additional hardship.\textsuperscript{126}

Although nonbank respondents have the option to voluntarily consent to CFPB supervision, there is hardly an incentive to do so. A consent agreement provides a unilateral benefit to the CFPB with no discernible benefit to the nonbank target.\textsuperscript{127} It allows the CFPB to impose an indefinite examination period rather than a two-year minimum, which raises questions as to why entities that voluntarily consent to the CFPB's authority should be subject to harsher treatment.\textsuperscript{128} Regardless of whether a nonbank consents to supervision, critics argue, nonbanks should have the opportunity to petition for termination of the order once it discontinues the alleged risky practice since additional examination beyond that point would seem meaningless.\textsuperscript{129} Additionally, waiving any right to judicial review of the consent agreement may be seen as "an inappropriate and indefinite surrender of access to the judicial system as a condition of voluntary cooperation."\textsuperscript{130}

\textbf{B. Defending the Final Rule in Light of the CFPB's Mission to Level the Playing Field}

1. Providing Additional Guidance for Risk Determination May Undermine CFPB Objectives

While the CFPB's standard for risk determination may be initially frustrating to nonbanks looking for a safe harbor, providing such specific guidance in the Final Rule may be premature. The CFPB is responsible for consistently enforcing consumer financial protection laws—especially in innovative markets for consumer financial products and services.\textsuperscript{131} Congress established a broad standard for the CFPB's risk determination analysis, but without a clear understanding of how it

\textsuperscript{126.} Commercial Law League of Am., \textit{supra} note 117.

\textsuperscript{127.} See Final Rule, 78 Fed. Reg. at 40378-79.

\textsuperscript{128.} Jones, \textit{supra} note 102.

\textsuperscript{129.} Harris, \textit{supra} note 105.

\textsuperscript{130.} Jones, \textit{supra} note 102.

applies in particular facts and circumstances, the CFPB is careful not to create exceptions that may backfire as markets for new financial products and services develop.

All covered persons are legally required to refrain from engaging in unfair, deceptive or abusive acts or practices (UDAAP) in violation of Dodd-Frank. The CFPB’s supervisory authority is one avenue it may take for detecting and assessing risks to consumers and to markets for consumer financial products and services. Consistent with the objectives of Dodd-Frank, in evaluating “risk to consumers” for its reasonable cause determination the CFPB intends to consider practices that involve “potentially unfair, deceptive, or abusive acts or practices, or . . . conduct that otherwise potentially violates applicable [f]ederal consumer financial law.”

The standard for unfairness involves a three-part test. An act or practice is unfair when: (1) it causes or is likely to cause substantial injury to consumers; (2) the injury is not reasonably avoidable by consumers; and (3) the injury is not outweighed by countervailing benefits to consumers or to competition. Substantial injury typically


134. See 12 U.S.C. § 5511(b) (2012) (describing objectives of the CFPB in exercising its authority to ensure “consumers are provided with timely and understandable information to make responsible decisions about financial transactions; consumers are protected from unfair, deceptive, or abusive acts and practices and from discrimination; outdated, unnecessary, or unduly burdensome regulations are regularly identified and addressed in order to reduce unwarranted regulatory burdens; [f]ederal consumer financial law is enforced consistently, without regard to the status of a person as a depository institution, in order to promote fair competition; and markets for consumer financial products and services operate transparently and efficiently to facilitate access and innovation”). But see Final Rule, 78 Fed. Reg. 40352, 40358 (July 3, 2013) (“[A]lthough not expressly applicable to an (a)(1)(C) proceeding, the Bureau may consider the (b)(2) factors to the extent applicable in making a reasonable-cause determination.”).

135. Final Rule, 78 Fed. Reg. at 40357 (explaining, generally, the type of conduct the CFPB will consider in evaluating risks to consumers for purposes of 12 U.S.C. § 5514(a)(1)(c)).

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involves monetary harm including, for example, costs or fees paid by a consumer resulting from an unfair practice. However, consumers must not be able to reasonably avoid the injury. The question is not whether a consumer could have made a better choice, but whether an act or practice hinders a consumer’s decision making, for example, by denying them access to important information to compare alternatives and select the best available option. Finally, to be unfair, the act or practice must be “injurious in its net effects.” Taking into account costs that would be incurred to prevent the injury, the injury must not be outweighed by any offsetting consumer or competitive benefits, such as lower prices, wider availability of products, or services resulting from competition.

Although Congress has not defined “deceptive” with regards to UDAAP, the CFPB adopted its deception standard from the FTC. A representation, omission, act or practice is deceptive when it misleads or is likely to mislead a consumer; the consumer’s interpretation of the representation, omission, act or practice is reasonable under the circumstances; and the misleading representation, omission, act, or practice is material. Whether the overall impression is misleading or deceptive depends on the context of a transaction, course of dealing, or advertisement, and must be evaluated from the perspective of a reasonable member of the target audience. Information is material if it is likely to affect a consumer’s choice of, or conduct regarding, the product or service.

Inadequate disclosures of material lease terms in

on-unfairness (adopting unfairness standard in consumer transactions).

137. UDAAP, supra note 136, at 2. Even an act that causes a small amount of harm to a large number of people may be considered to cause substantial injury. Id.
138. Id.
139. Id.
140. Id. at 3.
141. Such costs may include, for example, costs to the institution in taking preventative measures and costs of increased burden to society as a whole. Id.
142. UDAAP, supra note 136, at 3.
143. However, while it is clear that “deceptive” means something different than “unfair” or “abusive,” the CFPB concedes that it is not aware of any conduct that would be “deceptive” and not also “unfair” or “abusive.” The Semi-Annual Report of the Consumer Financial Protection Bureau: Hearing Before the H. Comm. on Fin. Servs., 112th Cong. 14 (2012) [hereinafter Semi-Annual Report].
144. UDAAP, supra note 136, at 5.
145. Id. at 5-6.
146. Id. at 6. Express claims made with respect to a financial product or service, as well as information regarding the central characteristics of a product or service including costs,
television advertising and misrepresentation about loan terms, for example, have previously resulted in FTC action and are equally as likely to trigger the deceptive standard when considered by the CFPB.\textsuperscript{147}

Congress added "abusive" as a UDAAP component to create a broader standard beyond the FTC's authority to regulate nonbanks engaging in "unfair or deceptive acts or practices."\textsuperscript{148} An abusive act or practice is one that

1. materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or
2. takes unreasonable advantage of—
   - a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;
   - the inability of the consumer to protect the interests of the consumer in selecting or using a consumer financial product or service; or
   - the reasonable reliance by the consumer on a covered person to act in the interests of the consumer.\textsuperscript{149}

"Abusive" means something other than unfair or deceptive, but Congress's definition is situational and subjective.\textsuperscript{150} To a large extent, it appears to be a "facts and circumstances" test,\textsuperscript{151} and CFPB Director Richard Cordray has emphasized that "reasonableness" is a factor

\textsuperscript{147} UDAAP, \textit{supra} note 136, at 7.
\textsuperscript{149} 12 U.S.C. § 5531(d) (2012).
\textsuperscript{150} Semi-Annual Report, \textit{supra} note 143, at 14 (testimony of Richard Cordray, Director, Consumer Financial Protection Bureau) (explaining the "abusive" standard used for risk determination).
\textsuperscript{151} \textit{Id.} (explaining that most good businesses will recognize an abusive practice when they see one).
particularly relevant to the standard.\textsuperscript{152}

While the CFPB may further define "abusive,"\textsuperscript{153} not only does it run the risk of contradicting Congress,\textsuperscript{154} but providing more substantive guidance for risk determination at this stage would undermine its mission to address risky practices that have yet to be identified.\textsuperscript{155} In order to craft effective policy to level the playing field, agency rules must be broad enough so that they are not easily circumvented, but narrow enough so as not to limit consumers' options in purchasing financial products or services.\textsuperscript{156} This balancing act has led other regulators, such as the Federal Reserve Board (FRB), to address potentially unfair and deceptive practices through case-by-case examinations, rather than through rulemaking.\textsuperscript{157} Accordingly, without prior case law or guidance from the FTC, the CFPB may similarly resort to its examination function over other nonbanks as a tool to appropriately develop the abusive standard.\textsuperscript{158}

\begin{itemize}
  \item \textsuperscript{152} Id.; see also Kevin L. Petrasic & Amanda J. Kowalski, \textit{The New UDAAP: The CFPB "Abusive" Standard – Will You Know It When You See It?}, \textit{STAY CURRENT} (June 2013), available at http://www.paulhastings.com/Resources/Upload/Publications/The_New_UDAAP_-_The_CFPB_"Abusive"_Standard_-_Will_You_Know_It_When_You_See_It_.pdf (discussing the lack of guidance regarding the CFPB's abusive standard within UDAAP).
  \item \textsuperscript{153} See \textit{SUPERVISION AND EXAMINATION MANUAL}, supra note 133 ("Public policy, as established by statute, regulation, judicial decision, or agency determination, may be considered with all other evidence to determine whether an act or practice is unfair.").
  \item \textsuperscript{154} \textit{Semi-Annual Report}, supra note 143, at 14 (testimony of Richard Cordray, Director, Consumer Financial Protection Bureau).
  \item \textsuperscript{155} See \textit{H. Comm. On Fin. Servs. Holds A Hearing On The Consumer Financial Protection Bureau Report}, 112th Cong. 15 (2012) [hereinafter \textit{CFPB Report Hearing}] (testimony of Richard Cordray, Director, Consumer Financial Protection Bureau) (responding to a question from Chairman Bachus regarding whether the CFPB should provide further guidance to the "abusive" standard, Cordray stated, "No, I don't think so. I just don't think that is probably the preferred approach, when Congress has defined the term already. We could further define the term, but are we going to define it differently from what Congress defined? I don't think so. We could perhaps clarify how it applies in particular facts and circumstances. But I think we ought to take some time with it, rather than up and just pontificating about it at the beginning . . . We are trying to be careful, here, measured and thoughtful. Sometimes that means you don't have all the answers in the first instance").
  \item \textsuperscript{156} \textit{Improving Consumer Protection in Financial Services, Hearing Before the H. Comm. on Fin. Servs.}, 110th Cong. 13 (2007) (statement of the Honorable Randal S. Kroszner, Governor, Board of Governors of the Federal Reserve System) (describing the nature of effective agency rulemaking authority).
  \item \textsuperscript{157} \textit{Id.} (noting that both the FRB and FTC have addressed potentially unfair and deceptive practices through case by case determinations rather than rulemaking because of the challenges in crafting effective rules).
  \item \textsuperscript{158} \textit{See Open For Business}, supra note 89, at 6 (testimony of Dan Sokolov, Deputy Associate Director, Consumer Financial Protection Bureau) ("It can be challenging to
Otherwise, explicitly delineating substantive standards for risky conduct may inadvertently carve out an exceptional safe haven for nonbanks that may pose risks to consumers through innovative products and services in consumer financial markets. In recognition of the CFPB’s mission to illuminate harmful misconduct in the shadow banking industry, restricting the scope of authority at this stage would undercut its flexible and proactive approach to consumer protection.¹⁵⁹ Even if it means the CFPB does not have all of the answers at this point, clarifying the standard over time is a more “measured and thoughtful” approach.¹⁶⁰

2. An Informal Mechanism to Verify Complaints and Other Sources of Information

Many of the concerns regarding the threat of the CFPB using inaccurate information are misplaced. The data collection phase is not intended to determine whether a nonbank has violated federal consumer protection laws or harmed consumers,¹⁶¹ and it can hardly be assumed


¹⁶¹. Final Rule, 78 Fed. Reg. 40352, 40359 (July 3, 2013) (“[The] process is not intended to determine whether a nonbank covered person has, in fact, violated applicable Federal consumer financial laws or harmed consumers. The level of inquiry necessary to make a finding of a violation of law would instead, occur, . . . in the course of supervisory activity such as an examination.”).
that the CFPB blindly bases a Notice solely on the number of complaints it receives. Rather, the CFPB intends to consider, among other things, the nature of the conduct relating to the complaints or other information, the severity of the risk alleged, and the number of consumers potentially affected.\textsuperscript{162} Taken together, these factors afford nonbanks a level of protection in weeding out frivolous complaints and minimizing the danger of equating the number of complaints against a nonbank with the risks actually posed to consumers.\textsuperscript{163}

More importantly, although it is not expressly described as a verification process, providing a nonbank with an opportunity to respond through a written and supplemental oral response serves the same function for verifying the information used for risk determination. Unless a document contains confidential or otherwise personally identifiable information, the CFPB places complaints in a public database and, therefore, nonbank respondents should typically have access to copies of the information the CFPB relied on to issue a Notice.\textsuperscript{164} If there is an incentive to address allegations at the outset of the process, then regardless of whether the specific complaints or information are provided to the nonbank, they would be advised to offer all relevant documentation and evidence that may be pertinent to the inquiry. Not only is this procedure common practice within administrative investigation,\textsuperscript{165} but it allows the CFPB to streamline the determination process through a diluted cross-examination mechanism. The CFPB combines verification and response into a single phase, allowing the agency to determine where supervision is needed, and where conduct is not risky enough to warrant the cost of examination.

Yet even those institutions that remain skeptical of this informal verification method have an independent opportunity to proactively address their concerns about inaccurate complaints. Since the entire

\textsuperscript{162} See id. (describing the factors the CFPB intends to consider with regard to complaints in deciding whether there is a sufficient basis to issue a Notice).

\textsuperscript{163} See id. ("The Bureau is committed to using its limited resources where most needed and intends to consider complaints and information from other sources with the efficient use of Bureau resources in mind.").

\textsuperscript{164} Id. at 40361; see Disclosure of Certain Credit Card Complaint Data, 77 Fed. Reg. 37558, 37568 (June 22, 2012) (explaining the CFPB's policy regarding public access to certain consumer complaints).

process is data-driven, nonbanks are advised to develop their own comprehensive complaint system to file, track, and resolve consumer complaints internally.\textsuperscript{166} Reviewing consumer complaints to identify patterns will allow nonbanks to develop a strong compliance program to internally examine practices for potentially unfair, deceptive, or abusive conduct.\textsuperscript{167} Addressing the problem upfront decreases the likelihood that disgruntled consumers will file separate complaints with the CFPB and will subsequently minimize the threat of CFPB supervision. This recommended action may have been an intended consequence by the CFPB, allowing it to retain a broad jurisdictional scope while recognizing the practical limitations of directly supervising every nonbank financial institution.\textsuperscript{168}

3. The Final Rule Provides Nonbanks with an Opportunity to Contest Supervision

The Final Rule addresses the threshold question of whether the CFPB has the authority to supervise the nonbank entity. Dodd-Frank explicitly grants the CFPB supervisory authority over certain nonbank institutions,\textsuperscript{169} which effectively requires them to leave their doors open to the CFPB for examinations.\textsuperscript{170} However, such authority exists in the context of § 5514(a)(1)(C) only where the CFPB, after providing notice and an opportunity to respond, has reasonable cause to determine that a nonbank poses a risk to consumers.\textsuperscript{171} Accordingly, prior to any

\begin{footnotesize}
\begin{enumerate}
\item[166.] Leonard N. Chanin, \textit{How to Avoid Enforcement Actions for Unfair or Deceptive Acts and Practices}, \textit{Banking Daily} (Sept. 16, 2013), http://news.bna.com.libproxy.lib.unc.edu/bdl/BDLNWB/split_display.adp?fedfid=36501853\&vname=bddbulallissues&split=0 (recommending a strong internal compliance program to proactively address potential UDAAP issues because regulatory agencies expect institutions to have robust compliance systems, monitor practices, and take remedial action, although “[d]oing so may not always prevent agency action, . . . even agency staff are human”).
\item[167.] Id.
\item[168.] See Petrasic & Labour, supra note 41 (noting that the uncertainty in how far the CFPB may stretch to gain supervisory authority over a nonbank appears intentional for the CFPB to achieve its statutory mandate).
\item[169.] See 12 U.S.C. § 5514 (2012) (describing nonbank covered persons subject to CFPB supervisory authority); see also Final Rule, 78 Fed. Reg. 40352, 40352 (July 3, 2013) (providing that nonbank entities are subject to applicable federal consumer financial laws regardless of whether they are subject to the CFPB's supervisory authority).
\item[170.] See 12 U.S.C. § 5514 (authorizing the CFPB to supervise certain nonbanks to assess compliance with federal consumer financial laws, obtain information regarding activities and compliance systems, and assess risks to consumers).
\item[171.] Id. § 5514(a)(1)(C).
\end{enumerate}
\end{footnotesize}
examination or any service of compulsory process, a nonbank has an opportunity to challenge the CFPB’s supervisory authority altogether.\textsuperscript{172}  

Moreover, the informal proceedings provide a less expensive alternative to a more formal, rigid process of investigation employed by other regulators.\textsuperscript{173} Neither the CFPB nor a nonbank respondent is forced to invest significant time or resources until after the CFPB can demonstrate its basis for authority.\textsuperscript{174} While other regulatory agencies such as the Office of the Comptroller of the Currency (OCC) and the FTC may offer a more robust opportunity for rebuttal, it is only within the context of formal adjudications and civil proceedings that these protections exist. Section 5514(a)(1)(C) does not require that a nonbank have the same opportunity to respond that it would in a formal proceeding because the Final Rule does not affect the substantive rights of any nonbank covered person.\textsuperscript{175} Supervision alone does not impose a penalty on a nonbank covered person, nor does it deprive a nonbank of any property or restrict its ability to engage in a viable business.\textsuperscript{176} Regardless of whether nonbanks are subject to the CFPB’s supervisory authority, they are still subject to federal consumer financial laws and CFPB enforcement power.\textsuperscript{177}

V. CONCLUSION: FUTURE CHALLENGES FOR THE CFPB AND CONSEQUENCES TO NONBANKS

The Final Rule serves as a spotlight for the CFPB to penetrate the shadow banking system to proactively address risky practices in emerging markets for consumer financial products and services. The CFPB’s supervisory jurisdiction is directed toward filling the gaps created by prior regulatory fragmentation and “larger participant” definitions that overlook smaller, yet noteworthy competitors. The


\textsuperscript{173} See generally Rules of Practice, 77 Fed. Reg. 3191 (Jan. 23, 2012) (describing the FTC’s proposed rule to improve investigatory procedures to make them more fair for respondents).

\textsuperscript{174} See Certner, supra note 172.


\textsuperscript{176} Id. at 40359.

\textsuperscript{177} Id. at 40353 (“[T]he final rule does not impose on nonbank covered persons any new substantive requirements... nonbank covered persons already must comply with applicable consumer financial law, and a final rule is not necessary to implement the Bureau’s supervisory authority under 12 U.S.C. 5514(a)(1)(C).”).
CFPB is adequately armed to extend its supervision over even the smallest institutions that choose not to abide by existing laws and regulations, ensuring a level playing field in markets for consumer financial products and services.  

The Final Rule also illustrates how the CFPB is able to use its authority over nonbanks to establish a national policy for consumer financial protection. Its broadly defined UDAAP standard, its data-driven complaint system, and its informal procedures allow the CFPB to advance its agenda for transparent, competitive markets through a hands-off approach. The CFPB cannot practically examine every nonbank institution for compliance with consumer financial protection laws, but the threat of supervision under the Final Rule may be adequate to encourage nonbanks to develop internal compliance and consumer complaint systems.

The CFPB has yet to initiate a proceeding under the Final Rule, but its ability to retain and defend its power "to regulate the previously unregulated" will ultimately depend on how it uses its nonbank supervisory authority. It could use the Final Rule to supervise institutions offering structured settlement, debt settlement, credit repair, tax preparation and tax restructuring services. Additionally, it may choose to supervise smaller entities within the "larger participants" markets, or over all nonbanks within a particular industry where a systematic violation is identified. Regardless of which entities become subject to the Final Rule, how the CFPB manages its power will be crucial to the success of its nonbank supervision program: "[m]anaged with a deft touch, the agency will

179. Petrasic & Jabour, supra note 41.
180. See, e.g., Chanin, supra note 166.
182. Petrasic & Jabour, supra note 41.
183. Weitzel & Faucette, supra note 181.
almost assuredly prosper; however, too light a touch or a heavy hand... could have repercussions on the U.S. economy as well as for the ability of U.S. financial firms to compete internationally.”

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185. Petrasic & Jabour, supra note 41.