Eleven States Now Involved in Lawsuit Against Dodd-Frank Financial Reform Law

February 19, 2013 - The financial reform law known as Dodd-Frank was pushed through Congress by using two primary marketing lines. First, it was billed as a law that would protect consumers. Second, it was also billed as a law that would prevent another financial crisis. But so far, about the only thing it really seems to have accomplished is an increase in bank fees and a lot of new litigation in the federal courts. Now eight more states have joined a lawsuit challenging the constitutionality of portions of the law.

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The original law suit was filed on behalf of the State National Bank of Big Spring Texas, the 60 Plus Association and the Competitive Enterprise Institute against the Treasury Department. It challenged the formation of the Consumer Financial Protection Bureau (CFPB) and alleged that the CFPB is unconstitutional. The reason for this claim is that the law delegates responsibilities of all three branches of government to the CFPB, without any oversight. And the CFPB is run by appointed bureaucrats rather than elected officials.

After the suit was filed, three states joined it but they were only interested in challenging one part of the law. That portion of Dodd-Frank which establishes a process known as "Orderly Liquidation". Under this section of the law, the federal government can make a determination that a private company is so important to the overall US economy that it can direct the FDIC to seize the company and liquidate it. Any company facing this scenario wouldn't have the option of going through bankruptcy and would have no due process rights. The same is true for any investors in a company that is seized in this way.

Put another way, Orderly Liquidation is supposed to address the issue of company's being "too big to fail"â€¦ the argument used to bail out the auto industry, insurance companies and most major US banks after the financial crisis which began

in 2008. The states decided to join the lawsuit because they are concerned that it could hurt companies and investors within their borders. They are also concerned that state pension funds and investments could be negatively impacted in any "orderly liquidation" if they own stock or bonds in a company being liquidated.

The federal government has asked the court to dismiss the case on the grounds that the states don't have standing and that their claims are purely speculation about something that could happen in the future. But the government may have real trouble getting the court to comply because of where the suit was filed.

The case was filed in the US District Court for the District of Columbia. This in the same court circuit that has already found that President Obama's recess appointments to the National Labor Relations Board were unconstitutional. Since the head of the CFPB - Richard Cordray - was appointed on the same day, using the same procedure, there is every reason to believe that Cordray's appointment is also unconstitutional. And that would open up a Pandora's Box.

Even though "orderly liquidation" falls under the Treasury Department rather than the CPFB, the DC Circuit has not shown a propensity to defer to Congress or the White House in its decision making process. Under Dodd-Frank, the CPFB has no authority without an agency director in place. If the court determines that the CPFB's authority is unconstitutional - either because of the way the law is structured or because Cordray's appointment was invalid - then it might be much easier for the court to also determine that "orderly liquidation" violates the Constitution's guarantee of due process.

There are several cases winding their way through the court system right now that involve portions of the Dodd-Frank law. A number of these are specifically directed at the formation of the CPFB. Since these cases are now in various federal circuits, there is a good chance that they will eventually wind up at the Supreme Court.

The original three states to join the suit were Michigan, Oklahoma and South Carolina. They have now been joined by Alabama, Georgia, Kansas, Montana, Nebraska, Ohio, Texas and West Virginia.

byJim Malmberg
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