

Client Alert

July 2017

The CFPB's Arbitration Rule: A Summary of the Rule, its Requirements, Potential Legal Challenges, and What Companies Should Do

Introduction and Summary of Final Arbitration Rule

On July 10, in a 775-page release, the Consumer Financial Protection Bureau ("CFPB") issued its long-awaited final arbitration rule ("Arbitration Rule") pertaining to consumer finance contracts. The Arbitration Rule, which until now was in the comment stage with its final issuance in question, largely mirrors the proposed rule from May 2016, with a few modifications. The Rule is important for three reasons: (1) it prohibits consumer finance companies from relying on class action waivers to block class action lawsuits; (2) it prohibits the inclusion of class action lawsuit waiver provisions in contracts pertaining to a broad swath of consumer products and services, or "covered products and services"; and (3) it requires covered providers to not only alter their form agreements, but to submit arbitration-related court and arbitration filings to the CFPB for watchdog purposes.

This alert summarizes the scope of the Arbitration Rule, its requirements, the possible challenges (legislative and otherwise to its enforcement), and what companies should do.

Which Finance Companies Are Within the Rule's Reach?

The Arbitration Rule applies to a broad range of consumer credit companies that offer or provide certain types of consumer financial products or services, or "covered transactions," as follows:

- Extensions of credit and participating in credit decisions
- Providing accounts and remittance transfers subject to the EFTA
- Auto-leasing and brokering of auto leases
- Providing accounts subject to the Truth in Savings Act
- Debt management, settlement and repair
- Credit report remediation
- Consumer report providers
- Check cashing
- Debt collectors, which are defined more broadly than the term is traditionally employed in the Fair Debt Collection Practices Act context

The Arbitration Rule specifically excludes a few entities and transactions, including:

- Broker-dealers and investment advisors
- Employers
- Entities regulated by the Securities and Exchange Commission, the Commodity Futures Trading Commission, or a state securities commission
- Federal agencies, states and tribes
- Entities and affiliates that provide covered services to no more than 25 consumers in the current year and the preceding year
- Merchants and retailers of nonfinancial goods that fall outside the CFPB's authority

What Are the Requirements of the Arbitration Rule?

The Arbitration Rule carries three (3) primary requirements, as follows:

- **First**, the Rule's "General Rule" makes it illegal for covered providers to "rely in any way on a pre-dispute arbitration agreement...with respect to any aspect of a class action" that concerns any covered product or service, including to "seek a stay or dismissal of particular claims or the entire action...."
- **Second**, covered providers must change the language of their arbitration agreements to delete class action waivers and to include the following notice: "We agree that neither we nor anyone else will rely on this agreement to stop you from being part of a class action case in court." And where the agreement existed previously between other parties, the company must amend the arbitration provision to contain the required language or provide written notice that the company waives any right to block a class action.
- **Third**, the Rule requires companies to submit arbitration-related filings from court cases and arbitrations to the CFPB for review. The filings will be monitored by the CFPB and posted on an Internet site for public access.

When Will the Arbitration Rule Take Effect?

The effective date is 60 days after the Rule is published in the Federal Register. The Rule would apply only to agreements entered into **after** the end of the 180-day period beginning on the Rule's effective date. As such, the Rule will apply to arbitration agreements entered into 241 days after publication in the Federal Register.

Will the Arbitration Rule Be Challenged or Overturned?

The Arbitration Rule may face challenges from a number of different angles. For example, Congress could seek to reverse the Rule using the Congressional Review Act ("CRA"). Under the CRA, agency action can be overridden by a resolution approved by a simple majority vote of both chambers of Congress and signed by President Trump. According to press reports, Senator Tom Cotton of Arkansas has already begun the CRA process. The Rule may also be challenged on the grounds that the CFPB erred or overstepped its authority. Specifically, the CFPB's authority underpinning the Rule is the Dodd-Frank Wall Street Reform and Consumer Protection Act, which authorized the CFPB to issue regulations regarding arbitration **only** if they (1) are in the public interest, (2) for the protection of consumers, and (3) consistent with findings from a study by the CFPB. A finding that any one of these three prerequisites to action is absent could doom the Rule. Not surprisingly, the CFPB devoted hundreds of pages in the 775-page release to rebutting the multitude of comments it received (the agency received approximately

110,000 comments), many of which claimed that the Rule is an abuse of authority and contradicts an honest reading of its own arbitration study.

What Should Consumer Finance Companies Do?

- **First**, covered providers should determine whether they and/or the products or services they provide are covered by the Arbitration Rule.
- **Second**, covered providers should inventory their consumer contracts to see whether they already include arbitration provisions, and if not, whether an arbitration provision should be added prior to the effective date of the Rule. Again, arbitration agreements entered into prior to the Rule's effective date will remain enforceable.
- **Third**, in the event the Arbitration Rule is not overridden, repealed or enjoined prior to its effective date, covered providers should consult with counsel on how to comply with the Rule, including amending their standard form contracts to include the express terms required by the Rule. They may also take the opportunity to re-evaluate the entirety of the arbitration agreement, including whether to permit class arbitrations, and whether to continue to require individual arbitrations since those are unaffected by the Rule. Attention should also be given to whether a specific state's laws can or should be designated in the agreement and any other contractual terms that may be included to help protect the company from class litigation and the costs associated with it.
- **Finally**, covered providers should consider how to build compliance with the Arbitration Rule into their general Compliance Management System, including compliance with the arbitration-filing submission requirement.

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