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CFPB's New Arbitration Rule - What Do We Need to Know?

September 14, 2017 | Eric L. Johnson

On July 19, the Consumer Financial Protection Bureau (CFPB) published a new arbitration rule (Rule) that would ban companies (or "Providers" in the Rule) from using pre-dispute arbitration agreements to prohibit consumers from seeking class relief in a court. The Rule is effective September 19 and requires full compliance by March 19, 2018 (the "Compliance Date"). Dealers that are exempt from the CFPB's jurisdiction under Section 1029 of the Dodd Frank Act will feel the impact of the Rule indirectly. However, banks and auto finance companies are not exempt from the Rule and will be impacted directly. The Rule is relatively short, but its impact will be "huuuuggge." Here's a summary of some of things you need to know about the new Rule and its chances of being nullified.

What does the Rule cover?

The Rule applies to the offering of consumer financial products or services unless the Provider of those products or services is either excluded from the Rule or not subject to the CFPB's jurisdiction. Therefore, if you're a franchise dealer, the Rule generally does not apply to you. However, the Rule does apply to banks and auto. finance companies that buy retail installment sales contracts (RISCs) or leases from franchise dealers.

How does the Rule affect arbitration?

Generally, the effect of the Rule is a ban on class action waivers ("Waivers") in pre-dispute arbitration agreements. A "pre-dispute arbitration agreement" is an agreement between a covered person and a consumer that provides for arbitration of any future dispute concerning a consumer financial product or service. As of the Compliance Date, consumers entering into RISCs containing pre-dispute arbitration agreements can't be stopped from filing class action claims in state or federal courts. The Rule also prohibits Providers from invoking a Waiver even after the Compliance Date. Waivers in pre-dispute arbitration agreements contained in RISCs entered into before the Compliance Date will still be enforceable unless and until the RISC (and the pre-dispute arbitration agreement) is transferred after the Compliance Date to a new owner or holder of the RISC.

Does the Rule require any changes to our pre-dispute arbitration agreements?

Yes, Providers will need to either remove or otherwise limit the effect of Waivers in

pre-dispute arbitration agreements entered into after the Compliance Date. In addition, the Rule requires that certain disclosures be made to consumers subject to pre-dispute arbitration agreements entered into after the Compliance Date. These disclosures must be made within 60 days after entering into a pre-dispute arbitration agreement.

(1) In all covered pre-dispute arbitration agreements: "*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. You may file a class action in court or you may be a member of a class action filed by someone else."*

(2) When the pre-dispute arbitration agreement applies to multiple products or services, only some of which are covered by the Rule, the Provider may include the following alternative provision in place of the one immediately above: "*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. The following provision applies only to class action claims concerning the products or services covered by that Rule: 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. You may file a class action in court or you may be a member of a class action filed by someone else."*

(3) When the pre-dispute arbitration agreement existed previously between other parties and does not contain either of the provisions in (1) or (2) above, the Provider must either

> (a) ensure the pre-dispute arbitration agreement is amended to contain the appropriate provision; or
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> (b) separately provide the consumer with the following written notice: "*We agree not to rely on 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 action filed by someone else."* When the pre-dispute arbitration agreement applies to multiple products or services, only some of which are covered by the Rule, the written notice may also include the following optional additional language: "*This notice applies only to class action claims concerning the products or services covered by the Arbitration Agreements Rule issued by the Consumer Financial Protection Bureau."*

(4) A Provider *may* add any one or more of the following sentences at the end of the disclosures required by sections (1) and (2) above:

> *(a) "This provision does not apply to parties that entered into this agreement before March 19, 2018."*
>
> *(b) "This provision does not apply to products or services first provided to you before March 19, 2018 that are subject to an arbitration agreement entered into before that date."*
>
> *(c) "This provision does not apply to persons that are excluded from the Consumer Financial Protection Bureau's Arbitration Agreements Rule."*

(d) "This provision also applies to the delegation provision." A Provider using this sentence as part of the disclosure required by sections (1) or (2) above is not required to separately insert those disclosures into a delegation provision that relates to a pre-dispute arbitration agreement. Delegation provisions are agreements to arbitrate threshold issues concerning a pre-dispute arbitration agreement and may sometimes appear elsewhere in a contract containing or relating to the arbitration agreement.

(5) In any provision or notice required above, if the Provider uses a standard term in the rest of the agreement to describe the Provider or the consumer, the Provider may use that term instead of *"we"* or *"you*."

(6) In any provision or notice required above, if a person has a genuine belief that sovereign immunity from suit under applicable law may apply to any person that may seek to assert the pre-dispute arbitration agreement, then the provision or notice may include, after the sentence reading, " *You may file a class action in court or you may be a member of a class action filed by someone else,"* the following language: *"However, the defendants in the class action may claim they cannot be sued due to their sovereign immunity. This provision does not create or waive any such immunity*." In the preceding sentence, the word "*notice"* may be substituted for the word "*provision"* when the included language is in a notice.

(7) A Provider may provide any provision or notice required above in a language other than English if the pre-dispute arbitration agreement also is written in that other language.

What information must be submitted to the CFPB?

An added bonus to the Rule is that Providers participating in arbitrations (either individual or class) pursuant to a pre-dispute arbitration agreement are required to submit detailed reports about the arbitration to the CFPB. These reports must be regular, thorough, redacted of personal and other information of individuals (but, not the Provider information) and will be posted by the CFPB online. The reports will be an operational nightmare and a virtual smorgasbord to enterprising Plaintiff's attorneys looking for a new target.

What are the chances the Rule will be nullified?

At this stage of the Rule, we appear to be down to two options: (i) use of the Congressional Review Act (CRA) by the Senate to nullify the rule and (ii) a lawsuit(s) by industry trade group(s) to try and get the courts to throw out the Rule. A third outside possibility is a new CFPB director and possible delays in the Compliance Date. It's still unclear if the Senate has the 51 votes necessary to nullify the Rule and the clock is ticking - it has only 60 legislative days to pass the CRA resolution. As for an industry lawsuit, it's not clear a judge would stay the Rule and litigation takes time - companies would still have to comply with the Rule in the interim. As for the outside option of a new CFPB director and delay of the Rule, it's too early to tell. Non-exempt dealers, banks and finance companies should be prepared for compliance with the Rule coming March.

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7037 Ridge Road, Suite 300, Hanover, Maryland 21076
410.684.3200

hudsoncook.com