PUBLICATION

CFPB Report Likely Precursor to Regulatory Limits on Mandatory Arbitration Provisions

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The Consumer Financial Protection Bureau (CFPB) released a study in March 2015 criticizing the use of mandatory, pre-dispute arbitration agreements in financial contracts with consumers. As expected, the CFPB found arbitration to be detrimental to consumers' interests when compared to litigation, particularly class action litigation. The study is widely perceived as a precursor to regulatory action that will substantially curtail or even eliminate the use of arbitration agreements in the consumer financial space.

The CFPB was established by Congress through the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. Through Dodd-Frank, Congress empowered the CFPB to review the use of pre-dispute arbitration agreements in consumer financial markets and restrict their use if deemed necessary. The CFPB conducted a study of the use of mandatory arbitration provisions in contracts for checking accounts, credit cards, prepaid cards, payday loans, private student loans and mobile wireless contracts.

A primary emphasis in the March 2015 report concerns the prohibition of class action lawsuits, a standard component in consumer arbitration provisions. The CFPB found that consumers recover substantially less in arbitration proceedings than in traditional litigation, particularly when compared to class action lawsuits. Moreover, consumers were found to be generally unaware of whether their financial services contracts contain arbitration provisions and often wrongly believe that they have the right to sue in court. The CFPB cites a host of additional concerns including the contention that there is no evidence that arbitration clauses lead to lower prices for consumers and that, contrary to traditional wisdom, arbitration is not cheaper and more efficient than litigation.

In the coming months, the CFPB will likely take action based on the report and could, for instance, bar class action bans or bar the use of pre-dispute arbitration agreements with consumers entirely. If the CFPB bans arbitration provisions, consumer arbitration will likely all but disappear in the financial markets space. Moreover, the CFPB's actions could influence other regulatory bodies, such as the Securities & Exchange Commission, to implement similar bans on mandatory arbitration provisions, thereby broadly impacting dispute resolution with consumers across the entire financial industry.

If such regulatory bans are put into place, the industry will face additional uncertainty as any ban will undoubtedly be challenged in court. The Federal Arbitration Act (FAA) provides that pre-dispute arbitration agreements involving interstate commerce – such as those used in the consumer financial industry – are valid and enforceable as written. Whether the CFPB can be delegated the power to unilaterally restrict the provisions of a U.S. law such as the FAA will be a substantial hurdle for the CFPB to overcome. While the outcome of any such litigation is uncertain, the limited powers of administrative agencies and the pro-arbitration policies adopted by the courts suggest that any CFPB action may be unenforceable without Congressional action and a Presidential signature. The only thing we know for sure is that we'll be watching this issue for quite some time.