Arbitration Rule

Preserving Consumer Access to Courts

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The US Chamber of Commerce and prominent financial industry groups (collectively, "Chamber") have now gotten into the act of trying to deprive consumers of their day in court.[1] The Chamber's view is that the Consumer Financial Protection Bureau ("Bureau") has promulgated an "unconstitutional and illegal" arbitration rule ("Arbitration Rule") that supposedly blocks companies from forcing consumers to go to arbitration instead of filing class action cases.

There are eighteen plaintiffs in the Chamber's suit, filed on September 29, 2017. They want to set aside the Arbitration Rule as invalid, alleging the measure was based on a "fundamentally flawed" study and is the "tainted" product of an agency structure that is itself unconstitutional.

So, now comes this lawsuit, filed in the Northern District of Texas, seeking to enjoin the Bureau from enforcing the new Arbitration Rule that prohibits most financial service providers from requiring consumers to sign mandatory arbitration agreements that bar class action lawsuits. This lawsuit is brought both by the Chamber and a coalition of corporate business lobbying groups. In the complaint for declaratory and injunctive relief, these plaintiffs argue the Arbitration Rule is invalid and must be set aside.

The claims are lined up in a section of the lawsuit, which I outline as follows:

> ...
> "**First**, the Rule is the product of, and is fatally infected by, the unconstitutional structure that Congress gave the CFPB when it created the Bureau in the Dodd-Frank Wall Street Reform and Consumer Protection Act ("the Dodd-Frank Act").

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> **Second**, the Rule violates the Administrative Procedure Act ("APA") because the CFPB failed to observe procedures required by law when it adopted the conclusions of a deeply flawed study that improperly limited public participation, applied defective methodologies, misapprehended the relevant data, and failed to address key considerations.
> **Third**, the Rule also violates the APA for the related reason that it runs counter to the record before the Bureau and fails to take account of important aspects of the problem it purports to address, making it the very model of arbitrary and capricious agency action.
> And
> **Fourth**, the Rule violates the Dodd-Frank Act because it fails to advance either the public interest or consumer welfare: it precludes the use of a dispute resolution mechanism that generally benefits consumers (i.e., arbitration) in favor of one that typically does not (i.e., class-action litigation)." (My emphases and change of format.)

Unless the federal court provides the plaintiffs' requested relief or federal lawmakers choose to act on the issue, the Bureau's new Arbitration Rule is set to become effective on October 18, 2017.

As you may know, for the most part, I have taken the opposite point of view than the plaintiffs. For a detailed understanding of my position, please read my article *Take-It-or-Leave-It Arbitration, Banning Consumers from the Court*.[2] You can download it from the Articles section of our Lenders Compliance Group website. [http://lenderscompliancegroup.com]

In particular, I object to this construal in the plaintiffs' claim:

> "Such a regulation, which eliminates a demonstrably effective method of dispute resolution while making it impossible for businesses to pass on the cost savings achieved through use of arbitration, neither advances the public interest in general nor protects consumers in particular."

The Bureau had been working on the Arbitration Rule for about two years and released its final rule in July 2017. Although the Bureau does not ban arbitration outright, as many consumer advocates had hoped, it does eliminate provisions that bar consumers from joining class actions.

Research conducted by the Bureau found that class action bans actually prevented consumers from getting redress for harm done by credit card companies, banks, payday lenders and other consumer financial firms.

According to the Bureau, because most of the disputes between consumers and banks deal with small dollar amounts, consumers tend to opt against going through the arbitration process, which is driven by financial institutions.

This is a classic David and Goliath scenario. QED

In other words, industry groups – such as the American Bankers Association, American Financial Services Association, Consumer Bankers Association, Financial Services Roundtable, and many Texas business

organizations – are fighting a rule that bars the fine-print requirements in financial contracts that compel consumers to use arbitration, rather than the U.S. legal system, to resolve complaints.

The Chamber's suit disputes the Bureau's Arbitration Study,[3] arguing that it doesn't meet the standards set out by Congress when the latter mandated, as part of the Dodd-Frank Act, that the Bureau study the use of arbitration and base any subsequent regulation on the findings.

In challenging the research, the plaintiffs claim that the Bureau did not conduct a "fair, unbiased and thorough study" as required by Congress, but instead relied on faulty methodologies, misread or ignored key data, didn't provide meaningful opportunities for public comment, and didn't address relevant policy questions surrounding the regulation of arbitration.

Thus, it is alleged, because the Bureau issued the Arbitration Rule without having first conducted a study that comports with what Congress wanted, the Arbitration Rule violates the Administrative Procedure Act.

Not stopping there, the plaintiffs take the position that because the Bureau's study supposedly yielded unreliable conclusions that did not take into consideration other available evidence in favor of arbitration, it is further alleged that there's no way the resulting Arbitration Rule could be considered either a valid exercise of the agency's discretion or in line with the Dodd-Frank Act's requirement that any such rule must be "in the public interest and for the protection of consumers."

Then, pivoting on the current controversies and litigation involving the constitutionality of the Bureau, the Chamber and its co-plaintiffs take aim at the Consumer Financial Protection Bureau itself, reprising the precise arguments about the purportedly unconstitutional "concentration of executive power in a single, unaccountable" Director of the Bureau. This line of attack is set forth in the plaintiffs' statement that the Arbitration Rule "was the product of an agency decision-making structure that was unconstitutionally insulated from political review;" and vitiated further because this "product," to wit, the Arbitration Rule, of the that "structure," to wit, the Bureau, means it "necessarily is tainted by the agency's unconstitutional character and must be invalidated."

How close does the timing of this barrage come to the attempts to eviscerate the Arbitration Rule?

Very close, indeed, given that the suit comes at the end of a week in which Senate Republicans appeared poised to move on a resolution to undo the Arbitration Rule through the Congressional Review Act, but, at this time, are seemingly constrained to temporarily demur, pending further efforts to secure votes.

It is worth noting that these salvos are part of a broader effort by Republicans in both houses of Congress and the White House to respond to criticism of the Arbitration Rule from banks and other financial industry players, who argue that arbitration is a cheaper and faster alternative for resolving disputes than class action litigation.

The U.S. House of Representatives voted in July to nullify the Bureau's Arbitration Rule, a little more than two weeks after it was released. President Donald Trump has said he supports the Congressional Review Act effort on the Arbitration Rule and is waiting to sign off on it.

Procedurally speaking, the Senate has until mid-November to vote on the Congressional Review Act measure under the law's requirement that a vote must be taken within 60 legislative days from a rule being entered into the Federal Register. The latest date allowed for a Senate vote, as a practical matter, is November 16, 2017.

Perhaps given the difficulties encountered by Republican efforts to repeal the Affordable Care Act, opponents of the Arbitration Rule seem somewhat anxious and are obviously taking no chances. Hence, the lawsuit is certainly one striking way to destroy the Arbitration Rule.

In my article, I pointed out that the usual gambit that the financial industry uses to effectuate its efforts to protect itself is by dressing up its position in seemingly altruistic and consumer-friendly language and flattering stratagems of consumer advocacy. Here's a sample of such sophistry from a statement offered by plaintiff organizations:

> "As Congress continues to consider action within its purview, we are filing this challenge to **ensure all legal remedies are utilized to preserve arbitration for consumers**."[4] (My emphasis.)

What is missing in the foregoing utterance is the all-important fact that compelling arbitration would defeat the constitutional right of aggrieved parties to their day in court! Arbitration is already available. It seems to me that there is no incompatibility between consumer advocacy and the protections afforded by the United States Constitution.

Actually, if the goal is to *preserve* consumer protection, why not preserve the consumer's constitutional right to a trial by jury, which is clearly stated in the Seventh Amendment of the US Constitution, specifically:

> "In Suits at common law, where the value in controversy shall exceed twenty dollars, **the right of trial by jury shall be <u>preserved</u>**, and no fact tried by a jury, shall be otherwise re-examined in any Court of the United States, than according to the rules of the common law.[5] (My emphasis and underline.)"

To quote Amanda Werner, the arbitration campaign manager for Americans for Financial Reform and Public Citizen, a backer of the Arbitration Rule, this lawsuit is a "desperate move" in light of what she described as the "massive resistance" encountered this week by the Congressional Review Act measure. She minced no words, when she stated, "What a brazen act of hypocrisy, that the financial services lobby is bringing a lawsuit with the goal of stopping consumers from having their day in court."[6]

In my article, I set forth a <u>Thought Experiment</u>.[7]

Consider it in your own deliberations on the Arbitration Rule.

THOUGHT EXPERIMENT

A final thought experiment in the form of three questions!

1. **Do you think a consumer should have his or her day in court?**

   Before you answer, consider that the Bureau's [Arbitration Rule] will allow groups of consumers to obtain relief when companies skirt the law. According to the Bureau, most consumers do not even realize when their rights have been violated. Often the harm may be too small to make it practical for a single consumer to pursue an individual dispute, even when the cumulative harm to all affected consumers is significant. The pilloried Arbitration Study found that only around 2 percent of consumers with credit cards who were surveyed would consult an attorney or otherwise pursue legal action as a means of resolving a small-dollar dispute. With class action lawsuits, consumers will have opportunities to obtain relief from the legal system that, in practice, they otherwise would not receive.

2. **Do you think that prohibiting a "Take-It-or Leave-It" arbitration clause would provide an incentive to companies to comply with the law to avoid group lawsuits?**

   Before you answer, keep in mind that mandatory arbitration clauses may enable companies to avoid being held accountable for their conduct. When companies know they can be called to account for their misconduct, they may be less likely to engage in unlawful practices that can harm consumers. Further, public attention on the practices of one company can affect or influence their business practices and the business practices of other companies more broadly.

3. **Do you think that increased transparency is a valuable service to consumers and merchants alike?**

   Before you answer, it is worth noting that the Bureau's Protection would make the individual arbitration process more transparent by requiring companies that use arbitration clauses to submit any claims filed and awards issued in arbitration to the Bureau. The Bureau would collect correspondence from arbitration administrators regarding a company's non-payment of arbitration fees and its failure to adhere to the arbitration forum's standards of conduct. The collection of these materials would enable the Bureau to better understand and monitor arbitration. It would also presumably provide insight into whether companies are abusing arbitration or whether the process itself is fair.

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[1] *Chamber of Commerce of the United States of America et al. v. Consumer Financial Protection Bureau et al.*; 3:17-cv-02670, 9/29/17, U.S. District Court, Northern District of Texas
[2] *Take-It-or-Leave-It Arbitration, Banning Consumers from the Court*," Jonathan Foxx, National Mortgage Professional Magazine, August 2017. Available at http://lenderscompliancegroup.com in the Articles Section
[3] *Arbitration Study, Report to Congress, pursuant to Dodd–Frank Wall Street Reform and Consumer Protection Act* § 1028(a), Consumer Financial Protection Bureau, March 2015
[4] *Bank Lobby Launches Legal Challenge to U.S. Consumer Lawsuit Rule*, Reuters, Lisa Lambert, September 29, 2017
[5] *Seventh Amendment,* U. S. Constitution, Bill of Rights
[6] *Business groups sue to stop rule that allows class-action suits against banks*, Los Angeles Times, Renae Merle, September 29, 2017; see also, *AFR Statement: Stop Senate Rush to Roll Back Protection from Forced Arbitration*, Americans for Financial Reform, September 25, 2017
[7] Op. cit. 2