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OPINION

Richard Cordray's Surprising Admission

Many banks haven't been requiring arbitration clauses.

By Darren McKinney

The U.S. Senate voted Tuesday to repeal the Consumer Financial Protection Bureau's rule prohibiting arbitration clauses in financial contracts. The Treasury Department and the Office of the Comptroller of the Currency had both weighed in with warnings about the rule's effects—criticisms that prompted a surprising admission from CFPB Director Richard Cordray.

The Treasury projected that the rule would have generated an additional 3,000 federal class-action lawsuits over five years, costing businesses $500 million to defend plus $330 million in payments to plaintiffs' lawyers.

The CFPB had denied those costs would be passed on to consumers in higher interest rates. But the comptroller's analysis of the CFPB's data found an 88% chance that the total cost of credit would increase and estimated the likely increase at almost 3.5 percentage points. "That means a consumer, living week to week, could see credit card rates jump from an average 12.5 percent to nearly 16 percent," acting Comptroller Keith Noreika wrote in an op-ed for The Hill newspaper. Mr. Noreika urged the Senate to "vacate" the rule, as the House had already done.

Here's where things got interesting. In response to the comptroller's analysis, Mr. Cordray fired off a letter to Sen. Sherrod Brown of Ohio, the Senate Banking Committee's ranking Democrat, insisting the criticism was "mistaken and unfounded."

Perhaps inadvertently, however, Mr. Cordray let slip a broader truth—that contrary to the argument of the rule's supporters all along, consumers are not being forced to sign contracts with mandatory arbitration clauses to access financial services.

"We know," Mr. Cordray wrote, "that roughly half of the credit card market does not have arbitration clauses in their agreements. If the OCC review were correct, it would mean that these banks are operating at a substantial competitive disadvantage." He added that the CFPB had surveyed a "random sample" of 141 community banks, and found only 7% of them use arbitration agreements.

To sum up, the head of the CFPB now admits that roughly half of big banks that issue credit cards, and nearly all smaller banks that provide checking accounts, do not require their customers to sign contracts with mandatory arbitration clauses. So how in the world did the CFPB ever conclude it needed to impose itself on a sound and functioning market—a market in which consumers have plenty of choices and banks that don't require arbitration are free to advertise themselves as such?

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