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To the Point!

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CFPB Arbitration Study: First Step to Restricting their Use?

The CFPB recently released the long-awaited arbitration study mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the *"Arbitration Study"*). In the Arbitration Study, the CFPB analyzed (1) the prevalence of arbitration clauses in certain consumer financial product markets, (2) the results of a national survey of credit card holders regarding their knowledge and understanding of arbitration clauses, (3) the different procedural rules applicable in consumer arbitration and select courts, (4) consumer disputes filed with the American Arbitration Association for six consumer financial product markets (*i.e.,* credit cards, checking accounts/debit cards, payday loans, prepaid cards, private student loans and auto loans), (5) individual consumer claims filed in federal court and class claims filed in federal and certain state courts, (6) how much consumers and companies use small claims court, (7) the terms of consumer financial class action settlements, (8) data on how public enforcement actions and private class actions overlap with respect to disputes about consumer financial products, and (9) the relationship between arbitration clauses and price and availability of consumer credit card products.

The 728-page Arbitration Study is highly data-centric and dense with statistics and tables. Noteworthy findings include the following:

- *Consumer Awareness.* Through its nationwide survey of over 1,000 credit card holders, the CFPB found that dispute resolution mechanisms play a limited role in consumers' decisions to obtain a particular card. The majority of the consumers surveyed did not know whether their credit card agreement included an arbitration provision. More than half of the consumers whose card agreements did include an arbitration provision incorrectly believed they could participate in class action lawsuits; interestingly, this percentage was roughly the same whether or not the consumer's card agreement contained an arbitration provision.

- *Readability.* Almost all of the arbitration clauses in contracts for consumer financial products reviewed by the CFPB were more complex and written at a higher grade level than the rest of the contract.

- *Class Actions.* The vast majority of the arbitration clauses the CFPB reviewed prohibited arbitration from proceeding on a class basis. Although the CFPB found that it is rare for a company to try to force an individual lawsuit into arbitration, it is common for arbitration clauses to be used to block class actions. For example, credit card issuers that were sued in a class action and had arbitration clauses in their card agreements filed motions to compel arbitration 65% of the time and were successful in doing so 61.5% of the time.

- *Impact of the Concepcion Decision.* Although many commenters had predicted that the Supreme Court's decision in *AT&T Mobility v. Concepcion* would significantly increase the number of companies that include no-class-arbitration provisions in their consumer financial product contracts, the CFPB found only a slight increase in its sample.

- *No Evidence of Cost Savings.* The CFPB did not any find evidence that the use of mandatory arbitration clauses lowered the price of financial services for consumers as some proponents of arbitration have suggested.

In its press release accompanying the Arbitration Study, the CFPB stated that arbitration clauses limit relief for consumers by restricting their ability to participate in class actions. The CFPB found that while very few consumers seek individual relief through either arbitration or federal courts, millions of consumers are eligible for relief each year through class action settlements.

The Arbitration Study included data on the average amount of relief obtained by consumers and companies who were granted relief through arbitration proceedings, which showed that consumers won an average of 57 cents per dollar they claimed, while companies won an average of 98 cents for every dollar claimed. Comparable data for class action proceedings was not available due to the difficulty ascertaining the amount that each individual class member receives when an award is granted; thus, it is not clear whether consumers receive greater relief through class action proceedings than through arbitration.

However, it is evident that vastly more consumers are eligible for relief through class actions than through arbitration, and the CFPB seems keenly focused on this discrepancy.

Although many in the banking and legal industry have suggested that the CFPB will almost certainly propose a rule restricting arbitration clauses in consumer financial contracts following the Arbitration Study, it is difficult to predict what action will be taken and how such potential restrictions would be implemented. Financial institutions should continue to monitor any CFPB releases concerning the Arbitration Study in the coming months for additional information or updates.

7th Circuit Requires Servicers to Credit Payments on the Day Authorized

In its March 11, 2015 opinion in *Fridman v. NYCB Mortgage Co. LLC*, the Seventh Circuit Court of Appeals held that the Truth-in-Lending Act (*"TILA"*) requires mortgage servicers to credit electronic payments on the date authorized by the consumer on the servicer's website, not on the date the servicer receives the payment from the consumer's bank.

TILA requires servicers to credit payments as of the "date of receipt" of the payment. The court reviewed the CFPB's official interpretations of Regulation Z, which provides that a paper check is received when the mortgage servicer receives it, not when the funds are collected. The court viewed an electronic authorization as similar to a paper check — both operate as the consumer's written permission for the payee to draw funds — and concluded that they should be credited when received by the servicers, not when the servicer acquires the funds. The court relied on the commentary that defines "date of receipt" to mean "the date that the payment instrument or other means of payment reaches the mortgage servicer," determining that electronic authorizations are an "other means" of payment that are to be credited on the date received by the servicer.

In reaching its decision, the court focused on TILA's consumer protection purposes, noting that the servicer decides how quickly to collect a payment when it receives a check or gets authorization on its website or over the telephone to transfer payments. If the "date of receipt" were interpreted as the date the creditor received the payment from the consumer's bank, "the servicer could decide to collect payment through a slower method in order to rack up late fees."

The NYCB Mortgage Company website included a cutoff time for receipt of electronic payment authorizations and a notification that payments made using an electronic authorization would be credited two business days after the authorization is submitted. While creditors are expressly permitted under TILA and Regulation Z to include a cutoff time for receipt of mail, electronic and telephone payments for open-end credit accounts (provided the cutoff time is no earlier than 5 p.m.) and to effect payments made through the creditor's website after the cutoff time on the next business day, the rules concerning receipt of payment for mortgage servicers do not include similar permissions.

The Seventh Circuit's ruling reverses the district court's summary judgment in favor of the servicer and revives Fridman's class action case. At this of stage of the litigation, the full impact of this holding is not clear, but it appears to be limited to mortgage payments. Thus, we recommend for mortgage servicers to apply the *Fridman* holding narrowly but to confirm what their current payment crediting practices are and explore what steps are necessary operationally to effect a change that would credit payments when electronic authorization is provided.

Target Data Breach Settlement

Target has agreed to pay $10 million in a proposed settlement to a class-action lawsuit stemming from its 2013 data breach, which occurred during the holiday shopping season (the *"Target breach"*). The proposal calls for individual victims who suffered unreimbursed losses to receive up to $10,000, which could include losses as a result of account freezes, late-payment fees, time spent addressing the unauthorized charges, costs associated with getting a credit report fixed and other costs. The settlement would also require Target to appoint a chief information security officer, keep a written information security program and provide security training to its employees, maintain a process to monitor for data security events and respond to such events deemed to present a threat.

In 2014 the American Bankers Association (the *"ABA"*) conducted a survey of more than 500 banks, which estimated that more than 8% of debit cards and 4% of credit cards were implicated in the Target breach. The survey revealed that the average loss was $331 per debit card with loss and $530 per credit card with loss. The Target breach resulted in reissuance of most cards by banks at their own expense. The ABA study determined that while banks of all sizes were affected by the data breach, banks with under $1 billion in assets spent just over $11 per debit card and $12.75 per credit card as compared to $3 per card by the largest banks (over $50 billion in assets) in reissuance costs, including card production, mailing and staff time.

In a response to the data breach settlement, the ABA called on Target to cover the hundreds of millions of dollars incurred by bankers in protecting their customers from losses. The ABA notes that the settlement does little to address the real problem — stopping a breach before it happens. The ABA believes Target — and the many other retailers who have suffered recent breaches due to gaps in their internal computer defenses — should be forced to do more.

Financial institutions should become familiar with the settlement and the process to submit claims and prepare their customer service personnel to respond to customer questions regarding the settlement.

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