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CFPB Proposes Rules Banning Use of Class Action Waivers in Consumer Arbitration Agreements

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Banks & Other Financial Institutions

The ***Consumer Financial Protection Bureau (CFPB)*** has proposed new rules that would largely ban the use of "no class action" arbitration provisions in consumer financial products and services agreements. 81 Fed. Reg. 32,830-01 (May 24, 2016).

The proposed rules would (1) prohibit companies from enforcing class action waivers in consumer financial agreements; (2) require those agreements to state that the arbitration provisions cannot be used to stop consumers from filing or participating in a class action; and (3) require arbitration providers to submit to the CFPB specific information about individual arbitrations.

The proposed rules would apply to contracts for most of the consumer financial products and services that the CFPB regulates, including bank accounts, credit card services, and various types of loans. The rules would not prohibit arbitration of individual disputes, provided that class claims are not involved. If a class action has been filed, a defendant could rely on an arbitration clause to seek a stay or dismissal only after the court has ruled that the case may not proceed as a class action.

These rules represent the most significant action the CFPB has taken since its inception. The rules are part of the executive branch's recent efforts to limit arbitration of consumer claims and challenge by regulation recent Supreme Court decisions that uphold the use of mandatory arbitration clauses in consumer cases. *See, e.g.*, *AT&T Mobility LLC v. Concepcion*. 131 S. Ct. 1740 (2011).

Industry groups have taken the position that the proposed rules would replace faster and less costly individual arbitrations with lengthy and expensive class action litigation. The rules have already drawn strong opposition and are likely to be challenged in court if approved.

Companies or others concerned about the proposed rules have until August 22, 2016 to submit comments. The rules do not require congressional approval.

Background on the Use of Arbitration Clauses

According to the CFPB, arbitration clauses are included in "hundreds of millions of consumer contracts" for consumer financial products and services, from bank accounts to private student loans to payday loans. These clauses often require consumers to submit any dispute to individual

arbitration, rather than raise their claims as part of a class action.

The CFPB is taking on these arbitration clauses with its new proposed rules. The CFPB was created by the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act. The Act required the CFPB to study the use of mandatory arbitration in consumer financial markets, and authorized the CFPB to issue rules to address any alleged harm to consumers.

In March 2015, the CFPB released its lengthy study of mandatory arbitration, which concluded that class actions provide more effective relief for more consumers than individual arbitration does. The financial industry has disputed these findings, arguing that consumers often fare better in arbitration, where they receive much higher individual awards than in class actions.

Other federal agencies, including the Department of Education and the Centers for Medicare and Medicaid Services, have also been seeking to restrict the use of mandatory arbitration clauses. But as federal agencies have been trying to limit the use of arbitration clauses, the judicial branch has been doing just the opposite. Recent Supreme Court rulings upholding individual arbitration, including *AT&T Mobility v. Concepcion*, have helped facilitate the increased use of arbitration clauses.

The Proposed Rules

Prohibition on Class Action Waivers

The CFPB's proposed rules would prohibit companies from using mandatory arbitration clauses to prevent class action lawsuits. Specifically, the proposed rules state that providers of covered consumer financial products and services "shall not seek to rely in any way on a pre-dispute arbitration agreement" to dismiss or stay a class action related to their products or services, "unless or until" the presiding court rules that class treatment is not appropriate, and the ruling is no longer subject to judicial review. In addition, the proposed rules require that arbitration agreements state the following: "We agree that neither we nor anyone else will use this agreement to stop you from being part of a class action case in court. You may file a class action in court or you may be a member of a class action even if you do not file it."

Consumer Financial Products and Services Affected

Most consumer financial products and services regulated by the CFPB would be subject to these new rules, including bank checking and deposit accounts, credit cards, prepaid cards, money-transfer services, certain auto and auto title loans, payday loans, installment loans, and private student loans. But merchants, retailers, and sellers of nonfinancial goods or services that provide credit or payment processing services to customers to facilitate payment of those products would not be subject to the proposed rules, unless they are "engaged significantly in extending consumer credit with a finance charge" or they extend credit that "significantly exceeds" the market value of the goods and services.

Reporting Requirements

The new rules do not ban arbitration clauses entirely. Companies may still require customers to resolve individual disputes through arbitration, so long as class claims are not involved. The proposed rules nevertheless require arbitration providers and companies that engage in individual arbitration of consumer disputes to submit certain documents to the CFPB when any claim is filed in arbitration concerning covered products or services. Companies must provide documentation of the

arbitration claims filed, the pre-dispute arbitration agreement, and any judgment or award issued, so that the CFPB can continually monitor the use of arbitration.

Effective Date; Not Applicable to Current Arbitration Agreements

The proposed rule will become effective 211 days after the final rule is published in the Federal Register. The proposed rule would apply to all contracts entered into 211 days after that date, but would not affect existing agreements.

Implications of the Proposed Rules

Critics of the proposed rules argue that they could cost companies billions of dollars by supplanting a faster and less expensive process of claim arbitration with lengthy, expensive, and complicated class action litigation. Credit card companies, banks, and financial firms could be exposed to a multitude of frivolous or borderline lawsuits from consumers who are no longer restricted from bringing class actions. The risk of litigation and legal costs for companies may rise, which many in the financial services industry believe may also lead to an increase in prices for consumers.

The battle lines have been drawn. Various industry groups have released statements opposing the proposed rules. They argue that individual arbitration provides consumers with a quick and cost-efficient method for resolving disputes, and that the CFPB's new rules will only enrich class action plaintiffs' lawyers while providing very few benefits to consumers. They also warn that the proposed rules may force companies to stop using arbitration clauses altogether, thereby eliminating a valuable option for consumers.

The proposed rules will likely face judicial challenge, perhaps all the way to the Supreme Court. With the composition of the Court an open question after the passing of Justice Scalia (who wrote the majority opinion in *Concepcion*), there are no clear predictions on how the Court will rule on this issue.

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