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CBA CONSUMER BANKERS ASSOCIATION
The Voice of the Retail Banking Industry

FINANCIAL SERVICES ROUNDTABLE

August 22, 2016

The Honorable Richard Cordray
Consumer Financial Protection Bureau
1700 G Street N.W.
Washington, DC 20552

Re: <u>Comments on the Bureau's Proposed Arbitration Rule</u>

Dear Director Cordray:

The American Bankers Association,[1] the Consumer Bankers Association[2] and the Financial Services Roundtable[3] (collectively, the Associations) appreciate the opportunity to provide comments regarding the Bureau of Consumer Financial Protection (Bureau's) proposed rule regulating consumer arbitration agreements in financial services contracts published in the Federal Register on May 24, 2016.[4]

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1 The American Bankers Association is the voice of the nation's $15 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $11 trillion in deposits, and extend more than $8 trillion in loans.

2 Founded in 1919, the Consumer Bankers Association (CBA) is the trade association for today's leaders in retail banking – banking services geared toward consumers and small businesses. The nation's largest financial institutions, as well as many regional banks, are CBA corporate members, collectively holding well over half of the industry's total assets. CBA's mission is to preserve and promote the retail banking industry as it strives to fulfill the financial needs of the American consumer and small business.

3 As *advocates for a strong financial future*™, FSR represents 100 integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. FSR member companies provide fuel for America's economic engine, accounting directly for $98.4 trillion in managed assets, $1.1 trillion in revenue, and 2.4 million jobs.

4 Arbitration Agreements, Proposed Rule, 81 Fed. Reg. 32830 (May 24, 2016) (hereinafter Proposed Rule).

The Associations have been active participants throughout the administrative process leading up to the proposed arbitration rule. In fact, this is the Associations' fourth submission to the Bureau on arbitration.[5]

Many of the Associations' members, constituent organizations and affiliates (collectively, members) utilize arbitration agreements in their consumer contracts and, indeed, many of those contracts were included in the Study's data set. The Associations' members are major stakeholders in the Bureau's examination of consumer arbitration and will be affected by the Bureau's proposed rule, most particularly by its proposed prohibition on class action waivers. More significantly, our members' customers would be negatively affected by the Bureau's proposal, decreasing their available avenues for quick and effective complaint resolution, and steering them into resolution channels where, as evidenced in the Bureau's own Study, they would receive poorer resolution.

I. EXECUTIVE SUMMARY

Section 1028 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) requires the Bureau to "conduct a study of, and to provide a report to Congress concerning, the use of agreements providing for arbitration of any future dispute between covered persons and consumers in connection with the offering or providing of consumer financial products or services." Section 1028 further provides that the Bureau, "by regulation, may prohibit or impose conditions and limitations for the use of [such] an agreement" if it "finds that such a prohibition or imposition of conditions and limitations is *in the public interest* and *for the protection of consumers*." The findings in such a regulation must also be "*consistent with the study*." (Emphasis added).

The proposed rule should not be made final, as proposed, because it is *not* in the public interest or for the protection of consumers, and it is *not* consistent with the Bureau's March 2015 empirical Study of consumer arbitration. It should be withdrawn and not re-proposed unless it is consistent with the statutory parameters.

First, the proposed rule is not "in the public interest," nor does it meet the requirement to provide for consumer protection, because it would inflict serious financial harm (1) on consumers (those whom the Bureau is charged in the statute with protecting), (2) on the American federal and state court systems, and (3) on financial services providers. The Bureau provides estimates of covered entities' costs that will result from the additional class action litigation that will be filed if the proposed rule becomes final. The costs are unprecedented and

5 On June 22, 2012, the Associations submitted comments in response to the Bureau's Request for Information Regarding Scope, Methods, and Data Sources for Conducting of Pre-Dispute Arbitration Agreements. On August 6, 2013, the Associations submitted comments in response to the Bureau's request for comments on its proposed telephone survey of consumers. And, on July 13, 2015, the Associations submitted comments on the Bureau's March 10, 2015 study on consumer arbitration (Study).

staggering. As discussed in Part II of this letter, the Bureau estimates that the proposed rule will cause **53,000 providers** who currently utilize arbitration agreements to incur between **$2.62 billion and $5.23 billion** on a continuing five year basis in defending against an **additional 6,042 class actions** that will be brought every five years after the proposed rule becomes final.[6] These costs are not one-time costs, but **continuing** costs as the increase in class action filings are perpetual.

However, it is consumers who will truly suffer if the proposed rule becomes final. As taxpayers, they will pay for the increased costs to the court systems required to handle the permanent surge of 6,042 additional class actions every five years. As litigants, they will suffer increased court backlogs that long delay resolution of their cases. As customers of the providers, they will be saddled with higher prices and/or reduced services, because the billions of dollars in additional class action litigation costs will be passed through to them in whole or in part. In at least 87% of the class actions they will not benefit, because, as the Bureau found, in 87% of class action settlements consumers receive no compensation, and in the rare cases where they do receive a cash payment from a class action settlement, it will be a pittance, inasmuch as the Bureau Study found that the average participant in the class actions who were granted any reward received $32.35. Meanwhile, billions of dollars will be paid to the lawyers "representing" them. Moreover, at the same time consumers will be spending more as taxpayers and users of financial services, they will lose the many benefits of arbitration that the Bureau acknowledges in the proposed rule – resolving disputes in months, not years (at a fraction of the cost of litigation), receiving an average recovery of nearly $5,400 (166 times the average putative class member's recovery of $32.35), and enjoying the much more accessible avenue of dispute resolution than having to go to court.

Also illustrating that the rule is not needed "for the protection of consumers," and therefore should not be made final, is the Bureau's conclusion that there is nothing about arbitration that is *per se* harmful to consumers or to society as a whole. The Bureau itself, in its own practices, encourages its own employees to use alternative dispute resolution to resolve workplace disputes because it provides "faster and less contentious results" and it **preserves** "confidentiality."[7] As discussed in Part III of this letter, the Bureau's own data contradict its conclusion that arbitration agreements with class action waivers harm consumers by blocking class action claims and suppressing the filing of others. Among other things —

(a) 85% of credit card issuers and 92.3% of banks do not have arbitration clauses in their consumer loan or deposit contracts;

(b) Claims were ordered to be arbitrated in only 8% of the class actions studied by the Bureau;

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6 Proposed Rule *supra* note 4, at 32907-32909.

7 *See* United States Government Accountability Office, Report to Congressional Requestors, *Consumer Financial Protection Bureau Additional Actions Needed to Support a Fair and Inclusive Workplace* ("GAO Report"), pp. 48-49 (May 2016).

(c) 87% of the class actions that the Bureau claims are not brought because of arbitration agreements would not produce any benefits to consumers in any event;

(d) Small-dollar consumer claims are resolved more effectively and efficiently through government complaint portals such as the one maintained by the Bureau, as well as through providers' own informal dispute resolution procedures; and

(e) The Bureau claims that its own supervisory and enforcement actions have resulted in over $11.4 billion in relief to more than 25 million consumers — an important data point omitted from the Study. In other words, in the Bureau's own public assertions, consumers received an average payment of $440.00, compared to the $32.35 received by the average putative class member, and billions of dollars were not diverted to pay plaintiffs' class action attorneys' fees.

The proposed rule also threatens to have an adverse impact on consumers because arbitration is likely to disappear almost entirely if class action waivers are eliminated. Consumers thus lose access to a fast, efficient, less expensive, and more convenient dispute resolution system. Most notably, it will no longer be a viable option for those who have small-dollar "non-classable" claims – *i.e.*, claims that are not amenable to class action disposition because they do not implicate systemic conduct. Consumers wanting to pursue non-classable claims will have to endure the inconvenience and costs of going to court. This includes taking time off from work, paying court costs, and facing the challenges inherent in the court system to prosecute such claims. Particularly for small dollar claims, consumers are likely to conclude that prosecuting the claim in court is more trouble than it is worth.

Moreover, the Bureau has ignored other dispute resolution mechanisms that address the Bureau's justifications for the proposal, specifically its concerns regarding resolution of small-dollar claims, redress for harms unknown to consumers, and the modulation of corporate behavior. The Bureau has discounted the impact of informal resolutions, its own Complaint Response Portal, and social media. It has also neglected to mention what elsewhere in its public statements the Bureau loudly touts, the power of government enforcement actions, including its own. Finally, the Bureau failed to consider, as required, alternatives that would address the Bureau's concerns, such as allowing enforcement of class action waivers for matters that the financial service provider has identified and resolved prior to a class action being filed.

Second, the proposed rule is not "consistent with the study." Notably, as discussed in Part III of this letter, the Bureau's commentary accompanying the proposed rule expressly *confirms* the Associations' position that arbitration is faster, more economical, and far more beneficial to consumers than class action litigation and that the arbitration process is fair to consumers.[8]

In truth, the Bureau's proposed ban on class action waivers and the resulting projected avalanche of additional class actions is *not necessary* to protect consumers and is *not supported* by the Bureau's empirical Study. Two noted arbitration scholars recently concluded that the

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8 *See* Associations' July 13, 2015 comment letter, available at http://www.aba.com/Advocacy/commentletters/Documents/cl-jointArbitration2015.pdf.

Bureau's Study "provides no foundation for imposing new restrictions or prohibitions on mandatory arbitration clauses in consumer contracts."[9] According to their critique, the Study "fail[s] to support any conclusion that arbitration clauses in consumer credit contracts reduce consumer welfare or that encouraging more class action litigation would be beneficial to consumers and the economy …. Substantially more and different evidence would be necessary to conclude that consumers are harmed by arbitration or that they would benefit from unleashing class action litigation more routinely."[10]

Third, the Study was incomplete on key issues that would have further demonstrated that the proposed rule is not in the public interest or needed for the protection of consumers. The Bureau neglected to review the effect of its own administrative and enforcement activities and did not study consumer satisfaction with arbitration, as recommended. Nor did it study either the impact on consumers and society if companies abandon arbitration or the costs to consumers and society of the additional 6,042 class actions that would be filed every five years. It also did not investigate whether class actions are necessary as a deterrent given the impact of modern social media. Finally, while its survey found a lack of awareness about arbitration as an option for dispute resolution, its Consumer Education and Engagement division spent none of its resources on educating consumers about arbitration.

II. THE PROPOSED RULE IS NOT IN THE PUBLIC INTEREST NOR DOES IT MEET THE REQUIREMENT TO PROVIDE FOR CONSUMER PROTECTION

The proposed rule would govern two aspects of consumer financial services dispute resolution. First, the proposed rule would prohibit covered providers of certain consumer financial products and services from using an agreement with a consumer that provides for arbitration of any future dispute between the parties and that bars the consumer from filing or participating in a class action with respect to the covered consumer financial product or service. Second, the proposal would require a covered provider that is involved in an individual arbitration pursuant to a pre-dispute arbitration agreement to submit certain specified arbitral records to the Bureau.

As noted, the Dodd-Frank Act permits the Bureau to restrict or prohibit the use of mandatory arbitration agreements in consumer financial service agreements only if it finds doing so is in the public interest and would provide for consumer protection**.** While these two concepts often overlap, we do not believe that the Bureau has justified in its Study or can justify the proposed class action waiver ban on either basis.

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9 Jason Scott Johnson & Todd Zywicki, *The Consumer Financial Protection Bureau's Arbitration Study: A Summary and Critique*, p. 5 (Mercatus Ctr., George Mason Univ., Working Paper (Aug. 2015), available at http://mercatus.org/sites/default/files/Johnston-CFPB-Arbitration.pdf.

10 *Id.* at 6, 14.

The increase in lawsuits resulting from the ban on class action waivers will increase court system – and therefore society's – costs and delay justice. Consumers will pay more and get less as financial service providers are forced to absorb the increased litigation costs. Moreover, consumers and society lose the benefits of arbitration, which is faster, cheaper, more convenient, and more rewarding to consumers than court and is more suitable for small dollar claims and non-classable claims. Furthermore, contrary to the Bureau's assertion, the data show that class action waivers do not foreclose the opportunity for class actions. Moreover, class actions are not necessary to address small dollar claims that people might not bother to bring to arbitration or court individually or harms about which people may be unaware. Nor are they necessary to serve as a deterrent to questionable or illegal practices. Other dispute resolution processes offer redress for these claims without imposing the costs and other harms to consumers and society that the proposed ban on class action waivers will bring.

A. Additional class actions will needlessly strain an already overburdened and underfunded court system, delay justice, and impose costs on taxpayers, which is not in the public interest and harms consumers.

The proposal is not "in the public interest" because it does not take into account that the proposed prohibition against the class action waiver will increase permanently the burden on courts, as the Bureau's own data demonstrate. The result will be increased taxpayers' expense and detrimental court delays in administering and resolving lawsuits.

In its commentary to the proposed rule, the Bureau estimates that the elimination of class action waivers will lead consumers to file **6,042 additional class actions in federal and state court** against 53,000 providers every five years.[11] This amounts to 100 new lawsuits a month. The Bureau estimates that financial service providers will pay between $2.62 billion and $5.23 billion dollars to defend, and in some cases, settle, the additional class actions. However, beyond the enormous costs financial service providers will continually incur, there are additional unrecognized, permanent costs and consequences. The Bureau completely **ignores the substantial delay in judicial administration and the permanent increased costs to federal and state courts** to administer the cases associated with this maelstrom of additional litigation.

The courts are currently grievously overburdened and underfunded. If the proposal is adopted, taxpayers will suffer delays and will pay for the extra resources needed to deal with this onslaught of additional class actions — taxpayers who will not even benefit from 87% of the cases for which there is no compensation and who will receive only a pittance in compensation

[11] The Bureau estimates that over a five-year period financial services providers will be sued in 514 additional federal court class actions. It further estimates that there will be 2,507 additional federal court class action cases filed during the five-year period that will settle individually. The Bureau anticipates that an equal number of class actions will be filed in state courts. Proposed Rule *supra* note 4, at 32907, 32909. 514 additional federal court class action cases settled on a class basis + 2,507 federal court class action cases settled on an individual basis = 3,021 additional federal court class actions + 3,021 additional state court class action cases = 6,042 total additional federal court and state court class action cases.

from the 13% that do settle after years of meandering through the courts. Instead, a handful of plaintiffs' lawyers will be the real beneficiaries if the proposed rule becomes final. Other cases will be delayed while every five years an additional 6,042 class actions clog the judicial system.

The Bureau estimated costs to financial service providers, but apparently assumed that there is no cost to society in maintaining a court system. Even unmeritorious class actions that may ultimately be dismissed or withdrawn place a great strain on the judicial system: they take up room on the docket and delay the adjudication of more meritorious cases; they require court administration and supervision, usually under the court's complex procedures protocol, for many months if not years; and, particularly if discovery is undertaken, they tax the scarce resources of the courts.

More than 30 years ago, Chief Justice Burger urged greater use of arbitration to reduce "the backlog of cases in the overburdened federal and state courts." "Protracted cases," he emphasized, "not only deny parties the benefits of a speedy resolution of their conflicts, but also enlarge the costs, tensions and delays facing all other litigants waiting in line." "In terms of cost, time and human wear and tear, arbitration is better by far," Chief Justice Burger concluded.[12] Class actions are the epitome of "protracted cases," to which Chief Justice Burger referred. Study data confirm that they typically last for two years or more, compared to arbitration proceedings which are initiated and concluded in a matter of months.[13]

Things have become dramatically worse during the three decades since Chief Justice Burger made his observations about the benefits of arbitration. A 2014 report on New York federal and state courts concluded that "[d]elays at every stage of every matter before the courts are now common: delays in getting into the courthouses, delays in processing documents, delays in the public's ability to obtain archived documents, delays in trial proceedings, delays in decisions."[14] Likewise, another report co-authored in 2014 by the former Chief Justice of the Minnesota Supreme Court observed:

> Citizens turn to our state courts when their lives are in crisis. But after years of underfunding, many state courts are unable to timely deliver the justice our citizens seek, and to which they are entitled …. Budget cuts in many states … have required court systems to lay off staff, reduce court hours, close or consolidate courts in some instances, and give priority to criminal cases that require [compliance with] speedy trial rules. This has resulted in significant

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12 *See* Giles Hudson, "Burger Urges Greater Use of Arbitration to Reduce Court Backlog" (Aug. 21, 1985), available at http://www.apnewsarchive.com/1985/Burger-Urges-Greater-Use-of-Arbitration-to-Reduce-Court-Backlog/id-a294b2e9e054f20b9c5b0ec9dc39dd73.

13 Study, § 1, p. 13; § 6, pp. 9, 43.

14 Task Force on Judicial Budget Cuts, Co-Chairs: Hon. Stephen G. Crane and Michael Miller, Report on Public Hearing Conducted on December 2, 2013, Executive Committee of the New York County Lawyers' Association (Jan. 2014).

> delays in resolving civil cases in jurisdictions where court funding has been cut. Delayed resolution through lack of judicial funding inflicts widespread economic harm. Because of uncertainty in the outcome of a pending trial or even a trial date, for that matter, businesses are reluctant to add employees, expand product lines, or invest in capital equipment all of which affects the vitality of the local economy.[15]

Further illustration of the burdens courts face is reflected in the statistics reported by the Administrative Office of the U.S. Courts, which found that the number of pending federal district court cases has risen from 370,067 in 2013 to 427,512 as of March 31, 2016.[16]

Not only will the influx of new class action suits delay justice, American taxpayers will pay, as it is they who fund the operation of the court system already under severe budgetary pressures. Chief Justice Roberts has identified "[t]he budget" as "the single most important issue facing the courts."[17] Congressional funding of the federal court system reached $6.697 billion in 2015.[18] At the same time, courts were struggling to contain and reduce costs. In 2014, the Director of the Administrative Office of the U.S. Courts emphasized the need to "assure that the limited resources available are carefully managed and properly spent."[19]

While the courts try to put themselves on a fiscal diet, the Bureau would load the scales with an additional 6,042 protracted and mostly meritless[20] class action suits, where arbitration, as demonstrated in Section III, is less expensive, more convenient, and more efficient than court litigation. The proposed rule would, if it becomes final, further undermine the ability of our already inadequate court system "to secure the just, speedy, and inexpensive determination of every action and proceeding."[21]

The Bureau ignores the broader impact of the proposed rule on society. Permanently burdening the court system with 6,042 additional class actions every five years in the hope that a few might succeed – and return a negligible $32.35 to the average class member – is indisputably bad public policy and is clearly not in the public interest.

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15 E.J. Magnuson, *et al.*, "The Economics of Justice," pp. 1-2 (DRI 2014).

16 Administrative Office of U.S. Courts, Federal Court Management Statistics, District Courts, p. 1 (Mar. 31, 2016).

17 2013 Year-End Report on the Federal Judiciary.

18 Administrative Office of U.S. Courts, Fiscal Year 2014 Funding for the Judiciary (2014).

19 Administrative Office of U.S. Courts, Annual Report 2014, Director's Message.

20 As discussed, 87% of the class actions studied by the Bureau produced no benefits to the putative class members.

21 Fed. R. Civ. P. 1.

B. The additional costs associated with the increase in class action lawsuits will result in higher prices, fewer choices, and lower quality services for consumers as providers pass their costs onto their customers. This result is not in the public interest and harms consumers.

The additional lawsuits will not only raise taxpayers' costs to support the court system and delay justice, they will increase what consumers pay for financial services and leave them with fewer choices and lower quality services. Simply put, basic economic theory holds that when expenses increase, prices rise, services decrease, and/or innovation slows.[22] None of these outcomes serves consumers or society.

As the Bureau acknowledges, if the proposed rule becomes final, the "vast majority" of companies using arbitration agreements, who presently have "virtually no exposure to class litigation," will face "at least as much exposure as is currently faced by those providers with similar products or services that do not use arbitration agreements."[23] According to the Bureau:

> [I]f the class proposal is finalized, those providers that are sued in a class action would also incur expenses associated with additional class litigation. The major expenses to providers in class litigation are payments to class members and related expenses following a class settlement, plaintiff's legal fees to the extent that the provider is responsible for paying them following a class settlement, the provider's legal fees and other litigation costs (in all cases regardless of how it is resolved), and the provider's management and staff time devoted to the litigation.[24]

As noted, the Bureau estimates that the cost for companies to defend and settle the additional 6,042 additional class actions will **total between $2.62 billion and $5.23 billion**

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22 Basic economic theory shows that if companies' costs increase, that pressure will show up somewhere else, affecting either costs or product. This means consumers pay more or get less. Many courts and commentators have so concluded. *See, e.g., Metro East v. Quest*, 294 F.3d 294, 297 (7th Cir.), *cert. denied*, 537 U.S. 1090 (2002) (The "benefits of arbitration are reflected in a lower cost of doing business that is passed along to customers. That is because by limiting discovery and dealing with individual rather than class claims it "curtails the cost of the proceedings and allows swift resolution of small disputes."); *Provencher v. Dell*, 409 F. Supp. 2d 1196, 1203 n. 9 (C.D. Cal. 2006) ("it is likely that consumers actually benefit in the form of less expensive computers reflecting Dell's savings from inclusion of the arbitration clause in its contracts"); *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (1991) ("it stands to reason that passengers containing a forum clause … benefit in the form of reduced fares …"); Stephen J. Ware, *Paying the Price of Process: Judicial Regulation of Consumer Arbitration Agreements*, 2001 J. Disp. Resol. 89, 91-93 (2001); Richard A. Posner, Economic Analysis of Law 7 (6th ed. 2003).

23 Proposed Rule *supra* note 4,at 32899.

24 *Id.* at 32905.

every five years. The Bureau acknowledges such costs and effects, explaining that the Bureau "believes that most providers would pass through at least portions of some of the costs [resulting from the proposed rule] … to consumers. This pass-through can take multiple forms, such as higher prices to consumers or reduced quality of the products or services they provide to consumers."[25]

A February 2016 study by Emory School of Law Professor Joanna Shepherd, "An Empirical Survey of No-Injury Class Actions," is also illuminating on this point.[26] Professor Shepherd concludes:

> Economic theory predicts that many no-injury class actions are of dubious social value and end up harming the very consumers they are meant to help. Both no-injury class action litigation and the threat of no-injury claims impose significant costs on businesses. Protracted adversarial litigation imposes significant costs on defendant businesses that must foot the costs of defending against, settling, and paying these claims. Even the possibility of a no-injury class action claim forces businesses to incur litigation expenses to determine the scope of the law and acceptable behavior. Moreover, the in-terrorem effect of class action lawsuits triggers defendants' risk-aversion and motivates them to settle claims for more than their expected value, often inducing a quick but expensive settlement. The litigation expenses, attorneys' fees, and settlement costs are initially borne by businesses. However, **they are soon passed on to consumers through increased prices, fewer innovations, and lower product quality. Indeed, several empirical papers confirm that businesses pass on litigation expenses to consumers across many different industries. Most consumers will receive little benefit in exchange for the higher prices, reduced innovation, and lower product quality**. Many of the no-injury claims concern business practices that cause little concrete consumer harm. As a result, forcing compensation or deterrence through litigation produces little, if any, tangible benefits to consumers.[27] (Emphasis added.)

In other words, consumers in general will pay so that a few will gain something, but very little. The resulting increased prices, fewer choices, lower quality services, and lack of meaningful benefit to consumers do not enhance consumer protection and are not in the public interest.

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25 *Id.* at 32911.

26 Joanna Shepherd, "An Empirical Study of No-Injury Class Actions," Feb. 1, 2016, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2726905.

27 *Id. at* 23-24.

C. Banning class action waivers harms consumers and is not in society's interest, because the ban will cause financial service providers to eliminate or greatly reduce arbitration as a dispute resolution option. This will occur despite the evidence that arbitration is faster, cheaper, and more convenient than court resolution, provides higher awards than class actions, and accommodates non-classable claims that would not be resolved by class actions.

Significantly, the Bureau does not directly propose to prohibit consumer arbitration agreements. The Bureau finds nothing inherently unfair or disadvantageous about consumer arbitration[28] and even urges its own employees to use alternative dispute resolution to resolve workplace disputes.[29] It found no evidence that arbitration was any less beneficial for consumers than individual litigation. Indeed, it acknowledges that after four years of research resulting in "the most comprehensive empirical study of consumer financial arbitration ever conducted,"[30] it has determined that "the evidence is inconclusive" on whether individual arbitration conducted during the Study period is superior or inferior to individual litigation in terms of remediating consumer harm.[31]

In fact, arbitrations, the Bureau admits, "proceed relatively expeditiously, the cost to consumer of this mechanism is modest …, at least some consumers proceed without an attorney," and consumers who prevail in arbitration may obtain "substantial individual awards" as "the average recovery … was nearly $5,400."[32]

Thus, the Bureau demonstrates in its Study that consumers do better in arbitration than in going to court. Awards are higher, resolution is faster, and consumer costs are less in arbitration than in court. The Bureau found that the average relief in affirmative arbitration claims was $5,389 compared to a mere $32.35[33] average for class actions, the time to resolve the matter is 12 times faster in arbitration than in class actions in court, and the cost of initiating arbitration is $200 compared to the $400 it costs to file a class action complaint in federal court.

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28 The proposed rule thus does not accept the misconception fostered by consumer advocates that companies have an unfair advantage in arbitration over consumers. *See* Study, § 5.6.12, pp. 56-57.

29 *See supra* note 7.

30 Director Cordray's Published Remarks, March 10, 2015 Field Hearing in Newark, New Jersey. *See* http://www.consumerfinance.gov/newsroom/prepared-remarks-of-cfpb-director-richard-cordray-at-the-arbitration-field-hearing/.

31 Proposed Rule *supra* note 4, at 32855.

32 *Id.*

33 *See* Study, § 5, pp. 13, 41; Proposed Rule *supra* note 4, at 32849 n. 305.

Other advantages of arbitration include its convenience and accessibility. Arbitration may be conducted not only in person, but by phone, email, or Skype, and it is more convenient, less expensive, and less intimidating than going to court, making it particularly amenable to small dollar claims. People avoid having to take off time from work and endure the hassles inherent in the court system. Arbitration is also less expensive than litigation because it is often subsidized by the financial service provider.[34] (*See* joint comment letter on proposed arbitration rule submitted by American Bankers Association, U.S. Chamber of Commerce and 27 other trade groups on August 22, 2016).

Notwithstanding these significant advantages of arbitration and the Bureau's conclusion that there is nothing about arbitration as a process that is *per se* harmful to consumers' rights or to society as a whole, the ban on class action waivers in the proposed rule will likely turn out to be a *de facto* prohibition on most, if not all, consumer financial services arbitration. Many, if not most, financial service providers anticipate they would abandon arbitration altogether, since the cost both of subsidizing individual arbitration proceedings and the cost of defending the anticipated onslaught of consumer class actions would be prohibitive.

The resulting harm from the loss of arbitration is most pronounced for non-classable cases, those disputes that lack the common elements necessary for a class action. Particularly for small claims, consumers may conclude that prosecuting the individual claim in court is more trouble than it is worth. Without arbitration, the typical consumer, "who has only a small damage claim" would be left "without any remedy but a court remedy, the costs and delays of which could eat up the value of an eventual small recovery." *Allied-Bruce Terminix Cos., Inc. v. Dobson*, 513 U.S. 265, 261 (1995). Those with non-classable claims will have the choice of not pursuing a claim or enduring the inconvenience, time, and costs associated with going to court with the prospect of little benefit at the end.

If the proposal is adopted, consumers will lose access to a convenient, affordable, efficient dispute mechanism that is especially suited to small dollar disputes and that accommodates non-classable cases which otherwise may not be resolved. The result is clearly not in the public interest and does not protect consumers.

D. Class action waivers do not foreclose the opportunity for class actions, and even if they did, few if any consumers would be harmed.

As noted above, the Bureau presented *no evidence* that arbitration is any less beneficial for consumers than individual litigation, and the agency encourages its own employees to use alternative dispute resolution to resolve workplace disputes.[35] Nevertheless, it concluded that

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34 Under the AAA and JAMS consumer arbitration rules, companies pay the lion's share of the filing, administrative and arbitrator costs, which in an individual arbitration can exceed $3,000.00. The consumer's share of the costs is capped at $200.00 (AAA) or $250.00 (JAMS). Many companies, in their arbitration agreements, also agree to pay the consumer's share of the costs.

35 *See supra* note 7.

arbitration agreements with class action waivers harm consumers, asserting that they block class action claims and suppress the filing of others.[36]

However, the Bureau's Study shows the opposite. The data clearly demonstrate that only a small percentage of class actions were impacted by arbitration agreements: "[C]ompanies moved to compel arbitration in 94 of the 562 class action cases in the bureau's dataset, and … the motion was granted in full or in part in 46 cases."[37] "In 8 percent of the 562 class cases (45 cases), all claims against a company were stayed or dismissed based on a company filing an arbitration motion."[38]

These data alone dispel the conclusion that arbitration is a barrier to class actions, since **in 92% of the class actions studied by the Bureau, arbitration was not even a factor**. These data are particularly remarkable since in the middle of the time period studied (2010-2012), the U.S. Supreme Court upheld the validity of class action waivers in consumer arbitration agreements in *AT&T Mobility LLC* v. *Concepcion*, 131 S. Ct. 1740 (2011). The Bureau's Study found that while *Concepcion* generated a "slight upward trend" in the use of arbitration provisions, "the increase has not been as dramatic as predicted by some commentators."[39]

Moreover, there is abundant competition in the financial services marketplace to accommodate consumers who prefer not to arbitrate. The Study found that 85% of credit card issuers and 92.3% of banks do not include arbitration provisions in their consumer contracts. These include four of the ten largest credit card issuers, Bank of America, Capital One, Chase, and HSBC, which before 2009 included arbitration provisions in their account agreements but no longer do so.[40] At least 25% of consumers whose credit card and deposit account contracts do contain arbitration provisions have a contractual right to reject the arbitration provision within 30 to 60 days of entering the contract without affecting any other provision in their contracts.[41]

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36 Proposed Rule *supra* note 4, at 32915 ("arbitration agreements effectively block consumers from participating in class proceedings").

37 *Id.* at 32847.

38 *Id.*

39 Study § 2, p. 12.

40 *Id.* § 2, pp. 10-11.

41 *Id.* § 2, p. 31. Scores of federal and state courts have enforced arbitration provisions on the basis that they permitted the consumer to opt out and, therefore, were not contracts of adhesion. *See, e.g.*, *Providian National Bank v. Screws*, 894 So. 2d 625 (Ala. 2003); *Tsadilas v. Providian National Bank*, 13 A.D.3d 190, 786 N.Y.S.2d 478 (N.Y. App. Div. 1st Dep't 2004), *appeal denied*, 5 N.Y.3d 702, 832 N.E.2d 1189, 799 N.Y.S.2d 773 (June 4, 2005); *Pivoris v. TCF Financial Corp.*, No. 07-C 2673, 2007 U.S. Dist. LEXIS 90562 (N.D. Ill. Dec. 7, 2007); *Martin v. Delaware Title Loans, Inc.*, No. 08-3322, 2008 WL 444302 (E.D. Pa. Oct. 1, 2008); *Clerk v. ACE Cash Express, Inc.*, No. 09-05117, 2010 U.S. Dist. LEXIS 7978 (E.D. Pa. Jan. 29, 2010).

The Study clearly shows that the vast majority of class actions fail, not because the underlying disputes are sent to arbitration for individual disposition, but because they inherently lack merit and/or are not certifiable. In the class actions studied by the Bureau, "[t]he most common outcome was a potential non-class settlement (typically, a withdrawal of claims by the plaintiff) …. Classwide judgment for consumers … [was] the least frequent of the identified outcomes …, occurring in less than 1% of cases."[42] The Study further found that "[c]lass certification rarely occurred outside the context of class settlement" and "[n]o class cases went to trial."[43] Even as to the 92% of the class actions studied that were not ordered to be arbitrated, the Study establishes that class actions are an exceptionally poor vehicle for producing relief to consumers. These numbers effectively challenge the notion that class actions are needed to protect consumers.

E. The alleged negative consequences to society and consumers of the class action waiver ban are not justified. Other dispute resolution mechanisms address such concerns as the lack of consumer awareness of harm, reluctance to pursue small dollar claims, and the assertion that class actions are needed to change corporate behavior.

The Bureau justifies banning class action waivers largely on the argument that class actions are necessary to address small dollar disputes and harms unknown to consumers. Further, the Bureau asserts that class action litigation, and the threat of class action litigation, are necessary to help regulate and change corporate behavior. These justifications, however, ignore a number of existing dispute resolution mechanisms which effectively and efficiently address those concerns and challenge the very foundation of the Bureau's policy proposal to ban class action waivers.

1. Class actions are ineffective in addressing small dollar claims and harms unknown to consumers.

To illustrate, in the 87% of class actions that produced no benefits to putative class members, the putative class members never learned about the case or the rights (allegedly) violated. These cases did not reach the stage where notice is given to the class members. Presumably, a similar trend would be manifest in the 6,042 additional class actions the Bureau estimates that will recur every five years if the proposed rule becomes final. In the vast majority of those additional cases, the class actions also will not serve to protect consumers who do not know that their rights (allegedly) were violated.

Similarly, class action lawsuits do little to assist consumers in resolving small dollar claims. The Bureau's own Study shows that the vast majority (87%) of class actions produce no benefits at all to the putative class members, while the few class members who do receive settlement payments get an average of $32.35 after waiting for years.

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42 Study, § 6, p. 37.

43 *Id.* § 1, p. 14.

2. **Most disputes are resolved informally**.

Significantly, the vast majority of consumer disputes are resolved by direct interaction between customer and financial institution or by informal methods without the need for arbitration or litigation (even small claims litigation), **a fact the Bureau has discounted.** Such methods include internal complaint resolution processes as well as the Bureau's consumer complaint portal, which are much more efficient and cost-effective from the consumers' and society's perspective.

First, financial services companies maintain internal complaint resolution programs which, unlike class actions, can address consumer disputes quickly and efficiently. Financial service providers are driven to support robust complaint resolution systems by the desire and need to satisfy customers in order to retain customer relationships and thereby survive in a competitive environment. And in today's world, where stories and complaints may be quickly and widely broadcast through the press and social media, companies have powerful incentives to resolve disputes fairly and quickly, especially small dollar disputes, even when they lack merit. Banks, in particular, have additional incentives to support strong complaint management systems and ensure complaints are resolved fairly because of the emphasis given to complaints in the examination process.

Second, the Bureau has established a Consumer Response Portal – a resource it regularly touts for its effectiveness in obtaining relief to consumers as well as encouraging fair practices. According to its website, as of July 1, 2016, approximately 930,700 alleged consumer complaints filed through the Portal were resolved,[44] and companies responded to 97% of the complaints in a timely manner, typically within 60 days. The resolutions often include monetary relief. The Bureau's Consumer Response Annual Report related that in 2015, this included median relief of $23 for 170 credit reporting complaints, $100 for 3,290 credit card complaints, $105 for 3,170 bank account and service complaints, $173 for 240 private student loan complaints, $317 for 400 debt collection complaints, $500 for 1,240 mortgage complaints, and $347 for 80 payday loan complaints, nearly all of which, it can be noted, exceed the usual class action relief (in the few instances when they yield to consumers any monetary awards).[45] In addition to the Bureau, a vast number of other federal agencies as well as state agencies, such as state attorneys' general offices, provide their own complaint portals.

Furthermore, according to the Bureau's Company Portal Manual, its complaint process includes using information "to help prioritize complaints for investigation" and "[c]omplaint data and information is shared with other offices within the CFPB, including but not limited to Enforcement and Supervision …."[46] This means that if there is a systemic problem, including,

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44 CFPB, Monthly Complaint Report, Vol. 13 (July 2016).

45 CFPB, Consumer Response Annual Report, pp. 1, 4 (March 2016).

46 CFPB, Company Portal Manual, ver. 2.16 (March 2016), p. 6. *See also id.*, p. 30 ("Consumer Response may conduct an independent investigation of any consumer complaint submitted to the CFPB … [including] the extent to which those concerns were adequately addressed in your company's response to the consumer).”

for example, one involving small dollar amounts or one involving potential harm about which people may be unaware, the Bureau and other federal agencies will learn of it, investigate and may take appropriate corrective or enforcement action.

3. Government enforcement actions are effective in addressing consumer harm and changing corporate behavior.

The Bureau's conclusion that class actions are necessary to resolve small dollar claims, address harms about which people are unaware, and modify and regulate corporate behavior belies the fact that the Bureau claims to be far more effective and efficient than class actions in addressing such matters from society's and consumers' perspective. Through 2015, the Bureau has ordered companies to pay more than $11.4 billion to more than 25 million consumers. Similarly, in January 2016, the CFPB stated: "In the six months covered by this report [July 2015-December 2015], our supervisory actions resulted in financial institutions providing more than $95 million in redress to over 177,000 consumers."[47] In the first four months of this year, the Bureau reported that its supervisory actions resulted in payments of $24.5 million in restitution to more than 257,000 consumers.[48]

Based just on the December 2015 data, the Bureau claims enforcement efforts have resulted in an average payment of $440 to each consumer, approximately 14 times the $32.35 cash payment received by the typical putative class member. Any assumption by the Bureau that class actions are necessary as an enforcement tool is contradicted by the data.

Moreover, the Bureau's Bulletin 2013-06 on responsible business conduct underscores the effectiveness of enforcement and the agency's expectation of self-monitoring and self-reporting.[49] The Bulletin makes clear that institutions should self-monitor and report to the Bureau any issues the institution discovers. It requires that institutions make full restitution to all affected customers, regardless of the amount involved.[50] Failure to do so may have negative supervisory consequences.[51]

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47 Semi-Annual Report of the Consumer Financial Protection Bureau," p. 12 (Jan. 2016).

48 CFPB, "Supervisory Highlights," p. 3 (June 2016).

49 CFPB, "Responsible Business Conduct: Self-Policing, Self-reporting, Remediation, and Cooperation" (June 25, 2013).

50 "When violations of federal consumer financial laws have occurred, the Bureau's remedial priorities include[e] obtaining full redress for those injured by the violations…" *Id.*, p. 4.

51 "[A] party may proactively self-police for potential violations, promptly self-report to the Bureau when it identifies potential violations, quickly and completely mediate the harm resulting from violations, and affirmatively cooperate with any Bureau investigation above and beyond what is required. If a party meaningfully engages in these activities…,

There is no doubt that government enforcement actions, and the threat of enforcement actions, not only put more money into people's pockets than class action suits and protect those unaware of any alleged harm, but they also modify corporate behavior. The Bureau clearly recognizes that enforcement actions and the threat of such actions compel changes in corporate behavior. Its Bulletin states that the Bureau's remedial priorities "include … ensuring that the party who violated the law implements measures designed to prevent the violation from recurring, and when appropriate, effectuating changes in the party's future conduct for the protection and/or benefit of consumers."[52] Recognizing the "important benefits gained by consumers through behavioral changes companies agree to make that benefit both existing customers and future customers,"[53] the Bureau frequently tries to secure such behavioral relief from companies through its own enforcement actions. Although the value of these behavioral changes are typically not quantified in case records, "the Bureau believes their value to consumers are significant."[54] Moreover, the enforcement actions impact not just the subject of the action, but all financial service providers. As Director Cordray stated, "[I]t would be 'compliance malpractice' for executives not to take careful bearings from the contents of these orders about how to comply with the law and treat consumers fairly."[55] The strength of the Bureau's enforcement powers in moderating corporate behavior is enhanced due to the premium that companies place on maintaining good relations with their customers and their reputation. As the Bureau is well aware, being the subject of a Bureau enforcement or supervisory action, especially as it is quickly, widely, and repeatedly circulated through social media forums and the press, serves to "shame" companies into compliance and deters unlawful and questionable conduct. Indeed, the Bureau acknowledges that two "important mechanisms" for incentivizing companies to conform their conduct to the law are reputation and public enforcement:

> The first incentive is the economic value for the provider to maintain a positive reputation with its customers, which will create an incentive to comply with the law to the extent such compliance is correlated with the provider's reputation …. The second incentive is to avoid supervisory actions or public enforcement actions by Federal and state regulatory bodies, such as the Bureau. In response to this, many providers have developed compliance programs, particularly where they are subject to ongoing active supervision by Federal or state regulators.[56]

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it may favorably affect the ultimate resolution of a Bureau enforcement investigation." *Id.* at 1.

52 *Id.*at 4.

53 Proposed Rule *supr*a note 4, at 32858-32859.

54 *Id.* at 32859.

55 *See* http://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-cfpb-director-richard-cordray-at-the-consumer-bankers-association/.

56 Proposed rule *supra* note 4, at 32900.

Thus, the threat of enforcement and the rules encouraging financial institutions to self-report, remediate, and modify practices ensure that consumers obtain redress (even if the harm involves a small amount and even if consumers are unaware of the harm) and changes corporate behavior, the stated justifications for banning class action waivers. These concerns are efficiently and effectively addressed without the consumer and societal harms from the demonstrated inefficiencies, costs, and delays inevitable with class actions.

In addition, in contrast to trial lawyers who receive the bulk of any class action awards, the Bureau and other agencies are more likely to pursue cases in a manner that yields awards predominantly to the offended consumers. In private class action litigation, counsel for the class seek a sizeable percentage of any recoveries obtained (almost half a billion dollars – $424,495,451 – in attorneys' fees in just the limited class action data base studied by the Bureau).[57] This arrangement influences the cases they select and how they resolve them. In contrast, for Bureau actions, there is no similar potential conflict between the interest of the consumers and the attorneys representing them. This means that government and financial service providers' resources are more likely to be efficiently managed and consumers' awards maximized. Notably, the $11 billion in consumer relief provided by the Bureau's enforcement activities through December 2015 was not reduced by billions of dollars to pay attorneys' fees.

4. Lack of use of arbitration is not indicative of the need for class actions.

The Bureau also attempts to justify the proposed rule, in part, on the relative infrequent use of arbitration to resolve disputes. The Bureau asserts that this indicates that individual arbitration is not as effective as class actions for resolving small dollar consumer claims. As discussed above, however, consumers have available, and use, superior, more efficient, and cost-effective alternatives to resolve small dollar disputes. In addition, there are other explanations for consumers' use of alternatives to arbitration, including the following:

(1) Cases are settled. For example, financial institutions settle cases with merit to avoid the significant arbitration costs. They may also settle cases that lack merit for the same reason.

(2) Consumer advocates have sent consistently negative messages about arbitration for almost two decades and have done their best to dissuade consumers from arbitrating.

(3) Consumer arbitration is still "the new kid on the block" compared to litigation.

(4) As discussed, vigorous governmental enforcement actions eliminate the need for consumers to initiate arbitration, including vigorous regulatory and supervisory activities by the Bureau itself.

(5) Individuals are turning increasingly to on-line arbitration and mediation resources to resolve small-dollar customer complaints.

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57 Study, § 8, p. 33.

(6) The Bureau has failed to educate consumers about the many benefits that arbitration can offer as opposed to litigation.[58]

In summary, the addition of 6,042 class actions every five years and the concomitant injury to society and consumers are high and unnecessary prices to pay to resolve small dollar claims, address harms about which people are unaware, or to moderate corporate behavior—the justifications for the prohibition on pre-dispute class action waivers. A variety of mechanisms, including internal and government complaint processes, public opinion, and the powerful enforcement authority of the Bureau and other government agencies address those concerns more effectively and efficiently than do class actions.

F. The Bureau should allow the enforcement of class action waivers for matters that the entity has identified prior to a class action being filed.

Dodd-Frank Act section 1022, which defines the Bureau's rulemaking authority, directs the Bureau to consider, "the potential benefits and costs to consumers and covered persons, including the potential reduction in access by consumers to consumer financial products or services resulting from such rule." Inherent in any cost-benefit evaluation is an obligation to consider less burdensome alternatives that will achieve the policy goals. The Bureau, however, has failed to consider alternatives that would address the Bureau's concerns without the need for a ban of class action waivers and the concomitant harm to consumers and society. By creating an outright ban on class action waivers, the Bureau failed to consider circumstances where class actions are not an effective or necessary mechanism to protect consumers from conduct that potentially presents a risk of harm to consumers.

The Associations urge the Bureau to consider an alternative that would permit the enforcement of class action waivers in three instances:

- The entity has reported the issue to the supervisory arm of the Bureau or appropriate government agency; or

- The Bureau has an ongoing investigation proceeding against the entity; or

- In response to a Bureau or other government agency action (e.g., the issuance of guidance) concerning a new interpretation or law the entity has within a defined period (e.g. 90 days), identified the issue and reported it to the appropriate agency.

The limited exception recognizes those situations where relief will be obtained for large number of consumers without the need for litigation and its related costs and burdens to society. Indeed, the Bureau has already noted the efficacy of such relief in its Bulletin on Responsible Business Conduct which requires financial institutions to self-monitor, self-report, and remediate – "even when the party believes that it may have identified a potential rather than an actual violation."[59] Thus, the Bureau expects the institutions it regulates to report and remediate not just

[58] *See* Associations' July 13, 2015 comment letter, pp. 12-13.

[59] Bulletin, *supra* note 49 at 4.

actual, but also potential, violations. Of course, as now, the Bureau would follow up on any reported issue with enforcement or supervisory action, if doing so is appropriate. Moreover, if an entity fails to take appropriate remediation, it will be subject to enforcement powers of the Bureau or other government agency. Thus, the exception allows an entity to give its customers complete relief as quickly as possible through existing supervisory and reporting mechanisms – efforts that are frustrated by class actions which overlap or follow after regulatory oversight.

A court, not the Bureau or other enforcement agency, would determine whether one of the three the conditions precedent had been satisfied and therefore, enables enforcement of the class action waiver in a particular class action suit. Thus, the Bureau or other government agency would not have to determine whether a particular class action may proceed.

This alternative solution not only requires no additional Bureau resources, it is better for consumer protection and better for society than class actions, because it creates a process and incentive to identify and resolve issues quickly and completely, without the additional and inefficient "transaction" costs associated with class action suits.

Consumers and society benefit, because in the three limited circumstances where the class action waiver would be enforceable, the issue resolution is not burdened by the additional transaction costs associated with class action litigation, as discussed above, and thus may put more money in consumers' pockets. Resolution would be entirely cost-based, with no money siphoned off to an unrelated party in settlements that tend to focus on paying transaction costs rather than consumer redress. Compare this outcome to class actions where the defendant is incented to attempt to pay the least amount acceptable to the plaintiff's counsel and the Court. Moreover, consumers may further benefit from self-reporting, because, as noted, the Bureau encourages institutions to remediate even "when the party believes that it may have identified a *potential* rather than an actual violation." (Emphasis added.) Consumers not only get more relief, they get it sooner. They receive money and other relief in weeks and months, rather than in years, as the Bureau found to be the case in class actions.

Consumers and society also benefit, because the lower costs for the financial service providers will be reflected in pressure on prices, services, and features for financial products, as discussed earlier. They also benefit from the reduced costs associated with less burdened federal and state court dockets and faster administration of justice.

The benefits of the exemptions are further amplified because the exemptions provide a powerful incentive for financial institutions to self-report and remediate. Institutions avoid the significant costs of class action suits, the adverse publicity, and the negative supervisory consequences of a regulator discovering the issue before they self-report, including the consequences described in the Bureau's Bulletin 2013-06.

Allowing class action waivers in the three limited circumstances not only makes more money available to remediate consumer complaints and reduces society's costs, it squarely addresses the Bureau's justifications for banning class action waivers: matters involving small amounts are addressed, consumers unaware of harm receive compensation, and responsible corporate behavior is encouraged.[60] Moreover, because the self-reporting entity knows that the Bureau may follow up with an enforcement action, it has an incentive to "implement measure[s] designed to prevent the violations from recurring, and, when appropriate, effectuat[e] changes in the party's future conduct for the protection and/or benefit of consumers," as the Bureau has indicated it expects institutions to do if they discover a violation.[61]

We also believe that the announcement of a new regulatory expectation or interpretation of law – effected by the issuance of guidance or an enforcement action – should be followed by a period during which all institutions may enforce a class action waiver with regard to that practice. Financial service providers – like everyone – are entitled to advance notice of what is considered an illegal practice, especially with regard to long-standing practices that have not been criticized previously. Fairness dictates that institutions be afforded reasonable time to adjust to new supervisory interpretations or expectations.

This approach of providing incentives to self-identify, report, and resolve is consistent with the Bureau's mission to protect consumers – and also consistent with the Bureau's repeated claims that it wishes to incentivize and reward good actors. In addition, it addresses the concerns the Bureau has cited as its justification for proposing an outright ban of class action waivers, a drastic course of action that will harm consumers and society. For these reasons, the Bureau should allow class action waivers in the limited circumstances described above.

G. The Bureau should also allow the enforcement of class action waivers where consumer protection statutes provide greater incentives for plaintiffs to pursue individual actions.

Most federal consumer protections statutes, and many state statutes as well, incentivize consumers to pursue individual actions rather than class actions, because they provide substantial statutory damages to prevailing plaintiffs and also enable them to recover their reasonable attorneys' fees, while placing a cap on the amount recoverable through class actions. In such circumstances, the proposed ban on class action waivers is unnecessary because a class action is not needed to protect consumers with small claims. Therefore, the Bureau should create an exception to the proposed rule where consumers can fare better by bringing individual actions under consumer protection statutes rather than class actions.

For example, several courts have held that class litigation is not the superior means of adjudication in Fair Debt Collection Practices Act cases where the potential recovery in individual actions is significantly greater than the recovery that may be obtained in a class action.

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60 Because the self-reporting entity knows that the Bureau may follow up with an enforcement action, it has an incentive to "implement[s] measure designed to prevent the violations from recurring, and, when appropriate, effectuat[e] changes in the party's future conduct for the protection and/or benefit of consumers," as the Bureau has indicated it expects institutions to do if they discover a violation. Bulletin, *supra* note 49 at 4.

61 *Id.*

For example, in *Leyse v. Corporate Collection Services*, No. 03 Civ. 8491(DAB), 2006 WL 2708451 (S.D.N.Y. Sept. 18, 2006), the court held that a class action was not the superior method of adjudication because of the *de minimis* recovery for class members, explaining that:

> Were putative class members to bring suit against CCS individually, statutory damages could amount to $1,000 per person. 15 U.S.C. § 1692k(a). But in a class action, each putative class member could only recover their proportion of "the lesser of $500,000 or 1 per centum of the net worth of the debt collector." 15 U.S.C. § 1692k(2)(B). Leyse and CCS agree that one percent of CCS' net worth is approximately $5,600 …. If $5,600 were divided evenly among forty consumers …, each putative class member could receive only up to $140, an amount significantly lower than what they could recover were they to bring suit individually. Furthermore, were Plaintiff's estimate of 11,000 consumers applicable to the putative class, each class member would be able to recover only fifty-one cents.

Id. at *9 n. 5.[62]

Data concerning actions under the Truth in Lending Act (TILA), 15 U.S.C. § 1640(a), is also instructive. TILA provides a prevailing plaintiff in an individual suit with minimum statutory damages between $500 and $5,000 and also allows the prevailing plaintiff to recover reasonable attorneys' fees, while capping statutory damages in a class action at $1 million or 1% of the net worth of the creditor. As the Associations pointed out in their June 22, 2012 comment letter, data from the years 2002-2011 show that 93% to 98% of all TILA claims brought in the federal courts were brought as individual actions, rather than class actions, even though TILA expressly permits class actions to be brought:

Year	**TILA Individual Actions**	**TILA Class Actions**
2002	539 (94% of total)	37 (6% of total)
2003	474 (93% of total)	39 (7% of total)
2004	554 (97% of total)	20 (3% of total)
2005	473 (97% of total)	19 (3% of total)

[62] *See also Gradisher v. Check Enforcement Unit, Inc.*, 209 F.R.D. 392, 394 (W.D. Mich. 2002) (ordering decertification where the recovery per class member was $0.06); *Sonmore v. Checkrite Recovery Services, Inc.*, 206 F.R.D. 257, 260-61 (D. Minn. 2001) (finding that the interest of class members in individually controlling the prosecution of their claims prevailed where class members were eligible for a maximum pro rata recovery of merely $25); *Jones v. CBE Group, Inc.*, 215 F.R.D. 558 (D. Minn. 2002) (holding that class action was not the superior means of resolving the dispute because the potential recovery for class members was, at most, *de minimis*).

2006	671 (98% of total)	17 (2% of total)
2007	665 (95% of total)	40 (5% of total)
2008	733 (94% of total)	51 (6% of total)
2009	1,320 (97% of total)	40 (3% of total)
2010	928 (98% of total)	17 (2% of total)
2011	539 (98% of total)	15 (2% of total)

Source: LexisNexis CourtLink® database.

These statistics and the case law strongly suggest that consumers benefit by bringing individual actions under statutes that provide a framework for damages because they typically obtain better results under these statutes on an individual basis. Moreover, because such statutes provide significant statutory damages to individuals and permit a successful plaintiff to recover his or her attorneys' fees and costs, there is an incentive for an attorney to represent the plaintiff in an individual action even in small dollar cases. This is further evidence that the proposed rule's ban on class action waivers is overbroad, since consumers in TILA, FDCPA, and similar consumer protection statutes are more likely to obtain more substantial recoveries in individual actions rather than via class actions. There is no reason to subject companies to the substantial costs and risks inherent in defending class action lawsuits under these circumstances, as the Bureau's concerns have been adequately addressed through the statutory framework.

H. The Bureau could have considered other alternatives without banning class action waivers that would have addressed its concerns.

The Bureau could have considered other steps, such as standards for arbitration agreements that would have addressed the concerns that led it to conclude a class action waiver ban was necessary. For example, to address its concern that people are reluctant to spend money and time to dispute small dollar complaints, it might require that arbitration be free and convenient for claims involving amounts less than a specific threshold. The Bureau should convene focus groups to determine the features that would best respond to any consumer hesitation in resolving small dollar complaints.

Summary.

The proposed rule does not benefit society or consumers. Both lose because, as taxpayers, consumers will have to pay for additional resources needed by courts to accommodate the permanent influx of 6,042 additional class actions every five years. They lose because the cost of defending and settling cases – estimated to be between $2.62 billion to $5.23 every five years (100 additional lawsuits each month) – will be passed along to consumers in whole or in part in the form of higher prices or reduced services.[63] Finally, they lose because, in exchange for waiting years to recover an average of $32.35, they lose all of the benefits of arbitration – benefits that the Bureau itself touts to its own employees[64] and expressly acknowledges in the proposed rule.

These unrecognized *social costs* do not serve the public interest or protect consumers. It is not in the public interest to have a judicial system that is overburdened with unproductive class actions that return little or nothing to consumers but generate billions of dollars for their lawyers. Equally, consumers are not protected if they pay more for financial services and lose the convenience, low-cost, and efficiency of arbitration, especially for "non-classable" claims that class actions cannot address.

Moreover, banning class action waivers is not necessary to address concerns related to resolving small dollar claims and harms about which people will be unaware. Nor is it necessary to regulate or modify corporate behavior. These matters are addressed through a variety of other means, including internal corporate compliant processes, the complaint portals of the Bureau and other government agencies, public opinion and social media, and through the tools for remedial action available to dozens of government agencies, including the Bureau, which have aggressively used their enforcement authority.

The Bureau failed to consider alternatives, as the Dodd-Frank Act requires, that would address the need for a ban of class action waivers. The Bureau should, for example, allow the enforcement of class action waivers for matters that the entity has identified and resolved prior to a class action being filed. It should also allow enforcement of class action waivers where consumer protection statutes provide greater relief for plaintiffs who pursue individual actions rather than class actions.

III. THE PROPOSED RULE IS NOT CONSISTENT WITH THE STUDY AND THEREFORE SHOULD BE WITHDRAWN

As discussed above, under the Dodd-Frank Act, the proposed rule must be consistent with the Bureau's Study. In their July 15, 2015, comment letter, the Associations demonstrated that the data in the Study would not support any ban on class action waivers. In particular, the Association's letter showed that the data in the Bureau's Study strongly support the conclusion that arbitration is more beneficial to consumers because it is faster, less expensive, and more effective than class action litigation, and consumers are far more likely to obtain a decision on the merits and receive more meaningful relief. Importantly, in the commentary to the proposed rule, the Bureau acknowledges and confirms the data on which the Associations based their

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63 The Bureau "believes that most providers would pass through at least portions of some of the costs [resulting from the proposed rule] … to consumers. This pass-through can take multiple forms, such as higher prices to consumers or reduced quality of the products or services they provide to consumers." (Proposed Rule *supr*a note 4, at 32911). Higher prices could also reduce access to credit.

64 *See supra* note 7.

comments, even while it strains to make the case that class action litigation is better for consumers than arbitration. The following comparisons of the Associations' July 15, 2015 letter with the proposed rule show that the data on which the Associations' letter was based are undisputed. **By validating the data on which the Associations based their arguments, the proposed rule strengthens the conclusion that the proposed ban on class action waivers is inconsistent with the Study.**

A. 87% of Class Actions Produce No Benefits to Putative Class Members.

- Associations: In 87% of the 562 class actions the Bureau studied, the putative class members received no benefits whatsoever because they were settled individually or withdrawn by the plaintiff or had reached no result while the Study was ongoing.[65]

- Proposed Rule: 61.1% of the class actions studied by the Bureau resulted in no relief at all to the putative class members: 24.4% involved a "non-class settlement," while 36.7% involved a "potential non-class settlement." 12.3% of the class actions resulted in court-approved class settlements. The remainder of the class actions reached no result during the Study.[66]

B. Consumers in Arbitration Recover 166 Times More than Putative Class Members.

- Associations: In the 13% of the class actions that settled, cash payments to "at least 34 million consumers" during the period studied were "at least $1.1 billion. "This means that the average class member's recovery was a mere $32.35.[67] By contrast, in arbitrations where consumers obtained relief on affirmative claims, the consumer's average recovery was $5,389 (166 times as much as the average putative class member's recovery).[68]

- Proposed Rule: On average, putative class members in settled class actions received "approximately $32 per class member."[69] "The Study also showed that those

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65 Associations' letter, p. 3; Study, § 1, pp. 13-14; § 6, p. 37.

66 Proposed Rule *supra* note 4, at 32847, 32908 n. 604

67 Associations' letter, p. 15. $1.1 billion divided by 34 million equals $32.35 per class member. In the Study, the Bureau did not do the simple long division. But the Associations did in their comment letter, and in the proposed rule the Bureau acknowledges that the number in fact is "approximately $32." (Proposed rule, 81 FR 32849 n. 305).

68 Study, § 5, pp. 13, 41. Consumers were also awarded attorneys' fees in 14.4% of the disputes resolved by arbitrators; the largest award of consumer attorneys' fees was $37,275. *Id.* § 5, p. 79.

69 Proposed Rule *supra* note 4, at 32849 n. 305.

consumers who do prevail in arbitration may obtain substantial individual awards – the average recovery … was nearly $5,400."[70]

C. The Claims Rate in Class Actions Is Abysmal.

- Associations: In the class settlements that required the putative class members to submit a claim form, the weighted average claims rate was only 4%, meaning that 96% of the potentially eligible putative class members failed to obtain any benefits because they did not submit claims.[71] In addition, even those minuscule claims rates fell by 90% if documentary proof was required to be submitted along with the claim.[72]

- Proposed Rule: In class actions where claim forms had to be submitted, "[t]he weighted average claims rate … was 4% …."[73]

D. Unlike Class Actions, Arbitrations Produce Merits Results.

- Associations: Consumers are more likely to obtain decisions on the merits in arbitration than in class action litigation. None of the 562 class actions studied by the Bureau went to trial.[74] By contrast, the Study found that of 341 cases resolved by an arbitrator, in-person hearings were held in 34% of the cases, and an arbitrator issued an award on the merits in about one-third of the cases.[75]

- Proposed Rule: "[I]n 32.2 percent" of the disputes filed during the first two years of the Study, "arbitrators resolved the dispute on the merits …. [W]hen there was a decision on the merits by an arbitrator, the average time to resolution was 179 days …. More than half the filings that reached a decision were resolved by 'desk arbitrations,' meaning that the proceedings were resolved solely on the basis of documents submitted by the parties. Approximately one-third … of proceedings were resolved by an in-person hearing, 8.2 percent by telephonic hearings …."[76]

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70 *Id.* at 32855.

71 Associations' letter, p. 8; Study, § 1, p. 17, § 8, p. 30.

72 *Id.*; Study, § 8, p. 31.

73 Proposed Rule *supra* note 4, at 32850.

74 Study, § 6, pp. 7, 38.

75 *Id.* § 5, pp. 11-12.

76 Proposed Rule, supra note 4, at 32845-32846.

E. Arbitration Is Up to 12 Times Faster than Class Action Litigation.

- Associations: Consumer arbitration is up to 12 times faster than consumer class action litigation. The data show that (i) the median desk arbitration (just documents) was resolved in 4 months; (ii) the median telephone arbitration was resolved in 5 months; (iii) the median in-person hearing was resolved in 7 months; and (iv) when the arbitration settled, the median arbitration proceeding lasted 2-5 months.[77] By contrast, the average class action settlement received final court approval in 1.89 years, and federal court multi-district litigation (MDL) class actions filed in 2010 closed in a median of 2.07 years.[78]

- Proposed Rule: AAA arbitrations "proceed relatively expeditiously."[79] Class cases in Multi-District Litigations closed in a median of 758 days.[80]

F. Arbitration Is Far Less Expensive than Litigation for Consumers.

- Associations: Consumers pay far less to arbitrate than to sue in court. Under the AAA's revised consumer rules, the consumer's share of administrator and arbitrator fees is capped at $200, with the company paying the remainder.[81] That is only one-half of the $400 it costs to file a new complaint in federal court.[82]

- Proposed Rule: "[T]he fee for filing a case in Federal court is $350 plus a $50 administrative fee – paid by the party filing suit …. In arbitration, under the AAA consumer fee schedule that took effect March 1, 2013, the consumer pays a $200 administrative fee, regardless of the amount of the claim."[83] "[T]he cost to consumers of this mechanism is modest."[84]

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77 Associations' letter, p. 7; Study, § 1, p. 13.

78 *Id.*; Study, § 6, pp. 9, 43.

79 Proposed Rule *supra* note 4, at 32847.

80 *Id.*

81 Associations' letter, pp. 7-8; Study, § 1, p. 13; § 4, pp. 10-11. Moreover, consumers are permitted to apply for a hardship waiver if they cannot pay these modest amounts, and many arbitration provisions offer to pay them for the consumer if requested or unconditionally. Study, § 2, pp. 58-59; § 5, pp. 12, 76-77.

82 Associations' letter, pp. 7-8; Study, § 4, p. 10.

83 Proposed Rule *supra* note 4, at 32844.

84 *Id.* at 32855.

Notably, the Bureau's findings also confirm the conclusions reached by the U.S. Chamber of Commerce's Institute for Legal Reform in a December 2013 empirical study of class actions, titled "Do Class Actions Benefit Class Members?"[85] The Chamber analyzed 148 putative consumer and employee class action lawsuits filed in or removed to federal court in 2009. Consistent with the Bureau's Study and the proposed rule, the Chamber's report found, *inter alia*, the following:

- Not one of the class actions studied ended in a final judgment on the merits for the plaintiffs. And none of the class actions went to trial, either before a judge or a jury.

- The vast majority of cases produced no benefits to most members of the putative class – even though in a number of those cases the lawyers who sought to represent the class often enriched themselves in the process.

- Over one-third (35%) of the class actions that were resolved were dismissed voluntarily by the plaintiff. Many of those cases settled on an individual basis, meaning a payout to the individual named plaintiff and the lawyers who brought the suit, even though the class members received nothing.

- Just under one-third (31%) of the class actions that were resolved were dismissed by a court on the merits, meaning that class members received nothing.

- For those cases that settled, there was often little or no benefit for class members. Moreover, few class members ever saw those paltry benefits, particularly in consumer class actions.

Professor Shepard's February 2016 study on no-injury class actions, discussed earlier in this letter, is also illuminating.[86] "No-injury class actions" are those in which "(1) the plaintiffs suffered no actual or imminent concrete harm giving rise to an injury-in-fact; (2) the only harm was a technical statutory violation; (3) any economic loss was negligible or infinitesimal; or (4) the sought recovery was typically unrelated to compensating plaintiffs for economic or other harm."[87] The data sample consisted of 432 cases resolved between 2005 and 2015 in federal and state courts located in 33 states. In the data, 155 cases involved claims brought under state statutes and 296 involved claims brought under a federal statute. The most common federal statutes giving rise to claims in the data were the Fair Debt Collection Practices Act, the Telephone Consumer Protection Act, the Fair Credit Reporting Act, and the Electronic Funds Transfer Act. Only 2.5% of the 432 cases studied by Professor Shepherd went to trial. The remainder were settled, for a total of about $4 billion (average $9.37 million). Of that, 37.9%

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85 A link to the report is available at http://www.instituteforlegalreform.com/resource/study-class-actions-benefit-lawyers-not-consumers/.

86 *See supra* page 10.

87 Shepherd, *supra* note 26 at 1.

went to class action lawyers as fees. Of the remaining 63.1% – over $2.4 billion, potentially available to class members – only 15% of that sum ever went to actual class members. The result is that only 9% (at most, depending on the claims rate) of the available funds went to the putative class members "with the rest going to lawyers or unrelated groups" such as *cy pres* recipients, failing to "achieve the compensatory goals of class actions."[88] Importantly, Professor Shepherd concludes –

> [R]egardless of the harm imposed on consumers by the business practice, many no-injury class actions produce little compensation for class members. Individual compensation all too often amounts to [no] more than a few dollars or a coupon. Moreover, few eligible class members—less than one percent in many cases—actually pursue claims to receive the modest compensation. In these cases, the true beneficiaries of no-injury class actions are the lawyers. Thus, the costs of no-injury class actions—increased business litigation costs, higher consumer prices, and fewer product innovations—are established by data and economic theory. In contrast, the benefits of many marginal no-injury cases are few or nonexistent. As a result, much of the no-injury class action litigation harms consumers rather than helping them as intended.[89]

The close correlation of the Shepherd data, the Chamber's data and the Study's data reveals an empirical consensus that class actions benefit plaintiffs' lawyers, but not the consumers. These studies confirm that in class actions: the vast majority of consumers receive no benefit whatsoever from being a class member; any economic benefit to individual class members in a class settlement is insignificant; and the merits of the dispute are not reviewed or resolved. By contrast, the Study's data (affirmed in the proposed rule) show that consumers can receive significant economic benefits in arbitration, they receive those benefits in months rather than years at little or no expense, and their disputes are resolved on the merits.

G. The Arbitration Process Is Fair to Consumers.

In their prior submissions, the Associations also demonstrated that arbitration agreements on the whole treat consumers fairly and that the AAA requires companies to adhere strictly to its Consumer Due Process Protocol. In particular, the Associations observed that most arbitration agreements allow consumers to pursue their claims in small claims court, require the arbitrator to apply applicable substantive law, set the arbitration hearing at a location reasonably convenient for the consumer, and provide that the remedies available at law remain available in arbitration.[90] The proposed rule concurs with these points:

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88 *Id. at* 2.

89 *Id.* at 23-24.

90 Associations' June 22, 2012 comment letter, p. 4.

- "[M]ost of the arbitration agreements contained a small claims court 'carve-out,' permitting either the consumer or both parties to file suit in small claims court."[91]

- A "number of arbitration provisions … allowed consumers to 'opt out' or otherwise reject an arbitration agreement.[92]

- "Most arbitration agreements reviewed in the Study contained provisions that had the effect of capping consumers' up front arbitration costs at or below the AAA's maximum consumer fee thresholds."[93]

- "[M]ost … arbitration agreements contained provisions requiring or permitting hearings to take place in locations close to the consumer's place of residence."[94]

- "[M]ost of the arbitration agreements the Bureau studied contained disclosures describing the differences between arbitration and litigation in court. Most agreements disclosed expressly that the consumer would not have a right to a jury trial, and most disclosed expressly that the consumer could not be a party to a class action in court …. The Study found that this language was often capitalized or in boldfaced type."[95]

- "Under the AAA's Consumer Rules, '[t]he arbitrator may grant any remedy, relief or outcome that the parties could have received in court, including awards of attorney's fees and costs, in accordance with the law(s) that applies to the case.'"[96]

- "[I]n most courts, individuals can either represent themselves or hire a lawyer as their representative. In arbitration, the rules are more flexible …. For example, the AAA Consumer Rules permit a party to be represented 'by counsel or other authorized representative ….'"[97]

- "[I]f a case in court does not settle before trial or get resolved on a dispositive motion, it will proceed to trial in the court …. [I]f an arbitration filing does not settle, the

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91 Proposed Rule *supra* note 4, at 32842.

92 *Id.*

93 *Id.*

94 *Id.*

95 *Id*.

96 *Id.* at 32844.

97 *Id.*

> arbitrator can resolve the parties' dispute based on the parties' submission of documents alone, by a telephone hearing, or by an in-person hearing."[98]

Thus, the proposed rule's prohibition on class action waivers in consumer arbitration agreements is inconsistent with the Study, because there is abundant data in the Study (affirmed in the proposed rule itself) that contradict the need for such a prohibition and demonstrate that arbitration is superior to class action litigation for the resolution of consumer financial services disputes. Inasmuch as the proposed rule is not "consistent with the Study," it exceeds the Bureau's authority under Section 1028 of the Dodd-Frank Act and should not be made final.[99]

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98 *Id.* Notably, in a prior study, the Bureau's own consultant concluded that arbitration benefits consumers more than litigation. *See* Christopher R. Drahozal, et al., "An Empirical Study of AAA Consumer Arbitration," 25 Ohio St. J. on Disp. Resol. 843 (2010). This article discusses the results of the March 2009 study of AAA consumer arbitrations undertaken by the Searle Civil Justice Institute, Northwestern University School of Law. The study was based on a review of 301 AAA consumer arbitrations (240 brought by consumers, 61 brought by businesses) that were closed by award between April and December 2007. It reached the following conclusions: (a) the upfront cost of arbitration for consumer claimants was quite low; (b) AAA consumer arbitration is expeditious (an average of 6.9 months); (c) consumers won some relief in 53.3% of the cases filed and recovered an average of $19,255 (52.1% of the amount claimed); (d) no statistically significant repeat-player effect was identified; and (e) arbitrators awarded attorneys' fees to prevailing consumers in 63.1% of cases in which the consumer sought such an award and the average attorneys' fee award was $14,574.

99 On August 17, 2016, The Pew Charitable Trusts released an issue brief, "Consumers Want the Right to Resolve Bank Disputes in Court," in which it urges the Bureau to "expeditiously finalize" its proposed arbitration rule. (*See* http://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2016/08/consumers-want-the-right-to-resolve-bank-disputes-in-court). Pew found, *inter alia*, that 95 percent of consumers want to be able to have a dispute with their banks heard in court and almost 9 in 10 consumers want to be able to participate in a group lawsuit. The findings were based in part on a telephone survey of 1,008 adults on their attitudes toward arbitration and dispute resolution alternatives conducted in November 2015. Pew states that the Bureau's arbitration Study and Pew's poll "make clear that, in most cases, consumers would not take individual legal actions over a dispute but want the right to join class actions to hold companies accountable." Pew ignores, however, that the Bureau's Study does not support the proposed rule. As discussed, the data in the Study shows that individual arbitration is far more beneficial for consumers than class action litigation. Had those data been part of Pew's survey questions, they would have gotten a completely different result. For example, if consumers had been asked, "If you had a dispute with your bank, and could choose between (A) going to arbitration and, if you won, recovering an average of $5,400 a few months after the arbitration started, or (B) being part of a class action in court in which 87% of the class members would never recover anything, while the remaining 13% would recover an average of $32 as part of a class settlement after waiting for two or more years," Pew would have found that

IV. The Study Was Incomplete on Several Key Issues that Would Have Further Demonstrated that the Proposed Rule Is Not in the Public Interest or Needed for the Protection of Consumers

In several other aspects, the Study also does not support the proposed *de facto* elimination of consumer financial services arbitration because it did not study several key issues that would have further shown that the proposed rule is not in the public interest or needed for the protection of consumers.

A. The Bureau neglected to analyze the effect of its own administrative and enforcement activities as recommended.[100]

As discussed above in Section II, the Bureau has certainly been more successful than class actions in addressing small-dollar disputes and harm about which people may be unaware and in deterring behavior. **Yet, notably, the Study excluded the bulk of the Bureau's own enforcement and supervisory actions from January 1, 2013, to date.**

The Bureau's statistics, noted earlier, on the billions of dollars paid to millions of consumers as a result of the Bureau's enforcement actions demonstrate both the power of the Bureau's enforcement authority and its use of such authority to address violations, particularly with regard to small dollar claims and harm about which people are unaware, the primary targets justifying the proposed class action waiver ban. Moreover, the Board itself claims its "own creation in 2010 may have increased incentives for some providers to increase compliance investments, although it did not begin enforcement actions until 2012."[101] Yet, remarkably, despite the Bureau's claims regarding its own significant impact on the issues it cites to justify the class action waiver ban, the Bureau failed to consider them in the proposed rule.

The Study should have accounted for all of the Bureau's enforcement activities to allow a proper comparison with class actions. Accordingly, the proposed rule should be withdrawn because it was not based on a complete record of the Bureau's own robust enforcement activities, and does not take the Bureau's future enforcement activities into account.

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consumers prefer arbitration to class action litigation and might not be urging the Bureau to finalize its proposed arbitration rule. In addition, as noted, the Bureau expects that consumers will pay for financial institutions' increased litigation costs in the form of higher fees and fewer services. The survey questions did not ask how much people are willing to pay to reserve their right to be part of a class action in which the average award is about $32. Moreover, like the Bureau in conducting its Study (see part IV.B of this letter), Pew failed to survey consumers who have actually been through arbitration.

100 *See supra* pages 16-18.

101 Proposed Rule *supra* note 4, at 32906.

B. The Bureau did not study consumer satisfaction with arbitration as recommended.

In their prior submissions, the Associations urged the Bureau to study *actual* consumer satisfaction with the arbitration process compared to actual consumer satisfaction with the class action process. The Bureau's 2013 telephone survey of 1007 consumers merely purported to explore consumers' "default assumptions" concerning arbitration and intentionally excluded consumers who had actually participated in an arbitration.[102] The Bureau's intentional refusal to study consumers' experience with arbitration is perplexing – and militates against its recommendations – since both logic and common sense dictate that understanding consumer satisfaction with arbitration is essential to a complete understanding of whether consumer arbitration is in the public interest.

Prior studies, available to the Bureau, overwhelmingly conclude that consumers prefer arbitration to litigation. As the Study acknowledges,[103] there is precedent for studying this issue. For example, in 2005 Harris Interactive conducted an online poll of 609 individuals who had participated in arbitration that reached a decision.[104] The poll found, *inter alia*, that –

(i) arbitration was widely seen as faster (74%), simpler (63%) and cheaper (51%) than going to court;

(ii) two-thirds (66%) of the participants said they would be likely to use arbitration again with nearly half (48%) saying they were extremely likely to do so. Even among those who lost, a third said they were at least somewhat likely to use arbitration again;

(iii) most participants were very satisfied with the arbitrators' performance, the confidentiality process and its length; and

(iv) although winners found the process and outcome very fair and losers found the outcome much less fair, 40% of those who lost were moderately to highly satisfied with the fairness of the process, and 21% were moderately to highly satisfied with the outcome.

As discussed in Section II, there are also important intangibles associated with arbitration that are not reflected in the Study, because the Bureau chose not to elicit or analyze actual consumer experience with arbitration or litigation. For example, as discussed earlier, arbitration offers conveniences, comfort, expediency, and efficiencies that resort to resolution via courts lacks.

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102 Study, § 3, p. 4 ("[w]e opted not to explore consumer satisfaction with arbitration (or litigation proceedings").

103 *Id.* § 3. p. 5 n. 5.

104 *See* Harris Interactive, *Survey of Arbitration Participant*s (April 2005), available at http://www.adrforum.com/rcontrol/documents/ResearchStudiesAndStatistics/2005HarrisPoll.pdf.

The Associations submit that, notwithstanding the Bureau's alleged difficulty in finding consumers who have personal experience with both arbitration and litigation,[105] the opinions of consumers who have experienced the arbitration process are at least as valuable (and probably more so) as the opinions of the consumers who were questioned in the Bureau's telephone survey but who had not actually participated in an arbitration. The Associations believe that the exclusion of individuals who had actual experience with arbitration diminished the value and relevance of the telephone survey specifically as well as the Study as a whole. The absence of data on consumer satisfaction with arbitration skewed the Study's conclusions. Therefore, the premise of the proposed rule that class actions are superior to arbitration for consumers is based upon incomplete data, undermining the admissibility of the Bureau's proposal.[106] For these reasons, it should be withdrawn.

C. The Bureau did not study the impact on consumers and society if companies abandon arbitration as recommended.

As discussed above in Section II, it is anticipated that most companies will abandon arbitration altogether if class action waivers are prohibited based on a cost-benefit analysis. Despite the negative impact of the result on consumers and the public interest, the Bureau failed to consider the impact on consumers if there is no arbitration option, especially for non-classable claims. Nor did it study or investigate how modifications to arbitration agreements and better consumer education might make arbitration more attractive for small-dollar claims, which would address the Bureau's contention that class actions are necessary to address such claims.

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105 Study, § 3 p. 5.

106 The Bureau also failed to study how the proposed rule will impact the burgeoning use of on-line dispute resolution services. For example, in comments submitted to the Bureau when it initially proposed the Study, Modria, one of the leading companies offering online arbitration and dispute resolution services, stated that it handles more than 60 million disputes a year. *See* http://www.regulations.gov/#! documentDetail;D=CFPB-2012-0017-0019. Even if only a fraction of the disputes handled by Modria involve consumer financial services companies, it is obvious that the universe of consumer disputes being addressed outside the courtroom is much larger and diverse than just the AAA database examined in the Study. Modria is only one of many online dispute resolution services. In their own initial comments on the Study, the Associations asked the Bureau to study the extent to which consumers resolve their disputes with businesses through online dispute resolution in order to place more traditional consumer arbitration services (such as the AAA) in the proper context. *See* http://www.regulations.gov/#!documentDetail;D=CFPB-2012-0017-0030. However, the Bureau did not do so. Before publishing the proposed rule, the Bureau should have studied whether and how such a regulation would impact this ever-growing national and international market for resolving consumer disputes online.

D. The Bureau did not study the cost to consumers and society of the perpetual addition of class actions.

As discussed above in Section II, the Bureau estimates that the total cost for companies to defend the expected additional federal *and* state court class actions combined will lie somewhere between $2.62 billion and $5.23 billion every five years and believes consumers would pay for at least portions of these costs through higher prices or reduced quality or services."[107] The Bureau concedes, as discussed earlier, however, that it is not able to estimate how much of that additional cost will be passed along to consumers.[108] The Bureau asserts that anywhere from 0% to 100%, and, in theory, even more than 100%, of the costs could be passed through to consumers.[109]

In the Study, the Bureau analyzed the effect on prices of several large credit card issuers agreeing to drop their arbitration agreements for a period of time as part of a class settlement. Mysteriously, it did not find a "statistically significant" effect on the prices those issuers would charge subsequent to the contract changes. First, the litigation costs may not be only reflected in the price, but in the features and services, as the Bureau acknowledges.[110] Second, the Bureau acknowledges in the proposed rule that this may not be an indicator of the pass-through rate that will occur with the predicted increase in class actions.[111] The Bureau should have analyzed this area more closely since the proposed rule could have a significant negative financial impact on consumers – the very individuals it claims to be protecting by the proposed rule.[112]

E. The Bureau did not investigate whether class actions are necessary as a deterrent given the impact of modern social media and other communication channels.

As discussed earlier, financial service providers have enormous incentive to ensure that their customers are satisfied and any disputes resolved fairly. Any frustration or dissatisfaction is quickly, immediately, and lastingly circulated around the globe. This phenomenon, coupled with the Bureau's and other government agencies' enforcement powers, obviates any need for class action suit as deterrent to questionable practices or legal violations. Yet, the Bureau ignored its impact on the need for class actions.

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[107] Proposed Rule *supra* note 4, at 32911.

[108] The costs "cannot be reliably predicted, especially given the multiple markets affected." *Id.*

[109] *Id.* & n. 618.

[110] *Id.*, 32911.

[111] *Id.*, 32911-32912.

[112] Indeed, basic economic theory argues that if companies' litigation costs increase, there will be a corresponding need to increase revenue or reduce value. This means consumers pay more or get less. Many courts and commentators have so concluded. *See supra* note 22.

F. Though the Bureau found consumers unaware of arbitration, it applied none of its education funds or other resources on educating consumers about arbitration as a dispute resolution option.

The proposed rule's class action waiver prohibition is also based on the premise that "consumers generally lack awareness regarding the effects of arbitration agreements."[113] In particular, the Study, based upon the Bureau's telephone survey of consumers, found that over 75% of consumers surveyed said they do not know whether their credit card agreement contained an arbitration clause. Notably, the Bureau acknowledges, however, that "[i]n principle, effective disclosures coupled with consumer education could make consumers more cognizant in selecting a financial product or service, of the existence and consequences of an arbitration provision in the standard form contract and, *ex post*, could make consumers who have a dispute with the provider cognizant of the option of pursuing the dispute in arbitration."[114] Yet this is an acknowledged remedy that the Bureau fails to recommend. The Bureau has, it should be noted, gone to great lengths to educate *its own* employees about the use of alternative dispute resolution to resolve workplace disputes. *See* GAO Report, *supra* note 7, at 49 ("CFPB makes alternative dispute resolution available through its EEO program as well as through its negotiated and administrative grievance policies, and on an ad hoc basis to address any workplace dispute. CFPB has publicized information about alternative dispute resolution, such as through its wiki[[115]] on the bureau's intranet and newsletters sent to managers and employees. In addition, in 2015, the Office of Civil Rights created an in-house training module on Alternative Dispute Resolution to supplement the EEO training managers and supervisors receive and to provide to nonsupervisory employees.").

V. COMMENTS ON SPECIFIC PARTS OF THE PROPOSED RULE THAT REQUIRE THE BUREAU'S CLARIFICATION

For the reasons outlined above, the Associations contend that the proposed rule should not be made final. In addition, the proposed rule includes a number of other issues that must be addressed.

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113 Proposed Rule *supra* note 4, at 32843. The Bureau based that conclusion on a telephone survey concerning consumer awareness of dispute resolution provisions in their credit card agreements, that it conducted as part of the Study. However, that survey has been justly criticized on the ground that it "lacked an adequate foundation, and thereby yielded unreliable data." Consumer Bankers Association, Written Statement of Dong Hong, p. 7 (May 18, 2016 hearing before the House of Representatives, Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit).

114 Proposed Rule *supra* note 4, at 32920.

115 A wiki is a website that provides collaborative modification of its content and structure directly from the web browser.

A. Application of the Proposed Rule to Life Insurance Companies.

We recommend that the Bureau eliminate any reference to the business of insurance. The Bureau stated that "the proposal would apply to extensions of credit by providers of whole life insurance policies (NAICS 524113) to the extent that these companies are ECOA creditors and that activity is not the 'business of insurance' under the Dodd-Frank section 1002(15)(C)(i) and 1002(3) and arbitration agreements are used for such policy loans."[116] The Associations seek the deletion because the Dodd-Frank Act expressly excludes the "business of insurance" from the list of covered products subject to the Bureau's jurisdiction[117] and prohibits the Bureau from enforcing the Act's provisions against "any person regulated by a state insurance regulator."[118] In addition, the McCarran-Ferguson Act (MFA) provides that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance."[119] Therefore, even though the Federal Arbitration Act (FAA)[120] generally requires arbitration agreements to be enforced if they are contained in contracts involving interstate commerce, some courts have held that if state law regulates the use of arbitration agreements as part of the "business of insurance," the MFA "reverse-preempts" the FAA, with the result that the arbitration agreement cannot be used to resolve disputes arising under insurance contracts.[121]

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116 Proposed Rule *supra* note 4, at 32917. NAICS 524113 is the government industry code for "direct life insurance carriers."

117 *See* 12 U.S.C. §§ 5481(C)(1) and 5517(m) (2014). The term ''business of insurance'' means the writing of insurance or the reinsuring of risks by an insurer, including all acts necessary to such writing or reinsuring and the activities relating to the writing of insurance or the reinsuring of risks conducted by persons who act as, or are, officers, directors, agents, or employees of insurers or who are other persons authorized to act on behalf of such persons."

118 *Id.* § 5517(f)(1). The term ''person regulated by a State insurance regulator'' means any person that is engaged in the business of insurance and subject to regulation by any State insurance regulator, but only to the extent that such person acts in such capacity.

119 15 U.S.C. §§ 1101 *et seq.*

120 9 U.S.C. §§ 1 *et seq.*

121 *See, e.g., Standard Sec. Life Ins. Co. v. West*, 267 F.3d 821, 823 (8th Cir. 2001) (denying motion to compel arbitration under the FAA in a dispute over a football player's insurance policy where MO. REV. STAT. § 435.350 (1994) regulated the business of insurance); *Blue Ridge Emergency Physicians, P.A. v. Emergency Physicians Ins. Co.*, C.A. No. 00428, 2011 U.S. Dist. LEXIS 26616, at *5-6 (D.C. S.C. March 15, 2011) (holding that the MFA reverse-preempted the FAA in malpractice insurance action because S.C. CODE ANN. § 15-48-10 (1976) specifically regulates the business of insurance); *Cont'l Ins. Co. v. Equity Residential Props. Trust*, 565 S.E.2d 603, 605-06

Since both the Dodd-Frank Act and the MFA recognize, as a matter of federal law, that states are the principal regulators of the "business of insurance," the one-paragraph discussion in the proposed rule regarding its possible application to whole life insurance policies appears to be questionable at best. Indeed, that is the only reference to life insurance producers in the entire 377-page rule. Moreover, this brief, one-paragraph discussion appears to be totally hypothetical in nature with little, if any, practical application. The Bureau itself acknowledges that it is "unlikely that a significant number of such providers would be affected because a number of state laws restrict the use of arbitration agreements in insurance products and, in any event, it is possible that the loan feature of the whole life policy could be part of the "business of insurance" depending on the facts and applicable law."[122]

Although it appears that the Bureau is describing an extremely narrow and hyper-technical application of the proposed rule that may never occur, this reference to insurance companies in the proposed rule causes uncertainty. Our insurance companies are concerned that this may signal that the Bureau is seeking to extend its regulatory powers to insurance companies notwithstanding the express language of the Dodd-Frank Act and the MFA. Under the MFA, the Bureau could only supersede state laws governing the business of insurance if the Dodd-Frank Act were an Act of Congress that regulates the business of insurance, but that is not the case. The Dodd-Frank Act's only mention of insurance with respect to the Bureau is to place express *limitations* on the Bureau's authority over the business of insurance and activities regulated by a state insurance regulator. Therefore, Congress did not intend for the Dodd-Frank Act to invalidate, impair, or supersede state laws that regulate the business of insurance.[123] The strong limitations in the Dodd-Frank Act on the Bureau's authority under that statute should be respected. To the extent the Bureau encroaches on the business of insurance, it threatens the state-based insurance regulatory system and further complicates an already complicated analysis concerning the MFA's "reverse-preemption' of state laws purporting to prohibit the use of arbitration to resolve insurance disputes. Therefore, the Bureau should delete any reference to insurance companies.

B. Third-Party Beneficiary Rights in Existing Contract.

Many arbitration agreements create third-party beneficiary rights in persons or entities having some connection with the subject matter of the contract. For example, an agreement might provide, "'Us/We/Our' means Company, any purchaser, assignee or servicer of the contract, all of their parent companies, and all subsidiaries, affiliates, predecessors and successors, and all officers, directors and employees of any of the forgoing." The Bureau states,

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(Ga. Ct. App. 2002) (holding that arbitration clause within an insurance contract was unenforceable where GA. CODE. ANN. § 9-9-2(c)(3) regulated the business of insurance).

122 Proposed Rule *supra* note 4, at 32917.

123 *See* J. Sivon and A. Maarec, "The CFPB and the Business of Insurance: An Analysis of the Scope of the CFPB's Authority Over Insurance Sales" (Sept. 9. 2015).

> Under the proposed rule, however, the purchase of the contract after the compliance date would create a new contract subject to the rule since the purchaser will have acquired rights in the contract. Section 1040.4(a)(2)(iii) requires a provider that enters into a pre-dispute arbitration agreement that had existed previously as between other parties and does not contain the provision required by § 1040.4(a)(2)(i) or (ii), either to ensure the agreement is amended to contain the required provision or to provide a written notice to any consumer to whom the agreement applies. This could occur when, for example, Bank A is acquiring Bank B after the compliance date specified in § 1040.5(a), and Bank B had entered into pre-dispute arbitration agreements before the compliance date specified in § 1040.5(a). If, as part of the acquisition, Bank A enters into the pre-dispute arbitration agreements of Bank B, Bank A would be required either to ensure the account agreements were amended to contain the provision required by § 1040.4(a)(2)(i), the alternative permitted by § 1040.4(a)(2)(ii), or to provide the notice specified in § 1040.4(a)(2)(iii).[124]

However, in the situation posited by the Associations, the purchaser will have already *had rights* in the arbitration agreement before the compliance date, because the purchaser was a third-party beneficiary. Therefore, as to the purchaser it is not a "new" agreement. The Bureau should clarify that a party who had third-party beneficiary or other rights in an arbitration agreement prior to the compliance date may continue to enforce that agreement, and is not subject to the proposed rule, if that third-party beneficiary acquires rights in the contract containing the arbitration agreement after the compliance date.

C. Grandfathering of Pre-Compliance Date Products and Services Where "New" Product or Service Is Added After Compliance Date.

The Associations note that the Bureau has requested comments on whether providers need "additional clarification regarding the application of proposed § 1040.4(a)(1) in class actions for multiple products and services, only some of which are covered by proposed § 1040.3."[125] The proposed rule states that it applies to any pre-dispute arbitration agreement "entered into" after the compliance date (the 211th day after publication of the final rule in the Federal Register). The commentary on the proposed rule states that a provider does not "enter into" a pre-dispute arbitration agreement (*i.e.*, the proposed rule does not apply) where it modifies, amends, or implements (a) the terms of a product or service that is subject to a pre-dispute arbitration agreement that was entered into before the compliance date or (b) the terms of a pre-dispute arbitration agreement itself. However, the commentary further states that a provider does enter into a pre-dispute arbitration agreement (*i.e.*, the proposed rule does apply) where the modification, amendment, or implementation constitutes providing a new covered product or service.[126] The Bureau should clarify why the proposed rule would apply to a contract that was

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124 Proposed Rule *supra* note 4, at 32929.

125 *Id.* at 32926.

126 *Id*. at 32885.

entered into before the compliance date, simply because a new product or service was added to it. The contract is still the same contract, albeit modified.

Moreover, proposed section 1040.3 describes "products or services" that are covered by the proposed rule, but there is no further guidance as to what constitutes a "new" product or service that, according to the Bureau, would trigger application of the proposed rule (at least with respect to the "new" product or service) if added after the compliance date, or whether amending the terms of a pre-existing product or service could transform the product or service into a "new" one. This could open up numerous gray areas and create substantial confusion. The Associations appreciate the Bureau's statement that the proposed rule is intended to apply a "narrow" interpretation of "entered into" in connection with post-compliance date modifications and amendments to an earlier contract[127] and believe that guidance on what "new" means in this context will provide greater clarity.

In addition, the Bureau should clarify how the "new" product and services rule interacts with the Bureau's rule regarding multiple products and services. The proposed rule recognizes that a contract can cover multiple products, some covered by the proposed rule and some not covered. The proposed definition of "provider" states in relevant part, "A provider as defined in § 1040.2(c) that also engages in offering or providing products or services not covered by §1040.3 must comply with this part only for the products or services that it offers or provides that are covered by § 1040.3."[128] The proposed rule also specifies special disclosure requirements for multiple product situations:

> 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 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. This provision applies only to class action claims concerning the products or services covered by that Rule.[129]

The Associations interpret these rules as meaning that if the arbitration agreement in a contract for covered products or services is in existence before the compliance date, the arbitration agreement continues to be effective as to those products and services after the compliance date, even if the contract is amended after the compliance date to add a "new" covered product or service. If the arbitration agreement contained a class action waiver, the

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[127] Id. ("The Bureau believes that the phrase entered into an agreement as used in Dodd Frank section 1028 can be interpreted to permit application of a Bureau regulation issued under the provision to agreements modified or amended after the compliance date, in certain circumstances. However, for the purposes of this proposal, the Bureau is proposing to interpret the phrase more narrowly ….").

[128] Proposed Rule *supra* note 4, at 32926.

[129] *Id.*

waiver would continue to be enforceable if a class action were brought that involved the pre-compliance date product or service. The arbitration agreement would not apply to a class action involving the new product or service, and an appropriate disclosure would need to be made, but the addition of the new product or service would *not* subject the *entire* contract to the coverage of the proposed rule. The Bureau should confirm that this understanding is correct in any final rule since it is a scenario that is likely to occur in transactions by the Associations' members.

D. Notice Required by § 1040.4(a)(2).

The proposed rule provides that upon entering into an arbitration agreement after the effective date, "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.'"[130] The Associations' Members are concerned that the Bureau's suggested language might be twisted into an argument that the defendant company in a class action has waived its right to assert defenses to class certification. The Associations request that the Bureau obviate such arguments by clarifying that inclusion of the Bureau's language in an arbitration agreement does not cause or constitute a waiver of any defenses that the company may assert in a class action filed in court involving a covered product or service, including but not limited to defenses to class certification.

VI. CONCLUSION

The proposed rule should not be made final because it is not in the public interest, it does not and is not needed to protect consumers, and it is not consistent with the Study, all of which are prerequisites for adopting such a rule. Nor did the Bureau, as required, consider alternatives such as allowing enforcement of class action waivers for matters that the entity has identified and resolved prior to a class action being filed. Moreover, numerous important issues – including consumer satisfaction with arbitration, the impact on consumers if companies abandon arbitration, the cost to consumers of 6,042 additional class actions, alternative arbitration terms, and the impact of arbitration education – have yet to be studied.

Once again, we appreciate the opportunity to submit these comments to the Bureau. Thank you for your consideration.

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130 *Id.*

Respectfully,

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