Insights: Alerts

Significant Changes in Store for Consumer Finance Businesses – What You Need to Know Now About the CFPB's New Arbitration Rules

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On May 5, 2016, the Consumer Financial Protection Bureau ("CFPB") issued new proposed rules for consumer financial services contracts. The proposed rules have two major components. First, the proposed rules prohibit class action waivers in pre-dispute arbitration agreements and require specific language in pre-dispute arbitration agreements noting the consumer's right to file or participate in a class action. Second, they require providers of consumer financial services or products with pre-dispute arbitration provisions to provide detailed information to the CFPB concerning arbitrations. Industry observers anticipated the proposed rules, which are open for public comment after publishing in the Federal Register, following the CFPB's issuance of its March 2015 Arbitration Study and October 2015 outline of proposals. While the proposed rules do not ban arbitration, providers of consumer financial services and products with pre-dispute arbitration provisions cannot use arbitration agreements to avoid class actions and must report detailed information about the arbitrations to the CFPB. With the publication of the proposed rules, therefore, we outline below some of the issues providers of consumer financial products or services should consider now.

Do The Proposed Rules Apply To My Products Or Services?

The proposed rules apply to a broad swath of financial products and services. In passing the Dodd-Frank Act, Congress barred the use of arbitration agreements in connection with mortgage loans and directed the CFPB to consider arbitration in other consumer contracts. The proposed rules would be applied to providers who lend, store, move, or exchange money. These include providers that:

- extend or regularly participate in credit decisions;
- extend or broker automobile leases;
- provide debt management or settlement services;
- provide consumer credit reports;
- provide accounts under the Truth in Savings Act;
- provide accounts and remittances subject to the Electronic Fund Transfer Act;
- transmit or exchange funds (that are not integral to another product or service not covered by the new rule);
- provide certain payment processing, check cashing, check collection, or check guaranty services; or
- collect debts related to the products and services described here.

The rules appear to cover most consumer financial services providers including banks, others lenders including credit card issuers and student loan originators, credit reporting agencies, and automobile lenders. If your business

provides financial services or products to consumers, the CFPB intends a broad interpretation and as such the proposed rules very well could impact your use of pre-dispute arbitration agreements.

When Do The Proposed Rules Take Effect?

The proposed rules do not take effect unless they become final, and the public comment process may impact the ultimate text of the rule. Even if the proposed rules are adopted in their current form, the ban on class action waivers would apply only to agreements entered into after 180 days from the effective date of the regulation. Therefore, the final regulation would not be applied to arbitration agreements until 2017 at the earliest. Moreover, a legal challenge to the new rules, once implemented, is likely.

What Should We Do Now?

Providers of consumer financial services or products should take advantage of this time to review their arbitration agreements to determine if they comply with the rules. If non-compliant, the providers should revise their arbitration agreements to eliminate class action waivers and to add the required language noting that there is no restriction on class actions.

What Do The Proposed Rules Require For Arbitration Agreements?

The proposed rules prohibit providers of certain consumer financial products or services from using an arbitration agreement to block class actions. Further, consumers must be apprised that arbitration cannot prevent them from participating in a class action. The CFPB's stated basis for making these changes is its preliminary finding in its 2015 Study that the class action is a "more effective" means to address purported violations of consumers' rights than individual actions, in court or arbitration. The authority of the CFPB to issue these regulations is likely to be the subject of future litigation, particularly given that these proposed rules challenge a line of Supreme Court precedent that allowed the enforcement of class-action waivers in contracts.

What Else Do The Proposed Rules Require?

The less publicized portion of the proposed rules would impose a significant data collection burden by requiring any providers who utilize pre-dispute arbitration agreements to collect and submit to the CFPB detailed records relating to any consumer arbitrations. The driver for this portion of the proposed rules appears to be the CFPB's stated goal to foster transparency in the arbitration of consumer disputes. The CFPB also appears interested in using this information to monitor the efficacy of arbitrations, in an effort to ensure that arbitrations are not skewed towards the providers of consumer financial services or products.

Preparing for the implementation of the final rules is recommended, given the significant changes in both contracting language and regulatory reporting contemplated by the proposed rules.