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# An Annotated Arbitration Clause

By Christopher A. Taravella, John C. Tracy, and Kathleen Moran*

**Christopher A. Taravella** is a lawyer at DaimlerChrysler Services North America LLC. He is a member of the Governing Committee of the Conference on Consumer Finance Law.

**John C. Tracy** is a lawyer at Daimler Chrysler Services North America LLC.

**Kathleen Moran** is a third-year law student at the University of Michigan where she is the administrative manager of the *Michigan Journal of Gender and Law*. She received a Bachelor of Business Administration, with honors, from the University of Notre Dame in 1997. Ms. Moran worked in finance-related areas at Sunoco, Inc. prior to law school. She spent the summer of 2001 working at the Ministry of Commerce in Cambodia, and the summer of 2002 working as a law clerk at DaimlerChrysler Services.

## I. Introduction—A Sample Arbitration Clause

This article describes issues relating to business-consumer arbitration. The issues discussed are organized according to the order in which they arise under the language of the sample arbitration clause provided below. The clause itself is an amalgam of numerous clauses contained in consumer contracts and is not meant to be representative of any particular clause currently in use. The sample arbitration clause is as follows:

* Your authors gratefully acknowledge the assistance of Donald Querio and Daniel J. O'Rielly, of Severson & Werson, San Francisco, Calif.

### Arbitration Clause

For purposes of the Arbitration provisions, the term "You" or "Your" refers to the Buyer and, to the extent applicable, the Co-buyer, and the term "Us," "Our," or "We" refers to the Creditor and/or Creditor's successors and assignees.

1. If either You or We choose, any dispute between You and Us will be decided by arbitration and not in court.

2. If a dispute is arbitrated, each of You and We will give up the right to a trial by a court or a jury trial.

3. You agree to give up any right You may have to bring a class-action lawsuit or class arbitration, or to participate in either as a claimant, and You agree to give up any right You may have to consolidate Your arbitration with the arbitration of others.

4. The information that can be obtained in discovery from each other or from third persons in an arbitration is generally more limited than in a lawsuit.

5. Other rights that each of You and We would have in court may not be available in arbitration.

Any claim or dispute, whether in contract, tort or otherwise (including any dispute over the interpretation, scope, or validity of this contract, the arbitration clause or the arbitrability of any issue), between You and Us, including Our employees or agents, which arise out of or relate to this contract or any resulting transaction or relationship shall, at the election of either of You or Us, be resolved by a neutral, binding arbitration and not by a court action. Whoever first demands arbitration may choose to proceed under the applicable rules of the American Arbitration Association, or its successor, which may be obtained by mail from the American Arbitration Association, Attn: Customer Service Department, 335 Madison Ave., 10th Floor, NY, NY 10017-4605 or on the Internet at http://www.adr.org/, or the applicable rules of JAMS, or its successor, which may be obtained by mail from JAMS, 1920 Main Street, Suite 300, Irvine, CA 92614 or on the Internet at: http://www.jamsadr.com, or the applicable rules of the National Arbitration Forum, or its successor, which may be obtained by mail from The Forum, P.O. Box 50191, Minneapolis, Minnesota 55405-0191, or on the Internet at http://www.arbitration-forum.com.

Whichever rules are chosen, the arbitrator shall be an attorney or retired judge and shall be selected in accordance with the applicable rules. The arbitrator shall apply the law in deciding the dispute. Unless the rules provide otherwise, the arbitration award shall be issued without a written opinion. The arbitration hearing shall be conducted in the federal district in which You reside. If You demand arbitration first, You will pay the claimant's initial arbitration filing fees or case management fees required by the applicable rules up to $125, and We will pay any additional initial filing fee or case management fee. We will pay the whole filing fee or case management fee if We demand arbitration first. We will pay the arbitration costs and fees for the first day of arbitration, up to a maximum of eight hours. The arbitrator shall decide who shall pay any additional costs and fees. Nothing in this paragraph shall prevent You from requesting that the applicable arbitration entity reduce or waive Your fees, or that We voluntarily pay an additional share of said fees, based upon Your financial circumstances or the nature of Your claim.

This contract evidences a transaction involving interstate commerce. Any arbitration under this contract shall be governed by the Federal Arbitration Act (9 U.S.C. § 1 *et seq*). Judgement upon the award rendered may be entered in any court having jurisdiction.

Notwithstanding this provision, both You and We retain the right to exercise self-help remedies and to seek provisional remedies from a court, pending final determination of the dispute by the arbitrator. Neither You nor We waives the right to arbitrate by exercising self-help remedies, filing suit, or seeking or obtaining provisional remedies from a court. If any provision of this arbitration agreement is found to be unenforceable or invalid, that provision shall be severed and the remaining provisions shall be given full effect as if the severed provision had not been included.

## II. If Either You or We Chooses, Any Dispute Between You and Us Will Be Decided by Arbitration and Not in Court

A mandatory arbitration clause is a contractual clause which states that parties will arbitrate out-of-court any disputes regarding the contract, and waive their rights to use the judicial system.[1] The United States Supreme Court has indicated its approval of arbitration, finding that "Section 2 [of the Federal Arbitration Act] is a congressional declaration of a liberal federal policy favoring arbitration agreements...."[2] Mandatory arbitration clauses are found in numerous contracts, both commercial and consumer. An arbitration clause, particularly in the context of a consumer contract, should be carefully drafted in order to resist any challenges and ensure that it will be upheld by a court of law.

There are three broad goals to consider in drafting an appropriate arbitration clause:

- It should be detailed enough to apprise consumers of their legal rights and disclose the material aspects of the arbitration process.
- It should use language that is clear and plain.
- It should be fair.[3]

Arbitration differs from litigation in that, among other things, there is no right to a jury trial,[4] class actions are generally not allowed,[5] discovery is limited,[6] the award might not be issued with a written opinion,[7] and the scope of appeals is

1. *See, e.g.*, Shelly Smith, *Mandatory Arbitration Clauses in Consumer Conracts: Consumer Protection and the Circumvention of the Judicial System*, 50 DePaul L. Rev. 1191, 1192 (2001); A. Daniel Woska, *Arbitration Clauses in Consumer Retail Installment Sales Contracts After the* Green Tree Financial v. Randolph *Decision*, 55 Consumer Fin. L.Q. Rep. 107 (2001). *See also infra* Pts. VIII. and XVIII.
2. Moses H. Cone Memorial Hospital v. Mercury Construction Corp., 460 U.S. 1, 24 (1983).
3. *See, e.g.*, Alan S. Kaplinsky and Mark. J. Levin, "Anatomy of an Arbitration Clause: Drafting and Implementation Issues Which Should be Considered by a Consumer Lender," American Law Institute—American Bar Association Continuing Legal Education, ALI-ABA course of study, Conference on Life and Health Insurance Litigation (May 10, 2001).
4. *See infra* Pt. IV. for discussion of parties' rights to a jury trial.
5. *See infra* Pt. V. for discussion of parties' rights to bring a class action or class arbitration.
6. *See infra* Pt. VI. for discussion of discovery limitations in an arbitration.
7. *See infra* Pt. XII. for discussion of written opinions in arbitration awards.

restricted.[8] Consumers may have little or no understanding of the arbitration process or the major differences between arbitration and litigation. When drafting an arbitration clause, it is therefore advisable to note the distinctive aspects of arbitration.

The sole basis for referring claims to arbitration is a contractual one, and any ambiguities will be resolved against the drafter; courts will sometimes exclude disputes from arbitration by construing the scope of an arbitration clause narrowly.[9] Therefore, it is imperative that the arbitration clause be drafted in a clear and precise manner. It should be written so that it is easily understood by the average consumer, avoiding "legalese" in favor of "plain English."

Finally, the arbitration clause should be drafted so that it is fair to both the consumer and the business. Courts will sometimes refuse to enforce an arbitration agreement that lacks mutuality,[10] so it is important that the business does not overreach itself in drafting the arbitration clause.

Businesses need to remain attentive even after the arbitration agreement is in effect. In a recent Alabama Supreme Court case, the consumer was able to successfully eliminate the arbitration agreement by submitting, with their check, an addendum that professed to do away with the arbitration clause in the original contract. The court found that the company's continued service and acceptance of the check constituted acceptance of the addendum, even though it was argued that the check had been processed by an employee lacking the authority to contract for the company.[11]

## III. Presentation and Placement of the Clause

*In Doctor's Assocs., Inc. v. Casarotto;*[12] the United States Supreme Court held under the Federal Arbitration Act (FAA) that arbitration clauses cannot be singled out for special requirements in terms of type size and location in the contract; they cannot be subjected to rules that are not applicable to contractual provisions generally.

Consumers sometimes argue that arbitration clauses are unconscionable because they were inconspicuously placed in the contract, were set forth in small type, etc. Usually, such claims are rejected.[13]

In a recent case involving the purchase of a vehicle, the Supreme Court of Mississippi affirmed the circuit court's finding of procedural unconscionability. It found that the arbitration agreement was unenforceable because the typeface was less than one-third the size of many other terms in the contract, was in very fine print, and appeared in regular type font. Furthermore, all of the details concerning the vehicle the consumer purchased were in boldface print, while the arbitration provision was not. The court also noted that the arbitration provision was preprinted on the contract.[14]

Highlighting the arbitration clause (boldface type, a larger font size, and/or placing the clause in a prominent place in the contract), even though the law does not require it, may substantially reduce the likelihood of success of claims that the clause was not noticeable.

## IV. If a Dispute Is Arbitrated, Each of You and We Will Give up the Right to a Trial by a Court or a Jury Trial

Most courts recognize that arbitration is a valid alternative to litigation,[15] and does not violate the Seventh Amendment of the United States Constitution.[16]

However, at least one court has found differently. In *City of Lincoln v. Soukup*,[17] the court noted the "longstanding rule in Nebraska that a contract to compel parties to arbitrate future disputes and thus to oust the courts of jurisdiction to settle such disputes is against public policy and is void." Although this case involved a grievance with a personnel board, a later Nebraska Supreme Court case insists that this doctrine applies only to contracts of insurance.[18]

## V. You Agree to Give up Any Right You May Have to Bring a Class-Action Lawsuit or Class Arbitration, or to Participate in Either as a Claimant, and You Agree to Give up Any Right You May Have to Consolidate Your Arbitration with the Arbitration of Others

### A. Cases Rejecting Class Action

Class actions will usually be denied whenever a pre-dispute mandatory arbitration provision is present, especially if the provision expressly precludes class action treatment.

8. *See infra* Pt. XII. for discussion of restrictions on the scope of appeals.

9. Kaplinsky and Levin, *supra* note 3.

10. *See infra* Pt. XVII. for discussion of the doctrine of mutuality for arbitration agreements.

11. Cook's Pest Control v. Rebar, 2002 WL 31780946 (Ala. Dec. 13, 2002).

12. 517 U.S. 681 (1996).

13. *See, e.g.*, Webb v. Investacorp, Inc., 89 F.3d 252 (5th Cir. 1996); Hill v. Gateway 2000, 105 F.3d 1147 (7th Cir. 1997); McCullough v. Shearson Lehman Bros., Inc., 1988 WL 23008 (W.D. Pa. Feb. 18, 1988).

14. *See* East Ford, Inc. v James E. Taylor, Jr., 2002 WL 1584301 (Miss. July 18, 2002).

15. *See e.g.*, GTFM, LLC v. TKN Sales, Inc., 257 F. 3d 235 (2d Cir. 2001) (finding that the Seventh Amendment does not apply to actions in state court, and that the binding arbitration process in the Minnesota Sales Representative Act (MSRA) is not unconstitutional nor did it violate GTFM's right to a jury trial); Marsh v. First USA Bank, N.A. 103 F. Supp. 2d 909 (N.D. Tex. 2000) (rejecting the plaintiff's arguments, which were based on unconscionability and invalid waiver of the Seventh Amendment right to a jury trial).

16. *See* U.S. Const. Amend. VII.: "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."

17. 340 N.W.2d 420, 423 (Neb. 1983).

18. *See* Rawlings v. Amco Ins. Co., 438 N.W. 2d 769 (1989).

Numerous courts have held that a prohibition of class-wide arbitration is not contrary to federal and state consumer protection statutes and is not unconscionable.[19] Many federal courts have held that unless the arbitration agreement or arbitration rules specifically provide for arbitration on a class-wide basis, the court may not order it.[20] Numerous federal cases have enforced arbitration agreements that contain provisions prohibiting class actions.[21]

These decisions reflect the U.S. Supreme Court's conclusion that the strong policy in favor of arbitration that is embodied in the FAA supersedes considerations of procedural efficiencies, even where federal statutory claims are involved. In *Gilmer v. Interstate/Johnson Lane Corp.*, for example, the plaintiff contended that claims under the Federal Age Discrimination in Employment Act (ADEA) could not be subject to arbitration because, among other reasons, "arbitration procedures cannot adequately further the purposes of the ADEA because they do not provide for federal class actions."[22] The Supreme Court rejected this argument, stating that "even if the arbitration could not go forward as a class action or class relief could not be granted by the arbitrator, the fact that the [ADEA] provides for the possibility of bringing a collective action does not mean that individual attempts at conciliation were intended to be barred."[23]

A number of state courts, consistent with federal practice, also have refused to compel class arbitration where the agreement does not authorize class-wide arbitration.[24] A few state courts have addressed the issue of an arbitration provision that expressly prohibits class actions.[25]

19. *See* Kaplinsky and Levin, *supra* note 3. *See also* discussion of waiver, *infra* at Pt. XVIII.

20. Cases enforcing arbitration agreements on an individual and not a class-wide basis where the agreements are silent as to class actions include: Johnson v. West Suburban Bank, 225 F.3d 366 (3d Cir. 2000); Champ v. Siegel Trading Co., Inc., 55 F.3d 269 (7th Cir. 1995) ("section 4 of the FAA forbids federal judges from ordering class arbitration where the parties arbitration agreement is silent on the matter"); Deiulemar Compagnia di Navigazione S.P.A. v. M/V Allegra, 198 F.3d 473 (4th Cir. 1999), *cert. denied*, 146 L. Ed. 2d 794 (2000) (follows *Champ*); Iowa Grain Co. v. Brown, 171 F.3d 504 (7th Cir. 1999) (consumer did not waive right to arbitrate by bringing class action in court since class actions cannot be arbitrated absent an explicit agreement); Randolph v. Green Tree Financial Corp., 244 F. 3d 814 (11th Cir. 2001) (holding "that a contractual provision to arbitrate Truth in Lending Act (TILA) claims is enforceable even if it precludes a plaintiff from utilizing class action procedures in vindicating statutory rights under TILA"); Arellano v. Household Fin. Corp., 2002 WL 221604 (N.D. Ill. Feb. 13, 2002) (TILA rescission claim must be resolved in arbitration on an individual, not a class-wide basis); Hale v. First USA Bank, N.A., 2001 WL 687371 (S.D.N.Y. June 12, 2001) (finding arbitration precludes a TILA class action); Furgason v. McKenzie Check Advance of Indiana, Inc., 2001 WL 238129 (S.D.Ind. Jan. 3, 2001) (holding that under Seventh Circuit precedent, a court may not order class-wide arbitration based on an arbitration clause that is silent on this issue); Gray v. Conseco, Inc., 2000 WL 1480273 (C.D. Cal. Sept. 29, 2000) (class-wide arbitration is inappropriate unless authorized by the arbitration clause); Thompson v. Illinois Title Loans, Inc., 2000 WL 45493 (N.D. Ill. Jan. 11, 2000); Brown v. Surety Fin. Service, Inc., 2000 WL 528631 (N.D. Ill. Mar. 23, 2000); Wood v. Cooper Chevrolet, Inc., 102 F. Supp. 2d 1345 (N.D. Ala. 2000); Herrington v. Union Planters Bank, N.A., 113 F.Supp. 2d 1026 (S. D. Miss. 2000) (compelling arbitration of the individual claim and dismissing the plaintiffs' class action allegations in connection with a Truth-in-Savings Act (TISA) claim), *aff'd*, 265 F.3d 1059 (5th Cir. 2001); Hyundai America, Inc. v. Meissner & Wurst GmbH & Co., 26 F. Supp. 2d 1217, 1219-20 (N.D. Cal. 1998); Bowen v. First Family Fin. Servs., Inc., No. 97-S-1279-N (M.D. Ala. June 17, 1998) (finding that being able to bring a class action is not a "right" under the Truth-in-Lending Act), *aff'd*, 233 F. 3d 1331 (11th Cir. 2000); Howard v. Klynveld Peat Marwick Goerderler, 977 F. Supp. 654, 665 n.7 (S.D.N.Y. 1997); Randolph v. Green Tree Financial Corp., 991 F. Supp. 1410 (M.D. Ala. 1997), *rev'd on other grounds*, 178 F.3d 1149 (11th Cir. 1999), *rev'd in part*, 531 U.S. 79 (2000); McCarthy v. Providential Corp., 1994 WL 387852 (N.D. Cal. July 19, 1994), *appeal dism'd*, 122 F.3d 1242 (9th Cir. 1997), *cert. denied*, 525 U.S. 821 (1998); Gammaro v. Thorp Consumer Discount Co., 828 F. Supp. 673, 674 (D. Minn. 1993), *appeal dism'd*, 15 F.3d 93 (8th Cir. 1994); Sims v. Unicor Mortgage, Inc., 1998 WL 34016832 (N.D. Miss. Sept. 8, 1998); Goodwin v Ford Motor Credit Co., 970 F. Supp. 1007 (M.D. Ala. 1997); Lopez v. Plaza Finance Co., 1996 WL 210073 (N.D. Ill. Apr. 25, 1996) (denying class certification based on a pre-dispute arbitration provision); Truckenbrodt v. First Alliance Mortg. Co., 1996 WL 422150 (N.D. Ill. July 24, 1996).

*See also* Caudle v. American Arbitration Ass'n, 230 F.3d 920 (7th Cir. 2000); Kirkpatrick v. J.C. Bradford & Co., 827 F.2d 718, 725 n.5 (11th Cir. 1987) (holding that investors whose contracts contain arbitration agreements cannot be members of a class); Kennedy v. Conseco Finance Corp., 2000 WL 1760943 (N.D. Ill. Nov. 29, 2000), *order modified on Jan. 11, 2001* (same); Marsh v. First USA Bank, N.A, 103 F. Supp. 2d 909 (N.D. Tex. 2000) (plaintiffs do not have statutory right

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under the TILA to pursue class action remedy in judicial forum); Stout v. J.D. Byrider, 228 F. 3d 709 (6th Cir. 2000) (same), *cert. denied*, *affirming* 50 F.Supp. 2d 733 (N.D. Ohio 1999); Cappalli v. Nat'l Bank of the Great Lakes, No. 99-CV-6214 (E.D. Pa. Aug. 22, 2000) (compelling arbitration of the named-plaintiff's claim brought under Section 85 of the National Bank Act), *aff'd*, 281 F.3d 219 (3d Cir. 2001); Coleman v. Nat'l Movie-Dine, Inc., 449 F.Supp. 945, 947-48 (E.D. Pa. 1978) (rejecting the plaintiff's argument that the action could not be stayed because the class action allegations were not referable to arbitration and compelling arbitration of the individual claims only); *In re* Managed Care Litig., 2002 WL 31154945 (S.D. Fla. Dec. 11, 2000); Erickson v. Paine Webber, Inc., 1990 WL 104152 (N.D. Ill. July 13, 1990); Capitol Life Ins. Co. v. Gallagher, 839 F.Supp. 767 (D. Colo. 1993), *aff'd*, 47 F.3d 1178 (10th Cir. 1995) (table); Hunt v. Up North Plastics, Inc., 980 F. Supp. 1046 (D. Minn. 1997); Lieschke v. RealNetworks, Inc., 2000 WL 198424 (N.D. Ill. Feb. 10, 2000); Chandler v. Drexel Burham Lambert, Inc., 633 F. Supp 760 (N.D. Ga. 1985); Meyers v. Univest Home Loan, Inc., 1993 WL 307747 (N.D. Cal. Aug. 4, 1993); Collins v. Int'l Dairy Queen, Inc., 169 F.R.D. 690 (M.D. Ga. 1997) (same); *In re* Piper Funds, 71 F.3d 298, 302-03 (8th Cir. 1995) (finding that a party's "contractual and statutory right to arbitrate may not be sacrificed on the altar of efficient class action management."); Sagal v. First USA Bank, N.A., 69 F. Supp. 2d. 627 (D. Del. 1999), *aff'd*, 254 F.3d 1078 (3d Cir. 2001) (recognizing that class-wide arbitration of a TILA claim was unavailable and that this did not make the clause unconscionable); Rains v. Found. Health Sys. Life & Health, 23 P.3d 1249, 1253 (Colo. Ct. App. 2001) (holding that an insurance company's arbitration clause was enforceable even though it required the plaintiff to arbitrate only her individual claims).

21. Lloyd v. MBNA America Bank, N.A. 2002 WL 21932 (3d Cir. 2002) (the right to bring a class action under the TILA may be waived by an agreement to arbitrate); Snowden v. CheckPoint Check Cashing, 290 F. 3d 631 (4th Cir. 2002); Shales v. Discover Card Services, Inc., 2002 WL 2022596 (E.D. La. Aug. 30, 2002) ("the court notes that such [class action] restrictions are routinely enforced in this jurisdiction."); Lozano v. AT&T Wireless, 216 F.Supp.2d 1071, 1074 (C.D. Cal. 2002) ("a prohibition on class wide arbitration…does not constitute substantive uncon-scionability."); Bischoff v. DirectTV, Inc., 180 F.Supp.2d 1097, 1108 (C.D. Cal. 2002) (the prohibition of class actions does not render an arbitration clause unenforceable); Zawikowski v. Beneficial Nat'l. Bank, 1999 WL 35304 (N.D. Ill. Jan. 11, 1999) (rejecting the plaintiffs' argument that the inclusion in a consumer loan agreement of a clause prohibiting class actions was void under public policy and holding that "[n]othing prevents the Plaintiffs from contracting away their right to a class action."); Doctor's Assocs., Inc. v. Hollingsworth, 949 F. Supp. 77, 80-81 (D. Conn. 1996); Goetsch v. Shell Oil Company, 97 F.R.D. 574 (W.D.N.C. 2000); Vigil v. Sears Nat'l Bank, 2002 WL 987412 (E.D. La. May 10, 2002) ( finding that the cardholder was given adequate notice of the clause prohibiting class actions and that it was bound by the strong presumption in favor of arbitration); Pick v. Discover Fin. Servs., Inc., 2001 WL 1180278 (D. Del. Sept. 28, 2001) (noting that "it is generally accepted that arbitration clauses are not unconscionable because they preclude class actions").

22. 500 U.S. 20, at 32 (1991).

23. *Id.* (quoting Nicholson v. CPC Int'l, Inc., 877 F.2d 221, 241 (3rd Cir. 1989) (Becker, J. dissenting)). *See also* Dean Witter Reynolds Inc., v. Byrd, 470 U.S. 213, 221 (1985) ("[T]he preeminent concern of Congress in passing the [FAA] was to enforce private agreements into which parties had entered, and that concern requires that we rigorously enforce agreements to arbitrate, even if the result is "piecemeal" litigation, at least absent a countervailing policy manifested in another federal statue."); Moses H. Cone Mem'l Hosp. v. Mercury Const. Corp., 460 U.S. 1, 33 (1983) ("The relevant federal law requires piecemeal resolution when necessary to give effect to an arbitration agreement."); Landers v. Crown Pontiac, 2001 WL 1867812 (N.D. Ala. May 31, 2001) (ordering arbitration where the plaintiff claimed that she and a putative class were subjected to discrimination due to the defendant finance company's practice of allowing the dealer to mark up the financing rate on retail installment contracts, known in the industry as a "dealer spread," dismissing the class action, and rejecting the argument that a contract governed by the FAA is unenforceable simply because it does not permit individuals to bring class actions.).

24. *See, e.g.*, Frame v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 20 Cal. App. 3d 668 (1971); Vernon v. Drexel Burnham & Co., 52 Cal. App. 3d 706 (1975); Harris v. Shearson Hayden Stone, Inc., 441 N.Y.S. 2d 70, 74-76 (N.Y. Sup. Ct. 1981), *aff'd*, 435 N.E.2d 1097 (1982); Leason v. Merrill Lynch, Pierce, Fenner & Smith, 1984 WL 8232 (Del. Chancery Aug. 23, 1984); Perry v. Beneficial Nat. Bank USA, 1998 WL 279174 (Macon Co., Ala. May 15, 1998) (reported in 2 Consumer Financial Services Law Report 5 (June 12, 1998)) (holding that the named plaintiff could only pursue her individual claims against Beneficial in the arbitration because Beneficial's arbitration agreement did not authorize class action arbitrations and because the plaintiff, having agreed to arbitrate, could not adequately represent the class); Med Center Cars, Inc. v. Smith, 727 So. 2d 9 (Ala. 1998) (denying class action arbitration and refusing to accept as persuasive the option of class-wide arbitration); *Ex parte* Green Tree Fin. Corp., 723 So. 2d 6 (Ala. 1998); Pyburn v. Bill Heard Chevrolet, 63 S.W. 3d 351 (2001) (inability to bring a class action in arbitral forum does not render arbitration clause ineffective); Stein v. Geonerco, Inc., 17 P.3d 1266 (Wash. Ct. App. 2001).

25. *See* Discover Bank v. Superior Court, 129 Cal. Rptr. 2d 393, 407 (Ct. App. 2003) (rejecting Szetela v. Discover Bank, 97 Cal. App. 4th 1094 (Ct. App. 4th Dist. 2002) and concluding that "section 2 of the FAA, which mandates enforcement of

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### B. Cases Supporting Class Action

Several courts have invalidated predispute mandatory arbitration provisions, based either entirely or partly on the fact that they precluded class action recovery.[26] Sometimes, courts will choose to sever only those provisions relating to the class action.[27]

Some state courts in California, Georgia, Pennsylvania, and South Carolina have permitted arbitration on a class-wide basis.[28] The arbitration agreements in these cases did not expressly prohibit class actions.[29]

As noted above, no federal court has authorized class arbitration unless such a procedure is expressly provided for in the arbitration agreement. The U.S. Supreme Court declined to address the issue in *Green Tree Fin. Corp.—Alabama v. Randolph*,[30] because it was not properly raised in the lower courts. In *Green Tree*, the consumer argued that her arbitration agreement was unenforceable because it precluded pursuit of her Truth In Lending Act (TILA) claim as a class action. *Green Tree* is significant for holding: (1) where the district court orders the parties to proceed to arbitration, and dismisses all the claims before it, the decision is "final" and therefore appealable; and (2) where the arbitration agreement is silent as to costs, the consumer bears the burden of showing the likelihood of incurring such costs in order to find the agreement unenforceable.[31] On remand, the Eleventh Circuit U.S. Court of Appeals in *Green Tree* denied the plaintiff's right to class treatment of the claim, not reaching the issue of whether there could ever be a class arbitration, but noting that federal courts had answered in the negative and only two state supreme courts had held otherwise.[32]

## VI. The Information That Can Be Obtained in Discovery from Each Other or from Third Persons in an Arbitration Is Generally More Limited Than in a Lawsuit

### A. In General

See *United Nuclear Corp. v. General Atomic Co.*;[33] *Board of Educ. Taos Mun. Schools v. The Architects, Taos*;[34] *Hayne,*

25. *(Continued from previous page)*

arbitration agreements, preempts any otherwise applicable California judicial law finding class action waivers to be substantively unconscionable and invalid"), *review granted*, 132 Cal. Rptr. 2d (2003); Gras v. Assocs. First Capital Corp., 786 A.2d 886 (N.J App. Div. 2001) (enforcing a "no class action" provision in an arbitration clause); Edelist v. MBNA Am. Bank, 790 A.2d 1249, 1261 (Del. Super. Ct. 2001) (finding that it was not unconscionable for an arbitration clause to preclude class-wide arbitration of disputes because, among other things, the "surrender of that class action right was clearly articulated in the arbitration agreement."); Lytle v. CitiFinancial Services, Inc., No. 00-7550 (Del. Cty. Ct. of Comm. Pleas, Pa. Mar. 7, 2001) (rejecting plantiffs' arguments that the arbitration clause was unenforceable because it prohibited class arbitration).

26. Cases where the courts have declared the entire arbitration agreement unenforceable include: Ting v. AT&T, 182 F. Supp. 2d 902 (N.D. Cal. 2002) (holding that the company's mandatory consumer arbitration clause was unconscionable and unenforceable, and that AT&T attempted to shield itself from liability by imposing on its customers a dispute resolution system that prevented them from participating in a class action and limited recovery of damages), *aff'd*, 319 F.3d 1126 (9th Cir. Feb. 11, 2003); Powertel, Inc. v. Bexley, 743 So. 2d 570, 576-77 (Fla. Dist. Ct. App. 1999) (concluding that an arbitration provision that precludes class action relief is unconscionable and unenforceable); Lozada v. Dale Baker Oldsmobile, Inc., 91 F. Supp. 2d 1087, 1105-06 (W.D. Mich. 2000) (finding an arbitration provision was unconscionable in part because it waived class remedies allowable under the TILA, as well as certain declaratory and injunctive relief under federal and state consumer protection laws); Hornstein v. Mortgage Market Inc.,1999 U.S. Dist. LEXIS 21463 (D. Ore. Jan. 11, 1999) (denying a motion to compel arbitration of a claim under the Federal Fair Labor Standards Act (FLSA), in part, on the basis that the arbitration clause offended the employee's right to maintain a class action under the FLSA. The same court later reversed itself on July 23, 1999); ACORN v. Household Intern., Int'l., 211 F. Supp. 2d 1160 (N.D. Cal. 2002) (holding that a provision prohibiting class actions, along with cost-splitting and confidentiality provisions, is procedurally and substantively unconscionable. The court refused to sever the offensive provisions and found the entire arbitration agreement unenforceable); Leonard v. Terminix Int'l Co., ___ So.2d ___, 2002 WL 31341084 at p.*6 (Ala. Oct. 18, 2002) (arbitration clause was unconscionable because it foreclosed "practical redress through a class action..."); State of West Virginia ex rel Dunlap v. Berger, 567 S.E.2d 265, 278 (W. Va. 2002) ("permitting the proponent of a[n arbitration] contract to include a provision that prevents an aggrieved party from pursuing class action relief would go a long way toward allowing those who commit illegal activity to go unpunished, undeterred and unaccountable."); Ramirez III v. Circuit City Stores, Inc., 76 Cal. App. 4th 1229 (1999) (declaring that an arbitration clause expressly precluding class action relief is unconscionable), *review granted and opinion superseded*, 995 P.2d 137 (Cal. 2000); Luna v. Household Finance Corp., 236 F. Supp. 2d 1166 (W.D. Wash. 2002) (finding the arbitration clause substantively unconscionable due to the class action prohibition, the non-mutuality of legal remedies, the confidentiality requirement, and the allocation of costs).

Three recent cases from California, invalidating "no class action" clauses in arbitration clauses as unconscionable under state law despite the apparent mandate to the contrary in the FAA, have stirred considerable controversy and are considered by some specialists in this area of law to be likely candidates for reversal or rejection by other courts. *See* Szetela v. Discover Bank, 97 Cal. App. 4th 1094 (Ct. App. 4th Dist. 2002); *ACORN*, 211 F. Supp. 2d 1160; *Ting*, 182 F. Supp. 2d 902; Alan S. Kaplinsky and Mark J. Levin, *The Gold Rush of 2002:*

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*California Courts Lure Plaintiffs' Lawyers (but Undermine Federal Arbitration Act) by Refusing to Enforce "No-Class Action" Clauses in Consumer Arbitration Agreements*, 58 Bus. Law. (1289) (2003). *But see Discover Bank*, 129 Cal. Rptr. 2d 393; *supra* note 25.

Indeed, there is now a split among the districts of the Court of Appeals in California. *Compare*, Mandel v. Household Bank (Nevada) Nat. Assn., 105 Cal. App. 4th 75 (2003) (following *Szetela*) and Discover Bank v. Superior Court, 105 Cal. App. 4th 326 (2003) (rejecting the *Szetela* reasoning).

27. *See e.g., Szetela*, 97 Cal. App. 4th 1094 (holding that an arbitration provision prohibiting arbitration of representative or class action claims was unconscionable, and striking only the anti-class action provision from the arbitration clause, leaving the possibility of classwide arbitration contrary to the parties' express agreement), *review denied* (July 31, 2002). *See supra* note 26. *See also Mandel*, 105 Cal. App. 4th 75; *but see Discover Bank*, 105 Cal. App. 4th 326 (holding that because the arbitration agreement was valid and governed by the FAA, the trial court was preempted from applying state substantive law to strike the class action waiver from the agreement). *See also* Bolter v. The Super. Ct. of Orange County, 87 Cal.App.4th 900 (2001) (holding that a provision precluding class-wide arbitration, when combined with a distant forum provision and a prohibition on punitive damages, made the arbitration provision unconscionable and severed those provisions). The *Bolter* court cited Cal. Civ. Code § 1670.5(a), under which the court, in its discretion, may refuse to enforce the contract as a whole if it is permeated by the unconscionability, or it may strike any single clause or group of clauses that are so tainted or so contrary to the essential purpose of the agreement, or it may simply limit unconscionable clauses so as to avoid unconscionable results. Later, however, the court modified its opinion to retain the clause prohibiting consolidation of claims, recognizing it as part of the enforceable portion of the arbitration agreement. *Id.*, No. 00273378, Order Modifying Opinion (Mar. 30, 2001).

In *ACORN*, 211 F. Supp. 2d 1160, 1170, the court noted that the remedy in *Szetala* went father than allowed under federal procedure, even applying state unconscionability standards. By contrast, *ACORN*, struck the entire arbitration cluase rather than ordering class arbitration against the wishes of the parties. *Id.*, at 1173-74.

28. *See* Kaplinsky and Levin, *supra* note 3.

29. *See, e.g.*, Keating v. Superior Court, 31 Cal.3d 584 (1982), *rev'd on other grounds*, 465 U.S. 1 (1984) (allowing class-wide arbitration in some cases as "the fairest and most efficient way of resolving the parties' dispute"); Izzi v. Mesquite Country Club, 186 Cal. App. 3d 1309 (1986); Lewis v. Prudential-Bache Securities, Inc., 179 Cal. App. 3d 935 (1986); Boynton v. Barnett, 233 S.E.2d 185 (Ga. 1977); Callaway v. Carswell, 242 S.E.2d 103 (Ga. 1978); Dickler v. Shearson Lehman Hutton, Inc., 596 A.2d 860 (Pa. 1991), *alloc. denied*, 616 A.2d 984 (Pa. 1992); Bazzle v. Green Tree Financial Corp., 569 S.E.2d. 349, 2002 WL 1955753 (S.C. Aug. 26, 2002) ("class-wide arbitration may be ordered when the arbitration agreement is silent if it would serve efficiency and equity and would not result in prejudice."), *cert. granted*, 123 S. Ct. 817 (2003).

30. 531 U.S. 79 (2000).

31. *See infra* this text at Pt. XIV. for further discussion of arbitration costs. *See also* Woska, *supra* note 1.

32. *See* Green Tree Fin. Corp.-Alabama v. Randolph, 244 F.3d 814, 815-16 (11th Cir. 2001). *See also* Woska, *supra* note 1.

33. 597 P.2d 290, 302 (N.M. 1979), *cert. denied*, 444 U.S. 911 (1979) ("[D]iscovery procedures have often been considered to be inconsistent with the reasons for arbitration.").

34. 709 P.2d 184, 186 (1985) (taking judicial notice that the "scope of discovery is considerably diminished under arbitration....").

*Miller & Farni, Inc. v. Flume*,[35] and *City of Pinehurst v. Spooner Addition Water Co.*[36]

### B. Insufficient Discovery as Grounds for Not Enforcing the Arbitration Clause

There are a few cases refusing to enforce arbitration agreements because of, among other things, the courts' concerns about insufficient discovery. These agreements, however, were all made in the context of employment arbitration.[37]

## VII. Other Rights That Each of You and We Would Have in Court May Not Be Available in Arbitration

### A. Disclosures in General

Arbitration disclosures are generally held not to be a legal requirement.[38] Court decisions under the Federal Arbitration Act hold that states cannot impose on arbitration clauses requirements that are not applicable to contract provisions generally.[39] In addition, several courts have held that there is no duty to explain arbitration clauses.[40]

### B. Exceptions

However, in *Patterson v. ITT Consumer Financial Corp.*,[41] the California Court of Appeals held an arbitration clause to be unconscionable on grounds that, among other things, the clause was not pointed out and the mechanics of arbitration were not sufficiently disclosed to the consumers at the time they signed the loan agreement. The Ohio Supreme Court followed *Patterson* in *Williams v. Aetna Finance*.[42] Voluntarily providing arbi-tration disclosures may alleviate the possibility of claims of unconscionability.

## VIII. Any Claim or Dispute, Whether in Contract, Tort or Otherwise (Including Any Dispute Over the Interpretation, Scope, or Validity of This Contract, the Arbitration Clause or the Arbitrability of Any Issue), Between You and Us, Including Our Employees or Agents, Which Arise Out of or Relate to This Contract or Any Resulting Transaction or Relationship Shall, at the Election of Either of You or Us, Be Resolved by a Neutral, Binding Arbitration and Not by a Court Action. Any Claim or Dispute Is to Be Arbitrated on an Individual Basis and Not as a Class Action

### A. Arbitrability

When it is asserted that a claim filed in court should be arbitrated, the decision must be made whether a valid agreement to arbitrate exists and whether the agreement to arbitrate includes that claim. The U.S. Supreme Court has held that if the parties clearly agree, those decisions will be made by the arbitrator.[43] However, it is for the court to determine if the parties have clearly so agreed, and state law governs this determination. If the arbitration agreement does not expressly give the arbitrator the authority to decide these issues, the court will do so.

A claim by the consumer that the entire contract was induced by fraud will not prevent a court from compelling arbitration; it is for the arbitrators to

35. 888 F. Supp. 949, 952-53 (E.D. Wis. 1995) (stating that arbitration proceedings need not be constrained by formal rules of procedure or evidence so long as the parties receive a fair hearing).

36. 432 S.W.2d 515, 518 (Tex. 1968) (the terms of the arbitration clause should control the scope of discovery).

37. *See, e.g.*, Cole v. Burns Int'l Security Services, 105 F.3d 1465, 1482 (D.C. Cir. 1997) (arbitration agreements should not be enforced unless they provide for "more than minimal discovery"); Hooters of America, Inc. v. Phillips, 39 F. Supp. 2d 582, 614-15 (D.S.C. 1998) (arbitration held unconscionable in part because the procedural rules were biased against the employee and in favor of the company where the company had total control over the selection of arbitrators, the employee had severely limited discovery, and witness disclosure and sequestration were one-sided), *aff'd on other grounds*, 173 F.3d 933 (4th Cir. 1999) (holding the employer had breached the arbitration agreement by issuing biased rules); Kinney v. United Health Care Servs. Inc., 70 Cal. App. 4th 1322 (1999) ("The unconscionable nature of the unilateral arbitral obligation is heightened by certain other terms of United's arbitration policy. Given that United is presumably in possession of the vast majority of evidence that would be relevant to employment-related claims against it, the limitations on discovery, although equally applicable to both parties, work to curtail the employee's ability to substantiate any claim against United."); Armendariz v. Foundation Health Psychcare Services, Inc., 24 Cal. 4th 83 (2000) (agreement to arbitrate employment discrimination claims is enforceable if "the arbitration (meets) certain minimum requirements, including neutrality of the arbitrator, the provision of adequate discovery, a written decision that will permit a limited form of judicial review, and limitations on the costs of arbitration"); Gonzalez v. Hughes Aircraft Employees Federal Credit Union, 990 P.2d 504 (Cal. 1999), *review granted and opinion superseded*, 978 P.2d 1 (Cal. 1999), *appeal dismissed per stipulation*, 990 P.2d 504 (Cal. 1999); Blount v. National Lending Corp., Inc., 108 F.Supp.2d 666 (S.D. Miss. 2000) (enforcing the arbitration clause despite assertions by the plaintiffs that they had no knowledge of it and that it was inconspicuous, where the arbitration agreement was a separate signed document).

38. Kaplinsky and Levin, *supra* note 3.

39. *See, e.g.*, Doctor's Assocs, Inc. v. Casarotto, 517 U.S. 681 (1996).

40. *See, e.g.*, Adams v. Merrill Lynch Pierce Fenner & Smith, 888 F.2d 696, 701 (10th Cir. 1989) (no duty to specially disclose that the written customer agreement contained an arbitration clause); McCarthy v. Providential Corp., 1994 WL 387852 (N.D. Cal. July 19, 1994) (rejecting the argument that the defendants had a duty to explain the arbitration clause to senior citizens), *appeal dismissed*, 122 F.3d 1242 (9th Cir. 1997); Bender v. Smith Barney, Harris Upham & Co., Inc., 789 F. Supp. 155, 159 (D.N.J. 1992) (no duty to explain the existence or scope of an arbitration clause); Blount v. National Lending Corp., 108 F. Supp. 2d 666 (S.D. Miss. 2000) (enforcing the arbitration clause despite assertions by the plaintiffs that they had no knowledge of it and that it was inconspicuous; the arbitration clause was a separate signed document).

41. 14 Cal. App. 4th 1659 (1993), *cert. denied*, 510 U.S. 1176 (1994).

42. 700 N.E. 2d 859 (Ohio 1998), *cert. denied*, 526 U.S. 1051 (1999).

43. First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938 (1995). *See also supra* Pt. II. The Supreme Court again addressed the issue of arbitrability in Howsam v. Dean Witter Reynolds, 123 S.Ct. 588 (2002) (holding that arbitrators have the sole authority for deciding if claims are eligible for arbitration according to a six-year limit under the rules of the NASD). The Court found that the phrase "question of arbitrability" has a limited scope, applicable in the kind of narrow circumstance where contracting parties would likely have expected a court to have decided the gateway matter. But the phrase is *not* applicable in other kinds of general circumstances where parties would likely expect that an aribtarator would decide the question.

decide if the contract as a whole was fraudulently induced.[44] Similarly, many courts have held that claims that a contract containing an arbitration clause is unconscionable or a contract of adhesion must be resolved in arbitration.[45] However, other courts have refused to submit these issues for arbitration.[46] At least one court has found that the question of whether a claim should be arbitrated depends on which party is requesting the arbitration.[47]

### B. Scope of the Arbitration Provision

Generally, at least in contracts subject to the FAA, ambiguities regarding the scope of an arbitration clause will be resolved in favor of arbitration.[48] However, if the arbitration clause is drafted too narrowly or is determined to be too vague, the dispute may not be sent to arbitration.[49]

In *Sullivan v. Sears*, the arbitration clause stated that the parties agreed to arbitrate claims "arising out of or related to the interpretation, performance or breach of any provision of this agreement." The court held that based on Florida Supreme Court precedent, injury (tort) claims were unrelated to the rights and obligations under the arbitration agreement. The court found no nexus between the dispute and the contract with the arbitration clause and went on to hold that ambiguous provisions of a contract for arbitration will be construed against arbitrating the dispute.

### C. Rights of Non-Signatories

Lenders usually want the flexibility to argue that non-signatories should be included in an arbitration so that they (the lenders) are not brought back into court by way of a third-party complaint filed by the non-signatories. Where the arbitration clause broadly encompasses "the relationships which result from" the contract, a court is more likely to conclude that non-signatories were intended to be covered by the arbitration clause.[50]

In some cases, courts have found non-signatories were compelled to arbitrate.[51] But other courts have held that the non-signatories were not obligated to arbitrate the dispute.[52]

44. *See, e.g.*, Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395, 403-04 (1967); Driscoll v. Smith Barney, Harris Upham & Co., 815 F.2d 655, 659 (11th Cir.), *cert. denied*, 484 U.S. 914 (1987).

45. *See, e.g.*, Green Tree Fin. Corp. v. Randolph, 531 U.S. 79 (2000) (enforcing agreement to arbitrate, though four justices focused on procedural fairness); Rojas v. TK Communications, Inc., 87 F.3d 745, 749 (5th Cir. 1996); Miller v. Drexel Burnham Lambert, Inc., 791 F.2d 850, 854 (11th Cir. 1986) (claim that contract is an adhesion contract is an issue for arbitration); Avena v. Franco, 1992 WL 392619, at 4 (E.D. Pa. Dec. 15, 1992) (plaintiffs' claims that the defendants coerced execution of the contracts must be resolved in arbitration); Nicholson v. CPC Int'l, Inc. 1988 WL 35382, at *2 (D.N.J. Apr. 18, 1988) (plaintiff's assertion that he signed the contract under duress and undue influence was an issue for arbitration), *aff'd*, 877 F.2d 221 (3rd Cir. 1989). *See generally* Woska, *supra* note 1.

46. *See, e.g.*, Circuit City Stores, Inc. v. Adams, 279 F.3d 889 (9th Cir. 2002) (deeming a contract to arbitrate too "one-sided" to enforce under California law despite a U.S. Supreme Court decision in the same case that the Federal Arbitration Act supported enforcement); Penn v. Ryan's Family Steak Houses, Inc., 269 F.3d 753 (7th Cir. 2001) (refusing to enforce an employee arbitration agreement because the company forced the employee to negotiate directly with the provider); Hooters of America, Inc. v. Phillips, 173 F.3d 933 (4th Cir. 1999) (focusing on the costs of arbitration to invalidate the contractual reference); Cole v. Burns Int'l. Security Services, 105 F.3d 1465 (D.C. Cir. 1997) (enforcing a contract to arbitrate but discussing "minimal standards of procedural fairness"); *ACORN*, 211 F.Supp. 2d at 1170 (holding an arbitration clause unconscionable); *Ting*, 182 F.Supp.2d at 928-38 (same), *aff'd*, 319 F.3d 1126 (9th Cir. Feb. 11, 2003); American General Finance, Inc. v. Branch, 793 So. 2d 738 (Ala. 2000) (the determination of whether an arbitration provision is unconscionable is for the court, not the arbitrator, even where the clause specifies "that all issues and disputes as to arbitrability of claims must also be resolved by the arbitrator."); Armendariz v. Foundation Health Psychcare Services. Inc., 24 Cal. 4th 83 (2000) (listing as factors bearing on the lawfulness of mandatory arbitration: discovery availability, neutral arbitrators, relief available, costs, and written award); Engalla v. Permanente Medical Group, Inc., 15 Cal. 4th 951 (1997) (refusing to enforce a contract to submit to an internal procedure controlled by Kaiser Permanente.). *See also supra* note 26.

47. *See* Wells v. Chevy Chase Bank, F.S.B., 768 A.2d 620 (Md. 2001) (arbitration clause did not permit the defendants to compel arbitration because the "claiming party"—meaning the plaintiffs—had to request it. The clause stated in relevant part, "Any controversy or claim…shall, at the request and expense of the claiming party, be submitted to mediation….").

48. *See, e.g.*, Volt Information Sciences, Inc., 489 U.S. 468 at 467, quoting Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 25 (1983); Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 626 (1985) ("intentions are generously construed as to issues of arbitrability"); Optopics Labs. Inc. v. Nicholas, 1997 WL 602750 (E.D. Pa. July 1997) (merger agreement's provision for arbitration of disputes concerning claims for contractual indemnity could not be circumvented by phrasing such a claim in the language of common law fraud); Green v. Bank One, 641 N.E.2d 1207 (Ill. App. Ct. 1994) (agreement stating that any claim "arising out of or relating to this [agreement]" should be submitted to arbitration indicated the parties' desire to submit to arbitration all issues concerning the contract); Green Tree Financial Corporation of Alabama v. Vintson, 753 So. 2d 497 (Ala. 1999) (holding that an arbitration clause that applies to claims "arising out of or relating to" the contract covers intentional torts); Green Tree Financial Corporation v. Shoemaker, 775 So. 2d 149 (Ala. 2000) (compelling arbitration of invasion of privacy and harassment claim pertaining to debt collection efforts); *Ex parte* Waites, 736 So. 2d 550 (Ala. 1999) (finding that whether an invasion-of-privacy claim against an auto dealer is arbitrable was for the arbitrator and not the court pursuant to a clause which covered any disputes "resulting from or arising out of the sale transaction entered into (including but not limited to: the terms of this agreement and all clauses herein contained, their breadth and scope, and any term of any agreement contemporaneously entered into by the parties…." even though the claim arose out of a separate auto sale in which the salesman made a disparaging remark about the plaintiff's credit standing); Carlin Pozzi Architects, P.C. v. Town of Bethel, 767 A.2d 1272 (Conn. 2001) (Under the positive assurances test the court could not determine with positive assurance that the parties intended to exclude issues of timeliness from arbitration. Thus, the court held that the question of the running of the statute of limitations is arguably within the scope of a broad arbitration agreement.). *See also* Wilson v. Wells Fargo Financial Acceptance, 2003 WL 1877336 (M.D. Tenn. Apr. 9, 2003) (finding that the scope of the arbitration agreement ("arising out of or relating to") encompassed discrimination claims).

49. *See, e.g.*, Tracer Research v National Environmental Services, 42 F.3d 1292 (9th Cir. 1994) (clauses that require arbitration of disputes "arising out of" or "arising under" the agreement held limited to contract interpretation and performance issues); Capital Investment Group, Inc. v. Woodson, 694 So.2d 1268 (Ala. 1997) (plaintiff's allegation of fraud did not "arise out of" or "relate to" the contract containing an arbitration clause where the fraud allegedly occurred before the plaintiff entered into the contract); Ryan Warranty Services v. Welch, 694 So.2d 1271 (Ala. 1997) (where the arbitration clause in an auto repair service agreement covered only disagreements concerning "costs," a suit by the car owner against the repair shop for breach of contract and fraud for denying the car owner's claim in its entirety, on the ground that the car owner had not complied with conditions in the repair service agreement, was not arbitrable); *Ex parte* Discount Foods, Inc., 711 So. 2d. 992 (Ala. 1998) (denying arbitration on the ground that an arbitration clause which covered "any controversy or claim between the parties" but did not mention "intentional torts" did not cover the intentional torts alleged by the plaintiff); Fountain Finance, Inc. v. Hines, 788 So. 2d 85 (Ala. 2000) (denying arbitration of an intentional tort claim pertaining to a repossession of an automobile dispute where the arbitration provision covered claims "resulting from or arising out of" the terms of financing the car).

50. *See* Green Tree Financial Corp. v. Lipham, No. 96-D-208-N (M.D. Ala. Sept. 4, 1997).

51. Pritzker v. Merrill Lynch, Pierce, Fenner & Smith, 7 F.3d 1110 (3d Cir. 1993) (an agent of a signatory to an arbitration agreement could invoke an arbitration clause under traditional agency theory even if the agent had not signed the clause); Blount v. National Lending Corporation, 108 F.Supp.2d 666 (S.D. Miss. 2000) (compelling arbitration on a Section 8 RESPA claim against the non-signatory mortgage brokers because the plaintiffs' claims that the lender paid an illegal kickback to the mortgage brokers in relation to the plaintiffs' mortgage closings were allegations of substantially interdependent and concerted misconduct); Smith v. EquiFirst Corp., 117 F.Supp. 2d 557 (S.D. Miss. 2000) (court compelled arbitration against non-signatory mortgage broker where borrowers' claims involved allegations of substantially interdependent and concerted misconduct by broker and lender); Landers v. Crown Pontiac, 2001 WL 1867812 at *2 (N.D. Ala. May 31, 2001) (enforcing an arbitration clause signed by the dealer and customer, in a dispute with the finance company assignee); Chrysler Financial Corp. v. Murphy, 1998 WL 34023394 (N.D. Ala. Aug. 5, 1998) (same); Nissan Motor Acceptance Corp. v. Ross, 703 So.2d 324 (Ala. 1997) (an assignee of a contract has the right to compel arbitration); Universal Underwriters Life Ins. Co. v. Dutton, 736 So. 2d 564 (Ala. 1999) (same); Ohio State Department of Admin. Serv. v. Moody/Nolan Ltd., 2000 WL 1808330 (Ohio App. Dec. 12, 2000) (assignee of subcontracts bound by arbitration clause); Capitol Chevrolet and Imports, Inc. v. Grantham, 784 So. 2d 285 (Ala. 2000) (spouse who did not sign the arbitration agreement was compelled to arbitrate her claims); *In re* FirstMerit Bank, N.A., 52 S.W. 3d 749 (Tex. 2001) (non-signing parties suing on contract were bound by arbitration clause). *See also supra* note 23.

52. *See, e.g.*, Westmoreland v. Sadoux, 299 F. 3d 462 (5th Cir. 2002) (holding that non-signatories to an arbitration agree-

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## D. Statutory Claims

A broad arbitration clause will be found to encompass statutory claims, and there is no prohibition in the FAA against arbitrating statutory claims.[53] But, see *Baron v. Best Buy Co., Inc.*,[54] in which the court suggested that a clause covering "[a]ny claim, dispute, or controversy (whether in contract, tort, or otherwise) arising or relating to this Agreement or the relationships which result from this Agreement…" may not encompass statutory claims.

In general, all federal statutory claims are governed by the FAA unless Congress intended that the FAA not apply. The party opposing arbitration of statutory claims must demonstrate that Congress intended to preclude a waiver of judicial remedies. The objecting party may show such congressional intent by pointing to the statute's text, legislative history, or the existence of an inherent conflict between arbitration and the statute's underlying purpose.[55]

State statutory claims are covered regardless of whether such statutes expressly preclude arbitration.[56]

52. *(Continued from previous page)*

ment cannot move to arbitrate unless the underlying suit involves claims arising from the overall contract or where the alleged wrongdoing implicated both the signatory and nonsignatory); Britton v. Co-Op Banking Group, 4 F.3d 742 (9th Cir. 1993) (holding that when the alleged wrongdoing did not arise from the contract, a non-signatory agent could not invoke the arbitration clause); Wilson v. Waverlee Homes, Inc., 954 F. Supp. 1530 (M.D. Ala. 1997), *aff'd without op.*, 127 F.3d 40 (11th Cir. 1997) (finding that a warrantor (the manufacturer), which was not a party to the retail agreement between the seller and the consumer containing a binding arbitration clause, could not enforce the arbitration clause in a dispute solely between the warrantor and the consumer. Arbitration was denied because the warrantor was neither a party to nor the agent or beneficiary of the contract containing the arbitration clause, and because plaintiff's warranty claims were governed by the Magnuson-Moss Act, which preserves a judicial forum for consumers.); *In re* Knepp., 229 B.R. 821 (N.D. Ala. 1999) (court refused to compel arbitration for a non-signatory); *Ex parte* Isbell, 708 So. 2d 571 (Ala. 1997) (manufacturer lacked standing to enforce seller's arbitration agreement); Universal Underwriters Life Ins. Co. v. Dutton, 736 So. 2d. 564 (Ala. 1999) (same); First Family Fin. Servs., Inc. v. Rogers, 736 So. 2d 553 (Ala. 1999) (same); Med Center Cars, Inc. v. Smith, 727 So. 2d 9 (Ala. 1998) (same); Equifirst Corp. v. Ware, 801 So. 2d 1 (2001) (individual who was not a party to the arbitration clause and was not seeking to enforce the contract containing the arbitration clause was not bound to arbitrate her claims); Oakwood Mobile Homes, Inc. v. Godsey, 824 So.2d 713 (Ala. 2001) (refusing to compel arbitration against a non-signatory plaintiff who was not seeking the benefits of the contract containing the arbitration clause).

53. *See, e.g.*, Kaplinsky and Levin, *supra* note 3.

54. 75 F. Supp. 2d 1368 (S.D. Fla. 1999).

55. *See, e.g.*, Randolph v. Green Tree Financial Corp., 244 F. 3d 814 (11th Cir. 2001) (compelling arbitration of a TILA claim even though it terminated a class action); Stout v. J.D. Byrider, 228 F. 3d 709 (6th Cir. 2000) (compelling arbitration of TILA

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claim), *cert. denied*; Randolph v. Green Tree Fin. Corp., 991 F.Supp. 1410 (M.D. Ala. 1998) (compelling arbitration of TILA and ECOA claims, notwithstanding that such statutes provide for procedural requirements for class action lawsuits), *reversed on other grounds*, 175 F.3d 1149 (11th Cir. 1999); *rev'd in part*, 531 U.S. 79 (2000) (compelling arbitration of a TILA claim, but not reaching the class action issue because it was not reached by the 11th Circuit); Sagal v. First USA Bank, N.A., 69 F. Supp. 2d 267 (D. Del. 1999) (compelling arbitration of a TILA claim, notwithstanding that such statute provides the procedural requirements for class actions), *aff'd*, 254 F.3d 1078 (3d Cir. 2001); Johnson v. First USA, No. 99-0123-E- BLW (D. Idaho Mar. 15, 2000) (compelling arbitration of TILA and RICO claims); Zawikowski v. Beneficial Nat'l. Bank, 1999 WL 35304 (N.D. Ill. Jan. 11, 1999) (compelling arbitration of a TILA class action claim); Lopez v. Plaza Finance Co., 1996 WL 210073 (N.D. Ill. Apr. 25, 1996) (compelling arbitration of a TILA claim, notwithstanding that such statute provides procedural requirements for class actions); Truckenbrodt v. First Alliance Mortg. Co., 1996 WL 422150 (N.D. Ill. July 24, 1996) (court held that it is not a violation of the ECOA if a lender requires a borrower to waive his or her right to sue for a TILA violation, despite the fact that the ECOA prohibits a lender from discriminating against a borrower who attempts to exercise rights granted under the TILA); Goodwin v. Ford Motor Credit Co., 970 F.Supp. 1007 (M.D. Ala. 1997) (compelling arbitration of a TILA claim); Dorsey v. H.C.P. Sales, Inc., 46 F. Supp. 2d. 804 (N.D. Ill. 1999) (compelling arbitration of a TILA claim); Thompson v. Illinois Title Loans, Inc., 2000 WL 45493 (N.D. Ill. Jan. 11, 2000)(compelling arbitration of TILA claims despite procedural requirements pertaining to class actions); Wood v. Cooper Chevrolet, Inc., 102 F.Supp.2d 1345 (N.D. Ala. 2000) (same; also holding that this was no violation of the ECOA); Marsh v. First USA Bank, N.A., 103 F.Supp.2d 909 (N.D. Tex. 2000) (compelling arbitration of TILA and ECOA claims); Brown v. Surety Fin. Serv., Inc., 2000 WL 528631(N.D. Ill. Mar. 23, 2000) (compelling arbitration of TILA claims); Cappalli v. National Bank of the Great Lakes, No. 99-CV-6214 (E.D. Pa. Aug. 22, 2000) (compelling arbitration of a claim under Section 85 of the National Bank Act), *aff'd*, 281 F.3d 219 (3rd Cir. 2001); Blount v. National Lending Corporation, 108 F.Supp.2d 666 (S.D. Miss. 2000) (compelling arbitration of a claim under the Real Estate Settlement Procedures Act (RESPA)); Gray v. WMC Mortgage Corp. and NewSouth Credit Corp., 2000 WL 33706390 (S.D. Miss. June 28, 2000) (same); Smith v. EquiFirst Corporation, 117 F. Supp. 2d 557 (S.D. Miss. Aug. 25, 2000) (same).

*See also*, Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 629 (1985) (compelling arbitration of Federal antitrust claim); Shearson/American Express, Inc. v. McMahon, 482 U.S. 220 (1987), and Rodriguez de Quijas v. Shearson/American Express, Inc., 490 U.S. 477, 484-85 (1989) (both compelling arbitration of federal securities fraud claims); *McMahon*, 482 U.S. 220 at 239-42 (compelling arbitration of a civil RICO claim); Vimar Seguros y Reaseguros S.A. v. M/V Sky Reeler, 515 U.S. 528, 534 (1995) (compelling arbitration of a claim under the Carriage of Goods by Sea Act); Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 26-28 (1991) (compelling arbitration of a claim brought under the Age Discrimination in Employment Act); Williams v. CIGNA Financial Advisors, Inc., 197 F.3d 752 (5th Cir. 1999) (same); Kotam Elecs., Inc. v. JBL Consumer Prods. Inc., 93 F.3d 724 (11th Cir. 1996), *cert. denied*, 519 U.S. 1110 (1997) (compelling arbitration of Sherman Act claim); McWilliams v. Logicon, Inc., 143 F.3d 573 (10th Cir. 1998), and Miller v. Public Storage Mgmt., Inc., 121 F.3d 215 (5th Cir. 1997) (both compelling arbitration of claims under the Americans with Disabilities Act); O'Neil v. Hilton Head Hosp., 115 F.3d 272 (4th Cir. 1997) (compelling arbitration of claims under the Family and Medical Leave Act); Pritzker v. Merrill Lynch, Pierce, Fenner & Smith, 7 F.3d 1110 (3rd Cir. 1993); Kramer v. Smith Barney, 80 F.3d 1080 (5th Cir. 1996); Williams v. Imhoff, 203 F.3d 758 (10th Cir. 2000); Arnulto P. Sulit, Inc. v. Dean Witter Reynolds, 847 F.2d 475 (8th Cir. 1988); Bird v. Shearson Lehman/American Express, Inc., 926 F.2d 116 (2d Cir. 1991) and *In re* Managed Care Litig., 2002 WL 31154945 (S.D. Fla. Dec. 11, 2000) (both compelling arbitration of claims brought under the Employee Retirement Income Security Act); Harter v. Iowa Grain Co., 220 F.3d 338 (9th Cir. Apr. 21, 2000) (compelling arbitration of a claim brought under the Commodity

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Exchange Act); Floss v. Ryan's Family Steak Houses, Inc., 211 F. 3d 306 (6th Cir. 2000) (claims under the Fair Labor Standards Act and Americans with Disabilities Act are arbitrable); Oldroyd v. Elmira Sav. Bank. 134 F.3d 72 (2d Cir. 1998) (compelling arbitration of claims brought under the Financial Institutions, Reform, Recovery and Enforcement Act); Kennedy v. Conseco Fin. Corp., 2000 WL 1760943 (N.D. Ill. Nov. 29, 2000), *as modified by a Jan. 11, 2001 order* (compelling arbitration of a TILA claim); Goetsch v. Shell Oil Company, 97 F.R.D. 574 (N.D.N.C. 2000) (compelling arbitration of a TILA claim); Wood v. Cooper Chevrolet, Inc., 102 F.Supp.2d 1345 (N.D. Ala. 2000) (compelling arbitration of a TILA claim); Herrington v. Union Planters Bank, N.A., 113 F.Supp.2d 1026 (S.D. Miss. 2000) (compelling arbitration of a Truth-in-Savings Act claim); Gray v. Conseco, Inc., 2000 WL 1480273 (C.D. Cal. Sept. 29, 2000) (compelling arbitration of TILA, RESPA and HOEPA claims); Johnson v. Ford Consumer Fin. Co., Inc., Civ. Action No. 4:97-371-24 (D.S.C. June 20 and August 1, 2000) (bench opinions) (compelling arbitration of claims under a South Carolina attorney preference statute).

*But see*, Amaro v. Continental Can Co., 724 F.2d 747 (9th Cir. 1984) (refusing to compel arbitration of ERISA claim); Duffield v. Robertson Stephens & Co., 144 F. 3d 1182 (9th Cir. 1998) (mandatory arbitration clause contained in NASD's U-4 form could not bar the plaintiff from bringing an action under Title VII. Although this case arose in the context of the securities industry, the court made clear that it's ruling related to all mandatory arbitration of statutory claims, except where the parties agree to submit their claims to arbitration after the claims arise), *overruled in* EEOC v. Luce Forward, 303 F.3d 994 (9th Cir 2002), *en banc hrg ordered*, 319 F.3d 1091, 2003 WL 282178 (9th Cir. 2003); Brown v. Trans World Airlines, 127 F.3d 337 (4th Cir. 1997) (mandatory arbitration clause contained in a collective bargaining agreement can bar a plaintiff from bringing a Title VII action, but finding that the particular arbitration clause at issue was not worded broadly enough to cover statutory claims); Johnson v. Tele-Cash, Inc., 82 F. Supp. 2d. 264 (D. Del. 1999) (refusing to compel arbitration of TILA and Electronic Funds Transfer Act claims, based on the inability to obtain class-wide relief in arbitration), *rev'd sub nom* Johnson v. West Suburban Bank, 225 F.3d 366 (3d Cir. 2000), *cert. denied*; and Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 170 F.3d 1 (D. Mass.1998) (mandatory arbitration clause contained in NASD's U-4 form did not bar the plaintiff from bringing an action under Title VII, the ADEA, or state anti-discrimination laws). *Rosenberg* holds the NYSE arbitration an "inadequate forum for the vindication of civil rights claims." *See also* Testerman v. Chrysler Corporation, 1997 WL 820934 (D.C. Cir. Dec. 30, 1997) (mandatory arbitration clause contained in a collective bargaining agreement did not bar the plaintiff from bringing an ADA action where the agreement did not specify that it applied to statutory claims); Hooters of America, Inc. v. Phillips, 39 F. Supp. 2d 582 (D.S.C. 1998) (mandatory arbitration clause contained in an employment agreement fell so far short of "minimally acceptable due process" that the court refused to enforce it as a bar against the employee's Title VII action); Cavanaugh v. Conseco Fin. Servicing Corp. 271 B.R. 414 (Bankr. D. Mass. 2001) (claims based on debtor's assertion of rights arising under the Bankruptcy Code were not subject to arbitration).

56. *See, e.g.*, Lozano v. AT&T Wireless, 216 F.Supp.2d 1071 (C.D. Cal. 2002) ("claims under [California's Consumer Loan Act] and [California Business and Professions Code] § 17200 are subject to arbitration."); Arriaga v. Cross Country Bank, 163 F. Supp. 2d 1189 (S.D. Cal 2001) (FAA preempts § 17200 of the California Business and Professions Code); Republic of the Phillippines v. Westinghouse Elec. Corp., 714 F. Supp. 1362 1373-74 (D. N.J. 1989) (claims under the New Jersey Consumer Fraud Act held arbitrable); Cybul v. Atrium Palace Syndicate, 639 A.2d 1146 (N.J. App. Div. 1994), *cert. denied*, 645 A.2d 140 (1994) (same); Alpert v. Alphagraphics Franchising, Inc., 731 F.Supp. 685, 688 (D.N.J. 1990) (same); Sagal v. First USA Bank, N.A., 69 F.Supp.2d 627 (D. Del. 1999), *aff'd*, 254 F. 3d 1078 (3d Cir. 2001) (Delaware Consumer Fraud Act); *In re* Conseco Finance Servicing Corp., 19 S.W.3d 562 (Tex. 2000) (claims under Texas Debt Collection Act and Texas Deceptive Trade Practices Act); Westendorf v. Gateway 2000, Inc., 763 A.2d 92 (Del. Supr. 2000), *aff'd*, 2000 WL 307369

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## IX. Whoever First Demands Arbitration May Choose to Proceed Under the Applicable Rules of the American Arbitration Association, or its Successor, or the Applicable Rules of JAMS, or its Successor, or the Applicable Rules of the National Arbitration Forum, or its Successor

### A. In General

The U.S. Supreme Court has held that parties may specify by contract the rules under which arbitration will be conducted.[57]

In addition, courts have refused to find an arbitration clause invalid solely because it does not specify procedures or rules for arbitration.[58]

### B. Neutrality

Using a national arbitration organization reduces the likelihood that a self-administered program will be found to be prejudiced. In *Engalla v. Permanente Med. Group, Inc.*,[59] the arbitration petition, brought by a large health maintenance organization, Permanente Medical Group, Inc., was denied by California's Supreme Court because Permanente's self-administered arbitration program was alleged to be corrupt, biased, and the result of inadequate disclosure to the program's participants.

On the other hand, Judicial Arbitration and Mediation Service (JAMS) and the National Arbitration Forum (NAF) operate on a for-profit basis, and are therefore potentially susceptible to alleged conflicts of interest when dealing with corporations that frequently use their services and provide the source of their income. The American Arbitration Association (AAA) is a non-profit organization, and therefore may be less vulnerable to such a charge. However, it is difficult to measure the seriousness of this issue.

One court refused to compel arbitration because the defendants failed to demonstrate that the NAF is a neutral, inexpensive and efficient forum.[60] The court reasoned that "it is unclear what procedures the NAF would apply to this dispute given the changing nature of the rules they adopt and the almost total discretion of the director [of the NAF] to issue or modify any award or rule." The reasoning of the *Baron* opinion was rejected, however, in *Marsh v. First USA Bank, N.A.*:[61] "Aside from the plaintiffs' conclusory allegations, there is no evidence whatsoever that they would be unfairly treated by an arbitrator." NAF procedures have been widely found to be fair and reasonable by many other courts.[62]

Questions may still arise regarding the relationship between the corporation and the most neutral arbitration organization.[63] The Sixth Circuit queried whether Employment Dispute Services, Inc. (EDSI) was suitable for the resolution of statutory claims "in light of the uncertain relationship between the employer and EDSI....Though the record does not clearly reflect whether EDSI, in contrast to the American Arbitration Association, operates on a for-profit basis, the potential for bias exists."[64]

In California, the Legislature has passed or considered a series of bills aimed at regulating arbitrators in consumer cases. The most extreme bill (AB 3029) would have allowed the consumer to reject a pre-selected arbitation service, but this was vetoed by the governor. The other four bills would: require that private judging companies disclose basic data regarding their involvement in, and the outcome of, mandatory consumer arbitration (AB 2656); prohibit private judging companies from serving in consumer arbitrations involving parties with whom they have a financial interest or relationship (AB 2574); prohibit neutral arbitrators or private arbitration companies from conducting mandatory consumer arbitration where the contract or rule provides that the consumer must pay a business' fees and costs (including the arbitrator's fees and costs), if it prevails, and implement a fee waiver policy for indigent consumers (AB 2915); and provide for disqualification of a judge who has a current arrangement concerning prospective employment as an arbitrator or, within the last two years has participated in discussions regarding prospective employment as an arbitrator if the arrangement or discussion was with

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(Del. Ch. Mar. 16, 2000) (same); Munoz v. Green Tree Fin. Corp., 542 S.E. 2d 360 (S. Car. 2001) (South Carolina Consumer Protection Code).

*But see* Broughton v. Cigna Healthplans, 21 Cal. 4th 1066 (1999) (refusing to compel arbitration of a claim for equitable relief asserted under the California Consumer Legal Remedies Act); Coast Plaza Doctors Hosp. v. Blue Cross of Calif., 83 Cal. App. 4th 677 (2000) (refusing to compel arbitration of a claim for equitable relief asserted under California's unfair competition law, California Business and Professions Code, §§ 17200 *et seq.*); Groom v. Health Net, 82 Cal. App. 4th 1189, 1199 (2000) (same); Gray v. Conseco, Inc., 2000 WL 1480273 (C.D.Cal. Sept. 29, 2000) (ordering arbitration of all claims, except for injunction, under Business and Professions Code § 17200), *modified by* Gray v. Conseco, Inc., 2001 WL 1081347 (C.D.Cal. Sept. 6, 2001) (holding arbitration would be on an individual rather than a class basis and while the § 17200 injunctive claim was stayed); and Cruz v. PacifiCare Health Systems, Inc., 30 Cal. 4th 303 (2003) (holding that injunctive relief claims under § 17200 could not be arbitrated, but that restitution and disgorgement claims under § 17200 are arbitrable).

57. *See* Volt Information Sciences, Inc. v. Board of Trustees of Leland Junior Stanford Univ., 489 U.S. 468 at 479 (1989).

58. *See, e.g.*, Federal Deposit Ins. Corp. v. Air Florida Sys. Inc., 822 F.2d 833, 842 (9th Cir. 1987), *cert. denied*, 485 U.S. 987 (1988); Wailua Assoc. v. Aetna Cas. & Sur. Co., 904 F. Supp. 1142, 1148-49 (D. Haw. 1995).

59. 15 Cal.4th 951 (1997).

60. Baron v. Best Buy Co., Inc., 75 F.Supp. 2d 1368 (S.D. Fla. 1999).

61. 103 F.Supp. 2d 909, 925 (N.D. Tex. 2000).

62. *See, e.g.*, Green Tree Financial Corp. v. Randolph, 531 U.S. 79 (2000) (Ginsburg, J, concurring in part and dissenting in part, joined in by Stevens, J, Souter, J and Breyer, J); Johnson v. West Suburban Bank, 225 F.3d 366, 374 n.2 (3d Cir. 2000); Gammaro v. Thorp Consumer Discount Co., 15 F.3d 93, 97 (8th Cir. 1994); Bank One v. Coates, 125 F.Supp. 2d 819 (S.D. Miss. 2001); Lloyd v. MBNA America Bank, N.A., 2001 WL 194300, at 3 (D. Del. Feb. 22, 2001); Western v. ITT- CFC, 1992 WL 473846, at 4 (N.D. Tex. Dec. 3, 1992); DiCrisci v. Lyndon Guaranty Bank of NY, 807 F.Supp. 947, 954 (S.D.N.Y. 1992); ITT Commercial Finance Corp. v. Wangerin, 1995 WL

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434459, at 2 (Minn. Ct. App. July 25, 1995). *Contra*: Patterson v. ITT Consumer Financial Corp., 14 Cal. App. 4th 1659 (1993) (NAF consumer arbitration program held to the unconscionable and unenforceable).

63. *See* Hayes v. County Bank, 713 N.Y.S. 2d 267 (2000) (court ordered the lender to respond to a discovery request pertaining to its relationship with the NAF).

64. Floss v. Ryan's Family Steak Houses, Inc., 211 F. 3d 306 (6th Cir. 2000).

a party to the proceeding or when the proceeding involves an issue related to arbitration (AB 2504).

## X. Whichever Rules Are Chosen, the Arbitrator Shall Be an Attorney or Retired Judge and Shall Be Selected in Accordance with the Applicable Rules

It is important that the chosen arbitrator will be a neutral and impartial party to the proceedings. In *Hooters of America, Inc. v. Phillips*,[65] the Fourth Circuit U.S. Court of Appeals held that Hooters had breached its contract and the implied covenant of good faith and fair dealing by adopting an arbitration procedure that, among other provisions, required that all arbitrators be selected from a Hooters list.

A challenge to the arbitrator's impartiality cannot be made until the conclusion of the arbitration, as illustrated in *Vera v. First USA Bank, N.A.*[66]

## XI. The Arbitrator Shall Apply the Law in Deciding the Dispute

In federal court cases under the FAA, the arbitration award will be granted when the applicable law is not manifestly disregarded and the basis for the award is not ambiguous.[67] The arbitrator's decision will be overruled when a well-defined law is ignored.[68] However, the outcome may be different in a state court, even where the FAA is the governing statute.[69]

Arbitration awards are presumed to be valid and courts may not substitute their judgment for that of the arbitrator selected by the parties.[70] But given the Second Circuit's opinion in *Halligan v. Piper Jaffray, Inc.*,[71] where the overwhelming evidence of age discrimination, the agreement that the arbitrators were informed of the law, and the lack of a written opinion, indicated the award was in manifest disregard of the law or facts, it is advisable to require arbitrators to follow the applicable substantive law.[72]

## XII. Unless the Rules Provide Otherwise, the Arbitration Award Shall Be Issued Without a Written Opinion

The FAA does not require written findings and conclusions, and compelling the arbitrator to provide them could affect the course of an appeal. Under the FAA, the grounds for appealing an arbitrator's award are very limited; one such ground is that the arbitrator exceeded his or her powers.[73] Some courts also review an award if the arbitrator "manifestly disregarded the law."[74] Having written findings and conclusions may assist one side or the other in arguing that the arbitrator did (or did not) exceed his or her authority or manifestly disregard the law.[75]

The AAA advises its commercial arbitrators to give no written explanation for their decisions, in order to make an appeal to the courts less likely.[76] Similarly, the NAF Code of Procedure provides that an award will not include any reasons, findings of fact, or conclusions of law unless required by the parties before the hearing.[77] JAMS, however, stipulates that the award will contain a concise written statement of the essential findings and conclusions on which the award is based.[78]

The California Supreme Court has held that "in order for such judicial review to be successfully accomplished, an arbitrator in a [California Fair Employment and Housing Act] case must issue a written arbitration decision that will reveal, however briefly, the essential findings and conclusions on which the award is based."[79]

In *Halligan v. Piper Jaffray, Inc.*,[80] the Second Circuit U.S. Court of Appeals noted the significance of a written opinion: "We want to make clear that we are not holding that arbitrators should write opinions in every case or even in most cases. We merely observe that where a reviewing court is inclined to find that arbitrators manifestly disregarded the law or the evidence and that an explanation,

65. Similar results were reached in Cheng-Canindin v. Renaissance Hotel Assocs., 50 Cal. App. 4th 676, 677-78 (Cal. Ct. App. 1997) (arbitration chaired by manager of hotel, with other members of hotel management as arbitrators); Ditto v. RE/MAX Preferred Properties, 861 P.2d. 1000 (Okla. App. 1993) (arbitrators selected by realty company from a pool of its realtors). *But see* 256 Woods v. Saturn Distribution Corp., 78 F.3d 424 (9th Cir.), *cert. denied*, 518 U.S. 1051 (1996) (upholding the validity of a clause in which the arbitrators would be two Saturn dealers and two Saturn employees).

66. 2001 WL 640979 (D. Del. Apr. 19, 2001).

67. Possehl Inc. v. Shanghai Hia Xing Shipping, 2001 WL 214234 (S.D.N.Y. Mar. 1, 2001).

68. Capo v. Bowers, 2001 WL 210359 (S.D.N.Y. Mar. 2, 2001).

69. Moncharsh v. Heily & Blase, 3 Cal. 4th 1 (1992) (holding that arbitration awards are not reviewable even for errors of law); Crowell v. Downey Community Hospital Foundation, 95 Cal. App. 4th 730 (2002) (same).

70. Herrendeen v. Daimler Chrysler Corp., 2001 WL 304843 (Ohio Ct. App. Mar. 30, 2001).

71. 148 F.3d 197 (2d Cir. 1998).

72. For more case law relating to the reviewability of an arbitrator's decision, *see also*: Bertha A. Harris et al. v. Parker College of Chiropractic, 286 F. 3d 790 (5th Cir. 2002) (when courts review awards issued under binding arbitration agreements with ambiguous language regarding judicial review, the review should be limited to "pure" questions of law rather than mixed questions of law and fact); Lapine Technology Corp. v. Kyocera Corp., 130 F.3d 884 (9th Cir. 1997) (federal courts can expand their review of an arbitration award beyond the limited grounds specified in the FAA if the parties have so agreed); Syncor Int'l. Corp. v. McLeland, 120 F.3d 262 (4th Cir. 1997), *cert. denied*, 522 U.S. 1110 (1998) (same); Gateway Tech's, Inc. v. MCI Telecom Corp., 64 F.3d 993, 996-97 (5th Cir. 1995) (same); New England Utilities v. Hydro-Quebec, 10 F. Supp. 2d 53 (D. Mass. 1998) (same); and Fils et Cables d'Acier de Lens v. Midland Metals Corp., 584 F. Supp. 240, 244 (S.D.N.Y. 1984) (same). *But see* Chicago Typographical Union v. Chicago Sun-Times, 935 F.2d 1501, 1505 (7th Cir. 1991) (parties are not free to contract for judicial review of an arbitrator's decision or award); UHC Mgmt. Co., Inc. v. Computer Sciences Corp., 148 F.3d 992 (8th Cir. 1998) (FAA precludes review of arbitrator's decision for errors of law); and Strogh Container Co. v. Delphi Indus., Inc., 783 F.2d 743 (8th Cir. 1986) (court indicated that it was not clear whether the parties may confer on a court the right to review an arbitrator's decision for errors of law).

73. 9 U.S.C. § 10(a).

74. *See, e.g.*, Merrill Lynch v. Bobker, 808 F.2d 930 (2d Cir. 1986).

75. *See supra* note 72.

76. *See* AAA Guide for Commercial Arbitrators, *available at* http://www.adr.org/index2.1_jsp?JSPssid=13758.

77. *See* Rule 37(g), *available at* http://www.arb-forum.com/arbitration/NAF/code.asp.

78. *See* JAMS Policy on Consumer Arbitrations Pursuant to Pre-Dispute Clauses, Minimum Standards of Procedural Fairness, Standard 9, *available at* http://www.jamsadr.com/consumer_arb_std.asp. "A concise written statement of the essential findings and conclusions on which the award is based" need not be a detailed "written opinion." *Id.*

79. Armendariz v. Foundation Health Psychcare Servs, Inc., 24 Cal. 4th 83, 107 (2000).

80. 148 F. 3d 197 (2d Cir. 1998).

if given, would have strained credulity, the absence of explanation may reinforce the reviewing court's confidence that the arbitrators engaged in manifest disregard."

Another issue to consider is the additional cost and time required when written findings and conclusions are issued. Given that the speed and relative inexpensiveness of arbitration are considered to be among its major benefits, requiring detailed written opinions erodes some of the advantages arbitration has over litigation.

## XIII. The Arbitration Hearing Shall Be Conducted in the Federal District in Which You Reside

Most courts have upheld arbitration clauses specifying distant locations and have concluded that the FAA preempts state statutes invalidating such clauses.[81] Other courts, however, have denied arbitration when the rules provide for a distant location.[82] Requiring arbitration hearings to take place in the federal judicial district of the consumer's residence may curtail allegations of overreaching by a business and preempt any argument by consumers that they are required to travel unreasonably far distances to arbitrate a claim.

## XIV. If You Demand Arbitration First, You Will Pay the Claimant's Initial Arbitration Fling Fees or Case Management Fees Required by the Applicable Rules up to $125, and We Will Pay Any Additional Initial Filing Fee or Case Management Fee. We Will Pay the Whole Filing Fee or Case Management Fee if We Demand Arbitration First. We Will Pay the Arbitration Costs and Fees for the First Day of Arbitration, up to a Maximum of Eight Hours. The Arbitrator Shall Decide Who Shall Pay Any Additional Costs and Fees

### A. Fees Found Unconscionable

Consumers sometimes contend that an arbitration clause is unconscionable because it imposes an unreasonable financial burden and effectively denies them an affordable forum. Some courts will refuse to enforce an arbitration clause that is silent as to fees.[83]

The U.S. Supreme Court addressed the issue in *Green Tree Financial Corp.—Alabama v. Randolph*.[84] The Supreme Court held that borrower failed to meet the burden of establishing that the arbitration would be prohibitively expensive where the arbitration clause was silent on the arbitration fees that would be borne by the borrower and the borrower failed to develop a record on this subject.[85]

Other courts may invalidate an arbitration clause based on its specified fee structure.[86] A few courts have forced the business to pay the costs of claims filed against them.[87]

81. *See, e.g.*, Carnival Cruise Lines, Inc. v. Shute, 499 U.S. 585 (1991) (upholding the validity of a forum selection clause); Scherk v. Alberto-Culver Co., 417 U.S. 506 (1974) (calling an arbitration provision "a specialized kind of forum selection clause."); KKW Enters., Inc. v Gloria Jean's Gourmet Coffees Franchising Group, 184 F.3d 42, 50- 52 (1st Cir. 1999); Doctor's Assocs., Inc. v. Hamilton, 150 F.3d 157, 163 (2d Cir. 1998), *cert. denied*, 525 U.S. 1103 (1999); Management Recruitors Int'l v. Bloor, 129 F.3d 851, 856 (6th Cir. 1997); M.C. Constr. Corp. v. Gray Co., 17 F.Supp. 2d 541, 547-49 (W.D. Va. 1998); and Alphagraphics Franchising, Inc. v. Whaler Graphics, Inc., 840 F.Supp. 708, 710 (D. Ariz. 1993).

82. *See* Patterson v. ITT Consumer Financial Corp., 14 Cal. App. 4th 1659 (1993) (arbitration denied because, among other things, the arbitration rules selected by ITT appeared to require that all arbitrations take place in a distant forum); Bolter v. The Superior Court of Orange County, 87 Cal.App.4th 900 (2001) (invalidating a forum selection provision); Keystone, Inc. v. Triad Sys. Corp., 971 P.2d 1240 (Mont. 1998) (arbitration denied because proceeding was to be held at a distant location).

83. *See, e.g.*, Lozada v. Dale Baker Oldsmobile, Inc., 91 F.Supp. 2d 1087 (W.D. Mich. 2000) (stating in dictum that an arbitration clause which made no provision for the payment of arbitration costs was unconscionable); Crawford v. Cavalier Homes of Alabama, Inc., No. 98-V-641 (State Court of Carroll County, Georgia July 6, 1999) (court invalidated a clause because the arbitration fees that the consumer could be forced to pay were not disclosed in the arbitration provision or any other document provided to the consumer at the point of sale and such costs ($1,250 filling fee, $150 daily administrative fee, and arbitrator's fees varying between $100 per hour and $1,000 per day) were significantly larger then court filing fees), *rev'd sub nom;* Results Oriented, Inc. v. Crawford, 538 S.E. 2d 73 (Ga. 2000) (finding that Crawford having denied any knowledge of any arbitration requirement at all had no idea of the costs of arbitration at the time of signing the documents and therefore had no ground for asserting unconscionability), *aff'd*, 548 S.E. 2d 342 (Ga. 2001); Myers v. Terminex Int'l, 697 N.E. 2d 277 (Ohio 1998) (rejecting an arbitration clause based on the fact that the amount of the filing fee was not discussed in the clause and exceeded the amount the consumer paid for the services).

84. 531 U.S. 79, 88-91 (2000).

85. *See also, ACORN*, 211 F.Supp.2d at 1173 (holding an arbitration clause unconscionable because of, among other things, its cost); *Ting*, 182 F.Supp.2d at 933-34 (same); Kaplinsky and Levin, *supra* note 26.

86. *See, e.g.*, Webb v. Investacorp, Inc., 89 F.3d 252, 255-59 (5th Cir. 1996); Rollins, Inc. v. Foster, 991 F. Supp. 1426, 1439 (M.D. Ala. 1998) (holding that the cost barrier for arbitration, together with the difficulty of finding counsel to press consumer cases in arbitration, may, if proven in a particular case, be sufficient to strike down an arbitration clause); Pitchford v. Oakwood Mobile Homes, Inc., No. 5: 99 CV 00053 (W.D. Va. Dec. 20, 1999) (Report and Recommendation of Magistrate) (invalidating an arbitration agreement because the consumer could be required to pay arbitration fees in excess of $1,000 for a claim over $200,000 where the ability to use the AAA's fee waiver provision for indigency was unclear), *aff'd*, 2000 WL 1728642 (W.D. Va. Nov. 13, 2000); *In re* Knepp, 229 B.R. 821, 838 (Bankr. N.D. Aia. 1999) (holding an arbitration clause to be unconscionable when the plaintiff in a Chapter 13 adversary proceeding could not afford to pay for arbitration, and finding it oppressive to a debtor seeking a fresh start to be required to pay initial fees for arbitration ranging from $500 to $7,000 and daily costs of hundreds of dollars); *Matter of* Teleserve Systems, Inc., 230 A.D. 2d 585 (N.Y. 1997); Sosa v. Paulos, 924 P.2d 357, 361-63 (Utah 1996) (holding unconscionable a provision in an arbitration agreement requiring a patient to pay the doctor's attorneys' fees even if the doctor lost the malpractice arbitration); Carole Ring & Assoc. v. Nicastro, 87 Cal. App. 4th 253 (2001) (a contract allowing for fees in arbitration is not binding in arbitration or in court); Williams v. Aetna Finance (700 N.E. 2d 859 Ohio 1998), *cert. denied*, 526 U.S. 1051 (1999) (striking down a clause which required the consumer to pay large fees simply to advance a case to arbitration); Patterson v. ITT Consumer Fin. Corp., 14 Cal. App. 4th 1659 (1993) (denying arbitration because, among other things, the arbitration rules selected by ITT required consumers to pay substantial filing and hearing fees); Brower v. Gateway 2000 Inc., 676 N.Y.S. 2d 569, 574 (N.Y. App. Div. 1998) (holding that the excessive cost entailed in arbitrating a $1,000 claim before the International Chamber of Commerce ($4,000, $2,000 of which is non-refundable even if the consumer prevails, for a claim of less than $50,000) is unreasonable.

For a discussion of the unique issues that can arise when seeking to enforce an arbitration clause in a bankruptcy case, *see* George J. Wallace, Gary D. Hammond, Jeffrey E. Tate, and Alvin C. Harrell, *Bankruptcy Update—Developing Issues*, 58 Bus. Law 1323 (2003).

87. *See, e.g.*, Diaz v. Josephthal Lyon & Ross, Inc., 1998 U.S. Dist. LEXIS 22204 (S.D. N.Y. 1998) (directed securities firm to pay the arbitrator's fees in full because it was standard industry practice); Solieri v. Ferrovie Dello Stato SPA, 1998 WL 419013 (S.D. N.Y. 1998) (court ordered tour company to pay $2,000 arbitration filing fee of a financially distressed widow); Wood v. Cooper Chevrolet, Inc., 102 F.Supp.2d 1345 (N.D. Ala. 2000) (following the 11th Circuit opinion in *Randolph* and refusing to compel arbitration of TILA claims unless the defendant agrees to pay the arbitration fees and its own attorney fees without seeking reimbursements; not enough just to advance fees); Smith v. EquiFirst Corporation, 117 F. Supp. 2d 557 (S.D. Miss. Aug. 25, 2000) (compelling arbitration of a clause providing that the lender would advance the first $150 of the filing fee, with the arbitrator to determine who should finally be responsible for the cost of arbitration); Kennedy v. Conseco Fin. Corp., 2000 WL 1760943 (N.D. Ill. Nov. 29, 2000) (rejecting the challenge to an arbitration clause requiring the consumer to pay the arbitration fees, because Conseco agreed in its reply brief to pay 100% of the arbitration fees if

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### B. Fees Found Acceptable

Most courts have refused to presume that an arbitrator would impose unreasonable fees when the arbitration clause is silent with respect to fees.[88]

Numerous courts have also rejected arguments of unconscionability as a result of prohibitive fees and have instead compelled arbitration.[89]

### C. Employment Arbitration Cases

Several employment arbitration cases have refused to enforce agreements requiring the employee-claimant to pay fees.[90]

However, in *Bradford v. Rockwell Semiconductor Systems, Incorporated*,[91] the court upheld a 50-50 fee-splitting arrangement with respect to an employee's arbitration of an ADEA claim resulting in the employee's payment of $4,470.88: "[T]he appropriate inquiry is one that evaluates whether the arbitral forum in a particular case is an adequate and accessible substitute to litigation, *i.e.*, a case-by-case analysis that focuses, among other things, upon the claimant's ability to pay the arbitration fees and costs, the expected cost differential between arbitration and litigation in court and whether that cost differential is so substantial as to deter the bringing of claims." And in *Arakawa v. Japan Network Group*, the court declined to invalidate an arbitration agreement that required an employee of a broadcasting company to split the fees and costs of

87. *(Continued from previous page)*

the consumer asked to be paid for such fees); Quinn v. EMC Corp., 109 F.Supp. 2d 681, 685-86 (S.D. Tex. 2000) (remedy for exorbitant fees is to require the company to pay, not to invalidate the arbitration provision); Smith v. Creative Res., 1998 WL 808605, at 3 (E.D. Pa. Nov. 23, 1998) (same); Woska, *supra* note 1.

88. *See e.g.*, Sydnor v. Conseco Financial Servicing Corporation, 252 F. 3d 302 (4th Cir. 2001); *accord* Koveleskie v. SBC Capital Markets, Inc., 167 F.3d 361 (7th Cir. 1999) (rejecting the argument that the arbitration clause was invalid because of potentially high arbitration fees); Rosenberg v. Merrill Lynch, Pierce, Fenner, Smith, Inc., 170 F.3d 1 (1st Cir. 1999) (rejecting an argument that the NYSE's arbitration procedures were unconscionable merely because the plaintiffs could be charged fees "which may be as high as $3,000 per day and tens of thousands of dollars per case," and concluding that the mere possibility of a negative outcome in a particular case does not invalidate arbitration); Sankey v. Sears, Roebuck and Company, 100 F. Supp. 2d 1290 (M.D. Ala. June 8, 2000) (court compeled arbitration of a clause that was silent as to who pays fees since, unlike the Eleventh Circuit opinion in *Randolph*, the case did not involve statutory claims); Howard v. Anderson, 36 F. Supp.2d 183 (S.D.N.Y. 1999) (court enforced an arbitration clause because the plaintiff "failed to present evidence that fees have been demanded of her at this time. Ultimately, [plaintiff] may not be responsible for any fees."); Palm Harbor Homes, Inc. v. Turner, 796 So. 2d 295 (Ala. 2001) (following the U.S. Supreme Court opinion in *Green Tree v. Randolph*); Woska, *supra* note 1; Kaplinsky and Levin, *supra* note 26.

89. *See, e.g.*, Doctor's Assocs., Inc. v. Hamilton, 150 F.3d 157 (2nd Cir. 1998) (following *Stuart, infra*, and rejecting the claim that a clause is invalid because the franchisee will be required to pay one-half of AAA's fees or $28,000 - $32,000); Hill v. Gateway 2000, 105 F.3d 1147 (7th Cir. 1997) (rejecting the consumer's claim that it was unfair to require the consumer to pay at least $2,000 in costs to resolve a complaint about a home computer); Doctor's Assocs., Inc. v. Stuart, 85 F.3d 975, 980 (2nd Cir. 1996) (rejecting the defendant's argument that the arbitration clause was unconscionable because, among other things, the clause did not disclose that the AAA charges as much as $5,000 for filing and administrative fees; Dorsey v. H.C.P. Sales, Inc., 46 F. Supp. 2d 804 (N.D. Ill. 1999) (holding that the court's job was not to evaluate the costs of arbitration on a case-by-case basis when determining whether it must compel arbitration); Wirdzek v. Monetary Mgmt., Inc., 1999 WL 688100 (E.D. Cal. May 25, 1999) (finding no unconscionability in a clause which may have resulted in the administrative costs being higher than the plaintiff's claim); Howard v. Anderson, 36 F.Supp.2d 183 (S.D.N.Y. 1999) (upholding an arbitration clause with a $500 filing fee where the plaintiff earned approximately $50,000 per year); Universal Underwriters Life Ins. Co. v. Dutton, 736 So. 2d. 564 (Ala. 1999) (holding that the trial court erred in shifting the burden of paying the arbitration filing fee from the consumer to the auto dealer); Broemmer v. Otto, 821 P.2d 204, 209 (Ariz. Ct. App. 1991) (rejecting an unconscionability claim based on the argument that AAA's fees were oppressive), *approved in part vacated*, 840 P.2d 1013 (Ariz. 1992); First Family Financial Services, Inc. v. Rogers, 736 So. 2d. 553 (Ala. 1999) (plaintiff presented insufficient evidence of financial hardship to render clause unconscionable); Wells v. Chevy Chase Bank, F.S.B., No. 24-C-99-000202 (Cir. Ct. Balt. City Aug. 16, 1999) (court rejected the plaintiff's claim that an arbitration clause was unconscionable because it required the plaintiff to pay

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excessive AAA fees that would equal or exceed the plaintiff's claim and cited the modest fees charged by AAA ($125 plus $100 for a telephonic hearing)), *rev'd on other grounds*, Wells v. Chevy Chase Bank, F.S.B., 768 A.2d 620 (Md. 2001); Commercial Credit Corp. v. Leggett, 744 So. 2d. 890 (Ala. 1999) (holding that the arbitration provision which required the consumer initiating arbitration to pay a $125 filing fee with the defendants obligated to pay the remaining fees for a one day (8 hour) hearing, regardless of the outcome, and with the losing party to pay the balance of the fees, was not unconscionable); *Ex parte* Dan Tucker Auto Sales, Inc., 718 So.2d 33 (Ala. 1998) (financial hardship, standing alone, is an insufficient basis to invalidate an arbitration agreement); Green Tree Fin. Corp. v. Wampler, 749 So.2d 409 (Ala. 1999) (same); Parkway Dodge, Inc. v. Yarbrough, 779 So. 2d 1205 (Ala. 2000) (same); *Ex parte* Foster, 758 So. 2d 516 (Ala. 1999) (same); Johnnie's Homes, Inc. v. Holt, 790 So. 2d 956 (Ala. 2001) (same, despite evidence indicating that the consumer would have to pay a $2,000 fee); A.P. Brown Co. v. Superior Court in and for Pima County, 490 P.2d 867 (Ariz. 1971) (same); Colquitt v. First USA Bank, N.A., 808 So. 2d 1018 (Ala. 2001) (refusing to overturn the trial court' order compelling arbitration notwithstanding the consumer's argument that the cost of arbitrating was nine times that of litigating in court).

*See also* Williams v. CIGNA Financial Advisors, Inc., 197 F.3d 752, 764-65 (5th Cir. 1999) (compelling arbitration of a claim under the Age Discrimination in Employment Act despite fact that the arbitrators required the plaintiff to pay half of the arbitration fees); Stout v. J.D. Byrider, 50 F. Supp. 2d. 733 (N.D. Ohio 1999) (compelling arbitration despite fact that the consumer would be required to pay AAA fees), *aff'd*, 228 F.3d 709 (6th Cir. 2000); Hale v. First USA Bank, N.A. 2001 WL 687371 (S.D.N.Y. June 12, 2001) (arbitration clause in credit card contract requiring plaintiff to pay $124 in arbitration fees was enforceable); Palmer-Scopetta v. Metropolitan Life Ins. Co., 37 F. Supp. 1364 (S.D.N.Y. 1999) (court enforced arbitration clause, concluding that the plaintiff could later seek judicial review of any unreasonable fee); Goodman v. ESPE America, Inc., 2001 WL 64749 (E.D. Pa. Jan. 25, 2001) (court upheld "loser pays" doctrine, *i.e.*, prevailing party is entitled to an award that includes all costs of arbitration, including reasonable attorney's fees); Brown v. Surety Fin. Service, Inc., 2000 WL 528631 (N.D. Ill. Mar. 23, 2000) (compelling arbitration of a consumer small claim under the AAA Commercial Arbitration Rules because of the safeguards protecting plaintiffs from inordinate arbitration costs, like Rule 51, which provides for waiver of filing and administrative fees in cases of extreme hardship and final apportionment by the arbitrator, and Rules 52 and 53, which provide for the assessment of arbitration fees against any party and for the arbitrator to serve without compensation for the first day); Blount v. National Lending Corp., 108 F.Supp.2d 666 (S.D. Miss. 2000) (compelling arbitration of a RESPA claim despite the fact that the arbitration agreement stated that each party was to bear its own costs and attorneys fees, since RESPA does not entitle the plaintiffs to costs and attorneys fees, but only states that the court may award costs and fees to the prevailing party, and since the AAA rules state that filing fees may be deferred in the case of extreme hardship and that the arbitrator may assess fees and expenses in such amounts as the arbitrator determines is appropriate); Smith v. EquiFirst Corp., 117 F. Supp. 2d 557 (S.D. Miss. Aug. 25, 2000) (same result as to NAF); Sobol v. Kidder, Peabody & Co., Inc., 49 F. Supp. 2d 208 (S.D.N.Y. 1999) (upholding an arbitrator's decision that the plaintiff, a securities industry employee, pay a $25,000 arbitration fee); Walker v. MDM Servs. Corp., 997 F.Supp. 822, 826 (W.D. Ky. 1998) (compelling arbitration because the plaintiff never proved that she would be required to pay the fees and where the rules enabled her to recover her costs); Ahing v. Lehman Brothers, Inc., 2000 WL 460443 at 13 (S.D.N.Y. Apr. 18, 2000) (upholding a fee-splitting provision); Cline v. H.E. Butt Grocery Co., 79 F.Supp.2d 730, 733 (S.D. Tex. 1999) (same); Victoria's Secret Stores, Inc. v. Epstein Contracting, Inc., 2001 WL 224515 (Ohio Ct. App. Mar. 8, 2001)

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(arbitrator's award of attorney fees upheld due to rational nexus between the parties' agreement and the award).

90. *See, e.g.*, Paladino v. Avnet Computer Techs., Inc., 134 F.3d 1054, 1062 (11th Cir. 1998) (invalidating a clause calling for arbitration of an employment discrimination claim under Title VII of the Civil Rights Act of 1964, where the employee would be required to pay a $2,000 filing fee and half of the arbitrator's fee); Circuit City Stores, Inc. v. Adams 279 F. 3d 889 (9th Cir. 2002) (finding the employment arbitration agreement unenforceable due to cost concerns, the one-sided nature of the agreement, and limitations on remedies); Maciejewski v. Alpha Systems Lab, Inc., 986 P.2d 170 (4th Dist. 1999) (denying a motion to compel arbitration, based in part on the fees to be borne by the employee); Shankle v. B-G Maintenance Management of Colorado, Inc., 1997 WL 416405, at 4 (D. Colo. 1997) (denying the employer's motion to compel arbitration because the employee was required to pay half of the arbitrator's fee of between $1,875 and $5,000, even if the employer initially "advanced" the employee's share), *aff'd*, 163 F.3d 1230 (10th Cir.1999); Horenstein v. Mortgage Market Inc., 1999 U.S. Dist. LEXIS 21463 (D. Ore. Jan. 11, 1999) (same); Davis v. LPK Corp, 1998 U.S. Dist. LEXIS 3504 (N.D. Cal. 1998) (denying the employer's motion to compel arbitration which would have cost the employee $2,000 per day); Zumpano v. Omnipoint Communications, 2001 WL 43781 (E.D. Pa. Jan. 18, 2001) (upholding an arbitration provision that required the former employee to potentially bear large fees, particularly since the former employer had shown that it was willing to consider paying such fees; in any event, the appropriate remedy in a situation involving exorbitant fees is not to nullify the arbitration clause but rather to require the employer to pay the fees); Cole v. Burns Int'l Security Servs., 105 F.3d 1465 (D.C. Cir. 1996) (holding that the employee should not be required to pay fees); Pinedo v. Premium Tobacco, Inc., 85 Cal. App. 4th 774 (2000) (same); Armendariz v. Foundation Health Psychcare Services, Inc., 24 Cal. 4th 83 (2000) ("(W)hen an employer imposes mandatory arbitration as a condition of employment, the arbitration agreement or arbitration process cannot generally require the employee to bear any type of expense that the employee would not be required to bear if he or she were free to bring the action in court.").

91. 238 F.3d 549 (4th Cir. 2001).

Title VII arbitration with the employer ($250 filing fee plus a $75 daily administrative fee); the court also declined to rule on the issue of whether the employee should be required to pay the arbitrator's fees, noting that the issue was up to the arbitrator's discretion and that it was premature to invalidate the agreement based on the possibility that the plaintiff might face significant arbitration fees.

In *Couglin v. Shimizu America Corp.*,[92] the court rejected the argument that the arbitration clause was unconscionable in that it required the employee to advance a $2,000 filing fee to the AAA in order to pursue the employment discrimination claim. *McCaskill v. SCI Management Corp.*[93] compelled arbitration of an employee's federal and state statutory and common law claims for retaliation and racial discrimination, despite the fact that the arbitration clause stipulated that the employee would be required to pay fifty percent of the arbitration costs, based on a lack of evidence that the employee could not afford such costs.

### D. NAF, AAA, JAMS Fees

The NAF, AAA, and JAMS all offer to hear small consumer claims, for fees that are similar to the $150 filing fee for claims in federal court:[94]

> NAF: claims under $2,500 at NAF cost $100, claims of up to $15,000 at NAF are $185.[95]
>
> AAA: claims under $10,000 cost $125.[96]
>
> JAMS: claims cost $125.[97]

Justice Ginsburg, in her dissent in *Green Tree Financial Corp.—Alabama v. Randolph*,[98] acknowledged the reasonableness of the fees charged by the AAA under its Consumer Arbitration Rules and by NAF under its small claims fee structure. Significantly, Justice Ginsberg did not find the arbitration fee unconscionable, but thought it best to refer the matter to the lower court for consideration before the Supreme Court reviewed the question.[99]

## XV. Nothing in This Paragraph Shall Prevent You from Requesting That the Applicable Arbitration Entity Reduce or Waive Your Fees, or That We Voluntarily Pay an Additional Share of Said Fees, Based Upon Your Financial Circumstances or the Nature of Your Claim

Some courts have stated that a procedure allowing a waiver of costs for indigent claimants, even if this procedure is not available until after a dispute arises, may defeat an argument that the costs are prohibitive.

Both the AAA[100] and NAF[101] rules provide for fee waivers for indigent parties. This alone is often enough for a court to reject a "prohibitive cost" argument.[102]

Given the *Green Tree III* Court's emphasis on individual evaluations of ability to pay in determining whether arbitration costs are prohibitive, a provision relieving a plaintiff of costs upon a showing of indigence could be beneficial to a business litigant.[103] A clause allowing for a waiver of filing fees and arbitration costs, and nullification of any fee allocation provision, for an indigent plaintiff, should strengthen the enforceability of an arbitration provision, while the absence of such a provision could possibly render the arbitration provision unenforceable. A defendant's offer to cover costs is often treated similarly.[104]

On the latter issue, however, the Eleventh Circuit U.S. Court of Appeals has concluded differently. In *Perez v. Globe Airport Security Servs., Inc.*,[105] that court addressed a similar offer by the defendant to cover the costs. Globe stated that it was willing to abandon use of the AAA, as required in the original agreement, in favor of less expensive private arbitration. The court rejected this argument and found that Globe's proposal constituted an offer to modify the original agreement. Therefore, Perez's rejection of Globe's offer to modify left the original contract intact. Ultimately, the court held that the arbitration agreement was unenforceable because, although Globe had previously agreed to abide by AAA rules, it included a cost-splitting provision in the agreement that contradicted the AAA rules and

92. 991 F.Supp. 1226 (D. Ore. 1998).

93. 2000 WL 875396 (N.D. Ill. June 22, 2000).

94. *See* 28 U.S.C. § 1914(a).

95. *See* NAF Code of Procedure, Fee Schedule, *available at* http://www.arb-forum.com/ arbitration/ NAF/Code linked/apdx c.htm.

96. *See* AAA Supplementary Procedures for Consumer-Related Disputes, *available at* http:// www.adr.org/index2.1.jsp?JSPssid=13777.

97. *See* JAMS Policy on Consumer Arbitrations Pursuant to Pre-Dispute Clauses, Minimum Standards Of Procedural Fairness, Standard 7, *available at* http://www.jamsadr.com/consumer_arb_std.asp.

98. 531 U.S. 79 (2000).

99. *Id.*, at 91-92. *See also, ACORN*, 211 F.Supp. 2d at 1173 (holding an arbitration clause unconscionable because of, among other things, high cost); *Ting*, 182 F.Supp. 2d at 933-34 (same), *aff'd*, 319 F.3d 1126 (9th Cir. Feb. 11, 2003); *see also supra* note 26.

100. *See* AAA Commercial Dispute Resolution Procedures, R-51, *available at* http:// www.adr.org / index2.1.jsp?JSPssid=13777&JSPaid=32122.

101. *See* NAF Code of Procedure, Rule 45, *available at* http://www.arb-forum.com/ arbitration/ NAF/ code.asp.

102. *See* Dorsey v. H.C.P. Sales, Inc., 46 F. Supp. 2d 804 (N.D. Ill. 1999) (flatly rejecting the argument that the clause was unconscionable because of the cost of arbitration); Legatree v. Luce, Forward, Hamilton & Scripps, 74 Cal. App. 4th 1105 (1999) (rejecting an argument that the arbitration clause design-

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ignating the AAA was unenforceable based on the AAA's high administration fees for employment arbitration, because of the AAA rule providing for deferral or reduction of fee for extreme hardship); *Ex parte* Dan Tucker Auto Sales, Inc., 718 So. 2d 33 (Ala. 1998) (rejecting the argument that the arbitration clause was unconscionable by reason of designating the AAA, based on the AAA's fees, and pointing out the relief available to distressed claimants).

103. *Green Tree III*, 531 U.S. 79, at 92 (2000). *See generally* Woska, *supra* note 1.

104. *See* Bank One v. Coates, 125 F. Supp. 2d 819, 834-35 (S.D. Miss. 2001); *see also* Roberson v. Clear Channel Broadcasting, Inc., 144 F. Supp. 2d 1371, 1373 (S.D. Fla. 2001) (upholding the arbitration provision because the defendant, both in its motion to compel arbitration and in its reply brief, stipulated that it would pay the plaintiff's costs of arbitration ); Camacho v. Holiday Homes, Inc., 167 F.Supp.2d 892 (W.D.Va. 2001) (agreement to arbitrate was unenforceable where the arbitral forum was "financially inaccessible" to the consumer, but the court indicated a willingness to reconsider if the creditor agreed to pay costs).

105. 253 F.3d 1280 (11th Cir. 2001).

allowed the arbitrator to award fees and costs at his discretion.[106]

## XVI. This Contract Evidences a Transaction Involving Interstate Commerce. Any Arbitration Under This Contract Shall Be Governed by the Federal Arbitration Act. Judgment Upon the Award Rendered May Be Entered in Any Court Having Jurisdiction

### A. The Federal Arbitration Act[107]

The FAA applies to arbitration clauses in state as well as federal courts, as long as the contract involves interstate commerce. The FAA includes the following noteworthy provisions:

- Section 2 validates written arbitration agreements in contracts "involving commerce" and in "maritime transactions."[108]
- Section 3 provides that courts "shall" stay actions on contracts with arbitration clauses, if requested by one of the parties.[109]
- Section 4 authorizes U.S. district courts to compel arbitration, where there is a basis for federal court jurisdiction independent of the arbitration clause, "upon being satisfied that the making of the agreement for arbitration...is not in issue."[110]
- Section 5 authorizes appointment of arbitrators if the contract doesn't provide for any appointment process or if the process fails.[111]
- Section 7 authorizes arbitrators to "summon" witnesses to the arbitration hearing, together with material documents.[112]
- Section 9 provides for confirmation of arbitration awards.[113]
- Section 10 provides that awards may be vacated on the following limited grounds:
  - When award was obtained through fraud, corruption or undue means;
  - Where evidence shows an arbitrator was partial or corrupt;
  - Where arbitrators were guilty of misconduct resulting in prejudices; or
  - When arbitrators exceeded their powers, or "so imperfectly executed them...."[114]
- Section 11 authorizes modification of the award to address material miscalculations and erroneous descriptions in order to effect the intent of the parties.[115]

### B. The FAA and State Law[116]

During the past decade, the U.S. Supreme Court has issued a number of decisions holding that the FAA preempts incompatible state laws and requires both federal and state courts to enforce valid arbitration agreements.[117] Other courts have reached similar conclusions.[118]

### C. The FAA and Federal Law

Congress has not shown an intention to preclude federal statutory claims from arbitration.[119] In a recent case, the Supreme Court held that the Equal Employment Opportunity Commission

106. For further cases accepting waiver, *see:* Large v. Conseco Fin. Servicing Corp., 292 F.3d 49 (1st Cir. 2002) (holding that the plaintiff could not show that arbitration costs were prohibitive because the defendant's offer to pay such costs mooted the issue of arbitration costs); Baugher v. Dekko Heating Tech., 202 F.Supp. 2d 847 (N.D. Ind. 2002) (recognizing a split among the district courts; the defendant could avoid discovery into the impact of costs on the plaintiff and possible nullification of the arbitration agreement by offering to pay the arbitration costs and fees); Arellano v. Household Finance Corp., 2002 WL 221604 (N.D. Ill. Feb. 13, 2002) (holding that the arbitration agreement was still enforceable even though the defendant only made its offer to pay the arbitration costs and fees at the time of its motion to compel arbitration); Cavanaugh v. Conseco Fin. Servicing Corp., 271 B.R. 414 (Bankr. D. Mass. 2001) (noting that the defendants had undercut the argument regarding unconscionability of arbitration costs and fees by offering to pay the costs and fees at the hearing).

For cases declining waiver, *see ACORN*, 211 F. Supp. 2d 1160 (holding that the defendant's subsequent offer to pay arbitration costs and fees was ineffective; the defendant could not revive a provision that was unconscionable in the first place); Cooper v. MRM Inv. Co., 199 F.Supp.2d 771 (M.D. Tenn. 2002) (refusing to accept the defendant's offer to pay the arbitration costs because it would be unfair to allow the defendant to draft an overreaching/illegal provision and then sever it only when challenged). *See also supra* note 26.

107. 9 U.S.C. §§ 1-16 (2000).

108. *Id.* § 2.

109. *Id.* § 3.

110. *Id.* § 4.

111. *Id.* § 5.

112. *Id.* § 7.

113. *Id.* § 9.

114. *Id.* § 10.

115. *Id.* § 11.

116. For a more thorough discussion on the FAA and preemption, *see* Stephen L. Hayford and Alan R. Palmiter, *Arbitration Federalism: A State Role In Commercial Arbitration*, 54 Fla. L. Rev. 175 (2002). *See also* Kaplinsky and Levin, *supra* note 26.

117. *See, e.g.*, Doctor's Assocs, Inc. v. Casarotto, 517 U.S. 681, 686-88 (1996); Allied-Bruce Terminex v. Dobson, 513 U.S. 265, 271-72 (1995); Southland Corp. v. Keating, 465 U.S. 1, 15-16 (1984); Perry v Thomas, 482 U.S. 483 (1987). In an influential decision, the Court held in Moses H. Cone Memorial Hospital v. Mercury Constr. Corp., 460 U.S. 1 (1983), that "Section 2 [of the FAA] is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary. The effect...is to create a body of federal substantive law of arbitrability, applicable to any arbitration agreement within the coverage of the [FAA]." 460 U.S. at 24.

118. *See, e.g.*, Bradley v. Harris Research, 275 F.3d 884 (9th Cir. 2001) (finding that the FAA preempts California law); Ottawa Office Integration v. FTF Bus. Sys., 132 F.Supp.2d 215 (S.D.N.Y. 2001) (FAA prevails over state law in interstate commerce dispute); Furgason v. McKenzie Check Advance of Indiana, Inc., 2001 WL 238129 (S.D.Ind. Jan. 3, 2001) (choice of state law to govern contract does not affect application of FAA); American Financial Services Association v. Burke, 169 F.Supp.2d 62 (D.Conn. 2001) (FAA preempts state predatory lending statute limitation on pre-dispute arbitration clauses).

119. *See, e.g.*, Shearson v McMahon, 482 U.S. 220 (1987); Gilmer v Interstate/Johnson Lane Corp., 500 U.S. 20 (1991) (neither general antiwaiver clauses nor multiple damages remedies and other "private attorney general" provisions of federal statutes demonstrate an intent by Congress to prevent binding arbitration pursuant to contractual arbitration clauses). *See supra* note 26.

(EEOC) can pursue victim-specific judicial relief in an enforcement action under the Americans with Disabilities Act. The Court found that because the EEOC was not a party to the arbitration agreement, there was no conflict between such remedies and the FAA. This does not, however indicate a major departure from the Court's pro-contract interpretation of the FAA.[120] This case affects only a small percentage of arbitration cases, those in which the EEOC acts as a party to litigation against an employer.[121] Furthermore, the Court had to grapple with more than the FAA; it had to reconcile the FAA with the EEOC's enforcement powers under federal employment discrimination statutes.[122] The case can be read to stand for the proposition that the Supreme Court refuses to enforce an arbitration agreement against a federal agency that is a non-signatory/non-party to an arbitration agreement.[123]

### D. Interstate Commerce

The FAA applies as long as the transaction involves interstate commerce. Courts generally have no difficulty in finding the contract relates to interstate commerce.[124]

There have been a few courts, however, who have failed to find the requisite interstate commerce necessary to bring the transaction under the umbrella of the FAA.[125]

A provision in the arbitration clause that the contract involves interstate commerce and that it is governed by the FAA reduces the possibility of uncertainty and may help to persuade the court that the FAA applies.[126]

### E. Venue

The FAA's venue provisions are permissive, allowing a motion to confirm, vacate, or modify to be brought either in the district where the award was made or in any district proper under the general venue statute.[127]

The FAA provides for judicial confirmation of awards if the parties agree under their arbitration clause, but, according to a recent federal appeals court ruling, there must still be an independent ground of federal question jurisdiction to merit review.[128]

## XVII. Notwithstanding This Provision, Both You and We Retain the Right to Exercise Self-Help Remedies and to Seek Provisional Remedies from a Court, Pending Final Determination of the Dispute by the Arbitrator

Several courts have resurrected the doctrine of mutuality, for arbitration agreements that force consumers to arbitrate their claims while the business reserves its own right to sue in court, holding that the lack of mutuality constitutes substantive unconscionability and makes the agreement unenforceable.[129]

However, the *Armendariz* opinion has been severely criticized by a federal district court in California, as unlawfully singling out arbitration agreements, since in non-arbitration agreements such non-mutual contract provisions are valid and are not considered unconscionable.[130] In fact, most courts today enforce arbitration provisions that impose obligations to arbitrate on one party but not the other, so long as the underlying contract as a whole is supported by consideration.[131]

Creditors often reserve the right in arbitration clauses to litigate ancillary

120. *See* Stephen J. Ware, *Arbitration under Assault, Trial Lawyers Lead the Charge*, Cato policy analysis No. 433, April 18, 2002, *available at* http://www.cato.org/pubs/pas/pa-433es.html.

121. *Id.*

122. *Id.*

123. *See* EEOC v. Waffle House, 234 U.S. 279 (2002).

124. *See, e.g.*, Allied-Bruce Terminex v. Dobson, 513 U.S. 265 (1995) (the "involving commerce" language of the FAA is as broad as the Commerce Clause itself, bringing innumerable consumer contracts within the ambit of federal arbitration law); Munoz v. Green Tree Fin. Corp. 542 S.E. 2d 360 (S. Car. 2001) (FAA applies to installment contract for home improvements between local home improvement contractor and homeowner); *In re* FirstMerit Bank, N.A. 52 S.W. 3d 749 (Tex. 2001) (installment contract to purchase mobile home was "related to" interstate commerce); Ballard Servs, Inc. v. Conner, 807 So.2d 519 (Ala. 2001) (contract for home improvements after fire damage had sufficient nexus to interstate commerce to trigger application of FAA).

125. *See, e.g.*, Tefco Finance Company v. Green 793 So. 2d 755 (2001) (court refused to compel arbitration where defendants offered no proof of interstate commerce); Keel Motors, Inc. v. Tolbert, 821 So. 2d 963 (2001) (Alabama high court found insufficient evidence of interstate commerce for arbitration under the FAA).

126. *See* Staples v. The Money Tree, Inc., 936 F. Supp. 856, 858 (M.D. Ala. 1996); *Ex parte* Stamey, 776 So. 2d 85 (Ala. 2000).

127. *See* Cortez Byrd Chips, Inc. v. Bill Harbert Constr. Co., 529 U.S. 193 (2000).

128. *See* Perpetual Securities, Inc. v. Julie Tang and Hua Yu Chen, 290 F.3d 132 (2d Cir. 2002).

129. *See, e.g.*, Gibson v. Neighborhood Health Clinics, Inc., 121 F.3d 1126, 1131 (7th Cir. 1997) (declining to enforce an employment arbitration agreement in the absence of consideration); Hull v. Norcom, Inc., 750 F.2d 1547, 1550 (11th Cir. 1985) (holding that "the consideration exchanged for one party's promise to arbitrate must be the other party's promise to arbitrate at least some specified class of claims" and, absent such an exchange, an arbitration provision in an employment agreement is invalid and unenforceable); Pitchford v. Oakwood Mobile Homes, Inc., No. 5: 99 CV00053. (W.D. Va. Dec. 20, 1999) (Report and Recommendation of Magistrate) (invalidating arbitration clause based on lack of consideration because of company's alleged breach of arbitration clause by sometimes seeking money damages in court); Harris v. Green Tree Financial, 1997 WL 805254 (E.D. Pa. Dec. 17, 1997); Arnold v United Companies Lending Corp., 511 S.E. 2d 854 (W. Va. 1998); Stirlen v. Supercuts, Inc., 51 Cal. App. 4th 1519 (1997); Iwen v. U.S. West Direct, a Div. Of U.S. West Marketing Resources, Inc., 977 P.2d 989 (Mont. 1999) (holding that an arbitration clause is unconscionable if it permits one party to file suit); Crawford v. Cavalier Homes of Alabama, Inc., No. 98-V-641 (State Court of Carroll County, Georgia July 6, 1999) (same), *rev'd*, Results Oriented, Inc. v. Crawford, 538 S.E. 2d 73 (2000); Armendariz v. Foundation Health Psychcare Services, Inc., 24 Cal. 4th 83, 114 (2000) (holding that a one-sided arbitration clause is unconscionable unless there is valid business justification for the one-sidedness of the clause); Cash In A Flash Check Advance of Arkansas v. Jimmie Sue Spencer and Dorothy Barnes, 74 S.W. 3d 600 (Ark. 2002) (holding that the contract lacked sufficient mutuality; finding that Cash In A Flash could use the arbitration agreement to shield itself from litigation, while reserving to itself the ability to pursue relief through the court system); Flores v. Transamerica HomeFirst, Inc., 93 Cal. App. 4th 846 (2001) (finding that the arbitration clause was unenforceable because it did "not display a modicum of bilaterality" as it barred a borrower from seeking judicial remedies while allowing the lender to seek remedies in court and initiate foreclosure proceedings while an arbitration is in process); Lytle v. Citifinancial Services, Inc., 810 A.2d 643, 665 (Pa. Super. Ct. 2002) (finding that "reservation by [the lender] of access to the courts for itself to the exclusion of the consumer creates a presumption of unconscionability").

130. *See* Gray v. Conseco, Inc., 2000 WL 1480273 (C.D.Cal. 2000) (ordering arbitration of all claims, except for injunction under Business and Professions Code § 17200), *modified by* Gray v. Conseco, Inc., 2001 WL 1081347 (C.D.Cal. 2001).

131. *See, e.g.*, Design Benefit Plans, Inc. v. Enright, 940 F. Supp. 200, 205-06 (N.D. Ill. 1996) (enforcing an arbitration clause even though one party had the option of choosing arbitration or litigation; so long as the contract as a whole is supported by consideration, it is not invalid for lack of mutuality of obligation or remedy); Latifi v. Sousa, 1996 WL 735260, at 5 (N.D. Ala. Dec. 23, 1996) (stating that parties do not have to exchange reciprocal promises to arbitrate); Conseco Finance Servicing Corp. v. Wilder, 47 S.W. 3d 335 (2001) (finding that use of an arbitration clause in an adhesion contract is not abusive or unfair).

remedies such as repossession, replevin, and judicial foreclosure. Several courts have upheld such clauses on the ground that strict mutuality of obligations is not required.[132]

A few courts have found that such a creditor carve-out is unconscionable, and have refused to enforce the arbitration agreement.[133]

Finally, it should be noted that the *Restatement (Second) of Contracts* states that there is no requirement of mutuality of remedy.[134]

## XVIII. Neither You nor We Waives the Right to Arbitrate by Exercising Self-Help Remedies, Filing Suit, or Seeking or Obtaining Provisional Remedies from a Court

The question may arise whether a party to an arbitration agreement may begin a legal action in court and then initiate arbitration if a counterclaim is filed against it. In reaching a decision on this matter, courts examine the facts of each case, including the length of time the matter was litigated in court, how closely related the counterclaim is to the principal claim, and whether prejudice would result to the defendant/counterclaim plaintiff.[135]

## XIX. If Any Provision of This Arbitration Agreement Is Found to Be Unenforceable or Invalid, That Provision Shall Be Severed and the Remaining Provisions Shall Be Given Full Effect as if the Severed Provision Had Not Been Included

Without a severability clause, it is unclear whether a court will sever from the arbitration agreement any offensive provision.[136] Given the strong public policy in favor of arbitration, most courts would likely sever the offensive language but otherwise enforce the arbitration agreement.[137] However, some courts have refused to sever the offensive provision, and consequently invalidated the entire arbitration agreement.[138]

132. *See, e.g.*, Hale v. First USA Bank, N.A., 2001 WL 687371(S.D.N.Y. June 12, 2001) (enforcing an arbitration clause despite carve-outs allowing judicial remedies); Thompson v. Illinois Title Loans, Inc., 2000 WL 45493 (N.D. Ill. Jan. 11, 2000); Goodwin v. Ford Motor Credit Co., 970 F.Supp. 1007 (M.D. Ala. 1997); Truckenbrodt v. First Alliance Mortg. Co., 1996 WL 422150 (N.D. Ill. July 24, 1996); Randolph v. Green Tree Financial Corp., 991 F.Supp. 1410 (M.D. Ala. 1998), *rev'd on other grounds*, 175 F.3d 1149, (11th Cir. 1999), *cert. pet. filed*, No. 99-1235; *In re* Pate, 198 B.R. 841 (Bankr. S.D. Ga. 1996); *Ex parte* Isbell, 708 So. 2d 571 (Ala. 1997); Lackey v. Green Tree Financial Corp., 498 S.E. 2d 898 (S.C. Ct. App. 1998); Munoz v. Green Tree Financial Corp., Unpublished Opinion No. 98-UP-448 (S. Car. Ct. App. Oct. 20, 1998), *aff'd*, 542 S.E. 2d 360 (S. Car. Sup. Ct. 2001) (lack of mutuality of remedy does not invalidate a contract).

*See also* Volt Information Sciences v. Leland Stanford Jr., U., 489 U.S. 468, 478-79 (1989); Doctor's Assocs., Inc. v. Stuart, 85 F.3d 975, 980-81 (2d Cir. 1996); Meyers v. Univest Home Loan, Inc., 1993 WL 307747 (N.D. Cal. Aug. 4, 1993); Patrick Home Center, Inc. v. Karr, 730 So. 2d 1171 (Ala. 1999); *Ex parte* Napier, 723 So. 2d 49 (Ala. 1998) (Alabama Supreme Court upheld the validity of Green Tree's arbitration agreement, notwithstanding the lack of mutuality); Dorsey v. H.C.P. Sales, Inc., 46 F.Supp. 2d 804 (N.D. Ill. 1999) (same); Pridgen v. Green Tree Financial Servicing Corp., 88 F.Supp. 2d 655 (S.D. Miss. 2000) (same); Raesly v. Grand Housing, Inc., 105 F.Supp. 2d 562 (S.D. Miss. 2000) (same); Brown v. Surety Fin. Service., Inc., 2000 WL 528631 (N.D. Ill. Mar. 23, 2000) (same); Green Tree Financial Corp. v. Davis, 729 So. 2d 329 (Ala. 1999) (same); *Ex parte* Parker, 730 So. 2d 168 (Ala. 1999) (same); Smith v. Sanderson Group, Inc., 736 So. 2d 604 (Ala. 1999) (same); Green Tree Agency, Inc. v. White, 719 So. 2d 1179 (Ala. 1998) (same); *Ex parte* Gates, 675 So. 2d 371 (Ala. 1996) (same); Green Tree Financial Corp. of Alabama v. Vintson, 753 So.2d 497 (Ala. 1999) (same); Harold Allen's Mobile Home Factory Outlet, Inc. v. Early, 776 So. 2d 777 (Ala. 2000) (same); *Ex parte* Perry, 744 So.2d 859 (Ala. 1999) (same); Ryan's Family Steak Houses, Inc. v. Regelen, 735 So.2d 454 (Ala. 1999) (same); Green Tree Fin. Corp. v. Wampler, 749 So. 2d 409 (Ala. 1999) (same); Johnnie's Homes, Inc. v. Holt, 790 So. 2d 956 (Ala. Jan. 12, 2001) (same); Pierson v. Green Tree Fin. Servicing Corp., 933 P.2d 955 (Okla. Civ. App. Div. 3 1997) (same).

133. *See, e.g.*, Arnold v. United Companies Lending Corp., 511 S.E. 2d. 854 (W. Va., 1998) (holding that a carve-out for collection and foreclosure proceedings was unconscionable under West Virginia's UCC). The California Court of Appeal, First Appellate District, Division Five invalidated an arbitration clause in a reverse mortgage because of the fact that it carved out foreclosures. *See also* Pinedo v. Premium Tobacco, Inc., 85 Cal. App. 4th 774, 781 (2000).

134. RESTATEMENT (SECOND) OF CONTRACTS § 363, and Comment.

135. *See, e.g.*, Doctor's Assocs., Inc. v. Distajo, 66 F.3d 438, 453-57 (2d Cir. Conn. 1995) (finding that the pursuit of eviction proceedings in state court at the direction of Doctor's Associates could constitute a waiver of their right to demand arbitration); Commercial Union Ins. Co. v. Gilbane Bldg. Co., 992 F.2d 386, 390-91 (1st Cir. 1993) (reversing the district court's finding that allowed the defendant's counterclaim to continue even though the plaintiff had initiated an arbitration action against the defendant, and instead holding that the parties were contractually bound to submit all their disputes to arbitration before the litigation occurred); Design Benefit Plans, Inc. v. Enright, 940 F. Supp. 200, 202-03 (N.D. Ill. 1996) (granting the plaintiff insurer's motion to compel arbitration because the defendant agent's counterclaim was subject to a valid, mandatory arbitration clause and there was no waiver).

*See also*, *ACORN*, 211 F.Supp.2d at 1170, holding that even though the provisional remedies are available to both parties, it is more likely that the creditor will use them to foreclose. This may be inconsistent with the numerous cases in which a debtor preliminarily enjoins foreclosure pending the resolution of a lawsuit. *See supra* note 26. Additionally, California's arbitration statute specifically provides for provisional remedies by the court pending the arbitration. *See* Cal. Code Civ. Proc. § 1281.8.

Timing often becomes relevant when determining if there is a waiver of the right to arbitrate. In Morrell v. Wayne Frier Manufactured Home Center, 834 So. 2d 395 (Fla. Dist. Ct. App. 2003), the defendant attempted to compel arbitration a year after the original claim had been made, and on the eve of trial. The court found that the defendant had waived its right to arbitrate by actively participating in the litigation up to that point. In Blankenship v. Town and Country Ford, Inc., 574 S.E. 2d 132 (N.C. Ct. App. 2002), the defendant failed to respond to the consumer's lawsuit, resulting in a default judgment against the defendant. The court rejected the defendant's subsequent attempt to rely upon the arbitration provision, finding that the defendant waived its right to enforce the arbitration agreement by failing to assert its right in response to the complaint. *See also supra* Pts. II and VIII.

136. *See supra* Pt. V. regarding class actions.

137. *See e.g.*, Great Earth Companies, Inc. v. Simons, 288 F.3d 878 (6th Cir. 2002) (severing a distant forum provision); Herrington v. Union Planters Bank, N.A. 113 F.Supp.2d 1026, 1033 (S.D. Miss. 2000) (finding that the waiver of punitive damages, if applicable to the plaintiffs' TISA allegations, is severable from the arbitration agreement); Graham v. Scissor-Tail, Inc., 623 P.2d. 165 (1981) (California Supreme Court severed provision designating a non-neutral arbitrator); Saika v. Gold, 49 Cal. App. 4th 1074 (1996) (court severed clause giving trial de novo to stronger party); Beynon v. Garden Grove Medical Group, 100 Cal. App. 3d 698 (1980) (court severed clause giving stronger party right to rearbitration); Bolter v. The Superior Court of Orange County, 87 Cal.App.4th 900 (2001) (severing provisions prohibiting class-wide arbitration, limiting damages and providing for a distant forum); Dunkin v. Bosney, 82 Cal. App. 4th 171, 196 (2000); Armendariz v. Foundation Health Psychcare Servs., Inc., 68 Cal. App. 4th 374, 380 (1998) (court severed provision limiting remedies); review granted, 973 P.2d 51 (1999), *rev'd* 24 Cal. 4th 83 (2000) ("If the central purpose of the contract is tainted with illegality, then the contract as a whole cannot be enforced. If the illegality is collateral to the main purpose of the contract, and the illegal provision can be extirpated from the contract by means of severance or restriction, then such severance and restriction are appropriate."). *See* Kaplinsky and Levin, *supra* note 3; Kaplinsky and Levin, *supra* note 26.

138. *See, e.g.*, Paladino v. Avnet Computer Technologies, Inc., 134 F.3d 1054 (11th Cir. 1998) (refusing to sever provisions regarding remedies); Baron v. Best Buy Co., Inc., 75 F. Supp. 2d. 1368 (S.D. Fla. 1999) (refusing to sever); Lopez v. Plaza Finance Co., 1996 WL 210073 (N.D. Ill. Apr. 25, 1996) (refusing to sever a provision that obligated the buyer, but not the seller, to submit its claims to arbitration, and therefore finding the entire agreement unenforceable); Stirlen v. Supercuts, Inc., 51 Cal. App. 4th 1519 (1997), and Gonzalez v. Hughes Aircraft Employees Federal Credit Union, 990 P.2d. 504 (1999) (both courts refused to enforce arbitration based on the existence of several offensive provisions that reserved the right to judicial redress for the employer, while forcing the employee to arbitrate all claims); Flores v. Transamerica HomeFirst, Inc., 93 Cal. App. 4th 846 (1st Dist. 2001) (refusing to sever an arbitration clause (which allowed the lender to seek redress and foreclosure in court but required the borrower to pursue claims in arbitration), and enforcing the remaining provisions of the contract, holding that "no single provision can be stricken to remove the unconscionable taint" in the contract).

The existence of a severability clause as part of an arbitration agreement mitigates the risk that a court may refuse to enforce the entire arbitration agreement based on one offensive provision.[139] In such states where the court has severed the class arbitration waiver provsion and elected to enforce the remainder of the arbitration agreement, considerations should be given to omitting the severability clause contained in the arbitration clause and relying on the general severability clause contained in the contract.

## XX. Punitive Damages

### A. Punitive Damages Under Federal Law

Arbitration clauses often contain a provision prohibiting an award of punitive damages. The legality of a provision in an arbitration agreement limiting or prohibiting punitive damages should turn on whether such a provision would be lawful in a general contract.[140] The U.S. Supreme Court has suggested that an arbitration agreement can limit available remedies as long as it does so unambiguously.[141] The Seventh Circuit U.S. Court of Appeals likewise has held: "[C]ourts would enforce a provision in an arbitration clause that forbade the arbitrator to award punitive damages....Indeed, short of authorizing trial by battle or ordeal, or more doubtfully, by a panel of three monkeys, parties can stipulate to whatever procedures they want to govern the arbitration of their disputes; parties are as free to specify idiosyncratic terms of arbitration as they are to specify any other terms in their contract. [citations omitted.] For that matter, parties to adjudication have considerable power to vary the normal procedures [citations omitted] and surely can stipulate that punitive damages will not be awarded."[142]

Other cases have similarly allowed for a waiver of punitive damages in an arbitration agreement.[143]

However, some courts have found arbitration agreements to be unenforceable, based either entirely or partly on the fact that they prohibited punitive damages.[144] A few courts have chosen to sever an offensive provision regarding punitive damages, and otherwise have enforced the arbitration agreement.[145]

### B. Punitive Damages and State Law

The award of punitive damages is subject to state law. Choosing the law of a state that forbids or limits the authority of an arbitrator to award punitive damages will obviously affect such a determination. For example, Illinois arbitration law, according to several Illinois appellate courts, precludes an arbitrator from awarding punitive damages unless the parties have expressly authorized it to do so.[146] The arbitration clause itself, rather than just the contract provisions, must indicate that it is governed by the preferable state law. Otherwise, federal

139. Drafters of an arbitration agreement in California should be wary of including a severance clause, lest a court order arbitration on a class-wide basis, a result that neither party intended when the arbitration agreement was signed. *See, e.g.*, Bolter v. The Superior Court of Orange County, 87 Cal.App. 4th 900 (2001); Szetela v. Discover Bank, 97 Cal. App. 4th 1094 (2002); Keating v. Superior Court, 31 Cal.3d 584 (1982); Izzi v. Mesquite Country Club, 186 Cal. App. 3d 1309 (1986); Lewis v. Prudential- Bache Securities, Inc., 179 Cal. App. 3d 935 (1986); Blue Cross of California v. Superior Court, 67 Cal. Ap. 4th 42 (1998). *See supra* note 26.

140. *See, e.g.*, Kaplinsky and Levin *supra* note 3.

141. *See* Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52 (1995).

142. Baravati v. Josephthal, Lyon & Ross, Inc., 28 F.3d 704, 709 (7th Cir. 1994).

143. Bonar v. Dean Witter Reynolds, Inc., 835 F. 2d 1378, 1387, n. 12 (11th Cir. 1988) (the court stated that the FAA would not override a clear provision in a contract prohibiting arbitrators from awarding punitive damages, but did not address enforceability of a waiver under state law in concluding that the appellees' signing of "an ambiguous agreement [that never mentioned punitive damages] could not have been intended to relinquish their right to punitive damages."); Raytheon Company v. Automated Business Systems, 882 F. Supp. 6, 12 (1st Cir. 1989) (in the context of a commercial arbitration between a manufacturer and dealer, the court stated: "Parties that do not wish arbitration provisions to exclude punitive damages claims are free to draft agreements that do so explicitly. In this case, no such exclusion from the general language of the arbitration clause exists. Accordingly, we conclude that the district court correctly ruled that the arbitrators were authorized to award punitive damages against Raytheon."); Great Western Mortgage Corp. v. Peacock, 110 F.3d 222, 231- 32 (3d Cir. 1997) (holding that challenges to provisions in an arbitration agreement allegedly waiving attorneys' fees and punitive damages and providing a shortened statute of limitations in a case based on a state anti-discrimination statute were for the arbitrator to decide), *cert. denied*, 522 U.S. 915 (1997); Farrell v. Convergent Communications, Inc., 1998 WL 774626 (N.D. Ill. Oct. 29, 1998) ("[T]his Court believes, and case law suggests, that limitations on the amount of damages alone does not render an agreement to arbitrate per se unconscionable, as parties are generally free to contract as they see fit."); DeGaetano v. Smith Barney, Inc., 1996 WL 44226 at *3 (S.D.N.Y. Feb. 5, 1996) (holding an arbitration agreement valid even though it precluded an employee bringing a Title VII sex discrimination action from obtaining attorney fees or punitive damages); Rosen v. Waldman, 1993 WL 403974, at *3 (S.D.N.Y. Oct. 7, 1993) (finding that arbitration agreements frequently impact on opportunities of the parties to obtain punitive damages and this does not invalidate an arbitration agreement.); Morrison v. Circuit City Stores, Inc., 70 F.Supp. 2d 815 (S.D. Ohio 1999); Federowicz v. Snap-On Tools Corp., Civ. 1992 WL 55723, at *3 (E.D. Pa. Mar. 12, 1992) (refusing to void an arbitration clause as unconscionable where the damages-limiting clause applied mutually to both parties); Allen Knitting Mills, Inc. v. Dorado Dress Corp., 333 N.Y.Supp. 2d 848 (1972) (same); East San Bernardino County Water Dist. v. City of San Bernardino, 33 Cal. App. 3d 942 (1973) (same).

144. *See, e.g.*, Graham Oil Co. v. ARCO Products Co., a Div. Of Atlantic Richfield Co., 43 F.3d 1244, 1247-48 (9th Cir. 1994), *cert. denied*, 516 U.S. 907 (1995) (holding that an arbitration agreement conflicted with the terms of the General Petroleum Marketing Practices Act, where the agreement would have precluded the plaintiff from recovering exemplary damages and attorneys' fees and would have shortened the statute of limitations); Johnson v. Hubbard Broadcasting, Inc., 940 F.Supp. 1447, 1459-62 (D. Minn. 1996) (arbitrator was allowed to decide the validity of provisions; but if the arbitrator interprets the arbitration agreement as waiving the right to attorneys' fees or punitive damages or as reducing the statute of limitations in a case involving federal and state civil rights laws, "the agreement would contravene federally established remedial measures, possibly rendering the agreement unen-

*(Continued in next column)*

144. *(Continued from previous column)*

forceable as unconscionable"); Stirlen v. Supercuts, Inc., 51 Cal. App. 4th 1519 (1997) (rejecting as unconscionable an arbitration clause which, among other things, precluded the employee from obtaining any relief other than actual damages); Arnold v. United Companies Lending Corporation, 204 W. Va. 229, 511 S.E. 2d. 854 (W. Va. 1998) (invalidating an arbitration clause in a residential mortgage transaction under the West Virginia Consumer Credit Code as a result of a lack of mutuality and a prohibition against the award of punitive damages); Powertel, Inc. v. Bexley, 743 So. 2d. 570 (Fla. 1999) (invalidating an arbitration clause that expressly limited the company's liability to actual damages); Ramirez III v. Circuit City Stores, Inc., 76 Cal. App. 4th 1229 (1999) (invalidating an arbitration clause that, among other things, limited punitive damages), *review granted and opinion superseded*, 995 P.2d 137 (Cal. 2000); State ex rel. Dunlap v. Berger, 567 S.E.2d 265 (W.Va. 2002) (finding that arbitration clauses that prohibit an award of punitive damages and class actions are unconscionable and unenforceable), *cert. denied*, Friedman's, Inc. v. West Virginia *ex rel* Dunlap, 123 S. Ct. 695 (2002).

145. *See, e.g.*, Gannon v. Circuit City Stores, Inc., 262 F.3d 677 (11th Cir. 2001) (severing a punitive-damages clause was held to be consistent with the terms of the contract, the intent of the parties, Missouri contract law, and federal law favoring the enforcement of arbitration agreements); Herrington v. Union Planters Bank, N.A., 113 F. Supp. 2d 1026, 1033 (S.D. Miss. 2000) (finding that the waiver of punitive damages, if it was related to the plaintiffs' TISA allegations, was severable from the arbitration agreement); Sims v. Unicor Mortgage, Inc., 1998 WL 34016832 (N.D. Miss. Sept. 8, 1998) (even if a waiver of punitive damages is contrary to public policy, such a provision is severable from an arbitration agreement); *Ex parte* Celtic Life Ins. Co. and *Ex parte* Jeffrey Fredrickson, 2002 WL 844768 (Ala. May 3, 2002) (severing a clause prohibiting punitive damages); Bolter v. The Superior Court of Orange County, 87 Cal.App.4th 900 (2001) (damages limitation severed); Cavalier Manufacturing, Inc. v. Jackson, 2001 Ala. LEXIS 373 (Ala. Oct. 5, 2001) (finding that "a predispute arbitration clause that forbids an arbitrator from awarding punitive damages is void as contrary to the public policy of this State"; the provision should be severed according to the agreement's severability clause).

146. *See* Ryan v. Kontrick, 1999 WL 167522 (Ill. Mar. 26, 1999); Edward Elec. Co. v. Automation, Inc., 593 N.E.2d 833 (Ill. 1992).

arbitration law, which is more deferential to punitive damage awards in arbitration, may apply:[147] "This Court's decisions make clear that if contracting parties agree to include punitive damages claims within the issues to be arbitrated, the FAA ensures that their agreement will be enforced according to its terms even if a rule of state law would otherwise exclude such claims from arbitration."[148]

### C. Treble Damages

An additional issue is whether treble damages are available if the arbitration clause prohibits punitive damages. In a recent case, the Fifth Circuit U.S. Court of Appeals held that an arbitration clause that prohibits the award of punitive damages does not preclude an arbitrator from awarding treble damages, finding that treble damages serve a distinct compensatory and remedial role rather than a punitive one.[149] However, other courts have found that treble damages are a form of punitive damages.[150]

## XXI. NAF, AAA, JAMS and Punitive Damages

The NAF, AAA, and JAMS generally discourage prohibitions on punitive damages. The AAA's procedures state that: "The arbitrator may grant any remedy, relief or outcome that the parties could have received in court."[151] JAMS' policy is that: "Remedies that would otherwise be available to the consumer under applicable federal, state or local laws must remain available under the arbitration clause, unless the consumer retains the right to pursue the unavailable remedies in court."[152] Likewise, in NAF's Frequently Asked Question section, it states that: "Parties are entitled to the same legal remedies in arbitration as the court system. The Forum's Arbitration Bill of Rights prohibits parties from unlawfully attempting to limit the other party's remedies in arbitration."[153]

Finally, the drafter of an arbitration clause forbidding an award of punitive damages by the arbitrator should weigh the impact of a consumer's argument that, having precluded the award of punitive damages by the arbitrator, such an award must be considered by a jury.

147. *See* Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52 (1995).

148. *See, e.g.*, Allied-Bruce Terminex v. Dobson, 513 U. S. 265 (1995).

149. *See* Investment Partners, L.P. v. Glamour Shots Licensing, Inc., 298 F. 3d 314 (5th Cir. 2002).

150. *See, e.g.*, Shearson/American Express v. McMahon, 482 U.S. 220, 240-41 (1987) (indicating in dicta that treble damages are primarily remedial and secondarily punitive); Genty v. Resolution Trust Corp., 937 F.2d 899, 910-11 (3rd Cir. 1991); Pine Ridge Recycling, Inc. v. Butts County, Georgia, 855 F. Supp. 1264, 1273 (M.D. Ga. 1994).

151. *See* AAA Supplementary Procedures for Consumer-Related Disputes, C-7, *available at* http:// www.adr.org/index2.1.jsp?JSPssid=13777.

152. *See* JAMS Policy on Consumer Arbitrations Pursuant to Pre-Dispute Clauses, Minimum Standards of Procedural Fairness, Standard 3, *available at* http://www.jamsadr.com/consumer_arb_std.asp.

153. *See* NAF FAQ's, *available at* http://www.arb-forum.com/about/questions.asp.