

Insights: Alerts

CFPB Issues Arbitration Agreements Final Rule

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On July 10, the Consumer Financial Protection Bureau (CFPB or Bureau) issued a final rule governing agreements that provide for the arbitration of any future disputes between consumers and providers of certain consumer financial products and services.¹ As expected, the final rule largely adopts the version proposed for comment on May 24, 2016.

Background

Congress directed the Bureau to study these pre-dispute arbitration agreements in the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).² In 2015, the Bureau published and delivered to Congress an arbitration study.³ In the Dodd-Frank Act, Congress also authorized the Bureau, after completing the study, to issue regulations restricting or prohibiting the use of arbitration agreements if the Bureau found that such rules would be in the public interest and for the protection of consumers.⁴ Congress also required that the findings in any such rule be consistent with the Bureau's study.⁵

Scope

The rule applies to providers (including both banks and nonbanks) of certain consumer financial products and services in the core consumer financial markets of lending money, storing money, and moving or exchanging money. This includes, subject to certain specified exclusions, providers engaged in:

- extending consumer credit, participating in consumer credit decisions, or referring or selecting creditors for non-incidental consumer credit, each when done by a creditor under Regulation B implementing the Equal Credit Opportunity Act (ECOA), acquiring or selling consumer credit, and servicing an extension of consumer credit;
- extending or brokering automobile leases as defined in Bureau regulation;
- providing services to assist with debt management or debt settlement to modify the terms of any extension of consumer credit or to avoid foreclosure, and providing products or services represented to remove derogatory information from, or to improve, a person's credit history, credit record, or credit rating;
- providing directly to a consumer a consumer report as defined in the Fair Credit Reporting Act (FCRA), a credit score, or other information specific to a consumer derived from a consumer file, except for certain exempted adverse action notices (such as those provided by employers);
- providing accounts under the Truth in Savings Act (TISA) and accounts and remittance transfers subject to the Electronic Fund Transfer Act (EFTA);

- transmitting or exchanging funds (except when necessary to another product or service not covered by this rule offered or provided by the person transmitting or exchanging funds), certain other payment processing services, and check cashing, check collection, or check guaranty services consistent with the Dodd-Frank Act; and
- collecting debt arising from any of the above products or services by a provider of any of the above products or services, their affiliates, an acquirer or purchaser of consumer credit, or a person acting on behalf of any of these persons, or by a debt collector as defined by the Fair Debt Collection Practices Act (FDCPA).

Persons Excluded From Coverage

Under the rule, certain persons are excluded from coverage, including:

- A person regulated by the U.S. Securities and Exchange Commission (SEC) (which includes broker-dealers and investment advisers, as well as their employees, agents, and contractors, to the extent regulated by the SEC), who is acting in an SEC-regulated capacity and incidentally provides a consumer financial product or service. This exemption also applies to any person to the extent regulated by a state securities commission as a broker-dealer or investment adviser.
- A person regulated by the Commodity Futures Trading Commission (CFTC) or any person with respect to any account, contract, agreement, or transaction to the extent subject to the jurisdiction of the CFTC.⁶
- Federal government agencies as defined in the Federal Tort Claims Act (28 U.S.C. § 2671), and any state, tribe, or other person to the extent the person qualifies as an arm of the state or tribe within the meaning of federal law concerning sovereign immunity and the person's immunities have not been abrogated by the U.S. Congress.
- Any person in relation to any covered product or service that the person and any affiliates collectively provide to no more than 25 consumers in the current calendar year, and that it and any affiliates have not provided to more than 25 consumers in the preceding calendar year.
- Merchants, retailers, and other sellers of nonfinancial goods and services under certain specified circumstances.
- Employers to the extent they are offering or providing a product or service to an employee as an employee benefit.
- Persons to the extent they are providing a product or service in circumstances where they are excluded from the Bureau's rulemaking authority.

Congress already prohibits arbitration agreements in the largest market that the Bureau oversees — the residential mortgage market. In the Military Lending Act, Congress also has prohibited such agreements in many forms of credit extended to service members and their families.

Highlights

In accordance with the Bureau's statutory authority, the rule imposes two sets of limitations on the use of pre-dispute arbitration agreements by covered providers of consumer financial products and services.

First, providers will be prohibited from using a pre-dispute arbitration agreement to block consumer class actions in court and most providers are required to insert language into their arbitration agreements reflecting this

limitation. This requirement is based on the Bureau's findings — which are consistent with the study — that pre-dispute arbitration agreements are being widely used to prevent consumers from seeking relief from legal violations on a class basis, and that consumers rarely file individual lawsuits or arbitration cases to obtain such relief.

Second, providers that use pre-dispute arbitration agreements will be required to submit certain records relating to arbitral and court proceedings to the Bureau. The Bureau will use the information it collects to continue monitoring arbitral and court proceedings to determine whether there are developments that raise consumer protection concerns that may warrant further Bureau action. The Bureau is also finalizing provisions that will require it to publish the materials it collects on its website with appropriate redactions as warranted, to provide greater transparency into the arbitration of consumer disputes. Publication on the CFPB's website will commence no later than July 2019.

The rule also requires providers in most cases to insert specified language into their arbitration agreements to explain the effect of the rule.

Implementation Period

Consistent with the Dodd-Frank Act, the rule applies only to agreements entered into on or after the end of the 180-day period beginning on the regulation's effective date, so agreements entered into before the effective date are grandfathered under existing law. The Bureau is adopting an effective date of 60 days after the final rule is published in the *Federal Register*.

The rule permits providers of general-purpose reloadable prepaid cards to continue selling packages that contain non-compliant arbitration agreements, provided they give consumers a compliant agreement as soon as consumers register their cards and the providers comply with the rule's requirement not to use an arbitration agreement to block a class action.

Potential Challenges Lie Ahead

This rule faces an uncertain political and legal future. In his remarks announcing the rule, CFPB Director Richard Cordray acknowledged his awareness that certain parties have indicated they will seek to have Congress nullify this new rule. The Congressional Review Act (CRA) allows both houses of Congress to vote on resolutions of disapproval for regulations within 60 legislative days of their publication in the *Federal Register*. If the president signs those resolutions, which can be brought to the floor without committee votes and do not need a 60-vote majority in the Senate to pass, the agency is prohibited from issuing a regulation that is "substantially similar" to the one that was nullified, unless it is authorized by Congress to do so. Prior to the Trump administration, the law had only been invoked once since it was passed in 1996. Since the start of the 115th Congress in January, 14 disapproval resolutions have been passed.⁷ The risk of CRA reversal is elevated in the current political environment; at least one Republican senator has already announced plans to draft a resolution of disapproval to overturn the rule under the CRA. The Financial CHOICE Act, which was passed by the House in June, would repeal the CFPB's authority to prohibit arbitration, but the fate of this bill in the Senate remains uncertain. Legal challenges based on claims that the final rule and arbitration study failed to comply with the Dodd-Frank Act and the Administrative Procedure Act also could be invoked.

¹Consumer Financial Protection Bureau, *Arbitration Agreements* (July 10, 2017), *available at* http://files.consumerfinance.gov/f/documents/201707_cfpb_Arbitration-Agreements-Rule.pdf.

²Public Law 111-203, 124 Stat. 1376 (2010), section 1028(a).

³Consumer Financial Protection Bureau, “Arbitration Study: Report to Congress, Pursuant to Dodd-Frank Wall Street Reform and Consumer Protection Act § 1028(a),” (2015), *available at* http://files.consumerfinance.gov/f/201503_cfpb_arbitration-study-report-to-congress-2015.pdf.

⁴Dodd-Frank section 1028(b).

⁵*Id.*

⁶This exclusion applies only to the extent an activity is regulated by the CFTC. See 15 U.S.C. 5481(20).

⁷While joint resolutions of congressional disapproval were introduced earlier this year concerning the CFPB’s Prepaid Rule, the matter failed to reach the floor for vote in either house by the May 11, 2017 deadline.

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