Testimony of

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before the

Subcommittee on Commercial and Administrative Law

of the

House Judiciary Committee

"Mandatory Binding Arbitration Agreements: Are They Fair for Consumers?"

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I appreciate the opportunity to participate in this hearing concerning the fairness of mandatory consumer arbitration agreements. The topic is important to millions of businesses and employers nationwide and to their customers and employees.

By way of background, I am a partner in the law firm of Ballard Spahr Andrews & Ingersoll, LLP in the firm's Philadelphia office. I obtained a B.A. and M.A. at New York University; a Ph.D. in English Literature at the University of Pennsylvania; and my J.D. at Villanova University. Following law school I clerked for the Honorable John Biggs of the United States Court of Appeals for the Third Circuit. I have practiced law for 30 years and for the past 11 years I have been extensively involved along with other partners in my firm with the drafting and enforcement of arbitration clauses in consumer contracts such as credit card and other loan agreements.

I have been counsel in numerous significant consumer arbitration actions in the United States Supreme Court and other federal and state appellate and trial courts throughout the

country.[1] I am often retained by national and state trade associations to submit amicus briefs in important consumer arbitration cases.[2] In addition, I have co-authored more than a dozen scholarly articles dealing with various consumer arbitration issues.[3] I have also served as an instructor in several continuing education seminars involving consumer arbitration. I am here today to provide my own views on the subject of consumer arbitration, and my law firm and I are not being compensated in any fashion for my testimony. Accordingly, my opinions do not necessarily reflect the opinions of any of my firm's clients.

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1 See, e.g., Green Tree Fin. Corp. v. Bazzle, 539 U.S. 444 (2003); Baron v. Best Buy Co., Inc., 260 F.3d 625 (11th Cir. 2001); Cappalli v. National Bank of the Great Lakes, 281 F.3d 219 (3d Cir. 2001); Providian Fin. Corp. v. Coleman, No. 02-60943 (5th Cir. May 21, 2003) (per curiam); Jenkins v. First American Cash Advance of Georgia, Inc., 400 F.3d 868 (11th Cir. 2005), cert. denied, 126 S. Ct. 1457 (2006); Kaneff v. Delaware Title Loans, Inc., No. 06-4703 (E.D. Pa. March 6, 2006); Shales v. Discover Card Services, Inc., Civil Action No. 02-80, 2002 WL 2022596 (E.D. La. Aug. 30, 2002); Perrone v. Household Bank (SB), N.A., No. L20010020 (D. Mass. June 26, 2001); Kennedy v. Conseco, No. 00-CV-04399 (N.D. Ill. Jan. 11, 2001); Zawikowski v. Beneficial National Bank, No. 98 C 2178, 1999 WL 35304 (N.D. Ill. Jan. 11, 1999); Pick v. Discover Fin. Servs., Inc., 2001 U.S. Dist. LEXIS 15777 (D. Del. Sept. 28, 2001); Gipson v. Cross Country Bank, Civil Action No. 2:03cv269-A, 2005 U.S. Dist. LEXIS 1400 (M.D. Ala. Jan. 28, 2005); Schuetz v. SLM Financial Corp., No. 1:03-CV-1842 (N.D. Ga. Sept. 26, 2003); Rosen v. Saks Inc., 2003 Ill. App. LEXIS 1252 (Ct. App., 1st Dist. Oct. 8, 2003), review denied, 2004 Ill. LEXIS 142 (Ill. Jan. 28, 2004); Providian National Bank v. Screws, 2003 Ala. LEXIS 298 (Ala. Sup. Ct. Oct. 3, 2003); Tsadilas v. Providian National Bank, No. 4948N, 2004 WL 2903518 (N.Y. App. Div. Dec. 16, 2004); Christine Williams v. Direct Cable TV, et al., No. CV-97-009, 1997 WL 579156 (Henry Co. Ala. 1997); Gloria Perry v. Beneficial National Bank USA, et al., No. CV-97-218, 1998 WL 279174 (Macon Co. Ala. May 18, 1998).

2 See, e.g., Salley v. Option One Mortgage Corp., No. 50 EAP 2005, 2007 Pa. LEXIS 1195 (Pa. Supreme Court) (amicus brief filed April 12, 2006); Discover Bank v. Szetela, No. 02-829 (U.S. Supreme Court) (amicus brief filed Dec. 30, 2002).

3 See, e.g., Arbitration of Consumer Financial Services Disputes 513 (PLI 1999); 53 Bus. Law. 1075 (May 1998); 54 Bus. Law. 1405 (May 1999); 55 Bus. Law. 1427 (May 2000); 56 Bus. Law. 1219 (May 2001); 57 Bus. Law. 1287 (May 2002); 58 Bus. Law. 1289 (May 2003); 59 Bus. Law. 1265 (May 2004); 60 Bus. Law. 775 (Feb. 2005); 61 Bus. Law. 923 (Feb. 2006); 62 Bus. Law. ___ (Feb. 2007).

INTRODUCTION

Based upon my experience, I firmly believe that the system that is presently in place in connection with consumer arbitrations under the Federal Arbitration Act ("FAA"), 9 U.S.C. §§1 et seq., is working very well and, in particular, provides abundant protections to consumers who are parties to arbitration agreements with companies or employers. These protections emanate from (1) the FAA itself, (2) the companies whose contracts contain arbitration agreements, (3) the neutral third-party arbitration administrators who typically administer companies' arbitration programs and (4) the state and federal courts which rigorously enforce the FAA and applicable state laws.

My partners and I have always counseled our clients that the fundamental principle in implementing a consumer arbitration program is to be fair to consumers. Our clients uniformly follow that advice, and I believe that the vast majority of companies that have adopted consumer arbitration programs likewise follow the same standard of fairness. As a practical matter, companies have no choice but to be fair in their consumer arbitration agreements, because if they are not, the arbitration administrators will not administer their arbitrations and the courts will not enforce their arbitration agreements.

Companies and employers favor arbitration because, as the United States Supreme Court has repeatedly stated, arbitration is faster, less costly and more efficient than litigation, *not* because it provides some sort of trap for unwary consumers. In fact, the Supreme Court has emphasized that arbitration is favored in consumer disputes: "[T]he Act [FAA], by avoiding 'the delay and expense of litigation,' will appeal 'to big business and little business alike, corporate interests [and] individuals.' Indeed, arbitration's advantages often would seem helpful to individuals, say, complaining about a product, who need a less expensive alternative to litigation." Allied-Bruce Terminix Cos., Inc. v. Dobson, 513 U.S. 265, 280 (1995) (citations

omitted). Arbitration enables companies to reduce the costs of dispute resolution which, in turn, inures to the benefit of consumers.

The Supreme Court has also stated in numerous cases that an arbitration agreement is not an exculpatory clause for companies or employers. That is because by agreeing to arbitrate, "a party does not forgo ... substantive rights" but "only submits to their resolution in an arbitral, rather than a judicial, forum." Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 26 (1991); accord, Green Tree Fin. Corp.-Ala. v. Randolph, 531 U.S. at 90 ("even claims arising under a statute designed to further important social policies may be arbitrated because 'so long as the prospective litigant effectively may vindicate [his or her] statutory cause of action in the arbitral forum,' the statute serves its functions") (citation omitted).

While you may read or hear about instances where a particular arbitration agreement did not strike the proper balance between protecting the consumer's rights and the company's rights, those instances are few and far between. In the vast majority of cases the existing system works -- and works very well -- because (1) companies and employers have gone to great lengths to make their arbitration programs fair, even to the point of giving consumers the unfettered and unconditional right to reject arbitration when they enter into the transaction; (2) the leading national arbitration administrators, such as the American Arbitration Association ("AAA") and the National Arbitration Forum ("NAF"), have adopted consumer due process protocols and consumer procedures and fee schedules which ensure that the consumer will be treated fairly and that arbitration will be affordable to the consumer; and (3) the courts have rigorously struck down arbitration agreements that they have found to be overreaching, unfair or abusive to consumers, while enforcing those that are legally and equitably sound. This existing

"check and balance" system operates dynamically and very successfully within the framework of the FAA to protect the rights of all parties to the consumer arbitration agreement.

EMPIRICAL STUDIES CONFIRM THAT CONSUMER ARBITRATION IS FAIR

It is my opinion that the present system of checks and balances in the area of consumer arbitration has never been more robust or more protective of consumers' rights. But you do not have to take just my word for it. There are a considerable number of empirical studies that have documented the success that consumers and employees have had in arbitration and the satisfaction that the majority of consumers and employees have expressed in the arbitration process. Those studies (some of which are attached as exhibits) include:

i. A synopsis of independent studies and surveys concerning the benefits of pre-dispute consumer arbitration was published by the NAF in 2004. See "Effective and Affordable Access to Justice by Consumers -- Empirical Studies & Survey Results." [Attached as Exhibit A]. The results were summarized as follows:

(1) Seventy-eight percent of trial attorneys find arbitration faster than lawsuits (ABA, 2003)

(2) Eighty-six percent of trial attorneys find arbitration costs are equal to or less expensive than lawsuits (ABA, 2003)

(3) Seventy-eight percent of business attorneys find that arbitration provides faster recovery than lawsuits (Corporate Legal Times, 2004)

(4) Eighty-three percent of business attorneys find arbitration to be equally or more fair than lawsuits (Corporate Legal Times, 2004)

(5) Individuals prevail at least slightly more often in arbitration than through lawsuits (Delikat & Kleiner, 2003)

(6) Monetary relief for individuals is slightly higher in arbitration than in lawsuits (Delikat & Kleiner, 2003)

(7) Arbitration is approximately 36% faster than a lawsuit (Delikat & Kleiner, 2003)

(8) Individuals receive a greater percentage of the relief they ask for in arbitration versus lawsuits (Maltby, 1999)

(9) Ninety-three percent of consumers using arbitration find it to be fair (Perino, 2003)

(10) Consumers prevail 20% more often in arbitration than in court (Perino, 2003)

(11) In securities actions, consumers prevail in arbitration 16% more than they do in court (U.S. General Accounting Office, 1992)

(12) Sixty-four percent of American consumers would choose arbitration over a lawsuit for monetary damages (Roper Survey, 2003)

ii. In December 2004, Ernst & Young issued a study ("Outcomes of Arbitration: An Empirical Study of Consumer Lending Cases") examining the outcomes of contractual arbitration in lending-related, consumer-initiated cases. [Attached as Exhibit B]. The study, based on consumer arbitration data from January 2000 to January 2004 from the NAF, observed that:

(1) Consumers prevailed more often than businesses in cases that went to an arbitration hearing, with 55% of the cases that faced an arbitration decision being resolved in favor of the consumer. This is the exact same win-rate for consumers as exists in state court. See Contract Trials and Verdicts in Large Counties, 1996, p.5 (April, 2000), Bureau of Justice Statistics, http://www.ojp.usdoj.gov/bjs/pub/pdf/ctvlc96.pdf.

(2) Consumers obtained favorable results in 79% of the cases that were reviewed. Favorable results include results from arbitration decisions, as well as settlements satisfactory to the consumer and cases that were dismissed at the claimant's request.

(3) 40% of consumers who brought claims actually got their "day in court" to tell their stories (see p. 9 table 3, with 97 of 226 cases resulting in an arbitration decision). Compare this to the fact that only 2.8% of cases in state court ever reach trial. Examining the Work of State Courts, p. 29 (1999-2000), National Center for State Courts. http://www.ncsonline.org/D_Research/csp/1999-2000_Files/1999-2000_Tort-Contract_Section.pdf.

(4) 69% of consumers surveyed indicated that they were very satisfied with the arbitration process.

iii. In April 2005, Harris Interactive released the results of an extensive survey of arbitration participants sponsored by the Institute for Legal Reform at the U.S. Chamber of Commerce. [Attached as Exhibit C]. The survey was conducted online among 609 adults who participated in a

binding arbitration case (voluntarily, due to contract language or with strong urging by the Court, but not a court order) that reached a decision. The major findings were:

(1) Arbitration is widely seen as faster (74%), simpler (63%), and cheaper (51%) than going to court.

(2) Two-thirds (66%) of participants say they would be likely to use arbitration again with nearly half (48%) saying they are extremely likely.

a. Even among those who lost, one-third say they are at least somewhat likely to use arbitration again.

(3) Most participants are very satisfied with the arbitrator's performance, the confidentiality of the process and its length.

(4) Predictably, winners found the process and outcome very fair and the losers found the outcome much less fair. However, 40% of those who lost were moderately to highly satisfied with the fairness of the process and 21% were moderately to highly satisfied with the outcome.

(5) While one in five of the participants were required by contract to go to arbitration, the remainder were voluntary – suggested by one of the parties, one of the lawyers, or the court.

(6) Two-thirds of the participants were represented by lawyers.

iv. RoperASW, 2003 Legal Dispute Study (Apr. 2003). [Attached as Exhibit D]. The survey concluded that 64% of individuals would choose arbitration over court litigation, 67% believe court litigation takes too long and 32% believe court litigation costs too much.

v. One study dealing with AAA employment arbitration found that employees won 73% of the arbitrations they initiated and 64% of all employment arbitrations (including those initiated by employers). See Lisa B. Bingham, Is There a Bias in Arbitration of Nonunion Employment Disputes? An analysis of Active Cases and Outcomes, 6 Int'l J. Conflict Management 369, 378 (1995).

vi. A study which compared the results in employment arbitration with the results in federal court during the same period of time found that 63% of employees won in arbitration compared to 15% of employees who won in federal court. Awards to employees in arbitration were on average 18% of the amount demanded versus 10.4% of the amount demanded in court. The study also demonstrated that while arbitration awards to employees are on average lower than judgments to employees in court, the outcome

for employees is still better in arbitration because of their higher win-rates of arbitration and the shorter duration of arbitration compared to court proceedings. See Lewis L. Maltby, Private Justice: Employment Arbitration and Civil Rights, 30 Colum. Hum. Rights L. Rev. 29, 46-48 (1998).

vii. In yet another study, it was reported that employees won 51% of arbitrations, while the EEOC won 24% of cases in federal court. See George W. Baxter, Arbitration in Litigation for Employment Civil Rights?, 2 Vol. of Individual Employee Rights 19 (1993-94).

viii. Another study reported that employees won 68% of the time before the AAA as contrasted with only 28% of the time in litigation. See William M. Howard, Arbitrating Claims of Employment Discrimination, Disp. Res. J. Oct-Dec 1995, at 40-43.

ix. See Consumer and Employment Arbitration in California: A Review of Website Data Posted Pursuant to Section 1281.96 of the Code of Civil Procedure, California Dispute Resolution Institute (August 2004). The report appears at HTTP://www.mediate.com/cdri/cdri_print_Aug_6.pdf. The report concluded that consumers prevailed 71% of the time.

x. Theodore Eisenberg and Elizabeth Hill, Arbitration and Litigation of Employment Claims: An Empirical Comparison, Disp. Resol. J. Nov. 2003 – Jan. 2004, at 44. Higher-compensated employees (*i.e.*, those with annual incomes of $60,000 or more) obtained slightly higher awards in arbitration before the AAA than in court. There was insufficient court data to make a similar comparison for employees with less than $60,000 of annual income, thus proving that such employees have difficulty finding lawyers who will represent them in court.

xi. Michael Delikat and Morris M. Kleiner, An Empirical Study of Dispute Resolution Mechanisms: Where Do Plaintiffs Better Vindicate Their Rights?, Disp. Resol. J. Nov. 2003 – Jan. 2004, at 56. The study compared the results of employment discrimination cases filed and resolved between 1997 and 2001 in the S.D.N.Y. versus with the NASD and NYSE. Employees prevailed 33.6% of the time in court versus 46% of the time in arbitration. The median damages award was $95,554 in court versus $100,000 in arbitration. The median duration was 25 months in court versus 16½ months in arbitration. They also found that of over 3,000 cases filed in court, only 125 (2.8%) went to trial, thus undermining the perceived importance that consumer advocates place on the right to trial by jury.

xii. Gary Tidwell, et al., Party Evaluation of Arbitrators: An Analysis of Data Collected from NASD Regulation Arbitrations (Aug 1999), available at http://www.nasd.com/wcb/groups/med_arb/documents/mediation_arbitrati

on/nasdw_009528.pdf. In surveying individual participants in NASD-sponsored arbitration for 1997 to 1999, over 93% agreed that their claims were handled "fairly and without bias."

xiii. Lisa B. Bingham, Is there a Bias in Arbitration of Nonunion Employment Disputes? An Analysis of Actual Cases and Outcomes, 6 Int'l J. of Conflict Mgmt. 369 (1995). In a study of 171 employment arbitration cases filed with the AAA in 1992, Bingham concluded that "employee claimants are more likely than employer claimants to recover a larger proportion of the amount of damages claimed when the arbitrator is paid a fee, recovering almost fourfold what employers recover ...." She concluded that her results "contradict the theory that employment arbitrators will be biased against individual employees . . . ." She opined that arbitrators want to "be acceptable to other parties, not just the repeat player involved in that case."

BRIEF BACKGROUND OF THE FAA

The FAA was enacted in 1925. At its heart is Section 2 of the FAA, 9 U.S.C. §2, which provides that:

> "A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."

Thus, by its plain terms, the FAA makes enforceable both pre-dispute arbitration agreements ("a controversy thereafter arising") as well as post-dispute arbitration agreements ("an existing controversy"). Countless millions of consumer arbitration agreements have been entered into in reliance on this language, creating a body of settled expectations among companies and consumers alike.

The application of the FAA to consumer transactions increased significantly during the past two decades, due largely to a series of landmark United States Supreme Court rulings which confirmed that parties are as free to enter into arbitration agreements as they are to

enter into any other type of contract, even though some states purported to prohibit pre-dispute arbitration agreements and some courts refused to enforce them. The Supreme Court held that:

- The FAA creates a body of federal substantive law of arbitrability which is applicable to arbitration agreements in contracts involving interstate commerce. Perry v. Thomas, 482 U.S. 483, 489 (1987).
- Interstate commerce is to be interpreted broadly. Citizens Bank v. Alafabco, Inc., 539 U.S. 52, 56 (2003) ("[w]e have interpreted the term 'involving commerce' in the FAA as the functional equivalent of the more familiar term 'affecting commerce' -- words of art that ordinarily signal the broadest permissible exercise of Congress' Commerce Clause power").
- The FAA "revers[ed] the longstanding judicial hostility to arbitration agreements ... and place[d] arbitration agreements upon the same footing as other contracts." Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 24 (1991); Shearson/American Express, Inc. v. McMahon, 482 U.S. 220, 225-26 (1987).
- Federal law strongly favors the arbitration of disputes and requires that courts rigorously enforce arbitration agreements. Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983).
- State laws that directly or indirectly undermine enforcement of the terms of private arbitration agreements or that single out arbitration for special treatment are preempted by the FAA. Doctor's Assocs., Inc. v. Casarotto, 517 U.S. 681, 687 (1996); Southland Corp. v. Keating, 465 U.S. 1 (1984).

- "Congress, when enacting this law [the FAA], had the needs of consumers, as well as others, in mind ...." Allied-Bruce Terminix Cos., Inc. v. Dobson, 513 U.S. 265, 280 (1995);
- The FAA "ensur[es] that private agreements to arbitrate are enforced according to their terms." Volt Info. Sciences, Inc. v. Board of Trustees of Leland Stanford, Jr. Univ., 489 U.S. 468, 479 (1989).

But the FAA does not totally displace state law. Section 2 of the FAA reserves to the state and federal courts the authority to invalidate or restrict arbitration agreements "upon such grounds as exist at law or in equity for the revocation of any contract." Therefore, state law contract defenses such as lack of assent and unconscionability can be asserted by consumers who believe that a pre-dispute arbitration agreement should not be enforced. Perry v. Thomas, 482 U.S. 483, 492 n. 9 (1987).

CONSUMER ARBITRATION AGREEMENTS ARE DRAFTED FAIRLY

The existing system of "checks and balances" works well because the vast majority of companies and employers draft arbitration agreements that are intended to be fair to consumers and employees. My partners and I routinely counsel clients to draft arbitration agreements that contain the following provisions, among others:

1. Give Consumer the Right to Reject Arbitration. To ensure that consumers have truly "agreed" to arbitrate, we advise companies to give consumers the unfettered and unconditional right to reject the arbitration provision at the time they enter into the contract or within a reasonable period of time thereafter and to prominently disclose that right. Several courts, in enforcing consumer arbitration agreements, have emphasized the fairness inherent in providing such an opt-out right. See, e.g., Circuit City Stores, Inc. v. Ahmed, 283 F.3d 1198 (9th

Cir. 2002); Circuit City Stores, Inc. v. Najd, 294 F.3d 1104, 1108 (9th Cir. 2002); Providian National Bank v. Screws, 2003 Ala. LEXIS 298 (Ala. Oct. 3, 2003); Tsadilas v. Providian Nat'l Bank, 13 A.D. 3d 190, 786 N.Y.S. 2d 478 (1st Dep't. 2004).

2. Require the Arbitrator to Apply Applicable Substantive Law, Including Fee-Shifting Statutes Which Give the Consumer the Right to Recover His or Her Counsel Fees If He or She Prevails in the Arbitration. We uniformly counsel companies to specify in their arbitration clauses that the arbitrator must apply applicable substantive law and award the same remedies (including punitive damages and equitable relief) that would be available to the consumer had the matter proceeded in court. In particular, our arbitration agreements preserve the consumer's right to recover attorneys' fees and costs from the company if provided by applicable law. (Most federal and state consumer protection statutes require such fee-shifting). That way, the consumer does not lose the benefit of any statutory remedies such as treble damages or fee-shifting by proceeding to arbitration. In some cases, our clients even provide by contract to bear the consumer's legal costs if the consumer prevails, whether or not the governing statute requires the company to bear such costs.

3. Avoid "Carve-Outs" from Arbitration that Unilaterally Favor the Company. For the most part, the arbitration agreement, as matter of fairness, should operate to bind both the company and the consumer. (There are, however, some notable exceptions to this principle. Numerous courts have enforced arbitration provisions in mortgage loan agreements that except foreclosure proceedings from the scope of the arbitration provision because foreclosure in court offers numerous statutory protections to consumers that are not easily

transferable to arbitration.[4] In addition, numerous courts have enforced arbitration agreements that permit the consumer to bring an action in small claims court rather than in arbitration;[5] in fact, the AAA will not administer an arbitration if the consumer was not given this option -- see Exhibit E attached hereto).

4. Arbitration Administrator. Most companies implementing arbitration on a widespread basis choose to utilize the services of a national arbitration organization with established rules and infrastructure. Major national administrators include the AAA and NAF. Companies use established arbitration organizations because: (a) it is more efficient administratively; (b) courts are already familiar with the major organizations and their arbitration clauses have frequently been subjected to judicial scrutiny and interpretation; (c) the organizations have adopted standard procedural rules which specify the mechanics of the arbitration process, the selection of arbitrators, and so forth. We advise companies to identify more than one potential arbitration administrator in the arbitration agreement and then give the consumer the right to choose which organization to use.

5. Arbitration Costs. We generally counsel companies to provide in their arbitration clauses that if the consumer requests, the company will pay all or substantially all of the consumer's arbitration filing, administrative and hearing fees and not seek to recover them even if the consumer loses. Some companies provide that the company will "advance" the consumer's arbitration costs, and let the arbitrator determine at the end who should ultimately be

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4 See, e.g., Delta Funding Corp. v. Harris, 2006 WL 2277984 (N.J. Aug. 9, 2006); Salley v. Option One Mortgage Corp., No. 50 EAP 2005, 2007 Pa. LEXIS 1195 (Pa. May 31, 2007).

5 See, e.g., Jenkins v. First American Cash Advance of Georgia, Inc., 400 F.3d 868 (11th Cir. 2005), cert. denied, 126 S. Ct. 1457 (2006).

responsible, subject to proviso that in no event will the consumer be responsible for more than what his or her court costs would have been had the matter been litigated in court. That is also fair because the consumer pays no more than what he or she would have paid in court.

6. Location of Hearing. Our arbitration agreements (and most other arbitration agreements) provide that any hearing will be in a location near the consumer's residence so that the consumer is not burdened with traveling a long distance or incurring extra costs.

7. Disclosures. We always advise companies to make sure that the differences between arbitration and litigation are clearly and conspicuously explained to the consumer in the arbitration agreement and related loan documents. We also counsel them to highlight the fact that the consumer has the right to reject the arbitration provision without any adverse effect on his or her account. Companies do value their customers' business and want them to make an informed choice.

THE MAJOR NATIONAL ARBITRATION ADMINISTRATORS HAVE ADOPTED STANDARDS AND PROCEDURES THAT ENSURE FAIRNESS TO CONSUMERS

The most widely used national arbitration administrators, including the AAA and the NAF, have committed themselves in writing to protecting the rights of consumers to a fair arbitration.

For example, the AAA has adopted a Consumer Due Process Protocol that must be complied with by companies which wish to use the AAA as an arbitration administrator. Numerous consumer advocates and governmental groups were members of the Advisory Committee that formulated the Protocol. The Protocol was adopted by the AAA in April 1998 to ensure that arbitration agreements between consumers and the companies they deal with are endowed with "fundamental fairness." The AAA has also adopted Supplementary Consumer

Rules for use in arbitrations between consumers and businesses and a special schedule of arbitration fees that caps the fee to the consumer on a claim of $10,000 or less at $125. All other arbitration fees are paid by the company. An impoverished consumer can also apply to the AAA for a waiver of all arbitration costs. [AAA materials are attached as Exhibit E].

The NAF has adopted a Code of Procedure which, among other things (1) requires that arbitrators be "neutral and independent" and (2) provides a procedure for disqualifying arbitrators "if circumstances exist that create a conflict of interest or cause the Arbitrator to be unfair or biased." The NAF has also issued a Code of Conduct for Arbitrators and an Arbitration Bill of Rights. As set forth therein, each NAF arbitrator is a former judge, practicing attorney or law professor with at least 15 years of experience; each arbitrator is an independent contractor with the NAF and not an NAF employee; and an arbitrator who has a conflict of interest or is unfair or biased cannot decide a case. Like the AAA, the NAF also has a reduced fee schedule for consumers and permits impoverished consumers to seek a waiver of fees altogether. [NAF materials are attached as Exhibit F].

Both the AAA[6] and the NAF[7] have been recognized by courts as reasonable, fair, cost-effective and impartial forums. Significantly, U.S. Supreme Court Justice Ruth Bader

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6 See, e.g., Olson v. AAA, 876 F. Supp. 850, 852 (N.D. Tex.), aff'd without op., 71 F.3d 877 (5th Cir. 1995); MCI v. Matrix Comm. Corp., 135 F.3d 27, 36-37 (1st Cir. 1998), cert. denied, 524 U.S. 953 (1998); Doctor's Assoc., Inc. v. Stuart, 85 F.3d 975, 981 (2d Cir. 1996); LLT Int'l, Inc. v. MCI Telecomm. Corp., 18 F. Supp. 2d 349, 354 (S.D.N.Y. 1998).

7 See, e.g., Marsh v. First USA Bank, 103 F. Supp. 2d 909, 925 (N.D. Tex. 2000) ("[The NAF] boasts an impressive assembly of qualified arbitrators .... All legal remedies and injunctive relief are available to the parties .... The filing fee structure is clearly stated and reasonably based on the amount of the claim .... The Court is satisfied that NAF will provide a reasonable, fair, and impartial forum within which Plaintiffs may seek redress for their grievances."); BankOne, N.A. v. Coates, 125 F. Supp. 2d 819, 836 (S.D. Miss. 2001), aff'd, 34 Fed. Appx. 964, 2002 WL 663804 (5th Cir. Apr. 5, 2002) (given the

(continued...)

Ginsburg characterized the AAA and NAF provisions limiting fees in consumer cases as a "model[] for fair cost and fee allocation." Green Tree Financial Corp.-Ala. v. Randolph, 531 U.S. 79, 95 (2000) (Ginsburg, J., concurring)

COURTS RIGOROUSLY PROTECT CONSUMERS FROM UNFAIR ARBITRATION AGREEMENTS

The FAA itself ensures that if a company attempts to enforce an arbitration agreement that the consumer believes is unfair, a court will hear the parties and determine

(...continued)

NAF's fairness "safeguards" -- including the availability of all legal remedies and injunctive relief and the ability to request a written opinion -- "the court is not persuaded that there ... exists any basis for finding the agreement unconscionable"); In re Currency Conversion Fee Antitrust Litig., 265 F. Supp. 2d 385, 412 (S.D.N.Y. 2003) (noting that the "fee schedule in the NAF Code has been upheld as adequate and fair by numerous courts" and rejecting plaintiffs' argument that "the NAF Code unreasonably subjects them to a 'loser pays' cost-shifting provision" because the "plaintiffs are in no worse a position under the NAF Code then they would be in federal court"); Bellavia v. First USA Bank, N.A., No. 02-C-3971, 2003 U.S. Dist. LEXIS 18907, *8 (N.D. Ill. Oct. 20, 2003) (rejecting allegation that the NAF is biased and emphasizing that the NAF rules allow the parties to select an arbitrator who has no affiliation with the NAF); Bank One N.A. v. Williams, No. 3:01CV24-D, 2002 U.S. Dist. LEXIS 27217 at *10-11 (N.D. Miss. April 29, 2002) (compelling arbitration and noting that "federal courts within the Fifth Circuit have repeatedly enforced arbitration provisions where the parties agreed to arbitrate pursuant to the NAF rules"); Hale v. First USA Bank, N.A., No. 00 Civ. 5406, 2001 U.S. Dist. LEXIS 8045 at *11-12 (S.D.N.Y. June 12, 2001) ("numerous courts have found the NAF to be an adequate and fair arbitral forum and have upheld arbitration provisions requiring arbitration in the NAF"); Vera v. First USA Bank, No. Civ. A. 00-89-GMS, 2001 WL 640979 (D. Del. April 19, 2001) (the "NAF is a model for fair cost and fee allocation"); Smith v. EquiFirst Corp., 117 F. Supp.2d 557, 564 (S.D. Miss. 2000) (holding that NAF "fees provisions do not foreclose plaintiffs' access to an arbitration forum that compares favorably to a judicial forum" and compelling arbitration); ITT Comm. Fin. Corp. v. Wangerin, No. C9-95-163, 1995 WL 434459, at *2 (Minn. Ct. App. July 25, 1995) (rejecting argument that NAF arbitrators were biased due to NAF's receipt of substantial business from ITT and holding that "by itself, no level of Forum business coming from respondent would indicate partiality of the arbitrator"). In sum, there is "no persuasive evidence that the National Arbitration Forum is anything but neutral and efficient." Lloyd v. MBNA Am. Bank, N.A., 2001 U.S. Dist. LEXIS 8279, *9 (D. Del. Feb 22, 2001), aff'd, No. 01-1752, 2002 U.S. App. LEXIS 1027 (3d Cir. Jan. 7, 2002).

whether the agreement is enforceable. Pursuant to Sections 3 and 4 of the FAA, 9 U.S.C. §§3, 4,[8] the court determines the existence, enforceability and scope of the arbitration agreement.

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[8] Those sections provide, respectively, as follows:

> "Section 3. Stay of proceedings where issue therein referable to arbitration
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> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration."
>
> "Section 4. Failure to arbitrate under agreement; petition to United States court having jurisdiction for order to compel arbitration; notice and service thereof; hearing and determination
>
> A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. Five days' notice in writing of such application shall be served upon the party in default. Service thereof shall be made in the manner provided by the Federal Rules of Civil Procedure. The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. The hearing and proceedings, under such agreement, shall be within the district in which the petition for an order directing such arbitration is filed. If the making of the arbitration agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof. If no jury trial be demanded by the party alleged to be in default, or if the matter in dispute is within admiralty jurisdiction, the court shall hear and determine such issue. Where such an issue is raised, the

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See, e.g., Howsam v. Dean Witter Reynolds, Inc., 537 U.S. 79, 94 (2002) (court determines whether a particular dispute falls within the scope of an arbitration clause and whether the clause is enforceable); Green Tree Fin. Corp. v. Bazzle, 539 U.S. 444, 452 (2003) (court determines "the validity of the arbitration clause [and] its applicability to the underlying dispute between the parties").

Proof that this system adequately safeguards the rights of consumers may be found in the numerous court opinions concerning class action waivers in consumer arbitration agreements. In order to keep arbitration simple, inexpensive and speedy, many consumer arbitration agreements provide that neither party has the right to bring a class action or representative suit in court or in arbitration with respect to claims that are subject to the arbitration agreement. Although consumers' lawyers often allege that class action waivers are unconscionable, the vast majority of federal courts, and most state courts, have enforced such waivers on the grounds that (1) a class action is a mere procedural right that parties may waive;[9]

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> party alleged to be in default may, except in cases of admiralty, on or before the return day of the notice of application, demand a jury trial of such issue, and upon such demand the court shall make an order referring the issue or issues to a jury in the manner provided by the Federal Rules of Civil Procedure, or may specially call a jury for that purpose. If the jury find that no agreement in writing for arbitration was made or that there is no default in proceeding thereunder, the proceeding shall be dismissed. If the jury find that an agreement for arbitration was made in writing and that there is a default in proceeding thereunder, the court shall make an order summarily directing the parties to proceed with the arbitration in accordance with the terms thereof."

[9] See, e.g., Lloyd v. MBNA America Bank, N.A., 27 Fed. Appx. 82, 2002 U.S. App. LEXIS 1027 (3d Cir. Jan. 7, 2002) (unpublished), affirming 2001 U.S. Dist. LEXIS 8279 (D. Del. Feb. 22, 2001) (holding in consumer dispute brought against credit card issuer under the common law and federal statutes that the right to a class action is "merely procedural" and may be waived); Thompson v. Illinois Title Loans, Inc., No. 99 C 3952, (continued...)

(2) as long as the arbitration agreement preserves the consumer's substantive rights, including the right to recover attorneys' fees and costs if he or she prevails in the arbitration, the class action waiver does not hinder the prosecution of the consumer's individual claims, impede the retention of an attorney to represent the consumer on an individual basis or exculpate the company from liability;[10] and (3) even without a class action, companies remain subject to

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2000 WL 45493, at *4 (N.D. Ill. Jan. 11, 2000) (waiver by arbitration agreement); Sanders v. Robinson Humphrey/American Express, Inc., 634 F. Supp. 1048, 1065 (N.D. Ga. 1986) (class action rule a mere "procedural device"), aff'd in part and rev'd in part on different grounds, 827 F.2d 718 (11th Cir. 1987), cert. denied, 485 U.S. 959 (1988); Dienese v. McKenzie Check Advance of Wis., LLC, No. 99-C-50, 2000 U.S. Dist. LEXIS 20389, at *24 (E.D. Wis. Dec. 11, 2000) (enforcing arbitration clause barring class actions since "consumers are not signing away a substantive right"); Caudle v. American Arb. Ass'n, 230 F.3d 920, 921 (7th Cir. 2000) ("[a] procedural device aggregating multiple persons' claims in litigation does not entitle anyone to be in litigation"); Zawikowski v. Beneficial National Bank, No. 98 C 2178, 1999 WL 35304 (N.D. Ill. Jan. 11, 1999, at *2 ("[n]othing prevents the Plaintiffs from contracting away their right to a class action").

10 See, e.g., Johnson v. West Suburban Bank, 225 F.3d 366 (3d Cir. 2000), cert. denied, 531 U.S. 1145 (2001) (enforcing class action waiver in action against payday lender alleging violations of Truth in Lending Act ("TILA")); Cappalli v. National Bank of the Great Lakes, 281 F.3d 219 (3d Cir. 2001) (unpublished) (enforcing class action waiver in action alleging violation of federal usury statutes, even though plaintiff's individual claim was only $33.02); Sagal v. First USA Bank, N.A., 254 F.3d 1078 (3d Cir. 2001) (unpublished), affirming 69 F. Supp. 2d 627 (D. Del. 1999) (compelling arbitration of TILA, Delaware Consumer Fraud Act and common law claims against credit card issuer even though a class action would not be available in arbitration); Lloyd v. MBNA America Bank, N.A., 27 Fed. Appx. 82, 2002 U.S. App. LEXIS 1027 (3d Cir. Jan. 7, 2002) (unpublished), affirming 2001 U.S. Dist. LEXIS 8279 (D. Del. Feb. 22, 2001) (in consumer dispute brought against credit card issuer under the common law and federal statutes, court enforced arbitration agreement that contained a class action waiver and rejected argument that agreement was unconscionable); Jenkins v. First American Cash Advance of Ga., Inc., 400 F.3d 868 (11th Cir. 2005) (court enforced class action waiver in arbitration agreement between consumer and payday lender, holding that where arbitration agreement permits fee shifting if allowed by applicable law and preserves the parties' substantive remedies, lawyers will be willing to represent the consumer on an individual basis and the company will not be immunized against unlawful conduct), cert. denied, 126 S. Ct. 1457 (2006); Gipson v. Cross Country Bank, 294 F. Supp. 2d 1251, 1261-62 (M.D. Ala. 2003) (rejecting argument that class action was necessary for

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plaintiff to vindicate her statutory rights because plaintiff could recover her attorneys' fees if successful in the arbitration); Snowden v. CheckPoint Check Cashing, 290 F.3d 631, 638-39 (4th Cir. 2002) (rejecting argument that plaintiff "will be unable to maintain her legal representation given the small amount of her individual damages" where statute permitted fee-shifting), cert. denied, 537 U.S. 1087 (2002); Ornelas v. Sonic-Denver T, Inc., No. 06-cv-00253, 2007 WL 274738, at *5-7 (D. Colo. Jan. 20, 2007) (enforcing class action waiver where statutes permitted fee-shifting and following the "numerous courts [that] have recognized that [class action waivers] are valid and fully enforceable"); Galbraith v. Resurgent Capital Services, No. Civ. S. 05-2133 KJM, 2006 WL 2990163 (E.D. Cal. Oct. 19, 2006) (class action waiver not unconscionable where plaintiff could recover attorneys' fees if successful); Carter v. Countrywide Credit Indus., Inc., 362 F.3d 294 (5th Cir. 2004); Iberia Credit Bureau, Inc. v. Cingular Wireless LLC, 379 F.3d 159 (5th Cir. 2004); Burden v. Check into Cash of Kentucky, LLC, 267 F.3d 483 (6th Cir. 2001); Bowen v. First Family Financial Services, Inc., 233 F.3d 1331 (11th Cir. 2000); Randolph v. Green Tree Fin. Corp. - Ala., 244 F.3d 1149 (11th Cir. 2001); Baron v. Best Buy Co., Inc., 260 F.3d 625 (11th Cir. 2001); Chalk v. T-Mobile USA, Inc., No. 06-CV-158-BR, 2006 WL 2599506 (D. Or.) (Sept. 7, 2006); Miller v. Equifirst Corp. of W. Va., Civil Action No. 2:00-0335, 2006 WL 2571634 (S.D.W. Va. Sept. 5, 2006); Rains v. Foundation Health Systems Life & Health, No. 99CA2398, 2001 Colo. App. LEXIS 580 (Ct. App. Colo. Mar. 29, 2001); Forrest v. Verizon Communications, Inc., 805 A.2d 1007 (D.C. Ct. App. Aug. 29, 2002); America Online, Inc. v. Booker, Case No. 3D00-2020, 2001 Fla. App. LEXIS 1079 (Ct. App. 3d Dist. Feb. 7, 2001); Fonte v. AT&T Wireless Services, Inc., 903 So. 2d 1019 (Fla. Ct. App. 4th Dist. 2005), app. denied, 918 So. 2d 292 (Fla. 2005); Wilson v. Mike Steven Motors, Inc., 111 P.3d 1076 (Kan. Ct. App. 2005); Walther v. Sovereign Bank, 386 Md. 412, 872 A.2d 735 (2005); Ranieri v. Bell Atlantic Mobile, 304 A.D. 2d 353, 759 N.Y.S. 2d 448 (App. Div. 1st Dep't 2003), leave denied, 1 N.Y. 3d 502 (2003); Brower v. Gateway, 246 App. Div. 2d 246, 676 N.Y.S.2d 569 (N.Y. 1st Dep't 1998); Tsadilas v. Providian National Bank, 13 A.D. 3d 190, 786 N.Y.S. 2d 478 (App. Div. 1st Dep't 2004), reargument denied, 2005 N.Y. App. Div. LEXIS 247 (Mar. 8, 2005), appeal denied, 5 N.Y.3d 702 (2005); Johnson v. Chase Manhattan Bank, N.A., 784 N.Y.S. 2d 921 (table), 2004 WL 413213, at *5 & n.2 (N.Y. Sup. Ct. Feb. 27, 2004), aff'd, 786 N.Y.S. 2d 302 (N.Y. App. Div. 2004); Strand v. U.S. Nat'l Bank, N.A., No. 20040068, 2005 ND 68, 693 N.W. 2d 918 (N.D. March 31, 2005); Pyburn v. Bill Heard Chevrolet, 63 S.W. 3d 351 (Tenn. Ct. App. 2001); AutoNation USA Corp. v. Leroy, 105 S.W. 3d 190 (Tex. 2003); Stein v. Geonerco, Inc., 105 Wash. App. 41, 17 P.3d 1266 (2001); Heaphy v. State Farm Mut. Auto. Ins. Co., 117 Wash. App. 438, 72 P.3d 220 (2003), review denied, 150 Wash. 2d 1037, 84 P.3d 1230 (2004); Tillman v. Commercial Credit Loans, Inc., 629 S.E.2d 865 (N.C. Ct. App. 2006).

individual actions by consumers and to enforcement actions by state and federal governmental administrative agencies such as attorney general offices, departments of banking and the Federal Trade Commission.[11]

Indeed, there is statistical proof that consumers are able to find attorneys to represent them on an individual basis in small dollar claims where the consumer, if successful, can recover attorneys' fees and costs. The overwhelming majority of TILA lawsuits filed each year are individual, not class action, lawsuits, even though the vast majority of suits involve small dollar claims[12] and class actions are permitted under TILA. TILA permits successful plaintiffs to recover their attorneys' fees and costs. 15 U.S.C. §1640(a). According to computer searches of the LexisNexis CourtLink® database, 688 TILA cases, of which only 17 were class actions, were filed in the federal courts in 2006; 492 TILA cases, of which only 19 were class actions, were filed in the federal courts in 2005; 574 TILA cases, including only 20 class actions, were filed in 2004; 513 TILA cases, of which only 39 were class actions, were filed in 2003; and 576 TILA cases, of which only 37 were class actions, were filed in 2002.

While some courts have concluded, based on the particular facts of the cases before them, that the class action waiver in question was unconscionable under state law, most of those cases involved arbitration clauses that also impaired the consumer's substantive rights, imposed unreasonable costs or were one-sided in favor of the company. See, e.g., ACORN v.

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[11] Johnson v. West Suburban Bank, 225 F.3d 366, 375-76 (3d Cir. 2000), cert. denied, 531 U.S. 1145 (2001); accord, Randolph v. Green Tree Fin. Corp. - Ala., 244 F.3d 1149 (11th Cir. 2001).

[12] TILA provides for statutory damages, typically ranging from $100 to $2,000, plus actual damages and attorneys' fees. 15 U.S.C. §1640(a). Actual damages are nearly impossible to prove because plaintiffs must show detrimental reliance. Turner v. Beneficial Corp., 242 F.3d 1023 (11th Cir. 2001) (citing cases), cert. denied, 534 U.S. 820 (2001).

Household Int'l, Inc., 211 F. Supp. 2d 1160 (N.D. Cal. 2002) (arbitration agreement exempted collection proceedings brought by lender against consumer from arbitration and cost of arbitration would be ten times the cost of court action); Luna v. Household Fin. Corp., 236 F. Supp. 2d 1166 (W.D. Wash. 2002) (company, but not consumer, reserved right to go to court rather than arbitrate); Ting v. AT&T, 319 F.3d 1126 (9th Cir. 2003) (agreement limited damages in cases of fraud and other intentional torts and imposed thousands of dollars in arbitration fees); Kinkel v. Cingular Wireless LLC, 223 Ill. 2d 1, 857 N.E.2d 250 (2006) (contract did not inform customer of the costs of arbitration and did not provide a cost-effective means for resolving the claim).

Class action waivers are an important part of a properly functioning consumer arbitration program because such programs can substantially lower litigation costs and the cost savings are passed through to consumers, in whole or in part, in the form of lower prices for goods and services. Stephen J. Ware, *Paying the Price of Process: Judicial Regulation of Consumer Arbitration Agreements,* 2001 J. Disp. Resol. 89, 91-93; Richard A. Posner, Economic Analysis of Law 7 (6th ed. 2003).

In any event, my intent here is not to debate whether class actions are good for consumers or whether class action waivers should be enforced, but rather to emphasize that there is presently an effective system in place to hear consumers' complaints about arbitration clauses and independently determine whether an arbitration should take place. To the extent courts have declined to enforce an arbitration agreement, that shows that the system is working. It should not be viewed as an indictment of all consumer arbitration agreements, the vast majority of which comply with federal and state law and are enforced by the courts.

CONCLUSION

For all of the foregoing reasons, it is my opinion that the rights of consumers are well protected by the FAA as presently enacted, by the careful drafting of arbitration agreements, by the widely used national arbitration administrators and by the federal and state courts. Thank you for your consideration of my views.