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COA INSTITUTE CASE STUDY ON THE CFPB'S ARBITRATION RULE:

How the Bureau Evaded Scientific Guidelines and Bypassed Peer Review

And How to Fix It



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I. Executive Summary

The Consumer Financial Protection Bureau (“CFPB” or “Bureau”) is an agency unlike most any other in the history of the United States. It possesses untold power over the American people and businesses, and the heft of this power is in a single agency director accountable to no one. As Judge Kavanaugh of the U.S. Court of Appeals for the D.C. Circuit held in a since-vacated decision, “the Director enjoys more unilateral authority than any other officer in any of the three branches of the U.S. Government, other than the President.”¹

In the Dodd-Frank Act of 2010, Congress delegated to the CFPB the power to regulate, if necessary, mandatory-binding arbitration clauses in consumer financial contracts. This power came with an important caveat: the CFPB must first conduct a study on the effect arbitration clauses have on consumers, and any regulation promulgated by the agency must be based on that study. Yet the CFPB already had the goal in mind to regulate and ban these arbitration clauses, driven largely by internal bias and promoted by third-party interests. Instead of conducting an objective study backed by peer review, the agency sought a pre-determined result, abusing junk science and methodology to get there. In doing so, it ignored the requirements of the Information Quality Act (“IQA”) and the ensuing Office of Management and Budget (“OMB”) bulletin requiring agency peer review. This paper examines the failings of the arbitration study and offers solutions to the potential new agency head to ensure future policy is informed by sound science.

II. Recommendations

The best way to curtail the CFPB’s abuse of junk science is to force the agency to follow the standards contained within the IQA and the OMB peer review bulletin. If the CFPB were to strictly adhere to the IQA’s standards of data quality—objectivity, integrity, and utility—and conduct rigorous, academic peer review, outcomes like the one detailed in this paper would be avoided.

¹ *PHH Corp. v. Consumer Fin. Prot. Bureau*, 839 F.3d 1, 7 (D.C. Cir. 2016), *vacated on reh’g en banc*, 881 F.3d 75 (D.C. Cir. 2018); *see Consumer Fin. Prot. Bureau v. RD Legal Funding, LLC*, No. 17-890, 2018 WL 3094916, at *35 (S.D.N.Y. June 21, 2018) (“Respectfully, the Court disagrees with the holding of the *en banc* court and instead adopts Sections I-IV of Judge Brett Kavanaugh’s dissent[.]”).

Cause of Action Institute (“CoA Institute”) recommends that the new CFPB Director, once confirmed, immediately institute rulemaking actions to codify these already-mandatory requirements of the IQA and peer review. This should apply to all studies or scientific findings released by the agency, whether they undergird a rule or not.² Although the Director could just order agency personnel to follow these directives through a memorandum, that would only be a temporary solution. Rulemaking under the Administrative Procedure Act (“APA”) would ensure that these science-based requirements have more permanence and apply regardless of who is running the agency five years from now.³ Furthermore, the new Director should require, whether through rulemaking or otherwise, that all published scientific findings be accompanied by full disclosure of outside datasets, sources, and lobbying.

III. What are Arbitration Clauses?

Arbitration has long been a part of the litigation landscape in the United States. It provides a valuable, accessible alternative to costly litigation and allows parties to settle their differences outside of a court room. In 1925, to counter previous hostility to arbitration, Congress passed the Federal Arbitration Act.⁴ This act promoted and codified arbitral awards between litigants that are enforced in the federal court system. In *AT&T Mobility LLC v. Concepcion*, the Supreme Court confirmed and upheld the viability and importance of the Federal Arbitration Act, finding that state laws that prohibit businesses from inserting class-action waivers into contracts were preempted by the Act.⁵ And in its most recent term, the Court held in *Epic Systems Corp v. Lewis* that individual arbitration agreements must be enforced as written.⁶ The federal courts, and most certainly the Roberts Court, have shown an affinity for arbitration. It is easy to see why: it promotes free bargaining between individuals while lessening the burden on an exploding federal court docket.

Mandatory pre-dispute binding arbitration clauses have become the norm in many, but not all, financial services contracts. These clauses, which are agreed to by consumers when they take a loan, open a credit card, or start a new checking account, require consumers to go to a neutral arbitrator rather than the federal courts when facing an irreconcilable dispute with their financial company.⁷ This could include things as minor as a misapplied \$30 late fee to major disputes over account balances. The

² This, of course, would extend to any scientific findings that are part of a proposed rule.

³ A future Director could institute rulemaking to reverse the requirements, but that is a cumbersome process subject to judicial review.

⁴ 9 U.S.C. § 1 *et seq.*

⁵ 563 U.S. 333 (2011).

⁶ 138 S. Ct. 1612 (2018).

⁷ The U.S. Constitution establishes the right to a jury trial for any civil action exceeding twenty dollars. U.S. Const. amend. VII.

consumer may be represented by counsel in the process, but is not required to, and the company typically, but not always, covers all associated costs.

On November 1, 2017, President Trump signed a Congressional Review Act (“CRA”) Joint Resolution of Disapproval that overturned the CFPB arbitration rule (the “Arbitration Rule”) and ensured that the agency could never pass a similar rule in the future without explicit congressional approval.⁸ The CRA is just about the only way to hold the CFPB accountable, other than a court order, and it requires full-bore legislation from Congress signed by the President to work. Regardless of the rule’s demise, this entire process warrants close examination. The abuse of junk science and methodology is not unique to the CFPB; continued reform of scientific oversight is necessary to rein in otherwise unaccountable agencies.

IV. Section 1028(b) of the Dodd-Frank Act

Section 1028(b) of the Dodd-Frank Act gives the CFPB authority to regulate arbitration clauses in financial services contracts. A mandatory prerequisite, though, is that the Bureau first conduct a study on the use of arbitration agreements.

The Bureau *shall* conduct a study of, and shall 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.⁹

Using the word “shall” above, Congress made clear that this is mandatory. That is, regardless of whether the Bureau wanted to initiate rulemaking on arbitration clauses, it had to conduct this study according to the will of Congress.

The Bureau, by regulation, *may* prohibit or impose conditions or limitations on the use of an agreement between a covered person and a consumer for a consumer financial product or service providing for arbitration of any future dispute between the parties, if the Bureau finds that such a prohibition or imposition of conditions or limitations is in the public interest and for the protection of consumers. The findings in such rule shall be consistent with the study conducted under subsection (a).¹⁰

Note, however, that the rulemaking is discretionary. If the Bureau found through its arbitration study that no new regulations on arbitration clauses were necessary, it did not need to promulgate new rules. Furthermore, Congress clearly established that the “findings in such rule shall be consistent with the study[.]”

⁸ Joint Resolution for Congressional Disapproval, Pub. L. No. 115-74, 131 Stat. 1243 (2017).

⁹ 12 U.S.C. § 5518(a) (emphasis added).

¹⁰ *Id.* § 5518(b) (emphasis added).

To summarize, the CFPB:

1. *Must* conduct a study on arbitration agreements;
2. *May* promulgate rules imposing conditions or limitations on such agreements;
3. *Must* ensure the findings in these rules are consistent with the study.

This comports with recent Supreme Court case law, which has ruled directly on the use of the words “may” and “shall” when combined in a statute.

Unlike the word “may,” which implies discretion, the word “shall” usually connotes a requirement. . . . When a statute distinguishes between “may” and “shall,” it is generally clear that “shall” imposes a mandatory duty.¹¹

The CFPB derives both its obligation to conduct the study and its authority to promulgate any rules from the Dodd-Frank Act. As explained above, however, Congress did not unilaterally ban binding arbitration clauses, although it certainly could have. Instead it asked for an in-depth study and then, if the science called for it, reasoned and calculated regulation.

V. The CFPB’s Arbitration Study—A Lobbied Effort

Following Congress’s statutory mandate, the CFPB initiated a study into arbitration agreements (the “Arbitration Study”). But there is one detail that cannot go overlooked: the study was coupled with heavy lobbying from the American Association for Justice (“AAJ”), a special interest group representing trial lawyers—who obviously benefit from an increase in class action law suits. Now, to be clear, lobbying an agency *before* a rulemaking docket is opened—that is, prior to the agency officially introducing the rule—is not illegal, nor should it be frowned upon. Citizens, whether they are individuals or organized into a trade group, have a right to petition their government and share ideas. Here, however, one sees the powerful influence of such a special interest on bureaucrats already cozy with them.

Through Freedom of Information Act (“FOIA”) requests, CoA Institute has acquired a number of communications sent by the AAJ to the CFPB. For example, one record captures an email conversation between Brian Dupré, Public Affairs Counsel with AAJ, and Kelvin Chen, a key employee at the CFPB involved in the arbitration study. Dupré’s initial email, one of many CoA Institute found, contains

¹¹ *Kingdomware Techs., Inc. v. United States*, 136 S. Ct. 1969, 1977 (2016) (emphasis added and citations omitted); see *Lexecon Inc. v. Milberg Weiss Bershard Hynes & Leach*, 523 U.S. 26, 35 (1998) (A statute’s use of the “mandatory ‘shall’ . . . normally creates an obligation impervious to judicial discretion.”); *Bennett v. Spear*, 520 U.S. 154, 175 (1997) (“[A]ny contention that the relevant [statutory] provision . . . is discretionary would fly in the face of its text, which uses the imperative ‘shall.’”).

background information on a recent, successful class action case. He explains the case and why it is an “example of a great consumer class action” and offers that the case includes useful data of arbitration agreements from payday lenders. He also notes that Mayer Brown did a “study” (Dupré used the quotes himself), but omitted one of the class actions detailed in his email.¹² Chen thanks him for his email and asks Dupré to “[p]lease keep us posted, particularly if you source any additional on-line-only payday lending agreements.”

-----Original Message-----

From: Dupre, Brian [mailto:Brian.Dupre@justice.org]
Sent: Thursday, September 04, 2014 5:17 PM
To: Chen, Kelvin (CFPB)
Cc: Wade-Gery, William (CFPB)
Subject: [SUSPECTED SPAM] 60 different payday loan arb clauses

Kelvin,

I had previously provided information about the Edwards v Geneva Roth case, a successful class action against illegal payday lenders in Indiana state court.

When the borrowers were litigating in the trial court, one of the arguments they made was that online payday loan customers had no choice but to have a contract with an arbitration clause because that was all the industry offered. To support that argument, they submitted an affidavit surveying 60 different online agreements and attaching them as exhibits. It's a large file scanned, but I am attaching a link where you can download it. <https://drive.google.com/file/d/0B3MGNh2YGiv7RVVxjMU0wSk5acXM/edit?usp=sharing>

Let me know if that doesn't work. This is from 2010, so you'll notice that about 25 or so use NAF. Many of the other clauses require arbitration to occur in a particular location (typically Florida, for reasons I don't know), but also Arizona, Nevada, Philadelphia, Los Angeles, etc.

Speaking of NAF, I found it interesting that one of the class action that helped shut down NAF, Anthony Magnone et al v. Accretive LLC et al, 09-06375 (C.D. Cal.), was filed in 2009. That case became part of the MDL, In re: National Arbitration Forum Trade Practices Litigation, MDL 2122. That class action settlement required NAF to dismiss all pending consumer arbitrations (valued at approximately \$1 billion), and Mann Bracken to cease all collection activities arising out of NAF arbitrations (estimated to be worth about \$3.8 billion to the class).

It's an example of a great consumer class action. What's really interesting is that MayerBrown's class action "study" purported to look at all class actions filed in 2009 (which should have included Magnone) and yet it didn't discuss the NAF case at all.

Hope this is useful.

Brian

Brian Dupré
American Association for Justice (AAJ)
202-684-9544
brian.dupre@justice.org

¹² Mayer Brown is traditionally viewed as a class action defense firm. See *Consumer Litigation & Class Actions*, MAYER BROWN, <https://www.mayerbrown.com/experience/consumer-litigation-class-actions/> (last visited July 17, 2018) (“The misuse of consumer litigation & class actions poses a significant threat in today's business world.”).

-----Original Message-----

From: Chen, Kelvin (CFPB) [mailto:Kelvin.Chen@cfpb.gov]
Sent: Friday, September 05, 2014 1:42 PM
To: Dupre, Brian
Cc: Wade-Gery, William (CFPB)
Subject: RE: 60 different payday loan arb clauses

Thanks, Brian. This is very useful.

Please keep us posted, particularly if you source any additional on-line-only payday lending agreements.

To: Chen, Kelvin (CFPB)[Kelvin.Chen@cfpb.gov]
Cc: Wade-Gery, William (CFPB)[William.Wade-Gery@cfpb.gov]
From: Dupre, Brian
Sent: Fri 9/5/2014 7:20:21 PM
Importance: Normal
Subject: RE: 60 different payday loan arb clauses
Received: Fri 9/5/2014 7:22:29 PM

Will do.

I happened to come across one the other day that still says all disputes will be heard by NAF, though NAF no longer accepts consumer arbitrations. See <http://paydayloanrightnow.com/notices-and-disclosures.html>.

Another one I have looked at requires arbitration to be conducted in Johnson County, Kansas under the AAA Commercial Rules (though the contract is governed by the laws of Florida). See <https://quickercash.com/about-us/terms-of-use.html>. The AAA Commercial Rules have a \$750 filing fee, and do not appear to allow for parties to attend by phone (though it is unclear and it appears that witnesses may call in). See https://www.adr.org/aaa/ShowProperty?nodeId=/UCM/ADRSTG_004103.

I believe others have more comprehensive information, and am looking into it.

In another email, Ivanna Yang, an AAJ staffer, passes along a [news article](#) to Chen, describing the “negative effects of forced arbitration for our service members[.]” Yang notes that it was AAJ who “brought this story to the attention of the reporters,” essentially acting as the source. Despite this, AAJ is never quoted or referenced in the article, effectively concealing its contributions. This is a perfect example of a special interest group planting a story in *The New York Times* with its own talking points and then sharing it with the CFPB.

To: Chen, Kelvin (CFPB)[Kelvin.Chen@cfpb.gov]
Cc: Duncan, Julia[Julia.Duncan@justice.org]
From: Yang, Ivanna
Sent: Tue 3/17/2015 5:53:14 PM
Importance: Normal
Subject: NY Times Article on Forced Arbitration
Received: Tue 3/17/2015 5:53:24 PM

Hi Kelvin,

Just wanted to pass along this article on the negative effects of forced arbitration for our service members which ran on the front page of the New York Times today. The article focuses on how forced arbitration undermines the Servicemembers Civil Relief Act and exposes how corporations like USAA and JPMorgan Chase use arbitration clauses to evade accountability. AAJ Communications and Public Affairs brought this story to the attention of the reporters and spoke with them at length about how forced arbitration hurts service members, as well as all Americans.

Looking forward to meeting next week,

Ivanna

<http://www.nytimes.com/2015/03/17/business/wronged-troops-are-denied-recourse-by-arbitration-clauses.html?hp&action=click&pgtype=Homepage&module=second-column-region&ion=top-news&WT.nav=top-news>

Dupré also passed along study data and research.

To: Dupre, Brian[Brian.Dupre@justice.org]
Cc: Wade-Gery, William (CFPB)[William.Wade-Gery@cfpb.gov]
From: Chen, Kelvin (CFPB)
Sent: Mon 3/10/2014 11:12:53 PM
Importance: Normal
Subject: RE: 2 pieces of research
Received: Mon 3/10/2014 11:12:00 PM

Thanks, Brian. We appreciate your input and look forward to reviewing these.

From:Dupre, Brian [mailto:Brian.Dupre@justice.org]
Sent: Thursday, March 06, 2014 12:22 PM
To: Chen, Kelvin (CFPB)
Cc: Wade-Gery, William (CFPB)
Subject: 2 pieces of research

Kelvin,

I want to pass along two pieces of research:

The first is a law review article by Sarah Cole, a professor at Moritz College of Law who specializes in dispute resolution. The article presents research that individual arbitration is not a “viable forum for consumers with low value claims,” which is somewhat surprising given that Prof. Cole’s scholarship is generally supportive of arbitration as a dispute resolution mechanism. AAJ’s views differ from hers in many regards, but her academic perspective on the vindication of low dollar consumer claims in arbitration vs class actions may be useful in your study.

The second is a document produced by the Center for Justice and Democracy regarding civil rights class actions. Link at <http://centerid.org/content/fact-sheet-civil-rights-class-actions-singularly-effective-tool-combat-discrimination>, and pdf attached. Much of it relates to employment discrimination, but the discussion of the Equal Credit Opportunity Act and the auto lending discrimination cases (eg, Jones v Ford Motor Credit in SDNY) might be useful.

Thanks,

Brian

Brian Dupré

American Association for Justice (AAJ)

These are just some of the many different emails exchanged between Dupré, Chen, and other staffers in which AAJ shared study data, exemplary cases, news clippings, and other information. To give an idea of just how key the relationship between AAJ and the CFPB was, AAJ took the time to set up a new staffer, Kristen Kreple, as Chen’s direct contact point after Dupré left to take a job at U.S. Department of Housing and Urban Development.

To: Kreple, Kristen[Kristen.Kreple@justice.org]
Cc: Wade-Gery, William (CFPB)[William.Wade-Gery@cfpb.gov]
From: Chen, Kelvin (CFPB)
Sent: Mon 9/29/2014 7:47:01 PM
Importance: Normal
Subject: RE: Proposed Department of Defense Rule
Received: Mon 9/29/2014 7:47:00 PM

Thanks, Kristen. We appreciate the updates from AAJ and look forward to meeting in person at some point.

From: Kreple, Kristen [mailto:Kristen.Kreple@justice.org]
Sent: Monday, September 29, 2014 3:43 PM
To: Chen, Kelvin (CFPB)
Cc: Wade-Gery, William (CFPB)
Subject: Proposed Department of Defense Rule

Hi Kelvin,

Now that Brian Dupre has left us for the greener pastures of HUD, I'll be sending you information that may be helpful.

I wanted to make sure you saw this – the Department of Defense revealed a proposed rule on Friday that would expand and strengthen the Military Lending Act by extending a ban on forced arbitration to all forms of payday loans, vehicle title loans, refund anticipation loans, deposit advance loans, installment loans, and unsecured open-end lines of credit and credit cards. As you probably know, the Military Lending Act of 2006 applies only to certain types of payday loans, car title and refund anticipation loans. Over the years, as lenders found ways to circumvent the law, it became clear that a more comprehensive approach is needed.

We are really pleased with this development.

I look forward to working with you!

Best,

Kristen

Kristen Kreple

Federal Relations Counsel

American Association for Justice (AAJ)

Formerly Association of Trial Lawyers of America

Kreple continued to feed class action information to the CFPB.

To: Kreple, Kristen[Kristen.Kreple@justice.org]
Cc: Duncan, Julia[Julia.Duncan@justice.org]
From: Chen, Kelvin (CFPB)
Sent: Fri 12/19/2014 2:57:38 AM
Importance: Normal
Subject: RE: Excellent class action study for your review -
Received: Fri 12/19/2014 2:57:00 AM

Thanks for bringing this to our attention, Kristen. I look forward to reviewing this.

From: Kreple, Kristen [mailto:Kristen.Kreple@justice.org]
Sent: Thursday, December 18, 2014 9:55 PM
To: Chen, Kelvin (CFPB)
Cc: Duncan, Julia
Subject: Excellent class action study for your review -

Hi Kelvin,

I hope you're well. I wanted to flag this brand-new class action report for you. Although it's technically written, it's chock-full of a lot of valuable data regarding class actions. I've included key facts below:

This much is clear: the CFPB and AAJ had a close, working relationship. Such behind-the-scenes lobbying is not unique; it happens all the time. Nor is it illegal,¹³ but it does provide evidence of the CFPB's alliances in pushing the Arbitration Rule. When an agency does something peculiar that benefits a single third party, who supports it can be instructive. It should come as no shock, then, that AAJ is a heavy contributor to Democratic political candidates and causes. Since 2008, the year of the financial crisis, AAJ has given a staggering \$16,855,914 to Democratic congressional candidates.¹⁴ In the same time period, AAJ donated a mere \$704,939 to Republican congressional candidates.¹⁵

VI. The CFPB's Political Motivations

The CFPB, the brainchild of Senator Elizabeth Warren and previously helmed by Democratic gubernatorial candidate Richard Cordray, an Obama nominee, was run as a left-leaning, progressive organization masquerading as a helpful government agency. The CFPB even used the favorite advertising company of both the Obama and Clinton campaigns, GMMB, Inc. [Documents](#) obtained by CoA Institute reveal just how deep GMMB's coordination with the CFPB went, including contracted access to

¹³ It would only be illegal if an outside group lobbied an agency on a rule without disclosing it on the record *after* the rule was formally noticed. Obviously, public comments on the record post-rulemaking are appropriate and encouraged. CoA Institute submitted its own regulatory comment on this rule.

¹⁴ OpenSecrets.org, <https://www.opensecrets.org/orgs/totals.php?cycle=A&id=D000000065> (last visited July 19, 2018).

¹⁵ *Id.*

extremely sensitive personally identifiable information (“PII”), despite an admission by CFPB staff that there was no need for it.¹⁶ The CFPB’s contract with GMMB made up nearly all the latter’s total business in 2016, when it was awarded more than \$14,000,000 in contract awards.

Not only that, but CoA Institute [documents](#) also reflect coordination between the CFPB and the White House on the arbitration rule. On September 16, 2014, Sameera Fazili, then-Senior Policy Advisor to the Obama White House’s National Economic Council, reached out to Chris D’Angelo, then-Chief of Staff at the CFPB, regarding the Arbitration Rule. A meeting was scheduled for September 23, 2014 with D’Angelo, Christopher Lipsett, and William Wade-Gery set to attend.

This all paints a clear picture: there were internal operating biases at Cordray’s CFPB. If the CFPB were created by a Republican Senator, run by a Republican appointee, and fueled by Republican special interests, there is no doubt it could swing the other way. That’s why science is important, and Congress seems to recognize that. Republican Mick Mulvaney, on his first day as Acting Director of the agency, [stated](#), “I’m just learning about the powers I have as acting director. They would frighten most of you.”

VII. The Cordray-English Gambit

If any other evidence of politicization is needed, Richard Cordray and Leandra English provided it on November 25, 2017. Cordray departed the CFPB to run for governor in Ohio as a Democrat and appointed English as Deputy Director just before resigning. He did so in an attempt to trigger a provision of the Dodd-Frank Act which, according to him, would automatically make the Deputy Director the Acting Director until a presidentially-nominated successor was confirmed by the Senate. This move seemed to be an obvious ploy to get around the Federal Vacancies Reform Act of 1998, which would allow the President to nominate an Acting Director, Mick Mulvaney, until Cordray’s successor could be confirmed.

[Press reports](#) indicate that Cordray and English engaged in this gambit alone, without the support of the CFPB and against the [legal opinion](#) of the Bureau’s General Counsel, assumingly in an attempt to continue pushing a political agenda at the agency. English [spent the days](#) after her “appointment” meeting and getting photo-ops with powerful elected Democrats such as Senator Chuck Schumer and the CFPB’s biggest apologist, Senator Elizabeth Warren. CoA Institute acquired documents showing the internal communications behind this gambit and detailed it [here](#).

¹⁶ This raises obvious questions about the firewalls in place to protect GMMB from using this confidential and sensitive information in other advertising campaigns, but that is not the purpose of this report.

English sued in the District Court of the District of Columbia, asking Judge Timothy Kelly, a recently-confirmed Trump appointee, to issue a Temporary Restraining Order barring Mulvaney from assuming the acting directorship and installing English. Judge Kelly denied English's motion. One former CFPB employee, speaking anonymously to American Banker, said of English's selection, "It's symptomatic of the environment at the CFPB where they just handpick whomever they want and this cronyism and favoritism leads to discrimination."¹⁷ The CEO of the Consumer Bankers Association, Richard Hunt, spoke highly of English in her role as Chief of Staff, but questioned her appointment to Deputy Director as English "has never run a government agency, never run a business and never worked at a bank[.]" adding, "I hope she's not being used as a pawn[.]" On July 6, 2018, Leandra English finally resigned her post at the CFPB and dropped her legal challenge.

VIII. Flaws of the Study

The CFPB not only had to adhere to the orders of Congress in Dodd-Frank to do the study, it was also required to follow prior instructions from Congress and ensuing OMB guidelines. The Bureau ignored both.

a. The Information Quality Act and OMB Guidelines

The Information Quality Act ("IQA") is a short piece of legislation enacted in December 2000 as Section 515 of the Treasury and General Appropriations Act for Fiscal Year 2001.¹⁸ 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.¹⁹ OMB issued guidelines in 2002, which provided "policy and procedural guidance" on the IQA and further defined statutory terms.²⁰ 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.²¹ "Objectivity" asks whether information is presented in a "clear, complete, and unbiased manner" and is "accurate, reliable, and unbiased[.]"²²

¹⁷ Under Cordray, the CFPB was accused of racial discrimination and other personnel mismanagement.

¹⁸ Pub. L. No. 106-554, §515, 114 Stat. 2763 [hereinafter Info. Quality Act]; *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>.

¹⁹ Info. Quality Act § 515(b)(2)(A)

²⁰ Office of Mgmt. & Budget, Guidelines for Ensuring and Maximizing the Quality, Objectivity, Utility, and Integrity of Information Disseminated by Federal Agencies, 67 Fed. Reg. 8,452 (Feb. 22, 2002) [hereinafter OMB Guidelines].

²¹ *Id.* at 8,453.

²² *Id.* at 8,459.

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.”²³ “Utility” demands that information be useful for intended users.²⁴ “Integrity” ensures that data is free from corruption and falsification.²⁵

b. The CFPB’s IQA Guidelines

The CFPB’s IQA guidelines are maintained on its website.²⁶ Many of the definitions the CFPB uses track closely, as they should, with OMB governing guidelines. On utility, the 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.”²⁷ When discussing objectivity, the 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.”²⁸

The CFPB asserts that its “guidelines are not intended to be legally binding regulations or mandates.”²⁹ The CFPB further writes that its guidelines “are not legally enforceable and do not create any legal rights or impose any legally binding requirements or obligations on the Bureau or the public.”³⁰ The CFPB’s position is clear: judicial review of its IQA compliance is not available. Regardless of whether that is true, this claim further solidifies the need for binding rulemaking from the agency forcing its staff to abide by the IQA. Both the IQA and OMB guidelines mandate that agencies “issue guidelines ensuring and maximizing” the quality of information. The CFPB must adhere to the law—the intent of Congress—and the governing OMB guidelines.

c. OMB Peer Review Bulletin

²³ *Id.*

²⁴ *Id.*

²⁵ *Id.* at 8,460.

²⁶ *Information quality guidelines*, CONSUMER FIN. PROT. BUREAU, <http://www.consumerfinance.gov/informationquality> (last visited July 17, 2018) [hereinafter “CFPB Guidelines”].

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.*

³⁰ *Id.*

In 2004, OMB issued a memorandum for the heads of departments and agencies containing the “Final Information Quality Bulletin for Peer Review.”³¹ 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.”³² The bulletin “establishes that important scientific information *shall be* peer reviewed by qualified specialists before it is disseminated by the federal government.”³³

The IQA peer review requirements apply to any influential scientific information disseminated by an agency.³⁴ OMB defines “dissemination [as] agency initiated or sponsored distribution of information to the public”³⁵ 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.”³⁶ “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[.]”³⁷

d. The CFPB’s Failure to Follow IQA Procedures

1. 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 have 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.”³⁸

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] a false apples-to-oranges comparison between class

³¹ Mem. from Joshua B. Bolten, Dir., Office of Mgmt. & Budget, to Heads of Dep’ts & 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>.

³² *Id.* at 1.

³³ *Id.* at 2 (emphasis added).

³⁴ *Id.* at 37.

³⁵ *Id.* at 35.

³⁶ *Id.* at 36.

³⁷ *Id.*

³⁸ Jason Scott Johnston & Todd Zywicki, *The Consumer Financial Protection Bureau’s Arbitration Study – A Summary and Critique* at 6 (Mercatus Center, Working Paper, 2015) [hereinafter Working Paper], *available at* <http://mercatus.org/sites/default/files/Johnston-CFPB-Arbitration.pdf>.

action *settlements* and arbitral *awards*.”³⁹ 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.⁴⁰ This “tends to overweight data from only half a dozen huge class action settlements[]”⁴¹ and, read correctly, would actually suggest that individual consumer relief from arbitration, as an average, brings larger benefits to more consumers than class actions.

Elsewhere, Professor Johnston points 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.”⁴² 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.”⁴³ Professor Johnston also explains 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.⁴⁴ 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.”⁴⁵ The 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.”⁴⁶ 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.”⁴⁷ In his harshest criticism, Professor Johnston writes,

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

³⁹ *Id.*

⁴⁰ *Id.* at 7.

⁴¹ *Id.*

⁴² *Id.*

⁴³ *Id.* at 24.

⁴⁴ *Id.* at 34. Checking the validity of statistical techniques is one of the features of peer review. *See supra* p. 14.

⁴⁵ Working Paper, *supra* note 38, at 34.

⁴⁶ *Id.* at 37.

⁴⁷ *Id.*

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.⁴⁸

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

As Professor Johnston concludes, 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."⁴⁹ Agency guidelines state that the CFPB "will produce information products that are presented in an unbiased, clear, complete, and well-documented manner."⁵⁰ And recall the OMB Guidelines, which demand that the information be "accurate, reliable, and unbiased[.]"⁵¹ The CFPB report fails to meet these standards.

CoA Institute also uncovered an August 19, 2015 Information Memorandum from Eric Goldberg, through David Silberman, to Director Cordray concerning Todd Zywicki and Jason Johnston's working paper critique.

Wednesday, August 19, 2015

Information Memorandum for the Director

FROM	Eric Goldberg, 5-9007
THROUGH	David Silberman, 5-7142
SUBJECT	Working paper critique CFPB's Arbitration Study from Profs. Todd Zywicki and Jason Johnston

Last week, Profs. Todd Zywicki (George Mason University School of Law) and Jason Johnston (University of Virginia School of Law) released a working paper that constitutes the longest analysis and critique of the Bureau's Arbitration Study released to date.

While the entirety of this memorandum is redacted in the FOIA production, its mere existence proves that Director Cordray and Deputy Director Silberman were acutely

⁴⁸ *Id.* at 55–56.

⁴⁹ Working Paper, *supra* note 38, at 6.

⁵⁰ CFPB Guidelines, *supra* note 26.

⁵¹ OMB Guidelines, *supra* note 20, at 8,459.

aware of the stinging critique of the study's methodology for years, but still moved forward with the rulemaking without properly addressing the issues identified by the working paper.

2. 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.⁵² If the 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.⁵³

The CFPB failed its duty of peer review. It made no public indication, either in the Arbitration Study itself or accompanying press, that peer review played any part in the Study's preparation.⁵⁴ This lack of peer review, as required under the IQA, together with the flawed methodology and incomplete data, raised serious questions about the integrity of the CFPB's rule. By neither using proper science nor conducting the legislatively mandated analysis, the Rule failed to follow congressional directions.

Interestingly, Congress seemed to predict that the CFPB would fail to submit the study to peer review. Internal CFPB communications show that, in May 2015, the Congressional Budget Office (“CBO”) sent a request to the CFPB for its expert advice on a possible legislative provision that would, among other things, require a rigorous peer review of the arbitration study. One CFPB staffer offered that “[p]erhaps these are requirements we'd comply with regardless,” but was rebuffed by another CFPB staffer, who wrote “it's not correct that the arb study requirements would have no impact because this draft language appears to require us to study certain things not included in the Bureau's March 2015 Study[.]”

⁵² See *AT&T Mobility LLC*, 563 U.S. at 345 (2011) (“[O]ur cases place it beyond dispute that the [Federal Arbitration Act] was designed to promote arbitration.”).

⁵³ See OMB Bulletin, *supra* note 31, 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.”) (internal citation omitted).

⁵⁴ The 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 26.

I think it will be important for us to understand exactly what the CBO ask is.

From:Goldberg, Eric (CFPB)
Sent: Friday, May 22, 2015 10:45 AM
To: Winseck, Brian (CFPB); Ling, Yuh Wen (CFPB); Wade-Gery, William (CFPB); Chen, Kelvin (CFPB); CFPB_OGC_Clearance
Cc: Galicia, Catherine (CFPB); Tindall, Anne (CFPB); Honig, Charles (CFPB); Alexandrov, Alexei (CFPB)
Subject: RE: CBO arbitration language

+Charlie and Alexei.

We will look at this, but it's not correct that the arb study requirements would have no impact because this draft language appears to require us to study certain things not included in the Bureau's March 2015 Study.

Eric

From:Winseck, Brian (CFPB)
Sent: Friday, May 22, 2015 10:43 AM
To: Ling, Yuh Wen (CFPB); Wade-Gery, William (CFPB); Chen, Kelvin (CFPB); Goldberg, Eric (CFPB); CFPB_OGC_Clearance
Cc: Galicia, Catherine (CFPB); Tindall, Anne (CFPB)
Subject: CBO arbitration language

All, CBO asked us to review the following draft statutory language related to the arbitration study and potential rulemaking. This language isn't public yet, but may be included in an appropriations bill in the future.

CBO is essentially looking for our best estimate of the cost to implement this provision. Regarding the arb study requirements, I'm assuming those would have no impact in that we've already published the study. There may be a cost impact for the Bureau related to the rulemaking requirements at the end of the provision. Perhaps these are requirements we'd comply with regardless, so the cost and policy impact would be little to none.

It would be great to get any feedback by COB Wednesday, May 27.

Thanks.

Brian

5-9774

3. The CFPB's Rulemaking was Arbitrary and Capricious

In addition to violating the IQA, the CFPB's rulemaking was arbitrary and capricious under the APA.⁵⁵ "[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."⁵⁶ If the relevant data are flawed or misinterpreted, then the rule itself could not stand under judicial review. Furthermore, courts have chastised agencies for taking positions inconsistent with their own findings.⁵⁷ Similarly, here,

⁵⁵ See 5 U.S.C. § 706.

⁵⁶ *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))

⁵⁷ *Id.* ("We have often declined to affirm an agency decision if there are unexplained inconsistencies in the final rule.").

some of the findings of the CFPB’s study conflicted directly with the purpose of the resulting rule.⁵⁸

Although 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.’”⁵⁹ More simply, “agencies do *not* have free rein to use inaccurate data.”⁶⁰ As the D.C. Circuit has 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.”⁶¹ Finally, an agency must consider all important aspects of a problem and ensure that the explanation for its decision is congruent with the evidence before it.⁶² In failing to do this, the now-repealed CFPB rule ran afoul of the APA.

e. The CFPB’s Response to CoA Institute’s Concerns was Woefully Inadequate

CoA Institute submitted a [regulatory comment](#) during the Arbitration Rule’s open comment period. In its final rule, the CFPB responded to CoA Institute’s comments directly. For example, CoA Institute detailed precisely how the CFPB ignored the requirements of the IQA. Furthermore, CoA Institute alleged that the CFPB failed to conduct a peer review of the study, as required by OMB. In its [final rule](#), the CFPB wrote:

One nonprofit commenter challenged the Bureau’s Study for its alleged failure to comply with the requirements of the Information Quality Act and a related OMB bulletin, asserting that the Study should have undergone a rigorous, transparent peer review process to ensure the quality of the disseminated information.

The CFPB’s answer to CoA Institute’s comment is inapposite and incomplete:

⁵⁸ *See supra* p. 15.

⁵⁹ *Burwell*, 786 F.3d at 60 (citing *Cape Cod Hosp. v. Sebelius*, 630 F.3d 203, 206 (D.C. Cir. 2011)).

⁶⁰ *Id.*

⁶¹ *Id.* at 56; see *Catamba Cnty., N.C. v. Env’tl 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. Sec. & 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[.]” (quotation marks omitted)).

⁶² *Burwell*, 786 F.3d at 57.

In response to concerns about the Bureau's compliance with the Information Quality Act, the Bureau did comply with the IQA's standards for quality, utility, and integrity under the IQA Guidelines.

The footnote the CFPB placed at the end of this sentence, which one would assume supports the Bureau's assertion, merely links to the agency's IQA guidelines on its website. The CFPB made no effort to answer CoA Institute's detailed criticisms or explain why the Bureau's study met the IQA's objectivity, utility, and integrity standards. One is left to draw the inference that the CFPB simply has no defense for the glaring vulnerabilities in the Arbitration Study. The Bureau's only play is to blindly link to IQA guidelines and hope the public takes its word for it.

The CFPB put similarly little effort into responding to CoA Institute's allegations regarding peer review.

Moreover, the Study did not fall within the requirements of the OMB's bulletin on peer review, contrary to what the commenter suggested. The bulletin applies to scientific information, not the "financial" or "statistical" information contained in the Study. The Federal financial regulators, including the Bureau, have consistently stated that the information they produce is not subject to the bulletin.

In its comment, CoA Institute anticipated the CFPB might make this argument:

CFPB may be claiming [an exemption from the peer review rules] 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.

Essentially, the CFPB appeared to play games of semantics, differentiating "financial" information from "scientific" information. As anyone who has a degree in economics knows, it is very much a science. The agency cannot be allowed to wriggle

out of an important peer-review requirement by simply stretching dictionary definitions.⁶³

The CFPB attempted to sow confusion regarding what peer review is and how it is conducted:

Although the Bureau did not engage in formal peer review, it did include with its report detailed descriptions of its methodology for assembling the data sets and its methodology for analyzing and coding the data so that the Study could be replicated by outside parties. The Bureau is not aware of any entity that has attempted to replicate elements of the Study; to the extent that the Bureau's analysis has been reviewed by academics and stakeholders those individual critiques are addressed above. The Bureau has monitored academic commentary in addition to the comments submitted and continues to do so.

This is not an adequate substitute for the OMB required peer review. The CFPB appears to be shifting blame onto outside groups for not “replicating” the study. This is something the agency could have and should have coordinated on its own.

IX. Conclusion

The abuse of junk science is one of the pitfalls of largely unrestrained agency power. The CFPB was motivated by political interests and the lobbying of third parties. This directly affected the quality of science used in its study and, ultimately, led to a flawed rule. In summary, the new CFPB Director should:

- Institute rulemaking to require agency personnel to use peer review mechanisms on all studies conducted by the agency, whether such studies undergird a rule or not.
- Promulgate a rule mandating that agency employees comply with the requirements of the IQA.
- Issue an order that the agency must, going forward, disclose all sources, outside lobbying, and other data used as the foundation of any study or rule.

⁶³ Other science-based agencies, such as the Environmental Protection Agency, have confirmed the importance of peer review. Env'tl Prot. Agency, Mem. on Peer Review & Peer Involvement at EPA (Jan. 31, 2006), *available at* https://www.epa.gov/sites/production/files/2015-01/documents/peer_review_policy_and_memo.pdf (“Peer review of all scientific and technical information that is intended to inform or support Agency decisions is encouraged and expected.”)

Without these important safeguards, the agency will be at the whim of whoever happens to control it during that five-year period. And this does not apply to Democrats alone; Republican administrations could also use the CFPB to unilaterally implement Republican views on the economy and consumer protection, outside the purview of Congress or even the President. Regulations and enforcement actions that have severe consequences for the American economy should not vacillate depending on who happened to last appoint the CFPB Director. They should be based on sound science and strictly adhere to the will of Congress.