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Advocates for Government Accountability
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BEFORE THE
CONSUMER FINANCIAL PROTECTION BUREAU

Washington, D.C.

Proposed Rule: Arbitration Agreements	)	**Docket No. CFPB-2016-0020**
	)	**RIN 3170-AA51**

COMMENT OF CAUSE OF ACTION INSTITUTE

August 17, 2016

I. Introduction

Pursuant to Section 553(c) of the Administrative Procedure Act ("APA"), Cause of Action Institute ("CoA Institute") hereby submits this Comment on the Consumer Financial Protection Bureau's ("CFPB") Arbitration Agreements rule ("Arbitration Rule").[1]

CoA Institute is a nonprofit, nonpartisan, strategic oversight group committed to ensuring that government decision-making is open, honest, and fair. In carrying out this mission, CoA Institute uses strategic litigation and investigative tools to hold government accountable and educate the general public about the importance of government transparency and accountability.

Section 1028 of Dodd-Frank mandated that CFPB conduct a study concerning "the use of agreements providing for arbitration of any future dispute between persons and consumers" relating to financial products and services.[2] Dodd-Frank further grants CFPB the authority to promulgate an arbitration rule, provided that "[t]he findings in such rule shall be consistent with the study[.]"[3] CFPB's resulting Arbitration Study[4] fails to meet the requirements of peer review and the required standards of the Information Quality Act ("IQA") that governs all federal studies of this kind. Accordingly, CFPB must delay this Arbitration Rule until a proper study, complete with peer review

[1] Consumer Fin. Prot. Bureau, Arbitration Agreements, 81 Fed. Reg. 32,829 (proposed May 24, 2016) (to be codified at 12 C.F.R. pt. 1040).
[2] Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. No. 111-203 (codified at 12 U.S.C. § 5518(a)) ("the use of agreements providing for arbitration of any future dispute between persons and consumers" relating to financial products and services").
[3] 12 U.S.C. § 5518(b).
[4] CONSUMER FIN. PROT. BUREAU, ARBITRATION STUDY (2015), *available at* http://files.consumerfinance.gov/f/201503_cfpb_arbitration-study-report-to-congress-2015.pdf.

and sound methodologies, can be completed. Otherwise, important legal and financial relationships will be changed based on unsound science and unsupported premises.

II. Background

a. The Information Quality Act and OMB Guidelines

The Information Quality Act is a short piece of legislation enacted in December 2000 as Section 515 of the Treasury and General Appropriations Act for Fiscal Year 2001.[5] The Act directs the Office of Management and Budget ("OMB") to issue guidance to agencies to ensure the "quality, objectivity, utility, and integrity" of information disseminated to the public.[6] OMB issued guidelines in 2002, which provided "policy and procedural guidance" on the IQA and further defined statutory terms.[7] In those guidelines, OMB set "quality" as the general term applicable to information disseminated to the public and established "objectivity, utility, and integrity" as defining terms.[8] "Objectivity" asks whether information is presented in a "clear, complete, and unbiased manner" and is "accurate, reliable, and unbiased[.]"[9] OMB adds, "[i]f data and analytic results have been subjected to formal, independent, external peer review, the information may generally be presumed to be of acceptable objectivity."[10] "Utility" demands that information be useful for intended users.[11] "Integrity" ensures that data is free from corruption and falsification.[12]

b. CFPB's IQA Guidelines

CFPB's IQA guidelines are maintained on its website.[13] Many of the definitions CFPB uses track closely, as they should, with OMB governing guidelines. On utility, CFPB explains, "When transparency of information is relevant to an assessment of the public's perception of its usefulness, the Bureau will address transparency – the clear, obvious, and precise nature of the data or analysis – when developing and reviewing information."[14] When discussing objectivity, CFPB guidelines mandate that "[w]here appropriate, data will be accompanied by full, accurate, and transparent documentation, and will disclose error sources affecting its quality. Analytic results will be generated using sound statistical and research methods."[15]

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[5] Pub. L. 106-554 (codified at 44 U.S.C. § 3516); *see also* CONG. RESEARCH SERV., THE INFORMATION QUALITY ACT: OMB'S GUIDANCE AND INITIAL IMPLEMENTATION, Order Code RL32532 (2004), *available at* https://www.fas.org/sgp/crs/RL32532.pdf.
[6] *Id*.
[7] Office of Mgmt. & Budget, Guidelines for Ensuring and Maximizing the Quality, Objectivity, Utility, and Integrity of Information Disseminated by Federal Agencies, 67 Fed. Reg. 8452 (Feb. 22, 2002) [hereinafter "OMB Guidelines"].
[8] *Id*. at 8453.
[9] *Id*. at 8459.
[10] *Id*.
[11] *Id*.
[12] *Id*. at 8460.
[13] *Information quality guidelines*, CONSUMER FIN. PROT. BUREAU, http://www.consumerfinance.gov/informationquality/ (last accessed May 19, 2016) [hereinafter "CFPB Guidelines"].
[14] *Id*.
[15] *Id*.

CFPB asserts that "[t]he guidelines are not intended to be legally binding regulations or mandates."[16] Such a statement can be found neither in the OMB guidelines nor in the statute itself. This statement was made by CFPB without statutory authority likely in an attempt to avoid meeting the problem it now faces with these rules. Both the IQA and OMB guidelines mandate that agencies "issue guidelines ensuring and maximizing" the quality of information. CFPB must adhere to the law—the intent of Congress—and the governing and overriding OMB guidelines.

c. OMB Peer Review Bulletin

In 2004, OMB issued a memorandum for heads of departments and agencies containing the "Final Information Quality Bulletin for Peer Review."[17] This bulletin "includes guidance to federal agencies on what information is subject to peer review, the selection of appropriate peer reviewers, opportunities for public participation and related issues."[18] The bulletin "establishes that important scientific information *shall be* peer reviewed by qualified specialists before it is disseminated by the federal government."[19]

The IQA peer review requirements apply to any influential scientific information disseminated by an agency.[20] OMB defines "dissemination [as] agency initiated or sponsored distribution of information to the public"[21] and "scientific information [as] factual inputs, data, models, analyses, technical information, or scientific assessments based on the behavioral and social sciences, public health and medical sciences, life and earth sciences, engineering, or physical sciences."[22] "Influential scientific information" is "scientific information the agency reasonably can determine will have or does have a clear and substantial impact on important public policies or private sector decisions[.]"[23]

III. The CFPB Failure To Follow IQA Procedures

a. Violation of IQA Quality, Utility, and Integrity Standards

The Arbitration Study does not meet the IQA standards for quality. As Professors Jason Scott Johnston and Todd Zywicki explained, "the CFPB's data do not allow for meaningful comparison between arbitration and class actions[,]" later adding that "[t]hese data suffer from a number of shortcomings."[24]

For example, CFPB presents "data on what consumers recover when arbitrations make a judgment in their favor but no data on what consumers recover when arbitrations settle . . . [inviting]

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[16] *Id*.
[17] Memorandum from Joshua B. Bolten, Dir., Office of Mgmt. & Budget, to Heads of Departments and Agencies concerning Issuance of OMB's "Final Information Quality Bulletin for Peer Review" M-05-03 (Dec. 16, 2004) [hereinafter "OMB Bulletin"], *available at* https://www.whitehouse.gov/sites/default/files/omb/memoranda/fy2005/m05-03.pdf.
[18] *Id.* at 1.
[19] *Id.* at 2 (emphasis added).
[20] *Id*. at 37.
[21] *Id*. at 35.
[22] *Id*. at 36.
[23] *Id*.
[24] Jason Scott Johnston & Todd Zywicki, *The Consumer Financial Protection Bureau's Arbitration Study – A Summary and Critique* at 6 (Mercatus Ctr., Working Paper, 2015) [hereinafter "Working Paper"], *available at* http://mercatus.org/sites/default/files/Johnston-CFPB-Arbitration.pdf.

a false apples-to-oranges comparison between class action *settlements* and arbitral *awards*."[25] Furthermore, CFPB uses "aggregate averages" to evaluate the effectiveness of class action cases. Rather than differentiating the different types of class actions, CFPB lumps them all together.[26] This "tends to overweight data from only half a dozen huge class action settlements[]"[27] and suggests that individual consumer relief from arbitration, as an average, brings larger benefits to more consumers than class actions.

Elsewhere, Professors Johnston and Zywicki point out that "the CFPB found that arbitration is such a simple and cheap process (now requiring only a $200 filing fee) that consumers achieve good outcomes even when they are not represented by counsel."[28] CFPB considers one important issue, concerning how arbitration procedures differ from federal court procedures, in the shortest section of the study, making "no attempt in the section to estimate the actual transaction costs that a consumer would face in pursuing an individual claim in federal court rather than in arbitration."[29] Professors Johnston and Zywicki also explain that "the Report fails to indicate whether the CFPB checked to ensure the validity of the econometric technique it used[]" in evaluating price changes between companies with arbitration clauses and ones without.[30] The technique CFPB used "is valid only if prices in the two groups of companies had been changing at the same rate before the imposition of the moratorium."[31] CFPB also struggles to properly consider all reasonable interpretations of its results. For example, "CFPB implies that the absence of . . . small-dollar claims from the dataset suggests that arbitration is not a feasible dispute resolution procedure for many consumers."[32] In reality, though, it is possible that the absence of small-dollar claims is a result of consumers resolving these low-dollar-amount disputes "without arbitration or litigation," instead relying on the bank's desire "to preserve customer goodwill and relationships."[33] In their harshest criticism, Professors Johnston and Zywicki write,

> In perhaps its most glaring omission, however, the CFPB Report makes no attempt to assess the merit of consumer class actions that end in the class action settlements it reports. It does not present any data that even illuminate which firms tend to settle and which do not and how key measures of class action performance (claims rates and attorneys' fees relative to the class payout) vary with the statutory basis of the claim settled. After reading the voluminous Report, one knows no more about whether the settlement of frivolous consumer class actions is a real social problem than one did before reading it. Likewise, one knows no more about whether arbitration realizes its promise of achieving more accurate determination of consumer disputes on the legal merits.[34]

These are only a sample of the methodological faults in CFPB's study.

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[25] *Id*.
[26] *Id*. at 7.
[27] *Id*.
[28] *Id*.
[29] *Id*. at 24.
[30] *Id*. at 34. Checking the validity of statistical techniques is one of the features of peer review. *See infra* p. 5.
[31] Working Paper, *supra* note 24, at 34.
[32] *Id*. at 37.
[33] *Id*.
[34] *Id*. at 55–56.

As Professors Johnston and Zywicki conclude, the CFPB study's "findings fail to support any conclusion that arbitration clauses in consumer credit contracts reduce consumer welfare or that encouraging more class action litigation would be beneficial to consumers and the economy."[35] Agency guidelines state that CFPB "will produce information products that are presented in an unbiased, clear, complete, and well-documented manner."[36] And recall OMB Guidelines, which demand that the information be "accurate, reliable, and unbiased[.]"[37] The CFPB report fails to meet these standards.

b. Lack of Peer Review

The CFPB Arbitration Study qualifies as "influential scientific information." It was disseminated to the public, includes scientific and data analysis, and will have a clear and substantial impact on important public policies and the private sector. The Study was mandated by statute and is the foundation of a new rulemaking that seeks to alter a long-standing and statutorily and judicially-favored dispute resolution process.[38] If CFPB had followed the IQA and the OMB bulletin, the Arbitration Study would have undergone a rigorous, transparent peer review process to ensure the quality of the disseminated information.[39]

CFPB failed its duty of peer review. CFPB has made no public indication, either in the Arbitration Study itself or accompanying press, that peer review played any part in the Study's preparation.[40] The lack of peer review, as required under the IQA, together with the flawed methodology and incomplete data raise serious questions about the integrity of CFPB's rules. In the absence of proper science or legislatively mandated analysis the Rule fails to follow the Congressional direction, and can be asserted only on whim.

IV. CFPB's Rulemaking is Arbitrary and Capricious

In addition to violations of the IQA, the CFPB rulemaking is arbitrary and capricious under 5 U.S.C. § 706(2)(A). "[A]n agency must examine *the relevant data* and articulate a *satisfactory explanation for its action* including a rational connection between the facts found and the choice made."[41] If the relevant data are flawed or misinterpreted, then the rule itself cannot stand. Furthermore, an agency may not take a position that is inconsistent with that agency's very own

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[35] *Id.* at 6.
[36] CFPB Guidelines, *supra* note 13.
[37] OMB Guidelines, *supra* note 7, at 8459.
[38] *See AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 345 (2011) ("[O]ur cases place it beyond dispute that the [Federal Arbitration Act] was designed to promote arbitration.").
[39] *See* OMB Bulletin, *supra* note 17, at 12 ("The National Academy of Public Administration suggests that the intensity of peer review should be commensurate with the significance of the information being disseminated and the likely implications for policy decisions.") (citation omitted).
[40] CFPB's IQA Guidelines contain a blanket disclaimer stating none of the materials the agency produces are subject to IQA and OMB's peer review provisions. CFPB Guidelines, *supra* note 13. CFPB may be claiming this under the authority of Section IX of the OMB Peer Review Bulletin, which finds that "accounting, budget, actuarial, and financial information, including that which is generated or used by agencies that focus on interest rates, banking, currency, securities, commodities, futures, or taxes[]" are exempt from peer review. However, neither the Arbitration Study nor the proposed regulations fall under any of these categories. It is a social and behavioral study—concentrating not only on award numbers, but also consumer preference and awareness—on how consumers fare in and react to two different circumstances: individual arbitration and class actions.
[41] *Dist. Hosp. Partners, L.P. v. Burwell*, 786 F.3d 46, 59 (D.C. Cir. 2015) (citing *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983)).

findings.[42] Here, some of the findings of the CFPB's study directly conflict with the purpose of the resulting rules.[43]

While agencies are granted broad discretion in rulemaking, this discretion "'is not unlimited' and [courts] will remand to the agency if it fails to apply its 'expertise in a reasoned manner.'"[44] More simply put, "agencies do *not* have free rein to use inaccurate data."[45] As the D.C. Circuit held, "[i]f an agency fails to examine the relevant data—which examination could reveal, *inter alia*, that the figures being used are erroneous—it has failed to comply with the APA."[46] Finally, the court made clear that agencies must consider all important aspects of a problem and ensure that the explanation for its decision is congruent with the evidence before the agency.[47] In failing to do this, the current CFPB proposed rule runs afoul of the Administrative Procedure Act.

Conclusion

CFPB must delay its rule and conduct a new, peer-reviewed study using accepted, scientific methodology.

Thank you for your consideration of the foregoing comments. Please feel free to contact me by telephone at (202) 470-2396 or by e-mail at eric.bolinder@causeofaction.org, if there is anything further that CoA Institute can provide to the Bureau.

Respectfully,

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[42] *Id*. ("We have often declined to affirm an agency decision if there are unexplained inconsistencies in the final rule.").
[43] *See supra* p. 4 ("[T]he CFPB found that arbitration is such a simple and cheap process (now requiring only a $200 filing fee) that consumers achieve good outcomes even when they are not represented by counsel.")
[44] *Dist. Hosp. Partners*, 786 F.3d at 60 (citing *Cape Cod Hosp. v. Sebelius*, 630 F.3d 203, 206 (D.C. Cir. 2011)).
[45] *Id*.
[46] *Id*. at 57; *see Catawba Cnty., N.C. v. Envtl. Prot. Agency*, 571 F.3d 20, 46 (D.C. Cir. 2009) (agencies "have an obligation to deal with newly acquired evidence in some reasonable fashion"); *see also New Orleans v. Secs. & Exch. Comm'n*, 969 F.2d 1163, 1167 (D.C. Cir. 1992) ("[A]n agency's reliance on a report or study without ascertaining the accuracy of the data contained in the study or the methodology used to collect the data is arbitrary[.]" (citation and quotation marks omitted)).
[47] *Dist. Hosp. Partners*, 786 F.3d at 57.