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FOCUSING ON SIGNIFICANT CASELAW AND EMERGING TRENDS

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GUEST COMMENTARY

CFPB MAKES CONSUMER ARBITRATION A NUMBERS GAME – AND THE NUMBERS OVERWHELMINGLY *SUPPORT* CONSUMER ARBITRATION

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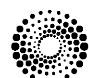
From the late 1990's until very recently, plaintiffs' lawyers and consumer advocates on the one hand, and counsel for consumer financial services companies on the other hand, vigorously debated the validity of consumer arbitration agreements containing class action waivers. That debate took place in hundreds of federal and state courtrooms throughout the country and generated countless judicial decisions, culminating in the Supreme Court's landmark rulings in *AT&T Mobility LLC v. Concepcion*[1] and *American Express Co. v. Italian Colors Restaurants.*[2]

In *Concepcion*, the Supreme Court held that express class action waivers in consumer arbitration agreements are enforceable under the Federal Arbitration Act, 9 U.S.C. §§ 1 *et seq.*, notwithstanding state unconscionability laws or state public policy. In *Italian Colors*, the Court held that there is no "vindication of statutory rights" exception to *Concepcion*. The Court rejected the plaintiffs' argument that the class action waiver was unenforceable because it was impossible for them to pursue their federal antitrust claims in an individual arbitration given the great cost of doing so compared to the relatively small amount of recoverable damages.

The battleground has now largely shifted to the administrative and political arenas. Section 1028 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted in 2010, established the Consumer Financial Protection Bureau. Section 1028 requires the CFPB 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 CFPB, "by regulation, may prohibit



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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 be "consistent with the study."

The bureau commenced its study of consumer arbitration in April 2012. Preliminary results were announced in December 2013. Finally, on Mar. 10, 2015, the CFPB released its final 728-page report. CFPB Director Richard Cordray called it "the most comprehensive empirical study of consumer financial arbitration ever conducted." That may be so, but it has not stopped others from joining the statistical fray:

- In December 2013, as a counterpoise to the CFPB's issuance of its preliminary study results, the U.S. Chamber of Commerce released a statistical analysis of class actions concluding that the vast majority of class actions "produce[] no benefits to most members of the putative class" but "can (and do) enrich [their] attorneys."[3]
- In late 2014, a group of St. John's University School of Law professors published the results of a survey purporting to explore the extent to which consumers are aware of and understand the effect of arbitration clauses in their consumer contracts. The survey essentially concluded that consumers do not understand arbitration clauses and, therefore, should not be bound by them.[4]
- More recently, a forthcoming article in the Georgetown Law Review will analyze an empirical study of approximately 5,000 American Arbitration Association consumer arbitrations conducted between 2009 and 2013 by two University of California (Davis) professors. That study was conducted to ascertain whether there is a "repeat player" effect that favors companies over consumers in arbitration (notwithstanding that the CFPB found no such effect in its Study).[5]

CFPB ARBITRATION STUDY RESULTS SUPPORT A FAULTY CONCLUSION

What do all of these numbers really show? In its 2015 press release announcing the final results of its study, the CFPB stated: "Today, the Consumer Financial Protection Bureau released a study indicating that arbitration agreements restrict consumers' relief for disputes with financial service providers by limiting class actions."[6] However, the statistics in the study actually contradict the CFPB's gloss that arbitration clauses are a barrier to class actions.

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In fact, as shown in a lengthy comment letter submitted to the CFPB earlier this month by three industry trade groups, the CFPB study confirms that arbitration is a faster, less expensive and far more effective way for consumers to resolve disputes with companies than class action litigation.[7] Based upon data reported in the comment letter:

- In 60 percent of 562 class actions studied by the CFPB, the putative class members received no benefits whatsoever. The cases were settled individually or withdrawn by the plaintiff.[8] There were final settlements in only 15 percent of the class actions. None went to trial.[9] Of the 15 percent of class actions that settled, consumers who received settlement cash payments got a paltry $32.35 on average[10] after waiting for up to two years.[11] As few as 4% of the class members who

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were eligible to receive benefits conditioned on submitting a claim form actually filed a claim.[12]

In sharp contrast, consumers who prevailed in an individual arbitration recovered an average of $5,389[13] (166 times as much as the average putative class member), and the entire arbitration process was concluded through hearing or settlement in an average of 2-7 months.[14] Moreover, the cost to the consumer for the entire arbitration was only one-half of the cost of simply filing a federal court complaint.[15] In contrast to the $32.35 received by the average class member, counsel for the class were awarded a staggering $424,495,451 — almost half a billion dollars — in attorneys' fees in just the *limited* class action data base studied by the CFPB.[16]

- The CFPB's study data completely undermines the notion that arbitration is a barrier to class actions. On the contrary, arbitration was a factor in only 8 percent of the 562 class actions studied by the CFPB.[17] Moreover, there is abundant competition in the financial services marketplace to accommodate consumers who prefer litigation to arbitration. 85 percent of credit card issuers and 92.3 percent of banks do not include arbitration provisions in their consumer contracts.[18] And, at least 25 percent 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.[19]
- The CFPB 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 — *i.e.*, they were one-off disputes that did not involve systemic issues and/or were otherwise not meritorious or certifiable. According to the CFPB study, 35 percent of the class actions filed between 2010-2012 were withdrawn by plaintiffs and 25 percent were settled individually.[20]
- The CFPB and other governmental administrative agencies are essentially displacing class actions as the "protector" of consumers. The CFPB has brought 47 enforcement actions between 2013 and the present.[21] As of July 2014, the CFPB's website stated: "To date, our enforcement actions have resulted in $4.6 billion in relief for roughly 15 million consumers harmed by illegal practices."[22] On average, based just on this data that is almost a year old, the CFPB's enforcement efforts have resulted in an average payment of $307 to each consumer, approximately 10 times the $32.35 cash payment received by the typical putative class member. For the average consumer, CFPB enforcement is far superior to private class actions as a vehicle for providing relief.
- The CFPB reported a relatively few number of consumer arbitrations (1,847) filed from 2010 through 2012.[23] However, contrary to the views of consumer advocates, that does not mean that consumers don't like arbitration or that it is an ineffective remedy. There are many other factors that affect the number of arbitrations filed by consumers. Those factors include, inter alia: (a) the vast majority of consumers resolve their disputes with businesses informally without the need for arbitration or litigation, (b) consumer arbitration is still in its infancy compared to court litigation, (c) plaintiffs' lawyers and consumer advocacy groups have sent consistently negative messages about arbitration to consumers for many years to dissuade them from using it, (d) governmental enforcement and supervisory actions have eliminated much of the need for consumers to bring private arbitration actions, and (e) individuals are turning increasingly to online arbitration and mediation resources to resolve small dollar customer complaints. The CFPB itself created a portal through which companies informally resolved more than 558,000 alleged consumer complaints in the past three years.

As the comment letter further emphasized, the CFPB has done little to educate consumers about the many benefits that arbitration can offer and the relative costs and benefits of arbitration and litigation — particularly class action litigation.

HOW OTHER STUDIES FAIL TO INDICT ARBITRATION

And what should we make of the two studies conducted by the St. John's and University of California professors? Among the many methodological flaws in the St. John's study is the critical fact that the authors did not interview consumers who actually had participated in arbitration and who would likely have positive comments about their experience. The CFPB also made a conscious decision to not survey consumers who had actually gone through an arbitration proceeding.[24]

And yet, a 2005 Harris Interactive online poll of 609 individuals who had participated in an arbitration that reached a decision reached the following conclusions, inter alia: (i) arbitration was widely seen as faster (74 percent), simpler (63 percent), and cheaper (51 percent) than going to court; (ii) two thirds (66 percent) of the participants said they would be likely to use arbitration again with nearly half (48 percent) 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 percent of those who lost were moderately to highly satisfied with the fairness of the process and 21 percent were moderately to highly satisfied with the outcome.[25]

As the Scottish scientist James Clerk Maxwell wrote, "If we betake ourselves to the statistical method, we do so confessing that we are unable to follow the details of each individual case." That is the Achilles' heel of not only the St. John's study but also, more importantly, the CFPB study: they are critically deficient in failing to examine the actual experiences of individual consumers who have gone through arbitration. In ascertaining whether consumer arbitration is in the public interest, which is the CFPB's charge, one would assume that consumers' actual experiences with arbitration and class action proceedings would be a core area of inquiry. But the CFPB deliberately avoided studying the issue, claiming that it is difficult to find consumers who have personal experience with both arbitration and litigation.[26]

The Georgetown Law Review study may have looked at thousands of actual arbitrations, but it, too, did not evaluate consumer experience. Rather, it looked narrowly at whether companies who appear in arbitration have a "repeat player" advantage over consumers. The CFPB Study examined this and concluded that that almost all of the arbitration proceedings involved companies with repeat experience in the forum. However, that was counter-balanced by the fact that counsel for the consumers were also usually repeat players in arbitration.[27] In 81 percent of the arbitrations in which consumers were awarded affirmative relief, the company was a "repeat player" but the consumer prevailed anyway.[28]

STUDIES CONFIRM ARBITRATION'S VALIDITY

The Georgetown study creates a dramatic build-up: the authors state that they will shed light on what occurs behind the "black curtain" of arbitration because prior commentators "have only the dimmest sense of what actually happens in the extrajudicial forum." They even claim (in complete contradiction of the CFPB study) that "arbitration has displaced litigation as the primary method by which consumers resolve disputes against companies" and has caused the "the demise" and "the abolition" of the consumer class action and a "massive shift" in the way that consumers resolve disputes with companies.

As for the alleged arbitrator bias against consumers caused by corporate "repeat players," it turns out there is none. Having insinuated that arbitration is part of a nefarious scheme by companies to deprive consumers of their rights, the Georgetown study itself completely dispels such a notion, concluding that "fortunately, we found little proof that private judges are prejudiced against consumers." The study further acknowledges that the AAA's due process protocol "makes it harder for arbitrators to feather their own nests. Unless the parties agree otherwise, the institution [AAA] takes the initiative and picks a decision-maker from its roster. Because there were 1,279 different arbitrators in our dataset, companies no longer have much control over the identity of the private judge. ... We simply do not find evidence linking the extreme repeat player effect to arbitrator partiality," the study admits. Obviously, these are findings that strongly support consumer arbitration, not findings that impugn it.

And there are many other pro-arbitration findings in the Georgetown study. The study acknowledges that the AAA has adopted Consumer Due Process Protocols which strive for fundamental fairness. In particular, as the study admits, the AAA "attempts to safeguard consumers' interests during the arbitrator-selection process. Unless the parties have agreed otherwise, the AAA will appoint an arbitrator from its roster, task that individual with divulging potential conflicts of interest, and consider objections to her nomination." The study also "confirmed that arbitration is almost certainly faster than litigation." It found that the average fully-litigated case in federal or state court takes about two years. By contrast, the average lifespan of an arbitration in which an award was issued was eight months. 35 percent of consumers represented themselves; 32 percent chose to submit the case on the documents; and 45 percent opted for phone-only hearings.

What "repeat player" boils down to, we learn on page 65 of the 65-page study, is the proposition that the "individualization of claims" allegedly resulting from the enforcement of class action waivers in Concepcion and Italian Colors "allows high-level and super repeat-players to hone their arbitral skills and therefore flourish in bilateral arbitration." In other words, experience in arbitration matters (just as it does in court proceedings). As discussed above, the CFPB's own Study found that while almost all of the arbitration proceedings it examined involved companies with repeat experience in the forum, that was counter-balanced by the fact that counsel for the consumers were also usually repeat players in arbitration. The Georgetown study simply confirms that the whole "repeat player" debate is a tempest in a teapot. It most certainly is not a ground that would weigh in favor of CFPB regulation of consumer arbitration agreements.

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LAWMAKERS ASK WHETHER CFPB REGULATION OF ARBITRATION IS NECESSARY

What is the bottom line? Although the CFPB and the academicians put consumer arbitration under the microscope and try to reduce it to statistical formulas and regression analyses, their own data confirm that arbitration is faster, cheaper, far more effective and fairer to consumers than class action litigation. And Congress itself is taking note of this. On June 17, a group of more than 80 House and Senate Republicans sent a letter to Director Cordray asking the CFPB to reopen its arbitration study.[29]

In their letter, the lawmakers comment that the process that led to the study was not "fair, transparent or comprehensive" and that, "[a]s a result, the flawed process produced a fatally-flawed study." Echoing concerns we have expressed about the CFPB's study's deficiencies, the lawmakers observe that "[r]ather than focusing on the critical question — whether regulating or prohibiting arbitration will benefit consumers — and devising a plan to address the issues relevant to resolving that question, the bureau failed to provide even the most basic of comparisons needed to evaluate the use of arbitration agreements." The lawmakers call upon the CFPB to "reopen the study process, seek public comment, and provide the necessary cost-benefit analysis for understanding how a similarly situated consumer would fare in arbitration versus a lawsuit."

The final chapter in this struggle between consumer advocates and the consumer financial services industry over the future of consumer arbitration has yet to be written. Based upon the data in its own study, the CFPB clearly should not regulate consumer arbitration agreements. Nevertheless, on July 15, Director Cordray announced that the CFPB will be moving ahead with rulemaking on arbitration and will soon be convening a small business review panel on the issue, which is the first step in the process. If the past is prologue, any regulation of consumer arbitration agreements or prohibition of class action waivers by the CFPB is virtually certain to face stiff resistance by the consumer financial services industry when comments are solicited. Moreover, in our view, any CFPB rule prohibiting or restricting pre-dispute arbitration agreements might also be vulnerable to a legal challenge. Stay tuned!

Notes

1 131 S. Ct. 1740 (2011).

2 133 S.Ct. 2340 (2013).

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

4 For a more detailed critique of the St. John's survey, see Kaplinsky & Levin, "Some Thoughts on the St. John's School of Law's Analysis of Consumer Understanding of Arbitration Agreements," available at http://www.cfpbmonitor.com/2014/11/10/some-thoughts-on-the-st-johns- school-of-laws-analysis-of-consumer-understanding-of-arbitration-agreements/; Kaplinsky & Levin, "Further Thoughts on the St. John's Consumer Arbitration Study," available at http://www.cfpbmonitor.com/2014/11/17/further-thoughts-on-the-st-johns-consumer-arbitration-study/.

5 For a more detailed critique of the Georgetown Law Review article, see Kaplinsky & Levin, "New Empirical Study of AAA Arbitrations Is a Study in Contradictions," available at http://www.cfpbmonitor. com/2015/06/22/new-empirical-study-of-aaa-arbitrations-is-a-study-in-contradictions/.

6 See http://www.consumerfinance.gov/newsroom/cfpb-study-finds-that-arbitration-agreements – limit-relief-for-consumers/.

7 The letter was submitted by the American Bankers Association, the Consumer Bankers Association and The Financial Services Roundtable (the "Associations) on July 13, 2015. Your authors served as counsel to the Associations in connection with the letter. A link to the letter is available at http://www.cfpbmonitor.com/2015/07/14/ trade-groups-comment-on-cfpb-final-arbitration-study-results/. Your authors also served as counsel to the Associations in their submission of a comment letter responding to the CFPB's April 2012 Request for Information Regarding Scope, Methods, and Data Sources for Conducting Study of Pre-Dispute Arbitration Agreements. A link to that letter is available at Kaplinsky & Levin, "Trade Groups Comment on Final Arbitration Study Results," http://www.cfpbmonitor.com/2012/06/25/trade-groups-comment-on-cfpb-arbitration-study/.

8 Study, § 1, pp. 13-14; § 6, p. 37.

9 *Id.* § 6, pp. 7, 38.

10 The study concluded that 34 million class members received a total of $1.1 billion. Id. § 8, pp. 27-28. Interestingly, the CFPB did not do the simple long division to calculate the $32.35, perhaps because it is an embarrassingly paltry amount.

11 *Id.* § 6, pp. 9, 43; § 8, pp. 36-37.

12 *Id.* § 8, p. 30.

13 *Id.* § 5, pp. 13, 41.

14 *Id.* § 1, p. 13.

15 *Id.*, § 1, p. 13; § 4, pp. 10-11.

16 *Id.* § 8, p. 33.

[17] *Id.* § 6, p. 38 ("[a]ll claims against a company party were stayed or dismissed for arbitration in 8% of the [class] cases").

[18] *Id.* § 1, pp. 9-10; § 2, pp. 7, 9, 14.

[19] *Id.*, § 2, p. 31.

[20] *Id.* § 1, pp. 13-14; § 6, p. 37.

[21] *See* http://www.consumerfinance.gov/administrative adjudication/.

[22] *See* http://www.consumerfinance.gov/blog/category/CFPB-milestones/.

[23] Study, § 5, p. 9.

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

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

[26] Study, § 3 p. 5.

[27] *Id.* § 1, p. 12; § 5, p. 10 & n. 16.

[28] *Id.* § 5, p. 67.

[29] A link to the letter is available at Mishkin, "Lawmakers Urge CFPB to Reopen Arbitration Study," http://www.cfpbmonitor.com/2015/06/18/lawmakers-urge-cfpb-to-reopen-arbitration-study/.

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