July 22, 2016

Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

Re: CFPB-2016-0020, RIN 3170-AA51

To Whom It May Concern:

Public Justice[1] offers its enthusiastic support for the Consumer Financial Protection Bureau ("CFPB")'s proposed rule entitled Arbitration Agreements, Docket No. CFPB-2016-0020, published in the Federal Register on May 24, 2016 at 81 FR 32830 ("Proposed Rule"). Because it will free consumers to join together in class actions to hold corporations accountable and deter misconduct, and because it will increase transparency around the pre-dispute arbitration provisions used in the financial services industry, the Proposed Rule is in the public interest and for the protection of consumers.

After conducting a thorough empirical study as required by the Dodd-Frank Wall Street Reform and Consumer Protection Act, 12 U.S.C. § 5518, the CFPB published a Report to

[1] Public Justice pursues high impact lawsuits to combat social and economic injustice, protect the Earth's sustainability, and challenge predatory corporate conduct and government abuses. For more than 15 years, Public Justice has operated a special project devoted to fighting abuses of mandatory arbitration. We have represented consumers in over fifty cases challenging unfair or overreaching forced arbitration clauses, in both state and federal courts. While arbitration clauses are widely enforceable as a matter of federal law, we have successfully had mandatory arbitration clauses declared unenforceable by courts in cases where corporations added outrageous terms to their arbitration clauses (such as requiring consumers with small claims to travel across the country), or where corporations have attempted to enforce arbitration clauses against consumers who never agreed to them, among other abuses.

Congress in March of 2015.[2] That Report analyzed over 850 mandatory pre-dispute arbitration provisions imposed on consumers by financial services corporations regulated by the CFPB, such as banks, credit card issuers, payday lenders, and companies providing private student loans. The Report also reviewed over 1800 arbitrations filed with the American Arbitration Association between 2010 and 2012 for disputes over the financial products and services that the CFPB regulates, as well as nearly 3500 individual cases filed in federal courts and 562 class actions filed in federal and selected state courts regarding the same products and services during the same three-year period.[3]

This deep dive into the data yielded five key conclusions: 1) tens of millions of American consumers of financial products and services are subject to mandatory pre-dispute arbitration provisions while very few consumers understand their legal significance; 2) nearly all pre-dispute arbitration provisions ban consumers from consolidating claims with other consumers and participating in a class action; 3) consumers filed very few arbitrations against lenders and other finance sector corporations, particularly over small-dollar claims;[4] 4) of the 562 class actions studied, nearly 100 were dismissed or stayed by a company filing a motion to compel arbitration and invoking the class action ban in its arbitration clause;[5] and 5) between 2008 and 2012, class action settlements yielded $2.7 billion in cash, in-kind relief and expenses paid by

[2] Bureau of Consumer Fin. Prot., Arbitration Study: Report to Congress, Pursuant to Dodd-Frank Wall Street Reform and Consumer Protection Act § 1028(a) (2015) ("Report"), available at http://files.consumerfinance.gov/f/201503_cfpb_arbitration-study-report-to-congress-2015.pdf.

[3] The Report also included an analysis of 400 federal consumer class action settlements over a five-year period, more than 40,000 filings in small claims court, and nearly 1200 federal and state public enforcement actions related to consumer finance.

[4]Specifically, consumers filed approximately 410 arbitrations annually with the American Arbitration Association ("AAA") regarding financial products and services between 2010 and 2012, with only around 25 of those arbitrations each year involving disputes over $1000 or less. Moreover, only 32, or 20%, of consumers whose claims were decided by an arbitrator in 2010 and 2011 received any affirmative relief whatsoever (with an additional 46 arbitrations resulting in debt forbearance), while companies prevailed in 227 of the 244 arbitrations resolved by an arbitrator during the same time period in which the companies had sought affirmative relief. 81 Fed. Reg. 32845-46.

[5] 81 Fed. Reg. 32848 and fn.278.

financial services companies, only 16% of which went to attorneys' fees, and at least 34 million consumers received cash relief as a result of these class action settlements.[6]

The Proposed Rule to prohibit financial services companies from using pre-dispute arbitration provisions to block class actions is thus consistent with, and flows directly from, the conclusions of the Report. Yet there are ways in which the final rule could be clarified and improved to better protect consumers, and Public Justice offers some suggestions along these lines. Most important, the circumstances in which providers are considered to "enter into" a pre-dispute arbitration agreement after the Proposed Rule's compliance date, and thus become bound by its requirements, must be expanded to cover providers who materially amend their agreements with consumers after the compliance date as well as providers who seek to rely on arbitration provisions to which they may not be a party. In addition, we recommend that the proposed notice to consumers who have purchased more than one product from a provider include a more detailed breakdown of which products are and are not covered by the rule, to avoid confusion and give consumers a meaningful explanation of their rights. Lastly, while the proposal to collect records of individual arbitrations will bring much-needed sunshine to the often secretive arbitration process, the trigger for providing records should be broadened beyond instances when a claim is filed in arbitration—an all too rare occurrence—to cover other ways in which these clauses are used to suppress claims.

I. The Proposed Rule's Prohibition of Class action Bans in Pre-Dispute Arbitration Agreements Is In the Public Interest and for the Protection of Consumers.

A. Class Actions Benefit Consumers and the Public in Both Financially Measurable and Other Ways.

As the CFPB summarized in its Notice of Proposed Rulemaking, Federal Rule of Civil Procedure 23 was amended in 1966 to allow named class representatives to bring claims on

[6] 81 Fed. Reg. 32849-50.

behalf of others harmed in a similar way by the same illegal conduct.[7] This representational device makes the court system more efficient by allowing like claims to be adjudicated together and avoiding duplication of resources. And where each class member's damages are minor in monetary terms, class actions "overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her own rights . . . by aggregating the relatively paltry potential recoveries into something worth someone's (usually an attorney's) labor."[8]

The "relatively paltry" amount of the individual recoveries in many class actions is a common refrain among critics of the CFPB's Report and its Proposed Rule. These industry spokespeople lament that the average recovery in consumer class settlements discussed in the Report was only $32 (although it seems unlikely that they would have been sanguine about relinquishing even more cash compensation to the 34 million consumers for which this average recovery amount was calculated). But it is precisely when individual damages are small that the class action device is most appropriate, and most necessary. If a credit card company charges an illegal fee of $.99 on each customer's bill each month, for example, the amount would be so negligible that most customers would probably not notice it. Even those who did notice the charge would be unlikely to take the time to investigate and determine that it is illegal. And of the tiny fraction of affected consumers aware of both the conduct and its illegality, none would go forward with the time and expense of filing suit, nor would they find an attorney willing to represent them, unless they could do so on a class action basis, for as Judge Richard Posner once put it, "only a lunatic or a fanatic sues for $30."[9]

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[7] 81 Fed. Reg. 32833.
[8] *Mace v. Van Ru Credit Corp.*, 109 F.3d 338, 344 (7th Cir. 1997)
[9] *Carnegie v. Household Int'l, Inc.*, 376 F.3d 656, 661 (7th Cir. 2004).

But a $.99 illegal fee, while barely affecting the bottom line of each monthly bill and thus escaping most consumers' notice, would still add up to millions of dollars in illegal profits when charged to hundreds or thousands of customers over hundreds and thousands of months. Thus, if the class action device were not available to the consumers victimized by this hypothetical scheme, their credit card company would be able to go on enriching itself by breaking the law at the expense of its largely unsuspecting customers.

The consumer protection laws were designed to remedy these sorts of wealth transfers from cash-strapped consumers to profitable corporations. In practice, class actions are the best—and sometimes the only—tool for returning ill-gotten gains to the consumers from whom they were taken.

As a real-life example of the illegal conduct that class actions can address, Public Justice's executive director, Paul Bland Jr., was co-counsel in *Wells v. Chevy Chase Bank*, a class action litigated in Maryland state court.[10] In that case, the credit card issuer had promised in promotional materials and in its contract that it would "never" raise interest rates above 24%, but then it did raise its interest rates above that point and imposed a number of other unlawful charges. The case was settled for $16.1 million (as well as actions taken to remove improper negative information from class members' credit records), and checks were mailed to approximately 200,000 class members. Similar stories no doubt underlie many of the 423 class action settlements totaling $2.7 million that were profiled in the CFPB Report.

Nor was the CFPB Report the first empirical study to conclude that class actions bring meaningful financial relief to large numbers of people. In a 2010 paper published in the Journal of Empirical Legal Studies, law professor (and former Scalia law clerk) Brian Fitzpatrick

[10] For a published decision outlining the facts of the case, *see Wells v. Chevy Chase Bank*, 832 A.2d 812 (Md. 2003) (no preemption under Home Owner Lending Act of breach of contract and consumer protection act claims against credit card issuer).

reported that in 2006 and 2007, federal district courts approved 688 class action settlements totaling $33 billion, of which approximately $5 billion or 15% went to cover attorneys' fees.[11]

And while the monetary value of class action settlements tends to dominate the headlines, equally if not more important—though harder to quantify — are the changes that class actions bring about in corporate behavior. Many class action awards and settlements include injunctive relief requiring companies to stop the practices that brought about the action, monitoring to ensure that further misconduct does not occur, and increased training or other safeguards to improve future compliance with the law. Even in the absence of such mandatory settlement terms, many companies take similar steps on their own in a proactive effort to anticipate and reduce their exposure to class action liability.

This is why the proliferation of pre-dispute arbitration agreements with class action bans has been so devastating for consumers seeking to hold financial services companies accountable for their actions, and why the remedy offered by the Proposed Rule is so desperately needed. Public Justice was involved in five class actions against payday lenders in North Carolina state court in 2010 and 2011. Three of these cases settled for $45 million, with payments sent to over 200,000 consumers. But because of arbitration provisions with class action bans, the other two cases were dismissed and resulted in no compensation to anyone, unless without our knowledge some of the affected consumers individually sought and received relief in arbitration.[12] Obviously this was unfair to the consumers in the last two cases. But the larger injustice is that as more and more consumer class actions suffered a similar fate over the last several years,

[11] Fitzpatrick, Brian T., An Empirical Study of Class Action Settlements and Their Fee Awards (July 7, 2010). Journal of Empirical Legal Studies, Vol. 7, 2010; CELS 2009 4th Annual Conference on Empirical Legal Studies Paper; Vanderbilt Public Law Research Paper No. 10-10; Vanderbilt Law and Economics Research Paper No. 10-06. Available at SSRN: http://ssrn.com/abstract=1442108 or http://dx.doi.org/10.2139/ssrn.1442108.

[12] These North Carolina payday cases were discussed in the CFPB's Preliminary Results published in December of 2013. Bureau of Consumer Fin. Prot., Arbitration Study Preliminary Results (Dec. 12, 2013), available at http://files.consumerfinance.gov/f/201312_cfpb_arbitration-study-preliminary-results.pdf.

corporations' incentives to ensure they were obeying the consumer protection laws, in order to minimize their risk of facing expensive class actions, has been severely eroded.

In other words, arbitration provisions with class action bans have largely neutralized the deterrent effect that the potential of class action liability otherwise serves, allowing financial services companies to violate the law with impunity. And ordinary consumers, especially low-income consumers who are most desperately in need of credit and have the least leverage in negotiating the terms on which they obtain that credit, have paid the price for this lack of accountability.

And consumers have paid a double price—not only have they lost the right to band together to hold corporations accountable for misconduct, but that right was stolen from them through stealth contracting, not bargained away through arms-length negotiation or lost openly through litigation. Defendants in putative class actions have every right to advance their positions against class certification and for smaller class recoveries (or no recoveries at all) in the courts where class cases are filed. That is the nature of our adversarial legal system.

But what these companies should not be permitted to do, and what the CFPB is both legally authorized and morally justified to stop them from doing with this Proposed Rule, is to use their superior bargaining power to slip a time bomb into contracts of adhesion with their customers—a time bomb that will only explode and harm the customer once a dispute arises and the customer begins investigating her legal options. The ability to band together in a class action is not only a legal right available to consumers with either federal and state law claims; it is one of the most powerful tools that consumers can use to level the playing field and get wealthy corporations to pay attention to them when they allege a widespread abuse or pattern of misconduct. When financial services companies slip class action bans into pre-dispute arbitration

agreements that consumers do not understand or have a chance to negotiate, they are preemptively depriving their weaker potential opponents of their most powerful weapon before the conflict even begins and without the potential opponents even realizing they've been disarmed. The Proposed Rule curtailing this deeply unfair practice is in the public interest and will protect consumers.

B. Neither Individual Arbitrations nor Public Enforcement Can Replicate the Benefits That Class Actions Afford.

Industry representatives have frequently opined, both in previous comments to the CFPB and in other written and oral statements, that those consumers who participate in arbitration usually have positive experiences and that if the CFPB engaged in a public education campaign informing consumers about arbitration, more people would use the system. This may or may not be true. We at Public Justice have spoken with dozens of individuals over the years who have gone through arbitration or were in the midst of doing so and were extremely dissatisfied with the process and the results. Media accounts of forced arbitration also feature primarily negative reactions from consumers who have had a front-row seat to the process.[13]

But the perceptions and experiences of the very few consumers who have gone through arbitration misses the larger systemic point, from the perspective of deterrence and remedying the overwhelming majority of illegal conduct. The structural forces that lead "only a lunatic or a fanatic" to sue for $30 lead to the same biases in the arbitral setting. Thus, while around 410 consumers filed claims with AAA between 2010 and 2012, only 25 of these claims each year were for amounts of $1000 or less. Another study of a broader cross section of consumer arbitrations found that only 184 of 4839 consumers, or less than 4%, arbitrated claims for $1000

[13] *See, e.g.*, Jessica Silver-Greenberg and Robert Gebeloff, "Arbitration Everywhere, Stacking the Deck of Justice": New York Times, November 1, 2015. Available at http://www.nytimes.com/2015/11/01/business/dealbook/arbitration-everywhere-stacking-the-deck-of-justice.html ("NYT, Arbitration Everywhere").

or less.[14] Even if the total participation rate in arbitration could be increased through a public education campaign, the same predominance of relatively large claims in arbitration would persist.

When the filing fee to bring an arbitration claim, not to mention the lost wages and productivity associated with preparing for and attending an arbitration, exceeds the value of the claim, deciding against arbitration is the rational economic choice, and no amount of education is going to change that. Of course, if the corporations that draft pre-dispute arbitration agreements were willing to let consumers utilize the claim-aggregating procedures of class actions in the arbitral setting, as the leading arbitration providers allow parties to do, then the economics of the situation would change and bringing small-value claims in arbitration would become more feasible. But financial services companies, and their lobbyists, have showed no interest in offering the option of class arbitration to their customers and instead have consistently vilified it.[15]

Thus, as long as arbitration continues to be a forum used, if at all, by consumers with relatively large individualized claims, it will never serve the same widespread deterrence and behavior-altering functions that class actions do. This is because many more people are affected by the sorts of uniform policies that inflict small monetary damages on all or most customers, such as an illegal surcharge or improper debt-collection phone call, than are affected by the relatively large disputed debts that tend to go to arbitration. These uniform policies inflicting small individual harms are ideally suited to classwide treatment, but they will almost never be

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[14] *See* David Horton & Andrea Cann Chandrasekher, After the Revolution: An Empirical Study of Consumer Arbitration, 104 GEO. L.J. 57, 117 (2015). *See also* NYT, Arbitration Everywhere, *supra* note 13 ("between 2010 and 2014, only 505 consumers went to arbitration over a dispute of $2500 or less").

[15] In a recent amicus curiae filing, for instance, the U.S. Chamber of Commerce argued that "[c]lass arbitration is a worst-of-all- worlds Frankenstein's monster: It combines the enormous stakes, formality and expense of litigation that are inimical to bilateral arbitration with exceedingly limited judicial review of the arbitrators' decisions." Br. of the Chamber of Commerce of the United States of America as Amicus Curiae in Support of Pl.-Appellants at 9, *Marriott Ownership Resorts, Inc. v. Sterman*, No. 15-10627 (11th Cir. Apr. 1, 2015).

brought in individual arbitration, because the "relatively paltry potential recoveries" for these sorts of claims, in the absence of aggregation, are simply not worth anyone's time or effort.

Similarly, public enforcement cannot fill the void in a landscape without consumer finance class actions. The CFPB studied nearly 1200 public enforcement actions brought by state and federal regulatory agencies over a five-year period and concluded in its Report that public enforcement actions rarely overlapped with private class actions, and that when there was overlap, the public enforcement more often followed the private class action than the other way around.[16] A letter from the attorneys general of seventeen states and the District of Columbia dated August 11, 2016 and submitted in this same docket ("Attorney General Letter") reiterated this theme, pointing out that their jurisdictions' consumer protection statutes contain private rights of action that were intended to "complement and extend" public enforcement efforts and supplement the finite resources of enforcement agencies.[17] The Attorney General Letter concluded that the Proposed Rule is in the public interest and for the protection of consumers because "class action settlements provide monetary relief to consumers, act as a deterrent to the specific defendant as well as to the industry, and lead to the reform of otherwise unchecked unlawful, unfair or deceptive business practices."[18] In short, class actions are an essential component of the infrastructure needed to hold corporations accountable for violating the law and harming consumers, and the Proposed Rule will restore that important bulwark of accountability in the consumer finance sector.

[16] 81 Fed. Reg. 32850-51.
[17] Attorney General Letter at 2 and fn. 2.
[18] Attorney General Letter at 4.

II. The Proposed Rule Can and Should Be Strengthened.

A. The Definition of "Pre-Dispute Arbitration Agreement" Should Be Expanded.

As currently phrased, the definition of "pre-dispute arbitration agreement" to be codified at 12 C.F.R. § 1040.2(d)[19] appears inconsistent with other provisions in the Proposed Rule. We believe that adding additional language to the definition (or to comment 2(d)-1 in Supplement I) will alleviate any potential confusion caused by these apparent inconsistencies.

First, the proposed definition limits pre-dispute arbitration agreements to agreements "between a provider and a consumer." But proposed comment 4-2 clarifies that "section 1040.4(a)(1) would also prohibit [a] debt collector from" seeking to thwart a class action based "on a pre-dispute arbitration agreement entered into by a merchant creditor who was excluded from coverage by § 1040.3(b)(5).," such as a doctor, hospital or auto dealership.[20] Thus, when the Proposed Rule refers to pre-dispute arbitration agreements, it must be understood to also include pre-dispute arbitration agreements entered into by entities that are not providers as defined in proposed § 1040.2(c). This potential inconsistency can be remedied by replacing the word "provider" in proposed § 1040.2(d) with the phrase "person as defined in 12 U.S.C. § 5481(19)."

Second, "pre-dispute arbitration agreement" is defined to cover those agreements "providing for arbitration of any future dispute between the parties." Because companies have been known to roll out new arbitration agreements with class action bans after a claim has already been filed, however, a clause should be added to this definition clarifying that a "pre-dispute arbitration agreement" also includes an agreement introduced to a consumer who is a

[19] Unless otherwise noted, all subsequent section references are to Title 12 of the Code of Federal Regulations.
[20] *See* further explanation of how debt collectors are prevented under proposed § 1040.4(a)(1) from relying on arbitration provisions entered into by entities outside of the CFPB's authority, such as those described in proposed § 1040.3(b)(5), at Fed. Reg. 32884.

putative class member after a claim has been filed but before a class is certified to pursue that claim.[21]

This additional language would make clear that the proposed rule against relying on pre-dispute arbitration provisions "with respect to any aspect of a class action that is related to any of the consumer financial products or services covered by § 1040.3"[22] applies to agreements imposed on consumers after a complaint is filed in an attempt to forestall potential classwide liability on that claim as well as to agreements that were in existence before a claim was ever filed. Such a clarification is certainly consistent with the Proposed Rule's purpose of preventing arbitration provisions from being used strategically to block consumers from filing and litigating class actions in court.

With these two modifications, proposed § 1040.2(d) would read as follows: "Pre-dispute arbitration agreement means any agreement between a consumer and a person as defined in 12 U.S.C. § 5481(19) providing for arbitration of any future dispute between the parties, including but not limited to agreements first transmitted to a consumer after a claim has been filed that would include that consumer as a class member but where no class has yet been certified."

Finally, comment 2(d)-1 should be supplemented, or a new comment 2(d)-2 added, to stipulate that agreements fall equally within the definition of "pre-dispute arbitration agreement," and are subject to all provisions of the Proposed Rule, even if they contain an opt-out provision. Corporations that draft arbitration provisions and bury them in contracts with consumers will sometimes point to opt-out provisions, and consumers' failure to opt out, as evidence of the

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[21] Section 1028 of the Dodd-Frank Act limits the CFPB's rulemaking authority to "pre-dispute arbitration agreements" and excludes agreements that consumers voluntarily "enter[] into" "after a dispute has arisen." 12 U.S.C. § 5518(c). However, before a class is certified no dispute has yet arisen between the defendant and the absent class members, and so the agreement is still a "pre-dispute arbitration agreement" as to those absent class member consumers.
[22] Proposed § 1040.4(a)(1).

consumer's assent to the terms or a badge of extra fairness for the arbitration agreement. But the only thing opt-out provisions actually show is that consumers are just as unlikely to pay attention to the opt-out provision as to the rest of the terms, until a dispute arises—at which point it will usually be too late to opt out. The NPRM noted both in its summary of the Report results and in a section on economic theory that very few consumers subject to arbitration agreements with opt-out provisions are aware of their ability to opt out during the window in which they can do so.[23] Thus, the presence or absence of opt-out provisions should have no bearing on whether an agreement is a "pre-dispute arbitration agreement" covered by the Proposed Rule.

B. The Scope of the Proposed Rule Should Be Broadened in Several Respects.

Although the Proposed Rule provides a fairly extensive list of products and services involved in the core consumer finance markets of lending money, storing money, and moving or exchanging money, the list of covered financial products and services at proposed § 1040.3(a) is underinclusive in some key areas. In addition, the exception for governments and government affiliates at proposed § 1040.3(b)(2) is ill-conceived and should be eliminated or modified.

For one thing, the limitation on proposed § 1040.3(a)(4)—that providers or users of consumer reports under the Fair Credit Reporting Act will only be covered by the Proposed Rule when they provide such reports directly to consumers—ignores much of the harm caused to consumers by inaccurate credit reports. Often consumers only learn that their credit score is incorrect or that their credit report contains erroneous entries when adverse action is taken against them by a potential landlord or employer—sources of adverse action not otherwise covered by proposed § 1040.3(a) and thus beyond the scope of proposed § 1040.3(a)(4) as written. Moreover, the credit bureaus frequently generate the highest volume of consumer complaints to the CFPB in its monthly reports, and many of those complaints do not derive from

[23] 81 Fed. Reg. 32843, 32920.

reports that were provided directly to consumers based on adverse action taken by products or services otherwise covered by proposed § 1040.3(a). This restriction should be lifted so that the full range of FCRA class actions can be brought without interference from providers attempting to rely upon pre-dispute arbitration provisions.

Additionally, although proposed § 1040.3(a)(3) discusses debt management and debt settlement services, none of the provisions of proposed § 1040.3(a) specifically mention so-called credit repair services. These schemes, which advertise improvement of a consumer's credit score in exchange for a fee, are almost always fraudulent and misleading, and should be separately enumerated in proposed § 1040.3(a). On a related note, proposed § 1040.3(a)(1)(iii) refers to lead generators, or entities that engage in "refer[ring] applicants or prospective applicants to creditors, or select[ing] or offer[ing] to select creditors to whom requests for credit may be made" consistent with its meaning in 12 CFR 1002.2(l)." But lead generators should also be covered under § 1040.3 when they offer to match consumers with other financial services such as the sorts of debt relief services discussed in proposed § 1040.3(a)(3).

A case in which Public Justice currently serves as co-counsel before the Ninth Circuit, *Rodriguez v. Experian Services Corp. et al.*, No. 15-56660, alleges that LowerMyBills, Inc., claiming an affiliation with Experian and using Experian's name and logos, acted as a lead generator in matching distressed consumers with debt relief services, one of which turned out to be a scam that took hundreds of thousands of dollars from putative class members while doing nothing to consolidate or renegotiate their debts. We are involved in the case because the defendants are seeking to use the pre-dispute arbitration agreement in LowerMyBills, Inc.'s online Terms of Use to dismiss the class claims and force the named plaintiffs into individual arbitration. The *Rodriguez* case is just one example of why lead generators for other covered

financial products and services, such as debt relief and debt settlement, must also be listed in proposed § 1040.3(a).

Finally, Public Justice objects to the exclusion from coverage for the federal government and its affiliates, as well as for state, local and tribal governments and their affiliates, to be codified at §1040.3(b)(2). The CFPB's explanation that this exclusion is warranted because governments and their affiliates will be held accountable through the democratic process[24] does not withstand close scrutiny. Because of the same factors that make class actions so valuable for rectifying consumer law violations—that many consumers will not realize they are being overcharged or otherwise mistreated, or will not realize that the conduct is illegal—these uninformed consumers will not take electoral action based on governmental misconduct about which they are unaware. This disconnect is magnified by the numerous other priorities and issues that motivate people to vote in particular ways, making it improbable that voting behavior will turn on a particular lending or money handling practice even if constituents are aware of that practice. And given the fact that not all constituents will be affected by an abusive practice, such as illegal collection activity by a student loan servicer affiliated with the government, even a group of angry former students who do care enough about the loan servicer's conduct for that conduct to affect their votes are unlikely to wield enough power to influence the outcome of an election at the local or state level (and certainly not at the federal level).

The problems with this governmental exclusion are compounded by an unadministerable qualification about territory and residence. The exclusion would apply to state, local and tribal governments and their affiliates only to the extent that they provide products or services covered by § 1040.3(a) "directly to a consumer who resides in the government's territorial jurisdiction."[25]

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[24] 81 Fed. Reg. 32881-82.
[25] Proposed § 1040.3(b)(2)(ii).

This would mean that governments and affiliates offering otherwise covered products or services would be subject to the Proposed Rule for consumers living outside of the government's territorial jurisdiction but would be exempt from the Proposed Rule for those consumers living within the government's jurisdiction. Perhaps most bizarre of all,a product or service's coverage status would change as to the same consumer depending on where the consumer reside at any particular time, not a theoretical or far-fetched situation given how often students, and people generally, move around in contemporary America. This uncertainty around coverage would pose logistical compliance headaches for potentially covered governmental and affiliate providers, as well as for the CFPB and any court later asked to sort out the resulting mess. Such headaches are best avoided by simply doing away with this exclusion.[26]

C. The Examples of Conduct That Constitutes "entering Into" a Pre-Dispute Arbitration Agreement Must Be Expanded to Include Material Amendments to Existing Agreements and Reliance on Arbitration Agreements by Non-Parties.

All of the obligations on providers described in proposed § 1040.4 are triggered by the provider "entering into" a pre-dispute arbitration agreement after the compliance date established in proposed § 1040.5(a). But comment 4-1, which provides examples of when a provider does and does not enter into a pre-dispute arbitration agreement for purposes of § 1040.4, is very problematic in its current form. First, examples i-C and ii-A, taken together, suggest that if a consumer had a product or service before the compliance date whose terms of service did not include a pre-dispute arbitration agreement, and the provider added such an agreement after the compliance date, then the provider would be subject to § 1040.4. But these examples also seem to suggest that if the provider already had a pre-dispute arbitration agreement in place before the

[26] If the CFPB decides to retain the governmental exclusion at proposed § 1040.3(b)(2), then at a minimum the definition of "affiliate" should be changed from the general-purpose definition found at 12 U.S.C. § 5481(1), which is not unique to the government setting, and the definition of "government affiliates" used by the Internal Revenue service should be used instead. *See* Rev. Proc. 95-48, 1995-2 C.B. 418, Section 4 (Nov. 20, 1995).

compliance date, but that arbitration provision did not ban class actions, the provider could nonetheless amend the arbitration provision after the compliance date to add such a class action ban and remain outside the scope of the Proposed Rule. Such a perverse outcome directly in conflict with the Proposed Rule's purpose could not have been intended, and comment 4-1 should be revised to avoid such absurd results.

The exception to "entering into" pre-dispute arbitration agreements found at comment 4-1-ii-A, for any "modifi[cation], amend[ment], or implement[ation of] the terms of a product or service that is subject to a pre-dispute arbitration agreement that was entered into before the date set forth in § 1040.5(a)" has other negative consequences as well. It would allow pre-dispute arbitration provisions with class action bans to remain in effect indefinitely, and would allow providers to continue enforcing those arbitration provisions to block consumers from bringing or participating in class actions for years or even decades, so long as the consumer was already a customer before the compliance date, no matter what other changes are made to the terms of the product or service after that date. Given that many consumers keep the same bank accounts and credit cards for years—even for their entire adult lives—and that advice to those trying to improve their credit scores often includes refraining from opening new accounts, this cramped view of "entering into" pre-dispute arbitration agreements will keep thousands of consumers trapped in contracts that can still be used against them to bar class actions and will blunt the rule's effectiveness in its goal of protecting consumers.

The CFPB should address these problems with proposed comment 4-1 by adding a non-exhaustive list of material amendments to the terms of a covered product or service that, when such amendments are made after the compliance date, would constitute entering into a pre-dispute arbitration agreement within the meaning of § 1040.4 and comment 4-1-i. This list

should include, at a minimum, changes to the price of the product or service (such as the interest rate of a loan or any fees periodically charged in conjunction with the product or service), addition of language regarding class actions, and any substantive amendment to the arbitration provision itself.

The juxtaposition between examples i-B and ii-B in comment 4-1 is also problematic in that it establishes party status as the key distinction between entering into and not entering into a pre-dispute arbitration agreement when a provider acquires a product subject to such an agreement. Public Justice litigates many cases in which companies seek to enforce arbitration provisions in contracts to which they are not parties based on such doctrines as alter-ego, agency, third-party beneficiary and estoppel.[27] Thus, just because a provider is not a party to a given arbitration agreement, this does not necessarily mean the provider would be unable to enforce it against a consumer, and based on the exception to "entering into" set forth in comment 4-1-ii-B, such non-party acquirers would be exempt from all of the requirements of § 1040.4. There is no basis for such differential treatment, given that non-party acquirers of covered products within the meaning of comment 4-1-ii are already defined as providers and thus subject to the CFPB's rulemaking authority. We therefore recommend that the distinction between parties and non-parties in comment 4-1 be eliminated in the final rule.

D. The Optional Notice Provision for Consumers with Both Covered and Non-Covered Products Should Be Required to Provide Product-Specific Information, and Amendment Should Be Favored Over Notice Whenever Possible Under Proposed § 1040.4(a)(2)(iii).

Public Justice applauds the plain language of the required notice to consumers set forth in proposed § 1040.4(a)(2)(i). The provision straightforwardly communicates to consumers the

[27] *Arthur Andersen LLP v. Carlisle*, 556 U.S. 624, 631 (2009).

nature and extent of their rights and is a refreshing contrast to the inscrutable Legalese found in many arbitration provisions and consumer contracts generally.

The picture is not nearly so clear, however, with respect to the optional notice set forth at proposed § 1040.4(a)(2)(ii). The impulse to inform consumers about the limitations of coverage is understandable, for consumers who read the language of § 1040.4(a)(2)(i) and believe that all of their products from the same provider are subject to the Proposed Rule when that is not the case are apt to be confused, disappointed or angry upon subsequently learning otherwise. However, without specifying which product(s) are subject to the Proposed Rule and which are not, the provision does not actually communicate anything very useful and will create more confusion than it will cure. We recommend that a provider of multiple products to the same consumer be required to deliver separate terms with each product, thus making it easy for consumers to differentiate between covered products whose terms contain the notice required by § 1040.4(a)(2)(i) and non-covered products that do not. Alternatively, if language like that proposed in § 1040.4(a)(2)(ii) is to be used, then the provider must identify by name the product(s) that are covered and any product(s) that are not covered—in other words, the provider must customize the notice to each consumer who has obtained both covered and non-covered products from that provider.

Finally, with respect to the situation when a provider enters into a pre-dispute arbitration agreement that previously existed between other parties without the required notice, the "amendment" and "notice" alternatives of proposed § 1040.4(a)(2)(iii)(A) and (B) are treated as equivalent options from which a provider can choose at will. Because these notice provisions are intended to be contractually binding, however,[28] and because amendments to contracts have more legal heft—and are more likely to garner a consumer's attention—than mere notices, the

[28] 81 Fed. Reg. 32890.

CFPB should require in the final rule that the agreement provision of § 1040.4(a)(2)(iii)(A) be used whenever it is possible for the provider to do so. The notice provision set out at § 1040.4(a)(2)(iii)(B) should only be permitted when amendment is contractually impossible, such as for lack of consideration.[29]

III. The Proposal to Collect Data About Individual Arbitrations Will Benefit Consumers and Serve the Public Interest, But as Written the Scope of Data to Be Collected Is Too Narrow.

The requirement that providers who enter into pre-dispute arbitration agreements after the compliance date provide information to the CFPB about the arbitrations in which they are involved, to be codified at § 1040.4(b), will bring enhanced transparency to an arbitration system that is all too often shrouded in secrecy. Public Justice is particularly gratified by the requirement that providers disclose information about non-payment of fees or failure to comply with due process protocols of arbitration providers, as we are hearing increasingly frequent anecdotal reports of arbitrations being placed on hold indefinitely or rejected by arbitration providers because of these sorts of failures and of consumers consequently being deprived of any forum in which to advance their claims.

But the record collection requirement, as written, will provide an incomplete picture of how arbitration provisions are truly being used, because many types of records need only be disclosed under the Proposed Rule once a claim is filed in arbitration. But as the CFPB's own Report demonstrated, very few claims are actually filed in arbitration each year regarding the consumer finance markets at issue. Instead, arbitration provisions are often deployed by companies when a lawsuit is filed, or when a consumer or her attorney first contacts the company to discuss the dispute, and the deterrent effect of the company disclosing the arbitration

[29] The language of § 1040.4(a)(2)(iii)(B) should also be revised to include a reference to other parties not being able to use the pre-dispute arbitration agreement to ban class actions, as all of the other provisions in § 1040.4(a)(2) do.

provision often results in no claim being filed in any forum. Thus to fully appreciate how the use of arbitration provisions plays out in discussions between providers and consumers, the requirements of § 1040.4(b)(1)(i)(B) should be triggered whenever a provider "relies upon" a pre-dispute arbitration provision, with the term "rely upon" to be defined with examples similar to those provided in comment 4(a)(1)-1 for reliance in the class action context. Public Justice recommends that the CFPB broaden the scope of records to be provided in the final rule and revise the language of § 1040.4(b)(1)(i) accordingly.

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In conclusion, we wish to commend the CFPB for all of the time its staff has spent on the issue of pre-dispute arbitration agreements over the past several years. The study that the agency has conducted, the Report it has produced, and the research underlying the Proposed Rule all demonstrate an impressive commitment to empiricism and methodological transparency. We are convinced that the Proposed Rule, supported by the data gathered and conclusions reached during those years of extensive study, is in the public interest and for the protection of consumers.

Sincerely,

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