KRIEG DEVAULT

Insights

CFPB Issues Long Anticipated Proposal to Significantly Limit Pre-Dispute Arbitration

May 8, 2016

By: Brett J. Ashton

The Consumer Financial Protection Bureau (the “CFPB” or the “Bureau”) released their long anticipated Proposed Rule on Arbitration late last week (the “Proposed Rule” or the “Rule”), significantly limiting the use of pre-dispute arbitration provisions in consumer financial products and services pursuant to their authority under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”). This blog post will provide a brief summary of key points of the Proposed Rule, and answer common questions we have heard from Client’s since its release late last week.

Bans Pre-Dispute Arbitration Clauses as a Tool to Avoid Class Action Litigation

The Proposed Rule prohibits a provider of consumer financial products and services from relying on a pre-dispute arbitration agreement to avoid class action litigation, and requires providers to insert additional disclosure language in their consumer agreements with respect to pre-dispute arbitration and provide the Bureau detailed information related to the use of any pre-dispute arbitration agreement in the future.

Who is covered by the Proposed Rule?

The Proposed Rule will apply to all “Providers” of consumer financial products or services with limited exceptions, including a Provider’s affiliate in certain circumstances. Most financial services companies will be considered a Provider under the proposed Rule.

What consumer financial products or services are covered by the Proposed Rule?

The Proposed Rule applies to:

- Providing an extension of credit defined as “consumer credit” under the Equal Credit Opportunity Act;
- Acting as a creditor by regularly participating in a credit decision;
- Acting as a creditor by referring applicants or prospective applicants to creditors, or selecting or offering to select creditors to whom requests for credit may be made;
- Acquiring, purchasing, selling or servicing an extension of credit;
- Extending or brokering an automobile lease;
- Providing services to assist with debt management, debt settlement, modify the terms of any extension of credit or avoid foreclosure;

- Providing a credit report, credit score, or any other information specific to a consumer from a credit report with limited exceptions;
- Providing savings accounts subject to the Truth in Savings Act;
- Providing accounts or remittance transfers subject to the Electronic Fund Transfer Act;
- Transmitting or exchanging funds, except when integral to another product or service not covered by the Proposed Rule;
- Accepting financial or banking data or providing a product or service to accept such data directly from the consumer for purposes of initiating payment by a consumer via any payment instrument, or initiating a credit card or charge card transaction for the consumer with limited exceptions;
- Check cashing, check collection and check guarantee services; or
- Collecting debt arising from any of the consumer financial products or services described in the Proposed Rule.

What consumer financial products or services are NOT covered by the Proposed Rule?

The Proposed Rule does NOT apply to:

- Broker dealers to the extent that they are providing products or services subject to rules promulgated or authorized by the U.S. Securities and Exchange Commission with respect to pre-dispute arbitration agreements;
- Any federal, state, local or tribal government, or their affiliates providing any product or service directly to a consumer;
- Any person who provides a covered financial product or service to no more than twenty-five (25) consumers in the current or preceding calendar year;
- Merchants, retailers, or other sellers of nonfinancial goods or services, including anyone who purchases or acquires an extension of consumer credit from these entities, provided their activities fall within the exemption from CFPB rulemaking established by the Dodd-Frank Act; or
- Any person to the extent the limitations in 12 U.S.C. §§ 5517 or 5519 apply to the person, or an exempt product or service offered or provided by the person.

Can pre-dispute arbitration provisions still be enforced in cases that are not class actions?

The Proposed Rule does not limit the use of pre-dispute arbitration provisions in cases that are not considered class actions; however, it does mandate several new requirements for their use, including added disclosures, amendments to agreements, and the submission of arbitral records to the CFPB that the Bureau plans to make publicly available.

Added Disclosures:

The Proposed Rule requires any Provider to ensure an agreement contains the following disclosure:

“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.”

If a pre-dispute arbitration clause is for multiple products and services, and only some of them are covered by the Proposed Rule, then the following alternative disclosure is required:

"We are providing you with more than one product or service, only some of which are covered by the Arbitration Agreements Rule issued by the Consumer Financial Protection Bureau. We agree that neither we nor anyone else will use this agreement to stop you from being part of a class action 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. This provision applies only to class action claims concerning the products or services covered by that Rule."

If pre-dispute arbitration agreements existed previously between other parties that don't contain the required disclosures under the Proposed Rule, the Provider has to either ensure the agreement is amended to provide:

"We agree that neither we nor anyone else who later becomes a party to this pre-dispute arbitration agreement will use it 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."

OR provide a new disclosure stating:

"We agree not to use any pre-dispute arbitration 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 even if you do not file it."

Submission of Records to the CFPB

The Proposed Rule provides that any pre-dispute arbitration agreement entered into must submit a copy of the following records, in a redacted form to protect the personal identifying information of the individuals:

- Information related to any claim filed in arbitration by or against the Provider, including the initial claim and counterclaim, the pre-dispute arbitration agreement filed with the arbitrator or arbitration administrator, any judgment or award issued by the arbitrator or arbitration administrator, and whether an arbitrator or arbitration administrator refuses to administer or dismisses a claim due to the Providers failure to pay the required filing or administrative fees, in addition to any communication the provider receives from the arbitrator related to the refusal; and
- Any communication the Provider receives from an arbitrator or an arbitration administrator related to a determination that a pre-dispute arbitration agreement does not comply with the administrator's fairness principles, rules or similar requirements, if such a determination exists.

The CFPB has indicated that it intends to make the information obtained publicly available, much as it does consumer complaints.

The Proposed Rule will be open for comment for ninety (90) days after its publication in the Federal Register, and then be effective thirty (30) days after the adoption of any Final Rule. The Final Rule will only apply to an agreement entered into after the end of the one hundred and eighty (180) day period beginning on the regulation's effective date.

Krieg DeVault Financial Institutions and Litigation attorneys are closely monitoring the Proposed Rule, and ready to provide guidance on how best to comply with these new regulatory requirements while minimizing risk to your financial institution.

[1]**The Proposed Rule adds "Part 1040 – Arbitration Agreements" to Title 12, Chapter X of the Code of Federal Regulations.**

[2]Proposed 12 CFR § 1040.4 Limitations on the use of pre-dispute arbitration agreements. (a) Use of pre-dispute arbitration agreements in class actions. (1) General rule. A provider shall not seek to rely in any way on a pre-dispute arbitration agreement entered into after the date set forth in § 1040.5(a) with respect to any aspect of a class action that is related to any of the consumer financial products or services covered by § 1040.3
including to seek a stay or dismissal of particular claims or the entire action, unless and until the presiding court has ruled that the case may not proceed as a class action and, if that ruling may be subject to appellate review on an interlocutory basis, the time to seek such review has elapsed or the review has been resolved.

[3]Proposed 12 CFR § 1040.4(a)(2) Limitations on the use of pre-dispute arbitration agreements. (a) Use of pre-dispute arbitration agreements in class actions. (2) Provision required in covered pre-dispute arbitration agreements. Upon entering into a pre-dispute arbitration agreement for a product or service covered by § 1040.3 after the date set forth in § 1040.5(a): (i) Except as provided in paragraphs (a)(2)(ii) or (iii) of this section or in § 1040.5(a), a provider shall ensure that the agreement contains the following provision: "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."

[4]Proposed 12 CFR 1040.2(c) Provider means: (1) A person as defined by 12 U.S.C. 5481(19) that engages in offering or providing any of the consumer financial products or services covered by § 1040.3(a) to the extent that the person is not excluded under § 1040.3(b); or (2) An affiliate of a provider as defined in paragraph (c)(1) of this section when that affiliate is acting as a service provider to the provider as defined in paragraph (c)(1) of this section with which the service provider is affiliated consistent with 12 U.S.C. 5481(6)(B).

[5]12 CFR 1040(3)(a)

[6]To the extent it is providing any product or service directly to a consumer who resides in the government's territorial jurisdiction.

[7]This exemption applies to merchants, retailers and other sellers of nonfinancial good or services to the extent they provide, purchase or acquire an extension of consumer credit that is of the type described in 12 U.S.C. 5517(a)(2)(A)(i) and they would be subject to the Bureau's authority only under 12 U.S.C. 5517(a (2)(B)(i) but not 12 U.S.C. 5517(a)(2)(B)(ii) or (iii)

[8]12 CFR 1040(3)(b)

[9]Proposed 12 CFR 1040.2(a) Class action means a lawsuit in which one or more parties seek class treatment pursuant to Federal Rule of Civil Procedure 23 or any State process analogous to Federal Rule of Civil Procedure 23.

[10]There is a limited exception to the disclosure requirements of the Proposed Rule for pre-packaged general-purpose reloadable prepaid card agreements pursuant to Proposed 12 CFR 1040.5(b)

[11]12 CFR 1040.4(a)(2)(i)

[12]12 CFR 1040.4(a)(2)(ii)

[13]12 CFR 1040.4(a)(2)(iii)