The Consumer Financial Protection Bureau (CFPB) released a proposed rule (the “Proposed Rule”) on May 5, 2016, that would prohibit financial services companies from using class action waivers in consumer arbitration clauses. In its current form, the Proposed Rule would impose two limitations on the use of pre-dispute arbitration agreements by financial services companies, which include, but are not limited to, entities that collect debt, lend money, store money, and move or exchange money. First, the Proposed Rule would prohibit financial services companies from using mandatory pre-dispute arbitration clauses to block consumer class actions in court. Second, it would require those companies that use pre-dispute arbitration agreements to follow certain delineated public disclosure and monitoring requirements.

According to the CFPB, class actions provide a more effective means for consumers to challenge problematic practices by banks and other financial institutions than arbitration proceedings. Additionally, the CFPB believes that class actions have the positive impact of more quickly changing the practices of banks and other financial institutions when those practices are harmful to consumers. The CFPB claims that class action waivers in arbitration agreements eliminate the deterrent effect of class actions and deny consumers their day in court.

The CFPB issued the Proposed Rule pursuant to its mandate under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank). Among other things, Dodd-Frank directs the CFPB to study the use of arbitration agreements in connection with consumer financial products and services outside of the mortgage context and authorizes the CFPB to prohibit or restrict the use of such agreements if the CFPB finds it in the public interest to do so. In 2012, the CFPB identified data sources for a study on the use of arbitration agreements in consumer contracts by publishing a request for information in the Federal Register. The CFPB received and reviewed approximately 60 comments and released the results of the study in March 2015. In October 2015, the CFPB announced its plan to release the Proposed Rule. As required under the Regulatory Flexibility Act, the CFPB convened a Small Business Review Panel (the “Panel”) to identify Small Entity Representatives (SERs) to provide feedback on the Proposed Rule prior to its release. In December 2015, the CFPB issued a final report summarizing the Panel’s recommendations and outlining various concerns raised by the SERs.

Based on the report, the SERs recommended that the CFPB seek additional comment or conduct additional research on the following topics before issuing the Proposed Rule:

- The costs associated with defending class actions for small companies;
- The availability and cost of insurance for small companies and whether it covers class action defense costs;
- When small entities may be indemnified by third parties for their behavior and related expenditures they could incur in class actions;
- The impact of class actions on small entities’ conduct;
- Whether publication of claims would provide an accurate picture of arbitration;
- Whether improved consumer access to individual arbitrations would provide the same benefits as class action litigation; and
- Whether specific features of cases affect the availability of consumer relief.

Despite the concerns raised by the SERs, the CFPB decided instead to issue the Proposed Rule without taking further comments.

Significantly, the Proposed Rule may conflict with the Supreme Court’s interpretation of the Federal Arbitration Act (FAA), including its decision in AT&T Mobility v. Concepcion, 563 U.S. 333 (2011). In Concepcion, the Court invalidated a decision by the California Supreme Court, which held that class action waivers in mandatory arbitration provisions were unconscionable. The Court reasoned that the rule adopted by the California Supreme Court was preempted by the FAA because it “[stood] as an obstacle to the accomplishment and execution of the full purpose and objectives of Congress” in enacting the FAA. However, despite the Court’s holding in Concepcion, the Proposed Rule seeks to invalidate altogether class action waivers in consumer financial and services contracts. As such, the Proposed Rule highlights a tension between the CFPB’s mandate under Dodd-Frank and the Supreme Court’s interpretation of the FAA that will test the Court’s holding in Concepcion. Indeed, if the Proposed Rule is issued in its present form, it seems only a matter of time before it is challenged on this ground.

The members of Drinker Biddle’s Financial Services
Team are ready to help you maintain a culture of compliance in today’s constantly changing regulatory environment. Our Team will continue to monitor the Proposed Rule and related CFPB activities. If you have any questions regarding the Proposed Rule, please do not hesitate to contact one of the lawyers listed below or your regular Drinker Biddle contact.

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