Banking and Finance Law Daily Wrap Up, TOP STORY—5th Cir.: FHFA organization violates separation of powers, unlike CFPB organization, (Jul. 18, 2018)

Banking and Finance Law Daily Wrap Up

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By Richard A. Roth, J.D.

Congress went too far in its effort to create a Federal Housing Finance Agency that would not be subject to political influence, a deeply divided three judge panel of the U.S. Court of Appeals for the Fifth Circuit has decided. An independent agency can be insulated, but it cannot be isolated, the opinion of the court said. As a result, the provisions of the Housing and Economic Recovery Act that allow the president to remove the FHFA director only for cause must be severed from the remainder of the Act, rendering the director removable at the president's discretion (*Collins v. Mnuchin*, July 16, 2018, *per curiam*).

The separation of powers discussion bears a striking similarity to the analysis of the Consumer Financial Protection Bureau's organization in *PHH Corp. v. CFPB*. However, the Fifth Circuit distinguished the two agencies by noting that the CFPB is restrained by the ability of the Financial Stability Oversight Council to block the Bureau's regulations from taking effect. There is no similar restraint on the FHFA, and that leads to a different result.

GSE shareholders' challenge. The genesis of the opinion was a suit by Fannie Mae and Freddie Mac shareholders who were challenging the "net worth sweep"—an agreement under which the Treasury Department provides financial support to the GSEs in exchange for quarterly dividends that equal each of the GSEs' net worth. The shareholders raised two claims: the FHFA exceeded its statutory authority in reaching the agreement, and the FHFA was structured unconstitutionally.

The opinion of the court examined the effect of five organizational factors on the constitutionality of the FHFA:

1. the for-cause protection from removal;
2. the single-director structure;
3. the absence of bipartisan balance;
4. the exemption from the appropriations process; and
5. the lack of formal executive branch control over the FHFA's operations.

While none of the five factors decided the outcome of the case individually, the combination of them all interfered with the president's ability to carry out his Constitutional duty of ensuring that federal laws were enforced, according to the opinion of the court.

FHFA v. CFPB. It was the fifth factor that separated the FHFA's structure from that of the CFPB, the opinion of the court said. The FHFA is supervised by the Federal Housing Finance Oversight Board, the court noted; however, that entity is purely advisory and has no authority to impose any requirements on the FHFA.

On the other hand, the FSOC has the power to nullify CFPB regulations that threaten the safety and soundness of the banking system or the stability of the financial system. A supermajority of the FSOC's 10 members are selected by the president, the opinion pointed out. That creates an "emergency brake" that is adequate to make the Bureau accountable to the president.

Severance as remedy. Like the three-judge panel in the D.C. Circuit's first *PHH Corp. v. CFPB* opinion, the court refrained from striking down the entire FHFA. Rather, it deemed the severance of the offending for-cause protection clause from the rest of the Act to be an adequate remedy. As a result, the FHFA will be converted to "a properly supervised executive agency."

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Dissenting opinions. Two of the three judges dissented from parts of the opinion of the court, which apparently was written by Judge Catharina Haynes.

Chief Judge Carl E. Stewart disagreed with the opinion of the court on the constitutionality issue. He echoed the *en banc* majority opinion in *PHH*, but added that he believed the FHFA also is subject to adequate presidential oversight. Judge Stewart was unconvinced that the FHFOB is not a sufficient check on the FHFA, even if it is merely an advisory board.

Judge Don Willett agreed that the FHFA is unconstitutional. However, he disagreed with a different, unrelated part of the opinion of the court—that HERA's anti-injunction provisions bar the shareholders from suing the agency. According to Judge Willett, the anti-injunction provision prevents suits against the FHFA as conservator; however, the new worth sweep was a step the agency could take only as the GSEs' receiver. The distinction makes the anti-injunction provisions inapplicable.

The case is No. 17-20364.

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