# A Funny Thing Happened On The Way To The Arbitral Forum:

# The Latest On The Use of Class Action Waivers In Arbitration Agreements In the United States

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# What is an arbitral class action waiver?

"Claims subject to Arbitration include, but are not limited to: …Claims made as part of a class action or other representative action, and the arbitration of such Claims must proceed on an individual (non-class, non-representative) basis. If you or I require arbitration of a particular Claim, neither … may pursue the Claim in any litigation, whether as a class action, private attorney general action, other representative action or otherwise."

-from *Fensterstock v. Educ. Fin. Partners, et al.,* which went to the US Supreme Court ("SCOTUS") (discussed below).

# 2017- a pivotal, contentious year as a result of a controversial election

2017 has proved a pivotal and contentious year in the development of US law concerning the enforceability of commonly used class action waivers in arbitration clauses, with major twists and turns in both the consumer and labor relations contexts, arising mostly from the Republicans' gaining control of Congress and the Presidency as a result of the November 2016 US election.

# CONSUMER CASES

# Background: *Discover Bank*, for example

*Discover Bank v. Superior Court*, 36 Cal. 4th 148, 30 Cal. Rptr 3d 76, 113 P.3d 11 (Cal. 2005).

-arbitration provision in a credit card agreement included the following: "Neither you nor we shall be entitled to join or consolidate claims in arbitration by or against other card members with respect to other accounts, or arbitrate any claim as a representative or member of a class or in a private attorney general capacity."

Held: where there is a class action/arbitration waiver in a consumer adhesion contract, disputes between the parties to that contract will predictably involve small amounts of damages, and plaintiff alleges that defendant had superior bargaining power and engaged in a fraudulent scheme to cheat numerous consumers out of small amounts of money, the class action/arbitration waiver is unconscionable under California law and will not be enforced.

# SCOTUS Steps In

*AT&T Mobility LLC v. Concepcion*, 563 U.S. 333 (U.S. 2011); 5-4 decision of SCOTUS, written by the late Justice Antonin Scalia.

Held: the Federal Arbitration Act pre-empts state laws such as California's *Discover Bank* rule, *i.e.*, a class action waiver contained *in the arbitration provisions* of a consumer contract is valid and should be enforced despite contrary state law.

# SCOTUS Steps In Again

*Affiliated Computer Servs. v. Fensterstock*, 564 U.S. 1001 (U.S. 2011) (NB: this was my case).

-the S.D.N.Y. and the Second Circuit, applying California law and thus *Discover Bank*, held that the class action waiver in a private student loan's arbitration provisions (quoted earlier) was unconscionable and so unenforceable.

SCOTUS's "GVR": "Petition for writ of certiorari granted. Judgment vacated, and case remanded to the United States Court of Appeals for the Second Circuit for further consideration in light of *AT&T Mobility LLC v. Concepcion*[.]"

# Even Non-Signatories Benefit!

On remand to the federal District Court:

*Fensterstock v. Educ. Fin. Partners, et al.*, 2012 U.S. Dist. LEXIS 124571 (S.D.N.Y. Aug. 30, 2012).

Defendant Affiliated Computer Services (“ACS”) was the loan servicer and not a party to the promissory note, so plaintiff claimed ACS could not avail itself of the class action waiver SCOTUS had upheld.

Held: “Under the doctrine of equitable estoppel, a non-signatory can compel arbitration 'where (i) there is a close relationship between the parties and controversies involved and (ii) the signatory's claims against the non-signatory are intimately founded in and intertwined with the underlying agreement containing the arbitration clause.' …The court finds that this case meets both requirements for the application of the doctrine of equitable estoppel, and that plaintiff is therefore estopped from avoiding arbitration against ACS.”

# Enter the Consumer Finance Protection Bureau

The CFPB is a federal agency created by the Dodd-Frank Wall Street Reform and Consumer Protection Act, which was passed in 2010 in response to the 2008 financial crisis and the recession that followed.

The CFPB is charged with consumer protection in the financial sector. Financial institutions subject to its jurisdiction include banks, credit unions, security firms, credit card companies, and mortgage servicers.

Section 1028(b) of the Dodd-Frank Act authorize the CFPB to “prohibit or impose conditions or limitations” on the use of consumer financial arbitration if the CFPB finds that such prohibition, condition or limitation would be “in the public interest and for the protection of consumers,” and supported by a study and a report to Congress.

# CFPB Action in 2016-17

May 5, 2016: The CFPB announces its proposed rule which would prohibit the inclusion in consumer financial agreements of any mandatory, pre-dispute arbitration provisions containing class action waivers.

July 17, 2017: The CFPB issues its Final Rule, found at 82 Federal Register 33210.

# CFPB Final Rule, July 19, 2017

"Pursuant to section 1028(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the [CFPB] is issuing this final rule to regulate arbitration agreements in contracts for specified consumer financial product and services. First, the final rule prohibits covered providers of certain consumer financial products and services from using an agreement with a consumer that provides for arbitration of any future dispute between the parties to bar the consumer from filing or participating in a class action concerning the covered consumer financial product or service. Second, the final rule requires covered providers that are involved in an arbitration pursuant to a pre-dispute arbitration agreement to submit specified arbitral records to the Bureau and also to submit specified court records. The Bureau is also adopting official interpretations to the regulation." 82 Fed. Reg. 33210 (July 19, 2017).

What happened between the CFPB's issuance of its proposed rule in May 2016 and its issuance of its Final Rule in July 2017?

# The November 2016 election

## The result: the Republicans gain control of the House, the Senate, and the Presidency in January 2017.

# The Congressional Review Act

5 U.S.C. Chapter 8 (§§ 801-808), "Congressional Review of Agency Rulemaking"

-enacted in 1996 as part of the Republican Party's "Contract with America Advancement Act" and signed into law by President Clinton.

-provides Congress with authority to overrule, using an expedited review process, any new federal regulation so long as Congress acts within 60 legislative days of its publication in the Federal Register.

-prohibits the federal agency that issued the overruled regulation from reissuing a substantially similar regulation.

# 2017 House of Reps. Action

On July 25, 2017, the U.S. House of Representatives passed H.J. Res. (“House Joint Resolution”) 111:

“Resolved by the Senate and the House of Representatives of the United States of America in Congress assembled, That Congress disapproves the rule submitted by the Bureau of Consumer Financial Protection relating to 'Arbitration Agreements' (82 Fed. Reg. 33210 (July 19, 2017)), and such rule shall have no force or effect.”

# State Attorneys General Weigh In

July 28, 2017: twenty-one state Attorneys General wrote a letter to U.S. Senate leaders urging the Senate not to repeal the rule:

"The CFPB's Arbitration Rule would deliver essential relief to consumers, hold financial services companies accountable for their misconduct, and provide ordinary consumers with meaningful access to the civil justice system."

# Rare Inter-Agency Disputes

In September, the Office of the Comptroller of the Currency issued a study that questioned the CFPB's methodologies and stated, for example, that the CFPB's Final Rule would actually raise the cost of consumer credit.

On October 23rd, the U.S. Treasury Department issued a report, titled "Limiting Consumer Choice, Expanding Costly Litigation: An Analysis of the CFPB Arbitration Rule," that concluded that the Final Rule would greatly increase class action lawsuits and settlements, adding that "[a]ffected businesses are unlikely to simply absorb these new financial burdens."

# The US Senate Acts By The Slimmest of Margins On October 24th

October 24th: The U.S. Senate, by the slimmest possible margin (51-50), joined the House of Representatives by voting to eliminate the CFPB's Final Rule.

The Republicans hold 52 seats in the Senate but two Republican Senators voted in favor of the Final Rule, resulting in a tie.

Vice President Pence cast the decisive vote pursuant to his authority under Article I, Sec. 3 of the U.S. Constitution: "The Vice President of the United States shall be President of the Senate, but shall have no Vote, unless [the Senators] be equally divided."

# President Trump Signs Last Week

President Trump signed the House/Senate resolution just last week, on November 1, 2017.

# LABOR CASES

# NLRB's *D.R. Horton* decision

The National Labor Relations Board is a U.S. government agency which was founded during the New Deal under the National Labor Relations Act of 1935. It is charged with, *inter alia*, enforcing federal labor laws involving collective bargaining and unfair labor practices.

*D.R. Horton, Inc. v. Michael Cuda* (NLRB Case No. 12-CA-25764), 357 NLRB No. 184 (Jan. 3, 2012): Because Section 7 of the NLRA gives employees the right to engage in "concerted activities for the purpose of collective bargaining or other mutual aid or protection," an employer violated it by requiring employees to agree to arbitration agreements with class action waivers.

"…[t]he FAA protects the right of parties to resolve statutory claims in an arbitral forum so long as 'a party does not forego the substantive rights provided by the statute.' … Thus, arbitration may substitute for a judicial forum only so long as the litigant can effectively vindicate his or her statutory rights through arbitration." *D.H. Norton* at 9.

The NLRB found that Section 7 supersedes the FAA and SCOTUS's decision in *AT&T v. Concepcion.*

# 2017: SCOTUS grants *certiorari* based on a "circuit-split"

January 2017: SCOTUS grants *certiorari* in the following cases to resolve a "circuit-split":

*Murphy Oil USA, Inc. v. NLRB*, 808 F.3d 1013 (5th Cir. 2015) (anti-*Horton*).

*Lewis v. Epic Sys. Corp.*, 823 F.3d 1147 (7th Cir. 2016) (pro-*Horton*).

*Morris v. Ernst & Young LLP*, 834 F.3d 975 (9th Cir. 2016) (pro-*Horton*).

# …and the Executive Branch changes its mind about *D.H. Horton*

In June 2017, the U.S. Solicitor General's office filed a brief *amicus curiae* with SCOTUS stating as follows:

"In *Murphy Oil*, this Office previously filed a petition for a writ of certiorari on behalf of the NLRB, defending the Board's view that agreements of the sort at issue here are unenforceable. After the change in administration the Office reconsidered the issue and has reached the opposite conclusion. Although the Board's interpretation of ambiguous NLRA language is ordinarily entitled to judicial deference, courts do not defer to the Board's conclusion as to the interplay between the NLRA and other federal statutes. We do not believe that the Board in its prior unfair-labor-practice proceedings, or the government's certiorari petition in *Murphy Oil*, gave adequate weight to the congressional policy favoring enforcement of arbitration agreements that is reflected in the FAA (emphasis added)."

# Composition of SCOTUS

SCOTUS heard argument last month, October 2017.

As a result of the 2016 election, Senator McConnell's controversial gamble paid off: in 2017, the conservative Justice Neil Gorsuch replaced the conservative late Justice Antonin Scalia, author of the *Concepcion* decision, maintaining the 5-4 conservative majority of SCOTUS.

Justice Anthony Kennedy, who is generally considered one of the conservatives, is at times a "swing-voter" who votes with the liberals.

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