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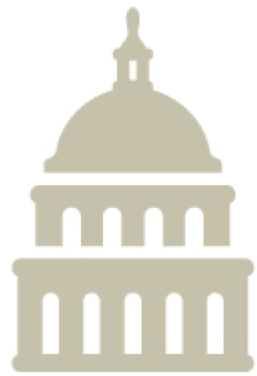
# Litigation Alert

**July 14, 2017**

## Key Points

- Banks and credit card companies will no longer be able to compel consumers into arbitration to avoid class action lawsuits, based on a new rule from the Consumer Financial Protection Bureau (CFPB).
- The new rule has received widespread criticism, with opponents arguing that the rule is anti-consumer, anti-business and promotes frivolous litigation.
- Congress can, and likely will, take action to nullify the new rule before it goes into effect next year, which would also prohibit the CFPB from attempting to enact any similar type of rule in the future.
- Even if Congress does not act, substantial political and legal challenges threaten to undercut the power of the CFPB, and of its Director, Richard Cordray, in particular.



# A New Wave of Class Actions Against Banks and Credit Card Companies? The CFPB’s New Rule and Its Likelihood for Survival

## Background of the CFPB’s New Rule

The CFPB was created by Dodd-Frank legislation in 2010, and, among other things, was tasked with studying and issuing a report on arbitration agreements in the financial products sector (e.g., bank accounts, credit card agreements). Dodd-Frank also authorized the CFPB to enact appropriate regulations based on the results of its study. In 2015, the CFPB concluded that class action waivers in banks’ and credit card companies’ arbitration agreements were harmful to consumers. As a result, on July 10, 2017, the CFPB issued a new rule prohibiting banks and credit card companies from including class action waivers in their arbitration agreements with consumers. Without such waivers, consumers are able to consolidate their cases into class actions, provided that they are able to meet other legal requirements for filing class actions.

In addition to prohibiting class action waivers in arbitration agreements, the rule imposes significant reporting requirements on banks and credit card companies that choose to continue using arbitration agreements. Companies are required to provide records to the CFPB regarding their arbitrations, including claims sought, counterclaims raised, other filings and final awards that are issued. The CFPB intends to post these materials (after redacting consumers’ personal information) on its website beginning in July 2019.

## Analysis of the New Rule: Arguments For and Against

The new rule has sparked contentious debate on both sides. Supporters of the rule argue that class actions are the only way for consumers to seek redress for low-value claims and for companies to be held liable for these harms. They argue that this is supported by the CFPB report’s data, which showed that only 78 consumers sought arbitration throughout the duration of the time period studied (2008–2012). They also rely on the report’s finding that there was no evidence to show that arbitration classes led to lower prices for consumers by allowing companies to avoid costly class actions.

On the other hand, opponents challenge the CFPB’s alleged basis for creating the rule, and they claim that the rule is actually anti-consumer, anti-business and serves only to benefit lawyers and spawn frivolous litigation.

Critics of the rule argue that, according to the CFPB’s own data, arbitration does a better job of protecting consumers than class actions do. The report shows that, from 2008-2012, consumers received only about 55 percent of the cash relief for which companies were held liable (as a result of settlements or otherwise), because of attorney’s fees and class members failing to claim their awards. Lawyers, on the other hand, earned more in attorney’s fees than what was distributed to consumers. Further, the average payout to consumers in class actions was $29 per person, whereas, in arbitration, the average payout was $4,615 per person.

Opponents further argue that not only does the new rule not help consumers, it actually hurts them, by making arbitration unavailable and raising consumer prices. Without the stability of knowing that claims will proceed quickly and individually at arbitration, they argue, companies will abandon their practice of paying for arbitration. Thus, consumers would not resort to arbitration unless they were willing to pay the costs, which can be in the tens of thousands of dollars (or more). Further, critics of the rule argue that, as companies’ costs increase due to class action litigation—which takes longer, costs more, and carries more financial risk for companies than arbitration—these costs will ultimately be borne by consumers because of increased prices.

## Will the New Rule Survive?

Notwithstanding the vigorous debate on both sides, Congress seems primed to take action against the CFPB to nullify the rule using its authority under the Congressional Review Act (CRA). Under the CRA, Congress can nullify a regulation by passing a resolution of disapproval within 60 days of the regulation being published in the Federal Register. The resolution of disapproval needs only a majority vote of both houses, and, if signed by the President, it would prevent the CFPB from attempting to enact any similar type of rule in the future without first getting congressional authorization.

The CFPB’s rule has not yet been published in the Federal Register, but Sen. Tom Cotton (R-AR) has already indicated that he will move for a resolution of disapproval, and Rep. Roger Williams (R.-TX) joined Sen. Cotton in publicly criticizing the rule.

Some hypothesize that the CFPB sought to issue the rule while Congress was busy with other matters (the health care bill, tax reform, Russia investigation), hoping that it would slide under the radar. However, Congress' other matters might have the opposite effect, since commentators have suggested that Republicans can use the nullification of the CFPB rule to save face in light of the challenges they have encountered with the health care bill.

Even if Congress does not take action under the CRA, several other challenges to the CFPB's authority loom in the background. First are challenges to the CFPB's leadership. The D.C. Circuit Court of Appeal recently held that the structure of the CFPB is unconstitutional and that the Director should be removable at the will of the President without the President needing a particular "for cause" justification. That case was reheard by the D.C. Circuit earlier this year, and, if the en banc panel reaches the same conclusion, it is likely that President Trump would replace the current Director, Richard Cordray. A new Director could put a "stay" on the rule, pushing back its effective date and calling for further commentary that could ultimately result in withdrawing the rule entirely.

Second, legislation is currently pending that seeks to reduce the CFPB's power. One proposed change would revoke the CFPB's authority to enact regulations that restrict arbitration clauses, thus removing the power that allowed the CFPB to create the new rule in the first place. Another proposed change would change the CFPB's leadership structure by no longer having a single director at the helm, but instead a multimember commission.

Lastly, the CFPB's rule can be challenged by other government agencies. The Office of the Comptroller of Currency (OCC) has already raised concerns with the rule. The head of the OCC asked the CFPB to provide the exact data and analysis that it used to support its conclusion that the rule was needed. Additionally, the Financial Stability Oversight Council has the authority to veto any CFPB regulation by filing a petition to veto within 10 days of the rule's publication in the Federal Register. If eight of the council's 11 members vote against the rule, it will be vetoed. Such a veto, however, does not automatically prohibit substantially similar rules in the future the way that Congress' nullification under the CRA does, because the CFPB would be able to propose changes and ask for Council approval later. There are only four Obama appointees currently on the Council, so President Trump would need only one to flip in order to have enough votes for a veto.

## Conclusion

If the CFPB's new rule goes into effect, it would deal a potential knockout blow to banks' and credit card companies' ability to avoid consumer class actions through arbitration agreements. According to the rule's opponents, the new rule is bad not only for business, but for consumers as well. Most likely, it will not survive for long. Congress, the President and other government agencies seem poised to take action to counteract the rule and restrict the CFPB's authority. As long as the rule stands, one thing is certain: it will continue to be the subject of debate and attack. It remains to be seen whether the rule will survive. Stay tuned.

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