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# ARBITRATION: IS IT FAIR WHEN FORCED?

## HEARING

BEFORE THE

## COMMITTEE ON THE JUDICIARY
## UNITED STATES SENATE

ONE HUNDRED TWELFTH CONGRESS

FIRST SESSION

OCTOBER 13, 2011

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# ARBITRATION: IS IT FAIR WHEN FORCED?

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**THURSDAY, OCTOBER 13, 2011**

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
*Washington, DC.*

The Committee met, pursuant to notice, at 2:05 p.m., in room SD–226, Dirksen Senate Office Building, Hon. Al Franken, presiding.

Present: Senators Franken, Whitehouse, Klobuchar, Blumenthal, and Cornyn.

## OPENING STATEMENT OF HON. AL FRANKEN, A U.S. SENATOR FROM THE STATE OF MINNESOTA

Senator FRANKEN. The hearing will come to order. I want to thank all the witnesses for being here today and thank everyone for being here.

We are in the middle of a vote, I believe, so some of my colleagues will be joining me shortly. I want to thank Chairman Leahy for giving me the opportunity to chair this hearing. And a special thanks again to the witnesses for sharing your time and expertise with this Committee. Before I introduce today's witnesses, I would like to take a few moments to clarify my intent in calling today's hearing.

The topic of mandatory arbitration is much more interesting than its dry-sounding title might suggest to people who do not know much about it, which includes almost everyone, every consumer and every employee. Today we are likely to discuss such wide-ranging legal issues as Federal preemption, statutory construction, and class actions in situations as varied as chicken farmers to cell phone users to auto dealers. To the extent possible, I would like to keep today's hearing focused on mandatory arbitration as opposed to other voluntary types of alternative dispute resolution, or ADR. I am not aware of any introduced legislation to "ban arbitration." I think everyone in this room can agree that there are some circumstances in which ADR, including post-dispute arbitration, should be encouraged. So let us focus our attention today on mandatory arbitration, which raises the most concern for me.

I would also like to use this hearing to broadly highlight all of the efforts that have been made over the years to properly limit the use of mandatory arbitration. I am far from the first Senator to champion this issue. Senator Feingold, a former colleague on this Committee, was a true pioneer, and Senator Feingold partnered



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with fellow Committee members to bring relief to certain groups particularly affected by mandatory arbitration.

The Ranking Member of this Committee, Senator Grassley, led the charge in limiting the use of mandatory arbitration clauses for poultry and livestock producers in contracts with their processors. He was able to secure the passage of a provision in the 2008 farm bill. I would like to submit for the record a letter from Craig Watts, a Fairmont, North Carolina, chicken farmer. He is one of many farmers who, under this law, has chosen to opt out of the arbitration clause in the contract he signed with his chicken processor. He notes that in his 20 years in contract poultry: "I know of no examples of anyone ever taking a dispute to the 'court of arbitration.' For a farmer it is just too expensive . . . But in the 2008 farm bill, Congress recognized how unconscionable these mandatory arbitration clauses were . . . and it resulted in the farmer getting to choose to keep it or opt out . . . it has not led to a wave of lawsuits as many had said . . . but I do believe it is an incentive to do business above board."

Another member of this Committee, Senator Hatch, led a similar effort to provide relief for auto dealers. In the Senate, this bill had 66 cosponsors. Thanks to Senator Hatch's efforts, America's auto dealers are now on a level contractual playing field with the big auto manufacturers.

These efforts all preceded my work on limiting forced arbitration for employees of defense contractors. They also preceded my introduction of the Arbitration Fairness Act this Congress and the bill I recently introduced with Senator Blumenthal, the Consumer Mobile Fairness Act. These bills, like the ones that have come before it, seek to limit the use of forced arbitration clauses in contexts where one party suffers from a substantially weaker bargaining position. These particular bills focus on consumers and workers who sign form contracts with corporations.

Critics may argue that these contracts were entered into voluntarily and that we are compelled to honor forced arbitration clauses or risk abolishing entirely the freedom to contract. I think several of today's witnesses can speak to this issue better than me.

I am very honored today to introduce Minnesota's Attorney General and my friend, Lori Swanson. In 2009, Attorney General Swanson sued the National Arbitration Forum on behalf of Minnesota consumers. At the time, the National Arbitration Forum was the country's biggest arbitrator of consumer credit disputes. In the course of her investigation, Attorney General Swanson revealed that the NAF, which presented itself to the public as a neutral arbitration company, was, in fact, working behind the scenes with the companies, against the best interest of consumers. In fact, the NAF boasted to the companies, "customers don't know what to expect from arbitration and are more willing to pay," and that "customers ask you to explain what arbitration is then basically hand you the money." But I will leave it to Attorney General Swanson to tell the rest of the story.

We are also pleased to have with us Dr. Deborah Pierce, currently the Associate Director of Emergency Medicine at Einstein at Elkins Park Hospital. She will share her experience from a previous employer and the subsequent arbitration process that she en-

dured after bringing a gender discrimination claim against that employer. Her story illustrates many of mandatory arbitration's serious problems, which have led me to question the merits of our current system.

We are joined also today by Paul Bland, a senior attorney at Public Justice. Mr. Bland has devoted nearly his entire career to representing consumer clients in countless cases around the country. He has a true wealth of knowledge on a range of issues, particularly consumer arbitration. Mr. Bland's experience litigating consumer cases after *Concepcion* will give us a realistic and, I think, sobering look at the prospects for consumer-enforced corporate accountability going forward.

We also welcome Professor Christopher Drahozal—I was so nervous about getting that pronunciation correct.

[Laughter.]

Senator FRANKEN. It does not mean I will get it right the next time. Professor Drahozal is the John M. Rounds Professor of Law and Associate Dean for Research and Faculty Development at the University of Kansas School of Law. Professor Drahozal has written extensively on the law and the economics of arbitration.

We also welcome Victor Schwartz, who is a partner at the firm of Shook, Hardy & Bacon LLP, and of the U.S. Chamber of Commerce and the U.S. Chamber Institute for Legal Reform. Thank you, all of you, for joining us.

Before I turn it over to today's witnesses, we are going to need to take a recess. I am sorry about that. I know that you are all eager to testify. I can see you almost frothing. But we are going to have to take a quick recess so I can go to the floor and vote. I should be back in 10 to 15 minutes, and by then I think we will have the other members who are down there, no doubt voting, too. We have two votes. That is what has occasioned this brief recess.

So the hearing stands in brief recess.

[Recess at 2:14 p.m. to 2:35 p.m.]

Senator FRANKEN. I want to thank all of the witnesses for indulging us. We voted, and so we are back in session, and before I turn it over to the Ranking Member and the witnesses, I want to reiterate my sincere goal that today we can find some common ground. We may not all agree on the best ways to move forward and on which legislative proposals are needed, but I hope we can walk away with a few areas of agreement. I will suggest the obvious: that there is a role for Federal courts in our justice system.

This past August, Justice Kennedy replied to a reporter's inquiry about the Court's current docket, and he said this: "The docket seems to be changing . . . A lot of big civil cases are going to arbitration. I don't see as many of the big civil cases." Personally, I am troubled that our private arbitration system is, at least in part, eclipsing the United States Supreme Court, the highest Court in the land. Perhaps today's hearing can help us determine whether there is a sound middle ground—one where we use arbitration to the fullest fair extent, but allow our Supreme Court to fulfill its role as the true final arbiter.

And now to my friend, the Ranking Member, Senator Cornyn.

## STATEMENT OF HON. JOHN CORNYN, A U.S. SENATOR FROM THE STATE OF TEXAS

Senator CORNYN. Well, thank you, Mr. Chairman. I am old enough to remember why alternative dispute resolution came of age and of interest, primarily because people found that the time that it took to get cases litigated and then appealed and get a final resolution and the cost of litigation gave rise to the demand for a more expeditious and a less costly means of resolving disputes.

Of course, it is not for everything. But what it means as a practical matter is that sometimes arbitration is the only cost-effective means of resolving a dispute because you cannot find a lawyer to take your case because you may be a person of modest means, may not be able to recover attorneys' fees. So there is an important role for arbitration.

I think there are just a few other points I want to make quickly. In my view, the scholarship and research uncovers several myths about arbitration. First of all, most arbitration is contractual. It is agreed to ahead of time. It is not imposed. It is agreed to. And, of course, when it is not agreed to—let us say there is some fraud in the inducement of the contract—there are remedies to void arbitration agreements. But most of them are a convenience to the parties and, as I said earlier, a more cost-effective and more timely way of resolving relatively small and including some larger disputes. But studies show that arbitrators have no discernible bias in favor of business interests or against consumers and employees.

Second, it is a myth that consumers have no meaningful choice about submitting an arbitration due to inferior bargaining power.

Third, it is a myth that arbitration procedures lack due process protections.

Fourth, it is a myth that consumers and employees still will have access to arbitration even if pre-dispute arbitration agreements are barred.

So I look forward to hearing the testimony of the witnesses and their suggestions, if they are critics of the Federal Arbitration Act or contractual agreements to arbitrate disputes that arise, what their suggestions are to us for making it cost-effective in the sense that it is within the reach of ordinary consumers who may be people of modest means. And it also is something that could be done on a timely rather than a protracted basis. Cost and time are the reasons why alternative dispute resolution came in vogue and why I think it still has an important role to play. But I look forward to hearing from the witnesses.

Senator FRANKEN. Thank you, Senator Cornyn.

As my distinguished Ranking Member was voting, he missed my opening statement, in which I said that we are all in agreement that arbitration can be very important and definitely has its place. And today I would really like to confine—we do not have to confine, but focus on mandatory arbitration. And I know that Senator Blumenthal would like to make a statement.

## STATEMENT OF HON. RICHARD BLUMENTHAL, A U.S. SENATOR FROM THE STATE OF CONNECTICUT

Senator BLUMENTHAL. Thank you, Senator Franken, and I want to thank Senator Franken for his leadership, thank the witnesses

for being here today, particularly my former colleagues, the Attorney General of Minnesota, Attorney General Swanson, and thank her for her excellent work in this area.

I agree with our distinguished Ranking Member that cost and time are greatly to be valued. Saving them is a profoundly important objective, and it is an objective well served by alternative dispute resolution and even by arbitration in many cases, but not when it is abusively applied and made mandatory, often without sufficient information to consumers, often imposed on them, as is the case in some of the instances where Attorneys General have taken action to protect consumers. And protecting consumers and employees is indeed the objective of two measures that I have supported with Senator Franken: the Arbitration Fairness Act and the recently introduced Consumer Mobile Fairness Act, designed to protect cell phone consumers from abusive practices.

So I am very interested in what you will tell us today, and I am very grateful to you for being here and for your work in this area, whatever your point of view. There is a legitimate debate on this issue, but most important, there is the legitimate goal of protecting consumers against the increasingly pervasive use of mandatory binding arbitration clauses. These can be a scourge on consumers when they are imposed and applied abusively, and I hope that the Congress can take action to provide more tools to law enforcement, such as our Attorneys General and our Federal authorities, to protect employees and cell phone users and homeowners and others from the potential excesses in this area, so thank you very much.

Senator FRANKEN. Thank you, Senator Blumenthal.

Senator Blumenthal has partnered with me on the Consumer Mobile Fairness Act, which is about consumers. The Arbitration Fairness Act is about both consumers and employees. We have both represented here today.

Before we come to the witnesses, I would quickly like to take the opportunity to submit documents for the record. First is the letter from poultry farmer Craig Watts, which I mentioned in my opening statement. I have letters of support from a coalition of more than 40 advocacy groups for the Arbitration Fairness Act and the Consumer Mobile Fairness Act.

[The letters appears as a submission for the record.]

Senator FRANKEN. The AARP has also submitted a statement for the record in support of the Arbitration Fairness Act that highlights the effects of forced arbitration on America's seniors.

[The AARP statement appears as a submission for the record.]

Senator FRANKEN. I also have a statement for the record from Chairman Leahy, who was not able to join us today.

[The prepared statement of Chairman Leahy appears as a submission for the record.]

Senator FRANKEN. Now I will turn it over to today's witnesses, beginning with Minnesota's Attorney General, Lori Swanson.

## STATEMENT OF HON. LORI SWANSON, ATTORNEY GENERAL, MINNESOTA, ST. PAUL, MINNESOTA

Ms. SWANSON. Well, good afternoon. Thank you, Mr. Chairman, for your leadership and, Senators, it is good to be here. I appreciate yours as well.

You know, the right to have disputes resolved through an impartial judge or jury is something that is deeply embedded in our American values and in our culture, yet millions of American consumers have given up that right to have their day in court without even knowing it through fine-print language contained in various customer agreements.

Many large corporations, ranging from banks to phone companies to utilities, have put into the fine print mandatory arbitration clauses through which the consumer waives in advance the right to have their day in court, to have their dispute resolved in court. The consumer waives this right even if they do not notice the clause and even if they did not have any meaningful opportunity to negotiate the clause.

In 2009, our office filed a lawsuit against the National Arbitration Forum. The Forum was the largest arbitration company for consumer disputes in the country. It handled more than 200,000 arbitration claims a year, and according to its own statement, it said that it was listed as the arbitrator in hundreds of millions—hundreds of millions—of consumer contracts.

The lawsuit alleged that the forum deceptively represented to consumers and the public that it was independent and neutral, operated like an impartial court system, was not affiliated with any party, and did not take sides between the parties. In fact, the National Arbitration Forum had extensive ties to the collection industry and was, in essence, an arm of the collection industry.

The forum, despite its public statements to the contrary, worked behind the scenes alongside companies and creditors against the interests of ordinary consumers to convince credit card companies and other debt buyers and other corporations to insert mandatory pre-dispute arbitration clauses into these hundreds of millions of contracts and then to appoint the forum to decide the disputes, essentially putting itself as part of the collection process. It encouraged creditors and corporations to file claims, essentially to file lawsuits, against consumers whose claims it would then adjudicate. It sometimes drafted the arbitration claims—in other words, essentially drafted the lawsuit that was going to be filed against the consumer—and referred creditors to the debt collection firms which then went after the consumers.

It also had extensive financial ties to the collection industry. A group of New York private equity funds engineered two transactions in which they simultaneously took control of one of the country's largest debt collection enterprises and affiliated itself with the forum through an infusion of $42 million, essentially being on both sides of the equation. The forum went to lengths to conceal these ties to the public and to consumers.

The case ultimately settled with a consent judgment barring the forum from the business of arbitrating credit card and other consumer disputes. And although that case dealt with a problem company, it did not and cannot deal with the systematic problems with consumer arbitration and mandatory binding clauses.

Through our investigation of the forum, we conducted interviews of over 100 consumers, talked to arbitrators, and talked to employees of the forum, and those conversations told us that consumers

are not getting a fair shake and due process of law with these types of claims.

First, there is unequal bargaining power between consumers and large corporations that present the consumer with take-it-or-leave-it contracts. In almost every interview we did of consumers, people told us, "We did not know about the clause, we were not aware of the clause, nor did we feel we could do anything about the clause."

The forum's own documents describe it this way. They say, "The customer does not know what to expect from arbitration and is more willing to pay." Or "Consumers ask you to explain what arbitration is and then basically hand you the money." Those were marketing documents that the forum gave to creditors convincing creditors to put clauses like these in.

In addition, the forum's own documents said, "Well, we have to insert these clauses in because consumers will not agree after the fact to arbitration." No, I think a lot of consumers would not agree after the fact to arbitration if they feel they are not getting a fair shake and due process of law.

It was also apparent that arbitrators have a powerful incentive to favor the dominant party in arbitration. The arbitration company knows who is bringing it the business, who is filing claims, and they have an incentive to favor that corporation. We heard from arbitrators who were deselected or not given more business after ruling in favor of the consumer, arbitrators who were not given more business after refusing to award attorney fees against the consumer, and we heard from employees who said they were told to assign certain arbitrators to certain cases who would be friendly to the creditor or not put the creditor to the proof and require the creditor to submit evidence that would sustain an arbitration award.

In addition, to make matters worse, it is often not the original creditor that files the arbitration claim. In today's world debt buyers will buy debt from cell phone companies and credit card companies and then resell that debt many times over. And so oftentimes the person filing the arbitration claim is a debt buyer many times removed from the initial transaction, and consumers told us because they did not know who the arbitration company was, oftentimes they did not even appear or respond to the papers because they were not aware they had agreed to it, did not recognize the name of the arbitration company.

Only the U.S. Congress, because of court rulings, has authority to make meaningful reform to this area of the law, and I appreciate your leadership in having this hearing.

[The prepared statement of Ms. Swanson appears as a submission for the record.]

Senator FRANKEN. Thank you, Attorney General.

Now we go to Dr. Pierce.

## STATEMENT OF DEBORAH PIERCE, M.D., ASSOCIATE DIRECTOR, DEPARTMENT OF EMERGENCY MEDICINE, EINSTEIN AT ELKINS PARK HOSPITAL, ELKINS PARK, PENNSYLVANIA

Dr. PIERCE. Thank you. Chairman Leahy, Chairman Franken, Ranking Member Cornyn, and distinguished members of the Com-

mittee, thank you for the invitation to speak to you today about my experience with mandatory arbitration.

My name is Deborah Pierce. I am currently the associate director of emergency medicine at Einstein at Elkins Park Hospital and the assistant residency director of the emergency medicine residency at Albert Einstein Medical Center in Philadelphia.

In June of 2004, I began working on a part-time basis with a physician practice group in suburban Philadelphia in a community hospital emergency department. After working successfully on a part-time basis for a year, I was offered a full-time position. The salary they offered me was much less than what I had been making, but the Chairman of the practice assured me that I would recoup my initial loss in salary after I became a partner in 2 years' time.

When I signed my employment agreement, I was unaware that it contained a mandatory arbitration clause. Even if I had known to look for such a provision, it would have meant nothing to me. I am an E.R. doc. I take care of people. I love doing that. I was offered a job that was giving me the opportunity to do what I love to do. And my choice was either to accept the terms of my contract or to not get the job.

During my 2 full-time years with the practice, my job performance was never questioned, and there were no concerns expressed to me about being voted into partnership. Every male physician before me had made partner after their first 2 years. Yet at the end of 2006, the Chairman told me that the partners had voted to deny me partnership and not renew my contract.

Four months later, a male physician with less experience and a history of performance problems came up for partner. Instead of being granted partnership, he was given an additional 9-month probationary period to improve what the Chairman testified were serious problems with his clinical practice. After the 9 months, he was made a partner. No such extension was granted to me, and in addition, I learned of other females who had been denied the promotion in a similar manner. This evidence was presented during my arbitration.

At the time I worked for the practice, it was a virtually all-male partnership where 17 out of 18 of the partners were men, and the pattern has not changed since I was denied partnership. The sole female partner left, and the practice remains an all-male partnership.

I brought my gender discrimination claim before the EEOC, and it determined that the practice violated Title VII in not affording me the same treatment as it did my male counterpart. The EEOC determination letter is attached to my written statement.

Because of the arbitration clause, my only recourse was to arbitrate my claim before the American Health Lawyers Association, otherwise known as AHLA. I expected the arbitration process to be fair and assumed my case would be heard by an unbiased arbitrator with knowledge of employment discrimination law. What I experienced was the exact opposite.

From the very first day of the arbitration, I had serious doubts that my arbitrator would be unbiased and fair. There were indications that the arbitrator had a previous relationship with the hos-

pital and the practice. Also, arbitration was far more costly than I could have ever anticipated. I was required to pay half of the arbitrator's $450-an-hour fee, and the entire process cost me more than $200,000, forcing me to take out a home equity loan. Employees of lesser income could never afford to arbitrate their claim.

The costs were also driven up because the arbitrator let the practice get away with behavior that, in my understanding, would have been sanctioned in a courtroom. The practice withheld and destroyed evidence that was critical to proving my claim. My attorneys filed sanctions motions, which were granted. For one of the motions, though, the arbitrator awarded me $1,000 in sanctions and then charged me more than $2,000 in fees for his time deciding on the motion. It is my understanding that this would not happen in a court of law.

I lost the arbitration, and the content of the arbitrator's ruling demonstrated that he neither applied applicable law to the facts in my case nor considered the majority of the evidence in my favor. After the arbitration, my attorneys wrote to AHLA, arguing that it failed to provide to me the services for which I have paid significant sums and that AHLA and the arbitrator failed to meet their obligations as described in AHLA's Rules of Procedure and Code of Ethics. AHLA responded by asserting that it does not certify or attest to the abilities, competence, or performance of its arbitrators and does not make any "warranties about the ability of the arbitrator to weigh facts and law." And I have attached to my statement both copies of those letters.

For me, the mandated arbitration process took away my faith in a fair and honorable legal system which is supposed to protect the rights of citizens. Mandatory arbitration is allowing employers to ignore this country's civil laws, civil rights laws, and never to be held accountable. I hope this process today results in a much needed change in the law so that no one who follows me has to endure what I experienced.

Thank you.

[The prepared statement of Dr. Pierce appears as a submission for the record.]

Senator FRANKEN. Thank you, Dr. Pierce.

Now we go to Paul Bland.

## STATEMENT OF F. PAUL BLAND, SENIOR ATTORNEY, PUBLIC JUSTICE, WASHINGTON, D.C.

Mr. BLAND. Thank you very much, Senator Franken.

Mandatory arbitration is a very unfair system in America for at least four reasons.

First of all, you have disputes between corporations and individuals in which you have one side—the corporation, who writes the contract—basically picking the company who picks the arbitrator who is going to decide the dispute. So you have a battle, you have a dispute, and one side is essentially picking who the judge is who is going to decide that. That is unfair.

Second, it is not a transparent system. It is very secretive. It is hard to find out what happens in arbitrations. They are closed. Most of them issue decisions but there is no written decision. It is very hard for a consumer to find out what has happened in pre-

vious cases. Unlike the court system, there is no public accountability. It is secretive.

Third is that there is no judicial review. No one ever looks over to see whether or not someone is getting it right. So if an arbitrator makes even a blatant error of law—some courts have said things like "wacky decisions of law" by arbitrators are not reviewable by a court. That is really a problem.

Fourth, after the Supreme Court decision last spring in the *Concepcion* case, where the Supreme Court overturned about 15 State Supreme Courts and literally over a hundred different lower-court decisions and invented a new rule of Federal law, now supposedly the Federal Arbitration Act prevents individuals from joining together in a class action in almost any circumstances, and there is a dispute about quite how broadly that should be read, but it is very hard to have a class action arbitration now.

Corporations uses these arbitration clauses as a shield against any kind of liability even if they break the law. Now, different companies use them as a shield in different ways. First, you have companies where the way they use them as a shield is to try to make it impossible for anyone to really bring an effective individual case against them. So, for example, most arbitrators are lawyers, and generally the people who show up on the arbitrators list that you get from the major companies are all lawyers who have worked for an industry. We just heard about the lawyer from the American Health Lawyers Association is going to be deciding a dispute against a health company. Similarly, I have had cases, for example, against a title insurance company. You get a list of arbitrators, and every one works for title insurance companies or for law firms who principally represent title insurance companies. That is not a very fair deal.

In the employment setting, there is a huge amount of data, and the employment data shows, first of all, that compared to court, employees who go to arbitration end up winning far fewer cases than they would win in court. A professor named Alexander Colvin has done a comprehensive study of the employment data of the American Arbitration Association over many thousands of cases and found that.

Second, even for the employees who do win something, they tend to win, on average, significantly less sums in arbitration than they would have won in court. It simply does work in that area. Now, there is not anywhere near the same kind of data for consumer cases because there are so few cases that consumers take to arbitration, but in the employment area the data is pretty clear.

With nursing homes, the trade associations just openly admit that the reason that they want mandatory arbitration clauses is to hold down liability. It is much harder to win a case when you are taking a case in front of a lawyer from the American Health Lawyers Association than a jury because the lawyer principals represents health companies and they are going to be more likely to find for the nursing home.

So there are some companies that try to use arbitration to win the individual case. There are other types of companies, really big companies, that do mass consumer businesses where what they are interested in is just trying to ban the class actions. For them, they

are actually fine with having a fair individual arbitration because hardly any cases actually go to individual arbitration.

Now, there are a lot of consumer cases where class action is not appropriate. The case is big enough, or there are lots of consumer cases involving identity theft or lemon laws or this kind of thing that are individual cases. But there are a lot of types of cases where the only way a case can be brought is as a class action. So, for example, you get a lot of scams, hidden overcharges hidden deep in the bill, formulas that are rigged so that people end up not getting the sort of rebate that they are supposed to get, bait-and-switches where people are promised one interest rate and get a different interest rate, things where contracts are broken, you are promised something and you do not get it, where it is the same for everybody, the exact same contract is broken in the same way or the same practice violates the same law for millions of people. And the vast majority of those people never figure it out because the nature of most consumer scams is that it is buried in the fine print in a way that people do not know about it. So there are not going to be a whole lot of cases.

In that sort of setting, say a million people are cheated out of $50, perhaps 100 of them figure it out. You know, from the perspective of a big company, from an AT&T or from a Bank of America, if all 100 consumers who figure it out out of the million get their money back, they have not lost anything, because for the other 999,900 people they just get to keep the money. So for them, they can have a really fair arbitration system, but the point is that by banning class actions, they keep many of these cases from going forward.

I looked at Professor Drahozal's testimony. He talked about in 1 year there were less than 1,000 cases in the entire United States that were handled by the American Arbitration Association where a consumer sued a business, in the entire United States. The small claims court in Silver Spring that I walk past every day on my way to the Metro to go downtown handles more than that many cases every month.

Last year I had three class action settlements where we got sent checks out to cheated consumers, where we sent checks to more than 100,000 consumers. The entire United States, all the arbitrations brought by consumers in America were less than 1,000? So by myself last year I was involved in—not by myself. I had a bunch of other lawyers working with me. But, anyhow, my team of lawyers, we had three cases where we got a hundred times as many consumers their money back as the total number of people who even went to the American Arbitration Association?

The point of consumer arbitration is to suppress claims, and that is just an extremely unfair way, and it is bad for America. It encourages business to cheat people and get away with it.

Thank you.

[The prepared statement of Mr. Bland appears as a submission for the record.]

Senator FRANKEN. Thank you, Mr. Bland.

Now we go to Mr. Schwartz.

Oh, I am sorry. Mr. Schwartz, hang on 1 second. I apologize. Senator Klobuchar has just arrived, and she has to go, so I would like to give her—you have only 30 minutes.

[Laughter.]

**STATEMENT OF HON. AMY KLOBUCHAR, A U.S. SENATOR FROM THE STATE OF MINNESOTA**

Senator KLOBUCHAR. Thank you. I will actually stay for the rest of the witnesses, but I did want to just thank Attorney General Swanson for being here. What great work you do on behalf of consumers in Minnesota. We have worked together for a long time, and I just want to thank you for being here, and thank you for holding this hearing, Mr. Chairman.

Senator FRANKEN. Mr. Schwartz.

**STATEMENT OF VICTOR E. SCHWARTZ, ESQ., PARTNER, SHOOK, HARDY & BACON LLP, U.S. CHAMBER INSTITUTE FOR LEGAL REFORM, U.S. CHAMBER OF COMMERCE, WASHINGTON, D.C.**

Mr. SCHWARTZ. Mr. Chairman and Ranking Member Cornyn and Mr. Blumenthal, thank you for having me here today. It may count against my time—I hope it does not—but, Senator, about 20 years ago you and I had a phone conversation. Somebody told you that I had a sense of humor and could do good imitations, and you heard them and you said, "Mr. Schwartz, I think you should stick to your day job." So I did, and I hope I do it all right today.

Senator FRANKEN. Something tells me I wish you had not.

[Laughter.]

Senator FRANKEN. Anyway, I am glad you are here, and it does not count against your time.

Mr. SCHWARTZ. My background is pretty simple. For 40 years I have been involved in the litigation system. I have had the privilege to represent plaintiffs and defendants. I was a law professor and a dean. I write a casebook that is used in most American law schools. Today I am testifying on behalf of the U.S. Chamber Institute for Legal Reform, which is an affiliate of the U.S. Chamber of Commerce. But my views, as Senator Cornyn and others have heard me before now, are strictly my own.

A minister I knew named Albert Sikkelee, a very brilliant man, gave me a piece of wisdom that I never forgot. He said ". . . something that is not in context is pretext." And to look at either the litigation system or the pre-dispute arbitration agreements that way alone is not very good. You have to look at them together. In some of Senator Cornyn's remarks, he did just that.

People are going to differ about this, but I agree with Professor Ware that no one is really forced to sign an arbitration agreement. Even with cell phones, there are some cell phone companies that do not make you sign a pre-arbitration agreement. And the way it is in our competitive world, if people really wanted to sell something and they could do better by not having the agreement in there, they would do it. Now, the product might cost more or the service might cost more, but that is a factor of our marketplace.

There is a lack of awareness sometimes, but our system of justice I think should encourage awareness, encourage people to look. And

one benefit of this hearing and work you have done is to let people realize that they should look carefully when they buy. Professor Drahozal has some very good things to say about that.

I think eliminating pre-dispute arbitration agreements is going to really benefit lawyers. That I know. In my own firm, if they get rid of all litigation, Shook, Hardy & Bacon would have to turn to some alternative employment. And the plaintiffs' lawyers who are on the other side, they have lobbied for legislation that would abolish pre-dispute arbitration agreements. If I were stylie plaintiff's lawyer, I probably would, too. Litigation is profitable. That is part of their business. Contingency fees can reach 50 percent. That is what they do.

Consumers do not really benefit from litigation. Lawsuits are not fun. Maybe some people in this room have been in them. You have some Attorneys General here. But being in court is not what it is on television. It is a woe. Learned Hand said, "Short of disease, a lawsuit is a person's worst nightmare." That is the alternative we are talking about. And getting a plaintiffs' lawyer to help you is getting more and more difficult. When I practiced, we rarely took a case that would be less than $25,000. Today, on average, it is up to $60,000. So if there is no pre-arbitration agreement, the person is not going to get a lawyer in many, many cases.

Professor Drahozal's data shows even more challenge for employees to get a lawyer to help them when they have been fired and I have seen that in my own life experience. Somebody who has been fired from his job calls me, he cannot afford a lawyer, they do not have an arbitration agreement. They go nowhere.

Class actions have been, we could be here for hours debating about them, but they are not always a rose petal for consumers. A recent one involved Bluetooth. I did not even know what a bluetooth was, but it something you stick in your ear and you can hear things better. Anyway, people claimed that the Bluetooth did not warn them boldly enough that if you turn it up too high, it would affect your hearing adversely. A class action was brought. What was the result? A hearing loss society got $100,000. The attorneys got $850,000. The people who had the Bluetooth that was allegedly too loud got nothing. So up it went to the Ninth Circuit, and there is a group called the Center for Class Action Fairness. It is very small, but they intervened and they got the Ninth Circuit to overturn the district court, but still no money has been granted to those who used the Bluetooth.

Now, taking one case of arbitration or taking one case of class action does not give you the whole picture. But the fact is that class actions are not good for all people all the time. Sometimes consumers lose.

There are benefits to pre-dispute arbitration. They are usually faster, they are usually cheaper, and they can produce results that are helpful to individuals who are involved in them if you look at it as a whole.

There are predatory practices, but we heard from a distinguished Attorney General there are a lot of cops on the beat to stop wrongful behavior. And there is individual bargaining power, somebody saying, "I simply will not do it."

Some have suggested that after a dispute arises, that is the time for arbitration. At least in my experience it is when people on each side of a dispute game the system. If the claim is inexpensive, defendents simply will not pay. If it is big, they plaintiffs to the litigation system. You do not reach agreement or having the dispute go.

I am glad these hearings are being held. I do not think the problems with pre-dispute arbitration are ones that have to be handled through legislation. All forms of dispute resolution have problems. Class actions have problems. Litigation has problems. But here there are self-correctives to the system, and I think they are the best approval.

[The prepared statement of Mr. Schwartz appears as a submission for the record.]

Senator FRANKEN. Thank you, Mr. Schwartz. What was the impression that you did for me on the phone?

Mr. SCHWARTZ. This is what I said: "I am going to tell you this right now. I think it is something you should be encouraged to do."

Senator FRANKEN. I got it. Mario Cuomo.

[Laughter.]

Senator FRANKEN. Professor Drahozal.

**STATEMENT OF CHRISTOPHER R. DRAHOZAL, JOHN M. ROUNDS PROFESSOR OF LAW, ASSOCIATE DEAN FOR RESEARCH & FACULTY DEVELOPMENT, UNIVERSITY OF KANSAS SCHOOL OF LAW, LAWRENCE, KANSAS**

Mr. DRAHOZAL. Thank you, Mr. Chairman. I cannot do impressions, and I will not even try, so I apologize in advance.

Mr. Chairman, Ranking Member Cornyn, members of the Committee, thank you for giving me the chance to be here today to talk about consumer and employment arbitration.

What I am going to focus on in my remarks is what I focused on in my statement, which is empirical research on consumer arbitration. And I am going to talk about consumer arbitration because that is what my research has focused on.

A couple of clarifications to Mr. Bland's comment on what the AAA caseload looks like, just to start with. First is the AAA had its own class arbitration caseload at the time, and so comparing class actions in court to the AAA's consumer individual caseload is not really the right comparison. And I do not know what the numbers are of how many parties were involved in the class arbitrations, but that comparison does not work.

And the other thing that does not quite work is if you look at small claims courts, the vast majority of those dockets are debt collection cases, and a very small part of this AAA caseload was debt collection cases. The majority, 60, 70 percent, were individual consumer cases brought by consumers as claimants. So it is clearly not a huge docket, but the comparisons understate the importance, I think, of the cases that are being dealt with.

I very much appreciate Mr. Bland's highlighting of the empirical evidence in the employment arbitration setting. Again, my particular expertise where I have done the research is consumer cases, but frankly, most of what I have found I think is consistent with

what the employment studies have found, and I will talk about that as well.

I do think it is important that we talk about empirical research because anecdotal cases are useful, and highlight things that happen or can happen, but only when you look systematically across types of cases, types of disputes, the legal system as a whole, do you get a sense of how important or unimportant certain things are. And so, again, I was heartened to hear Mr. Bland referring to empirical studies because I do think they are a very important part of this undertaking.

A couple of points to highlight from the empirical research that I have done. The first is that in evaluating arbitration—and Mr. Schwartz made this point as well—you need to compare it to something. You need to have a control group. And the logical control group is the court system. And so if you look, for example, at arbitration cases, in the debt collection context particularly, it is absolutely true that businesses win the vast majority of cases, 94 or 96 percent. But when you compare that to the control group—courts, small claims courts, other courts—the win rate is at least as high, if not higher, in court for businesses. Again, this does not necessarily mean arbitration is fair, but it means you need to have a baseline for comparing the results to. You cannot just look at arbitration and say, yes, it is good, yes, it is bad.

Similarly, you have to compare like cases in arbitration and in court. It can be really hard to do that. Comparing debt collection cases is a place where I think you can do a pretty good job. They are relatively consistent. The challenge with employment arbitration—Professor Colvin's study is a very good study, but even he recognizes the cases that are in arbitration are probably different from the ones in court. And following up on Mr. Schwartz's comment, if, in fact, arbitration is more accessible for lower-income employees, what you would, in fact, expect to see is lower amounts awarded in arbitration because there are different claimants in arbitration than there are in court. And Professor Colvin acknowledges that possibility and suggests that his data is, in fact, consistent with that conclusion.

Similarly, the businesses that were studied were ones that had their own dispute resolution process where they dealt with cases before they got to arbitration. It would not surprise me at all if those businesses, in fact, settled the hard cases and only arbitrated the easy cases. And if that is the case, again, you would expect to have a lower win rate in arbitration, not because arbitration is unfair but because the cases that are in arbitration are different. So you have to be very cautious in interpreting empirical results.

The second point is as a general matter—and you all have experienced this as much as I have, I am sure—legal changes cause changes in parties' behavior. Parties respond to changes in the rules. And so if there is a change in the legal rules governing the enforceability of pre-dispute arbitration agreements, I would expect businesses to respond. One way I would expect them to respond is by increasing prices or lowering wages or not raising wages as much in the employment context. And in particular, in the credit card context, which I have done some recent work on, I would expect that the effect would be harshest or strongest on the highest-

risk customers, the ones who have the fewest other options for getting credit, because if you look at the factors that explain why credit card issuers use arbitration clauses, the riskiness of their credit card portfolio is an important factor. Credit card issuers are more likely to be involved in litigation if they have credit card bills that are not paid. And so, not surprisingly, the issuers turn to arbitration in that setting. If they cannot turn to arbitration, one response that they might take is just not to lend money to these folks at all—that is not necessarily the case, but a possible consequence.

Then the final point, which is consistent with the empirical evidence, which is also something Mr. Schwartz suggested, is to the extent that lower-income consumers/employees are better able to bring claims in arbitration, if arbitration is not there, those agreements are not going to happen after the dispute arises. The vast majority of arbitrations arise out of pre-dispute clauses, and that is true not just in settings of unequal bargaining power. It is true between businesses and big businesses. In international arbitration, the vast majority of claims arise out of pre-dispute clauses, and that is because once there is a dispute, the Mr. Schwartzes and Mr. Blands of the world cannot agree that they want to go to arbitration, so they just stay in court, which is the default.

I am looking forward to having the chance to answer the Committee's questions, and, again, I appreciate the opportunity to be here.

[The prepared statement of Mr. Drahozal appears as a submission for the record.]

Senator FRANKEN. Thank you, Professor Drahozal.

Well, I guess I will start the questioning. Attorney General Swanson, the testimony you gave is that basically the fix was in with the National Arbitration Forum right?

Ms. SWANSON. I think that is a fair assessment.

Senator FRANKEN. OK. And they were the biggest arbitrator of consumer arbitration?

Ms. SWANSON. Biggest arbitrator of consumer arbitration in the country.

Senator FRANKEN. OK. Now, I reviewed some of Mr. Schwartz's past writings, and in them he criticized State Attorneys General for engaging in lawsuits on behalf of injured persons in their States, saying that it was "a subversion of 200 years of law," and that it violated the idea of equal protection under the law.

Attorney General Swanson, if State Attorneys General like yourself could not bring claims on behalf of your citizens and those same citizens were required to submit to arbitration, what type of redress would those Minnesotans have available to them, or would the wrongs simply go unaddressed?

Ms. SWANSON. Mr. Chairman, Senators, I think in many cases the wrongs would go unaddressed. We live in a world where consumers, unfortunately, often find they are dealt an unfair hand by large corporations. The reality of the world we live in is that many private lawyers charge more by the hour than a lot of our citizens make in a week. And so if you are that individual citizen, it can be oftentimes very hard for you to be able to get an attorney, and I think that Attorneys General play a very important role in enforcing the law, holding wrongdoing accountable, making sure that

we have a fair marketplace and a level playing field for businesses that do follow the law.

I saw some of Mr. Schwartz's other testimony at one point when he was trying to stave off regulation. I noticed he said, well, we do not need certain regulations because we have Attorneys General on the beat. And I think it is important that we have Attorneys General on the beat in order to enforce the laws. You know, what we are talking about is making sure that consumers get a fair shake.

In the recent Supreme Court case involving AT&T, in the majority opinion Justice Scalia said, "The times in which consumer contracts were anything other than adhesive are long past." The reality of these fine-print contracts is that they are very long and they have gotten longer. They are very dense. I think our original Constitution is 4,000 words, and some of these consumer contracts are 20,000 words or more, drafted with terms that are very much lopsided against the consumer and to give every advantage to the company.

Senator FRANKEN. Adhesive contracts or contracts of adhesion are really where you have no choice.

Ms. SWANSON. Where you have no choice. They are presented to the consumer, take it or leave it. The reality is if you are trying to do business, they are presented to you. You are not going to negotiate; you are not going to red-line out a term. You are going to take it or not. And so when mandatory pre-dispute arbitration clauses are put into contracts, it is basically asking the consumer to give up their legal rights, their fundamental American legal right to have their day in court, without oftentimes knowing it, and as we have seen with our case involving the National Arbitration Forum, sometimes in ways that are very detrimental and unfair to the consumer.

Senator FRANKEN. Dr. Pierce, thank you for appearing before us today and sharing your, frankly, horrific story. Mr. Schwartz wrote in his testimony, "It is important to remember, and not gloss over the fact, that arbitrators such as those in the AAA and other organizations are professionals. They are independent legal experts who abide by a comprehensive set of rules and procedures . . ."

I was wondering how that squares with the response you received from the American Health Lawyers Association after you complained that the arbitrator assigned to your case lacked the knowledge and experience to adequately handle your claim. The association wrote, and I quote, "In the process of selecting an arbitrator, the AHLA ADR service makes no warranties about the ability of the arbitrator to weigh facts and law."

Does Mr. Schwartz's claim that these are legal experts who abide by a comprehensive set of rules and procedures make sense to you? Does it jive with your experience?

Dr. PIERCE. No, that was exactly not my experience. My experience started out with the first day of the arbitration, which was held in the arbitrator's office, we were given the library space to use and walked into the library space and noticed that two rows of binders in the library had the name of the hospital that I had the issue with on the binders and clearly demonstrated that his law firm had done business, what looked like significant business to me, with the hospital in the past.

One day we actually got to the law offices early and found the chairman of the department, of the emergency department, walking out of the arbitrator's office with a cup of coffee, clearly having just had coffee with the arbitrator prior to us getting there.

And then during the actual arbitration—I am not an attorney. I honestly cannot probably represent all of the legalese correctly, but during the arbitration there were multiple times that my attorneys told me that decisions were made and people's testimony changed and things happened that would never have happened in a court of law. We had one physician who had given a deposition, and during the arbitration she gave the exact opposite testimony, and it was very significant testimony. It was about this probation vote and whether or not they had done one for me. And she completely changed her idea, and the arbitrator said—or my attorneys asked her if she had changed her testimony, and she acknowledged she did and said—when they asked why, she said, "Well, I have subsequently talked to my attorneys and talked to the Chairman of the department and realized that the story was different than I thought." And they challenged this to the arbitrator, and the arbitrator said essentially—and forgive my paraphrasing, but essentially that is fine, I am glad her memory is better.

Senator FRANKEN. OK. Well, I think we get the idea. This was a guy who worked for a firm that had obviously done cases for the people you were arbitrating against, and when the AHLA says that they do not have to appoint anyone who has the ability to weigh facts and the law, I think that tells a lot.

I will go to the Ranking Member.

Senator CORNYN. Well, I think we would all agree that not only must a process for dispute resolution be fair in fact but that there has to be an appearance of fairness, too, for people to have confidence in the outcome. But I want to quote another famous Minnesotan besides the distinguished Chairman and the Attorney General of Minnesota, and that is Warren Burger. Warren Burger was recognized as one of the primary advocates of alternative dispute resolution, and he said in one quote, "The notion that most people want black-robed judges, well-dressed lawyers, and fine-paneled courtrooms as the setting to resolve their dispute is not correct. People with problems, like people with pain, want relief, and they want it as quickly and as inexpensively as possible."

So I happen to agree with Professor Drahozal that it is important that we not make judgments here, just as in an arbitration or in a court of law, based on anecdote, and some of what we have heard from Dr. Pierce and Attorney General Swanson and others is very deeply concerning. But I do think the courts are equipped, by and large, to deal with those because, of course, even under the Federal Arbitration Act of 1925, the court can still invalidate an arbitration contract on the basis of fraud, duress, or unconscionability. You mentioned contracts of adhesion, one type of those.

But I guess I would like to get a clarification, General Swanson. You are not suggesting by your testimony that contracts to arbitrate should be unenforceable as a general rule, are you?

Ms. SWANSON. Mr. Chairman, Ranking Member Cornyn, I think right now the law is such that contracts that are in consumer contracts generally are held by courts to be enforceable. What I have

tried to do with my testimony is explain some of the problems we have seen with arbitration when it comes to consumers who do not have much clout, do not have much power against a big corporation that does, and some of the unfairness that we have seen result from that when it comes to making sure that people have their legal rights protected.

Senator CORNYN. We have three former Attorneys General here on the panel, it just happens, so all of us have had the experience of heading up a consumer protection division and finding recourse for people who need justice to be done. But what I do not understand is, are you suggesting that they should be unenforceable? Or is the ability of a court to set aside an arbitration, a contract to arbitrate pre-dispute on the basis of fraud, duress, or unconscionability? Are those not adequate to address the injustices that you have seen?

Ms. SWANSON. Mr. Chairman, Ranking Member Cornyn, no, I do not believe those are adequate to address the types of abuses that we have seen. You know, the Arbitration Fairness Act has been introduced by Senator Franken based upon all of the interviews and evidence that my office has seen with consumers and arbitrators as well as employees of the National Arbitration Forum who were told basically do not assign certain arbitrators, make sure whatever arbitrator you put on a claim is anti-consumer or, by gosh, let us make sure that an arbitrator does not ask for evidence. Based upon all of that, I certainly support the Arbitration Fairness Act that would eliminate pre-dispute mandatory arbitration clauses in, among other consumer contracts.

Senator CORNYN. So what recourse would a consumer have if they have, let us say, a $100 dispute? Would they have to hire a lawyer on an hourly basis at $450 an hour or $100 an hour? Would they have to find a way to get a lawyer to represent them on a contingency fee? But $100 is not enough money really to enable you to find a lawyer to help you litigate that.

Ms. SWANSON. Mr. Chairman, Senator Cornyn, under the Arbitration Fairness Act, I do not believe anything would prohibit a consumer from agreeing after the fact to arbitration if they wanted to. The kinds of abuses I am talking about are in these pre-dispute arbitration clauses when consumers waive their legal rights beforehand, before a dispute arises. I think they would always be at liberty to agree in an arm's-length transaction to arbitration or to file a claim in small claims court. I know those differ from State to State. In our State I think you can file claims up $7,500, and they would be at liberty to do that as well.

Senator CORNYN. Well, I guess the difference that I would have with you is you apparently do not agree that contracts should be enforced when they require arbitration. That is your position.

Ms. SWANSON. Well, Mr. Chairman, Senator Cornyn, I think the courts, by and large, have enforced contracts where they require arbitration as the U.S. Supreme Court just did. My position would be that the law should be changed by the U.S. Congress, that the Congress is the only body that can change the law, and that it ought to change the law to be more protective of consumers.

Senator CORNYN. Mr. Schwartz, I just happen to be old enough that I remember practicing law in San Antonio, Texas, when I was

a district judge, when listening to the call of Warren Burger and others who complained about the cost and the delay associated with getting resolution of claims called for a new system of alternative dispute resolution. And, actually, we would have courts hold—we created a settlement week where people could mediate or arbitrate or otherwise resolve their legal disputes short of a full-blown jury trial with all of the attendant costs and delay related to that.

How do we reconcile, in your view, the concerns that have been expressed, which I am sympathetic to, that in some instances these contracts to arbitrate are not done on an equal bargaining basis or that they do not actually serve the ends of justice?

Mr. SCHWARTZ. There are, as you suggested, Senator, means to address those. If an arbitration agreement has you have to arbitrate in another city and it is far far away, it is unenforceable. If they try to eliminate punitive damages, it is unenforceable. And I think there are individual cases where people can complain about the system, but there are avenues in existence to remedy those. And when Attorney General Swanson went after a bad company, she remedied it. In response to Senator Franken's earlier observation about my discussion about Attorney General roles, I believe that enforcing the laws of your own State against fraud is absolutely the role of the Attorney General. If the Attorney General goes into tort law and tries to be a plaintiff's attorney, I do not think that is a good idea.

So I think there are avenues in existing law to provide for the bad apples. The good apples are, as you are suggesting, for thousands of people who cannot get representation for small claims. If it is an after-dispute situation, the companies are not going to just mail a person a check. They have sort of got the person over a barrel, and that is why eliminating pre-dispute arbitration is not a good idea. More people will suffer than would gain.

Senator CORNYN. Thank you, Mr. Chairman. I am going to have to leave, unfortunately, because of the joint address to Congress. The President of South Korea is here addressing Congress. But thank you very much for holding the hearing.

Senator FRANKEN. If you have a second before you leave, I just would like to bet you a steak dinner that you cannot find before 4 o'clock the mandatory arbitration clause in here.

Senator CORNYN. I do not know what that is you are handing me.

Senator FRANKEN. I am sorry. It is terms and conditions for a checking and savings account in a bank.

I am kidding. You do not have to do that. I would not do that to you.

Senator CORNYN. Well, my point is, Mr. Chairman, that even though consumers may not know there is an arbitration provision in the contracts, there is a positive societal good for having an expeditious and inexpensive way to have these small claims resolved without litigation. I have spent most of my professional life in a courtroom, and like others here on the panel who have as well, giving someone a guarantee to a jury trial for a small dispute when they cannot find a lawyer to represent them, with tremendous delays associated with repetitive appeals, is not my ideal of justice.

We need to provide an opportunity for people to have a forum that is fair and involves efficient resolution of disputes appropriate to the nature of the dispute and subject to the existing law. That is my position.

Thank you.

Senator FRANKEN. Thank you. I understand that.

We will go now to Senator Blumenthal.

Senator BLUMENTHAL. Thank you, Senator Franken, and thank you for your leadership in this area, which I think has been very, very valuable. Attorney General Swanson, you can tell the people of Minnesota that they are well served by Senator Franken's leadership.

I want to ask you first, part of the problem in the National Arbitration Forum practices resulted from the arbitration clauses essentially being concealed or obfuscated. Is that correct?

Ms. SWANSON. Mr. Chairman, Senator Blumenthal, that is part of the problem. The National Arbitration Forum actually employed a vice president of clause placement who was in part paid commissions to go out to large corporations and convince them to put clauses in the agreements. It would help write the clauses that would go into the agreements and then afterward would actually help file and write the claims that would be used against consumers. But, absolutely, that was one of the problems, is the clauses were concealed and not very obvious.

Senator BLUMENTHAL. And you would agree, Mr. Schwartz, that that kind of practice really is abusive and should be illegal?

Mr. SCHWARTZ. If the laws in Minnesota were violated, they should be prosecuted.

Senator BLUMENTHAL. Well, in your view, you would condemn such practices, would you not?

Mr. SCHWARTZ. The type of things that the Attorney General spoke of on their surface—I have not looked at the whole case—do sound like that they are illegal.

Senator BLUMENTHAL. Would you agree that clauses that are not fairly explained and indeed are concealed or obfuscated requiring arbitration are abusive and should be illegal?

Mr. SCHWARTZ. Well, fairness is in the eyes of the beholder, so I have difficulty answering that question at that degree of generalization.

Senator BLUMENTHAL. So that a clause that is concealed in fine print, deliberately hidden from consumers, would be OK with you?

Mr. SCHWARTZ. That is a "When did you stop beating your wife?" question. I mean, if somebody deliberately makes it so obscure that no reasonable person could find something, then you walk into unconscionability, sir.

Senator BLUMENTHAL. Well, isn't the problem really today in the wireless and the cable industry and many industries where there really is effectively no consumer choice, that not only is there a lack of what you have called "equal bargaining power" but also that consumers cannot, even with due care, discern that there is a mandatory pre-dispute arbitration clause? Isn't that part of the problem today?

Mr. SCHWARTZ. I think that there should be, and there are, alternative as—when we talk about cell phones, some companies do not

require mandatory arbitration agreements, and that market forces should be used to have people have situations where they have a choice. And if there is just no market for it, then there is no market for it.

Again, I am not talking about something where somebody is engaged in behavior that violates a State law. That was something that the Attorney General went after. But fine print is part of our lives. There is fine print on a lot of things, and that alone is not, to me, an unlawful practice.

Senator BLUMENTHAL. Well, I do not disagree with you that fine print is not unlawful. The question is how the fine print is depicted, and I would be willing to say, without knowing the answer—and I learned as a prosecutor never to ask a question if I did not know the answer—that you have defended and prosecuted cases where there were in effect unfair practices that may not have violated the law but your feeling was they should have violated—there should be a law to prohibit them.

Mr. SCHWARTZ. I have not had the privilege that you have had to be Attorney General of a State or a prosecutor. I have been a plaintiffs' lawyer, and I have done defense work. But I have not engaged in criminal practice of law on either——

Senator BLUMENTHAL. But there are many contracts that you have encountered that essentially were misleading if they were not properly explained?

Mr. SCHWARTZ. This is just my personal life. I have not encountered that type of thing, and if I ever have, I simply would not deal with that merchant or deal with that service provider. But that would be—that is a personal answer in my life.

Senator BLUMENTHAL. But, in fact, in many instances of consumer life, consumers may have no choice, even if there is no gun pointed to their head, which is, again, the phrase you used, but to use a service or buy a good where pre-dispute mandatory arbitration is imposed. And we are not talking about arbitration that is knowingly entered into after there is a dispute. We are talking about mandatory pre-dispute arbitration without in any way dismissing your arguments that there may be benefits to knowing and informed arbitration clauses after the dispute has arisen.

Mr. SCHWARTZ. I want to know more about—and you can share with me, or this hearing is not the end of all hearings on this subject—precisely the type of situation that you are talking about where the person absolutely needs the service. I mean, a surprise to some in this room, I lived in a world where there were no cell phones, and I kind of made it. I was all right. So that is why I want to get a little bit more specific. If somebody cannot eat or cannot buy food in a supermarket, that is something I would want to think about. But I do not think where I go to Shopper's Food Warehouse—maybe they will give me a discount for mentioning them—that there is some agreement when I am buying those groceries that I cannot sue them if the food is bad.

Senator BLUMENTHAL. Well, my time has expired. I appreciate your——

Senator FRANKEN. We will do a second round.

Senator BLUMENTHAL. I appreciate your testimony, and I am grateful that there will be a second round. Thank you. And in the

meantime, I am going to try to find the arbitration clause in here, although I have not been promised a steak dinner.

[Laughter.]

Senator FRANKEN. If you can find it, you will have a steak dinner.

Senator BLUMENTHAL. Thank you.

Senator FRANKEN. And that goes for you, Mr. Schwartz. Would that be fair to you to ask you to find the arbitration clause in that document?

Mr. SCHWARTZ. I think that would be fine, but I do not want to do it here because I do not want to interfere with the President of South Korea. I will do it——

Senator FRANKEN. I think he will be done with his speech before you find it.

[Laughter.]

Senator FRANKEN. Senator Whitehouse.

Senator WHITEHOUSE. Thank you, Chairman. First of all, let me thank you for holding this hearing. I think Americans today are the people in the history of the planet who are most bedeviled by fine print, and it is an unfortunate and noxious part of most of our daily lives. As Mr. Schwartz had pointed out, it is not illegal for there to be fine print, but, nevertheless, we do find that there is an enormous amount of mischief that is often buried in the fine print. Indeed, your Attorney General who is here discovered really a systematic racket run for the purpose of cheating consumers by not just some little fly by-night corporation but by the largest arbitration company in the country.

So it is hard to deny that this is a really significant issue when you look at how bad the practices are, how one-sided the negotiating posture is, and just the plain experience of it. I mean, you can just stack up people like Dr. Pierce over and over again who have had miserable experiences with arbitration, did not know, for instance, that the companies that appeared before the arbitrators all the time got to pick who the arbitrators were; and if you ruled against them, they could knock you out. It is like picking a panel. If you do not get a hanging judge, you throw them out until you have got all hanging judges, and because you are coming in case after case, you can basically filter out anybody who will decide for consumers. Unless you are that lucky person who got that arbitrator for the first time, who decided for you before they came in and swept you out for having had the temerity to decide for a consumer. And the problem of take-it-or-leave-it contracts makes it just so much worse, and I think Mr. Schwartz was stretching the credulity of this Committee a little bit when he suggested that one could get by in this modern age, particularly in a busy life, as he has, without access to, say, a cell phone. Maybe you have a lot of staff people who can run around with you and answer the phone, but I think for most Americans, a cell phone is a pretty basic thing, and I do not think anybody feels they have negotiating leverage in that contract.

Take a look at a credit card contract. Those used to be a page or two long. Now they are 20 pages long. We have an entire agency that has had to be built to try to cope with the tricks and the traps that were built into the credit card contract, such as declaring the

day over at 11 in the morning so that when they opened the mail after 11 in the morning, mail that came in that day was late, and the consumer could be whacked with a significant interest rate increase. That is the kind of practice that creeps into the fine print. And so I think it is really important that we do this.

My observation on this is the following: The Bill of Rights provides, "In suits at common law, where the value in controversy exceeds $20, the right of trial by jury shall be preserved." Fairly strong, clear language.

The Bill of Rights also provides in the Second Amendment that, "A well regulated militia, being necessary to the security of a free state, the right of the people to keep and bear arms, shall not be infringed."

I would be interested in how many of my colleagues on the other side of the aisle would be willing to concede that in hidden language in a pre-dispute contract you could be obliged to give up your Second Amendment rights. I think we would hear pretty strong blowback from some very big organizations and from a lot of folks. And yet for some reason the individual right to a trial by jury does not seem to have the same energetic defense. And that was interesting because we just had in the Judiciary Committee Justice Scalia and Justice Breyer for kind of a novel discussion about the role of the Court, and they both agreed how important the jury was not just as a little machine that sat in the judicial system to do fact finding, but in the overall plan of the American system of Government, it was part of the architecture that the Founders put together of bicameral legislature, of independent judiciary, of separate executive, and of a jury where, when all else failed, you could get heard by a jury of your peers. And it strikes me that there is a lot more at stake here than just settling disputes when the right to the jury that is in the Constitution is so readily dealt away.

Attorney General Swanson, your reaction?

Ms. SWANSON. Mr. Chairman, Senator Whitehouse, I agree with that. I think that it is very much a strong part of our American history and culture as well as in the Constitution that people ought to have their right to have their day in court. Yet millions upon millions of consumers in America are losing that right to have their day in court before a jury in the fine print of these outrageously long contracts without even knowing it and without having meaningful choice. As we have seen in our case involving the National Arbitration Forum, often that has resulted in a tremendous injustice where essentially the little guy, the consumer, ends up not getting a fair shake. And, you know, in the case of the National Arbitration Forum, you essentially had that arbitrator who by his own words was in hundreds of millions of consumer contracts in America acting as the judge, the jury, the law clerk, and almost the plaintiff all in one. And it engaged in conduct that would never be tolerated in a court of law, that would not be allowed in a court of law, going out there hustling clients to sign up with it so they could then deprive people of their legal rights.

Senator WHITEHOUSE. What industries are the worst offenders in terms of—I should not say "worst offenders." What industries do American consumers engage with who are the most frequent con-

tracts that American consumers enter into? Cell phones, credit cards. Who else?

Ms. SWANSON. Mr. Chairman, Senator Whitehouse, it runs across the table. In addition to the ones you mentioned, it is utilities, it is satellite television services, virtually—pick a service contract that has—you know, the 20-, 30-page service contracts, it is in there. You know, in the financial services industry, they will put arbitration clauses in.

An area that is increasingly a problem are these debt buyers. It is oftentimes not just the initial creditor now who is pursuing a claim, but credit card companies, cell phone companies, others will sell debt for pennies on the dollar, maybe 3 cents on the dollar. Billions of this debt is bought and sold every day in this country. Debt buyers will generally only buy a data stream of electronic records of consumers who might owe money, and so we have seen many abuses where debt buyers, who oftentimes are the third or fourth debt buyer removed from the initial contract, pursue people who either do not owe the money—maybe they have a similar-sounding name or a similar address; maybe they were a victim of identity theft; maybe they paid back the money long ago. Yet arbitration has even been used as a sword against them.

And so imagine the surprise of a consumer who was handed a 20- or 30-page fine-print contract from an original creditor, only to have that creditor sell the debt ad nauseam down the stream to companies they have never heard of and then to get hauled into arbitration by an arbitration company they have never heard of in a faraway State. We heard from people like that, and they said, "We did not feel we had a fair shake. We did not even respond to the arbitration claim because we did not think it was for real. We had not heard of the plaintiff, and we had not heard of the arbitration company." And that is not giving the American consumer a fair shake.

Senator WHITEHOUSE. Well, thank you, Chairman, for your efforts to see that American consumers do get a fair shake.

Senator FRANKEN. Thank you, Senator Whitehouse.

I was really struck by what you said about the Constitution because, in fact, this is a bank contract, and on page 86 of this contract, you do give up your right to bear arms.

[Laughter.]

Senator FRANKEN. I mean, it is an amazing coincidence about that, and I think that it is too bad our colleagues are not here to be as upset about that as they would be.

I was also struck by your talking about—picking up on what Mr. Schwartz said about having lived in a world without cell phones. In fact, in your written testimony you testified that, "Consumers and employees voluntarily enter into these contracts." And I would submit that they do not know their—I do not think this is voluntary. And Dr. Pierce did not know, and Dr. Pierce is probably—how many degrees do you have? A few. How many? Just give me some idea of what they are.

Dr. PIERCE. I have a bachelor's in chemical engineering, a master's in biochemistry, and a doctorate, medical doctorate.

Senator FRANKEN. OK. So you are probably in the top, you know, 50 percent of education in this country.

[Laughter.]

Senator FRANKEN. Right?

Dr. PIERCE. I hope so.

Senator FRANKEN. OK. And you were not aware that you had an arbitration agreement. OK. Mr. Schwartz testified that, "Consumers and employees voluntarily enter into these contracts. It may seem extraterrestrial, but I have lived in a world where people did not have cell phones or the gadgetry we see in our daily lives. Folks did survive."

Mr. Bland, this seems to me to suggest that if consumers do not like mandatory arbitration clauses, they should just avoid them, and this strikes me as kind of dubious. In your opinion, is it really possible to live a normal, 21st century life and manage to avoid arbitration clauses? What would they have to live like, exactly?

Mr. BLAND. Well, these clauses are in everything. I mean, they are in everything. I have seen a mandatory arbitration clause in an organ donor transplant contract. I have seen mandatory arbitration clauses in pet kennel contracts. You want to take your cat in while you go out of town. You cannot buy a new car in the United States without signing an arbitration clause because the car finance company has made all the new car sellers—at least if you finance the car. To get a car you have to have an arbitration clause. The major cell phone companies all have arbitration clauses.

There is almost nothing you can buy on the Internet—if you want to buy a computer—almost any service or good you want to get on the Internet, you click a box, and if you open up the box and scrolled and scrolled and scrolled and scrolled and scrolled and scrolled, et cetera, you know, at some point you would find the arbitration clause buried way in there. It is ubiquitous throughout American society now.

The idea that, yes, you know, you have a choice to live in a world where you do not have a phone or a credit card or a car or play computer games or have, you know, children who eat——

Senator FRANKEN. The Unabomber could have avoided a mandatory arbitration clause.

Mr. BLAND. And he was a very free man out there, you know. He enjoyed all sorts of freedoms in that cabin, I am sure. But, yes, exactly, it is completely unrealistic. And the idea that it would be an organ donor transplant or that it is a requirement before you can get into a nursing home, you know, the vast majority if not over 90 percent of nursing homes in America have mandatory predispute binding arbitration clauses. I talked to a ton of people who were in these homes who had no idea that that was there. They signed something. A lot of these people are in pain. I represented a client who was a stroke victim who they got to sign one of these arbitration clauses. She had no idea. Actually, I should not pick her out like she is particularly—I mean, even though she is particularly vulnerable, I have talked to over 1,000 consumers doing case intakes for consumer cases. I have never met a consumer who knew that the arbitration clause was there before a lawyer had told them, usually me. It is like being an oncologist giving people bad news. They say, "Do I have a lawsuit here?" It is like, "Actually, you probably do not have a lawsuit because there is an arbitration

clause that is going to bar you from suing, and you have to go to someone who they pick." And people cannot believe it. They are furious. They are outraged. The idea that all these people chose to do this, this idea that there is this voluntary choice, that all these Americans are out there saying, "Gosh, what I was really hoping to do was be forced into mandatory arbitration in front of this company in Minnesota." You know, I do not meet those people in my real life, and I answer my phone a lot.

Senator FRANKEN. Professor Drahozal in his testimony talks about empirical evidence. In service of empirical evidence, he says that 82.9 percent or 247 of 298 credit card users do not use mandatory arbitration clauses, which I think implies to anyone who reads it that mandatory arbitration is not widespread. But that does not reflect the number of credit card users, does it? So when we are using empirical research, there are numbers and then there are damn lies, right?

Mr. BLAND. Yes, Senator.

Senator FRANKEN. I am sorry. That was——

Mr. DRAHOZAL. I would be happy to talk about those numbers, but I am not going to take up your time.

Senator FRANKEN. OK.

Mr. BLAND. A tiny number of banks control nearly all the credit cards in America. If you take Citi and American Express and Discover and Chase and so forth, if you get about seven or eight credit card issuers, you are up over 90 percent, if not over 95 percent——

Senator FRANKEN. So, in other words, the big issuers are the ones with the arbitration contracts—mandatory arbitration——

Mr. BLAND. Although right now at the moment, four of the biggest credit card issuers do not have the arbitration clauses or class action bans because there is an antitrust suit which alleged that they had all gotten together and agreed to have essentially the same arbitration clause. And so to settle the antitrust case, four of the biggest banks in America are sort of taking a time-out in which they agreed to a settlement and which they said that they would not use mandatory arbitration for 3½ years. And then, you know, of course, on the 181st day of the fourth year they are going to rush and put these things back in. And then you will have upwards of 95 percent of all American credit card holders having arbitration clauses again.

Senator FRANKEN. OK. Well, I think it is important to be careful how we use empirical data. I would like to go to Senator Blumenthal.

Senator BLUMENTHAL. Thank you.

Professor, I wanted to ask you about some of the empirical work that you have done. Have you focused specifically on mandatory pre-dispute——

Mr. DRAHOZAL. Yes, there are two different types of studies that you do. One is you look at the arbitration proceedings and see how the arbitrators decide things, and the vast majority of those proceedings arise out of pre-dispute agreements. So the proceedings are the result of arbitration clauses in form contracts. And then the other type of study is to actually look at the contracts, so the credit card data that Chairman Franken referred to is data I collected from a Federal Reserve web page that now has available every

credit card, supposedly anyway, virtually every credit card contract in the country, and those are all pre-dispute.

Senator BLUMENTHAL. Do you divide your research into clauses that are mandatory and clauses that offer some choice?

Mr. DRAHOZAL. When looking at the arbitration clauses, a lot of credit card issuers do not have arbitration clauses at all, but they tend to be small banks or credit unions. So there are choices out there for consumers. So there are lots of choices in that sense, although not many consumers take them up on it.

Within the clauses themselves, some of them have opt-out provisions that are similar in result to the poultry contracts that the Chairman referred to earlier, where the contract shows up and the consumer has the option under the terms of the contract to opt out. So those in a sense have a choice, at least formally.

Senator BLUMENTHAL. Do you know what proportion of mandatory arbitration clauses—or strike that. Do you know what proportion of arbitration clauses are mandatory and are pre-dispute as opposed to post-dispute?

Mr. DRAHOZAL. By definition, all arbitration clauses are pre-dispute because they are clauses in a contract. There are arbitration agreements that are entered into post-dispute, and I do not know of any evidence of the number of those agreements.

Senator BLUMENTHAL. Well, there by definition would be decisions made post- or pre-dispute to enter into arbitration. Is that correct? In other words, you can decide after the dispute arises to enter into the arbitration or you can agree before?

Mr. DRAHOZAL. Right. In the latter case, there is no good evidence on how many agreements there are, post-dispute agreements, but there are very few arbitrations that arise out of post-dispute agreements.

Senator BLUMENTHAL. And have you looked at what the costs are relatively to those arbitration clauses that are agreed to after the dispute as opposed to mandated pre-dispute?

Mr. DRAHOZAL. In the evidence I have looked at and the evidence I have seen, both in the employment context and in the consumer context—there are just not enough cases——

Senator BLUMENTHAL. And the reason is that there are very few instances where consumers are offered any real choice. Isn't that correct?

Mr. DRAHOZAL. I guess I would say there are very few circumstances in which parties after a dispute arises can agree to arbitrate, because at that point it is in one party's interest to be in court. It is either going to be in the business's interest if they want to try to go to an expensive forum that the consumer will not be able to bring a claim in, or it is going to be in the consumer's interest if they have a claim that they think that they want to get before a jury, for example.

So you are right, I agree. After a dispute arises, parties cannot agree. But I think it is because of the litigation dynamics at that point that they just cannot come to an agreement to arbitrate. They will just plow ahead in court, which is the default.

I am sorry. I may not be understanding your question. I apologize.

Senator BLUMENTHAL. No, I think you have answered the question that there really is not enough data to show that the costs and the time that we are trying to save really are the result, necessarily the result of mandatory pre-dispute arbitration clauses because the others are relatively rare, for whatever reason.

Mr. DRAHOZAL. I would say it is the other way around, though. You are not going to get the cost savings in arbitration if you limit it to post-dispute because nobody is going to agree post-dispute.

Senator BLUMENTHAL. And you may be right——

Mr. DRAHOZAL. So the cost savings are pre-dispute.

Senator BLUMENTHAL. You may be right, but you do not have research to show it as you sit here.

Mr. DRAHOZAL. The research, the data that are available suggest very rare incidence of post-dispute agreements.

Senator BLUMENTHAL. Because they are relatively rare.

Mr. DRAHOZAL. Yes, absolutely.

Senator BLUMENTHAL. In other words, almost all of the clauses are mandatory pre-dispute clauses that are imposed by companies like AT&T or the bank—and I do not want to single out the bank that—and I have read it, and quite honestly—and I have had some litigation experience myself. . . . I cannot really understand it.

Mr. DRAHOZAL. Credit card contracts are actually much better, for what it is worth. They have a lot of bold print about arbitration in general, and you can actually search them on the Federal Reserve web page. My guess is we could find it fairly quickly if we had Google and could do it electronically. But, yes, they are long contracts, and there is a lot of stuff in them. Agreed.

Senator BLUMENTHAL. Thank you.

Senator FRANKEN. Senator Whitehouse.

Senator WHITEHOUSE. It strikes me, Professor Drahozal, that there is a lot of import to the statement that you made—I think I have it exactly right because I wrote it down just as you said it—"nobody is going to agree post-dispute to an arbitration clause."

Mr. DRAHOZAL. I guess I would say very rarely, but yes. You probably quoted me right, but very rarely——

Senator WHITEHOUSE. When you have a post-dispute arbitration, it is between two construction companies that have an issue, and they do not want to hassle it out, they do not want to be in court, they do not want the lawyers involved. They are going to have a long-term relationship. They are friends. The CEOs probably play golf together. They need this sorted out. They bring in an arbitrator, and they agree whatever the outcome is going to be, that is what it is. But they are big players, and that is the sort of archetypal post-dispute arbitration agreement——

Mr. DRAHOZAL. No, no. Actually, most big businesses that use arbitration agree in contracts as well. If you look at the data on international arbitrations, which are big players——

Senator WHITEHOUSE. No, no. I am asking about post-dispute.

Mr. DRAHOZAL. They have very few post-dispute arbitration——

Senator WHITEHOUSE. And they tend to be big companies that are trying to sort out some problem, right?

Mr. DRAHOZAL. No, actually—I mean, the rates are similar.

Senator WHITEHOUSE. What do they tend to be?

Mr. DRAHOZAL. The rates are similar between consumers, employees, and big businesses. Nobody uses post-dispute arbitration—again, I am exaggerating, "nobody." It is very rare.

Senator WHITEHOUSE. But you are saying that for effect, and I understand you did not mean that to be 100 percent true.

Mr. DRAHOZAL. I was being a little sloppy.

Senator WHITEHOUSE. But there is a point that is buried in there, which there is a reason that nobody is going to agree post-dispute. It is because these are one-sided agreements that somebody loses advantage by virtue of this. Otherwise, they would be empirically just as willing to agree post-dispute as pre-dispute. No?

Mr. DRAHOZAL. Yes, and the advantage varies depending upon the case. Sometimes it is the consumer who loses, sometimes it is the business who would lose. And since it is pre-dispute, they can work it out and they do not know——

Senator WHITEHOUSE. How often do you suppose it is the business in a large-scale consumer arbitration clause that—empirically, how often do you think it is the business that loses as the result of that rather than the consumer once the——

Mr. DRAHOZAL. That is hard to know. There actually is——

Senator WHITEHOUSE.—dispute arises?

Mr. DRAHOZAL. There are no systematic data either way as to how often it is the consumer or how often it is the business. There actually is a case involving the motor vehicle franchise arbitration statute, which makes unenforceable arbitration clauses between car dealers and manufacturers. There actually is a recent case where the car dealer wanted to arbitrate, and the business said, No, the statute says these agreements are unenforceable. So you do see it. It is hard to know how often, I agree, but that is a lack of data, and there are attempts to find out the answers to those questions. But it certainly happens, absolutely.

Senator WHITEHOUSE. And if you have one of these consumer take-it-or-leave-it arbitration clauses that are in a general contract, are they limited to small dollar amounts, or do they have a threshold so that if it turns out to actually be a really big deal for somebody, they still have their right to get before a jury and that this is really just a way of sort of clearing the decks of the small clutter, the $100 disputes here and there? Is there a cap on them once the dispute gets to a certain point you actually get to go back to the jury again?

Mr. DRAHOZAL. No, it is usually the other way around. There is a floor. The American Arbitration Association's policy is that consumers can always go to small claims court. An increasing number of credit card contracts have that as well. So it is in some ways the other way around, that up to a certain point for very small claims, whatever the threshold is for small claims court, which varies by State, consumers or businesses both can still go to court.

Senator WHITEHOUSE. But if it is a bigger claim and, therefore, more dangerous to the company, then that is when they push you toward arbitration under the clause?

Mr. DRAHOZAL. Well, I would say there is probably an in-between category—these were the cases that Mr. Schwartz would be talking about—where the claims are big enough—and, again, there is some data that is consistent with this—that the claims are big enough

that they could be brought in arbitration, but they are not big enough to get a lawyer to justify going to court. But then beyond that——

Senator WHITEHOUSE. But that was not my question. My question was: In terms of the way these arbitration clauses are structured, your testimony is that the structure is that they tend to kick in for higher-dollar claims and let you out for lower-dollar claims. They give you a right to small claims court, but if it is a more significant claim than small claims court, that is where you really are barred by the arbitration clause. Do I have that correct?

Mr. DRAHOZAL. I would say there are three categories. There are the very small claims where you can go to small claims court under the clauses. There are the mid-sized claims which are not big enough to justify going to court, but that you could bring in arbitration. And then there are the very big claims that you would want to go to court for. And the theory or the argument is—and, again——

Senator WHITEHOUSE. And the arbitration clause covers both of the latter two?

Mr. DRAHOZAL. Both of the latter two. And so the implicit deal that you can make in pre-dispute arbitration that you cannot make in post-dispute arbitration is the consumer gets the right to bring the mid-sized claims in arbitration in exchange for giving up the right to bring the big claims in court. And, again, there is some data consistent with that, but it is a hard thing to study.

Senator WHITEHOUSE. And one last question, if I might, for the Attorney General. You have looked at a lot of this. You are pretty expert. You brought the case against the arbitration company, your office did. If you are in one of these consumer contracts, like a telephone or a credit card or other type of contract, how variable is the nature of the claims themselves? Does it tend to be that each one is its own type of claim and it would be really hard to aggregate them? Or would it be more likely that they would be the type of claim that you could actually probably get a couple hundred consumers together because they are all being screwed the same way, to be blunt about it, and, therefore, if you did not have the arbitration clause, you would actually have no trouble getting a lawyer and getting into court even if you were in Professor Drahozal's second category because so many other people are being treated just the same unfair way you are that you can aggregate it and you can actually get some justice that way? What is your take on that?

Ms. SWANSON. Mr. Chairman, Senator Whitehouse, my take on that is that they tend to fall into the latter category. In other words, there is a lot of commonality oftentimes between the claims. It might be a corporation engaged in a systemwide deceptive trade practice where consumers are basically cheated out of smaller amounts of money, but cheated in the same way oftentimes using the fine-print language of the contract to first cheat the consumer or deceive the consumer, but then they are using the contract language to try to take away their rights. So my impression is there is a lot of commonality. In fact, some of the claims that we as State Attorneys General bring, obviously not being able to represent a private individual, we have to bring cases where the public interest is affected, and I think certainly a lot of the cases that we bring

could be claims that people could also bring on their own potentially because of the uniformity.

Senator WHITEHOUSE. And by definition, if it is systematic deception by the company, it is going to sweep a large number of consumers into the same category of deceived consumer.

Ms. SWANSON. That is exactly right, thousands, tens of thousands, or more consumers similarly situated.

Senator WHITEHOUSE. OK. Thank you very much again, Chairman. I think this has been a very helpful hearing, and I appreciate that you——

Senator FRANKEN. What do you mean "been"?

Senator WHITEHOUSE. Well, I have to leave now so it is going to be less interesting after I am gone.

Senator FRANKEN. That is for sure.

[Laughter.]

Senator FRANKEN. I am sticking around for a third round. I am not sure if you have to go. You do? OK. Well, you just got me.

Senator BLUMENTHAL. But I would like to thank the witnesses very much for being here. You have been excellent, and this has been very informative, and I really appreciate your work, Mr. Chairman. Thank you very much.

Senator FRANKEN. Thank you. I am going to just ask a few more questions.

Mr. Bland, in terms of the last question that Senator Whitehouse asked and that General Swanson spoke to, the commonality of small kinds of ripoffs, essentially, can you give us maybe one or two examples of those kinds of things?

Mr. BLAND. Sure. AT&T added onto its monthly bill $3 for roadside assistance. I do not know if you know what it is. The idea, I guess, is that if you get lost, you know, AAA would be able to find you because they could use the GPS on your cell phone. They do not ask people whether they want this or not. They do not get any approval. They do not get any prior authorization. You just suddenly have this new service you did not order which costs $3. They do this for millions of people.

So we had a class action in Florida saying that they should not be allowed to charge people for some hidden charge in the bill that people did not authorize, did not agree to. It breaks the contract. It is a deceptive trade practice and so forth.

Senator FRANKEN. But according to *Concepcion*, can you file that?

Mr. BLAND. Well, we argued—I represented the plaintiffs in this case. We argued that *Concepcion* had an exception that in limited cases where you can prove that without a class action that people would not be able—that they would be completely shut out and get no justice, the catch phrase in the Supreme Court is they would not be allowed to "effectively vindicate" their rights, that if you could prove with evidence that without a class action people would not be able to effectively vindicate their rights, that the class action ban should be struck down.

The Eleventh Circuit Court of Appeals ruled against us, and they said in their decision—which I think is wrong, but you have seen a lot of courts doing this in the wake of *Concepcion*. The Eleventh Circuit said that we have proven that only an infinitesimal number

of consumers would ever be able to get their rights under the consumer protection laws vindicated, and everyone else would be out of luck, even if everything that had happened to them was illegal, but that still, according to the Supreme Court in *Concepcion*, the way this Federal court of appeals read *Concepcion* meant that the class action ban had to be enforced and the arbitration clause had to be enforced and the case was thrown out.

So you have a bunch of people who are scammed all in the exact same way, and only an infinitesimal number of people are going to be able to go forward under arbitration in individual cases to get their money back, and everyone else is out. And so AT&T basically is rewarded because they have done something that is a scam——

Senator FRANKEN. Let me get this right. So the court ruled that because an infinitesimal number of people could get their money back, their $3 a month back, then you could not go to court?

Mr. BLAND. It is not clear if this court——

Senator FRANKEN. Because infinitesimal was good.

Mr. BLAND. Yes, that was good.

Senator FRANKEN. It was better than zero.

Mr. BLAND. Well, you know, it is possible——

Senator FRANKEN. It had to be zero?

Mr. BLAND.—if it had been zero we still would have lost. I mean, they basically said that the Supreme Court wants these class action bans enforced so strongly, you know, even if we had been able to prove that no one ever, no matter what, could ever get through to arbitration, if the arbitration had been on—you know, the class action had to be on Mars on Leap Day or something, I still think that that court was going to say that the Supreme Court was telling it that you always have to enforce the contract.

Senator FRANKEN. You told me also about American Express or something?

Mr. BLAND. Yes. We represent a guy who is an accountant and extremely involved in math, and he got an American Express card because he wanted the rebate. You are supposed to be able to get up to 5 percent back. So he goes out and spends a bunch of money on his American Express card, and he checks the rebate. It takes him pages to try and figure out the formula that is set out in their contract, and he realizes that the rebate is much, much smaller than the formula that is set out in their contract. And he tries to get information from the bank, and they stonewall him and so forth. We end up bringing a class action.

It turns out that American Express just routinely cheats people on the rebate. The rebates are much smaller than they are supposed to be. You have a formula that is promised to you up to 5 percent. Nobody gets 5 percent. And you never get what the formula promises you. They simply have rigged a lower formula that gives you less than the rebate.

So we had a case in which we proved in court that this case could not be brought in an individual action. Almost nobody except for our accountant math whiz client even would ever figure this out that they were being cheated from this sum. But even say there were another 100 people like him who figured it out, they would not ever be able to find a lawyer. So even if they figured out how they were scammed and they figured out that you go to arbitration,

they would not know how to bring the right kind of claims under the consumer protection acts and sort of get their actual remedies back. But the point is that American Express is doing this to millions of people, and we have a Federal district judge in New Jersey who says it does not matter if nobody will ever get their money back from being cheated here, that the point of arbitration clauses is supposedly in 1925 Congress loved arbitration so much that it loved it way more than contract law, which does not let you have exculpatory clauses, and loved it way more than consumer protection laws, and that the Arbitration Act just wipes this all away. That is the way that Court reads *Concepcion*. So we are appealing. We think that that is a little extreme. It goes beyond that *Concepcion* is terrible but not that terrible. But, you know, there is a bunch of cases like this in which courts are throwing out class actions where it has been proven that without the class action no one will get any remedy. It is incredibly unfair.

Senator FRANKEN. OK. I believe one of the witnesses, either Mr. Schwartz or Mr. Drahozal—I think it was Mr. Schwartz—said that one of the myths is there is not due process. There were several myths that were listed, and one of them was that there is not due process in arbitration.

General Swanson, would you like to speak to that? Is there discovery? Is there appeal? What can you do?

Ms. SWANSON. Well, arbitration is very different than a court of law. First of all, you start with this selection bias where the people who are appointing the arbitrator are the corporations that draft the arbitration clause, and they get the power of deciding essentially what company will serve as the arbitration company, so they compose the panel of deciders, if you will, for that case. So that is sort of the first step along the way of the due process problems.

In addition to that, we have heard from many consumers when they do get hauled into an arbitration forum with an unknown company where they did not even know they had agreed to arbitration, they will ignore the paperwork, not respond to it because they do not think it is for real. They think it is a scam, and they simply throw it away, and then a judgment ends up being entered in their name without any ability on their part to appear.

In addition to that, no transparency. In court the dockets are generally open. You know where the filings are. You can read the record. In arbitration they are not, and so there is no transparency. They are secret proceedings, generally no appellate rights from arbitration, and so you are stuck with whatever the ruling is, and if you have one of those unfair arbitrators, then generally there is no ability to appeal it as you would in court. Everyone has a right to appeal final judgment of a district court, and that does not exist in arbitration.

Then, in addition to that, oftentimes arbitrators do not provide written records or written orders. A judge will usually elaborate and give a written order in terms of their rationale, what the findings are, why they ruled a certain way. Oftentimes arbitrators do not do that. It is simply you win/you lose, and that really can undermine consumers' confidence, understandably, in the integrity of the process. They do not know why they lost. They just know they

lost. And so a lot of those due process protections that are just fundamental to a court of law can be lacking in arbitration.

Senator FRANKEN. And there is no written decision, I mean, you do not have to produce a written decision in arbitration.

Ms. SWANSON. There is no requirement usually that a written decision be produced. An arbitrator could, but usually not. And so usually it is just judgment entered for corporation, $5,000, without any reasoning.

Senator FRANKEN. That hardly seems like due process.

Mr. Bland, I just want to read Professor Drahozal's conclusion because he talks about—and I think he spent a great deal of his career studying the empirical evidence here. Is that correct?

Mr. DRAHOZAL. A fair bit.

Senator FRANKEN. A fair bit of your career. So your conclusions—these are the conclusions: "To reiterate: my view is that sound public policy should be based on careful empirical study and not simply anecdotal reports. The available empirical evidence does not support the view that arbitration is necessarily unfair to consumers. Rather, that evidence suggests that pre-dispute arbitration clauses make some, if not many, consumers better off"—it suggests that—"and that broad-ranging restrictions on arbitration may well be counter-productive."

Does that seem like pretty thin gruel to you?

Mr. BLAND. It reminds me of the people who say that we have to keep studying global warming until it is too late to do anything or the people who used to say that you had to study, you know, whether or not whether cigarette smoking was bad for children. I mean, at some point there is a certain level of common sense, I think, that the Congress can act on. Here we have got a system in which one side to a dispute is essentially picking the judges in a non-transparent system where you cannot bring a class action even if everyone is treated the same and it is a small amount of money and that means it shut down everything, and you also have no meaningful judicial review.

I do not know why you need empirical evidence to get the idea that that is not a fair system. I do not see why you cannot apply some principled understanding as to what a justice system should be like. When the Founding Fathers said things like, well, we want to have a right to a jury trial, or they set out a variety of things you get to confront witnesses and so forth, they did not first go in and do studies to see, well, gee, you know, we are going to convict more people where you could not confront a witness or not. They could tell it was a fair idea. The idea of saying that you are going to have a system where one side picks the judges essentially, I think that that is clearly unfair in general. What happens is you have got the stronger party to a dispute setting up a system that systematically, repeatedly, predictably, and, in fact, in reality always ends up favoring them—or not always ends up favoring them, but the vast majority of the time ends up favoring them. And the idea that we need to study that more, I mean, we can always study everything. We could hire 100 professors to do studies forever. And is the chamber ever going to come in and say, you know, "It turns out it is not that fair to let our guys write the contracts on how to do disputes, you know, the studies finally proved scientifically

that letting us pick the judges turns out to favor us"? You know, I do not think we have to wait for that day because for one thing I will be dead, it will be so far from now. No matter what they do with the genome project, I will be dead by then. It is just never going to happen in our lifetime that they are going to admit that there is finally enough evidence.

You have enough evidence to tell that this is unfair. I think the Congress should act. I think your bill is great. I think you are a hero to the consumer movement with pushing this cause, and we are really grateful for it.

Senator FRANKEN. Well, thank you for saying that. We have been here a long time, and I do not want to try everyone's patience. I just want to thank you all for your testimony. I think you are right, Mr. Schwartz, that this is not the end of this, I am sure. And I want to thank you all for coming today.

The hearing will stand adjourned, and we will keep the record open for 1 week. Thank you.

[Whereupon, at 4:20 p.m., the Committee was adjourned.]

[Questions and answers and submissions follow.]

# QUESTIONS AND ANSWERS

**"ARBITRATION: IS IT FAIR WHEN FORCED?"**
**OCTOBER 13, 2011**

**Answers to Questions for the Record**
**Christopher R. Drahozal**

**Questions for Mr. Drahozal from Senator Cornyn**

- At the hearing, we heard from Mr. Bland that businesses are "essentially picking the judges" in arbitration. Please explain the typical procedures for selecting the arbitrator who will decide a given dispute. Can you explain the difference between an arbitration organization or administrator and the arbitrator himself or herself? How does existing law prevent the imposition of a biased decisionmaker by one party?

By definition, arbitration is a process in which a neutral decision maker — the arbitrator — chosen by the parties (not just one of them) resolves the parties' dispute. The arbitrator is distinct from the arbitration provider or organization. The arbitrator is the private judge, the person who resolves the parties' dispute. The arbitration provider or organization provides administrative services to the parties to facilitate the resolution of the dispute, but is not the arbitrator. An agreement that sets up a dispute resolution process in which one party unilaterally picks the arbitrator would not be enforceable under federal or state arbitration law.[1] Courts would invalidate such an agreement under general contract law principles,[2] and would vacate an award arising out of such a process on grounds of "evident partiality."[3]

Parties can agree to a variety of mechanisms for selecting arbitrators, all of which are designed to result in a neutral decision maker. First, the parties can agree on the arbitrator themselves.[4] Second, some arbitration providers use a listing process, under which the parties rank a list of prospective arbitrators and the highest ranked arbitrator is selected.[5] Third, with a three-arbitrator panel, each party can pick an arbitrator and have the two party-appointed arbitrators pick the presiding arbitrator.[6] Fourth, parties can agree to have the arbitration provider select the arbitrator, subject to a party's ability to strike an arbitrator the party finds objectionable.[7] Whatever the mechanism chosen, standards such as the Consumer Due Process Protocol make clear that "[a]ll parties are entitled to a Neutral [i.e., an arbitrator] who is

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1 Cheng-Canindin v. Renaissance Hotel Assocs., 57 Cal. Rptr. 2d 867 (Cal. Ct. App. 1996) (denying petition to compel arbitration because "there is no third party decision maker, the procedure totally lacks impartiality, and it is controlled exclusively by one of the parties to the dispute").

2 Hooters of Am., Inc. v. Phillips, 173 F.3d 933 (4th Cir. 1999) (refusing to enforce arbitration agreement when all arbitrators "must be selected from a list of arbitrators created exclusively by [the employer]").

3 9 U.S.C. § 10(a)(2).

4 *E.g.*, Am. Arb. Ass'n, Commercial Arbitration Rules, Rule R-12(a).

5 *E.g.*, *id.* Rule R-11(a), (b).

6 *E.g.*, *id.* Rule R-13(a).

7 *E.g.*, Am. Arb. Ass'n, Consumer-Related Disputes Supplementary Procedures, Rule C-4. For a description of the arbitrator selection process used in a AAA debt-collection arbitration program, see Christopher R. Drahozal & Samantha Zyontz, *Creditor Claims in Arbitration and in Court*, 7 HASTINGS BUS. L.J. 77, 105 (2011) (pre-screening of arbitrators to avoid conflicts of interest and random assignment of cases to arbitrators).



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independent and impartial" and that "[t]he Consumer and Provider should have an equal voice in the selection of Neutrals [i.e., arbitrators] in connection with a specific dispute."[8]

Mr. Bland's characterization seems to be based on the allegations of bias against an arbitration provider, the National Arbitration Forum (NAF). Even assuming the truth of those allegations (of which I have no personal knowledge), the NAF no longer administers consumer arbitrations. In 2009, the NAF agreed to stop administering new consumer arbitrations in settlement of Attorney General Swanson's consumer fraud suit against it.[9] And this year, the NAF agreed to stop administering consumer arbitrations altogether (when not prohibited from doing so), as part of a settlement of private litigation brought against it.[10] A federal statute making pre-dispute arbitration agreements unenforceable was not necessary to deal with the NAF; existing law proved adequate.

By comparison, for consumer arbitrations administered by the American Arbitration Association (AAA) (another arbitration provider), the Searle Study found: (1) no evidence of bias by arbitrators in favor of repeat businesses (instead the evidence suggests that any repeat-player effect is due to better case screening by those businesses);[11] (2) that the AAA's review of arbitration clauses for compliance with the Consumer Due Process Protocol "appears to be effective at identifying and responding to those clauses with protocol violations";[12] and (3) that the AAA refused to administer a significant number of consumer arbitrations because the business failed to comply with the Consumer Due Process Protocol.[13] In short, the available empirical evidence provides every reason to believe that the AAA does not engage in the sort of behavior that resulted in the demise of the NAF.

- Arbitration is different from litigation in court because parties have greater flexibility to vary applicable procedures by contract. How do current law and market dynamics ensure that the parties with greater bargaining power (usually companies) do not impose an arbitration system that deprives consumers or employees of access to fair procedures for resolving their disputes?

Both current law and the dynamics of the marketplace provide protections to consumers and employees from unfair arbitration clauses.

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[8] Consumer Due Process Protocol, principle 3, *available at* http://adr.org/sp.asp?id=22019.

[9] Consent Judgment, Minnesota v. National Arbitration Forum, Inc., No. 27-CV-09-18550 (Minn. Dist. Ct. July 17, 2009), *available at* http://pubcit.typepad.com/files/nafconsentdecree.pdf.

[10] Stipulation and Agreement of Settlement, In re: National Arbitration Forum Trade Practices Litigation, Civ No. 10-2122 (PAM/JSM) ¶ 4.1.1 (D. Minn. Apr. 6, 2011), *available at* http://www.arbitrationsettlement.com/pdf/settlement-agreement.pdf; Memorandum and Order, In re: National Arbitration Forum Trade Practices Litigation, Civ. No. 10-2122 (PAM/JSM) (D. Minn. Aug. 8, 2011), *available at* http://www.lieffcabraser.com/media/pnc/9/media.899.pdf (approving settlement). In addition, the settlement includes stipulated facts to assist parties in challenging awards made under the NAF's auspices. Stipulation and Agreement of Settlement, *supra*, ¶ 2.

[11] Searle Civil Justice Institute, Consumer Arbitration Before the American Arbitration Association 80 (Mar. 2009), *available at* http://adr.org/si.asp?id=6610.

[12] *Id.* at 110.

[13] *Id.* at 93.



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First, courts can and do police unfair arbitration clauses using a variety of contract law doctrines. The most common, of course, is unconscionability, which courts have used to invalidate a variety of provisions in arbitration clauses deemed to be unfair.[14] Although the Supreme Court's decision in *AT&T Mobility LLC v. Concepcion* held that the Federal Arbitration Act preempted California's use of its unconscionability doctrine to invalidate arbitration clauses with class arbitration waivers,[15] the Court's holding does not purport to preclude use of the unconscionability doctrine (much less other contract law doctrines) to police other provisions in arbitration clauses.[16]

Second, private regulation by arbitration providers enhances the fairness of consumer and employment arbitration clauses. As noted above and in my written statement, both the AAA and JAMS have promulgated "due process protocols" and enforce those protocols by refusing to administer arbitrations under agreements that do not comply. Such private regulation "complements existing public regulation of the fairness of consumer arbitration clauses," and "[a]ny consideration of the need for future legislative action should take into account the effectiveness of such private regulation."[17]

Third, businesses face reputational constraints in promulgating form contract terms, including arbitration clauses. As I have written previously:

> A business that develops a reputation for sharp dealing, whether through low-quality goods, arbitrary dealings with employees, or unfair contract terms — including arbitration clauses — will suffer in the marketplace. A good reputation is valuable to a business. Individuals regularly consider reputation in deciding whether to contract with a corporation. The individual need not have particularized knowledge of the "fine print" in the contract if he or she can rely on the corporations' general reputation for fair dealing.[18]

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[14] *E.g.*, David Horton, *Arbitration as Delegation*, 86 N.Y.U. L. REV. 437, 460 (2011).

[15] 131 S. Ct. 1740 (2011).

[16] *E.g.*, Mission Viejo Emergency Med. Assocs. v. Beta Healthcare Group, 128 Cal. Rptr. 330, 339 n.4 (Cal. App. 2011) ("Defendants appear to argue that *AT&T* essentially preempts all California law relating to unconscionability. We disagree, as the case simply does not go that far. General state law doctrine pertaining to unconscionability is preserved unless it involves a defense that applies 'only to arbitration or that derive[s] [its] meaning from the fact that an agreement to arbitrate is at issue.' This simply does not apply here."). Indeed, Mr. Bland has identified a number of grounds on which courts might continue to police the use of class arbitration waivers in arbitration clauses. Leslie Bailey & Paul Bland, How Courts Can and Should Limit AT&T Mobility v. Concepcion, *available at* http://www.publicjustice.net/Resources/How-Courts-Can-and-Should-Limit-ATT-v-Concepcion.aspx (last visited Oct. 31, 2011). While I do not agree with all of their positions, the listing certainly suggests that courts might continue to play an important role in regulating the use of class arbitration waivers even after *Concepcion*.

[17] Christopher R. Drahozal & Samantha Zyontz, *Private Regulation of Consumer Arbitration*, 79 TENN. L. REV. ___ (forthcoming 2012).

[18] Christopher R. Drahozal, *"Unfair" Arbitration Clauses*, 2001 U. ILL. L. REV. 695, 768-69.



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As I concluded then: "Certainly reputation does not perfectly constrain corporations from cutting corners at times (or just making mistakes), but it is a constraint that arbitration critics frequently fail to consider."[19]

- I want to be sure that consumers and employees have realistic opportunities to obtain redress for legal violations. Please explain how we can secure the most justice for the most people and why.

I agree that the goal of securing the most justice for the most people is an important and desirable one. In addition, of course, the cost of any dispute resolution system also must be taken into account. Such a cost constraint seems implicit in the question, which I understand to be asking how to provide the most justice to the most people given resource constraints.

I cannot (although I wish I could) explain how to accomplish that goal for every party and under every circumstance. As indicated in my written statement, however, arbitration pursuant to pre-dispute agreements can enhance the availability of justice for consumers and employees in ways that would not be possible if pre-dispute agreements were unenforceable. Employment lawyer Lewis Maltby, who I quoted in my statement, provides an illustration: "most employees will not be able to secure their employer's agreement to arbitrate once a dispute arises. The vast majority of employment disputes, however, do not involve enough damages to support contingent fee litigation. Therefore, outlawing pre-dispute agreements to arbitrate will leave many employees with no access to justice."[20]

Moreover, to the extent that arbitration reduces the process costs of resolving disputes, it will free up resources to be put to other uses, which may include dispute resolution or may include other things that benefit consumers (such as lower prices) and employees (such as higher wages).

- Are there any recent technological innovations that make arbitration more accessible, user-friendly, or efficient? Please describe.

The Internet and other technological innovations can be used to make arbitration more user-friendly and more accessible to consumers and employees. Online arbitration can provide a more flexible means of resolving disputes (consumers and employees can participate without having to miss work to appear in court, for example). It can also be faster (enhancing the speed of communications) and cheaper (permitting face-to-face hearings over the Internet and thus reducing or eliminating the need to travel).

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[19] *Id.*

[20] Lewis L. Maltby, *Out of the Frying Pan, into the Fire: The Feasibility of Post-Dispute Employment Arbitration Agreements*, 30 WM. MITCHELL L. REV. 313, 314 (2003).



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**QUESTION FOR THE RECORD FROM SENATOR CHARLES GRASSLEY
TO
PROFESSOR CHRISTOPHER R. DRAHOZAL**

1. Please provide any additional thoughts that you might have on the issues raised by the hearing, including but not limited to expanding on your testimony, responding to the testimony of the other witnesses and/or anything else that came up at the hearing, which you did not have a chance to respond to.

I appreciate the opportunity to conclude with a final comment on the current state of the empirical research on consumer and employment arbitration. It is simply not the case, as Mr. Bland seems to suggest, that I or others insist on the need to do more research in the face of repeated studies finding arbitration is bad for consumers.[21] The empirical record in fact shows the opposite: as I explained in my written statement, the available empirical evidence "suggests that pre-dispute arbitration clauses make some, if not many, consumers better off, and that broad-ranging restrictions on arbitration may well be counter-productive." That research, like all empirical research, is subject to caveats and limitations. But despite the caveats and limitations, such empirical research remains essential for sound policy making, and does not support broad-ranging restrictions on the use of pre-dispute arbitration clauses.

[21] Hearing Tr. at 92 (comparing defenders of consumer and employment arbitration to "people who say we have to keep studying global warming until it is too late to do anything" or objecting in the face of repeated studies that smoking does not cause cancer).



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**QUESTION FOR THE RECORD**
**FROM SENATOR CHARLES GRASSLEY TO VICTOR E. SCHWARTZ**
**FOLLOWING THE SENATE JUDICIARY COMMITTEE HEARING:**
**"ARBITRATION: IS IT FAIR WHEN FORCED?"**
**OCTOBER 13, 2011**

1. Please provide any additional thoughts that you might have on the issues raised by the hearing, including but not limited to expanding on your testimony, responding to the testimony of the other witnesses and/or anything else that came up at the hearing, which you did not have a chance to respond to.

It does need to be emphasized that in almost all situations involving consumer products and services a purchaser does have a choice to obtain what he or she wants without entering into a pre-dispute arbitration agreement. There are, for example, cell phones and credit card providers that do not require such agreements. Because these products generally cost more for consumers, and consumers typically do not purchase a product or service with a high expectation that they will want to sue the seller down the road, the cost-versus-benefit has not resulted in widespread consumer demand for them. If a situation arose where all sellers had pre-dispute arbitration agreements and there was a consumer demand for their absence, market forces would meet consumer demand because of the potential to significantly increase sales. To the best of my knowledge, that has not occurred because the demand has not been sufficient.

In addition, people seeking employment often have options to be employed where they are entitled to sue their own employer. Unfortunately, data suggest that even where this "lawsuit option" exists, it is not very helpful for employees who believe they have been wrongfully terminated. Some data suggest that the ability to obtain attorneys in such situations occurs only about five percent of the time.

In my own firm, Shook Hardy & Bacon, there is a pre-dispute arbitration agreement among partners. But, like doctors, accountants, and other professionals, I would have alternative options where I might have chosen to be a partner where such pre-dispute agreements are not requested. Again, the marketplace varies on this point; if there was universal application of such agreements, there would be data and other evidence to support that contention. Further, as is the case with products and services, if this was perceived by employees to be a major problem or injustice, employers seeking to differentiate themselves to attract more qualified job applicants would predictably decline to use such clauses in their employment agreements.

Another point I wanted to make, but did not have the opportunity during the hearing, relates to the argument that arbitration clauses are unfair because they can be "buried in the fine print" of consumer and employment agreements.

First, as a matter of sound public policy, consumers should be encouraged to fully read and understand the agreements they sign. If someone is making a significant purchase such as a car or home, or making a decision regarding a credit card or other financial instrument that they expect to own for years or even decades, they should be reading full terms of the contract. Similarly, any person entering into an employment agreement that directly relates to his or her livelihood, should be responsible for reviewing that agreement carefully. In turn, of course, businesses should endeavor to ensure that the terms of their agreements are comprehensible to customers and employees.

Second, the argument that arbitration clauses are "buried" in these agreements fails to put these provisions in the context of the complete consumer or employment agreement. Litigation or arbitration arising out of any consumer or employment agreement is a relatively uncommon occurrence. It makes sense that the arbitration provision would not in every case be shown prominently on the first page of the agreement. For example, consumers deciding whether to obtain a particular credit card are far more likely to be concerned with the monthly fees they will incur, ATM charges, and applicable interest rates on any late payments than they are with whether they must arbitrate their claim should anything go wrong. If arbitration clauses were placed in front of such provisions, consumers would likely complain that these other, more most important provisions of the agreement were then "buried in the fine print." Regardless, I believe this problem is greatly exaggerated. If a provision is truly obscured or intentionally difficult to understand, courts can and do address that problem via the doctrine of procedural unconscionability,[1] providing incentive for businesses to ensure that their contracts are forthright with respect to any arbitration agreement.

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[1] *See, e.g.*, *Razor v. Hyundai Motor America*, 854 N.E.2d 607, 622-23 (Ill. 2006) (procedural unconscionability may not be based solely on use of consumer form contract, but will be found where "a term is so difficult to find, read, or understand that the plaintiff cannot fairly be said to have been aware he was agreeing to it"). To be sure, courts will not invalidate terms simply because they are part of a form contract. *See, e.g.*, *Harris v. Green Tree Fin. Corp.*, 183 F.3d 173, 182-83 (3d Cir. 1999) (arbitration clause not procedurally unconscionable because of its placement on reverse side of contract). But particularly if an arbitration provision is difficult to find or understand, courts will almost certainly scrutinize the substantive terms very closely to ensure that they are fair. *See, e.g.*, *Armendariz v. Found. Health Psychcare Servs., Inc.*, 6 P.3d 669, 690 (Cal. 2000) ("the more substantively oppressive the contract term, the less evidence of procedural unconscionability is required to come to the conclusion that the term is unenforceable, and vice versa" (internal marks omitted)).



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Lastly, I simply wanted to clarify a point raised by the Honorable Senator Franken. He indicated that in one of my writings I had criticized state attorneys general for engaging in lawsuits on behalf of injured persons in their states, saying that it was "a subversion of two hundred years of law" and that it violated the idea of equal protection under law. I want to clarify that my article suggested that state attorneys general should pursue their role in enforcement of state laws just as Minnesota Attorney General Lori Swanson did when she found an arbitration group she believed had engaged in fraudulent practices. What my article suggested is that state attorneys general should not leave their role of enforcement of state law to become substitute plaintiffs' attorneys and bring novel tort actions that are best left to the private sector. When attorneys general do that, they engage in regulation through litigation, and often use tort law for purposes that it was not intended to achieve. The principal purpose of tort law is to compensate an individual who has been harmed by the wrongful conduct of another; tort law should not be used by state attorneys general as a substitute to the judgment of legislatures and the executive branches of government. Finally, to the best of my knowledge, I have never suggested that if an attorney general does engage in being a substitute plaintiff's lawyer that such action violates the equal protection provisions of the Constitution of the United States.

**QUESTIONS FOR THE RECORD**
**FROM SENATOR JOHN CORNYN TO VICTOR E. SCHWARTZ**
**FOLLOWING THE SENATE JUDICIARY COMMITTEE HEARING:**
**"ARBITRATION: IS IT FAIR WHEN FORCED?"**
**OCTOBER 13, 2011**

1. Some argue that, if arbitration of disputes involving relatively small claims is eliminated, individuals will not be disadvantaged because they will be able to pool most small claims into a class action in court. What percentage of consumer and employee claims are likely to be eligible for class treatment? In your view, are class actions an adequate substitution for arbitration?

An extremely small percentage of consumer and employer claims are likely to be eligible for class treatment. As the Supreme Court of the United States reiterated in *Wal-Mart Stores, Inc. v. Dukes*, 131 S. Ct. 2541 (2011), "[t]he class action is 'an exception to the usual rule that litigation is conducted by and on behalf of the individual named parties only.'" *Id.* at 2550 (quoting *Califano v. Yamasaki*, 442 U. S. 682, 700-01 (1979)). Under Federal Rule of Civil Procedure 23, which governs class actions in federal court, facts and legal issues common to a class must predominate over facts and legal issues not in common. The plaintiff who seeks to represent a class must be an adequate representative and must possess claims that are typical of other proposed members' claims. These hurdles are hard to overcome. In most cases, consumer and employee disputes involve highly individualized fact patterns, for example, a consumer had a unique charge on his or her cable bill or an employee was discriminated against in a particular way by specific individuals. The class action system, in contrast, is set up for people with claims that are almost identical, for example, people who have been killed in a plane crash. Thus, in most instances, class action treatment would not be available as a substitute for contractual pre-dispute arbitration. The data bear this out. Even of the subset of lawsuits actually pleaded as class actions, nearly four-fifths are never certified.[1]

If a class action does proceed, there are many instances where the plaintiff's lawyers who bring the case garner substantial fees and the individual consumers are left with little or no recovery. In some cases, as I indicated in my testimony, a charity selected by the plaintiff's lawyers may end up receiving more than the injured consumer. In addition, because "successful" consumers may only be entitled to collect a paltry sum in a class action, many consumers do not even bother to try to collect. Thus, the class action device often does not work to the benefit of consumers.

For each of these reasons, class action are, in general, not an adequate substitution for contractual pre-dispute arbitration.

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[1] *See* Thomas E. Willging & Shannon R. Wheatman, *Attorney Choice of Forum in Class Action Litigation: What Difference Does it Make?*, 81 NOTRE DAME L. REV. 591, 635-36, 638 (2006).



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2. I want to be sure that consumers and employees have realistic opportunities to obtain redress for legal violations. Please explain how we can secure the most justice for the most people and why.

Pre-dispute arbitration agreements provide a vehicle for both consumers and employees to obtain redress for legal violations. In many instances, these agreements provide parties with the only realistic opportunity to obtain relief, particularly in light of the significant shortcomings of class actions (discussed above) and the difficulty of finding a lawyer willing to take on a case involving a relatively small sum of money.

Arbitration offers user-friendly procedures that allow individuals to make their case even without an attorney. And the flexibility that arbitration offers is vastly underappreciated. Individuals may have a hearing scheduled for a convenient time and place; as alternatives, the parties (if they prefer), may be able to resolve the dispute by conference call or on the papers alone. We are even starting to see online claims resolution. When individuals in the real world weigh the costs and benefits of pursuing a claim, the ability to get resolution through a simplified, easy-to-use process—one that often does not require taking time away from work or home duties—can make a difference.

Naturally, to ensure that the greatest number of people receive justice, it is important that arbitration agreements are fair and that decisions are made by neutral arbitrators. But it is also important to recognize that existing law includes multiple layers of protection on this front. Through an evenhanded application of the unconscionability doctrine, judges are able to determine whether an arbitration agreement is "unconscionable" to an individual consumer or employee and therefore invalid. There are literally hundreds of such decisions striking down arbitration agreements when those agreements are unfair. For instance, procedures that would be unduly burdensome to the individual, such as an inconvenient location[2] or unreasonable costs,[3] will not be upheld. Nor will agreements that limit individualized damages or remedies that would be available to a customer or employee,[4] or unfairly curtail the window of time in which to bring a claim.[5] Further,

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[2] *See, e.g.*, *Hollins v. Debt Relief of Am.*, 479 F. Supp. 2d 1099 (D. Neb. 2007); *Dominguez v. Finish Line, Inc.*, 439 F. Supp. 2d 688 (W.D. Tex. 2006); *Philyaw v. Platinum Enters., Inc.*, 54 Va. Cir. 364 (Va. Cir. Ct. 2001); *Pinedo v. Premium Tobacco Stores, Inc.*, 102 Cal. Rptr. 2d 435 (Ct. App. 2000).

[3] The Supreme Court has held that a party to an arbitration agreement may challenge enforcement of the agreement if that agreement would force the individual to pay excessive costs to access the arbitral forum. *Green Tree Fin. Corp.-Ala. v. Randolph*, 531 U.S. 79 (2000); *see also, e.g.*, *Phillips v. Assocs. Home Equity Servs., Inc.*, 179 F. Supp. 2d 840 (N.D. Ill. 2001); *Camacho v. Holiday Homes, Inc.*, 167 F. Supp. 2d 892 (W.D. Va. 2001); *Brunke v. Ohio State Home Servs., Inc.*, 2008 WL 4615578 (Ohio Ct. App. Oct. 20, 2008); *Liebrand v. Brinker Rest. Corp.*, 2008 WL 2445544 (Cal. Ct. App. June 18, 2008); *Murphy v. Mid-West Nat'l Life Ins. Co. of Tenn.*, 78 P.3d 766 (Idaho 2003).

[4] *See, e.g.*, *Alexander v. Anthony Int'l, L.P.*, 341 F.3d 256 (3d Cir. 2003); *Mortgage Elec. Registration Sys., Inc. v. Abner*, 260 S.W.3d 351 (Ky. Ct. App. 2008); *Woebse v. Health Care & Retirement Corp. of Am.*, 977 So. 2d 630 (Fla. Dist. Ct. App. 2008); *Carll v. Terminix Int'l Co.*, 793 A.2d 921 (Pa. Super. Ct. 2002); *Stirlen v. Supercuts, Inc.*, 60 Cal. Rptr. 2d 138 (Ct. App. 1997).

[5] *See, e.g.*, *Alexander v. Anthony Int'l, L.P.*, 341 F.3d 256 (3d Cir. 2003); *Adler v. Fred Lind Manor*, 103 P.3d 773 (Wash. 2004); *Stirlen v. Supercuts, Inc.*, 60 Cal. Rptr. 2d 138 (1997).



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any agreement that lets the business "pick the judge" would certainly be struck down by our courts.[6] Some critics of arbitration repeat the mantra that companies "pick their own judges" in arbitration. That is false. Ordinarily, the drafter of an arbitration agreement designates an arbitration organization to administer the arbitration, but that organization itself selects a neutral arbitrator, with both parties typically participating in the process and possessing the right to object to an arbitrator.

Leading arbitration service providers have also developed rigorous standards to help assure fair results, such as the consumer due process protocol of the not-for-profit American Arbitration Association (AAA). And with judges enforcing the unconscionability doctrine, business have a strong incentive to provide for the AAA and other reputable forums like JAMS to administer arbitrations.

3. Arbitration arose as an alternative to the complex, expensive and time-consuming procedures of our litigation system. In our courts today, what obstacles does an individual consumer or employee face when he or she seeks to bring a claim for relief?

An individual consumer or employee has many obstacles to overcome if he or she seeks redress with the litigation system. The first major obstacle for the consumer or employee is to obtain a lawyer who will represent the individual. In that regard, litigation is expensive and plaintiffs' lawyers typically do not bill by the hour. Most plaintiffs' lawyers are very selective in their cases; they will only take cases where they are reasonably certain that they will win. Otherwise, the plaintiff's lawyer could devote hours to litigation and never be compensated. While it is true that the "bottom feeder class" of plaintiffs' lawyers bring frivolous claims and relief is needed to stop them from doing so (*see, e.g.,* S. 533, the Lawsuit Abuse Reduction Act), most plaintiffs' lawyers do play by the rules of economics and only pursue claims where they have a high probability of winning (or securing a lucrative settlement

Even if an individual's claim has merit, there must be sufficient damages to warrant a plaintiff's lawyers' time to pursue the claim. Good data suggest that many plaintiff's lawyers are reluctant to take a claim under $60,000.[7] Data also suggest that employees who allege discrimination after being terminated can only find lawyers to represent them in about five percent of cases.[8] As a National Law Journal editorial just this week

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[6] *See, e.g., Murray v. United Food & Commercial Workers Int'l Union*, 289 F.3d 297 (4th Cir. 2002); *Hooters of Am., Inc. v. Phillips*, 173 F.3d 933 (4th Cir. 1999); *Roberts v. Time Plus Payroll Servs., Inc.*, 2008 WL 376288 (E.D. Pa. Feb. 7, 2008); *Missouri ex rel. Vincent v. Schneider*, 194 S.W.3d 853 (Mo. 2006).

[7] *See* Elizabeth Hill, *Due Process at Low Cost: An Empirical Study of Employment Arbitration Under the Auspices of the American Arbitration Association*, 18 OHIO ST. J. ON DISP. RESOL. 777, 783 (2003).

[8] Theodore J. St. Antoine, *Mandatory Arbitration: Why It's Better Than It Looks*, 41 U. MICH. J.L. REFORM 783, 792 (2008).



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concluded, "[i]ncreasing numbers of litigants have no access to the system at all, because the ante is too high."[9]

Further, assuming an individual can find an attorney to take on his consumer or employee claim, there are substantial delays in the litigation system. In some metropolitan areas it may be two or three years until a final result.[10] Even then, the case may be appealed to a higher court. Also, in terms of results, they may appear random. Some plaintiffs "hit the jackpot" and receive very substantial awards, but others receive little or nothing. Each of these obstacles demonstrate that, in many cases, arbitration provides a welcome alternative to litigation.

4. Some have argued that the Supreme Court's decision in *AT&T Mobility LLC v. Concepcion* will "immunize" corporations from the consequences of their alleged wrongdoing by providing an alternative in the place of class actions. What do you believe will be the impact of *Concepcion*?

   The *Concepcion* case will not immunize corporations for the consequences of their wrongdoing. Arbitration provides a fair means for an employee or consumer with a legitimate claim to pursue that matter individually, even if the amount of the claim is modest. Class actions, in comparison, are not necessary to achieve individual justice, and, as explained in greater detail above, often do not serve consumers' best interests. Hence, whether class actions are available or not does not mean a defendant corporation may act with impunity; if corporations engage in wrongdoing, they are accountable to every single individual harmed, and could be liable for additional punitive damages as well. In addition, businesses that sell to consumers are regulated by multiple state and federal agencies. I do not think state officials such as my fellow witness Minnesota Attorney General Lori Swanson would be likely to agree that corporations are now immune from her oversight. National businesses are subject to oversight by 51 attorneys general and the FTC, as well as numerous industry-specific regulators.

   With regard to the *Concepcion* case specifically, the effects are still uncertain. The Supreme Court paid close attention to the particular arbitration agreement that was involved in the case itself and deemed it to be a fair and just one. It is unclear whether class actions would be prohibited if a pre-dispute arbitration agreement was not fair and did not secure appropriate checks and balances to protect the rights of an individual. Many courts are addressing these arguments now, and we do not know what the consensus result will be. Regardless, class actions are, again, not some panacea to prevent corporate wrongdoing, nor does their absence insulate wrongdoers for any unlawful acts.

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[9] Rebecca Love Kourlis, *Overhaul Civil Litigation*, Nat'l L.J. Oct. 31, 2011.

[10] *See Threadbare American Justice*, N.Y. Times, Aug. 17, 2011 ("Swamped by this huge docket, no state court system now delivers justice as it needs to.").

5. Your prepared statement noted that: "The argument that consumers lack bargaining power is a fallacy; consumers gain more bargaining power everyday through increased competition and more avenues, such as on the Internet, to rate products and services." Can you elaborate?

In my prepared statement, I indicated that the argument that "consumers lack bargaining power is a fallacy" for several reasons. First, we live in a highly competitive world where consumers have many choices with regard to products and services. If enough consumers complain about a product or service, a savvy and well-informed public will simply choose to do business with someone else. In today's marketplace, these shifts occur very quickly. Companies such as Blockbuster Video and Borders bookstores are a recent testament to this fact. Consumers have at their fingertips considerable information to guide their choices. There are, for example, numerous websites dedicated to consumer product and service ratings which millions of Americans view daily. Moreover, at no other point in history has a society had such choice and consumer bargaining power. With technology and other innovations, this bargaining power will likely only increase with time.

Second, because our marketplace is driven by consumer demand, if consumers demand that a particular product or service be available, and accompanying that product or service include the right to sue the defendant and not be subject to pre-dispute arbitration, entities will arise to provide that product or service. The product or service may cost more, the same way automobiles with extraordinary features cost more than those that do not have them, but enterprising businesses will fill this demand. Also, if enough people no longer want pre-dispute arbitration agreements, similar to the way consumers no longer wanted to travel to a local video store to obtain a movie, the practice of not including pre-dispute arbitration clauses in consumer agreements would become the norm. Thus far, there does not appear to be broad scale consumer demand for products and services that have no pre-dispute arbitration agreements.

Third, it is a fallacy that consumers lack bargaining power because even though there is no broad based demand for no pre-dispute arbitration agreements, there is so much consumer choice that virtually any product or service can be obtained without a pre-dispute arbitration agreement. One can, for instance, readily use a search engine such as Google to determine such providers if this represents a significant preference when deciding to purchase a product or service. Somewhat ironically, the proposed legislation would virtually eliminate a consumer's choice to use arbitration. As the evidence abundantly demonstrates, the option of post-dispute arbitration is little more than an illusion.

# SUBMISSIONS FOR THE RECORD

**Testimony for the Record**
**Of**
**Richard W. Naimark**
**On behalf of the American Arbitration Association**

**United States Senate**
**Committee on the Judiciary**
**October 13, 2011**

**"Arbitration: Is it fair when forced?"**

We appreciate the opportunity to share the American Arbitration Association's (AAA) experiences on these important issues being considered by the Judiciary Committee as it examines the use of arbitration.

The AAA is a not-for-profit public service organization with an 85-year history in the administration of justice. The AAA has pioneered the development of dispute resolution processes, arbitration rules, protocols, and codes of ethics jointly authored with the American Bar Association, which may serve as best practices for arbitration involving individuals in conflict with organizations.

We have a long and honorable history of working with government at all levels in the development and implementation of fair and efficient alternative dispute resolution (ADR) programs. Last year, for example, we carried out a national program under Congressional authority which resulted in the fair and fast resolution of thousands of complex disputes. We have worked with the U.S. Department of Justice, the Centers for Medicare & Medicaid Services, and the Federal Communications Commission in the development of programs to bring the advantages of ADR to the public sector.

These programs have a common element: they draw upon the AAA's considerable, time tested experience with modification to reflect the specific requirements of the program and the specific disputes being addressed. Congress took this approach in late 2009, and the result was the highly successful AAA Automobile Industry Special Binding Arbitration Program, in which the AAA provided a forum under statutory authority to nearly 3000 dealerships that had been closed as a result of the reorganization of Chrysler and General Motors.

We must make no mistake in our focus on this subject, the primary issue at hand today is access to justice. The reality in this country is that our legal system is difficult to navigate for most individuals. Individuals who have claims with a dollar value below $50,000 - $65,000 have a difficult time obtaining legal representation, regardless of the



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validity of the claim. The litigation process is exceedingly difficult for pro se individuals to pursue. Arbitration can, and does, provide ready access to justice IF due process protections are built in. This is an important distinction.

In furtherance of this important public policy discussion, the AAA several years ago developed model draft federal legislation which would codify many of the due process protections contained in the consumer and employment due process protocols. As an example, this model bill would require "clear, prominently visible and adequate notice of the arbitration provision and of the consequences of the arbitration provision..." This draft bill can serve as a basis for a more effective and constructive approach to ensuring fairness when using ADR. We believe a system that offers ready access to justice yet provides procedural safeguards for consumers makes more sense than stripping away ready access to redress.

This model legislation also incorporates a mechanism to greatly reduce the likelihood of unintentional legislative impact on international and commercial arbitration – the creation of a new chapter within Title 9 of the U.S. Code, which we are pleased to see has been incorporated into several bills introduced during this Session of Congress., under the leadership of Sen. Franken and others.

**This "Chapter 4" approach, combined with a protocol-based approach to codifying appropriate standards and protections, would provide the best course of action for Congress to enhance the use of arbitration in the healthcare, employment, and consumer contexts.**

**Consumer Arbitration**

In recent years, the use of ADR and arbitration has grown to include consumer agreements. Often implemented through standardized contracts, the use of arbitration in consumer agreements for the purchase of goods and services has raised legitimate concerns regarding fairness, rights, and the ability of the parties to participate. The AAA's administration of consumer arbitrations is currently governed by the *Consumer Due Process Protocol* and a specialized set of implementing rules and procedures

To evaluate and address concerns unique to consumer arbitration, the AAA convened the National Consumer Disputes Advisory Committee in 1997, which was composed of consumer, government, legal, business, and academic experts drawn from such organizations as the AARP, Consumers Union, Consumer Action, American Council on Consumer Interests, the Federal Trade Commission, the National Association of Attorneys General, the National Association of Consumer Agency Administrators, Fannie Mae, and Freddie Mac. One of the Advisory Committee's specific objectives was



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to have the Consumer Protocol influence state and federal laws governing consumer arbitration.

The result of the Advisory Committee's deliberations was the *Consumer Due Process Protocol*, which articulates a number of fundamental principles to enhance the fairness and efficiency of consumer ADR. The *Consumer Due Process Protocol* constitutes a voluntary set of standards and minimum requirements. Although the AAA has adopted this Protocol, it is not necessarily applied to arbitrations outside of AAA administration. The *Consumer Dur Process Protocol* provides for common sense "fair play" requirements such as reasonable fees for the consumer, reasonably accessible locale, no limitation of any remedy that would be accessible in court. Of particular note is the provision in the Consumer Due Process Protocols that ensures access to small claims court for consumers who wish to opt out of the arbitration avenue. Most significantly, the AAA will not administer an arbitration that does not materially comply with the provisions of the *Consumer Due Process Protocol.*

The AAA applies the *Consumer Due Process Protocol* primarily through our Supplementary Procedures for Consumer-Related Disputes ("Supplementary Procedures"). The Supplementary Procedures also establish guidelines for consumers to request a deferral or waiver of fees, including requesting an arbitrator who will serve without charge. One unique aspect of the Supplementary Procedures is the "small claims opt out" which permits a consumer, whether they are a claimant or respondent in a case, to opt out of an arbitration and into a small claims court proceeding.

**Employment Arbitration**

In the employment arena, the AAA similarly convened the Task Force on Alternative Dispute Resolution in Employment, a coalition of consumer, employee, business, and regulatory interests, to develop the *Due Process Protocol on Mediation and Arbitration of Statutory Disputes Arising Out of the Employment Relationship.*

The Task Force included individuals from the Federal Mediation and Conciliation Service, the ACLU, the ABA, the AAA, the National Employment Lawyers Association, and other interested organizations.

The Task Force's work product represents the best consensus thinking about what constitutes due process, fair play, and a level playing field in the area of employee-employer disputes. There was no limitation of subject matter for discussion.

Employment arbitrations conducted under the Due Process Protocols have been proceeding in an orderly and efficacious manner for ten years and have provided redress for thousands of employees and employers in that time. Studies support the balance and effectiveness of the process in this setting.



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**Healthcare Arbitration**

In 1997, the leading associations involved in medicine, law, and ADR formed the Commission on Health Care Dispute Resolution. Representatives of the American Medical Association, the American Bar Association, and the AAA developed standards on the appropriate use of ADR in resolving disputes in the health care environment. The resulting *Healthcare Due Process Protocol* serves as a widely accepted standard for the use of ADR in this important field. As noted by the Commission, its Final Report is "...meant to provide guidance not only to private managed health care organizations considering the voluntary adoption of ADR programs as a form of review of plan determinations, but also to legislative and regulatory bodies considering the establishment of standards governing the use of ADR in the health plan environment."

**Conclusion**

We appreciate the opportunity to present the AAA's recommendations and suggestions on the resolution of consumer, healthcare, and employment disputes. Based on the AAA's 85 years of experience, we believe that with appropriate safeguards, properly executed and designed arbitration can provide a prompt, effective, and fair forum for the resolution of these disputes while ensuring individuals access to justice. In this time of economic stress and significant dislocation it is essential to keep our systems of redress and resolution accessible, balanced and fair. The protocols and the draft legislation noted above draw upon the collective wisdom of experts and key organizations in their respective fields, and should be given further serious consideration by Congress as it responds to issues in the use of arbitration.

**STATEMENT FOR THE RECORD**

**OF**

**AARP**

**SUBMITTED TO THE**

**SENATE JUDICIARY COMMITTEE**

**ON**

**ARBITRATION: IS IT FAIR WHEN FORCED?**

**OCTOBER 13, 2011**

**AARP**
**601 E Street, N.W.**
**WASHINGTON, D. C. 20049**

**For further information, contact:**
**Deborah Chalfie**
**Government Affairs**
**(202) 434-3760**

On behalf of AARP's millions of members our members and all Americans age 50 or older, AARP endorses the Arbitration Fairness Act (S. 987). This legislation would correct a disturbing line of Supreme Court cases and invalidate the myriad of one-sided, predispute, mandatory arbitration clauses now being used to deny workers and consumers a wide range of legal rights. AARP thanks Senator Franken and the Senate Judiciary Committee for holding today's hearing to increase awareness of this affront to justice.

There is nothing objectionable about voluntary, post-dispute arbitration, where both parties agree to bypass the courts and use a dispute resolution process such as mediation or arbitration. These procedures can offer the parties many advantages and may be well-suited for some types of disputes, such as family disputes or contractual disputes between commercial entities. However, the answer to the question posed by the title of this hearing — is arbitration fair when it is forced, rather than being voluntarily agreed to by both parties — is clearly "No."

Ever since the *Gilmer v. Interstate/Johnson Lane Corp.* decision in 1991,[1] when the US Supreme Court enforced an arbitration clause and held that an Age Discrimination in Employment Act claim could be kept out of the courts at the employer's option, AARP has been deeply concerned about the rapidly increasing use of forced arbitration clauses in employment and consumer contracts. Forced arbitration has become routine, permeating many relationships and transactions of importance to seniors:

- ***Employment*** – It is conservatively estimated that 15-25% of all nonunion private sector employees are subject to a forced arbitration clause as a condition of employment.[2] Forced arbitration requirements often appear in their personnel policies or even the job application. Even when employees are aware of such clauses, they are rarely in a position to "shop around" for a new job if they disagree with the requirement. Because forced arbitration does not provide the same substantive and procedural protections as a court, it is inconsistent with efforts to enforce fundamental rights such as those covered by civil rights laws.[3] Requiring workers to choose between getting or keeping a job, or giving up their rights under federal and state law to sue their employers for discrimination, flies in the face of the purposes underlying these laws.

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[1] *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991).
[2] Alexander Colvin, "Empirical Research on Employment Arbitration: Clarity Amidst the Sound and Fury?," 11 *Employee Rights & Employment Policy J. 405, 411 (2007), available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1090335.
[3] *See* EEOC, Policy Statement on Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment, No. 915-002 (July 10, 1997), *available at* http://www.eeoc.gov/policy/docs/mandarb.html.



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- ***Nursing home admissions*** - When older loved ones suffer a decline in health or are discharged from the hospital unable to care for themselves, family caregivers are often faced with the daunting task of finding nursing home care. Often, these decisions are made in a context of crisis and vulnerability, when there is not enough time to adequately investigate and compare nursing facilities. Instead, most people seeking nursing home admission for a loved one are focusing on the quality and range of services available, and whether they can afford the cost. However, should there later be a complaint of abuse, neglect, assault, malnutrition, or even death, the resident and family are barred from seeking redress in the courts.

- ***Financial products and services*** – The securities industry was one of the first to incorporate forced arbitration into its agreements.[4] According to Public Citizen, 10 out of 10 brokerage companies and 5 out of 7 major banks require agreement to forced arbitration as a condition of doing business with them.[5] Fortunately, consumers of financial services may be getting some relief: provisions in the Dodd-Frank financial regulation legislation prohibit the use of forced arbitration in mortgage and home equity loans,[6] and empower the Securities and Exchange Commission[7] and the new Consumer Financial Protection Bureau[8] to prohibit their use in financial services agreements with consumers.

- ***Consumer contracts*** - It has become commonplace for consumer contracts for goods and services to require consumers to give up their rights to go to court in the event of a complaint. According to the Public Citizen study, 7 out of 10 major cell phone service providers, 5 out of 13 cable/internet companies, and 4 out of 9 computer manufacturers impose forced arbitration as a condition of doing business.[9] In fact, it was a consumer case — AT&T charged a $30 sales tax for "free" cell phones — that was behind the recent *AT&T v. Concepcion* case.[10]

Across the board, the targets of forced arbitration agreements are rarely aware of these clauses buried in the fine print, and even when they are aware of them, they are not necessarily adequately informed about their import, nor are they given any meaningful chance to negotiate them. To the contrary,

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[4] *See* Jean Sternlight, "Creeping Mandatory Arbitration: Is It Just?," 57 Stan. L. Rev. 1631, 1636 (2004-2005), *available at* http://scholars.law.unlv.edu/facpub/280/.
[5] Public Citizen, *Forced Arbitration: Unfair and Everywhere* 1 (2009), *available at* http://www.citizen.org/documents/UnfairAndEverywhere.pdf [hereinafter *Forced Arbitration*].
[6] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1414(e), 124 Stat. 1376, 2151 (2010).
[7] *Id.*, § 921, 124 Stat. 1841.
[8] *Id.* § 1028, 124 Stat. 2003-2004.
[9] *Forced Arbitration*, *supra* n. 5.
[10] 131 S. Ct. 1740 (2011).



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arbitration clauses are typically included in contracts of adhesion imposed by the party with superior bargaining power, on a take-it-or-leave-it basis.

The *Gilmer* Court rejected as unpersuasive every single argument about the procedural and substantive flaws inherent in forced arbitration. The assertion that sending a case to arbitration is just a change in forum and has no impact on substantive rights is an essential underpinning of much of the Court's jurisprudence on forced arbitration, but it is patently false.

The inferior rights and remedies available in arbitration compared with courts significantly disadvantage the complainant: discovery is limited; the employer selects the arbitrator; the arbitrator need not follow the law and yet there is no appeal except under limited circumstances; no requirement for a published opinion, and thus no public accountability and no precedent; damages and remedies may be limited by the arbitration agreement; the loser risks having to pay the other side's attorney's fees, a significant deterrent not present in court; and the worker is denied a trial by jury or even a neutral judge paid by the government, and instead is subject to a decision-maker paid by an interested party with repeat business for that firm.

As a result, several studies have found that forced arbitration produces one-sided results. A study by the Committee for Responsible Lending found that "[c]ompanies that have more cases before arbitrators get consistently better results from these same arbitrators," even after controlling for other possible sources of bias.[11] In an empirical study released this year on how employees fare in forced arbitration, the researchers found "strong evidence" that employees' win rates (just 21%) and the size of their awards were significantly lower when the employer is a repeat player and has several cases, an effect that is multiplied when an arbitrator is involved in more than one case for the same employer.[12]

More recently, the Supreme Court has extended its line of cases upholding forced arbitration to bar class arbitration — consumers who have been harmed in small dollar amounts are not permitted to try to level the playing field by combining their small claims into a class complaint.

This highlights perhaps the worst outcome of forced arbitration: it undermines the rule of law itself. If employers and corporations can unilaterally opt-out and escape accountability in the courts for violations of the law, the law and the rights guaranteed under the law become unenforceable and therefore meaningless. By depriving aggrieved individuals of access to the courts — the intended

[11] Joshua Frank, *Stacked Deck: A Statistical Analysis of Forced Arbitration* 7 (Center for Responsible Lending, 2009), *available at* http://www.responsiblelending.org/credit-cards/research-analysis/stacked_deck.pdf.

[12] Alexander Colvin," An Empirical Study of Employment Arbitration: Case Outcomes and Processes," 8 J. Empirical Legal Stud. 1, 5-6 (2011), *available at* http://onlinelibrary.wiley.com/doi/10.1111/j.1740-1461.2010.01200.x/pdf.



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mechanism for vindicating their rights, either individually or as a class — the civil rights and consumer protection laws are functional nullities. Such lawlessness directly undermines core statutory provisions enacted by Congress to protect the American people.

In a brief recently filed in Florida in a consumer case in which Sprint charged improper roaming fees, AARP argued that:

> Many corporations — unwilling to submit to the proscriptive ground rules and remedial framework provided by statute — have gone rogue. Corporate lawyers have seized upon arbitration provisions as a tool to shield them from liability for their wrongdoing. ... [T]heir specific purpose is to immunize corporate defendants from the risk of liability for wrongdoing by deterring or even preventing potential victims from seeking redress.[13]

**Conclusion**

In order to restore the protections that Congress has enacted into statute, AARP's believes that pre-dispute mandatory arbitration provisions in employment contracts, financial services agreements, consumer transactions, and in contracts for health and long-term care services should be prohibited and unenforceable.

We look forward to working with Senators on both sides of the aisle to protect and enforce the statutory rights you have worked so hard to create in the workplace and the marketplace.

[13] *Pendergast v. Sprint Nextel Corp.*, Case No. Sc-10-19, Brief *Amicus Curiae* of AARP in Support of Appellant 2 (Fla. Sup. Ct. 2012).



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TESTIMONY TO THE UNITED STATES SENATE JUDICIARY COMMITTEE

# ARBITRATION: IS IT FAIR WHEN FORCED?

**October 13, 2011**

**by F. Paul Bland**[1]

**Senior Attorney, Public Justice**

**Of Counsel, Chavez & Gertler**

[1] F. Paul Bland, Jr., is a Senior Attorney for Public Justice, where he handles precedent-setting complex civil litigation. He is also co-counsel at Chavez & Gertler, a private law firm. He has argued or co-argued and won more than twenty reported decisions from federal and state courts across the nation, including cases in five of the U.S. Courts of Appeal and at least one (and as many as six) cases in state Supreme Courts. He is a co-author of a book entitled *Consumer Arbitration Agreements: Enforceability and Other Issues*, and numerous articles. For three years, he was a co-chair of the National Association of Consumer Advocates. In 2010 he was named a "Champion of Justice" by the Maryland Legal Aid's Equal Justice Counsel. In 2006 he was named the "Vern Countryman" Award winner in 2006 by the National Consumer Law Center, which "honors the accomplishments of an exceptional consumer attorney who, through the practice of consumer law, has contributed significantly to the well being of vulnerable consumers." He also has won the San Francisco Trial Lawyer of the Year in 2002 and Maryland Trial Lawyer of the Year in both 2001 and 2009. Prior to coming to Public Justice, he was in private practice in Baltimore. In the late 1980s, he was Chief Nominations Counsel to the U.S. Senate Judiciary Committee. He graduated from Harvard Law School in 1986, and Georgetown University in 1983.



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## INTRODUCTION AND SUMMARY

Thank you for inviting me to participate in this important hearing. My testimony will make the following points:

- A large and rapidly growing number of corporations are requiring millions of consumers and employees to give up their rights to a trial by jury and to bring cases in the U.S. public civil justice system, and instead submit all of their legal claims to binding mandatory arbitration.[2]
- Recent decisions by the U.S. Supreme Court, as well as lower courts, have made it significantly more difficult for consumers and employees to challenge even the most abusive mandatory arbitration clauses. These decisions, including the recent case of *AT&T Mobility LLC v. Concepcion*, have curtailed efforts by states to protect consumers and employees against unfair contract terms.
- In many cases, mandatory arbitration clauses have the effect of immunizing corporations from any liability or accountability even when they have blatantly violated consumer protection or civil rights laws. As a result, corporations are able to break consumer protection laws by doing things such as misleading consumers about the costs of loans or engage in similar bait-and-switch practices, and the legal system does nothing to deter these behaviors or compensate cheated consumers. This is not "just" an issue of fairness to consumers, it also undermines the marketplace when there is no enforcement of the rules of the road:

[2] The concerns addressed in this testimony all relate to pre-dispute arbitration agreements, meaning contract provisions agreed to in advance of any dispute or claim arising that require a party to take any legal claims that may later arise to arbitration instead of to court. The concerns discussed here do not relate to post-dispute arbitration, in which two parties to an existing dispute agree after the dispute has arisen to submit that dispute to arbitration.



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honest companies are at a disadvantage against corporations willing to cheat consumers.

- Most consumers and employees have little or no meaningful choice about submitting to arbitration. Few people read or understand the fine print that strips them of their rights; and because arbitration clauses are found in nearly all consumer contracts, most consumers have no choice but to accept them.

**BACKGROUND ABOUT PUBLIC JUSTICE**

Public Justice is a national public interest law firm dedicated to using trial lawyers' skills and resources to advance the public good. We specialize in precedent-setting and socially significant litigation, and carry a wide-ranging docket of cases designed to advance the rights of consumers and injury victims, environmental protection and safety, civil rights and civil liberties, occupational health and employee rights, protection of the poor and the powerless, and overall preservation and improvement of the civil justice system.

Public Justice was founded in 1982 and is currently supported by more than 3,000 members around the country. More information about Public Justice and its activities is available on our web site at www.publicjustice.net. Public Justice does not lobby and generally takes no position in favor of or against specific proposed legislation. We do, however, respond to informational requests from legislators and persons interested in legislation, and have occasionally been invited to testify before legislative and administrative bodies on issues within our expertise. In keeping with that practice, we are grateful for the opportunity to share our experience with respect to the important issues this Committee is considering today. In this connection, we have extensive experience with respect to abuses of mandatory arbitration,



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having litigated (often successfully) a large number of challenges to abuses of mandatory arbitration in state and federal courts around the nation.

## I. MOST CONSUMER AND EMPLOYEE CONTRACTS REQUIRE BINDING ARBITRATION.

In just the last generation, there has been a largely unnoticed but very important revolution in the way many corporations do business. Fifteen to twenty years ago, only a handful of corporations required consumers or non-unionized employees to submit their claims to binding arbitration. Now, these mandatory arbitration clauses are in hundreds of millions of form contracts. Here are just a few examples:

- It is very hard to get most loans, credit cards, checking accounts or other financial services products without submitting to an arbitration clause.[1]
- The vast majority of cell phone and residential phone companies require their customers to accept binding arbitration clauses on a take-it-or-leave-it basis. It would be hard for a customer to get a cell phone without giving up basic legal rights to redress if they are cheated by the carrier.
- Millions of persons are required by their employers to submit all claims – wage and hour claims, civil rights claims, everything – to binding arbitration. Employers such as Anheuser-Busch, Cheesecake Factor, Circuit City, Ford Motor Co., Hooters, Hughes Electronics, Kentucky Fried Chicken, Lenscrafters, Marriott International, Pfizer, Rockwell, Ralph's Grocery/Albertsons, Waffle House and General Electric (among

[1] There is one important exception. Several years ago, Congress made it a misdemeanor for a lender to put an arbitration clause into many loan agreements with members of the military or their dependent family members. 10 U.S.C. § 987 (e)(2)-(4); (f)(1). There is a serious policy question as to how mandatory arbitration could be so unfair when it is imposed upon a member of the military that it is a crime, yet it is supposed fair and proper to impose it on other citizens.



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thousands of others) all require their employees to agree to mandatory arbitration clauses as a condition of getting or keeping a job.[2] *See* Alexander J.S. Colvin, *Employment Arbitraiton: Empirical Findings and Research Needs*, Dispute Resolution J. (Aug./Oct. 2009) (studies show as many as 46.8% of non-union businesses use employment arbitration).

- The vast majority of car dealers in the U.S. have inserted binding arbitration clauses into their car sales contracts. (Only a few car dealers in the entire nation had such clauses sa decade ago.)[3]
- It is hard to buy a computer without submitting to a binding arbitration clause. Dell, Gateway, and other major companies insist upon them. Most products or services one would purchase over the internet are only available if one clicks on a box "agreeing" to many thousands of words of fine print (which very few people read), and nearly all of those "terms and conditions" provisions now include an arbitration clause that bans class actions.

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[2] As one example of how courts often do not protect employees from mandatory arbitration, *see Garrett v. Circuit City Stores*, 449 F.3d 672 (5th Cir. 2006). In that case, a company allegedly did not preserve the job of a military reservist who was sent to Iraq. When he sued under the Uniformed Services Employment and Reemployment Rights Act (USERRA), 38 U.S.C. § 4302(b), the Court held that he had lost his right to bring this claim in court and had to bring his claim to a private arbitrator. There is no little irony that someone who has risked his life protecting our freedoms would be forced to lose a number of his own constitutional freedoms as a result of a fine print contract. In upholding the arbitration agreement, the court expressly ignored language in the House Committee Report that stated that arbitration of a USERRA claim would not be required or binding. *Id.* at 679.

[3] By contrast, back in 2002, automobile dealerships lobbied strenuously for and won a federal statute that bars car manufacturers from insisting that car dealers arbitrate disputes. 15 U.S.C. § 122 6 (a)(2). The Congress has only protected car dealers, however, and not car buying consumers.



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- Mandatory arbitration is growing rapidly as a requirement for patients to receive necessary medical services. Many HMOs have arbitration clauses; more doctors have such clauses; the vast majority of nursing homes have arbitration clauses in the fine print of their contracts; I have seen such a clause in a contract providing for an organ transplant.

- Mandatory arbitration clauses are in contracts for a wide range of other consumer goods and services – home sales contracts, insurance companies, rental car companies, mortuaries, pest control companies, securities broker services, pet boarding companies, etc., all regularly require customers to sign them as a condition of service.

## II. CONSUMERS HAVE LITTLE CHOICE BUT TO AGREE TO MANDATORY ARBITRATION CLAUSES.

Literally millions of Americans have unknowingly received mandatory arbitration clauses in a manner that ensures that the clauses would not be read or understood by all but a very few of their recipients. I have seen hundreds of arbitration clauses, including clauses used by some of the largest and richest corporations in the United States, that are (a) cast in dense and cryptic legalese incomprehensible to lay persons (and even many lawyers); (b) set forth in minuscule print, often on the back side of a document; and (c) buried in the center of a mailing that contained a variety of other pieces, most of which were solicitations and advertisements unlikely to be read by most recipients.

Many on-line contracts bury the arbitration clauses hundreds of lines deep in the fine print; the corporations know that most normal people will just click "agree" rather than scroll down so far. Even when consumers are asked to sign or initial below or at the arbitration clause, it is often in the context of a transaction where the consumer is asked to quickly flip through a



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large body of "standard" documents or contract provisions, which rarely include an explanation of the arbitration clause.[1]

Most people first learn that a company says that they have lost the right to sue – and have "waived" their constitutional right to trial by jury and a day in court – only after a dispute rises. In most cases, an individual's first awareness of an arbitration clause comes as a bitter surprise. We have spoken to literally hundreds of persons on this topic over the past few years, including homeowners, farm operators, consumer and civil rights attorney's, consumers, employees, journalists and arbitrators. Again and again in those conversations, we have heard from people – often very angry and very dissatisfied people – who were utterly unaware that they had been sent an arbitration clause, and who believed that they had never agreed to such a clause. *See also* Fannie Mae Announcement 04-06, Sept. 28, 2004 ("We also recognize, however, that borrowers who would prefer to present their grievances in court may unknowingly agree to mandatory arbitration at the time they sign their mortgage documents."); Linda J. Demain and Deborah Hensler, *"Volunteering" to Arbitrate Through Predispute Arbitration Clauses: The Average Consumer's Experience*, 67 Law & contemp. Problems 55, 73-74 (Winter/Spring 2004) ("Given the lack of information available to consumers in predispute arbitration clauses, and the difficulty of obtaining and deciphering these clauses, it is likely that most consumers only become aware of what rights they retain and what rights they have waived after disputes arise."); Christine Reilly, *Achieving Knowing and Voluntary Consent in Pre-Dispute Mandatory Arbitration Agreements at the Contracting Stage of Employment*, 90 Cal. L. Rev. 1203, 1225 (2002) (empirical research demonstrates that employees "do not understand the remedial and

[1] In one case in which we were counsel, the first sentence of a payday lender's arbitration clause was 256 words long!



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procedural consequences of consenting to arbitration" and that "[v]ery few are aware of what they are waiving.").

Unfortunately, most courts do little to require that individuals actually receive meaningful notice that they are supposedly "agreeing" to give up their constitutional rights and submit to arbitration.

- In one case, where a consumer bought a computer over the phone, the arbitration clause was sent to consumers inside the box with a computer. For a consumer to reject the clause, she would have to pack up and send back the computer in the box (at her own expense) within 30 days. While anyone familiar with human nature and consumer behavior can predict that few consumers would take such a step, courts have upheld such clauses. *E.g., Hill v. Gateway 2000 Inc.*, 105 F.3d 1147 (7th Cir. 1997).
- Alabama's highest court upheld an arbitration agreement that was not even in the contract that the consumers signed. Public Justice represented a husband and wife who purchased title insurance when they bought a farm. When they later found out that there were serious defects in the title, the title insurance company attempted to force them to arbitrate their claim despite the fact that the original contract they signed had not contained the arbitration clause. Instead of including the arbitration agreement in the contract, the insurance company had sent it to the consumers in the mail weeks later, arriving after the parties were already enmeshed in their legal dispute. Yet the court held it was enforceable. *McDougle v. Silvernell*, 738 So. 2d 806 (1999).
- And in an unusual case where one of our clients did know her employer gave her an arbitration clause and refused to sign it, the U.S. Court of Appeals for the Eleventh Circuit held that she was still bound by it because she failed to quit her job as a nurse at



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Baptist Medical Center-Princeton in Alabama, after having worked there as a nurse for almost 30 years. *Luke v. Baptist Medical Center-Princeton*, No. 03-14342 (11th Cir. March 11, 2004).

- In another case, a court compelled arbitration against the estate of a woman who died in a nursing home. Although the woman was legally blind and could not understand the contents of the papers she signed, the court said that no one can defend against the enforcement of a contract just because they signed it without reading it. *Estate of Etting v. Regent's Park at Aventura, Inc.*, 891 So.2d 558 (Fla. Dist. Ct. App. 2004).

Data support the predictable conclusion that many consumers do not read or understand the long, fine-print mailings sent to them by credit card companies. A recent study conducted by Credit.com found that 66% of credit cardholders did not know what, if any, changes had been made to their credit card agreements. Eileen A.J. Connelly, *Credit Card Holders Frequently Don't Pay Attention to Changes Made to Accounts, Survey Finds*, Star Trib. (Minneapolis), March 1, 2009. In at least one case, evidence showed that a bank knew only four percent of cardholders would read its bill stuffers. *See* Sen. Russell D. Feingold, Mandatory Arbitration: What Process Is Due?, 39 Harv. J. on Legis. 281, 296 (2002) (citing case); *see also* Shmuel I. Becher, *Asymmetric Information in Consumer Contracts: The Challenge That Is Yet to Be Met*, 45 Am. Bus. L.J. 723, 730-31 (2008) ("empirical evidence shows that most consumers do not read [standard form contracts]"); Amy J. Schmitz, *Consideration of "Contracting Culture" in Enforcing Arbitration Provisions*, 81 St. John's L. Rev. 123, 160 (2007) ("consumers rarely read or understand" arbitration agreements); Debra Pogrund Stark & Jessica M. Choplin, *A License to Deceive: Enforcing Contractual Myths Despite Consumer Pscyhological Realities*, NYU J. Law



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& Business (2009), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1340166 (discussing studies showing that consumers are unlikely to read standard-form contracts).

Similarly, studies conducted by the Government Accountability Office ("GAO") and Federal Reserve Board found that many credit card terms and disclosures are too complex for consumers to understand. *See* GAO, Increased Complexity in Rates and Fees Heightens Need for More Effective Disclosures to Consumers 6 (2006), *available at* http://www.gao.gov/new.items/d06929.pdf; Macro Int'l, Inc., Design and Testing of Effective Truth in Lending Disclosures (2007), *available at* http://www.federalreserve.gov/dcca/regulationz/20070523/Execsummary.pdf.[5] The GAO and Federal Reserve Board studies focused on contract terms that have a direct effect on cost, but presumably consumers spend even less time trying to understand terms, like mandatory arbitration clauses, that affect cost indirectly.

Many contracts are so dense and incomprehensible that the purported "opt out" provisions now included in some agreements are an entirely illusory improvement. Companies know that very few consumers read standard-form contracts, understand them, understand the differences between arbitration and litigation, are able to assess those differences, and have time to reject the default arbitration option by exercising any opt-out right (in the unlikely event that a consumer has actually read and understand the arbitration clause). *See, e.g.*, *Ting v. AT&T*, 182 F.Supp.2d 902, 933 (N.D. Cal. 2002) (citing the defendant's own research showing that many consumers would not read its dispute-resolution agreement), *aff'd in relevant part and reversed in part on other grounds*, 319 F.3d 1126 (9th Cir. 2003); *see also* Richard H. Thaler & Cass R. Sunstein, Nudge: Improving Decisions about Health, Wealth and Happiness 34-36 (2008) (discussing biases that affect consumer behavior and will make opt-outs unlikely). As the most

[5] *See also* GAO at 37-38 (discussing finding that credit card agreements are written at too high a reading level for many consumers to understand); Bar-Gill & Warren at 27-28 (discussing the GAO and Federal Reserve Board studies)



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companies certainly know, they are the real potential beneficiaries of opt-out language; consumers will hardly ever opt out, but companies can – and do – point to their "opt out" provisions in an attempt to defend arbitration against unfairness challenges in court.

## III. RECENT DECISIONS BY THE U.S. SUPREME COURT, AS WELL AS LOWER COURTS, HAVE MADE IT SIGNIFICANTLY MORE DIFFICULT FOR CONSUMERS AND EMPLOYEES TO RESIST MANDATORY ARBITRATION, EVEN IN THE MOST EGREGIOUS CASES.

On April 27, 2011, the U.S. Supreme Court decided *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011). *Concepcion* held, 5-4, that the Federal Arbitration Act ("FAA") preempts a state rule of contract law – in this case, California's "*Discover Bank* rule," which, according to the Court, would invalidate a class action ban in an arbitration clause—and force the parties into non-consensual class arbitration—whenever (a) the term is imposed in a consumer contract of adhesion; (b) the plaintiffs' claims involve predictably individually small damages; and (c) the defendant has allegedly engaged in a scheme to cheat consumers.[3] The Court held that the FAA, which was passed in 1925 (long before class actions even existed), wiped away key rules of contract law that would apply to all other types of contracts, to the extent that those rules would apply to arbitration clauses. Justice Scalia's opinion acknowledged that under California law, a contract term banning class actions would not be enforceable in a case involving very small individual claims if the term was in a "regular" contract that did not contain an arbitration clause. Under Justice Scalia's approach, however, if a corporation sticks an arbitration clause into its contract and then puts the otherwise illegal class action ban term into the arbitration clause, *now* federal law overrides the normal rule of state contract law.

[3] The preempted rule was adopted by the California Supreme Court in *Discover Bank v. Superior Court (Boehr)*, 113 P.3d 1100 (Cal. 2005).



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The *Concepcion* case was somewhat shocking, in many ways, to most legal observers. About 15 state Supreme Courts (and many more state courts of appeals) had considered the enforceability of class action bans in arbitration clauses, and every single one had considered this to be an issue governed by state law. A larger number of federal appellate decisions had addressed the issue, and all but one decision (and that one decision was later overturned by that circuit when it was sitting *en banc*, meaning all the members of that Court sitting together voted down the ruling of the original three judge panel) had found this to be an issue of state law, and *scores* of U.S. federal district courts had agreed. The Supreme Court's decision in *Concepcion*, by the usual 5-4, overturned (or at least arguably overturned) literally scores of lower court decisions, by inventing an new rule of federal law.

It was immediately clear to everyone who follows these issues that the U.S. Supreme Court's decision in *Concepcion* would immunize many corporations from class actions, by wiping away the common sense-based *Discover Bank* rule. In that case, the California Supreme Court had held that a contract term banning class actions would effectively eliminate the rights of the vast majority of consumers in a case that involved claims of less than $50 per person. It is common sense, and prior to *Concepcion* had been acknowledged by dozens of courts, that consumers with such small claims would never find representation and would never receive relief if they had to proceed on a class action basis. Under the *Discover Bank* rule, consumers did not have to prove that class action bans were unenforceable in very small dollar cases, because courts could simply presume that through their common sense.

Unfortunately, it is possible that *Concepcion* will be read even more broadly than is strictly necessary, and if so will wipe away the vast majority of consumer and employment class



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actions (or at least all class actions in cases where the corporation has an arbitration clause).[4] *Concepcion* held that federal law allows companies to use contractual arbitration clauses to ban their customers or employees from joining together in a class action. As in *Citizens United*, the Court expanded the rights of big business; but this time instead of giving them control over elections, it gave them a way to opt out of the civil justice system.

Arguably, *Concepcion* appeared to have one saving grace: it did not say anything about overturning the rule (set out in a long line of other Supreme Court cases) that arbitration clauses are only enforceable if the parties can "effectively vindicate their statutory rights" in arbitration. *See, e.g., Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 637 (1985) (explaining that statutory claims are arbitrable "so long as the prospective litigant effectively may vindicate its statutory cause of action in the arbitral forum"). Consumer and civil rights lawyers have been arguing that *Concepcion* should be "harmonized" with those earlier cases by creating an exception to the rule that class action bans are generally enforceable. Our argument has been that if a group of consumers or employees *proved* through hard evidence that they could not get justice without a class action (in other words, that they could not "effectively vindicate their statutory rights" if the arbitration clause was upheld), then courts should hold that the class action ban in the company's arbitration clause would be unenforceable.

Unfortunately, however, some lower courts are interpreting *Concepcion* as holding that contract terms banning class actions have to be enforced even when a court finds that the evidence in a case has proven that the ban on class actions guts consumer protection or civil rights laws. According to several federal district judges and a panel of judges on the 11th Circuit

[4] Indeed, in the wake of the decision, a prominent corporate defense firm trumpeted how their clients "can use this ruling to essentially eliminate one of the biggest litigation threats facing their businesses – the wage-and-hour class action." http://www.venable.com/files/Publication/50a0a297-3965-47ef-b87e-8e9308810f57/Preview/PublicationAttachment/e1dd5045-7f75-4f76-a702-9b4db2ef3320/The_End_of_Wage-and-Hour_Class_Actions.pdf



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Court of Appeals, for example, *Concepcion* apparently means that bans on class actions are always enforceable – even if that means consumers are left with no means of vindicating their rights. According to these courts, no consumer or employee would ever be able to challenge the presence of a class action ban in an arbitration agreement, even if it meant that they could never obtain relief for being wronged. *See, e.g., Cruz v. Cingular Wireless, LLC*, 2011 WL 3505016 (11th Cir. 2011) (discussed below); *Kaltwasser v. AT&T Mobility LLC*, 2011 WL 4381748 (N.D. Ca. 2011).

The potential impact of this rule, if it takes hold, will be devastating for consumers and employees. Assume a restaurant chain starts paying all its female employees half of what it pays male workers in the same positions, in violation of state labor laws. If the restaurant has a term in its contract prohibiting employees from going to court and instead requiring one-on-one arbitration, none of the women can join together to take on the company. Only the tiny handful willing to risk their jobs by bringing a claim in arbitration by themselves stand a chance. And even if they win, the company can keep paying all the other women half their pay. Under this reasoning, this get-out-of-jail-free card for businesses is what Congress supposedly intended when it passed the Federal Arbitration Act in the 1920's.

These decisions are already having real world impact. We have represented plaintiffs in numerous cases who would not have been able to vindicate their right if they were required to pursue arbitration on an individual basis. In a case in New Jersey, *Homa v. American Express*, our client, Mr. Homa experienced first-hand how the current legal framework can allow companies to cheat millions of customers and get away with it through their use of an arbitration agreement. Mr. Homa agreed to purchase a credit card based on the company's offer of a specific set of conditions and terms. In fact, however, he discovered that the terms that were



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advertised were far better than what a cardholder could ever receive and that the credit card company was misleading people about the true cost of its loans (by exaggerating the size of the rebates the cardholders were supposed to receive).

Mr. Homa, who is far better at numbers than the average consumer, figured out the scam -- that his rebate was much lower than he had been promised -- and tried to get his money back. The company rebuffed him at every turn, telling him he had miscalculated the rates and that he was not entitled to his money. He finally went to a lawyer, who told him that, while he had a valid claim, the damages in his case were so small that it did not make financial sense to pursue his claim on an individual basis. After realizing that the company had likely cheated many consumers in this bait and switch scheme, Mr. Homa on sought to hold the company liable for its unfair and deceptive lending practice by filing a class action complaint in federal court.

Because the amount of individual damages was so small and the nature of the claims was so complex, no one could actually obtain a remedy on an individual basis. The company nevertheless sought to force Mr. Homa into arbitration on an individual basis, but this effort was firmly rejected by the Third Circuit -- until the U.S. Supreme Court decided *Concepcion*. After *Concepcion*, despite an unchallenged evidentiary record in the case that proved that no one could effectively vindicate their statutory rights under American Express's arbitration clause, the district court held that it doesn't matter whether consumers could vindicate their rights or not, because companies supposedly have a federal right to gut these statutory rights.

Other similar examples abound. In *Cruz v. Cingular Wireless*, the Eleventh Circuit held that even if AT&T Mobility's clause was proven as a matter of fact to bar all but an "infinitesimal" number of plaintiffs from vindicating their statutory rights, that it must be enforced in light of *Concepcion*. The court held that if Florida law would be to the contrary, that



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this would not matter because the Federal Arbitration Act "unquestionably" would preempt this law. The allegations in that case involved a company's violation of Florida's Unfair Trade Practices Act by imposing an individually trivial monthly charge for a purportedly "optional" Roadside Assistance service that the plaintiffs had never requested or enrolled in. The evidence in that case established that, because the amount of money that each individual customer was cheated out of was a mere $2.99 a month, no one would ever pursue arbitration on an individual basis. The court essentially agreed, but said it did not matter. In short, under the Eleventh Circuit's reading of *Concepcion*, federal law pre-empts and overrides state laws that would protect any more than an "infinitesimal" number of consumers from having their rights violated under consumer protection statutes.

And, in a case in Ohio, a state court recently held that consumers could not avoid an unfair arbitration agreement, despite the fact that the company, a chain of 19 car dealerships, had explicitly violated the law and deceived customers by routinely selling former rental cars as used cars without disclosing their rental history. *See Wallace v. Ganley Auto Group*, 2011 WL 2434093 (Ohio Ct. App. 2011). Because consumers tend to refuse to pay as much for rental cars as they would pay for non-rental cars, the Ohio Attorney General requires used car dealers to disclose whether a used car was formerly a rental car or not, through two little boxes on the sales contract. This car dealer repeatedly checked "no" to this question for cars that were, in fact, rental cars. The court enforced the company's arbitration clause even though the evidence in the case established that no consumer would ever have been able to find an attorney to represent them individually. This again did not matter to the court, which said that courts and states are unable to apply or formulate rules that would invalidate arbitration agreements even if it could be shown that no one could vindicate their rights under the arbitration agreement. As a result of this



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Court's reading of *Concepcion*, a used car dealer has been given free reign to lie to its customers about something that would matter to many of them, and there is no meaningful way for them to get any relief.

If more courts start heading this direction, businesses will be able to bar people from taking the ONLY kind of legal action that could deter them from breaking certain types of consumer protection laws. And most Americans probably have no idea that their rights are so at risk.

Class action suits allow consumers to pool their individual resources, which is crucial when going up against well-funded corporations. As Congress stated, "Class action lawsuits are an important and valuable part of the legal system when they permit the fair and efficient resolution of legitimate claims of numerous parties by allowing the claims to be aggregated into a single action against a defendant that has allegedly caused harm." Class Action Fairness Act of 2005, 28 U.S.C. §1711 (2005). Stopping individuals from bringing class action suits effectively immunizes corporations from any legal accountability for certain categories of illegal acts they might commit, even when it is very clear that they have broken the law.

In many cases, class action bans insulate credit card companies from accountability because consumers cannot feasibly pursue certain claims on an individual basis, particularly cases in which individual claims are too small and complex to attract a private attorney. As an earlier Supreme Court explained, "small recoveries do not provide the incentive for any individual to bring a sole action." *Amchem Products, Inc v. Windsor*, 521 U.S. 591, 617 (1997). Class actions solve this problem and serve an important function by aggregating the potential recoveries "into something worth someone's (usually an attorney's) labor." *Id.*



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Class actions also serve an important role in cases involving complex wrongdoing such as the rebate scam that would not be apparent to consumers from the face of their credit card statements. In cases like Mr. Homa's, individual consumers must rely on others who know more about the underlying facts – often one particularly motivated consumer who is able to discover them with the help of an attorney.[24] Public Justice is involved now in a case against American Express, in which the plaintiff alleges that although American Express promised 3% cash back to consumers who spent more than $6,000, no consumer could ever actually receive a 3% return on total expenditures because of the way American Express calculated its cash back rewards. Most credit cardholders would probably never discover this practice on their own, which means they will only be able to recover (and to deter American Express's alleged wrongdoing) through the mechanism of a class action.

In *Ting v. AT&T*, for example, the company stipulated that class action bans are sometimes exculpatory. 182 F. Supp. 2d 902, 918-19 (N.D. Cal. 2002), *aff'd in part, rev'd in part on other grounds*, 319 F.3d 1126 (9th Cir. 2003). After a full trial, the court issued a 74-page decision striking down AT&T's class action ban as unconscionable under California law. *Id.* at 930-31. Prior to AT&T's promulgation of its contract, consumers had brought several successful class actions against phone carriers. *Id.* at 917-18. In one case, AT&T paid 100% of the class members' damages; in another, a class recovered $88 million from a different carrier. *Id.* at 918. AT&T conceded that none of the lawyers in those cases would have brought them on an individual basis. *Id.* at 918-19. Relying on this and a wealth of other evidence, the district

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[24] *See, e.g.*, *Gentry v. Super. Ct.*, 42 Cal. 4th at 461 ("[S]ome individual employees may not sue because they are unaware that their legal rights have been violated."); *Muhammad v. County Bank of Rehoboth Beach, Del.*, 912 A.2d 88, 100 (N.J. 2006) ("[O]ften consumers do not know that a potential defendant's conduct is illegal. When they are being charged an excessive interest rate or a penalty for check bouncing, for example, few know or even sense that their rights are being violated.") (citation omitted).



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court found that AT&T's class action ban "functions as an effective deterrent to litigating many types of claims . . . and, ultimately, would serve to shield AT&T from liability even in cases where it has violated the law." *Id.* at 918.

Public Justice is co-counsel in a series of five cases involving payday lenders in North Carolina. North Carolina has a usury rate of 36% per year. Many payday lenders charge interest rates of over 500% per year. In 1997, the North Carolina legislature permitted payday lenders to charge over 400% interest for a limited time on a test basis, but that statute expired in 2001 and was not re-enacted despite fierce lobbying. State officials notified the payday lenders at that time that further operations would be illegal, but payday lenders continued to charge their customers interest rates more than ten times the legal rate. The predatory nature of payday lending has been established by numerous studies, as approximately 95% of payday borrowers are not able to pay off the loans on time and end up rolling them over, often many times. It is not uncommon for individuals to borrow $500 and end up paying thousands of dollars in interest, but still owe the $500 at the end of that period. In any case, while the North Carolina Commissioner on Banks and the state's Attorney General shut down payday lending after several more years, the payday lenders had not paid back any of the illegal overcharges to their consumers until our consumer class actions were filed. To date, we have resolved three of those class actions for more than $44 million, with checks having been mailed to more than 300,000 North Carolina consumers. (By contrast, I've been told by an official with the American Arbitration Association that the total number of *all* of the consumer arbitrations filed with it for 2010 by any consumer against any corporation in the United States was about 1,300 cases.)

Arbitration clauses that ban class action proceedings prevent many consumers who have been harmed by corporate wrongdoing from seeking relief. These class action bans also shield



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corporations from liability for their illegal activities. This not only hurts the consumers who have already been harmed and cannot get their money back, but also hurts future consumers because often corporations abandon illegal practices the moment that a class action is filed. Allowing corporations to use arbitration clauses to ban class action proceedings encourages deceptive and predatory behavior by corporations, and injures consumers.

## V. COMPANIES DO NOT FORCE THEIR CONSUMERS AND EMPLOYEES INTO ARBITRATION BECAUSE IT IS CONSUMER OR EMPLOYEE FRIENDLY; RATHER, THEY DO IT BECAUSE THEY KNOW THAT IT WILL REDUCE THEIR COSTS AND LIABILITY FOR VIOLATING THE LAW.

A common refrain by many companies when asked about their unyielding effort to force their consumers and employees into arbitration is that they are doing this because it is better for consumers and employees. For example, in front of the Supreme Court, AT&T Mobility claimed that its clause provides "a realistic and effective dispute-resolution mechanism for consumers," and that, notwithstanding its ban on class actions, it "remains liable to all of its customers for all wrongdoing." *See* AT&T Br. in *Concepcion*, at p.44. This claim, however, is consistently contradicted by the actual data demonstrating how few consumers and employees actually pursue arbitration. After it won the *Concepcion* case, in contrast, in the *Cruz* case, AT&T argued that the court had to enforce its clause if it doing so would guarantee no recovery for all but an "infinitesimal" number of consumers.

Corporate advocates have spent a lot of money trying to generate data to compare the outcomes in a very small number of consumer cases that have been arbitrated against selected control groups of cases that went to court, with the goal of proving that arbitration is fair. (Corporate advocates talk a lot less about arbitration in the employment setting, because there is a LOT more data there, and – as will be established shortly – the data proves that employees win less often in arbitration than in court and when they do win, they win smaller sums than they



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would have been likely to win in court.) While a lot of the empirical data pulled together by tort-reformers about consumer cases is partisan and dubious, one empirical fact is hard to question: arbitration clauses serve to SUPPRESS consumer claims. Put another way, uncontested statistical data obtained in several cases has demonstrated that the vast majority of dissatisfied customers do not bring arbitrations against companies. For example, by the end of 2007, AT&T had become the largest wireless provider in the nation, with over 70 million customers. *See Coneff v. AT&T Corp.*, 620 F. Supp. 2d 1248, 1252 (W.D. Wa. 2009). But between January 1, 2003, and December 31, 2007, only *170 customers in the entire country* filed arbitration actions against AT&T.[5] And only 256 claims were filed in small claims court against AT&T in 2007 nationwide.

In comparison, Consumers Union reported that the year AT&T and Cingular merged, the companies had the worst records of customer complaints filed with the FCC.[6] Meanwhile, Consumer Watchdog, a non-profit consumer advocacy organization, received thousands of complaints from consumers.[7] A class action was brought as a result of those complaints.[8]

Within 24 hours of the press announcement that the class action had been filed, 1,800 AT&T customers contacted Consumer Watchdog with the same claims. As of March 2007, 4,700 complaints were received.[9] "No other legal action brought by [Consumer Watchdog] has . . . resulted in such a tremendous number of complaints following the announcement of a suit."[10]

This example is not an outlier. In the *Homa* case discussed above, involving American Express, evidence demonstrated that, despite the fact that American Express has millions of

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[5] Decl. of Bruce Simon in Supp. of Pls.' Opp'n to Am. Mot. to Compel Arbitration 2-3, *Coneff*.
[6] Decl. of Kevin Coluccio in Supp. of Pls.' Opp'n to Am. Mot. to Compel Arbitration, Ex. S, *Coneff*.
[7] Decl. of Douglas Heller in Supp. of Pls.' Opp'n to Am. Mot. to Compel Arbitration 2, *Coneff*.
[8] *Id.* at 2.
[9] *Id.* at 2-3.
[10] *Id.* at 2.



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customers, since 2006 only *twenty-three* arbitrations on any issue have been reported by either of the two largest arbitration providers in the country.[11] And in a case from California, discovery revealed that, other than the named plaintiff, only *one* of the putative class members had ever challenged Circuit City's overtime policy. Decl. of Ellen Lake in Supp. of Pls.' Opp. to Mot. to Compel Arbitration ¶ 7, *Gentry v. Circuit City Stores, Inc.*, No. BC280631, 2008 WL 8009240 (Cal. Super. Ct. Aug. 28, 2008). Moreover, between 1998 and 2008, only *two* California Circuit City employees had brought *any* claims in arbitration. *Id.* at ¶ 8.

In the North Carolina payday lending cases described above, there had not been ANY individual arbitrations filed against any of the payday lenders. None.

Moreover, at least one industry – nursing homes – has been straightforward in explaining that profits have driven the rise in mandatory arbitration. The industry openly admits that the reason it places arbitration clauses in the fine print of its contracts is because they save the industry money. Arbitration agreements allow the industry to escape financial responsibility for wrongdoing and increase profits because the agreements allow the nursing homes to choose their own arbitrators. Not surprisingly, those arbitrators have been shown to be beholden to the nursing home industry. They rule for the nursing home more often than the public courts would. They give smaller awards to injured residents than the public courts would. In 2008, Congressman Lamar Smith testified that "arbitration in the nursing home and assisted living sector arose out of the need to find some way to control escalating costs in the 1990s."[12] These efforts have proven successful, as the average nursing home claim amount in the United States shrank from $261,000 in 1998 to an estimated $116,000 in 2008. Arbitrated cases pay about 35% less to wronged consumers than non-arbitrated cases and cost nursing home companies

[11] Decl. of Matthew Wessler in Supp. of Pls.' Opp'n to Mot. to Compel Arbitration, *Homa*.
[12] Congressional testimony of Lamar Smith on H.R. 6126, July 30, 2008.



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about 41% less in legal fees.[13] Given these numbers, it's easy to see why the use of mandatory arbitration can be viewed as a good return on investment, even if this return is conditioned on hurting the very consumers and employees who support the business in the first place.

## IV. ARBITRATION IS OFTEN CLOAKED IN SECRECY, WHICH DISADVANTAGES CONSUMERS AND FAVORS CORPORATE REPEAT PLAYERS.

Another reason why companies want to force all their consumers and employees into arbitration is that the results of any arbitration will be secret. Arbitration is all-too-often completely secretive, with strict confidentiality rules sometimes limiting what can be publicly revealed either about the underlying facts of a dispute or about the arbitrators' rulings. Reporters are generally not allowed to be present in arbitrations, and proceedings are closed to the public. These characteristics are not inherent to arbitration, but too often become part of the process.

In addition, some arbitration clauses and the rules of some arbitration providers require that all parties to a dispute keep all facts about both the dispute and the arbitrator's resolution of the dispute "confidential." Furthermore, "[a]rbitrators have no obligation to the court to give their reasons for an award," *United Steelworkers of Am. v. Enterprise Wheel & Car Corp.*, 363 U.S. 593, 976 n.8 (1960), and it is common for arbitrators to provide no written explanation for their decisions. *See* Paul D. Carrington & Paul H. Haagen, *Contract and Jurisdiction*, 1996 Sup. Ct. Rev. 331, 397-98 (1996). Even when arbitrators do produce written decisions, "arbitrators' cisions are not intended to have precedential effect even in arbitration (unless given that effect by contract), let alone in the courts." *IDS Life Ins. Co. v. SunAmerica Life Ins. Co.*, 136 F.3d 537, 543 (7th Cir. 1998). Professor Richard Reuben, a proponent of alternative dispute resolution, has cautioned that arbitration can sacrifice important public values of transparency and

[13] Nursing home residents often sign away rights to sue, Jessica Fargen, Boston Herald, March 8, 2010



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accountability. Richard C. Reuben, *Democracy and Dispute Resolution: The Problem of Arbitration*, 67 Law & contemp. Probs. 279, 298-302 (Winter/Spring 2004).

This secrecy tends to reduce the ability of consumer attorneys to effectively represent their clients. *See* Jean Sternlight, *Panacea or Corporate Tool?: Debunking the Supreme Court's Preference for Binding Arbitration*, 74 Wash. U. L.Q. 637, 683-84 (1996) ("[A] consumer's attorney often relies on public information gained from other lawsuits to build her own claims of negligent or intentional misconduct. Repeat-player companies can gain similar information through private channels. Thus, by requiring private arbitration the company may again deprive the consumer of certain relief she might have obtained through litigation." (citations omitted)); *cf.* Marcus Nieto & Margaret Hosel, *Arbitration in California Managed Health Care Systems* 22 (2000) ("[P]laintiffs in California health care claims generally do not have information about arbitrators' decision records before selecting a neutral arbitrator. In contrast, health care plans do have information about the win-lose decisions of arbitrators. This information gap may favor health care plans.").

## V. ARBITRATION COMPANIES HAVE POWERFUL INCENTIVES TO FAVOR THE CORPORATIONS THAT SELECT THEM THROUGH THEIR STANDARD FORM CONTRACTS.

I have had numerous conversations with lawyers for corporations and advocates for individuals generally, and have participated in multiple mediations and settlement negotiations, and our experience is that the nearly universal perception among both plaintiff-side and defense-side lawyers is that arbitrators are more likely to have a pro-corporate defense attitude than are judges or juries. Exhaustive empirical evidence in the employment setting has proven this. Alexander J.S. Colvin, *Empirical Research on Employment Arbitration: Clarity Amidst the Sound and Fury*, 11 Employee Rights & Employment Policy J. 405 (2007) ("the more recent data on cases deriving from employer-promulgated agreements . . . suggest that employee win



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rates and damage awards are lower than indicated by the earlier studies and lower than those in litigation").

There is also evidence that companies believe arbitration is "fair" only when it can be used against consumers. For example, many of the same corporations that applaud arbitration when it is imposed against consumers are reluctant to agree to arbitration when it might be imposed against them. *See* Bar-Gill & Warren at 78 n.254 (noting that "arbitration clauses . . . are much more common in consumer contracts than in business-to-business contracts") (citing additional sources); Public Citizen, *Auto Dealers and Consumers Agree: Mandatory Arbitration Is Unfair* (listing various statements made by auto dealer representatives critical of arbitration and in support of bill to ban mandatory pre-dispute arbitration between dealers and car manufacturers), available at http://www.citizen.org/congress/civjus/arbitration/articles.cfm?ID=650.

A stark example of the double standard here can be found in the *Concepcion* case. Justice Scalia writes that it would be very unfair to require a corporation to go into arbitration where the arbitration would go forward on a class action basis. He says corporations should be able to insist upon individual arbitration. One of his reasons is that there is no meaningful judicial review of arbitrators' decisions, so if an arbitrator awarded a group of cheated consumers a lot of money, the corporation wouldn't be able to appeal that decision. By contrast, when the Supreme Court was considering whether to force civil rights claims in employment cases into arbitration, the employees argued, in effect, "you can't force something as important as civil rights claims into mandatory arbitration, because there is no real judicial review." The Supreme Court rejected this argument, saying that limited judicial review was a basic feature of arbitration, and that it was fine to force employment claims into arbitration. Under Justice



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Scalia's construct, mandatory arbitration is fine for things such as employment civil rights claims, but not fair for things that would matter to a corporation, such as a class action.

## VI. ARBITRATORS ARE IMMUNE FROM ANY MEANINGFUL JUDICIAL REVIEW.

The general rule is that judicial review of arbitrators' decisions "is very narrow; one of the narrowest standards of judicial review in all of American jurisprudence." *Lattimer-Stevens Co. v. United Steelworkers of Am. Dis. 27*, 913 F.2d 1166, 1169 (6th Cir. 1990).[20] Consider the following examples:

- The U.S. Court of Appeals for the Seventh Circuit remarked in a decision that courts should not review arbitrators' interpretations of contracts even if they are "wacky," so long as the arbitrator attempted to "interpret the contract at all." *See Wise v. Wachovia Securities, Inc.*, 450 F.3d 265, 269 (7th Cir. 2006).
- The U.S. Court of Appeals for the Third Circuit considered an arbitrator's decision that "inexplicably" cited and relied upon language that was not included in a key document. The court held that "such a mistake, while glaring, does not fatally taint the balance of the arbitrator's decision in this case. . . ." *Brentwood Medical Associates v. United Mine Workers of America*, 396 F.3d 237 (3d Cir. 2005).
- In a case involving baseball player Steve Garvey, the U.S. Supreme Court held that "courts are not authorized to review the arbitrator's decision on the merits" even if the

[20] *See also First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 942 (1995) ("the court will set aside [an arbitrator's] decision only in very unusual circumstances."); *Baravati v. Josephthal, Lyon & Ross*, 28 F.3d 704, 706 (7th Cir. 1994) ("[j]udicial review of arbitration awards is tightly limited."); *IDS Life Ins. Co. v. SunAmerica Life Ins. Co.*, 136 F.3d 537, 543 (7th Cir. 1998) ("judges follow the law . . ., while arbitrators, who often . . . are not lawyers and cannot be compelled to follow the law and their errors cannot be corrected on appeal (there are no appeals in arbitration), although there are some limitations on the power of arbitrators to flout the law."); *Di Russa v. Dean Witter Reynolds Inc.*, 121 F.3d 818, 821 (2d Cir. 1997) (to modify or vacate an arbitration award, a court must find both that (1) the arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether, and (2) the law ignored by the arbitrators was well defined, explicit, and clearly applicable to the case).



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arbitrator's fact finding was "silly." *Major League Baseball Players Ass'n v. Garvey*, 532 U.S. 504, 509 (2002).

- The California Supreme Court has held that even when an arbitrator's decision would "cause substantial injustice," it was not subject to judicial review. *Moncharsh v. Heily & Blase*, 3 Cal. 4th 1 (1992).

The law governing judicial review of arbitration also encourages arbitrators not to give any reasons for their decisions, because then it is entirely impossible to attack those decisions. *See Fellus v. AB Whatley, Inc.*, 2005 WL 9756090 (N.Y. Sup. Ct. Apr. 15, 2005) (in the absence of a reasoned decision supporting an arbitration award, there was no basis for court to decide whether arbitrator manifestly disregarded the law.); *H&S Homes v. McDonald*, 2004 WL 291491 (Ala. Dec.17, 2004) (in the absence of an explanation of damages awarded by arbitrator, court had no basis to determine whether arbitrator manifestly disregarded the law; arbitrator's failure to give reasons for the award did not itself constitute manifest disregard of the law). Seveal arbitrators have told me that they are discouraged by major arbitration firms from producing written decisions in most cases, because doing so puts them beyond any scrutiny. The upshot of all this is clear – arbitration is largely a system above and beyond the law.

This lack of judicial review undermines the public function of litigation. "By closing off access to proceedings, eliminating judicial precedent, and allowing parties to write their own laws, we compromise society's role in setting the terms of justice." *See* Jean Sternlight, *Panacea or Corporate Tool?: Debunking the Supreme Court's Preference for Binding Arbitration*, 74 Wash. U. L.Q. 637, 695 (citations omitted); *see also* Mike Ward, *Texas' chief justice calls for overhaul of state courts,* American-Statesman, February 21, 2007 ("'A privately litigated matter may well affect public rights,' [Chief Justice Wallace] Jefferson said. 'Its resolution may



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ultimately harm the public good or, because those decisions are secret, impede an innovation to a recurring problem, much to the detriment of Texas citizens.'").

**CONCLUSION**

In all too many cases, the promise of fair and inexpensive arbitration is not kept for American consumers and employees, and companies use mandatory arbitration clauses as a tool to avoid accountability.



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**Statement for the Record of**
**Christopher R. Drahozal**

**John M. Rounds Professor of Law**
**University of Kansas School of Law**

**October 13, 2011**

**Senate Judiciary Committee**

**Hearing on**
**Arbitration: Is It Fair When Forced?**

Chairman Franken, Ranking Member Cornyn, and Members of the Committee:
I am pleased to submit this statement for the record addressing the use of arbitration to resolve consumer and employment disputes. I am the John M. Rounds Professor of Law at the University of Kansas School of Law and an Associate Reporter for the Restatement, Third, of the U.S. Law of International Commercial Arbitration. I also served as the Chair of the Consumer Arbitration Task Force of the Searle Civil Justice Institute, and in that capacity was an author of the "Searle study," which examined in detail consumer arbitration cases administered by the American Arbitration Association ("AAA").[1] I submit this statement, not on behalf of any of those entities, but as an individual scholar who specializes in arbitration law.

**I. Overview: Empirical Research and the Fairness of Consumer Arbitration**

Both sides in the debate over the fairness of consumer and employment arbitration have recognized the importance of empirical research. Indeed, even Public Citizen, a vocal critic of consumer arbitration, has stated that it "agree[s]" that "congressional scrutiny of arbitration 'can be dangerous if the terms of the debate focus too much on anecdote and too little on systematic study.'"[2] According to Professor Peter B. Rutledge, "it now appears to be common ground that the policy debate over the Arbitration Fairness Act should focus on empirical data."[3] If so, that is an important and valuable development. Anecdotes alone do not provide a solid basis for legislative action.

But of course one must be cautious in evaluating empirical data as well. Even the best empirical studies have limits or are subject to qualifications. And numbers can be misleading if misinterpreted. So empirical studies must be used thoughtfully as a basis for making policy, recognizing both their value and their limitations.[4] My goal in this statement is to describe the empirical literature on consumer arbitration (which is what my research has focused on), highlighting both insights that the literature provides and circumstances in which it has been misconstrued.

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[1] *See* Consumer Arbitration Task Force, Searle Civil Justice Institute, Consumer Arbitration Before the American Arbitration Association: Preliminary Report (Mar. 2009), *available at* http://www.adr.org/si.asp?id=6610; *see also* Consumer Arbitration Task Force, Searle Civil Justice Institute, Creditor Claims in Arbitration and in Court: Interim Report (Nov. 2009). The Searle Preliminary Report is published as Christopher R. Drahozal & Samantha Zyontz, *An Empirical Study of AAA Consumer Arbitration*, 25 OHIO ST. J. ON DISP. RESOL. 843 (2010) [hereinafter Drahozal & Zyontz, *AAA Consumer Arbitration*]; and Christopher R. Drahozal & Samantha Zyontz, *Private Regulation of Consumer Arbitration*, 79 TENN. L. REV. ___ (forthcoming 2012), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1904545 [hereinafter Drahozal & Zyontz, *Private Regulation*]. The Searle Interim Report is published as Christopher R. Drahozal & Samantha Zyontz, *Creditor Claims in Arbitration and in Court*, 7 HASTINGS BUS. L.J. 77 (2011) [hereinafter Drahozal & Zyontz, *Creditor Claims*]. For the convenience of the Committee, I have attached the Executive Summary of both reports to this statement.

[2] Public Citizen, The Arbitration Debate Trap: How Opponents of Corporate Accountability Distort the Debate on Arbitration 2 (2008) (quoting Peter B. Rutledge, *Whither Arbitration?*, 6 GEO. J. L. PUB. POL'Y 549, 589 (2008)).

[3] Peter B. Rutledge, *The Case Against the Arbitration Fairness Act*, DISP. RESOL. MAG., Fall 2009, at 4, 4; *see also* Peter B. Rutledge, *Common Ground in the Arbitration Debate*, 1 Y.B. ARB. & MED. 1, 8 (2009) ("there now appears to be a consensus that the future of arbitration should be decided by data, not anecdote") (emphasis omitted).

[4] For a discussion of the limitations of the data used in the Searle study, for example, see Drahozal & Zyontz, *AAA Consumer Arbitration*, *supra* note 1, at 846, 896-97.



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The following summarizes the key points in the statement below:

- Most consumer contracts do not include arbitration clauses, and even most credit card issuers do not, and never have, included arbitration clauses in their cardholder agreements.
- High business win rates in arbitration do not show that arbitration is biased against consumers. Business win rates are as high, if not higher, in comparable court cases as they are in arbitration.
- Higher win rates of repeat businesses in arbitration are likely due to their better ability to screen cases and not due to biased decision-making by arbitrators.
- Many consumer arbitration clauses do not include class arbitration waivers, and it is unlikely that all businesses — or even all credit card issuers — will respond to the Supreme Court's decision in *AT&T Mobility v. Concepcion* by switching to arbitration.
- Restricting the enforcement of pre-dispute arbitration clauses is likely to have unanticipated consequences, harming rather than helping at least some if not many consumers.

**II. Consumer Choice and Pre-Dispute Arbitration Agreements**

A central theme in criticisms of consumer arbitration is that consumers do not have any choice if they want to avoid arbitration.[5] But it emphatically is not the case that all consumer contracts include arbitration clauses. To the contrary, the best available empirical evidence, although now somewhat dated, is that most consumer contracts do *not* include arbitration clauses.[6] Rather, it is only particular types of consumer contracts that include arbitration clauses.

Credit card agreements are commonly cited as a type of contract as to which consumers have no choice but to agree to arbitration.[7] In a 2009 House Hearing on the use of arbitration clauses by credit card issuers, Congressman Cohen (Tenn.) stated the commonly held view that

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[5] *E.g.*, S. 987, Arbitration Fairness Act of 2011, 112th Cong., § 2(3) (2011).

[6] Linda J. Demaine & Deborah R. Hensler, *"Volunteering" to Arbitrate Through Predispute Arbitration Clauses: The Average Consumer's Experience*, 67 LAW & CONTEMP. PROBS. 55, 62 (2004) ("Across the industries studied, fifty-seven of the 161 sampled businesses (35.4%) included arbitration clauses in their consumer contracts."). The use of arbitration clauses varied widely by type of industry. *Id.* at 63.

[7] Other studies of the use of arbitration clauses in consumer contacts include Florencia Marotta-Wurgler, *"Unfair Dispute Resolution Clauses: Much Ado About Nothing?*, *in* BOILERPLATE: THE FOUNDATIONS OF MARKET CONTRACTS 45 (Omri Ben-Shahar ed., 2007) (finding that only 6.0% of software license agreements studied included arbitration clauses, although noting that some of the contracts studied were commercial rather than consumer contracts); and Theodore Eisenberg, Geoffrey P. Miller, & Emily Sherwin, *Arbitration's Summer Soldiers: An Empirical Study of Arbitration Clauses in Consumer and Nonconsumer Contracts*, 41 U. MICH. J.L. REFORM 871, 883 (2008) (finding that 20 of 26, or 76.9%, of sample of consumer contracts included arbitration clauses; sample included consumer financial services and telecommunications contracts).



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"[n]early every credit card issuer includes an arbitration agreement in [its] ... contracts with cardholders."[8] David Arkush of Public Citizen has stated that "[n]early every consumer lender puts a clause in the standard-form contract saying that the consumer can never sue the company, for anything."[9]

In fact, it has never been the case that "[n]early every credit card issuer" uses arbitration clauses. As of December 31, 2009, over 80 percent (247 of 298, or 82.9%) of credit card issuers did *not* use arbitration clauses in their cardholder agreements.[10] Many, but not all, of those issuers were credit unions that offered credit cards to their members. Barely 17 percent (51 of 298, or 17.1%) of issuers used arbitration clauses in their credit card agreements.[11]

The reason for the perception that consumers had limited choice as to credit cards was that almost all of the very large credit card issuers used arbitration clauses. But even that has changed. As of December 31, 2009, just over 95 percent of credit card loans outstanding were by issuers that used arbitration clauses in their cardholder agreements. One year later, as of December 31, 2010, that percentage had declined to 48 percent.[12] The most recent data thus suggest that consumers have a much larger degree of choice (and, indeed, always have had a much larger degree of choice) than commonly perceived.

One additional point: critics assert that if arbitration is "fair," consumers will agree to it after a dispute arises, implying that the only reason for businesses to use pre-dispute arbitration agreements (and deny consumers the choice of going to court) is to take advantage of consumers. That is not the case: pre-dispute arbitration clauses permit consumers and businesses to enter into deals that make them both better off, deals that they could not enter into after a dispute arises. As I have explained in prior writing:

> [T]hat an individual who agreed to arbitrate before a dispute arose changes his or her mind [after a dispute arises] does not necessarily mean that enforcing the

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[8] *See Federal Arbitration Act: Is the Credit Card Industry Using It to Quash Legal Claims?*: Hearing Before the House Subcomm. on Comm'l and Admin. Law of the House Comm. on the Judiciary 1-2, 111th Cong. (2009), *available at* http://judiciary.house.gov/hearings/printers/111th/111-39_49475.PDF.

[9] Memo to Elizabeth Warren: How to Protect Consumers (Sept. 17, 2010) (quoting David Arkush, director, Public Citizen's Congress Watch division), *available at* http://blogs.reuters.com/reuters-wealth/2010/09/17/memo-to-elizabeth-warren-how-to-protect-consumers/.

[10] The Credit CARD Act of 2009 requires credit card issuers to supply their credit card agreements to the Federal Reserve, which in turn is to make them available to the public via the Federal Reserve web page. Credit Card Accountability Responsibility and Disclosure Act of 2009, § 204(a), 123 Stat. 1734, 1746-47 (May 22, 2009) (codified at 15 U.S.C. § 1632(d)(3)); 12 C.F.R. § 226.58; *see* Board of Governors, Federal Reserve System, Consumer Credit Card Agreements Search, http://www.federalreserve.gov/creditcardagreements/ (last visited October 7, 2011). The data described in the text were collected from credit card agreements available on the Federal Reserve web page.

[11] Christopher R. Drahozal & Peter B. Rutledge, Arbitration and Consumer Credit 20 & tbl. 3 (July 6, 2011), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1880180.

[12] Peter B. Rutledge & Christopher R. Drahozal, Contract and Choice 5 (Sept. 26, 2011) (work in progress; preliminary results). Most of the decline appears to be due to two factors: (1) the decision of the National Arbitration Forum to cease administering new consumer arbitrations in settlement of Minnesota Attorney General Swanson's consumer fraud suit against the NAF; and (2) the decision of four large issuers to settle an antitrust suit against them by agreeing to remove arbitration clauses from their cardholder agreements for three-and-one-half years. *Id.* at 4. Whether those issuers will resume use of arbitration clauses after that period expires is unknown.



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> predispute arbitration agreement is unfair. The individual may have been willing to give up the right to bring high-dollar but rare claims before a jury in exchange for the ability to pursue low-dollar but more common claims in arbitration. Such a deal is possible only before a dispute arises, when there is uncertainty as to what type of claim (if any) will materialize. Once the individual knows what type of claim he or she has (either high-value or low-value), either the individual may be unwilling to arbitrate (if it is a high-value claim) or the corporation may be unwilling to arbitrate (if it is a low-value claim that could not economically brought in court). By entering into a predispute arbitration agreement in such circumstances, the parties can enter into a deal that makes both of them better off. Permitting the individual (or the corporation for that matter) later to avoid arbitration would effectively preclude such deals from being made, making the parties worse off. Enforcement of the predispute arbitration agreement in this sort of case would be the fair, not the unfair, approach.[13]

The empirical evidence, while not decisive, is consistent with this view. The vast majority of consumer and employment arbitrations arise out of pre-dispute, not post-dispute, arbitration agreements.[14] That is true even for international arbitrations — a setting in which no one contends that arbitration is being used to take advantage of a weaker party.[15] The rarity of post-dispute arbitration agreements, even in international arbitration, suggests that parties can more readily enter into pre-dispute arbitration agreements than post-dispute agreements. Precluding parties from using pre-dispute arbitration agreements thus is likely to reduce, possibly dramatically, the use of arbitration to resolve consumer and employment disputes.

**III. Outcomes in Consumer Arbitration**

Critics of consumer arbitration have cited what they see as excessively high win rates for businesses as evidence that arbitration is unfair to consumers.[16] While I applaud their reliance on data rather than anecdotes, the conclusions critics draw from that data are incorrect.

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[13] Christopher R. Drahozal, *"Unfair" Arbitration Clauses*, 2001 U. Ill. L. Rev. 695, 749; *see also* Peter B. Rutledge, *Who Can Be Against Fairness? The Case Against the Arbitration Fairness Act*, 9 CARDOZO J. CONFLICT RESOL. 267, 278-80 (2008); Stephen J. Ware, *The Case for Enforcing Adhesive Arbitration Agreements – with Particular Consideration of Class Actions and Arbitration Fees*, 5 J. AM. ARB. 251, 262-64 (2006).

[14] Drahozal & Zyontz, *Private Regulation*, *supra* note 1, at 49 ("Indeed, virtually all of the 301 cases in the [consumer] case file sample — 290 (or 96.3%) — arose out of pre-dispute agreements; 11 (or 3.7%) arose out of post-dispute agreements to arbitrate."); Lewis L. Maltby, *Out of the Frying Pan, into the Fire: The Feasibility of Post-Dispute Employment Arbitration Agreements*, 30 WM. MITCHELL L. REV. 313, 319 (2003) ("AAA found only 6% (69/1148) of their 2001 employment arbitrations were the result of post-dispute agreements. In 2002, the frequency of post-dispute agreements was even lower, 2.6% (29/1124).").

[15] Stephen R. Bond, *How to Draft an Arbitration Clause (Revisited)*, 1(2) ICC INT'L CT. ARB. BULL. 14 (1990), *reprinted in* CHRISTOPHER R. DRAHOZAL & RICHARD W. NAIMARK, TOWARDS A SCIENCE OF INTERNATIONAL ARBITRATION: COLLECTED EMPIRICAL RESEARCH 65, 67 (2005) ("Of the cases submitted to the ICC Court, only four [of 237] in 1987 and six [of 215] in 1989 resulted from *a compromis*, that is, an agreement to submit an already-existing dispute to arbitration.").

[16] *E.g.*, Letter from Professors of Consumer Law and Banking Law to Senators Dodd and Shelby and Congressmen Frank and Bachus, Statement in Support of Legislation Creating a Consumer Financial Protection Agency 6 (Sept. 29, 2009), *available at* http://law.hofstra.edu/pdf/Media/consumer-law%209-28-09.pdf ("Studies



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First, win rates in consumer arbitration vary depending on the type of case being resolved and numerous other factors. Businesses do not always win in arbitration. For example, the Searle study found that consumer claimants won some relief in 53.3 percent of the AAA consumer arbitrations studied, and that, in those cases, consumers were awarded 52.1 percent of the amount they sought.[17]

Second, and more fundamentally, evaluating whether a win rate is too high (or too low) cannot be done in the abstract. It must be based on a comparison to a base line — or, in other words, you need to have a control group. The obvious control group to use here is courts: outcomes in arbitration cases need to be compared to outcomes in comparable cases in court in order to draw any conclusions about how consumers fare.[18] This is easier said than done, of course. It is hard to control for differences across types of cases. Important differences, such as the legal and factual strength of the case, are difficult to observe. That said, there is one type of case in which the characteristics of the cases are likely to be at least roughly comparable in arbitration and in court: debt collection cases brought by businesses — which happens to be the exact type of case cited by the critics as showing a high business win rate in arbitration.

So how do consumers fare in debt collection cases? In arbitration, as the data cited above suggest, businesses win the vast majority of the cases. The Searle study, for example, found that "[c]reditors won some relief in 86.2 percent of the individual AAA debt collection arbitrations and 97.1 percent of the AAA debt collection program arbitrations that went to an award."[19] But the study found that creditors won some relief at an even higher rate (ranging from 98.4 percent to 100.0 percent of the cases) in debt collection cases in court.[20] Likewise, while prevailing creditors were awarded from 92.9 percent to 99.2 percent of the amount sought in AAA arbitrations, they were awarded from 96.2 percent to 99.5 percent of the amount sought in debt collection cases in court.[21]

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have found the arbitrators find for companies against consumers 94 to 96% of the time, suggesting that arbitration providers are responding to the incentive to find for those who select them: the companies that insert their names in their form contracts.").

[17] Drahozal & Zyontz, *AAA Consumer Arbitration*, *supra* note 1, at 897-99. By comparison, business claimants won some relief in 83.6% of the AAA arbitrations studied, and in those cases recovered 93.0% of the amount sought. *Id.* at 898-99. The reason for the difference, as stated in the study, is not that arbitration is biased in favor of businesses but rather that businesses bring different types of claims than consumers. *Id.* at 901 ("Business claimants usually bring claims for specific monetary amounts representing debts for goods provided or services rendered. Many of the cases are resolved *ex parte*, with the consumer failing to appear. By comparison, cases with consumer claimants are much less likely to involve liquidated amounts and more likely to be contested by businesses.").

[18] *E.g.*, *Maine* Bureau of Consumer Credit Protection, Report to Committee: Compilation of Information Provided by Consumer Arbitration Providers 7 (Apr. 1, 2009) ("[A]lthough credit card banks or assignees prevail in most arbitrations, this fact alone does not necessarily indicate unfairness to consumers. The fact is that the primary alternative to arbitration (a civil action in court) also commonly results in judgment for the plaintiff."), *available at* http://www.maine.gov/pfr/consumercredit/documents/ArbitrationProvidersReport.rtf.

[19] Drahozal & Zyontz, *Creditor Claims*, *supra* note 1, at 80.

[20] *Id.* For data availability reasons, the study examined debt collection cases in Oklahoma and Virginia state courts, and student loan collection cases in federal court. I have every reason to believe the results would have been the same if we had studied other courts instead.

[21] *Id.* at 80-81. Controlling for confounding factors using multiple regression analysis did not change the results. *Id.* at 98-101.



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I certainly do not claim that these data show that arbitration is better for consumers than litigation. But likewise the data provide no support for the view that consumers fare worse in arbitration than they do in comparable cases in court.[22] And the data show definitively that high business win rates in arbitration do not in and of themselves prove that arbitration is unfair to consumers.

**IV. Incentives of Arbitrators and Arbitration Providers**

A more specific concern about outcomes in arbitration is the view that the structure of the arbitration process results in decisions that are biased in favor of businesses. Because arbitrators get paid only when they are selected to serve, rather than being paid salaries like judges are, critics assert that arbitrators will tend to favor "repeat players" — parties that will likely appear in arbitration on multiple occasions and so have more opportunities to appoint arbitrators than non-repeat players. Indeed, some have extended the criticism to providers of arbitration services, which are alleged to favor businesses (repeat players) over consumers in appointing arbitrators or otherwise structuring the arbitral process.

The evidence on whether repeat players have a higher success rate in arbitration is mixed. As noted above, businesses do have a higher win rate in arbitration than consumers, but that is likely due to the different types of claims businesses assert.[23] The usual test for the existence of a repeat-player effect has been to compare win rates for repeat businesses in arbitration to win rates for non-repeat businesses in arbitration.[24] The Searle study, for example, found that under this usual approach, repeat businesses had a slightly higher win rate against consumers than non-repeat businesses, but that the difference was not statistically significant. Under an alternative definition of repeat business, the study found a greater repeat-player effect, albeit even then one that was only weakly statistically significant.[25] Other studies, usually of AAA employment arbitrations, also have found that repeat businesses have a higher win rate in arbitration than non-repeat businesses.[26]

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[22] For evidence on comparative outcomes in employment cases in arbitration and court, see, *e.g.*, Theodore Eisenberg & Elizabeth Hill, *Arbitration and Litigation of Employment Claims: An Empirical Comparison*, DISP. RESOL. J., Nov. 2003-Jan. 2004, at 53 ("These results are consistent with arbitrators, at least those participating in AAA-sponsored arbitration, not acting in a materially different fashion than in-court adjudicators."). However, it is much more difficult to be confident that the cases being compared are actually comparable in the employment setting than in the debt collection setting.

[23] *See supra* note 17.

[24] *E.g.*, Lisa B. Bingham, *Employment Arbitration: The Repeat Player Effect*, 1 EMP. RTS. & EMP. POL'Y J. 189, 189-90 (1997). An alternative test would be to compare win rates for repeat businesses in arbitration to win rates for repeat businesses in court.

[25] Drahozal & Zyontz, *AAA Consumer Arbitration*, *supra* note 1, at 909-11.

[26] Bingham, *supra* note 25, at 213; Lisa B. Bingham, *Unequal Bargaining Power: An Alternative Account for the Repeat Player Effect in Employment Arbitration*, IRRA 50TH ANN. PROC. 33, 38-39 (1998); Lisa B. Bingham, *On Repeat Players, Adhesive Contracts, and the Use of Statistics in Judicial Review of Employment Arbitration Awards*, 29 MCGEORGE L. REV. 223, 223 (1998); Alexander J.S. Colvin, *An Empirical Study of Employment Arbitration: Case Outcomes and Processes*, 8 J. EMP. LEGAL STUD. 1, 11-16 (2011).



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But bias is not the only, or even the most likely, explanation for such a repeat-player effect. Repeat businesses are likely to be more sophisticated at screening cases and settling disputes than non-repeat businesses. As such, one would expect them be more likely than non-repeat businesses to settle the strong claims against them and arbitrate only the weak claims. If so, one would expect to find exactly the pattern described above: that repeat businesses have higher win rates than non-repeat businesses. One implication of this alternative theory is that repeat businesses will likely settle cases at a higher rate than non-repeat businesses. And that is exactly what the Searle study found: "that repeat businesses are more likely to settle or otherwise close cases before an award than non-repeat businesses."[27] Accordingly, the study concludes, "the repeat-player effect is more likely due to case screening by repeat businesses than arbitrator (or other) bias."[28]

As for alleged bias by arbitration providers in favor of businesses, such allegations seem belied by the adoption and enforcement of "due process protocols" by the two leading providers of arbitration services in the United States (the AAA and JAMS).[29] Due process protocols are private fairness standards designed to enhance the fairness of arbitration for consumers and employees.[30] Arbitration providers enforce the due process protocols by refusing to administer arbitrations under agreements that do not comply with the applicable protocol.[31]

The Searle study examined the AAA's enforcement of the Consumer Due Process Protocol, and concluded that the AAA "appears to be effective at identifying and responding to those clauses with protocol violations."[32] The study found that the arbitration clauses in 98.2% of the AAA cases studied either complied with the Due Process Protocol or that the AAA properly identified and responded to any non-compliance.[33] In addition, the AAA refused to

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[27] Drahozal & Zyontz, *AAA Consumer Arbitration*, *supra* note 1, at 913.

[28] *Id.* at 916. Lisa Bingham likewise concludes that the repeat-player effect was likely due, not to bias, but rather to better case screening by businesses. Lisa B. Bingham & Shimon Sarraf, *Employment Arbitration Before and After the Due Process Protocol for Mediation and Arbitration of Statutory Disputes Arising Out of Employment: Preliminary Evidence that Self-Regulation Makes a Difference*, *in* ALTERNATE DISPUTE RESOLUTION IN THE EMPLOYMENT ARENA: PROCEEDINGS OF THE NEW YORK UNIVERSITY 53RD ANNUAL CONFERENCE ON LABOR 303, 323 tbl. 2 (Samuel Estreicher & David Sherwyn eds. 2004).

[29] Most of the criticisms of arbitration providers were directed at the National Arbitration Forum, which no longer administers consumer arbitrations. As noted above, the NAF settled a consumer fraud suit brought against it by Minnesota Attorney General Swanson by agreeing not to administer new consumer arbitration cases. *See supra* note 12.

[30] *See* National Consumer Disputes Advisory Committee, Consumer Due Process Protocol (April 17, 1998), *available at* www.adr.org/sp.asp?id=22019; *see also* Task Force on Alternative Dispute Resolution in Employment, Due Process Protocol for Mediation and Arbitration of Statutory Disputes Arising Out of the Employment Relationship (May 9, 1995), *available at* www.adr.org/sp.asp?id=28535; Commission on Health Care Dispute Resolution, Health Care Due Process Protocol (July 27, 1998), *available at* www.adr.org/sp.asp?id=28633; National Task Force on the Arbitration of Consumer Debt Collection Disputes, Consumer Debt Collection Due Process Protocol – Statement of Principles (Oct. 2010), *available at* http://www.adr.org/si.asp?id=6248; JAMS, JAMS Policy on Consumer Arbitrations Pursuant to Pre-Dispute Clauses: Minimum Standards of Procedural Fairness (revised Jan. 1, 2007), *available at* www.jamsadr.com/rules/consumer_min_std.asp; JAMS, JAMS Policy on Employment Arbitration, Minimum Standards of Procedural Fairness (revised Feb. 19, 2005), *available at* www.jamsadr.com/rules/employment_Arbitration_min_stds.asp.

[31] *See* Drahozal & Zyontz, *Private Regulation*, *supra* note 1, at 16-18.

[32] *Id.* at 5.

[33] *Id.* The Searle study did not examine AAA enforcement of the employment due process protocol, but the available evidence suggests that AAA enforcement is effective in the employment context as well. *See* Bingham &



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administer at least 85 consumer cases (constituting 9.4 percent of its consumer caseload) because of protocol violations during the period studied, and over 150 businesses have waived problematic provisions or revised their arbitration clauses as a result of AAA protocol compliance review.[34] It is hard to square the AAA's enforcement of the Consumer Due Process Protocol with the suggestion that arbitration providers are systematically biased in favor of businesses.[35]

**V. Arbitration Clauses and Class Arbitration Waivers**

An important and as yet unanswered question is the effect of the Supreme Court's recent decision in *AT&T Mobility LLC v. Concepcion* on the use of arbitration clauses.[36] In *Concepcion*, the Court held that the Federal Arbitration Act preempts California's ability to use its unconscionability doctrine to invalidate arbitration clauses with class arbitration waivers — provisions that require arbitration to proceed on an individual rather than a class basis.[37] It is too soon after the decision in *Concepcion* to be able to evaluate empirically its effects. But the available empirical evidence does suggest a couple of possibilities worth noting.

First, prior to *Concepcion*, the use of class arbitration waivers varied by widely by industry, and many consumer arbitration agreements did not include class arbitration waivers at all. The Searle study found that of the arbitration clauses giving rise to AAA consumer arbitrations during the time period studied, only 36.5 percent (109 or 299) included class arbitration waivers.[38] All of the cell phone contracts included class arbitration waivers, as did all of the credit card contracts. But none of the insurance contracts and none of the real estate brokerage agreements included class arbitration waivers. And somewhat over half of the car sale contracts (53.1%) and home builder contracts (64.7%) included class arbitration waivers.[39]

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Sarraf, *supra* note 28, at 321 (finding consumer win rate increased after adoption of Employment Due Process Protocol); Eric Tuchmann, The Arbitration Fairness Act, Analyzed: International Dispute Negotiation Podcast 62, minute 14:05 (Feb. 20, 2009), *available at* http://www.cpradr.org/Resources/ALLCPRArticles/tabid/265/ID/455/IDN-62--The-Arbitration-Fairness-Act-Analyzed.aspx ("So if we tell them there's a problem with it in the employment context they're very likely to welcome our suggestions and make the changes that we're asking for. The consumer situation is a little bit different. Those are much more likely to be one-off disputes with customers.... The results are a little bit more mixed in the consumer context with organizations' willingness to comply with our requests.").

[34] Drahozal & Zyontz, *Private Regulation*, *supra* note 1, at 5. To be clear, the number of businesses waiving or revising problematic provisions is over the entire course of AAA application of the protocol, not just during the time period studied.

[35] Certainly there are other arbitration providers than the AAA and JAMS. Any concerns about those providers not following a due process protocol could be dealt with by legislation such as S.1186, the Fair Arbitration Act of 2011, 112th Cong. (2011), rather than a total prohibition of pre-dispute arbitration clauses in consumer and employment contracts.

[36] 131 S. Ct. 1740 (2011).

[37] *Id.* at 1753.

[38] Drahozal & Zyontz, *Private Regulation*, *supra* note 1, at 51.

[39] *Id.* One implication of this data is that making all consumer arbitration clauses unenforceable because of concerns about the availability of class relief would be overbroad. *See* Christopher Drahozal, Concepcion *and the Arbitration Fairness Act*, SCOTUSBLOG (Sep. 13, 2011, 11:46 AM), http://www.scotusblog.com/2011/09/concepcion-and-the-arbitration-fairness-act/.



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Second, even after *Concepcion*, it is unlikely that all consumer contracts — or even all credit card contracts, which ordinarily include class arbitration waivers when they include arbitration clauses — will begin using arbitration clauses. As Professor Rutledge and I conclude in a recent paper:

> Our finding that issuers are less likely to use arbitration clauses when located in states that (prior to *Concepcion*) had held class arbitration waivers unenforceable suggests that the use of arbitration clauses will increase as a result of *Concepcion*. But the significance of other variables in the model (the riskiness of the credit card portfolio, the degree of specialization in credit card loans, the size of the issuer, and the issuer's organizational form) suggests that not all credit card issuers are likely to use arbitration clauses following the decision in *Concepcion*.[40]

To illustrate the point: very few credit card issuers (5 of 97, or 5.2%) located in states that had held class arbitration waivers unenforceable prior to *Concepcion* used arbitration clauses. But even in states that had held class arbitration waivers enforceable prior to *Concepcion*, only a minority of credit card issuers (23 of 103, or 22.3%) used arbitration clauses.[41] That percentage likely will increase after *Concepcion*. But given the other factors that seem to explain the use of arbitration clauses by credit card issuers, these data suggest that the use of arbitration clauses will not become ubiquitous after *Concepcion*, even in the credit card industry.

**VI. Unintended Consequences of Restrictions on Consumer Arbitration Clauses**

After teaching contract law for seventeen years, it is clear to me that when parties face restrictions on one type of contract term, such as an arbitration clause, they often respond by changing other terms of their contract. And, in some cases, they might even respond by refusing to enter into a contract altogether. Too often decision makers do not consider these sorts of unintended consequences in evaluating the costs and benefits of proposed laws.

Several such unintended consequences might result from the adoption of restrictions on the use of pre-dispute arbitration clauses in consumer and employment contracts.

First, consumers and employees without disputes — who have no complaint with their treatment by a business — likely will be made worse off by legal restrictions on the use of arbitration. The cost savings that businesses achieve through arbitration benefit consumers by enabling the businesses to reduce prices and employers to increase wages.[42] Removing those cost savings by restricting the use of arbitration will have the opposite effect. The effect is likely to be particularly pronounced for those least able to afford it. For example, the consumers most likely to be affected by restrictions on the use of arbitration clauses in credit card agreements are those with low credit ratings who have few alternative sources of credit. A statistical examination of the factors explaining the use of arbitration clauses by credit card issuers finds a

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40 Drahozal & Rutledge, *Consumer Credit*, *supra* note 11, at 23.

41 *Id.* at 23 & tbl. 8.

42 *E.g.*, Ware, *supra* note 13, at 254-57.



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strong correlation between the riskiness of the issuer's credit card portfolio and its use of arbitration clauses.[43] If credit card issuers can no longer include arbitration clauses in their cardholder agreements, they may become less willing to lend to those higher risk consumers.

Second, restrictions on the enforceability of arbitration agreements may reduce rather than enhance the ability of some consumers and employees to have their claims heard. The available empirical evidence suggests that for relatively low-dollar claims, arbitration may be a more accessible forum than court.[44] Employment lawyer Lewis Maltby makes the point bluntly in the context of employment arbitration: "[M]ost employees will not be able to secure their employer's agreement to arbitrate once a dispute arises. The vast majority of employment disputes, however, do not involve enough damages to support contingent fee litigation. Therefore, outlawing pre-dispute agreements to arbitrate will leave many employees with no access to justice."[45]

Finally, some consumers will be less able to have their cases actually heard if the availability of arbitration is restricted. Very few court cases actually make it trial. Indeed, in 2009, only 1.2 percent of federal court dispositions were by either jury trial or bench trial.[46] Most court cases are resolved instead by dispositive motions or settlement. Consumers who bring those cases never have a "day in court" to tell their story to a judge or jury. By comparison, the Searle study found that over 50 percent of consumer claims in AAA arbitrations made it to a hearing before an arbitrator, and over 30 percent were resolved by the issuance of an award after a hearing.[47] To the extent there is value in consumers actually being able to present their claim to a neutral decision maker, restricting the availability of arbitration will deprive consumers of that value.

**VII. Conclusions**

To reiterate: my view is that sound public policy should be based on careful empirical study and not simply anecdotal reports. The available empirical evidence does not support the view that arbitration is necessarily unfair to consumers. Rather, that evidence suggests that pre-dispute arbitration clauses make some, if not many, consumers better off, and that broad-ranging restrictions on arbitration may well be counter-productive.

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[43] Drahozal & Rutledge, *Consumer Credit*, *supra* note 11, at 23.

[44] Eisenberg & Hill, *supra* note 22, at 53.

[45] Maltby, *supra* note 14, at 314.

[46] *See* Admin. Office of the U.S. courts, Judicial Facts and Figures tbl.4.10 (2010), *available at* http://www.uscourts.gov/uscourts/Statistics/JudicialFactsAndFigures/2009/Table410.pdf.

[47] Drahozal & Zyontz, *AAA Consumer Arbitration*, *supra* note 1, at 881 fig. 5. Of the hearings in the consumer cases studied, 62.1% were either in person or by telephone; the remaining cases involved document-only hearings. *Id.* at 893. But in the cases with document-only hearings, the consumer had the right to request an in-person or telephone hearing and evidently did not do so. *Id.* at 865 ("For claims seeking $10,000 or less, the default rule is that the case will be resolved on the basis of documents only. Either party may request a telephone or in-person hearing, however. Likewise, the arbitrator may hold a telephone or in-person hearing if he or she decides one is necessary. For claims seeking over $10,000, the default rule is that the arbitrator will hold either a telephone or in-person hearing unless the parties agree otherwise.").



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ATTACHMENT 1:

# CONSUMER ARBITRATION BEFORE THE AMERICAN ARBITRATION ASSOCIATION

## Executive Summary
**March 2009**

### *Issues and Background*

Empirical evidence has become a central focus of the policy debate over consumer and employment arbitration. Both supporters and opponents of the proposed Arbitration Fairness Act, which would make pre-dispute arbitration clauses unenforceable in consumer and employment (and franchise) agreements, have recognized that empirical evidence on the fairness and integrity of consumer and employment arbitration proceedings is essential to making an informed decision on the bill. Yet the empirical record, particularly on consumer arbitration, has critical gaps.

One set of issues on which further empirical research would be helpful is the costs, speed, and outcomes of consumer arbitrations. How much do consumers pay to bring claims in arbitration? How long do consumer arbitrations take to resolve? How do consumers fare in arbitration, particularly against businesses that are repeat users of arbitrators and arbitration providers? While a number of important studies on employment arbitration have been provided, the empirical record on these issues in consumer arbitrations is sparse.

A second set of issues of interest involves the enforcement of arbitration due process protocols -- privately created standards setting out minimum requirements of procedural fairness for consumer and employment arbitrations. Due process protocols commonly require independent and impartial arbitrators, reasonable costs, convenient hearing locations, and remedies comparable to those available in court. Leading arbitration providers have pledged not to administer arbitrations arising out of arbitration clauses that violate the protocols. But empirical evidence on the effectiveness of these private enforcement efforts is lacking.

### *Searle Civil Justice Institute Task Force on Consumer Arbitration*

To shed light on these issues, the Searle Civil Justice Institute (SCJI) undertook a large-scale study of consumer arbitrations administered by the American Arbitration Association (AAA). The AAA is a leading provider of arbitration services, including arbitrations between consumers and businesses. SCJI commissioned a Task Force to advise and lead this study of consumer arbitrations. Although the study will ultimately examine many aspects of AAA consumer arbitrations, the initial research inquiries were directed at two topics:

1. *Costs, Speed, and Outcomes of AAA Consumer Arbitrations.* This aspect of the Preliminary Report assesses key characteristics of the AAA consumer arbitration process. In particular, it examines the following research questions:



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- General characteristics of AAA consumer arbitration cases including claimant type (i.e., consumer or business), types of businesses involved, and amounts claimed.
- Costs of consumer arbitration (arbitrator fees plus AAA administrative fees), including the impact of the arbitrator's power to reallocate such fees in the award.
- Speed of the arbitration process from filing to award, in the aggregate and by claimant type (i.e., consumer or business).
- Various measures of outcomes such as win-rates, damages awarded, and evidence of as well as possible explanations for any repeat-player effects.

In addition to these broad research questions, SCJI also examined the extent to which consumer arbitrations are resolved ex parte; the frequency with which arbitrators award attorneys' fees, punitive damages, and interest; and results for consumers proceeding pro se.

2. *AAA Enforcement of the Consumer Due Process Protocol.* This aspect of the Preliminary Report provides an empirical analysis of how effectively the AAA enforces compliance with the Consumer Due Process Protocol. It considers a number of key research questions including:

    - To what extent do the consumer arbitration clauses comply, in their own right, with the Due Process Protocol?
    - How effective is AAA review of arbitration clauses for compliance with the Due Process Protocol?
    - To what extent does the AAA refuse to administer consumer cases because of the failure of businesses to comply with the Due Process Protocol?
    - How do businesses respond to AAA enforcement of the Protocol?

In addition to these research questions, SCJI examined several other issues that arise in connection with the Due Process Protocols.

### *Data and Methodology*

SCJI reviewed a sample of AAA case files involving consumer arbitrations. The primary dataset consists of 301 AAA consumer arbitrations that were closed by an award between April and December of 2007. (The focus on cases closed by an award during this particular timeframe is based on the availability of the original case files.) This sample of cases was then coded for approximately 200 variables describing various aspects of the arbitration process, including a review of the arbitration clause in the file. In addition, when possible a broader AAA dataset comprising all consumer cases closed between 2005 and 2007 was utilized. The AAA maintains this dataset in the ordinary course of its business, collecting data for internal purposes but not recording all variables of interest to SCJI. The data were analyzed using standard statistical methods in order to describe and evaluate consumer arbitrations as administered by the AAA.



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## *Key Findings – Costs, Speed, and Outcomes of AAA Consumer Arbitrations*

**The upfront cost of arbitration for consumer claimants in cases administered by the AAA appears to be quite low.**

In cases with claims seeking less than $10,000, consumer claimants paid an average of $96 ($1 administrative fees + $95 arbitrator fees). This amount increases to $219 ($15 administrative fees + $204 arbitrator fees) for claims between $10,000 and $75,000. These amounts fall below levels specified in the AAA fee schedule for low-cost arbitrations, and are a result of arbitrators reallocating consumer costs to businesses.

**AAA consumer arbitration seems to be an expeditious way to resolve disputes.**

The average time from filing to final award for the consumer arbitrations studied was 6.9 months. Cases with business claimants were resolved on average in 6.6 months and cases with consumer claimants were resolved on average in 7.0 months.

**Consumers won some relief in 53.3% of the cases they filed and recovered an average of $19,255; business claimants won some relief in 83.6% of their cases and recovered an average of $20,648.**

The average award to a successful consumer claimant in the sample was 52.1% of the amount claimed and to a successful business claimant was 93.0% of the amount claimed. This result appears to be driven by differences in types of claims initiated by consumers and business. Business claims are almost exclusively for payment of goods and services while consumer claims are seeking recovery for non-delivery, breach of warranty, and consumer protection violations.

**No statistically significant repeat-player effect was identified using a traditional definition of repeat-player business.**

Consumer claimants won some relief in 51.8% of cases against repeat businesses under a traditional definition (i.e., businesses who appear more than once in the AAA dataset) and 55.3% against non-repeat businesses – a difference that is not statistically significant.

**Utilizing an alternative definition of repeat player, some evidence of a repeat-player effect was identified; the data suggests this result may be due to better case screening by repeat players.**

Consumer claimants won some relief in 43.4% of cases against repeat businesses and 56.1% against non-repeat businesses under an alternative definition (based on the AAA's categorization of businesses in enforcing the Consumer Due Process Protocol) – a difference that is statistically significant at the 10% level. However, 71.1% of consumer claims against repeat businesses so defined were resolved prior to an award, while only 54.6% of claims against non-repeat businesses were resolved prior to an award. This suggests that such effect is attributable to better



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case screening by repeat players (i.e., settling stronger consumer claims and arbitrating weaker claims).

**Arbitrators awarded attorneys' fees to prevailing consumer claimants in 63.1% of cases in which the consumer sought such an award.**

Consumer claimants sought to recover attorneys' fees in over 50% of the cases in which they were awarded damages and were awarded attorneys' fees in 63.1% of those cases. In those cases in which the award of attorneys' fees specified a dollar amount, the average attorneys' fee award was $14,574.

## *Key Findings – AAA Enforcement of the Due Process Protocol*

**A substantial majority of consumer arbitration clauses in the sample (76.6%) fully complied with the Due Process Protocol when the case was filed.**

Most arbitration clauses in consumer contracts that come before the AAA are consistent with the Consumer Due Process Protocol as applied by the AAA. The same is true for cases in which protocol compliance was a matter for the arbitrator to enforce.

**AAA's review of arbitration clauses for protocol compliance was effective at identifying and responding to clauses with protocol violations.**

In 98.2% of cases in the sample subject to AAA protocol compliance review, the arbitration clause either complied with the Due Process Protocol or the non-compliance was properly identified and responded to by the AAA.

**The AAA refused to administer a significant number of consumer cases because of Protocol violations by businesses.**

In 2007, the AAA refused to administer at least 85 consumer cases, and likely at least 129 consumer cases (9.4% of its consumer case load), because the business failed to comply with the Consumer Due Process Protocol. The most common reason for refusing to administer a case (55 of 129 cases, or 42.6%) was the business's failure to pay its share of the costs of arbitration rather than any problematic provision in the arbitration clause.

**As a result of AAA's protocol compliance review, some businesses modify their arbitration clauses to make them consistent with the Consumer Due Process Protocol.**

In response to AAA review, more than 150 businesses have either waived problematic provisions on an ongoing basis or revised arbitration clauses to remove provisions that violated the Consumer Due Process Protocol. This is in addition to the more than 1550 businesses identified by the AAA as having arbitration clauses that comply with the Protocol. By comparison, AAA has identified 647 businesses for which it will not administer arbitrations because of Protocol violations.



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### *Policy Implications and Next Steps*

The empirical findings in the SCJI Preliminary Report on AAA consumer arbitrations have important implications for those interested in discussing and formulating public policy regarding arbitration.

1. Not all consumer arbitrations, arbitration providers, or arbitration clauses are alike. Differing results from empirical studies of arbitration may reflect variations associated with case mix, type of claimant, or provider review processes. This suggests the need for a nuanced approach to public policy concerning arbitration.

2. Private regulation complements existing public regulation of the fairness of consumer arbitration clauses. Policy makers should not ignore the role that arbitration providers can play in promoting fairness on behalf of consumers.

3. Courts could usefully reinforce the AAA's enforcement of the Consumer Due Process Protocol by declining to enforce an arbitration clause when the AAA has refused to administer an arbitration arising out of the clause or by otherwise reinforcing the role of the Due Process Protocol.

4. Arbitration may be less expensive for consumers than sometimes believed. For many consumers, the AAA arbitration process costs less than the amount specified in the AAA rules because arbitrators often shift some portion of the costs to businesses. Moreover, arbitrators award attorneys' fees to a substantial proportion of prevailing consumers in AAA consumer arbitrations.

5. Empirical studies have tended to find that repeat players fare better in arbitration than non-repeat players. To the extent such a repeat-player effect exists in arbitration, the critical policy question is what causes it. Our findings are consistent with prior studies in suggesting that any repeat-player effect is likely caused by better case screening by repeat players rather than arbitrator (or other) bias in favor of repeat players. A further as yet unresolved question is whether a repeat-player effect exists in litigation, and, if so, how litigation compares to arbitration in this regard.

While the empirical results presented in the SCJI Preliminary Report on Consumer Arbitration may usefully inform the policy debate on consumer arbitration, the Report nonetheless has limitations. First, its findings are limited to AAA consumer arbitrations. Empirical results from studying AAA consumer arbitration do not necessarily apply to other arbitration providers. Second, its findings on the costs, speed, and outcomes of AAA consumer arbitrations are difficult to interpret without a baseline for comparison, such as the procedures and practices in traditional court proceedings. A future phase of this research project by the Searle Civil Justice Institute's Task Force on Consumer Arbitration will undertake that comparison. It will seek to compare the procedures in AAA consumer arbitration with procedures available for consumers in court as well as comparing empirically key process characteristics of courts and arbitration.



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ATTACHMENT 2:

# CREDITOR CLAIMS IN ARBITRATION AND IN COURT INTERIM REPORT NO. 1

## Executive Summary
**November 2009**

### *Issues and Background*

With the recent settlement of a lawsuit brought by the Minnesota Attorney General against the National Arbitration Forum alleging fraud and deceptive practices, debt collection arbitration has again become a central focus of the policy debate over consumer arbitration. Some critics of consumer arbitration assert that the high win rate of business claimants in debt collection arbitrations alone shows that arbitration is biased in favor of businesses. Others compare the win rate of business claimants in arbitration to the win rate of consumer claimants in arbitration, concluding that the higher win rate of business claimants provides evidence of bias.
Neither of these measures, however, necessarily shows bias in arbitration. Instead, the proper comparison is between outcomes for business claimants in arbitration and outcomes for business claimants in comparable cases in court. But despite the need for such a comparison, on this issue, as with many issues in consumer arbitration, empirical studies are lacking.

This Interim Report builds on the Preliminary Report, Consumer Arbitration Before the American Arbitration Association, issued in March 2009 by the Searle Civil Justice Institute's Consumer Arbitration Task Force ("SCJI Task Force"). It seeks to compare the outcomes of AAA debt collection arbitrations to the outcomes of debt collection cases in court to help in evaluating arbitration as a means of resolving consumer disputes.

### *Data and Methodology*

The arbitration cases examined by the SCJI Task Force are 105 debt collection cases closed from April through December 2007 and included among the cases analyzed in the Preliminary Report (the "individual AAA debt collection arbitrations"). These cases are supplemented by 47,124 cases closed from March 2008 through June 2009 and brought by a single debt buyer as part of a consumer debt collection program administered by the AAA (the "AAA debt collection program arbitrations").

The court cases examined by the SCJI Task Force are 382 cases terminated between late 2006 and late 2007 seeking collection of unpaid student loans in federal court; 749 debt collection cases closed between April and December 2007 from Oklahoma state courts; and 283 debt collection cases closed in 2005 from Virginia state courts. The court systems included in the study were chosen solely for reasons of data availability.



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The Task Force focused on debt collection cases because debt collection cases tend to present relatively simple legal and factual issues and thus are relatively comparable in arbitration and in court. The data were analyzed using standard statistical methods to control for other identifiable differences among the cases, such as the amount claimed, the type of creditor, and whether the consumer appeared.

## *Key Findings*

**Creditors prevailed less often (that is, consumers prevailed more often) in the arbitrations studied than in court.**

In the cases studied, creditors won some relief in 86.2% of the individual AAA debt collection arbitrations and 97.1% of the AAA debt collection program arbitrations that went to an award. By comparison, creditors won some relief in 98.4% to 100.0% of the debt collection cases in court that went to judgment. This finding still holds even after controlling for differences among the types of cases and the venue in which they were brought.

**Creditor recovery rates in the arbitrations studied were lower than, or comparable to, creditor recovery rates in court.**

In the cases studied, prevailing creditors were awarded 92.9% of the amount sought in the individual AAA debt collection arbitrations and 99.2% of the amount sought in the AAA debt collection program arbitrations. By comparison, prevailing creditors were awarded from 96.2% to 99.5% of the amount sought in the debt collection cases in court. Even after controlling for differences among the cases, there was no statistically significant difference between creditor recovery rates in arbitration and in court.

**Consumer response rates in the arbitrations studied did not differ systematically from consumer response rates in court.**

In the individual AAA debt collection cases studied, consumers responded (i.e., did not default) in between 65.7% and 79.0% of the cases. In the AAA debt collection program arbitrations studied, consumers responded in between 1.9% and 14.8% of the cases. By comparison, the consumer response rate in the court cases studied ranged from 6.9% to 41.2%.

**The rate of other case dispositions (e.g., dismissals and settlements) did not differ systematically between the arbitration and court cases studied.**

Just under half (44.8%) of the individual AAA debt collection arbitrations studied were disposed of other than by award (e.g., by dismissal, withdrawal, or settlement), while 13.2% of the AAA debt collection program arbitrations studied were disposed of other than by award. By comparison, 22.1% to 35.0% of the debt collection cases in court were disposed of other than by judgment.



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### *Policy Implications*

The empirical findings in the SCJI Interim Report have important implications for the formulation of public policy regarding arbitration.

1. These empirical findings should dispel the notion that high creditor win rates and recovery rates in debt collection arbitrations in and of themselves show that arbitration is biased in favor of businesses. In fact, in the cases studied, creditor win rates and recovery rates were as high or higher in court than in arbitration.

2. High creditor win rates and recovery rates appear to be due to characteristics of debt collection cases rather than the venue – court or arbitration – in which those cases are resolved. Accordingly, it would appear that any policy prescriptions to deal with such concerns should focus on the process of debt collection rather than on dispute resolution venue.

3. Consumer response rates may also be due to characteristics of debt collection cases rather than the venue in which those cases are resolved. While the consumer response rate in AAA debt collection program arbitrations was low, the response rate in individual AAA debt collection arbitrations was higher – indeed, higher than the response rate in debt collection cases in court. Nonetheless, the low consumer response rate in debt collection cases in some venues suggests that further research into the reasons for the low response rate may be important to formulating policy in this area.

While the empirical results presented in the Interim Report may usefully inform the policy debate on consumer arbitration, the Report nonetheless has limitations. First, empirical results from studying AAA debt collection arbitrations do not necessarily apply to other types of arbitration or other arbitration providers. But in setting national policy concerning arbitration, information on consumer arbitrations administered by the AAA is necessary for making an informed decision. Second, the findings on debt collection actions in court necessarily are limited to the courts studied, but those findings appear broadly consistent with previous studies of debt collection cases in court. Third, to the extent we focus on court judgments and arbitration awards, differential settlement rates among the venues might bias our results. Fourth, cases are not selected into arbitration randomly; thus, finding truly comparable cases between court and arbitration is extremely difficult. Despite these limitations, however, the report furthers our empirical understanding of arbitration as a means of resolving consumer disputes, and contributes new information to the policy debate.



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# Fair Arbitration NOW

End Forced Arbitration – www.FairArbitrationNow.org

October 12, 2011

The Honorable Richard Blumenthal
United States Senate
Washington, DC 20515

The Honorable Al Franken
United States Senate
Washington, DC 20515

Re: S.1652, Consumer Mobile Fairness Act of 2011 Will Restore Consumers' Rights in Wireless Sector

Dear Senators Blumenthal and Franken:

A broad group of civil rights, consumer, employment, health, and labor organizations, representing millions of Americans, writes to express our strong support for your recently introduced legislation, the Consumer Mobile Fairness Act of 2011, S. 1652. Your legislation would bar forced arbitration clauses in consumer wireless contracts, restoring consumers' rights and eliminating this prevalent anti-consumer practice in the wireless industry.

The wireless industry has engaged in certain anticompetitive and unfair practices, charging consumers exorbitant early termination fees and illegal data charges, as well as including other deceptive costs on consumers' monthly wireless bills. Simultaneously, the companies have sought ways to evade accountability for their wrongdoing. They have inserted class action bans within forced arbitration clauses in their standardized contracts, restricting the rights of their approximately 300 million American customers.

Wireless carriers present individual arbitration as a streamlined way to resolve disputes, but the process is an impractical and rarely used option for consumers. In fact, class action bans effectively shield corporations from liability for their misconduct because consumer disputes against wireless carriers typically involve amounts of money that are too small to make pursuing an individual case feasible. On the other hand, class actions enable individuals to combine their limited resources, give them notice and allow them to vindicate their rights. In many instances, they would be—if not banned by the companies—the only viable method to resolve many wireless-related claims.

Prior to the Supreme Court's critical decision in *AT&T Mobility v. Concepcion*, courts applying the laws of 20 states had held that class action bans were void where they had the effect of exculpating the company from liability. In *Concepcion*, the Court ruled that under the Federal Arbitration Act states cannot stop corporations from using forced arbitration clauses to ban class actions, as a way to avoid accountability to their customers. In this case, Vincent and Liza Concepcion sued AT&T in 2006, alleging that the company defrauded millions of customers by advertising phones as "free," then tacked on an

undisclosed $30 charge for the phone. The $30 charge would, if multiplied across millions of AT&T customers, amount to millions of dollars in allegedly wrongful gains. The Court allowed AT&T to invoke the contractual ban on class actions inserted within its arbitration clauses and to require customers to bring their claims individually.

Your introduction of S. 1652 comes at a critical time. The Consumer Mobile Fairness Act would clarify federal law, accommodate numerous states' efforts to protect their residents from class action bans, and restore consumers' legal rights to hold the wireless industry accountable in court. We applaud your leadership, and look forward to working together on this issue.

Sincerely,

The Fair Arbitration Now Coalition
(To view a list of organizations and individuals that support ending the predatory practice of forced arbitration in consumer and non-bargaining employment contracts, please visit: http://www.fairarbitrationnow.org/content/coalition).

cc: Members of the Senate Judiciary Committee
Senate Majority Leader Harry Reid
Senate Minority Leader Mitch McConnell

**Senate Judiciary Committee**
**Hearing "Arbitration: Is It Fair When Forced?"**
**Statement for the Record**
**U.S. Senator Al Franken**
**October 13, 2011**

Thank you everyone for being here today. Thank you to my colleagues for their interest in this issue, and thank you to Chairman Leahy for giving me the opportunity to chair this hearing. And a special thanks to today's witnesses for sharing their time and expertise with the committee. Before I introduce today's witnesses, I'd like to take a few moments to clarify my intent in calling today's hearing.

The topic of mandatory arbitration is much more interesting than its dry-sounding title might suggest. Today, we're likely to discuss such wide-ranging legal issues as federal preemption, statutory construction, and class actions in situations as varied as chicken farmers to cell phone users to auto dealers. To the extent possible, I'd like to keep today's hearing focused on mandatory arbitration, as opposed to other voluntary types of alternative dispute resolution, or ADR. I'm not aware of any introduced legislation to "ban arbitration." I think everyone in this room can agree that there are some circumstances in which ADR, including post-dispute arbitration, should be encouraged. So let's focus our attention today on mandatory arbitration, which raises the most concern for me.

I'd also like to use this hearing to broadly highlight all of the efforts that have been made over the years to properly limit the use of mandatory arbitration. I'm far from the first Senator to champion this issue. Senator Feingold, a former colleague on the Committee, was a true pioneer. And Senator Feingold partnered with fellow Committee members to bring relief to certain groups particularly affected by mandatory arbitration.

The Ranking Member of this Committee, Senator Grassley, led the charge in limiting the use of mandatory arbitration clauses for poultry and livestock producers in contracts with their processors. He was able to secure the passage of a provision in the 2008 Farm bill. I'd like to submit for the record a letter from Craig Watts, a Fairmont, North Carolina chicken farmer. He is one of many farmers who, under this law, has chosen to opt-out of the arbitration clause in the contract he signed with his chicken processor. He notes that in his twenty years in contract poultry:

> "I know of no examples of anyone ever taking a dispute to the 'court of arbitration.' For a farmer it is just too expensive. . . But in the 2008 Farm Bill, Congress recognized how unconscionable these mandatory arbitration clauses were. . .and it resulted in the farmer getting to choose to keep it or opt out. . . it has not led to a wave of lawsuits as many had said. . . but I do believe it is an incentive to do business above board."

Another member of this Committee, Senator Hatch, led a similar effort to provide relief for auto dealers. In the Senate, this bill had 66 cosponsors. Thanks to Senator Hatch's efforts, America's auto dealers are now on a level contractual playing field with the big auto manufacturers.

These efforts all preceded my work on limiting forced arbitration for employees of defense contractors. They also preceded my introduction of the Arbitration Fairness Act this Congress, and the bill I recently introduced with Senator Blumenthal, the Consumer Mobile Fairness Act. These bills, like the ones that have come before it, seek to limit the use of forced arbitration clauses in contexts where one party suffers from a substantially weaker bargaining position. These particular bills focus on consumers and workers who sign form contracts with corporations.

Critics may argue that these contracts were entered into voluntarily and that we are compelled to honor forced arbitration clauses or risk abolishing entirely the freedom to contract. I think several of today's witnesses can speak to this issue better than I.

I am very honored today to introduce Minnesota's Attorney General, and my friend, Lori Swanson. In 2009, Attorney General Swanson sued the National Arbitration Forum on behalf of Minnesota consumers. At the time, the National Arbitration Forum was the country's biggest arbitrator of consumer credit disputes. In the course of her investigation, Attorney General Swanson revealed that the NAF, which presented itself to the public as a neutral arbitration company, was in fact working behind the scenes with the companies, against the best interest of consumers. In fact, the NAF boasted to the companies, quote, "customers don't know what to expect from arbitration and are more willing to pay," and that, quote, "customers ask you to explain what arbitration is then basically hand you the money." But I'll leave it to Attorney General Swanson to tell the rest of the story.

We're also pleased to have with us Dr. Deborah Pierce, currently the Associate Director of Emergency Medicine at Einstein at Elkins Park Hospital. She will share her experience from a previous employer and the subsequent arbitration process she endured after bringing a gender discrimination claim against that employer. Her story illustrates many of mandatory arbitration's serious problems, which have led me to question the merits of our current system.

We're joined also today by Paul Bland, a senior attorney at Public Justice. Mr. Bland has devoted nearly his entire career to representing consumer clients in countless cases around the country. He is a true wealth of knowledge on a range of issues, particularly consumer arbitration. Mr. Bland's experience litigating consumer cases after *Concepcion* will give us a realistic and sobering look at the prospects for consumer-enforced corporate accountability going forward.

We also welcome Professor Christopher Drahozal, the John M. Rounds Professor of Law and Associate Dean for Research and Faculty Development at the University of Kansas School of Law. Professor Drahozal has written extensively on the law and economics of arbitration. We also welcome Victor Schwartz, who is a partner at the firm of Shook, Hardy & Bacon LLP, and of the US Chamber of Commerce and the US Chamber Institute for Legal Reform.

Before I turn it over to today's witnesses, I want to reiterate my sincere goal that today we can find some common ground. We may not all agree on the best ways to move forward, and on which legislative proposals are needed, but I hope we can walk away with a few areas of agreement. I'll suggest the obvious—that there is a role for federal courts in our justice system.

This past August, Justice Kennedy replied to a reporter's inquiry about the Court's current docket, and he said this: "The docket seems to be changing. . . A lot of big civil cases are going to arbitration. I don't see as many of the big civil cases." Personally, I'm troubled that our private arbitration system is, at least in part, eclipsing the United States Supreme Court, the highest court in the land. Perhaps today's hearing can help us determine whether there is a sound middle ground—one where we use arbitration to the fullest fair extent, but allow our Supreme Court to fulfill its role as the true final arbiter.

Thank you.

Prepared Statement of Ranking Member Charles E. Grassley of Iowa
U.S. Senate Committee on the Judiciary
Hearing on "Arbitration: Is It Fair When Forced?"
Thursday, October 13, 2011

Mr. Chairman, I appreciate you holding this hearing.

It's important to study the role of arbitration and its impact on our society. But any study must be fair and balanced. And any study must be sensitive to the difficult economic conditions our citizens are dealing with.

Today, more than 14 million Americans are unemployed. That's a 9.1 percent unemployment rate. We also have an additional 8.8 million Americans who are underemployed. And the real unemployment numbers appear to get worse each month.

During these trying economic times, Congress must be focused on helping private businesses to create jobs. Congress should not be passing broad sweeping legislation that increases the number of costly and burdensome lawsuits filed each year. In particular, we should not be encouraging more class action lawsuits.

The Federal Arbitration Act currently allows courts to invalidate unconscionable arbitration agreements. It also allows courts to invalidate agreements obtained by fraud or duress. Each case is unique and arbitration agreements can be written in a variety of ways. Thus, any issues might be better addressed, case-by-case, by the courts, rather than by broad sweeping legislation.

So I look forward to reviewing the testimony from the witnesses and working with members of the Judiciary Committee on finding the right approach.

Thank you.

**Statement Of Senator Patrick Leahy (D-Vt.),**
**Chairman, Senate Judiciary Committee,**
**Hearing On "Arbitration: Is It Fair When Forced?"**
**October 13, 2011**

Today the Senate Judiciary Committee is once again highlighting how decisions of the Supreme Court affect hardworking Americans. The Court's arbitration decisions have denied thousands of Americans access to their courts and access to fair and impartial justice. I thank Senator Franken for taking the lead to address these decisions with critically important legislation, the Arbitration Fairness Act of 2011, and for chairing this timely hearing.

As I have noted before, in mandatory arbitration, there is no transparency. There is no independent arbitrator. There are no juries. There is no appellate review. Simply put, there is no rule of law and there is no justice.

Earlier this year, in *AT&T v. Concepcion*, the Supreme Court, in a narrowly divided 5-4 opinion, held that class action bans, if part of an arbitration clause, are enforceable, and any state law that says otherwise is preempted by the Federal Arbitration Act. The Supreme Court, once again, misinterpreted Congress' intent to favor corporations and further weaken protections for consumers.

Mandatory arbitration makes a farce of the right to a jury trial and the due process guaranteed to all Americans. But in its misinterpretation of statutes, the Supreme Court went beyond hampering just the rights of consumers by limiting their ability to bring claims against corporations. The Court twisted the intent of the Federal Arbitration Act to override the right of each state to protect its citizens.

Last year, in *Rent-A-Center v. Jackson,* the Supreme Court, in another 5-4 decision, held that courts do not retain the authority to hear claims that an arbitration agreement is unconscionable if the agreement delegates that determination to the arbitrator. That decision was a blow to our nation's historic civil rights laws and the protections that American workers have long enjoyed under those laws.

The four dissenting Justices noted that the question of whether a legally binding and valid arbitration agreement existed is an issue that the relevant statute assigns to the courts. When Congress passed the Federal Arbitration Act, it was clearly not intended to prevent employees from having access to an impartial court determination of whether the agreement was unconscionable. In this way, the ruling turns that purpose, and even the Court's own precedent, upside down. Justice Stevens, writing for the dissent, noted that he does "not think an agreement to arbitrate can ever manifest a clear and unmistakable intent to arbitrate its own validity."

Congress never intended the Federal Arbitration Act to become a hammer for corporations to use against consumers or American workers. Nor did Congress intend to limit Americans' ability to ban together in class proceedings. Class actions are an effective way to ensure consumer protection and protect hardworking Americans.

Now more than ever, Congress needs to respond to clarify the original intent of the Federal Arbitration Act and undo the damage the Supreme Court's misguided opinions have caused. Our laws must work for all working Americans, not just corporations. This effort should be bipartisan. I am disappointed that thus far, it has not been.

I look forward to hearing from our witnesses.

# # # # #

May, 2011

The Honorable Patrick Leahy, Chairman
The Honorable Chuck Grassley, Ranking Member
U.S. Senate Committee on the Judiciary
224 Dirksen Senate Office Building
Washington, DC 20510

Re: Letter in Support of the Arbitration Fairness Act of 2011, S. #

Dear Chairman Leahy and Ranking Member Grassley:

We, the undersigned organizations, strongly support the Arbitration Fairness Act of 2011 (or "AFA"), S. #, introduced in the Senate by Senator Al Franken (D-Minn.). This important legislation would end the predatory practice of forcing non-union employees and consumers to sign away their rights to legal protections and access to the courts by making pre-dispute binding mandatory arbitration ("forced arbitration") clauses unenforceable in civil rights and employment and consumer disputes. Forced arbitration is proliferating in employment and everyday consumer contracts for products and services such as credit cards, cell phones, home construction, mortgages, student loans, health insurance policies and nursing homes.

**Consumer, employee contracts with arbitration clauses are often non-negotiable.**

Corporations that place forced arbitration clauses in their standard contracts with consumers and non-union employees, shield themselves from accountability for wrongdoing. The contracts typically state who the arbitrator will be, under what rules the arbitration will take place, the state the arbitration will occur in, and the payment terms for the arbitration. Arbitration clauses are often contained in non-negotiable contracts and a person has no choice but to acquiesce or forgo the goods, services and/or employment altogether.

**Forced arbitration erodes traditional legal safeguards as well as substantive civil rights and consumer protection laws.**

None of the safeguards of our civil justice system are guaranteed for persons attempting to enforce their employment, consumer and civil rights in forced arbitration. There is no impartial judge or jury, but rather arbitrators who rely on major corporations for repeat business. With nearly no oversight or accountability, businesses or their chosen arbitration firms set the rules for the secret proceedings, often limiting the procedural protections and remedies otherwise available to individuals in a court of law. For example, the ability to obtain key evidence necessary to prove one's case is restricted or eliminated. In addition, the exorbitant filing fees, continuous fees for procedures such as motions and written findings, and "loser pays" rules in arbitration are prohibitive to many individuals, particularly in this weak economy when so many Americans are struggling just to make ends meet.

Forced arbitration also weakens the value of federal and state laws intended to protect consumers and employees by removing individuals' ability to enforce those laws in court. For example, a cornerstone of hard-won civil rights protections is the right for victims of workplace discrimination or harassment to have their claims heard by an impartial judge and jury. Increasingly, employers strip this right away and require workers to agree to forced arbitration as a condition of hiring or continued employment. By being forced into binding mandatory arbitration, an estimated 30 million non-union workers have lost essential protections established by our nation's civil rights laws.[1]

Other laws at risk include other provisions of the Civil Rights Acts of 1964 and 1991, the Age Discrimination in Employment Act, the Americans with Disabilities Act, the Family and Medical Leave Act, the Fair Labor Standards Act, the Equal Pay Act, the Uniformed Services Employment and Reemployment Rights Act, the Sherman Act, the Securities Act of 1933, the Securities Exchange Act of 1934, the Truth in Lending Act, and the civil provisions of the Racketeer Influenced and Corrupt Organizations Act.

Courts also have held that the Federal Arbitration Act (FAA) trumps state laws, even those intended to protect consumers, such as anti-predatory lending laws. Consequently, unscrupulous lenders use forced arbitration in subprime mortgages, payday loans, credit card contracts and nursing home contracts, thereby avoiding accountability.

On April 27, 2011, the U.S. Supreme Court dealt a devastating blow to consumers and employees, ruling that companies can ban class actions in the fine print of contracts. In *AT&T v. Concepcion*, the Court held that corporations may use arbitration clauses to cut off consumers and employees' right to join together through class actions to hold powerful corporations accountable.

The *AT&T v. Concepcion* ruling makes it all the more vital for Congress to pass the AFA to provide individuals with a choice to arbitrate a claim rather than forcing them into arbitration. The AFA would eliminate use of these pre-dispute clauses in consumer and employment contracts, returning the FAA to its original intent to facilitate private arbitration between sophisticated parties on equal footing.

**The AFA would allow consumers to choose arbitration after the dispute arises.**

The AFA does not seek to eliminate arbitration and other forms of alternative dispute resolution agreed to voluntarily after a dispute arises. Nor would it affect collective bargaining agreements that require arbitration between unions and employers. Its sole aim is to end the unscrupulous business practice of forcing consumers and employees into biased arbitrations by binding them long before any disputes arise.

We strongly support the Arbitration Fairness Act of 2011, which would restore access to our civil justice system and preserve important civil rights, employment and consumer protections. We urge you and the other members of Congress to pass S.#.



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Sincerely,

Alliance for Justice
American Association for Justice
American Civil Liberties Union
American Federation of Labor-Congress of Industrial Organizations (AFL-CIO)
American Federation of State, County and Municipal Employees (AFSCME)
Americans for Financial Reform
Arizona PIRG
Center for Responsible Lending
Citizen Works
ConnectiCOSH
Consumer Action
Consumers for Auto Reliability and Safety
Consumer Federation of America
Consumer Watchdog
Consumers Union
Empire Justice Center
Essential Information
Homeowners Against Deficient Dwellings
Home Owners for Better Building
Leadership Conference on Civil and Human Rights
Legal Services of New Jersey
Maryland Consumer Rights Coalition (MCRC)
MASSPIRG
MYF Legal Services, Inc.
NAACP
National Association of Consumer Advocates
National Community Reinvestment Coalition
National Consumer Law Center (On behalf of its low income clients)
The National Consumer Voice for Quality Long-Term Care (formerly NCCNHR)
National Consumers League
National Fair Housing Alliance
National Employment Lawyers Association
National Women's Health Network
National Women's Law Center
Neighborhood Economic Development Advocacy Project
New Jersey Citizen Action
Public Citizen
Public Justice Center
The Rural Advancement Foundation International (RAFI-USA)
Sargent Shriver National Center on Poverty Law
Service Employees International Union (SEIU)
USAction
Union Plus
U.S. Public Interest Research Group



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cc: Members of the Senate Judiciary Committee
Senate Majority Leader Harry Reid
Senate Minority Leader Mitch McConnell
Members of the House Committee on the Judiciary
House Speaker Nancy Pelosi
House Minority Leader John A. Boehner

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[1] *See* Alexander J.S. Colvin, *Empirical Research on Employment Arbitration: Clarity Amongst the Sound and Fury?*, 11 EMPLOYEE RTS. & EMP. POL'Y J. 405, 411 (2007)("[A] current estimate in the range of 15 to 25 percent of employers having adopted employment arbitration seems reasonable."). The 30 million figure is based upon a civilian labor force of 154.4 million Americans, as reported by the Bureau of Labor Statistics. Approximately 18.5 million American workers are unionized, leaving roughly 135 million non-union employees.



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**FOR IMMEDIATE RELEASE – October 13, 2011**

**CONTACT**
Eric M. Gutiérrez, Legislative & Public Policy Director
(202) 898-2880 x 115;egutierrez@nelahq.org

**The National Employment Lawyers Association Supports the Arbitration Fairness Act of 2011**
***Senate Committee on the Judiciary Holds Hearing—"Arbitration: Is It Fair When Forced?"***

(Washington, DC) – This afternoon, the Senate Committee on the Judiciary will conduct a hearing entitled, "Arbitration: Is It Fair When Forced?" The purpose of the hearing is to shine a light on the pervasive practice of forced arbitration clauses in employment and consumer contracts. The Arbitration Fairness Act of 2011 (AFA), H.R. 1873/S. 987, introduced in Congress by Senator Al Franken (D-MN), Senator Richard Blumenthal (D-CT) and Representative Henry C. "Hank" Johnson (D-GA), would prohibit pre-dispute forced arbitration of employment and consumer claims. Senator Franken will preside at the hearing.

Scheduled to testify is Dr. Deborah Pierce, Associate Director, Department of Emergency Medicine, Einstein at Elkins Park Hospital in Elkins Park, PA. Dr. Pierce attempted to sue her employer for discrimination but was compelled to arbitration after inadvertently signing a forced arbitration clause in her employment contract.

"NELA applauds Senators Franken and Blumenthal for highlighting how the use of forced arbitration clauses in the employment context stands in direct opposition to the civil rights and employment laws of this country. Dr. Pierce's story is not unusual. We wholeheartedly support the AFA and plan to do everything possible to ensure it becomes law," stated Eric M. Gutiérrez, NELA's Legislative & Public Policy Director.

Terisa E. Chaw, NELA's Executive Director, added "The efforts of Senators Franken and Blumenthal and Representative Johnson in banning forced arbitration are to be commended. As it becomes increasingly more difficult for employees to vindicate their rights and hold their employers accountable in a court of law, America's workers need the AFA more than ever. Today's Senate hearing exposes the injustices of forced arbitration and moves us closer to full enforcement our nation's workplace laws."

NELA is at the forefront of lobbying for the passage of the AFA. NELA's public interest arm, The Employee Rights Advocacy Institute For Law & Policy, commissioned a national study which found that a solid majority of Americans (59%) *opposes* forced arbitration clauses in the fine print of employment and consumer contracts, including both men and women, as well as majorities of Democrats, Independents, and Republicans. Similarly, strong majorities (59%) *support* the AFA, which also crosses gender and political lines. The study can be found at www.employeerightsadvocacy.org.

*The National Employment Lawyers Association advances employee rights and serves lawyers who advocate for equality and justice in the American workplace. NELA provides assistance and support to lawyers in protecting the rights of employees against the greater resources of their employers and the defense bar. It is the country's largest professional organization exclusively comprised of lawyers who represent individual employees in cases involving employment discrimination and other employment-related matters. NELA and its 68 state and local affiliates have more than 3,000 members around the country.*

# # #

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nelahq@nelahq.org · www.nela.org · Fax: 866.593.7521

**Testimony of Dr. Deborah Pierce,**
**Associate Director of Emergency Medicine, Einstein at Elkins Park Hospital**
**on "Arbitration: Is It Fair When Forced?"**
**Before the Senate Committee on the Judiciary**
**United States Senate**
**October 13, 2011**



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**Testimony of Dr. Deborah Pierce,**
**Associate Director of Emergency Medicine, Einstein at Elkins Park Hospital**
**on "Arbitration: Is It Fair When Forced?"**
**Before the Senate Committee on the Judiciary**
**United States Senate**
**October 13, 2011**

Chairman Leahy, Chairman Franken, Ranking Member Grassley, and distinguished Members of the Senate Judiciary Committee, thank you for the invitation to speak to you today about my experience with mandatory arbitration.

I would like to express my strong support of S.987, the "Arbitration Fairness Act," a bill that would prevent companies from inserting mandatory pre-dispute arbitration clauses in their consumer and employment contracts. I would also like to thank Senator Franken for introducing the bill and Senators Blumenthal and Whitehouse for cosponsoring this important legislation.

My name is Deborah Pierce. I currently am the Associate Director of Emergency Medicine at Einstein at Elkins Park Hospital, and the Assistant Residency Director of the Emergency Medicine Residency at Albert Einstein Medical Center in Philadelphia, Pennsylvania. I received my undergraduate degree in chemical engineering from Lehigh University and my medical degree from Philadelphia College of Osteopathic Medicine. I also have a masters degree in biochemistry. After my internship, I did a residency in emergency medicine. Upon completion of my residency, I started my academic career at Cooper Hospital/University Medical Center, where I spent seven years as the Associate Residency Director and as an Assistant Professor of Emergency Medicine at Robert Wood Johnson Medical School. After leaving Cooper, I started working for Albert Einstein Medical Center as the Associate Director Emergency Medicine Residency, where I worked for two years.

In June of 2004, during my second year at Einstein, I began working on a part-time basis with a physician practice group in a large, suburban-Philadelphia community hospital's emergency department. This private practice group manages the medical care of all of the patients in the hospital's emergency department. After working successfully on a part-time basis for the



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practice for one year, I was offered a full-time position. The salary offered to me by the practice was $40,000 less than I currently was making at Einstein, but the chairman of the practice assured me that the pay cut would be more than made up when I made partner two years after my hire. Based on the assurance of partnership, I accepted the position and left my full-time position at Einstein.

When I signed my employment agreement, I was unaware that it contained a mandatory arbitration clause. Even if I had known to look for such a provision, it would have meant nothing to me at that time. I consider myself an educated person, but I am not a lawyer and would not have known to recognize that the forced arbitration clause meant that I could never bring any future claims against the practice in a court of law. I also had no information about what the arbitration would involve. Further, even if I had understood the provision, I could not have removed it from the agreement. I had a choice: either accept the terms of the agreement, including the mandatory arbitration provision, or refuse to sign it and not get the job.

During my two full-time years with the practice, my job performance was never questioned and I consistently demonstrated that I was able to efficiently and successfully diagnose and treat patients as well as lead a team of medical providers under the stressful and chaotic working conditions of a busy emergency department. At no time during those two years was I told that there were any concerns about me being voted into partnership status, as every male physician before me had been made partner at the conclusion of their first two years. Yet at the end of 2006, to my shock and dismay, the chairman of the practice called me into his office, told me that the partners had voted to deny me partnership status and informed me that when my two-year employment agreement expired in June of 2007, I would be terminated. When I asked him for the reason why I was denied, he told me that he did not have to give me one.

Four months later, it is my understanding that a male physician with substantially less experience and whose two-year history with the practice apparently included performance problems, came up for partnership consideration. Instead of terminating his employment agreement and firing him, the practice voted to extend this male physician's agreement for an additional nine months in order to provide him a "probationary period" of time to improve what the chairman of the



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practice testified were "serious" problems with this physician's clinical medical practice. At the end of the nine-month period, the partners unanimously agreed to grant him partnership status. No such contract extension or probationary period was ever extended to me.

Two days after I was denied partnership, a partner in the practice handed me the phone number of a female physician who used to work for the practice, whom I did not know, and suggested that I reach out to her. He asked that I not tell anyone about him having given me her number. When I spoke with this female physician, she told me that despite her excellent job performance, she had been forced out of the practice prior to the partners taking a partnership vote on her and that she firmly believed that she too had been the victim of gender discrimination. Because she moved out of state immediately after being terminated, she had decided not to pursue action against the practice. She testified on my behalf at the arbitration. I subsequently learned of the practice's differential treatment of another female physician applicant, and presented evidence during the arbitration regarding that female physician as well.

At the time I worked for the practice, it was a virtually all-male partnership where seventeen out of the eighteen partners were men and the practice had already forced the resignation of a female founding member. This pattern has not changed since I was denied a position as partner. Since I left in 2007, the token woman partner remaining in the practice left and the practice has terminated the employment of highly qualified female physicians prior to their becoming eligible for partnership. To this day, the practice remains an all-male partnership.

Shortly after my termination, I brought my gender discrimination claim before the Equal Employment Opportunity Commission (EEOC). After an investigation, the EEOC determined that the practice violated Title VII in not affording me the same treatment as it did my male counterpart. I have attached to this Statement a copy of the EEOC's August 16, 2007 Determination for your review.

If I had not been forced to arbitrate my gender discrimination claim, I would have filed suit in federal court following receipt of the EEOC's Determination and Right to Sue letter. Instead, my only option for recourse at that point was, as required in my agreement, to arbitrate my



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employment discrimination claim before the American Health Lawyers Association (AHLA). Though extremely disappointed that I would not get an opportunity to have a jury of my peers determine the validity of my claim, both my attorneys and I expected the arbitration process to be fair and assumed my case would be presided over by an unbiased arbitrator with employment discrimination experience and a strong, working knowledge of the applicable evidentiary and employment discrimination laws. What I experienced, however, was exactly the opposite.

From the very first day of the arbitration, I had serious doubts that my arbitrator would be unbiased and fair. The arbitrator's law firm where the arbitration was held had rows of binders on display which were labeled with the name of the hospital whose emergency room was staffed by the doctors who denied me partnership. This indicated to me that he or his firm had previously represented the hospital. It was extremely troubling to me throughout the process to know that the hospital could be a repeat client and continued source of income for the arbitrator, whereas I was not and would never be. In addition, I was outraged to see, upon arriving early to the arbitrator's office one morning, the chairman of the practice walking out of the arbitrator's office carrying a cup of coffee. How can an arbitrator possibly be neutral and fair in administering justice in my case when part of his income depends on repeat business and he appears to be engaging in ex parte communications with the very person who was primarily responsible for the partnership's conduct?

I also had serious doubts about the knowledge and employment discrimination experience of the arbitrator, a health law attorney. Because I was forced to arbitrate my claims through the American Health Lawyers Association, I was severely limited as to the types of arbitrators available to preside over my claim. Despite having represented on his arbitration profile that he had thirty-four years of experience in resolving employment disputes, it seemed to me during the arbitration that the arbitrator had very little experience with employment law disputes and the applicable burdens of proof and standards of the law.

In terms of the costs, arbitration was far more costly than I could have ever anticipated. The arbitration provision in my employment agreement required me to pay half of the arbitrator's hourly fee of $450. The entire process cost me more than $200,000 and forced my husband and



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me to take out a home equity loan which to this day, more than three years later, we are still paying off. My law firm, which took my case on a partial contingent fee, spent and lost close to $500,000 in arbitrating my case. As a medical professional who earns a good salary, I had to go into debt in order to pay the fees and costs of my arbitration. Had I not found a law firm willing to take my case on a partial contingent fee, even I would not have been able to afford to arbitrate my claim. I don't know how anyone who earns what would be considered an average salary would ever be able to afford to arbitrate his or her discrimination claims. After my experience, it is simply unbelievable to me that one could claim that arbitration is a low-cost alternative to the court system.

The costs of the arbitrator were also driven up by the fact that the arbitrator let the practice get away with behavior that, in my understanding, would have been severely sanctioned and more importantly, not tolerated, in a courtroom setting. One of the major cost drivers of the arbitration was that the practice withheld and destroyed evidence that was responsive to my attorneys' discovery requests and critical to proving my claim. It was not discovered until several days into the 13-day arbitration that the practice had destroyed and withheld documents, when several questions elicited answers from the witnesses that demonstrated that many critical documents had not been turned over to my attorneys. My attorneys demanded that the documents be produced. This occurred several times over the course of the witnesses' testimony and, each time, the arbitration had to be stopped so that my attorneys could cull through and review the previously withheld documents and incorporate the hundreds of pages of new documents into the presentation of my case. Eventually, my attorneys were forced to request that the arbitration be suspended for several days because there were so many responsive documents dumped on them in the middle of the arbitration. By the time this additional discovery was completed, the practice had turned over more than 600 pages of critical documents, constituting 26% of the documents produced over the eight-month period of the arbitration process. It is my understanding that this behavior would never have been countenanced by a federal court, which has the power to sanction both a party and its attorneys for such egregious conduct.

During the course of the arbitration, my attorneys repeatedly made motions seeking a dismissal of the proceeding so that we could file my claim in a court of law. Each time, the arbitrator



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summarily denied the motion. In addition, my attorneys filed three different sanctions motions, one of which was for the practice's deliberate delay of the proceedings. The violations complained of in this motion were so outrageous, involving both significant delay and deliberate destruction of responsive documents, that the arbitrator granted the motion. However, despite finding in my favor and ordering the practice to pay me $1000.00 in sanctions, he turned around and charged me more than $2000.00 in fees for his time in deciding the motion! It is my understanding that in a court of law, I would not have been penalized for having brought a meritorious motion that the court granted in my favor. So when all was said and done, I was forced to pay the arbitrator more than double what I recovered for the practice's sanctioned misconduct.

When the arbitrator finally ruled on my case, he of course found that the other side had not treated me in a discriminatory fashion, despite the clear and overwhelming evidence to the contrary and the intentional misconduct on the practice's part throughout the arbitration. The content of his ruling demonstrated that he neither applied the applicable law to the facts of my case nor considered the majority of my substantial evidence presented over the course of the 13-day arbitration. In one particularly demonstrative example, one of the witnesses when testifying during the arbitration unequivocally contradicted her earlier deposition testimony on a critical issue -- whether or not the practice ever voted to give me a probationary period like it did my male counterpart. When cross-examined about the contradictory testimony, the witness unbelievably testified that since her deposition, her memory had been "clarified" after (1) speaking to her attorneys; (2) reviewing some unspecified documents; and (3) meeting with her fellow partners to "re-establish[] the chronology of events" related to the meeting in which the partners voted on my partnership. Despite the vehement objections of my attorneys, the arbitrator not only permitted this witness' testimony into the record, but relied on it in rendering his decision against me. What he clearly did not rely on in reaching his decision, was any of the evidence presented by me regarding the practice's differential treatment of other female physicians. Unbelievably, he failed to so much as mention that evidence in his opinion.

Because of the additional substantial expense both I and my law firm would have had to incur, and my understanding that my chances of convincing a judge to overturn the arbitrator's decision



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were not great, I felt I had no viable option to appeal following his decision. On September 8, 2008, my attorneys submitted a lengthy letter to the President and Executive Vice President/Chief Executive Officer of the American Health Lawyers Association (AHLA), arguing that AHLA failed to provide to me the services for which I paid significant sums under the arbitration contract and that AHLA and the arbitrator failed to meet their obligations as described in AHLA's Rules of Procedure for Arbitration and Code of Ethics for Arbitrators. AHLA virtually ignored my attorneys' arguments and instead responded by repeatedly asserting that it does not certify or attest to the abilities, competence or performance of its arbitrators and does not make any "warranties about the ability of the arbitrator to weigh facts and law." I have attached to my Statement copies of both my attorneys' letter to AHLA and AHLA's response.

I interpreted AHLA's response to mean that it refused, and will continue in the future to refuse, to police the actions of its arbitrators and that despite how egregiously unfair the result of an AHLA arbitration may be, there is nothing that can be done about it.

Even as an educated physician, I never could have navigated the legally intricate arbitration system without the help of my attorneys. Yet because of the astronomical costs associated with my arbitration and the losses it incurred, it is my understanding that the law firm that represented me is no longer representing employees who have been forced to sign mandatory arbitration agreements as a condition of their employment. What that says to me is that until this bill gets enacted into law, there will be countless numbers of employees with no recourse whatsoever to pursue a remedy for their employment discrimination claims. In my opinion that is an absolute travesty of justice.

For me, the mandated arbitration process was unbelievably expensive, unfair and biased. It took away my faith in a fair and honorable legal system which is supposed to protect the civil rights of its citizens. I am hoping that this process today results in a much needed change in the law so that no one who follows me has to endure what I experienced. The mandatory arbitration system must be repaired to ensure that it truly is a voluntary system whereby people can fairly seek justice for the wrongs committed against them. Congress provided in the employment discrimination laws the right of an aggrieved employee to have her claims heard in federal court.



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Employers are unilaterally denying that right to employees with impunity. Congress should restore employees' access to the courts in discrimination cases by passing the Arbitration Fairness Act.

Thank you for the opportunity to share my story.



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September 8, 2008
Via Federal Express

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**Re: Dr. Deborah L. Pierce v. Abington Emergency Physician Associates, P.C.: A-020907-497**

Dear Messrs. Hamme and Leibold:

On behalf of our client, Dr. Deborah L. Pierce, we are writing this letter to inform the American Health Lawyers Association ("AHLA") of several very serious issues concerning the handling of the above-referenced employment discrimination case by Vasilios J. Kalogredis, the AHLA arbitrator, and to request an investigation of this matter. We have performed our due diligence before writing to you by reviewing the case in depth. We believe that the arbitrator's Opinion was so deeply flawed and his failure to consider the evidence so substantial, that Dr. Pierce's civil rights claims were not properly heard; moreover, we believe that some of the billing for the arbitrator's work was inappropriate and excessive. Simply put, we believe that AHLA failed to provide to Dr. Pierce the services for which she paid significant sums under the arbitration contract. As set out below, it is our contention and belief that AHLA and Mr. Kalogredis failed to meet their obligations and our rightful expectations in this matter as described in AHLA's Code of Ethics for Arbitrators and AHLA's Rules of Procedure for Arbitration. Specifically, we maintain that AHLA and Mr. Kalogredis fell short of meeting the following qualifications set forth in the Code of Ethics for Arbitrators:

1.01 Honesty, Fairness and Impartiality
1.02 Competency
1.03 Knowledge
1.05 Timeliness

## I. The Requirements for an Arbitrator in this Matter

An arbitration clause in her employment contract with Abington Emergency Physician Associates, P.C. ("AEPA") required that Dr. Pierce arbitrate her employment discrimination claims, civil rights claims, before an AHLA arbitrator. Pursuant to AHLA's rules, we submitted a Request for Dispute Resolver List, an AHLA form, (Exhibit 1) on which we made clear that this was an employment discrimination case based on sex.[1]

Essential in this case, as in all cases of employment discrimination, is that the arbitrator be well versed in the intricacies and nuances of employment discrimination law. This is an area of law that absolutely requires a fact-finder to undertake an extremely fact-intensive analysis before reaching a decision as to the merits of the claims. Any practitioner who is experienced, knowledgeable and competent in the field of employment discrimination law knows and understands the central importance of a careful and full consideration of the relevant facts of a case. Fact-finders must obtain the entire picture of the workplace in order to understand the often subtle and hidden forms of discrimination that now exist. The days of "smoking-gun" evidence are generally in the past. It is for this reason that the outcome of discrimination cases, perhaps more than any other type of case, turns on ensuring that the fact-finder has a comprehensive understanding of the facts and then performs a thorough legal analysis by applying the law to the facts. A fact-finder who fails to undertake a thorough analysis of all the relevant facts of an employment discrimination case raises questions about his fairness, competency and knowledge in this area of the law, deficiencies which could cause him to fall short of meeting the requirements of AHLA Code of Ethics Rules 1.01, 1.02 and 1.03.

The profile of Mr. Kalogredis, (Exhibit 2) provided to us by AHLA at the commencement of this case states that he has thirty-four (34) years of experience resolving labor and employment disputes. We relied on that profile in selecting him and based our selection on the representation that he was knowledgeable, experienced and competent to preside over Dr. Pierce's gender discrimination claims and, ultimately, to issue a decision in the case that meets the requirements of the AHLA arbitration contract. It now appears that our justifiable reliance on AHLA's profile was misplaced.

## II. AHLA's Contractual Obligations to Dr. Pierce Were Not Met Because Mr. Kalogredis' Opinion Failed to Consider Her Evidence

In our view, the Opinion issued by Mr. Kalogredis on June 25, 2008 demonstrated a fundamental lack of knowledge and experience in considering and deciding employment discrimination claims, demonstrated by his disturbing failure to consider the

[1] Paragraph 4 of the Request states that Dr. Pierce was denied shareholder status on the basis of her gender; Paragraph 5 states that Dr. Pierce had filed an employment discrimination charge with federal and state agencies; and Paragraph 6 requests all relief available pursuant to Title VII and the Pennsylvania Human Relations Act.



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plaintiff's evidence and legal arguments and culminating in his failure to apply the law to the facts of the case. The most important skill necessary to the analysis of any employment discrimination case is the ability to apply the law to the evidence in the case. We believe that Mr. Kalogredis failed to do that in his Opinion, substantially ignoring the majority of Dr. Pierce's evidence to the material detriment of her case. Mr. Kalogredis' Opinion consisted of a regurgitation of the law set forth by the parties in their post-arbitration briefs, and a handful of conclusory statements. Incredibly, he failed to address or analyze almost all of Dr. Pierce's evidence set forth in detail in (1) her Pre-Hearing Statement (Exhibit 3); (2) at the lengthy hearing which ran 13 hearing days from February 25, 2008 to March 19, 2008; or (3) in her Post-Hearing Brief (Exhibit 4); regarding AEPA's discriminatory conduct, its differential treatment of other female employees, and the inconsistent testimony of several of AEPA's witnesses.

A critical part of the shifting burden analysis applied to employment discrimination cases is the plaintiff's opportunity to prove that the employer's "legitimate business reasons" for her termination are pretextual. Significantly, Mr. Kalogredis' Opinion virtually ignored the vast majority of Plaintiff's evidence that AEPA's articulated reasons for its actions were pretextual; such an oversight undermines the very legitimacy of the decision. Failure to properly analyze and weigh our client's evidence may be indicative of a lack of fairness and impartiality, both of which are required under Rule 1.01 of AHLA's Code of Ethics.

As arbitrator, Mr. Kalogredis had the discretion to conclude that the evidence did not prove pretext, but that discretion requires that the arbitrator actually consider, and base his decision on, the evidence. The case law unequivocally required that Mr. Kalogredis, as fact-finder, review each of AEPA's articulated reasons for not granting Dr. Pierce shareholder status and then analyze whether each reason was credible, taking into account the evidence presented by Dr. Pierce refuting those reasons. (*See* Plaintiff's Pre-Hearing Statement, Exhibit 3, and Plaintiff's Post-Hearing Brief, Ex. 4). An arbitrator who is competent and knowledgeable, (as required under AHLA Code of Ethics 1.02 and 1.03) would have undertaken this very analysis. We believe that by failing to do so, Mr. Kalogredis abrogated the weighty responsibility he had to fairly judge Dr. Pierce's civil rights claims, and AHLA therefore breached its arbitration contract with Dr. Pierce.

**a. <u>A Comparison of Mr. Kalogredis' Opinion and Dr. Pierce's Post-Hearing Brief Demonstrates that Mr. Kalogredis Failed to Consider the Majority of Dr. Pierce's Evidence</u>**

A comparison of Dr. Pierce's evidence adduced at the hearing (set forth in her Post-Hearing Brief which is replete with cites to the record (Ex. 4)), with the Opinion and Order issued by Mr. Kalogredis (Ex. 5), demonstrates that he gave little to no consideration to Dr. Pierce's substantial proof. Dr. Pierce produced significant evidence of pretext to refute AEPA's proferred business reasons for not promoting her to shareholder: that (1) Dr. Pierce did not "work harmoniously with others;" (2) was "unlikely to contribute in a positive way to the overall success of AEPA;" and (3) that her



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productivity was insufficient for shareholder status. As shown below, Mr. Kalogredis almost uniformly failed to consider, let alone analyze, Dr. Pierce's evidence.

1. **Working harmoniously with others" and "contributing in a positive way to the overall success of AEPA."**

- Evidence introduced by Dr. Pierce showing that there was no complaint about her working harmoniously with others or contributing positively to the overall success of the corporation in the two years prior to her shareholdership vote **was completely ignored** by Mr. Kalogredis in his Opinion. (Plaintiff's Post-Hearing Brief, Ex. 4, p. 32).
- Evidence introduced by Dr. Pierce showing a dearth of factual testimony about these three alleged complaints prior to and even during the meeting at which her shareholder candidacy was discussed **was completely ignored** by Mr. Kalogredis in his Opinion. (Plaintiff's Post-Hearing Brief, Ex. 4, p. 33). Similarly, evidence introduced by Dr. Pierce showing that she was never told of any problems regarding her "interaction with co-workers" **was completely ignored** by Mr. Kalogredis in his Opinion. (Plaintiff's Post-Hearing Brief, Ex. 4, p. 36).
- Evidence introduced by Dr. Pierce showing that AEPA witnesses were not credible as they had at best a vague recollection of facts surrounding AEPA's "legitimate business reasons" **was completely ignored** by Mr. Kalogredis in his Opinion. (Plaintiff's Post-Hearing Brief, Ex. 4, p. 37).
- Evidence introduced by Dr. Pierce showing that AEPA witnesses were not credible as they lacked specifics to support their conclusory allegations **was completely ignored** by Mr. Kalogredis in his Opinion. (Plaintiff's Post-Hearing Brief, Ex. 4, p. 37).
- When Dr. Pierce introduced evidence that it was AEPA's own shareholders, and not Dr. Pierce, who were "failing to contribute to the best interests of the corporation," and that male physicians were held to a lower standard than she, Mr. Kalogredis analyzed the matter by conclusorily stating that the AEPA shareholders **were "fine with this" and that the "process has been properly and consistently handled."** (Plaintiff's Post-Hearing Brief, Ex. 4, p. 40; Opinion, Ex. 5, p. 11).

2. **Productivity**

Mr. Kalogredis completely ignored Dr. Pierce's evidence of pretext in response to AEPA's position that Dr. Pierce's productivity was insufficient for shareholder status.

- Evidence introduced by Dr. Pierce that contrary to AEPA's claims, Dr. Pierce's productivity increased while a male doctor's (who also was a shareholder candidate) productivity decreased prior to their respective shareholder candidacy votes, was **completely ignored** by Mr. Kalogredis, who merely accepted AEPA's pretextual claim at face value. (Plaintiff's Post-Hearing Brief, Ex. 4, p. 42).



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- Evidence introduced by Dr. Pierce that male doctors slowed down the volume of patients being treated, but that she did not, **was similarly completely ignored** by Mr. Kalogredis. (Plaintiff's Post-Hearing Brief, Ex. 4, p. 45).
- Evidence that AEPA managing physicians Kidwell and Ball manipulated AEPA shareholders regarding the primary reason given for not selecting Dr. Pierce for partnership (productivity) was **completely ignored** by Mr. Kalogredis in his Opinion. (Plaintiff's Post-Hearing Brief, Ex. 4, p. 49).
- Evidence introduced by Dr. Pierce that AEPA's own doctors admitted that they did not understand productivity data at the time they voted on Dr. Pierce's shareholder status was **again completely ignored** by Mr. Kalogredis in his Opinion. (Plaintiff's Post-Hearing Brief, Ex. 4, p. 50).
- Finally, evidence proffered by Dr. Pierce that Dr. Kidwell clearly intentionally misrepresented to AEPA shareholders and to Dr. Pierce that productivity was listed as a job requirement in her contract was **also completely ignored** by Mr. Kalogredis in his Opinion. (Plaintiff's Post-Hearing Brief, Ex. 4, p. 53).

### 3. Evidence of preferential treatment of a male doctor

Discrimination can be proven by evidence showing that the employer gives preferential treatment to a similarly situated employee not in the plaintiff's protected class. When Dr. Pierce showed that AEPA voted to give preferential treatment to a male doctor in substantially similar circumstances, Mr. Kalogredis merely concluded "I do not see disparate treatment here. All shareholders were given the opportunity to express their opinions pro and con . . ." as to the male doctor's candidacy as well as Dr. Pierce's. (*See* Plaintiff's Post-Hearing Brief, Ex. 4, p. 39; Opinion, Ex. 5, p. 7). Instead of considering Dr. Pierce's evidence of differential treatment and analyzing whether it demonstrated pretext or discrimination, Mr. Kalogredis **essentially held that as long as AEPA chose to treat them differently there was no 'disparate treatment.'** *Id.* With respect to Dr. Pierce's probation vote, the shareholders' testimony was nowhere close to consistent as to whether or not Dr. Pierce passed a probation vote. (*See* Plaintiff's Post-Hearing Brief, Ex. 4, pp.19-22). Four shareholders testified that they were certain that Dr. Pierce **had passed** the vote. *Id.* One shareholder completely changed her testimony on the subject between her deposition and her hearing testimony. *Id.* at 57-59. Another shareholder testified that no probation vote was ever taken for Dr. Pierce. *Id.* at 21. With seemingly no analysis whatsoever, and ignoring the blatant, transparent contradictions in the testimony of the AEPA shareholders, Mr. Kalogredis' blithely concludes that "[i]n spite of what may have been some confusion at the time, she was not offered that one-year probationary period." (*See* Ex. 5). This conclusory statement is false – there were many shareholders who were not confused at all about the results of the probation vote for Dr. Pierce and were certain that Dr. Pierce had passed the vote.



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**4. Evidence of differential treatment of other female employees and defendants' contradictory testimony**

In addition, Mr. Kalogredis made no mention in his Opinion of the evidence that Dr. Pierce presented of AEPA's differential treatment of other female employees – direct evidence of differential treatment of at least one other female physician, Dr. Susan Nowak -- (Plaintiff's Post-Hearing Brief, Ex. 4, pp. 54-56); nor did he mention the blatant evidence of contradictory testimony by AEPA witnesses during the hearing which, Dr. Pierce argued in her Post-Hearing Brief, rendered their testimony unworthy of belief (Ex. 4, pp. 57-59). Again, the arbitrator may reject any of the plaintiff's evidence as not probative of discrimination, **but his Opinion lacks any indication that he even considered the evidence.** As stated above, it is absolutely essential that a fact-finder in an employment discrimination case give full and fair consideration to evidence of pretext, and a failure to do so strongly suggests a lack of impartiality, competence or knowledge of employment discrimination law. (AHLA Rules 1.01, 1.02 and 1.03).

**b. Mr. Kalogredis Ignored and Failed to Consider his own Findings Issued In Deciding Plaintiff's Motions for Sanctions**

Credibility determinations are central to rendering decisions in employment law cases where the issue of pretext is in dispute because evidence of dishonesty goes to the very essence of whether an employer is telling the truth about its reasons for the adverse employment action. During this litigation Dr. Pierce filed not one, not two, but three motions for sanctions due to AEPA's misconduct, all of which were granted. Mr. Kalogredis' Opinion ignores the evidence of AEPA's lack of credibility which he himself had found in deciding those compelling motions for sanctions. The first was a Motion for Assessment of Fees and Costs necessitated by AEPA's refusal to arbitrate in this arbitration that AEPA, not Dr. Pierce, had mandated, until a court could decide AEPA's motion to compel arbitration! Mr. Kalogredis found that AEPA "continually failed to comply with [his] orders and the contractually agreed to process," and "continually ignored this Arbitrator's communications and caused delays and disruptions." (*See* Mr. Kalogredis' July 25, 2007 letter Opinion and Order, Exhibit 6). In granting Dr. Pierce's motion Mr. Kalogredis stated that AEPA's "total disregard of the process [was] unacceptable." *Id.* Plaintiff's second Motion for Sanctions requested an adverse evidentiary inference necessitated by AEPA's destruction of tape recordings of two AEPA shareholders' meetings. Mr. Kalogredis granted the Motion, finding that AEPA **intentionally** destroyed the tapes which contained information relative to the shareholder candidacies of both Dr. Pierce and her nearest comparator. (*See* Kalogredis January 21, 2008 letter opinion, Ex. 7). Plaintiff's third Motion for Costs and Fees arose out of AEPA's withholding, until after the start of the arbitration hearing, twenty-five percent of the documents responsive to Plaintiff's document requests necessitating the extraordinary adjournments of the hearing for a number of days to take depositions, review documents and for Plaintiff's counsel to prepare a second time for the testimony of virtually all the witnesses. Mr. Kalogredis found that "AEPA had possession of the documents in question, had knowledge of their existence, and had a responsibility to have all of its shareholders turn over the documents they had. Also, AEPA was represented by



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experienced, able and employment law specialty legal counsel." (*See* Kalogredis Opinion and Order of May 19, 2008, Ex. 8). He found that Dr. Pierce had in fact been prejudiced and that nothing could be done to completely obviate the effect of AEPA's conduct, *Id.* at p. 4, which resulted in multiple "elements of prejudice." *Id.* at 4-5. Although Mr. Kalogredis found that AEPA had engaged in prejudicial conduct which could not be cured, he did not consider this conduct whatsoever in his limited review of the evidence adduced at the hearing. His failure to take into account such a significant finding in his weighing of the evidence suggests a lack of impartiality, competency and knowledge of procedure. (AHLA Rules 1.01, 1.02 and 1.03).

## III. The Billing for the Arbitrators' Time in Rendering His Opinion and Decision was Excessive

In total, Dr. Pierce paid Mr. Kalogredis **$58,521.51, one-half of his $117,000 fee,** for his services in this case. From very early on in the process, Dr. Pierce and this firm were concerned about the billing practices of Mr. Kalogredis, yet because the case was pending we were not in any position to complain to him or AHLA about it.

We believe that the records show that Mr. Kalogredis overbilled for the work performed in deciding the matter and writing his Opinion; the Opinion issued ignores significant amounts of evidence presented, fails to apply the law to the facts adduced by Plaintiff, has no cites to the record and lifts entire sections from the parties' own briefs. It appears clear to us that the Opinion issued by Mr. Kalogredis could not possibly have taken him the approximately fifty (50) hours of work he billed after the hearing. This raises the possibility of two significant breach of contract claims on behalf of Dr. Pierce: first, that the services contracted for were not provided (the Opinion being of significantly substandard quality) and second, that the services billed for were not provided (the time billed not reasonably bearing a relation to the services provided).

## IV. Mr. Kalogredis Did Not Properly Assess the Costs of Plaintiff's Sanctions Motions

Similarly, Mr. Kalogredis' treatment of the onerous financial burden visited upon Dr. Pierce by Defendant's misconduct suggests a cavalier attitude toward his responsibility to properly assess sanctions. In his July 25, 2007 Order granting Plaintiff's first Motion for Sanctions for Delay of Proceedings he ordered AEPA to pay her $1,000.00 in sanctions, but he charged Dr. Pierce more than $2,000 for his time in deciding the Motion rather than assess his fees entirely to AEPA, which not only wiped out the entire $1000.00 but ended up costing her a significant amount. Although she prevailed on the Motion, she had to pay Mr. Kalogredis more than double what she recovered from AEPA for its egregious conduct. (*See* Ex. 6 and Mr. Kalogredis' bill for the period June 27, 2007 (when Plaintiff filed her Motion) to July 25, 2007, when Mr. Kalogredis ruled on the Motion, Ex. 9).

As set forth above, in his finding regarding Dr. Pierce's second Motion, Mr. Kalogredis found that AEPA intentionally destroyed evidence, but inexplicably denied



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Dr. Pierce's request for attorney's fees for having to file the Motion due to AEPA's wrongdoing. No explanation or justification was given by Mr. Kalogredis. (*See* Ex. 7).

With respect to Dr. Pierce's third motion for sanctions for AEPA's intentional failure to produce evidence, although Mr. Kalogredis found that AEPA's conduct prejudiced Dr. Pierce, and that such **prejudice could not be cured**, he granted only one-half of the attorney fees the prejudicial conduct cost Dr. Pierce, and denied all of the court reporter's fees, without explanation. (*See* Ex. 8). Moreover, he charged Dr. Pierce for his time in finding that AEPA had caused uncurable prejudice to Dr. Pierce, refusing Dr. Pierce's request to shift such fees to AEPA stating his original decision was meant to be 'final.' *Id.* at 2. Again, no explanation or justification for his arbitrary decision was set forth.

## V. The Arbitrator Delivered an Opinion That is Untimely, in Violation of Rule 6.04, AHLA's Rules of Procedure for Arbitration

Pursuant to AHLA's Rules of Procedure for Arbitration, Rule 6.04, Mr. Kalogredis was required to issue his Opinion "no later than thirty days from the date of the closing of the hearing." The parties and he agreed that the closing of the hearing would be on the date that he received the parties' post-hearing briefs, which was May 12, 2008. Thirty days from May 12th was June 11th, decision day. To put things in perspective, June 11 was close to three (3) months after the hearing had concluded and close to two (2) months after Mr. Kalogredis had received all of the arbitration transcripts. Mr. Kalogredis had nearly ninety (90) days – after having already heard the evidence during the arbitration hearing – to issue his Opinion.

On June 11, however, after having not received any Opinion, Plaintiff's counsel emailed Mr. Kalogredis that it was her understanding that his Opinion was due that day and to ask when we could expect it. It was not until the next day that he responded to the email and notified the parties that he would not be adhering to AHLA's thirty-day rule. At no time did Mr. Kalogredis seek the parties' consent to violate Rule 6.04's thirty-day mandate. He did not issue his Opinion until June 25, 2008, forty-four (44) days after the close of the hearing. In that time period between June 11 and June 25, he charged $6,401.00 for his services (he charged a total of $18,315 to the parties from the date the hearing ended until the date he issued his Opinion). (*See* Kalogredis bills for the time period March 19, 2008 through June 25, 2008, Ex. 10). Mr. Kalogredis breached AHLA's Rules of Procedure and Dr. Pierce should not have had to pay for any of his services past June 11, 2008.

## VI. AHLA Should Investigate the Provision of Arbitration Services in this Matter.

For the above reasons, Dr. Pierce and we request that AHLA undertake an investigation of the services provided in this matter by Mr. Kalogredis, including his compliance with the requirements of AHLA's Code of Ethics, its Rules of Procedure for Arbitration and his billing practices.



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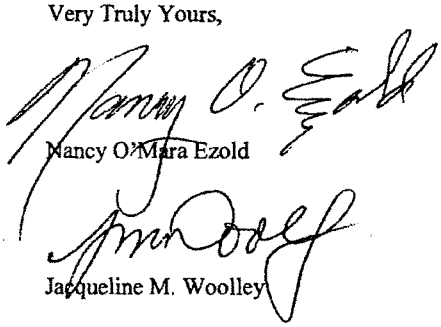
This plaintiff was forced to use AHLA's arbitrators to decide issues that are not even remotely related to health law. Although Mr. Kalogredis might be knowledgeable regarding health law matters, our experience in this costly case was that he lacks the requisite experience when it comes to hearing and deciding statutory claims of employment discrimination. We question whether AHLA engages in a certification process adequate to insure that its arbitrators are competent to issue binding decisions on very serious, fact-intensive and subtle civil rights cases of employment discrimination. If AHLA is failing to engage in such a process, it puts at risk the integrity and protection of the civil rights of the thousands of employees, like Dr. Pierce, who must rely upon the quality and fairness of AHLA's approved arbitrators.

Very Truly Yours,



Nancy O'Mara Ezold

Jacqueline M. Woolley

cc: Dr. Deborah L. Pierce (w/o encl.)(via email)
Vasilios J. Kalogredis, Esquire (w/o encl.)(via First Class Mail)



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AHLA ADR SERVICE

1025 Connecticut Avenue, NW, Suite 600, Washington, DC 20036-5405 • (202) 833-1100 • Fax (202) 833-1105

September 18, 2008

**VIA UPS**

Nancy O'Mara Ezold, Esq.
Jacqueline M. Woolley, Esq.
Nancy O'Mara Ezold, P.C.
One Belmont Avenue, Suite 501
Bala Cynwyd, PA 19004

**Re: Dr. Deborah L. Pierce v. Abington Emergency Physician Associates, P.C.; A-020907-497**

Dear Counsel:

Thank you for your letter of September 8, 2008 regarding the above-referenced matter as it relates to the arbitrator's qualifications, his handling of the dispute, the arbitrator's opinion, and his billing practices. You not only expressed disappointment in the arbitrator's handling of the case, you "believe that AHLA failed to provide to your client the services for which she paid significant sums under the arbitration contract." You write that both "AHLA and Mr. Kalogredis failed to meet their obligations and our rightful expectations in this matter as described in AHLA's Code of Ethics for Arbitrators ("Code of Ethics") and AHLA's Rules for Procedure for Arbitration ("Arbitration Rules")."

While Mr. Kalogredis can respond for himself if he so chooses, we disagree with your analysis that the American Health Lawyers Association's Alternative Dispute Resolution Service ("the AHLA ADR Service" or "the Service") did not meet its obligations under the Code of Ethics and Arbitration Rules. In brief, you make the following allegations against the American Health Lawyers Association (AHLA):

1) Mr. Kalogredis somehow misled you in his resolver profile by saying that he had thirty-four (34) years of experience in resolving labor and employment disputes. You relied on this representation in choosing him, and you were injured by this reliance on "AHLA's profile" of Mr. Kalogredis.
2) AHLA did not meet its "contractual obligations" because Mr. Kalogredis failed to consider the plaintiff's evidence and legal arguments, culminating in his failure to apply the law to the facts of the case.
3) AHLA failed to engage in a "certification" process adequate to insure that its arbitrators are competent, as shown by Mr. Kalogredis' alleged overbilling for his work, misallocation of costs on plaintiff's sanctions motions, and failure to file his opinion and order within the thirty (30) days required by the Arbitration Rules.

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**1) Allegation of misleading information in Mr. Kalogredis' profile.**

In your letter, you imply without offering any evidence that Mr. Kalogredis inflated his years of experience in resolving labor and employment issues. Based on the fact that he has been selected in numerous other cases and no complaints have ever been filed against him for lack of experience or for mishandling a case, we have every reason to believe that his profile is accurate. However, the Service has not independently investigated whether the profile is accurate because the Arbitration Rules and the Request for Dispute Resolver List are crystal clear that the Service does not certify the information placed in the resolver profile:

> By invoking these Rules of arbitration by the Service, all parties acknowledge that the Service does not verify the information submitted to the Service by prospective arbitrators nor does the Service certify or in any way attest to the abilities or competence of such persons. *American Health Lawyers Association Alternative Dispute Resolution Service Rules of Procedure for Arbitration,* Introduction, A-6 (Revised July 2008)[1].

The Arbitration Rules are not limited to a solitary mention of this disclaimer:

> The Service has not investigated, and makes no representation or warranty with respect to the accuracy or completeness of any information furnished or required to be furnished in any Application Form or with respect to the competence or training of any such arbitrator. *American Health Lawyers Association Alternative Dispute Resolution Service Rules of Procedure for Arbitration,* Section 2.02, A-8-A-9 (Revised July 2008).

This disclaimer not only appears in two places in the Arbitration Rules, it is squarely and clearly disclosed on the form signed by Dr. Pierce on February 8, 2007, which was used to request a dispute resolver list.

> Each requesting party ... (iv) recognizes that neither the Health Lawyers nor the Service certifies or verifies the qualifications or the experience of the dispute resolver(s)... Request for Dispute Resolver List, clause 13, signed by Deborah L. Pierce, February 8, 2007.

In agreeing to use the AHLA ADR Service, your client selected an appointing authority that in no way certifies or investigates representations by potential arbitrators in their resolver profile. Therefore, the claim that alleged misleading information on Mr. Kalogredis' resolver profile contributed to AHLA or the AHLA ADR Service failing to live up to its contractual obligations is completely without merit.

**2) Allegation that Mr. Kalogredis' failure to consider your client's legal and factual arguments contributed to AHLA's failure to meet its contractual obligations.**

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[1] The Arbitration Rules were last amended July 1, 2008, but the language of the rules cited in this letter were not changed in any material respect.

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In this portion of the letter, you essentially re-argue your legal theory and factual analysis in an effort to demonstrate that AHLA "breached its arbitration contract" because Mr. Kalogredis failed to "apply the law to the facts of the case."

Your argument reveals a fundamental misunderstanding of the role of the AHLA ADR Service in the arbitration process. The Arbitration Rules make clear that the AHLA ADR Service is the appointing authority for each case that comes before the Service. Pursuant to the Arbitration Rules' introduction, "[w]hen parties agree to arbitrate under these Rules, they thereby accept the terms of these Rules and authorize the Service to assist in the process of selecting an arbitrator..." *American Health Lawyers Association Alternative Dispute Resolution Service Rules of Procedure for Arbitration,* Section 1.01, A-7 (Revised July 2008).

By assisting in the process of selecting an arbitrator, the AHLA ADR Service makes no warranties about the ability of the arbitrator to weigh facts and law and certainly does not vouchsafe for the outcome of a particular proceeding. The Arbitration Rules clearly delineate the Service's lack of involvement in the substantive legal analysis of this or any other case through this broad indemnification clause:

> All parties using these Rules or the Service indemnifies, holds harmless and releases the American Health Lawyers and the Service, their directors and members of their governing boards, and their officers, employees, agents, attorneys, consultants and representatives from any and all liability to the party or to a person or entity claiming through the party by reason of or in any way related to the Service, the arbitrator, the Rules, including the applicable Code of Ethics, or of any action taken or not taken with respect thereto. *American Health Lawyers Association Alternative Dispute Resolution Service Rules of Procedure for Arbitration,* Introduction, A-6 (Revised July 2008).

Your client had ample opportunity to make her factual and legal case to the arbitrator. The arbitrator held against you, and we understand your frustration with the outcome. Your disappointment in the result or in the arbitrator's handling of the case, however, cannot be transformed into a colorable breach of contract argument against the AHLA ADR Service when the Arbitration Rules clearly delineate that the Service is an appointing authority that must be indemnified by all parties for any claims "by reason of or in any way related to ... the arbitrator." Id.

Your effort to transform a request for a dispute resolver list into a breach of contract claim against the AHLA ADR Service also lacks merit. You paid a modest administrative fee for the AHLA ADR Service to facilitate your selection of an arbitrator consistent with the Service's Arbitration Rules. You paid this fee because your client signed a contract with Abington Emergency Physician Associates, P.C. on July 1, 2006 and in that agreement, your client agreed to settle "[a]ny controversy, dispute or disagreement arising out of or relating to this Agreement, or the breach thereof" by arbitration in accordance with the American Health Lawyers Association Alternative Dispute Resolution Service Rules of Procedure for Arbitration. *Physician Employment Agreement*, Section 16, p. 13 (July 1, 2006). The Arbitration Rules provide a method by

which the AHLA ADR Service facilitates the selection of an arbitrator, and the Service fulfilled its limited role as outlined in the Arbitration Rules. Your client has no breach of contract claim against the AHLA ADR Service.

3) **Allegation that the arbitrator's failures related to billing, misassessment of costs, and untimely filing of his order means that AHLA failed to certify the competence of its arbitrators adequately.**

The issues of whether the arbitrator overbilled you and misassessed costs on your motions for sanctions are once again issues between you and the arbitrator. The AHLA ADR Service facilitates your selection of an arbitrator, but is not in a position to micromanage the arbitrator's billings nor his decisions related to the allocation of costs on motions. The Arbitration Rules are clear that arbitrators, unimpeded or overseen by the Service, have complete discretion over remedies and the assessments of costs and expenses to the prevailing party. See *American Health Lawyers Association Alternative Dispute Resolution Service Rules of Procedure for Arbitration,* Rule 6.06, A-16 (Revised July 2008).

According to your letter, the arbitrator chose to issue his opinion and order forty-four (44) days after the close of the hearing, instead of the thirty (30) calendar days from the date of closing of the hearing or proceeding as required in the Arbitration Rules. See *American Health Lawyers Association Alternative Dispute Resolution Service Rules of Procedure for Arbitration,* Rule 6.04, A-15 (Revised July 2008). If true, this would be inconsistent with the Arbitration Rules, and such rules provide recourse to a party when a dispute arises among the parties concerning the mental or physical competence of the arbitrator or any similar matter in which the propriety of continued service by the arbitrator is challenged. Under Rule 7.05,

> [i]f ...the competence of the arbitrator or any similar matter in which the propriety of continued service by the arbitrator is challenged and such dispute cannot be resolved among the parties and the arbitrator, the Service, at its sole discretion, may resolve such issue, may remove the arbitrator and may make another appointment based on the parties' stated preferences with respect to any list submitted to them...". *American Health Lawyers Association Alternative Dispute Resolution Service Rules of Procedure for Arbitration,* Rule 7.05, A-18 (Revised July 2008)

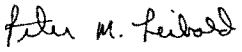
This is the only remedy that is given to the AHLA ADR Service under the Arbitration Rules if one or both parties feel that an arbitrator is unqualified or failing to abide by the Arbitration Rules. This discretionary remedy is a last resort and will only be granted if the equitable benefit to the parties outweighs the cost, expense and time of replacing the arbitrator. Since no such motion was made under Rule 7.05 and the case is completed, the issue is moot.

Finally, we note that - other than what we have already described under Rule 7.05 – there is a vehicle for seeking redress of the types of claims made in your September 8th letter, and it involves making a timely request under the Arbitration Rules to the arbitrator to

reconsider his determination under Rule 6.08, A-16 of the Arbitration Rules (Revised July 2008).

Ultimately, all of your claims against AHLA and the AHLA ADR Service hinge on a misapprehension of the services provided by the AHLA ADR Service and a misunderstanding of the relationship that exists between your client and the AHLA ADR Service. The AHLA ADR Service facilitated your selection of an arbitrator under the Arbitration Rules. It did not and does not certify its arbitrators' qualifications or his or her performance of his arbitration duties. Therefore, your disappointment in the outcome and in the arbitrator's performance simply cannot amount to any credible claim that AHLA or the AHLA ADR Service failed to live up to its obligations under the Arbitration Rules.

Sincerely,



Peter M. Leibold
EVP/CEO

cc: Vasilios J. Kalogredis, Esq.
Thomas J. Bender, Esq.
Joel Hamme, Esq.
Rita Brinley, Manager, ADR Service

**U.S. EQUAL EMPLOYMENT OPPORTUNITY COMMISSION**
**Philadelphia District Office**

801 Market St., Suite 1300
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PH: (215) 440-2602
FAX: (215) 440-2604

**Charge Number: 530-2007-01826**

Dr. Deborah Pierce
417 Militia Hill Rd.
Fort Washington, PA 10934

Charging Party,

v.

Abington Emergency Physician Associates
1200 Old York Rd.
Abington, PA 19001

Respondent.

**DETERMINATION**

Under the authority vested in me by the Commission, I issue the following determination as to the merits of the above cited charge.

Timeliness and all other jurisdictional issues for coverage have been met. Charging Party alleges that she was discriminated against based upon her sex (female) when her Employment Agreement was terminated effective June 30, 2007, in violation of Title VII of the Civil Rights Act of 1964, as amended (Title VII).

Charging Party began working for Respondent as a part-time physician in July of 2004. In July of 2005, Charging Party began to work a full-time schedule. Charging Party states that per the Employment Agreement, she was to become eligible for shareholder status on July 1, 2007. Respondent considers the following factors when determining if an associate physician is eligible for shareholder status: (1) commitment to employment; (2) ability to work harmoniously with other employees of and sources of business to the Employer; (3) likelihood of contributing in a positive way to the overall success of the Employer; and (4) compliance with the Employer's Corporate Bylaws, standards and polices.

Charging Party contends that during her employment, she successfully met each of these standards. Charging Party denies that she was ever told that her medical skills or job performance were unsatisfactory or not shareholder material. Charging Party alleges that all of

the male associate physicians who have become eligible for consideration for shareholder status have been elected to such status.

Charging Party contends that on November 9, 2006, she was informed by Dr. Kendel Kidwell (President) that the shareholders had voted not to elect her to shareholder status in the practice. Charging Party alleges that when she asked for the reasons for this decision, Dr. Kidwell refused to tell her and told her that for confidentiality reasons, he was not at liberty to provide her with any specific reasons.

In March of 2007, Respondent voted on the candidacy of a male associate physician, Dr. Michael Nelson, who had less experience. Charging Party alleges that instead of terminating his employment, Respondent extended Dr. Nelson's Employment Agreement for a probationary period of nine months. Charging Party alleges that this allowed him to improve certain areas of his performance before being reconsidered for shareholder status at the end of 2007. Charging Party was not offered any contract extensions or probationary periods prior to terminating her Employment Agreement in November 2006. Charging Party alleges that after her Employment Agreement was terminated, she was replaced by a part-time male associate physician.

Respondent claims that Charging Party was terminated for low productivity and poor interaction with her co-workers. However, Respondent failed to provide any disciplinary documentation which would show that Charging Party exhibited these deficiencies. In addition, Charging Party's evaluation dated October of 2005, indicated that she received a "satisfactory" rating in her "ability to work well with others." The evidence showed that other male associate physicians consistently had low productivity but were not discharged. Charging Party did not have the lowest productivity of the associate physicians; however, none of the male associate physicians were terminated.

The investigation further revealed that Dr. Michael Nelson was offered an additional nine month probationary period after he was initially denied shareholder status. Respondent indicates that he was not offered shareholder status at that time due to his productivity statistics and his method of providing medical services. Respondent admitted that it had no problems with the quality of care that Charging Party provided, yet she was not offered the same opportunity. Respondent contends that it was not be in the "best interest" of Charging Party or the practice to offer a probationary period because it would not resolve concerns about Charging Party's interactions with co-workers. Respondent failed to provide a substantive explanation or evidence to show why Charging Party was not offered a probationary period. Further, there is no evidence to show that Charging Party's performance deficiencies were any worse than her male counterpart. After Charging Party's Employment Contract was terminated, she was replaced by a male part-time associate physician.

Based on this analysis, I have determined that the evidence obtained during the investigation establishes violations of Title VII in that Charging Party was not afforded the same opportunity as her male counterpart to extend her contract and was instead discharged from her position.



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Upon finding that there is reason to believe that violations have occurred, the Commission attempts to eliminate the alleged unlawful practices by informal methods of conciliation. Therefore, the Commission now invites the parties to join with it in reaching a just resolution of this matter. The confidentiality provisions of the statute and Commission Regulations apply to information obtained during conciliation.

In this regard, conciliation of this matter has now begun. Please be advised that any reasonable offer to resolve this matter will be considered. The Commission can seek an amount inclusive of full backpay (total wage loss) with interest, plus compensatory and/or punitive damages, benefits and actual monetary costs incurred by the Charging Party. The attached Conciliation Agreement provides more details concerning proposed relief. Again, the Commission is postured to consider any reasonable offer during this period. If an offer has not previously been submitted, Respondent is requested to accept, reject, or submit a counteroffer to the conciliation proposal within fifteen (15) days of the date of this Determination.

If the Respondent declines to discuss settlement or when, for any other reason, a settlement acceptable to the EEOC is not obtained, the Respondent will inform the parties and advise them of the court enforcement alternatives available to aggrieved persons and the Commission.

On Behalf of the Commission,

August 16, 2007
Date

William S. Cash
for Marie M. Tomasso
District Director

cc: Jacqueline Woolley, Esq. (for Charging Party)
Christina Winston, Esq. (for Respondent)



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**U.S. EQUAL EMPLOYMENT OPPORTUNITY COMMISSION**
**Philadelphia District Office**

21 South 5th Street, Suite 400
Philadelphia, PA 19106-2515
(215) 440-2600
TTY (215) 440-2610
FAX (215) 440-2604, 2632 & 2805

**CONCILIATION AGREEMENT**

In the Matter of:

U. S. EQUAL EMPLOYMENT OPPORTUNITY COMMISSION

and

DR. DEBORAH PIERCE
Charging Party

and

ABINGTON EMERGENCY PHYSICIAN ASSOCIATES, PC

Respondent

Charge Number 530-2007-01826

*****

A charge having been filed under Title VII of the Civil Rights Act of 1964 (Title VII), as and the U.S. Equal Employment Opportunity Commission (EEOC), by the Charging Party against the Respondent, the charge having been investigated and reasonable cause having been found, the parties do resolve and conciliate this matter as follows:

## I. GENERAL PROVISIONS

1. EEOC May Review Compliance With Agreement - The Respondent agrees that the EEOC, on request of any Charging Party or on its own motion, may review compliance with this Agreement. As a part of such review the EEOC may require written reports concerning compliance, may inspect the premises, examine witnesses and examine and copy documents.

2. Agreement Does Not Constitute Admission of Violation - It is understood that this Agreement does not constitute an admission by any Respondent of any violation of any statute administered by the EEOC.

3. Charging Party's Covenant Not to Sue - The Charging Party hereby waives, releases and covenants not to sue Respondent with respect to the matters which were alleged in this charge on file with the EEOC, subject to performance by the Respondent of the promises and representations contained herein. The EEOC shall determine whether the Respondent has complied with the terms of this Agreement.

4. All Employment Practices are to be Conducted in a Non-Discriminatory Manner - All hiring, promotion practices, and other terms and conditions of employment shall be maintained and conducted in a manner which does not discriminate on the basis of race, color, sex, religion, national origin, age or disability in violation of any statute administered by the EEOC.

5. Retaliation Prohibited - The Parties agree that there shall be no discrimination or retaliation of any kind against any person because of opposition to any practice declared unlawful under any statute administered by the EEOC or because of the filing of a charge; giving of testimony or assistance or participation in any manner in any investigation, proceeding or hearing under any statute administered by the EEOC.

6. Reporting Provisions - The Respondent agrees to retain the records and to provide the written reports under the subsequent section of this Agreement entitled "Reporting Provisions." Reports will be furnished to the Office of the EEOC which has signified final approval of this Agreement.

7. Enforcement of Agreement - The parties agree that this Agreement may be specifically enforced in court and may be used as evidence in a subsequent proceeding in which any of the parties allege a breach of this Agreement.

8. Impact Upon EEOC's Processing - EEOC agrees not to use the subject charge as the jurisdictional basis for a civil action under the ADA, but does not waive or in any manner limit its right to process or seek relief in any other charge or investigation including, but not limited to, a charge filed by a member of the Commission against the Respondent.

## II RELIEF

1. Compensatory (Nonpecuniary) and Punitive Losses or Damages - [To Be Determined]

2. Retaliation Prohibited - Respondent agrees to refrain from retaliation of any kind against Charging Party because of her opposition to any practice declared unlawful under ADA or Title VII, or because of the filing of a charge; giving of testimony or assistance; or participation in any manner in any investigation, proceeding or hearing under Title VII or ADEA.

3. Notice Requirement - The Respondent agrees to sign, circulate to its employees and conspicuously post an Anti-Discrimination Policy in both English and Spanish languages. Respondent will post copies of the Anti-Discrimination Policy on all employee bulletin boards for a period of six (6) months from the date of receipt of the signed agreement.

4. Training Requirements - The Respondent agrees to provide, at its own expense, eight hours of EEOC Technical Assistance Training to its managers and supervisors regarding their obligations under and provisions of Title VII and the ADEA.

## III REPORTING PROVISIONS

The Respondent agrees to provide written notice to this office within thirty (30) days of satisfying each obligations under the ADA.

## SIGNATURES

I have read the foregoing Conciliation Agreement and accept and agree to the provisions contained therein:

| | |
|---|---|
| Date | For Respondent |
| Date | Deborah Pierce<br>Charging Party |

Approved on behalf of the Commission:

| | |
|---|---|
| Date | Marie M. Tomasso<br>District Director |

WILLIAMS & SANTONI LLP
Attorneys at Law

Joseph T. Williams
Jane Santoni
M. Bradley Hallwig, Of Counsel
Kathleen S. Skullney, Of Counsel
Silbiger &Coleman, Of Counsel

October 14, 2011

***Via electronic mail: peach_soltis@franken.senate.gov***

Senator Al Franken
United States Senate
309 Hart Office Building
Washington DC 20510

**Re: Arbitration Fairness Act**

Dear Senator Franken,

I am writing to support the above bill and to give my reasons why.

I am an attorney and been practicing consumer protection law since 2002. Every day since then I hear tragic stories of people getting ripped off by unscrupulous businesses. I have represented people who have lost homes, cars, bank accounts, and suffered great harm and indignity as a result. I am one of about 10 lawyers in my entire state of Maryland doing this type of work privately, and if there is a question that my motives are driven by greed, I would be happy to compare my income to that of the lobbyists who oppose this bill.

Perhaps you are aware that the founders of this country had 27 grievances against King George stated in the Declaration of Independence. One of those 27 was for "depriving us in many cases, of the benefits of Trial by Jury." The founders of this country thought this right was so important that it is contained in two Amendments in the Bill of Rights of the Constitution – Six and Seven. The right to free speech did not even get its own Amendment – it had to share!!

Amendment Seven states, "In Suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury, shall be otherwise re-examined in any Court of the United States, than according to the rules of the common law."

Whenever I file a consumer protection suit and ask for a jury trial, I am met with a Motion to Stay or Dismiss based on an arbitration clause, which is now contained in just about any consumer contract – cell phones, car sales, new home purchases, credit card agreements, even my daughter's field hockey camp. People cannot purchase these goods or services without being forced to waive

Williams & Santoni, LLP • 401 Washington Avenue, Suite 200 • Towson, Maryland 21204
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their constitutional rights and, as you know, the courts are upholding these contracts.

Currently, I have the following cases in my office which are being stalled (sometimes for years) because of requests for arbitration. To illustrate the extent of the problem, these are all cases where we believe the arbitration clause does not even apply. The mere existence of an arbitration clause is delaying and depriving my clients of their constitutional right:

1. *Noohi v. Toll Bros,* United States District Court, District of Maryland, action number 1:11-cv-585-RDB. This is a class action suit against Toll Bros, Inc. We allege in the suit that monies were taken for down payments (in our clients' case, in excess of $77,000) and not returned when financing was not obtained. No construction was begun. The case was filed on March 3, 2011 and a Motion to Dismiss based on arbitration is still pending.

2. *Biddy v. Klein*, Circuit Court of Maryland for Baltimore City, case number 24-C-10-007454. This is a suit by 18 homeowners in Baltimore City who claim they were sold new homes with defective HVAC systems, resulting in temperature differences of 20 degrees or more. The case was filed on November 10, 2010, but a petition to stay based on an arbitration clause has been filed and the case may be removed from the jury.

3. *Carter v. Car Center*, United States District Court, District of Maryland, action number 11-cv-01081-RWT. This is a suit filed on April 26, 2011 claiming unfair and deceptive trade practices when Mr. Carter purchased and financed a car but was told approximately two months after sale that the contracted for financing did not materialize. He was forced to return the car. An arbitration request was filed, and the case is at a standstill.

4. *Bratcher v. Deer Park Automotive*, Circuit Court of Maryland for Baltimore County, case number 03-C-11-006043. This suit was filed on June 15, 2011 and the allegations are that the dealership sold Ms. Bratcher a car with an undisclosed bent impact bar and which was a prior short term rental. A Motion to Stay based on arbitration clause was filed on August 11, 2011 and the case is at a standstill.

5. *Ricks v. Wilson Powell Lincoln-Mercury*, Circuit Court of Maryland for Prince George's County, case number CAL 10-23033. This suit was filed on July 14, 2010 alleging that Mr. Ricks was sold a vehicle and signed a financing contract. When the dealer did not obtain the contracted for financing it demanded return of the vehicle and, using a police officer moonlighting for the dealership, threatened criminal arrest. Although the trial court denied the dealership's Petition to Compel Arbitration, appeals have been filed and the case has been at a standstill for about one and a half years.

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Please contact me if you would like more details on these or any other cases I may have regarding arbitration. Thank you for your consideration and hard work protecting Americans' constitutional rights!

Very truly yours,

Jane Santoni

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Testimony of

VICTOR E. SCHWARTZ

Partner, Shook Hardy & Bacon, L.L.P.

On behalf of
The U.S. Chamber of Commerce and the U.S. Chamber
Institute for Legal Reform

Before the
U.S. SENATE COMMITTEE ON THE JUDICIARY

Hearing on
"Arbitration: Is It Fair When Forced?"

Dirksen Senate Office Building, Room 226
October 13, 2011
2:00PM

Submitted by:
Victor E. Schwartz, Esq.
Shook, Hardy & Bacon, LLP
1155 F Street, NW – Suite 200
Washington, D.C. 20004
Phone: 202-783-8400
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**TESTIMONY OF VICTOR E. SCHWARTZ**
**BEFORE THE**
**U.S. SENATE COMMITTEE ON THE JUDICIARY**

**Hearing on**
**"Arbitration: Is It Fair When Forced?"**

**October 13, 2011**

Chairman Franken, Ranking Member Cornyn, and Members of this distinguished Committee, thank you for your most gracious invitation for me to testify today about pre-dispute arbitration agreements.

By way of background, for over 40 years, I have worked in and with our litigation system. I was privileged to do plaintiffs' work for over a decade and defense work for over 25 years. I have been a law professor and am co-author of the most widely used torts casebook in the United States, *Prosser, Wade & Schwartz's Torts, Cases and Materials*. Its 12th edition was published last year. I have also served as dean of the University of Cincinnati College of Law and have been an active member of the American Law Institute, serving as an Advisor for the *Restatement of Torts, Third* project. Currently, I am a partner at the law firm of Shook Hardy & Bacon, LLP and chair the firm's Public Policy Group.

Today, I have the honor of testifying on behalf of the U.S. Chamber Institute for Legal Reform and the U.S. Chamber of Commerce. The U.S. Chamber Institute for Legal Reform (ILR) is an affiliate of the U.S. Chamber of Commerce dedicated to making our nation's legal system simpler, fairer and faster for everyone. Founded by the Chamber in 1998 to address the country's litigation explosion, ILR is the only national legal reform advocate to approach reform comprehensively, by working to improve not only the law, but also the legal climate. The U.S. Chamber of Commerce is the world's largest business federation, representing the interests of



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more than three million businesses and organizations of every size, sector and region. As has been true each time I have testified before this distinguished Committee, my views are my own.

* * *

The wisest minister I have ever known, Albert Sikkelee, once said in a sermon, "something not placed in context is pretext." While Reverend Sikkelee was speaking of selective uses of portions of the *Bible*, his words ring true with respect to the topic we are discussing today, namely, pre-dispute arbitration agreements. To evaluate them properly, they must be placed in context of our total litigation system.

Consumer Contracts Are Voluntary Contracts

Mr. Chairman, I realize that some call these agreements "mandatory" or "forced." I also appreciate that this is your sincere view. But, as learned Professor Stephen Ware of the University of Kansas School of Law and other scholars have observed, no one forces an individual to sign a contract.[1] In this country, we have choices. It is true that in some industries pre-dispute arbitration agreements are widespread, but still one does not have to sign them. If an individual wants to purchase a particular product or service from a particular provider or seller, for example a Sprint cell phone, they can choose whether the benefits outweigh having to arbitrate their claim should a problem arise.

In our competitive world, if contractual arbitration were an anathema to millions of consumers, and there was consumer outrage about them, an enterprising business seeking a competitive advantage would simply offer a product or service without such a provision. Presumably, that entity would have to charge a premium to cover the substantial litigation costs,

[1] *See* Stephen J. Ware, *The Case for Enforcing Adhesive Arbitration Agreements – with Particular Consideration of Class Actions and Arbitration Fees*, 5 J. AM ARB. 251, 262 n.21 (2006) (citing those who make this argument).



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but if submitting to arbitration was such a vital concern in consumer decision-making, a market for non-arbitration agreements would likely develop. Alternatively, if consumers were unaware of arbitration provisions in any contract they signed, yet neglected to read carefully, greater awareness of this issue over the past decade or more – during which the use of the agreements has grown – would also give rise to such a market. Banning or otherwise limiting the use of pre-dispute arbitration clauses would ignore these market dynamics, and likely force consumers to pay more for products or services. It would also promote unsound public policy by reducing incentives for consumers to carefully read and understand the contracts they enter if they can later escape arbitration provisions.

Eliminating Pre-Dispute Arbitration Agreements Would Benefit Lawyers, Not Consumers

If pre-dispute arbitration agreements were abolished in whole or in part, the clear, unmistakable beneficiaries would be lawyers. From my experience, I can say that if there were true mandatory arbitration agreements in all aspects of life, my law firm, other defense litigation law firms, and many plaintiffs' law firms might have to consider another business or profession. The legal profession thrives on litigation, and in the absence of pre-dispute arbitration agreements, the only choice by which we have to resolve disputes would be litigation; an avenue that is both time consuming and expensive for all parties.

The costs associated with hiring a plaintiffs' lawyer on a contingency fee basis plus expenses can run upwards of fifty percent of the ultimate recovery, sometimes even more. In this regard, it is not surprising that the American Association for Justice (formerly the Association of Trial Lawyers of America) reports significant lobbying in an effort to outlaw pre-dispute arbitration agreements. But plaintiffs' lawyers are not alone in making money when people litigate disputes. Defense firms charge by the hour and these transaction costs can be



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extraordinarily high as well. There are also significant court costs adding to these already high priced litigations, not to mention expenditures of scarce judicial resources. Taken together, these high transaction costs benefit attorneys, but can leave many consumers with comparatively little after years of litigation. As Judge Learned Hand once observed, "short of disease, a lawsuit is a person's worst nightmare." Arbitration, in comparison, often significantly reduces these transaction costs.

If pre-dispute arbitration agreements were abolished, in whole or part, some believe that it would open the portals for an attractive path of righting wrongs, namely class actions. But class actions are not ideal. Most importantly, the vast majority of consumer claims are individualized, for example, a dispute about an overcharge on one person's bill or a product that is a lemon. Class actions are of no help in these circumstances.

Even in the rare situation when a dispute is amenable to class action treatment, the device has many shortcomings and can adversely affect people who feel they have been victimized. Often, consumers will have to submit complex claims forms to obtain recovery. But few individuals understand how to fill them out, and even fewer bother to do so. Sometimes, and there are numerous examples where this is the case, consumers become victims of the lawyer-tilted class action system and actually receive no direct benefit from consumer class actions.

In a recent Ninth Circuit case, class action lawyers representing customers who owned "Bluetooth" headsets claimed that manufacturers committed fraud when they failed to give prominent warnings indicating that listening to the headsets continually at loud volumes might cause hearing damage.[2] The potential litigation costs prompted the defendant to settle the class action. What did the settlement involve? Over $100,000 was to be given to a hearing loss

[2] *See In Re Bluetooth Prod. Liab. Litig.*, No. 09–56683, 2011 WL 3632604 (9th Cir. Aug. 19, 2011) (holding trial court abused its discretion in approving settlement and fee agreement).



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charity. The plaintiffs' lawyers in the case were to receive $850,000 in fees. The people who claimed the hearing loss – a physical injury – were set to receive virtually nothing from the settlement.

A group called The Center for Class Action Fairness intervened in the case and successfully argued before the Ninth Circuit that the lower court should review its approval of this valueless class action settlement. The case was remanded, providing a modest potential victory for the plaintiffs, but after years of litigation the customers still have recovered nothing. This is just one recent example. There are numerous other examples of multi-million dollar class actions where consumers get little or nothing and attorneys are well paid.[3]

The "Bluetooth" case and others illustrate that there are serious concerns with how class actions function in this country. Does that mean that every consumer class action is totally unsound? No. But the notion that they are a panacea, or even that they are more often beneficial than not, is belied by the evidence. I simply mention the case because it shows the fallacy of judging any dispute resolution system by one or two poster person cases where a victim can tell a potentially compelling story.

Contractual Pre-Dispute Arbitration Provides Important Benefits from Consumers' Perspective

In comparison to the litigation system, pre-dispute arbitration agreements can, and routinely do, benefit consumers who bring a claim in terms of affordability, timeliness, accessibility, and clarity and flexibility with respect to the process.

[3] *See, e.g.*, Steven B. Hantler & Robert E. Norton, *Coupon Settlements: The Emperor's Clothes of Class Actions*, 18 GEO. J. LEGAL ETHICS 1343, 1344 (2005).



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Data, as set forth in articles by my fellow witness, Christopher Drahozal,[4] and studies by Professor Stephen Ware[5] and Professor Peter Rutledge,[6] show that contractual pre-dispute arbitration is usually both more affordable and efficient for consumers than full-scale litigation. These studies reflect my own experience. For over four decades, I have seen that making claims in courts can be very costly. Years can go by before there is any result. Even with regard to the most modest disputes made in small claims courts, claimants can experience substantial delays, particularly in light of shrinking court budgets in many states.[7] Arbitration offers lower transaction costs through simplified procedures and less attorney involvement, and improved timeliness by not having to wait to have a claim adjudicated in an ever increasingly overcrowded court system.

Contractual pre-dispute arbitration also provides greater accessibility for many consumers or employees to have their claims adjudicated. In many instances, the litigation system may not be accessible to these individuals. Plaintiffs' lawyers properly operate in a for-profit industry; they will typically only take cases where they believe they have a substantial likelihood of success and where the economic value of the case will justify their time investment. Prominent plaintiffs' lawyer, Kenneth Connor, was most honest when he said "from an economic feasibility standpoint [I] cannot handle the case that is not likely to deal back a

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[4] *See* Christopher R. Drahozal, *An Empirical Study of AAA Consumer Arbitrations*, 25 OHIO ST. J. ON DISP. RESOL. 843 (2010).

[5] *See* Stephen J. Ware, Testimony before the House of Representatives Judiciary Subcommittee on Commercial and Administrative Law (September 15, 2009), *available at* 2009 WL 2942430.

[6] *See* Peter B. Rutledge, *Who can be Against Fairness? The Case Against the Arbitration Fairness Act*, 9 CARDOZO J. CONFL. RESOL. 267 (2008).

[7] *See, e.g., Budget Cuts Have Widespread Impact on NY State Courts Report*, Reuters, Aug. 16, 2011, *available at* http://newsandinsight.thomsonreuters.com/Legal/News/2011/08_-_August/Budget_cuts_have__widespread__impact_on_NY_state_courts-report/.



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return."[8] Some studies show that most lawyers will not take a case unless the plaintiff's claim is worth at least $60,000.[9] Most consumer claims are of relatively modest value and, therefore, unlikely to motivate a plaintiff's lawyer to get involved. Similarly, a recent study concluded that only about 5% of employees who contend they were discriminated against can access the litigation system given its economic realities; for them, "it looks like arbitration – or nothing."[10]

Contractual pre-dispute arbitration, when contrasted with the litigation system, is also more simple, clear, and flexible from the point of view of the consumer. In arbitration, consumers can often submit and respond to claims using their own words. They are not bound by the formalities of the legal proceedings that take some individuals three years or more of law school to learn. In addition, consumers in arbitration can appear in person, or if they prefer by telephone, or by simply submitting documents. Some arbitration providers are even moving towards online claims resolution. Litigation, in contrast, generally requires the claimant to take time away from work, family, or other activities, causing great inconvenience.

Arbitration Produces Equally Valid and Just Results Compared with the Litigation System

A core argument of opponents of contractual pre-dispute arbitration is that it unfairly "stacks the deck" against the consumer or an employee. It has been argued that because pre-dispute arbitration clauses sometimes permit businesses to select the organization that will administer the arbitration, a powerful incentive is created for that organization's arbitrator to

[8] Hearing on H.R. 6126, the "Fairness in Nursing Home Arbitration Act of 2008" before House of Representatives Judiciary Subcommittee on Commerce and Administrative Law, 110th Congress (2008) (statement of Kenneth Connor).

[9] *See, e.g.*, Elizabeth Hill, *AAA Employment Arbitration: A Fair Forum at Low Cost*, 58 DISP. RESOL. J. May-Jul. 2003, at 8, 10-11.

[10] *See* Theodore St. Antoine, *Mandatory Arbitration: Why It's Better Than It Looks*, 41 U. MICH. J.L. REFORM 783, 792 (2008).



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unjustly favor the defendant in order to secure future business. This argument is unsound for several reasons.

First, while an arbitration agreement may designate a service provider, both parties will typically have a role in selecting the individual arbitrator who will conduct the dispute. Moreover, arbitration service providers such as the American Arbitration Association (AAA) have conflict-of-interest rules that provide for the disqualification of any arbitrator who may have an interest in the outcome of the dispute.[11]

Second, it is important to remember, and not gloss over the fact, that arbitrators such as those in the AAA and other organizations are professionals. They are independent legal experts who abide by a comprehensive set of rules and procedures, and take an oath to render objective decisions, not unlike a judge or other court officer. Many arbitrators are, in fact, former judges. Accordingly, it is not surprising that no broad-based objective study supports the accusation that the average arbitrator is unable or unwilling to separate whatever alleged financial interests could exist and reach an unbiased, objective decision.

Third, as the writings of Professors Ware, Drahozal and Rutledge show, consumers often receive the same or better result in arbitration as in courts. One possible reason for this is that many arbitrators specialize in particular fields. In some instances, they may possess greater subject matter knowledge than a judge in a court of general jurisdiction.

Witnesses in this hearing will likely differ on this key point and cite reports that suggest consumers perform worse in arbitration. It is important to put such studies in context. There is an inherent selection difference between the types of cases that proceed to arbitration and those that proceed in the court system; they are apples and oranges. Common sense tells us that given

[11] *See, e.g.*, American Arbitration Association, *Commercial Arbitration Rules and Mediation Procedures* R-17, *available at* http://www.adr.org/sp.asp?id=22440#R17.



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the higher costs of the court system, claimants are more likely to take on the burdens of litigation when they believe their claim is particularly strong or where the amount sought is so high that it leaves no room for settlement; these considerations function to weed out plaintiffs with weaker claims. Arbitrators, in comparison, generally decide the sound claims along with the weak and meritless ones. Thus, it would not be surprising to find that businesses prevail more often in arbitration. That said, the weight of the empirical studies still show that individuals fare just as well in arbitration as in court.

Finally, from a business point of view, the premise that a business would wish to place its customers into a forum where there is no fair chance to have cases properly heard is deeply flawed. Stated plainly, businesses want repeat customers. They often make accommodations for consumers when under no obligation to do so. For example, if one takes a product back to a store, that business will often take the product back even though they may not be fully, or actually, responsible for a product's damage or defect. And for the same reason, the alternative dispute resolution systems that businesses offer to their customers are aimed at ensuring that customers are satisfied that they receive a fair shake. Whereas the burdens and shortcomings of the litigation system make it more likely that businesses will lose customers due to acrimony, arbitration is more likely to lead to a prompt settlement that satisfies both sides and makes it more likely that a customer will continue to do business with the company.

Other Misconceptions About Contractual Pre-Dispute Arbitration

Another commonly employed argument against pre-dispute arbitration provisions is that they disadvantage consumers and employees because these groups have no bargaining power or have unequal bargaining power. This argument adds that these arbitration clauses are often buried in the "fine print" or are in contracts written in "legalese," leaving many consumers or



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employees unaware that these provisions even exist. But, here is the key point mentioned in the beginning of my testimony. Consumers and employees voluntarily enter these contracts. It may seem extraterrestrial, but I have lived in a world where people did not have cell phones or the gadgetry we see in our daily lives. Folks did survive. If consumers balked at these agreements and refused to buy products or services unless they could litigate disputes, it is my belief that at least one or more companies would offer a non-arbitration alternative; in fact in many industries where arbitration is used, some non-arbitration alternatives exist. The argument that consumers lack bargaining power is a fallacy; consumers gain more bargaining power everyday through increased competition and more avenues, such as on the Internet, to rate products and services.

This same rationale also rebuts another commonly asserted argument that contractual pre-dispute arbitration creates incentives for businesses to engage in predatory practices. First, as previously explained, customers do as well, if not better, in arbitration than they do in court. Second, existing law prevents businesses from drafting arbitration agreements that tilt the playing field in their direction. Both state and federal courts routinely exercise authority under Section 2 of the Federal Arbitration Act to invalidate arbitration provisions that are unfair to consumers or employees. Examples include provisions imposing on consumers high or inappropriate costs, burdensome travel, or punitive damage limits. Third, businesses face multiple layers of government oversight. Businesses that sell to consumers are generally regulated by at least the Federal Trade Commission and one other federal agency, as well as all 50 state attorneys general and a myriad of state agencies and commissions. These agencies and offices routinely pursue allegations of wrongdoing, especially the use of unfair and deceptive practices. Hence, there already exists multiple "checks" on the scope and limits of arbitration agreements.



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A final misconception about contractual pre-dispute arbitration is that by eliminating such agreements a robust market for post-dispute arbitration of claims would develop that would better serve consumers. A basic understanding of litigation dynamics demonstrates why this would not be the case. In the absence of contractual pre-dispute arbitration, plaintiffs would presumably be permitted to contract with defendants to have their dispute arbitrated. Under this scenario, claimants with very modest (low dollar amount) claims would likely prefer arbitration because it is less expensive than the court system; however, most defendants would likely prefer to litigate in the court system because the higher transaction costs serve to both weed out the more speculative claims and provide the defendant with greater settlement leverage. The result? The parties would be unlikely to agree to arbitration. The same outcome would also occur when the roles are reversed and the plaintiff has a relatively high dollar amount claim. Here, the defendant would likely prefer arbitration to minimize costs, but the plaintiff would want to proceed in the court system to either increase settlement leverage or potentially obtain a substantial jury award. The result in either case is that the litigation adversaries would be unlikely to agree to the others' preferred means of dispute resolution. This is precisely why the availability of pre-dispute arbitration is so important and desirable; it establishes up-front how a claim will be adjudicated.

Conclusion

Everyone knows the universal truth; nothing is perfect. Contractual pre-dispute arbitration is not perfect, but I can assure this Committee that the litigation system is not perfect either. My life has taught me that common sense is a good guide. If the concerns put forth by those who oppose pre-dispute arbitration agreements were universal, those concerns would be on the front page of every paper in America. That has not occurred. We see much more in the



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media about the pitfalls of litigation. For instance, as the *New York Times* recently observed, "[s]tate courts, which handle the vast majority of civil and criminal cases, are in a state of crisis."[12] Today, these courts are "less and less able to deliver justice."[13] Contractual pre-dispute arbitration and our class action and individual litigation systems can both be improved, but abolition of contractual pre-dispute arbitration is not the answer.

Thank you for the opportunity to testify today and I look forward to your questions.

[12] Editorial, "Thread Bare American Justice", N.Y. Times, August 18, 2011, at A20.
[13] *Id.*



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***Testimony***
***Of***
***Lori Swanson***
***Minnesota Attorney General***

***United States Judiciary Committee***
***October 13, 2011***
***226 Dirksen Senate Office Building***
***2:00 p.m.***

***"Arbitration: Is It Fair When Forced?"***



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Good afternoon. Thank you for the opportunity to testify before the United States Senate Judiciary Committee on the topic of mandatory arbitration of consumer disputes.

**I. Arbitration of Consumer Disputes.**

The Federal Arbitration Act--passed in 1925--was originally designed to facilitate merchants of relatively equal bargaining power to agree to arbitration after a dispute arose and to mutually select an arbitrator to resolve the dispute. In recent years, however, companies expanded arbitration to a wide range of consumer contracts where the consumer has little bargaining power.

The right to have disputes resolved through an impartial judge or jury is deeply imbedded in our democracy and our values. In recent years, however, American consumers--in one contract or another--have given up the right to have their day in court through language contained in the "fine print" of consumer agreements. Large corporations often include--in the fine print of their consumer contracts--pre-dispute arbitration clauses, in which the consumer may be required to waive--in advance--his or her right to have a dispute resolved in court. Instead, the consumer may be required to resolve the dispute through arbitration. This language is generally binding on the consumer even if he or she does not notice the arbitration clause.

**II. National Arbitration Forum Lawsuit and Consent Judgment.**

In 2009, the Minnesota Attorney General's Office filed a lawsuit against the National Arbitration Forum--the then-largest arbitration company in the country for consumer credit disputes--alleging that it misrepresented its independence and hid from consumers and the public its extensive ties to the collection industry.



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The lawsuit alleged that the National Arbitration Forum deceptively represented to consumers and the public that it was independent and neutral, operated like an impartial court system, was not affiliated with any party, and did not take sides between parties.

The lawsuit alleged that the Forum worked behind the scenes--alongside creditors and against the interest of ordinary consumers--to convince credit card companies and other creditors to deprive consumers of their legal rights by inserting arbitration provisions in their customer agreements and then to appoint the Forum to decide the disputes. The lawsuit alleged that the Forum paid commissions to executives to convince creditors to put mandatory arbitration clauses in their customer agreements and to thereafter convince creditors to use the Forum to decide those claims, in order to generate arbitration filings in the Forum--and hence, revenue--for itself. In soliciting creditors to use its arbitration services, the Forum made representations that aligned itself against consumers, such as that "[t]he customer does not know what to expect from Arbitration and is more willing to pay," that consumers "ask you to explain what Arbitration is then basically hand you the money," and that "[y]ou [the creditor] have all the leverage [in arbitration] and the customer really has little choice but to take care of this account."

The lawsuit also alleged that the Forum had financial ties to the collection industry. Beginning in 2006 and through 2007, Accretive--a family of New York private equity funds--engineered two transactions. In the first transaction, Accretive formed several equity funds under the name "Agora" (meaning "Forum" in Greek), which invested $42 million in the Forum and obtained governance rights in it. In the second transaction, three of the country's then-largest debt collection law firms--Mann Bracken of Georgia, Wolpoff & Abramson of Maryland, and Eskanos & Adler of California--merged into one large national law firm called Mann Bracken. Accretive then acquired the majority interest in a debt collection agency called Axiant,



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which acquired the collections operations of Mann Bracken. Through these transactions, Accretive took control of one of the country's largest debt collection enterprises and became affiliated with the Forum, the country's largest consumer collection arbitration company. The lawsuit alleged that, in 2006, the Forum processed just over 214,000 consumer collection arbitration claims, of which 125,000, or nearly 60 percent, were filed by these firms.

In the course of our year-long investigation, we heard from arbitrators who were "deselected"--or not given more cases--after ruling for the consumer or not awarding the credit card company any attorneys' fees. We heard from employees who were told to find arbitrators who were anti-consumer and not to assign additional cases to arbitrators who asked the creditors to provide evidence to support their claims. We also interviewed over 100 consumers who were confused by the process, were unaware they had agreed to arbitration, and did not feel they got a fair shake in arbitration.

The company signed a Consent Judgment to resolve the lawsuit. Under the Consent Judgment, the company is barred from the business of arbitrating credit card and other consumer disputes and must stop accepting new consumer arbitrations or in any manner participating in the processing or administering of new consumer arbitrations, such as arbitrations involving consumer debt, including credit cards, consumer loans, telecommunications, utilities, health care, and consumer leases.

**III. Problems with Mandatory Arbitration in Consumer Contracts.**

Our investigation of the Forum and interviews of consumers highlighted underlying problems with the arbitration of consumer disputes arising out of mandatory arbitration clauses in fine-print consumer contracts:



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First, there is unequal bargaining power between consumers and large corporations, which often present consumers with "take it or leave it" fine print contracts. In almost every interview we conducted of consumers during our investigation of the Forum, we found that the consumer was not aware of the arbitration provision, in most cases never saw the provision, and was given virtually no opportunity to negotiate or reject the provision. Yet, through these provisions, consumers gave up their right to have their day in court.

Second, it was apparent from interviews with consumers, arbitrators, and employees of the Forum that arbitrators have a powerful incentive to favor the dominant party in an arbitration; namely, the corporation. There is a term commonly used in the arbitration industry called "repeat player bias," describing the phenomena where an arbitrator is more likely to favor the party that is likely to send future cases. Corporations, and not consumers, generally select which arbitration companies they will appoint to process disputes, and arbitration companies compete for this business. If a particular corporation selects a particular arbitration company to resolve disputes, that arbitration company makes money. If a particular arbitration company is not "friendly" enough to the corporation, the corporation can select another arbitration company to resolve its claims. Similarly, the arbitration company wields great power in selecting which arbitrators will be in its network. In the case of the Forum, arbitrators and employees told us that arbitrators who issued an award against the corporation, or who failed to award attorneys' fees against the consumer, were sometimes "deselected" and not appointed to future proceedings. This bias does not exist in a court, where the judge is not reliant on a dominant player for his or her future income.

Third, during our investigation of the Forum, we were told by consumers that because they were unaware of the arbitration provision, they often did not recognize the significance of



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the arbitration notice serviced on them. In other words, since they did not know that they agreed to arbitration, and were unfamiliar with the arbitration process or the arbitration administrator, consumers told us they did not know they were obligated to respond to the arbitration notice. As noted above, the Forum's own documents describe it this way: "[t]he customer does not know what to expect from Arbitration and is more willing to pay," and consumers "ask you to explain what Arbitration is then basically hand you the money."

Fourth, the due process protections found in court may be lacking in arbitration. For instance, consumers subject to a mandatory arbitration clause generally have no right to appeal in most cases to a judge if there is an adverse arbitration ruling. Similarly, the arbitrator's decision may not be supported by a written order, so the consumer may not understand the basis for the decision and therefore may question the integrity of the process.

**IV. Conclusion.**

In short, while our Consent Judgment with the National Arbitration Forum may have removed a problem company from the consumer arbitration marketplace, it did not and cannot solve the systemic problems with mandatory pre-dispute arbitration clauses in fine-print consumer contracts. The Federal Arbitration Act has been interpreted by the federal courts to prohibit state legislatures from meaningfully regulating these clauses. Therefore, Congress is the only legislative body that can protect consumers from the unfairness that may arise from the use of mandatory arbitration clauses in consumer contracts.

Thank you for inviting me to this hearing.



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Dear Members of the Judiciary Committee,

Arbitration probably began as a noble concept to speed the process of justice up if both parties were willing to forgo the court system. The key term here is willing. About 20 years ago contract poultry producers were issued new contracts with a little known term in rural America known as the mandatory arbitration clause. This arose due to the fact that many of the large poultry companies were losing contract disputes and this was the quick fix to be inoculated from our court system.

Mandatory arbitration is commercial justice, plain and simple. It is set up to favor corporations by eliminating the rights of individuals or small businesses to access the court system. If arbitration was the best way to settle a dispute it would never be made mandatory, both parties would enter into it voluntarily.

When there is an imbalance of power between the two principals entering into a contract as there is in contract poultry farming, the less powerful, i.e. the farmer, will sign his rights away in order to keep a contract and avoid total financial ruin. Arbitration is a cost prohibitive, lawless process that is only understood by a handful that has none of the rules of basic justice. Even if a farmer knew this, not much thought is put into the process of dispute resolution when the contract is "take it or leave it". Or in other words, agree to all terms or go bankrupt.

This is my twentieth year in contract poultry and I know of no examples of anyone ever taking a dispute to the "court of arbitration". For a farmer it is just too expensive, the total reward may not even cover the arbitrators fees (as some arbitrators can make as much as $10,000 per day). But in the 2008 Farm Bill, Congress recognized how unconscionable these mandatory arbitration clauses were in our contracts and it resulted in allowing the farmer to choose to keep or opt out of mandatory arbitration when entering any new, modified or amended contract. It has not led to a wave of lawsuits as many had said it would but I do believe it is an incentive to do business above board.

Too many people have lost their lives defending the rights of Americans to use the court system our democracy provides. The sacrifices of these folks will be in vain if in a free land we allow the use of mandatory arbitration as a stipulation in any contract.

Sincerely,

Craig Watts
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