Congressional Research Service
Informing the legislative debate since 1914

Legal Sidebar

Fifth Circuit: CFPB's Funding Authority is Unconstitutional

Updated March 9, 2023

In 2010, Congress established the Consumer Financial Protection Bureau (the CFPB or Bureau) as an independent bureau within the Federal Reserve System. As with other financial regulators, Congress gave the CFPB more independence from political control than a typical Cabinet department. One director, serving a five-year term, would oversee the Bureau's rulemaking, enforcement, and adjudication functions for federal consumer financial laws. The director would not hold this position at the pleasure of the President, but instead could be removed only for "inefficiency, neglect of duty, or malfeasance in office." The director also would not depend on annual appropriations. Funding would come mostly from the combined earnings of the Federal Reserve.

A decade after the CFPB's creation, though, the Supreme Court in *Seila Law LLC v. Consumer Financial Protection Bureau* held that the Bureau's structure violated the constitutional separation of powers. The Court explained that the for-cause removal provision was "enough to render the agency's structure unconstitutional." The Court added that the Bureau's permanent funding source further aggravated the President's inability to control the director because the President could not influence the director by recommending or vetoing annual appropriations bills. However, the Court did not hold that the funding authority, itself, was unconstitutional. Severing the removal provision from the statute was enough to cure the constitutional defect because the President could now remove the director at will.

While the Bureau's funding authority occupied the background in *Seila Law*, it fills the foreground in a recent decision of the U.S. Court of Appeals for the Fifth Circuit (Fifth Circuit), *Community Financial Services Association of America v. Consumer Financial Protection Bureau*. On October 19, 2022, the Fifth Circuit held that the CFPB's funding authority violated the Constitution's Appropriations Clause and the separation of powers. On February 27, 2023, the Supreme Court granted the government's petition to review the Fifth Circuit's decision.

The Fifth Circuit's decision is significant as the first appellate decision—and perhaps the first court decision ever—to conclude that congressional action, as opposed to executive or judicial action, can violate the Appropriations Clause. This Sidebar examines the Fifth Circuit's decision and its potential implications for the Bureau's continued operations.

Congressional Research Service
https://crsreports.congress.gov
LSB10891

Federal Funding Principles and the CFPB

The Appropriations Clause states that "[n]o Money shall be drawn from the Treasury, but in Consequence of Appropriations made by Law." The clause's chief function is to constrain the disbursing power of executive branch officials. Payments from the Treasury can be made only if allowed by an appropriation made by an act of Congress.

The U.S. Constitution imposes two constraints on the process that Congress may use to enact appropriations. First, appropriations must be made through bicameral passage and presentment just like other statutes. Second, appropriations to "raise and support Armies" may not exceed a two-year term. The Constitution does not prescribe anything else about the process for making appropriations.

Congress's process for making appropriations has evolved substantially since ratification of the Constitution. Today, Congress provides spending authority in statutes that, during their congressional consideration, fall into one of two general procedural categories. These congressionally established categories reflect Congress's judgment about the best way to make legislative decisions. The first category of legislation that provides spending authority is an *appropriations bill.* Such legislation provides funding for the ongoing operation of federal departments, agencies, and government activities for a particular fiscal year. The appropriations provided in these bills are categorized as *discretionary* authority. The appropriations committees have jurisdiction over appropriations bills. For the most part, programs funded by these bills receive fixed-period appropriations, whose spending authority expires after a date certain. To continue the program, Congress must provide new appropriations. Congressional practice has been to enact appropriations bills in some form annually.

The second category of bills that Congress uses to provide spending authority are *direct spending bills*, which are under the jurisdiction of legislative committees. Funding provided in this way is also termed *mandatory* authority. Typically, when Congress provides mandatory authority, it remains available without annual congressional action unless modified or repealed by a later statute. Programs funded in this way (e.g., Medicare, Social Security) constitute the majority of annual federal outlays.

The Bureau is not funded through discretionary funds from an appropriations act. The Bureau relies on mandatory funding, chiefly through its Consumer Financial Protection Fund (the Bureau Fund or Fund). Congress does not make annual appropriations to the Bureau Fund, and by statute, the Fund is not "subject to review" by the appropriations committees. Instead, the statute authorizes the Bureau's director to determine the amount "reasonably necessary to carry out the authorities of the Bureau" and request that amount from the Board of Governors of the Federal Reserve System. The Federal Reserve Board must then transfer from its combined earnings to the Bureau Fund the amount specified by the director, so long as it does not exceed a fixed percentage of the Federal Reserve's operating expenses. Congress stipulated that amounts in the Bureau Fund "shall not be construed to be Government funds or appropriated monies." Amounts in the Bureau Fund are "immediately available" and do not expire.

The Bureau's chief funding source thus differs from annually appropriated accounts for most executive agencies, but it is similar to other agencies that are supported in whole or in part by direct spending bills, including other financial regulators. The Federal Reserve, the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration, the Farm Credit Administration (FCA), the Office of Financial Research (OFR), and the Federal Housing Finance Agency (FHFA) cover all or part of their costs with funds derived from regulated entities or other investments. Statutes specify that assessments by the Federal Reserve, the OCC, the FCA, the FDIC, the FHFA, and the OFR are not "Government" or "public" funds, nor are they "appropriated" money. Like the CFPB, these agencies do not rely on appropriations acts to continue their activities from year to year.

The Fifth Circuit's Reasoning

The Fifth Circuit's three-judge panel decision stems from a challenge to the Bureau's Payday Lending Rule (the Rule) brought by payday lenders and credit access firm associations arguing that, even after *Seila Law*, the Bureau's structure is unconstitutional. Among other challenges to the Rule, the plaintiffs cast the Bureau Fund as "usurp[ing] Congress's role in the appropriation of federal funds" in violation of the Appropriations Clause and separation of powers.

The court largely agreed that the Fund was unconstitutional. It began by describing the Appropriations Clause's role in the separation of powers. Citing Supreme Court case law, the Fifth Circuit explained that Congress's control over money in the Treasury limits all powers of the other two branches. That is, no action by the other branches may permit disbursements from the Treasury unless supported by an appropriation. According to the Fifth Circuit, the clause is more than a restraint on the executive and judiciary; the clause also "affirmatively obligates Congress to use" its "power over fiscal matters" to preserve the separation of powers and individual liberty.

The Fifth Circuit then identified two features of the Bureau Fund that, in the court's view, show Congress abdicated this duty. The first and "[m]ost anomalous" evidence was the Bureau's power to requisition funds from the Federal Reserve, a "self-actualizing, perpetual funding mechanism." According to the court, Congress ceded both "*direct control* over the Bureau's budget by insulating it from annual or other time limited appropriation" and "*indirect control*" by drawing Bureau funding from Federal Reserve earnings, which are themselves "outside the appropriations process."

The second problematic feature of the Fund identified by the court was how Congress structured the Fund. In the Fifth Circuit's view, the Fund is "off the books" because it is allegedly not a "Treasury account" but a "separate" account at a Federal Reserve bank. Fund amounts are available to the director upon transfer, do not expire, are not government funds or appropriated monies, and are not reviewable by the Appropriations Committees. The Fifth Circuit wrote that these provisions resulted in Congress "relinquish[ing] its jurisdiction to review agency funding," as well.

The Bureau's arguments to the contrary did not persuade the court. The Fifth Circuit disagreed that the Bureau Fund passed constitutional scrutiny because a statute created it. Here, the court distinguished two types of statutes: "mere enabling legislation" and an "appropriation." As a constitutional matter, only the latter statute type authorizes outlays from the Treasury. The Fifth Circuit reasoned that Congress did not make an appropriation under the Constitution when it created the Bureau Fund because Congress specified that amounts in the Fund are not "appropriated monies."

The Fifth Circuit also declined the Bureau's invitation to follow other federal courts, including the U.S. Court of Appeals for the D.C. Circuit, that have affirmed the Fund's constitutionality. Those other decisions, the Fifth Circuit wrote, were based "largely on one factor": the self-funded nature of other financial regulators. "Even among self-funded agencies," the court stated, "the Bureau is unique." It has "a perpetual self-directed, double-insulated funding structure" that "goes a significant step further than that enjoyed by the other agencies." The court also emphasized that the Bureau was led by a single director, answerable to the President with "plenary regulatory authority."

Finally, the court highlighted possible implications of the CFPB's arguments. If it were enough for the Bureau Fund to derive from a statute, then "what would stop Congress from similarly divorcing other agencies from the hurly burly of the appropriations process?"

Analysis of the Fifth Circuit's Decision

By holding that Congress's creation of the Bureau Fund "violates the Appropriations Clause," the Fifth Circuit appears to have broken new jurisprudential ground. When the Supreme Court has invalidated appropriations, it has done so because those appropriations conflicted with other constitutional provisions (e.g., the Bill of Attainder or Article III Compensation Clauses) or another branch's core constitutional functions (e.g., exercising the judicial power). The Court has not described the Appropriations Clause, itself, as a provision that Congress could violate by making funding available in a statute.

The Court has, however, rejected a claim that Congress failed to make a valid appropriation because it allegedly gave an agency too much discretion over its spending authority. In the 1937 decision *Cincinnati Soap Co. v. United States*, petitioners challenged a statute directing payment of coconut oil tax proceeds to the Philippines without saying how the funds were to be used. (The Philippines was then a "Commonwealth" transitioning to eventual independence from the United States.) The Court explained that at the time of its decision no tax proceeds had been transmitted from the United States to the Philippines and appeared to question whether an appropriation had been made. The Court went on to state, though, that Congress "has wide discretion in the manner of prescribing details for which it appropriates." Broad delegations of spending authority, the Court wrote, had "never seriously been questioned." The Fifth Circuit did not consider the merits of a similar non-delegation theory concerning the Bureau Fund; it held that the plaintiffs forfeited that theory by not pressing it in the district court.

While the Fifth Circuit held that the statute establishing the Bureau Fund was not an appropriation in the constitutional sense, the Supreme Court has not articulated a test for deciding that question. In its certiorari petition, the Department of Justice (DOJ) has urged the Court to apply the "classic elements of an appropriation" to decide whether the Bureau Fund qualifies as an appropriation in the constitutional sense. Those elements derive from a statutory rule of construction: a "law may be construed to make an appropriation out of the Treasury" only if it "specifically states that an appropriation is made or that such a contract may be made." Under Comptroller General opinions, Congress's use of the phrase "specifically states" is not equivalent to "expressly states." A statute qualifies as an appropriation if it has a specific direction to make a payment and a source of funds for the payment, even if the statute omits a term like "appropriation." Further supporting this position, the Government Accountability Office (GAO) has characterized the Bureau Fund as a "permanent appropriation" in supplemental data supporting its 2018 government-wide inventory of accounts with spending authority and permanent appropriations.

The Fifth Circuit's decision also poses statutory interpretation questions. The court reasoned that Congress did not make an appropriation under the Constitution when it created the Bureau Fund because Congress specified that amounts in the Fund are not to "be construed to be Government funds or appropriated monies." Similar rules of construction have existed for the other financial regulators since at least the 1930s. Lower federal courts and the Government Accountability Office (GAO) have not previously interpreted the rules of construction as a statement of the *constitutional* character of funds. They have instead understood the rules of construction to have *statutory* implications. GAO has interpreted these rules of construction as describing how collections are to be credited—that is, not to the accounts that comprise the "general fund" but to a special fund of earmarked collections. GAO has also stated that this language frees funds from generally applicable statutory limits on the use of "appropriated" funds, such as prohibitions on using these funds to pay court judgments or reimburse certain officer expenses. DOJ has applied similar reasoning. Finally, federal courts have cited the rule of construction as relevant to whether a federal agency qualifies as a "nonappropriated fund" agency, a class of agencies to which the Tucker Act's statutory waiver of sovereign immunity may not apply.

The Fifth Circuit decision also appears to have held that the 111th Congress's stipulation that the Bureau Fund is not "subject to review" by the appropriations committees surrendered Congress's jurisdiction to review CFPB funding. The Supreme Court has explained, though, that "one legislature cannot abridge the powers of a succeeding legislature." It is also unclear whether the statute's bar on the appropriations committees' review of Bureau funding is equivalent to surrendering *Congress's* legislative and implied oversight powers. The statute expressly subjects the Bureau to congressional oversight, including requirements that the CFPB director biannually report to and appear before its authorizing committees to (among other things) justify the Bureau's budget request for the previous year.

Potential Legal Ramifications for the CFPB

After holding that the Bureau Fund violates the Appropriations Clause and the separation of powers, the Fifth Circuit did not consider (as the *Seila Law* Court did) whether this constitutional defect could be cured by severing provisions of the statute. Rather, the Fifth Circuit vacated the Payday Lending Rule because "the funding employed by the Bureau to promulgate the [rule] was wholly drawn through the agency's unconstitutional funding scheme." The court explained: "without its unconstitutional funding, the Bureau lacked any other means to promulgate the" Rule.

Although the Fifth Circuit decision only expressly affects the CFPB's Payday Lending Rule, its legal reasoning could reverberate well beyond that one regulation. The reasoning could call into question the legality of every CFPB action funded by the Bureau Fund. The CFPB uses the Bureau Fund to cover the costs of nearly all of its "vast rulemaking, enforcement, and adjudicatory" activities. The Bureau's only other source of funding—its Civil Penalty Fund—consists of civil penalties collected pursuant to enforcement actions that were themselves funded by the Bureau Fund. The Civil Penalty Fund cannot be used to cover the Bureau's day-to-day expenses, but rather can only be used for the limited purposes of victim payments, consumer education, and financial literacy.

Thus, the Fifth Circuit's decision could cast legal doubt over every substantive action that the CFPB has taken since at least July 21, 2011, when the Bureau's authorities went into full effect, if not since its inception a year earlier, as well as any future Bureau action. This would include myriad regulatory actions, such as dozens of rulemakings, enforcement actions, and examinations the Bureau has conducted over the past 12 years. The ruling also could affect the CFPB's day-to-day administrative actions necessary to further its statutory mission, like the payment of salaries to its approximately 1,500 employees, as well as its capital investments and procurements.

The Fifth Circuit decision is already affecting other CFPB enforcement actions. Within days of its publication, a number of defendants in CFPB enforcement cases petitioned courts to dismiss the CFPB's claims or provide other relief as a result of the Fifth Circuit's decision. At least one federal court has stayed an enforcement proceeding pending the Supreme Court's review of the Fifth Circuit decision. Similar legal challenges will also likely be brought against future enforcement actions, rulemakings, or other regulatory actions taken by the CFPB until the cloud of uncertainty over the Bureau's funding is cleared either by the Supreme Court or congressional legislation that, for instance, converts the Bureau's funding to annual discretionary appropriations. The decision also has the potential to create legal uncertainty in multi-trillion-dollar consumer financial markets that operate in accordance with the federal consumer financial laws implemented by the CFPB. These laws, including the Truth in Lending Act, Real Estate Settlement Procedures Act, Equal Credit Opportunity Act, and Fair Credit Reporting Act, govern a wide array of consumer financial products and services. Casting doubt upon the legality of the many regulations the CFPB has issued to implement these laws could disrupt these markets, subject financial institutions to legal risks by unsettling legal responsibilities, and render statutory protections unenforceable.

Author Information

Sean M. Stiff
Legislative Attorney

David H. Carpenter
Legislative Attorney

Disclaimer