CALIFORNIA BANKERS ASSOCIATION

CBA Regulatory Compliance Bulletin

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Congress Overturns The CFPB's Arbitration Rule

Coming immediately after the release of the U.S. Treasury's blistering report critical of the CFPB's arbitration rule and underlying analysis, the Senate passed by a vote of 51-50 a resolution under the Congressional Review Act (CRA)[1] to disapprove that rule. The CRA empowers Congress under an expedited legislative process to review new federal regulations and, by enacting a joint resolution, to overrule a regulation. The House of Representatives had earlier this year in July also voted to disapprove the CFPB's regulation. On November 1, the President signed the joint resolution, making the demise of the CFPB's regulation final.

Section 1028 of the Dodd-Frank Act authorizes the CFPB to regulate arbitration agreements in consumer financial services contracts in the public interest, for the protection of consumers, and consistent with a study that the CFPB was required to conduct. That study, issued in March 2015, was clearly intended to make the case for limiting if not eliminating use of arbitration agreements. Nevertheless the data that the CFPB reviewed painted a more complex picture. It found, among other things, that arbitration is a more efficient and effective way to resolve disputes compared to law suits. For example arbitration usually takes months as opposed to years to resolve disputes. Where consumers prevailed in arbitration, the study found that the size of the awards is comparable to damages obtained in court, and far exceeds payouts typically meted out to class action members.

Perhaps because of the ambiguity of its own findings, the CFPB's final rule did not ban arbitration agreements outright. However, any agreement to use arbitration may not also include a class arbitration waiver. This meant that financial services providers had little incentive to offer arbitration as a means to settle disputes since they also had to leave themselves exposed to the significant financial risks associated with arbitrating mass claims. As the Treasury's report pointed out, the costs of defending mass torts give class action attorneys great leverage in order to compel defendants to settle even meritless lawsuits.

In a statement released on the day that the President signed the joint resolution, Acting Comptroller of the Currency Keith Noreika said that the action "is a victory for consumers and small and midsize banks across the country because it stops a rule that likely would have significantly increased the cost of credit for

[1]

hardworking Americans and taken away a valuable tool for resolving differences among banks and their customers."

Elimination of the rule means return to the status quo before the rule was issued, and in California that picture is also less than clear. In the employment context the California Supreme Court has specifically affirmed the enforceability of a mandatory arbitration agreement that included a class action waiver.[2] However, that same case would disallow arbitration of actions brought under the Private Attorneys General Act of 2004 or PAGA.[3] And a federal court has found that an agreement that required arbitration to be conducted in "separate proceedings" violated the National Labor Relations Act's protection of employees' ability to engage in "concerted activity."

In the context of financial services Governor Brown this year signed into law SB 33, which makes arbitration agreements unenforceable in consumer contracts involving depository financial institutions although in narrow circumstances.[4] And any arbitration agreement has to be carefully drafted to avoid challenges based on principles of unconscionability.

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[2] *Iskanian v. CLS Transportation Los Angeles, LLC.* (2014) 173 Cal.Rptr.3d 289.
[3] California Labor Code Section 2698 *et seq.*

[4] See CBA's Regulatory Compliance Bulletin on SB 33.