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Re: Comment from Texas Appleseed on Docket No. CFPB-2016-0020, RIN 3170-AA51 regarding the Consumer Financial Protection Bureau's Proposed Rule Banning the Use of "No Class Action" Pre-Dispute Arbitration Agreements

Dear Ms. Jackson,

Texas Appleseed appreciates the opportunity to respond to the Consumer Financial Protection Bureau's (CFPB's) request for comments regarding the proposal to ban the use of "no class action" pre-dispute arbitration agreements published on May 24, 2016 in the Federal Register (81 Fed. Reg. 32,380-01).

Introduction

Texas Appleseed is a public interest justice center working to change unjust laws and policies that prevent Texans from realizing their full potential. Working with pro bono partners and collaborators, Texas Appleseed develops and advocates for innovative and practical solutions to complex issues. As part of its work, Texas Appleseed also conducts data-driven research to better understand inequities and identify solutions for concrete, lasting change. Texas Appleseed is part of a non-profit network of 17 justice centers in the United States and Mexico.

Through its Fair Financial Services Project, Texas Appleseed is a leader in advocating for reform of the payday and auto title lending industry in Texas and remittance laws at the state and federal level. Texas Appleseed's work is built on a commitment to transparency for consumers so they know the true cost and terms of the services they are receiving upfront. Texas Appleseed is also part of the Texas

Fair Lending Alliance, a coalition of organizations and individuals working to transform the Texas payday and auto title loan market from one reliant on consumers' being trapped in a cycle of debt to one that encourages both borrower and lender success.

Because of Texas Appleseed's expertise in payday and auto title lending as well as remittances, these comments focus on the effect a ban on prohibiting class actions in pre-dispute arbitration agreements would have for consumers in these sectors. Texas Appleseed supports an expansive rule that pulls in consumers from across the financial products and services market. The following comment covers the ability of class actions to remedy harms within the financial products and services market as well as many of the flaws in the private arbitration system. The comment concludes by highlighting areas where it is necessary to strengthen the proposed rule.

Importance of Ensuring Consumer Access to Class Actions with Respect to Financial Products and Services

Arbitration agreements were historically used to settle commercial disputes between companies, often similarly positioned entities.¹ These companies negotiated arbitration agreements as a mutually preferable alternative to litigation. During the last two decades of the 20th century, companies began using arbitration agreements in contracts, often form contracts that were not negotiated, with consumers, employees, investors, and franchisees. This tactic allows companies to block litigation—both individual and class action lawsuits—from a wide range of parties. Since the 1990s, the use of arbitration agreements in consumer contacts for financial products and services has become commonplace.

In the consumer lending industry in Texas, almost all contracts for payday and auto title loans have an arbitration agreement that borrowers are required to sign to apply for a loan. Most contracts also include a ban on class actions; some include other provisions such as limits on available damages or waivers to jury trials. Given the flaws inherent to the arbitration system outlined in this comment and the ability of class action lawsuits to remedy harms and incentivize better practices, Texas Appleseed supports ensuring class action lawsuits are available to consumers by preventing companies from banning them through pre-dispute arbitration agreements.

Class actions are a valuable tool for consumers where the economic value of a company's harms individually are small, but touch a large number of consumers. By joining similarly situated plaintiffs, class actions can motivate companies to admit their misdeeds and change their practices. Even the threat of class actions can go far in policing companies' behavior because of the potential cost to companies.

Under current arbitration agreements with class action bans, some companies find ways to skirt the laws without much accountability due to the hurdles plaintiffs face in pursuing companies through arbitration. Customers of financial services, such as remittances, as well as financial products, such as payday and auto title loans, are precisely the type of plaintiffs who would benefit from the ability to pursue a class action lawsuit, because the dollar value of the associated individual claims

¹ 81 Fed. Reg. 32,830-01 (May 24, 2016) at 21-23.

is often insufficient to justify the potential costs of arbitration or litigation. The examples below highlight one instance where a class action helped consumers and one where the payday loan businesses succeeded in using their pre-dispute arbitration agreements as both a sword and a shield.

1. Justice Delivered: Remittances and Class Actions

The following class action filed on behalf of millions of consumers changed the practices of two of the largest providers of international remittances. In 1999, MoneyGram, Western Union and Orlandi Valuta settled class-action lawsuits filed against them in Illinois, Texas, and California alleging they overcharged customers wiring money to Mexico over an almost ten-year period.² Specifically, the lawsuits concerned the companies' practice of earning substantial profits by using unfavorable foreign exchange rates without disclosing the rates to consumers.³ The companies settled with the plaintiffs, agreeing to give discount coupons to former customers and contribute \$4.6 million to a community fund.⁴ In addition, they agreed to disclose information on profits earned from foreign exchange rates in the future.⁵

Without this class action, consumers and the public may never have learned of this hidden practice, and consumers may not have had the opportunity to obtain restitution. There were a large number of people affected by the defendants' practices. In fact, at least 13 million people were potential plaintiffs in the lawsuit; however, due to the high mobility of the largely immigrant population at least 40 percent of letters sent to potential plaintiffs were returned to sender.⁶ Some observers criticized the settlement as too favorable for the defendants because the discount coupons—one \$6 coupon or two \$4 coupons—guaranteed repeat business for the defendants.

The suit might not have resulted in as large of a payout as some advocates wanted, but it was able to bring these unscrupulous practices to light and correct them for the entire market moving forward, while also securing restitution for consumers. After this settlement, companies across the international remittance market adopted the practice of disclosing exchange rates at the front end of the transaction, so customers could effectively compare prices to all destinations where exchange rate information could be made available, not just Mexico. The move towards transparency that resulted from this lawsuit coincided with a drop in total cost to send international remittances across different markets.⁷ And these beneficial results were all due to the class action tool.

² Migration News, *Mexico: Remittances*, Vol. 6 Num. 6 (June 1999), available at <https://migration.ucdavis.edu/mn/more.php?id=1823>.

³ Lee Romney, *Court Clears Cash-Wiring Settlement*, Los Angeles Times (Oct. 10, 2001), available at <http://articles.latimes.com/print/2001/oct/10/business/fi-55435>.

⁴ *Id.*

⁵ *Id.*

⁶ *Id.*

⁷ According to a June 2004 study, the cost to send \$200 to Mexico dropped from 13% of the amount sent to 7.32% of the amount sent over the years from 2000 to 2004. See Manuel Orozco, *The Remittance Marketplace: Prices, Policy, and Financial Institutions*, 11 Pew Hispanic Center (June 2004).

2. Justice Denied: Illegal Filing of Criminal Charges Against Payday Borrowers

A 2013 news story uncovered that payday loan businesses⁸ in Texas were using “bad check” or “theft by check” charges as a debt collection tool, in contravention of both the letter and spirit of state criminal law⁹ and state and federal fair debt collection laws.¹⁰

When taking out a payday loan, most payday loan businesses require borrowers provide a post-dated check or debit authorization to withdraw funds from their account. If a customer cannot pay when the loan is due, some businesses try to collect by illegally filing “bad check” charges with local prosecutors, in effect using the Texas court system as a “de facto collection agenc[y].”¹¹ Payday loan businesses engage in this practice despite state laws that forbid them from even threatening to pursue criminal charges against payday borrowers, except in limited instances, such as when the business can prove the borrower is guilty of fraud or forgery.¹² This pursuit of borrowers through the criminal court system often occurs even when the borrower has paid well over the amount borrowed through fees and interest charges.

Following the news report, Texas Appleseed submitted open records requests to a number of district and county attorneys across the state. The open records requests found approximately 1,500 instances of criminal complaints filed by 13 payday loan businesses where a borrower was charged with bad check or theft by check charges or where a district attorney’s office sent the borrower a notice to pay on behalf of a payday loan business.¹³

⁸ In Texas, payday lenders are classified as Credit Access Businesses (CABs) under the Texas Finance Code Section 393. Throughout this comment, the term payday lenders is used to refer to CABs.

⁹ See Tex. Fin. Code §§ 393.001 & 393.601. The Credit Services Organizations Act was passed in 1987, in order to rein in abuses by credit repair businesses. It is under Title 5 of the Texas Finance Code, “Protection of Consumers of Financial Services.” Starting in 2005, payday and auto title lending businesses moved, en mass, from licensing as consumer lenders, under Chapter 342 of the Texas Finance Code, to registration as credit services organizations (CSOs). As CSOs, these businesses can arrange loans “by others” in partnership with third-party lenders that lend under the 10% constitutional usury cap. This system enables these businesses to get around rate and fee caps for consumer loans because the fees charged by CSOs are uncapped. In 2011, in the 82nd Texas Legislative Session, HB 2594 created the credit access business designation (CAB) and required licensing by the Texas Consumer Credit Commissioner as a first step to better understand use of the CSO model by payday and auto title businesses. The new law went into effect on January 1, 2012. All CABs must also be registered as a CSO. Cash Biz was a registered CSO prior to the adoption of HB 2594 and obtained a CAB license after the law went into effect on January 1, 2012.

¹⁰ Forrest Wilder, *Fast Cash: How Taking Out a Payday Loan Can Land You in Jail*, Texas Observer (Jul. 16, 2013), available at <https://www.texasobserver.org/cash-fast-how-taking-out-a-payday-loan-could-land-you-in-jail/>.

¹¹ *Id.*

¹² See Forest Wilder, *Report: Texas Payday Lenders and Prosecutors Team Up to Criminally Pursue Borrowers*, Texas Observer (Dec. 17, 2014), available at <https://www.texasobserver.org/report-texas-payday-lenders-prosecutors-team-criminally-pursue-borrowers/>.

¹³ Letter from Texas Appleseed to Director Richard Cordray, et al. (Dec. 17, 2014), available at <https://www.texasappleseed.org/sites/default/files/Complaint-CriminalCharges-PaydayBusinesses-Final2014.pdf>. The data requests were limited to complaints and cases filed between January 1, 2012 and dates in the spring of 2014 (the date each records request was filed) due to a Texas law change that went into effect on January 1, 2012, further clarifying that credit access businesses (Texas licensing designation for payday and auto title loan businesses) may not pursue criminal charges for nonpayment except in cases of clearly established fraud.

Collin County, a north Texas county, documented over 700 criminal complaints related to a defaulted payday loan, collecting over \$131,000 from 204 individuals.¹⁴

In a court in Harris County, in the Houston area, arrest warrants were issued in more than 42 percent of the bad check cases filed based on criminal complaints from a payday loan business, and at least six people served jail time because they could not pay fines and court costs along with the money owed on the loan.

To make matters worse, even after filing criminal complaints in contravention of state law, payday loan businesses then attempted to use the arbitration agreements in their contracts with consumers to protect them from any liability in court surrounding the illegal pursuit of criminal charges. Two class action lawsuits were filed—against PLS Loan Store and CashBiz—alleging malicious prosecution, violations of the Texas Deceptive Trade Practices Act, fraud, and violations of the Texas Finance Code.¹⁵ Each of the lower courts ruled in favor of the plaintiffs, asserting the companies waived their ability to force arbitration when they pursued borrowers through the criminal courts.

Both courts noted the specific role of the payday loan businesses in initiating the bad check charges against borrowers. Despite the strong presumption against finding a waiver of arbitration, the El Paso district court found the payday loan businesses “sought to gain a significant benefit by engaging the criminal justice system. . .[and] are not afforded a ‘second bite at the apple’ through arbitration.”¹⁶ The appeal of this decision is pending in the Fifth Circuit, while the Fourth Court of Appeals in San Antonio, Texas, sided 2-1 with the defendants, forcing the plaintiffs to arbitrate and breaking up the class.¹⁷ The Fourth Court of Appeals focused its analysis on the payday loan business’ conduct *after* filing suit, finding that “they were insufficient to rise to the level of ‘substantial invocation’ of a litigation process” despite noting that the payday loan business’ actions were “presumably vindictive.”¹⁸ Further, the majority opinion stated that it did not consider Cash Biz’s complaints to the district attorney as indicative of its desire to obtain repayment of the loans through the criminal process. The dissenting opinion in the Fourth Court of Appeals’ decision takes issue with all of these points—arguing that the analysis should not be limited to actions taken after the filing of the lawsuits and that the evidence showed Cash Biz used the criminal court process to collect money from borrowers.¹⁹

To date, these suits have not considered the merits of the cases, leaving the individual harms to the plaintiffs caused by the defendants’ egregious business practices unaddressed, as the effort continues to simply give the plaintiffs their fair day in court. If the new rules from the CFPB had been in effect at the time of these loan contracts, these suits would have been permitted to proceed on the merits as class actions.

¹⁴ *Id.*

¹⁵ See *Vine et al. v. PLS Financial Services, Inc.*, EP-16-CV-31-PRM (W.D. Tex. Jun. 6, 2106); *Henry v. Cash Biz LP*, Cause No. 2015C101545 (San Antonio—224th Jud. Dist. 2016).

¹⁶ See *Vine et al.*, at 17.

¹⁷ See *Cash Biz LP v. Henry*, No. 04-15-00469-CV (Tex. App.—San Antonio 2016).

¹⁸ *Id.* at 15.

¹⁹ See *Cash Biz LP v. Henry*, No. 04-15-00469-CV at 4 (Tex. App.—San Antonio 2016) (dissenting).

The ability of the payday loan businesses to use arbitration agreements as both a sword and a shield is noteworthy, especially since the businesses' initiated the wrongfully filed criminal charges against borrowers by bringing the cases to prosecutors. Further, without the ability to pursue these grievances as a class action and in court, the lawsuits lose their muscle. The ban also blocks beneficial market-wide impacts of class action lawsuits to end unconscionable practices. Individual claimants are left to shoulder the burden of finding and paying an attorney individually while the companies shed much of the liability that could have ensued from a class action for their widespread harmful practices.

Arbitration: A Flawed System for Resolving Consumers' Disputes

Proponents of arbitration claim it gives individuals an easier way to handle disputes, but the evidence reviewed by Texas Appleseed indicates the opposite is true. Because it can be difficult to evaluate some aspects of arbitration given the secretive nature of the process, Texas Appleseed spoke with lawyers who have arbitrated cases and/or struggled to bring a case in court due to arbitration provisions. In addition, Texas Appleseed examined 13 payday and auto title loan contracts from various businesses, executed from 2010 to 2016. Every contract contained a class action ban; ten of the contracts also included bans on class arbitration.

Of particular note is the structure and use of opt out provisions, allowing the borrower to opt out of the arbitration clause. Twelve of the 13 contracts included opt out language. Opt out provisions are overly burdensome and offer only a facade of an equalized playing field. Consumers often never learn about them, because they are included in fine print among the many pages of a contract. In the event a consumer tries to opt out of the arbitration agreement, the process for opting out often creates a repeated burden, requiring consumers send official letters for each bi-weekly loan or other small and often repeating transaction. Additionally, it is common for consumers to approach financial product and service transactions with an assumption that the business is operating legally. Only after it is too late, after harmful practices have occurred, do many people even think about possible legal remedies.

So, consumers sign on the dotted line not realizing that they are signing away their right to an impartial judge or jury with certain procedural and evidentiary standards. Not only do they lose the practical ability to appeal an adverse decision as described below, but they also cannot join other consumers to bring a class action suit or even a class arbitration against a company for unfair practices that individually might be difficult, if not impossible, to litigate. Borrowers are left without access to courts or the ability to band together and increase the potency and impact of their claims, either through a class action or class arbitration. Because of the many challenges of arbitration detailed in this section, lawyers spend a lot of time trying to get around arbitration clauses, without getting to the merits of the case.²⁰ For consumers, this process often means delayed or denied access to justice.

The following evaluation of the arbitration system and how well it serves consumers of financial products and services is drawn from Texas Appleseed's research and interviews with attorneys. The deficiencies highlighted below tilt the scales of justice towards businesses, which are not only

²⁰ Interview with Tracey Whitley, lawyer with Texas Rio Grande Legal Aid (Jul. 6, 2016).

more familiar with arbitration clauses (often hiring sophisticated lawyers to design them) than consumers of financial services, but also are repeat players in arbitration proceedings, giving them increased familiarity with individual arbitrators.

1. Secretive System Limits Accountability

Arbitration decisions are not public; in fact, the outcome of cases and the reasons behind those outcomes are considered confidential.²¹ This lack of even the most basic information keeps arbitration shrouded from any public scrutiny or accountability. Given real concerns over inherent bias within arbitration proceedings, this secrecy is even more troubling. The federal government does not currently require cases that go to arbitration to be reported in any manner.²²

It is worth mentioning that California and Maryland require online, quarterly publication of arbitration outcomes by arbitration companies with information about the dispute and its outcome.²³ Texas Applesed examined this data from the American Arbitration Association (AAA) and JAMS, but found the inconsistencies and incomplete fields make it difficult to use the data as a meaningful tool to assess case outcomes.²⁴

The procedure by which an arbitrator arrives at a decision is also usually secret—this secretive aspect is in direct contrast to courts, where the public record of the proceeding, such as which evidence is admissible, as well as myriad other trial decisions, can be challenged in court. Also, unlike court cases, where decisions could be reported on in a local newspaper or on the radio, arbitration decisions are entirely out of the public eye. Public scrutiny can have a real deterrent effect; without it, companies might not be as concerned with skirting the rules.

In addition to the secrecy of the process, arbitration outcomes do not set precedent. Precedent is the underpinning of our legal system in that it ensures that similar facts produce similar outcomes. Judges are bound to follow precedent under *stare decisis*; however, in arbitration, arbitrators are not held to follow precedent. Decisions in arbitration are left to arbitrators themselves.

2. Appealing an Adverse Arbitration Decision is Almost Impossible

The Federal Arbitration Act (FAA) significantly limits the ability to appeal an arbitration decision.²⁵ Reversing an arbitration award under the FAA is restricted to instances where there is serious fraud or misconduct by arbitrators.²⁶ Even assuming the parties can afford

²¹ National Consumer Law Center, *Forced Arbitration: Consumers Need Permanent Relief*, 6 (2010).

²² Jessica Silver-Greenberg & Michael Corkery, *In Arbitration, a 'Privatization of the Justice System'*, N.Y. TIMES, Nov. 1, 2015, available at http://www.nytimes.com/2015/11/02/business/dealbook/in-arbitration-a-privatization-of-the-justice-system.html?_r=0.

²³ Cal. Code of Civil Procedure §1281.96 (2015); MD Comm. L. Code §§14.3901-3905 (2013).

²⁴ For example, one data field was “Prevailing Party” but for a large percentage of the fields, including those cases where the outcome was “Awarded” (not just those that “Settled”), the field simply had a “---.”

²⁵ See 9 U.S.C. §10(a).

²⁶ *Id.*

to appeal a decision, to consider an appeal of an arbitration decision, a court must have a record to examine.²⁷ As detailed below, arbitration is expensive, particularly for parties with relatively smaller harms and fewer resources such as payday loan borrowers. Unless the parties are willing to pay for it, most arbitration proceedings do not have a transcript taken by a court reporter.²⁸ To have a record costs more money, which may not be feasible.

In addition, arbitrators also often only issue a “standard award” which simply recites which party won along with any damages and costs.²⁹ In contrast, a “reasoned award” requires arbitrators to spend more time issuing their decision, thereby adding to the parties’ expense. In addition, at least under the AAA’s rules, the arbitrator cannot be called as a witness in litigation for any proceeding related to the arbitration of the parties.³⁰

Most of the time parties in arbitration are “stuck with whatever comes out of arbitration” and “often the arbitrator will split the baby. . . give a little bit to each side.”³¹ This situation can be especially frustrating for plaintiffs when the arbitrator does not follow the law, something that appellate courts have said is not in itself grounds for reversal.³²

3. Bias within the System

While the extent of any bias on the part of arbitrators can be difficult to assess given the secretive aspects of the system, a 2015 investigation of arbitration by the New York Times found evidence of bias. In addition, there is significant anecdotal evidence that arbitration favors defendants.

The investigation by the New York Times was based on thousands of court records and interviews with hundreds of lawyers, corporate executives, judges, arbitrators and plaintiffs in 35 states. The paper found the scales of justice were slanted towards defendants at least in keeping class actions out of court.³³ The Times evaluated this issue by examining federal cases filed from 2010 until 2014 and found that of the 1,179 class actions that companies sought to push into arbitration, judges ruled in their favor in four out of every five cases. Once blocked from going to court as a group, most people dropped their claims entirely. This last finding speaks to the facts explored in this comment that pursuing a claim in arbitration is expensive and finding a lawyer is extremely difficult, leaving many potential plaintiffs with legitimate claims stranded.

²⁷ *Physicians Insurance Capital v. Praesidium Alliance Group*, 562 F. App’x 421 (6th Cir. 2014).

²⁸ American Bar Association, *Appealing Arbitration Decisions: Practice Tips for Young Lawyers* (Sept. 5, 2014), available at <http://apps.americanbar.org/litigation/committees/adr/articles/summer2014-0914-appealing-arbitration-decisions-practice-tips-young-lawyers.html>.

²⁹ *Id.*

³⁰ *Consumer Arbitration Rule R-49(e)*, American Arbitration Association, available at <https://www.adr.org/aaa/ShowProperty?nodeId=/UCM/ADRSTAGE2021425&revision=latestreleased>.

³¹ Interview with Dugan Kelley of Christman, Kelley & Clarke P.C., Jul. 19, 2016.

³² *Id.*

³³ Jessica Silver-Greenberg & Robert Gebeloff, *Arbitration Everywhere, Stacking the Deck of Justice*, N.Y. TIMES, Oct. 31, 2015, available at <http://www.nytimes.com/2015/11/01/business/dealbook/arbitration-everywhere-stacking-the-deck-of-justice.html>.

In the New York Times' interviews, more than "three dozen arbitrators described how they felt beholden to companies" because with every decision came "the threat of losing business."³⁴ All of the lawyers interviewed for this comment agreed that too often arbitrators seem inclined to appease the defendants. As one lawyer said, "Arbitrators like to have business and make a lot of money arbitrating cases, if you are chosen by a car dealership, you want to make the car dealership happy."³⁵ Also implicit is that arbitrators are used to having multiple cases from the same defendants.

When the process for choosing an arbitrator is not specified in the parties' contract, JAMS provides each party with three candidates.³⁶ Each party then ranks the names with the ability to strike up to one name from the list. The first one or two that both parties agree on are then appointed as the arbitrators.³⁷ Once selected, the choice of the arbitrator cannot be appealed. AAA selects the arbitrator from its list of approved arbitrators; if one side objects to the service of a particular arbitrator, AAA will consider that party's objections in weighing whether to disqualify the arbitrator.³⁸ The grounds for disqualification include an issue of partiality or lack of independence; inability or refusal of arbitrator in performing his or her duties with diligence and in good faith or any grounds for disqualification provided by applicable law.³⁹ However, the AAA has total discretion in this decision. In a court, if a plaintiff feels that a judge is not impartial or seems inclined to the opposing side, the plaintiff can request a jury trial. In arbitration, there is no right to a jury. This restriction limits the plaintiff and creates an advantage for the defendant.

In most of the contracts from payday and auto title loan businesses, the selection of the arbitrator is governed by the rules of the particular association listed in the contract. Many contracts also included specific waivers of the constitutional right to a jury, as part of the arbitration agreement, and also separate and apart from the arbitration agreement.⁴⁰

4. Strict Limits on Discovery

One of the perceived benefits of arbitration to corporations is minimizing the cost of discovery, which can be expensive. The FAA is largely silent on discovery and simply lays out an arbitrator's ability to summon witnesses.⁴¹ In arbitration agreements, parties can elect to apply various rules of discovery, such as the arbitration organization's rules or pre-agreed upon discovery terms. Most often, discovery is left up to the arbitrator, who

³⁴ Jessica Silver-Greenberg & Michael Corkery, *In Arbitration, a 'Privatization of the Justice System'*, N.Y. TIMES, Nov. 1, 2015, available at http://www.nytimes.com/2015/11/02/business/dealbook/in-arbitration-a-privatization-of-the-justice-system.html?_r=0.

³⁵ Interview with Daniel Dutko, lawyer with Hanszen Laporte (July 5, 2016).

³⁶ JAMS, *Streamlined Arbitration Rule 12*, available at <https://www.jamsadr.com/rules-streamlined-arbitration/#Rule12>.

³⁷ *Id.*

³⁸ AAA, *Consumer Arbitration Rules* 18,19, available at <https://www.adr.org/aaa/ShowProperty?nodeId=/UCM/ADRSTAGE2021425&revision=latestreleased>.

³⁹ *Id.*

⁴⁰ 2016 Advance America Consumer Contract. See Supplemental Resource on p.15 of this document for an overview of the contracts reviewed.

⁴¹ 9 USC Section 7.

determines the scope and amount of discovery. For example, JAMS gives arbitrators factors to consider when outlining discovery, but ultimately leaves the decision to the “good judgment of the arbitrator.”⁴² Similarly, the AAA states in its rules for arbitration that the arbitrator has full discretion on “what evidence will be admitted, what evidence is relevant, and what evidence is material to the case.”

Such uncertainty and discretion can lead to mixed results. One lawyer arbitrating a case against a payday loan business in Texas requested a store manager or employee as the witness.⁴³ Instead of bringing someone who interacted with customers regularly, the business brought a regional manager who could not attest to the alleged store level violations. The arbitrator only allowed one witness per side and insisted that the witness was sufficient despite the lawyer’s objections, leaving the borrower without a way to prove the allegations. By overly limiting discovery, the borrower’s ability to argue her case was severely hampered.

Further, as another lawyer pointed out, discovery would help uncover more on how the businesses operate and what additional harms they might be promulgating.⁴⁴ Or as one lawyer put it, “without discovery, it is harder to show how bad they really are . . . without discovery, you only have open records requests.”⁴⁵ One lawyer noted that his request for audit reports of certain payday loan businesses from the state regulator, the Texas Office of the Credit Consumer Commissioner (OCCC), was denied by the arbitrator. The audit reports would have provided an objective look at the company’s violations.

5. High Cost and Difficulty Finding Counsel for Cases in Arbitration

There are two ways that the high cost of arbitration keeps plaintiffs from pursuing their cases in arbitration. First, arbitration can be expensive and many plaintiffs cannot afford to access or take the risk of having to pay for arbitration (depending on the contract and the arbitration provider, the defendant may foot part of the bill for arbitration). Second, given the high cost along with the perceived or real low chance of success, plaintiffs often cannot find attorneys to take cases that have restrictive arbitration clauses, particularly if they are seeking relatively small amounts of damages, as is the case with payday loan borrowers.

Often, businesses will cover the cost of arbitration upfront. Covering the costs of arbitration is a strategy used by businesses to avoid the invalidation of an arbitration agreement on the grounds of unconscionability.⁴⁶ However, responsibility for payment of the fees can be conditional on the outcome. In several contracts reviewed, the business agrees to advance the fees, but the consumer must reimburse the fees if the arbitrator rules

⁴² JAMS, *JAMS Arbitration Discovery Protocols* 3, available at https://www.jamsadr.com/files/Uploads/Documents/JAMS-Rules/JAMS_Arbitration_Discovery_Protocols.pdf.

⁴³ At the request of the lawyer, her name and identifying information has been withheld.

⁴⁴ Some contracts maintain borrowers’ ability to pursue an action in small claims court, but there is no automatic right to conduct discovery in small claims court. If discovery is granted, it is often very limited, especially in comparison to the available discovery in county, district, or federal court. Further, there is no ability to bring class actions in small claims court.

⁴⁵ Interview with Daniel Dutko, lawyer with Hanszen Laporte (Jul. 5, 2016).

⁴⁶ Interview with Rich Tomlinson, lawyer with Lone Star Legal Aid (Jul. 6, 2016).

in favor of the business.⁴⁷ In at least one instance, for the company to cover the fees the borrower has to recover more than the settlement amount offered by the business prior to arbitration.⁴⁸ In other contracts, the arbitration fees the borrower has to pay are limited to the costs of filing the action in state court.⁴⁹

If the arbitration is conducted by JAMS or AAA, there are maximum amounts for which consumers are financially responsible.⁵⁰ These amounts are similar to what a consumer would pay to file a case in small claims court. Should the parties choose to use a local judge or other party to arbitrate the case, there are no rules governing that person's fees. In those instances, arbitration fees can quickly mount. Similar to court, where a party unable to pay to file a case can apply for a fee waiver, at least AAA has a process whereby a consumer can appeal for a waiver.⁵¹

However, the fee arrangement is only one part of the expenses in arbitration. Attorney fees, witness expenses, and other costs are all significant. Notably, all 13 of the payday and auto title contracts reviewed for this comment stated that each party was responsible for its own attorney fees, expert fees, and other expenses.⁵² These expenses can be significant and some may not be transparent from the beginning of the process. For example, AAA charges extra fees for use of a hearing room.

Given the unpredictability of the cost of the arbitration process as well as the risks of a biased arbitrator, many plaintiffs' attorneys are unwilling to take cases to arbitration. For lawyers who could potentially represent payday and auto title borrowers, "[arbitration] doesn't make sense for a small case, especially if the lawyer does not think the arbitrator is going to award a reasonable amount."⁵³ As a result of these barriers, arbitration clauses often stand in the way of justice.

Without an attorney, borrowers are at a significant disadvantage. The difficulties in finding legal counsel willing to take consumer arbitration is compounded by the decreasing trend of the number of lawyers representing consumers, an issue identified by several lawyers interviewed. "If we only have legal aid lawyers and the attorney general pursuing suits that mandate arbitration, then a lot of people won't be helped and market will become more like the Wild West."⁵⁴ Legal aid lawyers can afford to take a case, even if arbitration is the only avenue, because their paychecks are not dependent on the outcome of the case. Allowing class actions might incentivize more lawyers to take consumer cases, leaving

⁴⁷ See Supplemental Resource on p.15 of this document for an overview of the contracts reviewed.

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ See JAMS, *Consumer Minimum Standards* (eff. Jul. 2009), available at <https://www.jamsadr.com/consumer-minimum-standards/>; AAA, *Consumer Arbitration Rules: Costs of Arbitration* (eff. Jan. 2016).

⁵¹ Texas does not have a law requiring arbitrators provide fee waivers. Under California law, both JAMS and AAA provide fee waivers for consumers living under 300% of the Federal poverty guideline. Cal. Code of Civ. Pro. Sec. 1284.3.

⁵² *Supra* note 47.

⁵³ Interview with Daniel Dutko, lawyer with Hanszen Laporte (Jul. 5, 2016).

⁵⁴ Interview with Rich Tomlinson, lawyer with Lone Star Legal Aid (Jul. 6, 016).

fewer consumers stranded, with no recourse for illegal, harmful or abusive market practices.

In conclusion, arbitration is supposed to function as an alternative forum where plaintiffs can raise all of the claims provided by law, but the effect is that many arbitration agreements simply shave away consumer rights.

Areas Where Rule Should be Strengthened

Based on the evidence cited in this comment, Texas Appleseed believes that eliminating class action bans in pre-dispute arbitration agreements will have beneficial impacts for consumers of financial products and services and support legal and conscionable business practices in the market. Texas Appleseed also supports the rules' provisions for data collection. However, the rules can be stronger in specific places to bolster consumers' access to justice.

1. The CFPB should prohibit forced individual arbitration.

The preceding section details the many flaws in the arbitration that result in the inability of consumers to receive a fair consideration of their claims. Customers of financial products are often presented with pages of small print in which the arbitration agreements are buried. They are often unaware of the full impact of accepting these agreements, until they go to contest a company's practice or policy and are forced into arbitration.

Forced arbitration is a problem for both individuals and class actions cases and should be prohibited in both instances. The CFPB's ban should be extended to include pre-dispute arbitration agreements for individuals.

2. Companies should report all uses of forced arbitration to the CFPB, not just cases that result in an arbitration proceeding.

Once a court compels arbitration, consumers may feel compelled to settle on weak terms or dismiss their case. It is possible that the mere threat of arbitration has a chilling effect on consumers challenging harmful market practices. Reporting on the settlements that occur before arbitration as well as instances where consumers abandon their claims should also be included in the CFPB's rules. Such information is necessary to provide a complete picture of the effects of pre-dispute arbitration agreements in contracts.

3. Credit reporting, credit repair, lead generators, and personal finance apps should be fully covered.

The rule should be expanded to fully cover credit bureaus and credit repair providers, both of which have been the subject of numerous consumer complaints to the CFPB. Lead generators should also be covered as well as personal finance apps; both services leave consumers vulnerable to the misuse of their sensitive bank and personal information. This

misuse can occur from data breaches and unauthorized charges, but also the sale of their personal information to future parties. Further, lead generators should be fully included, not just when they provide leads for credit. Consumers of these products should not be left out of the rule's protections.

4. If agreements are amended after the rule's effective date, they should be included in the rule.

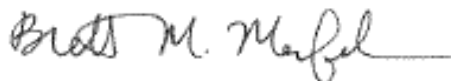
The rule should also apply to contracts and existing arbitration clauses that are modified, amended, or renewed after the rule is in effect, not only to contracts entered into after its effective date. For example, credit cards and bank accounts should be subject to the rule if the agreement is amended after the effective date. Not doing so could keep these entities exempt from the rule for decades, even while banks retain the right to amend the contracts unilaterally.

Texas Appleseed is grateful for the CFPB's efforts to protect consumers and hopes that these rules are the first step in protecting all consumers of financial products and services from forced arbitration.

Sincerely,



Ann Baddour
Director of Fair Financial Services Project



Brett M. Merfish
Staff Attorney

Supplemental Resource:
Overview of Payday Loan Contract Arbitration Clauses

Contract Data

Credit Access Business (CAB) Name	Third Party Lender	Year	Process for Opting Out of Arbitration Provision? (Yes/No)	Notes on process to opt out?	Separate Jury Trial Waiver? (Yes/No)	General Class Action Ban? (Yes/No)	Specific Ban on Class Arbitration? (Yes/No)	Fees Arrangement (Yes/No)	Notes on Fee Arrangement	Arbitration Company Listed? (Both AAA and JAMS, Both w. option to choose a local arbitrator)	Allow Small Claims Court? (Yes/No)	Notes
ACE	Bastion Funding Tx LLC	2016	Yes	Must opt out every time have a "transaction" or new loan contract and must sent a separate letter within 30 days of each	Yes	Yes	Yes	Yes	ACE will pay reasonable fees and costs, attorneys and witness costs, but only if ACE loses.	Both AAA and JAMS	No	Two pages single spaced covering arbitration, noting that the decision of arbitrator is final and binding except for appeals under the FAA or claims exceeding 50K (those exceeding 50K will be appealed to panel of 3 arbitrators).
ACSO of Texas	NCP Finance	2012	Yes	Must opt out by sending written letter within 30 days	Yes	Yes	No	Yes	ACSO will advance fees regardless, but if lose or withdraw then have to reimburse what would have cost to file in state court less any already paid expenses.	Both w. option to choose a local arbitrator	Yes	
Advance America	Bastion Funding Tx LLC	2016	Yes	Must opt out every time have a new loan contract and must sent a separate letter within 30 days of contract	Yes	Yes	No	Yes	Advance America will pay the arbitrator's fees and any other expenses imposed by the arbitration provider. If borrower recovers an award of monetary or equitable relief greater than the amount offered to settle the case prior to arbitration, then AA will pay reasonable attorney's fees.	"Nationally recognized provider of arbitration services"	Yes	
Cash America	NCP Finance	2011	Yes	Must opt out by sending written letter within 60 days	Yes	Yes	Yes	Yes	Cash America will pay arbitration fees regardless of outcome but not other expenses	Both w. option to choose a local arbitrator	Yes	
Cash America	Willshire Consumer Credit	2011	Yes	Must opt out by sending written letter within 60 days	Yes	Yes	Yes	Yes	Only will pay fees for borrower if borrower prevails.	Both w. option to choose a local arbitrator	Yes	
Check-n-Title Finance	RMI Capital	2015	Yes	Must opt out by sending written letter within 15 days	Yes	Yes	Yes	Yes	If requested in writing, Check n Title will consider paying the costs of arbitration, but not the other party's expenses.	Both w. option to choose a local arbitrator	No	Specifically notes that there is a new arbitration agreement with each rollover of the loan.
EZ Loan	Integrity Funding Texas	2010	No	N/A	Yes	Yes	No	Yes	EZ will pay arbitration fees but each side pays own expenses.	Both w. option to choose a local arbitrator	Yes	
Loan Star	Integrity Funding Texas	2011	Yes	Must send written letter within 25 days	Yes	Yes	Yes	Yes	If cannot pay fees, can ask lender in good faith for assistance. Regardless, must pay attorney and witness expenses and specifically notes that leaves open right of either party to recover fees from the other party under applicable law.	Both w. option to choose a local arbitrator	Yes	
The Cash Store	TreeMac Funding Group LLC	2011	Yes	Must opt out by sending written letter within 60 days	Yes	Yes	Yes	Yes	Cash Store will pay arbitration fees if plaintiff demands arbitration and requests it, regardless of whether the plaintiff wins or loses, but each party must pay attorney fees and expenses.	Both w. option to choose a local arbitrator	Yes	Party can file in small claims court but appeal from small claims court must be resolved in binding arbitration.

Contract Data

Credit Access Business (CAB) Name	Third Party Lender	Year	Process for Opting Out of Arbitration Provision? (Yes/No)	Notes on process to opt out?	Separate Jury Trial Waiver? (Yes/No)	General Class Action Ban? (Yes/No)	Specific Ban on Class Arbitration? (Yes/No)	Fees Arrangement (Yes/No)	Notes on Fee Arrangement	Arbitration Company Listed? (Both AAA and JAMS, Both w. option to choose a local arbitrator)	Allow Small Claims Court? (Yes/No)	Notes
The Cash Store	TreeMac Funding Group LLC	2012	Yes	Must opt out by sending written letter within 60 days	Yes	Yes	Yes	Yes	If requested, the Cash Store will pay all the costs of arbitration, but not the other party's expenses	Both w. option to choose a local arbitrator	Yes	
The Cash Store	TreeMac Funding Group LLC	2015	Yes	Must opt out by sending written letter within 60 days	Yes	Yes	Yes	Yes	The Cash Store will pay arbitration fees if requested to do so.	Both AAA and JAMS	Yes	
The Money Store/Speedy Cash	SGS Finance	2013	Yes	Must opt out by sending written letter within 45 days	Yes	Yes	Yes	Yes	The Money Store will advance fees regardless, but if lose or withdraw then have to reimburse what would have cost to file in state court less any already paid expenses.	Both w. option to choose a local arbitrator	Yes	
Title Max	NCP Finance	2013	Yes	Must opt out every time have a new loan contract and must sent a separate letter within 30 days of contract	Yes	Yes	Yes	Yes	Title Max only covers arbitration fees if claimant wins, fees are limited to the amount the initiating party would have paid in state court.	Both w. option to choose a local arbitrator	Yes	If award exceeds 25K, can appeal to arbitrator or three arbitrator panel, they will pay cost of an appeal unless claimant wants a panel then claimant would have to pay difference.