**Senate Judiciary Committee Hearing**
**"The Federal Arbitration Act and Access to Justice:**
**Will Recent Supreme Court Decisions Undermine the**
**Rights of Consumers, Workers, and Small Businesses?"**

**Questions for the Record Submitted by**
**Senator Al Franken for Archis Parasharami**

**Question 1: Before *Italian Colors* was decided, you wrote that corporations should consider removing certain provisions from their arbitration agreements. These included costs that are excessive in the context of small claims, waivers of substantive rights available under applicable laws, and requirements that people travel to distant places to arbitrate. Today, do you advise corporations to remove these features from the arbitration agreements they have with their consumers and workers?**

Both before and after the Supreme Court's decision in *American Express v. Italian Colors Restaurant*, I have written that companies should consider adopting arbitration provisions that are favorable to consumers and employees. As I wrote in a subsequent version of the article referred to in the question—one published in August 2013, some months after the *Italian Colors* decision:

"Some unconscionability challenges attack features of the arbitration agreement that arguably tilt the process in favor of the company, such as requirements that consumers or employees pay arbitration costs that are excessive in the context of small claims, waive substantive rights available to remedy an individual's claims under applicable law or travel to distant places to arbitrate. Many of these features are common in business-to-business agreements. To forestall unconscionability challenges, companies should consider removing these artifacts of older business agreements from their consumer or employee arbitration agreements. In addition, drafters may consider adding some or all of the following hallmarks of pro-consumer arbitration provisions":

- "Low-cost or cost-free arbitration: Make arbitration affordable for customers and employees. Consider offering to pay the full costs of arbitration for modest-size claims.
- "Mutuality: To the greatest extent possible, both parties should be obligated to arbitrate claims, and any exceptions to arbitration should be fully mutual.
- "Do not impose limits on legal remedies: Courts remain skeptical of efforts to bar statutory or punitive damages and recovery of statutory attorneys' fees or to shorten statutes of limitations.

- "Offer a convenient location for the non-business party: Courts are reluctant to enforce arbitration agreements that require a consumer or employee to cross the country to arbitrate.

- "Confidentiality: Although confidentiality is often thought of as a benefit of arbitration, some courts have expressed concerns with arbitration agreements that require a consumer or employee to keep the results of arbitration secret.

- "Neutral arbitrator-selection process: When specifying an organization as the forum for arbitration of disputes, make sure that the organization and its process for selecting arbitrators are reputable and unbiased."

I further stated in the article that "given the Supreme Court's ruling in [*AT&T Mobility LLC v.*] *Concepcion*, companies that adopt arbitration provisions similar to AT&T's clause will likely benefit from what one judge has described as a 'safe harbor.'"

Although I cannot comment on confidential legal advice I provide to specific clients, I can state that, in general, I offer views similar to those expressed above when counseling clients about how to adopt or revise consumer and employment arbitration agreements.

**Question 2: During the hearing, Ms. Teske testified about a service member who tried to file a class action lawsuit under the Servicemembers Civil Relief Act (SCRA) after a bank illegally foreclosed on his home while he was serving in Iraq. Ms. Teske put forth evidence indicating that other service members' SCRA rights also had been violated because of the bank's policies and practices. However, because the service member's mortgage documents included a mandatory, pre-dispute arbitration clause and a class action waiver, the service member's case was dismissed, and he was unable to bring either a class action or a class arbitration. As a result, it is likely that other service members are unaware of their SCRA rights or that those rights may have been violated. Does this seem like a just result to you?**

Please let me begin by reiterating what I indicated at the hearing: I support our service members and am truly grateful for their service to this Nation. In addition, I oppose any violations of the substantive legal rights of our service members.

It is not possible to assess the case described in the question without more information. Unfortunately, Ms. Teske's testimony fails to identify the case in question. I understand from Ms. Teske's testimony that, after the arbitration provision was enforced, the service member she represented was able to obtain a

settlement of his claims on an individual basis. I would need more information about the settlement to offer any views on whether the service member achieved a just result.

The question also appears to ask whether it was appropriate that the service member was able to achieve an individual settlement only, instead of pursuing claims on behalf of other service members who were potential members of a class. Again, without knowing more about the case, it is not possible to determine whether, in the absence of an arbitration agreement, a class action would have delivered meaningful benefits to class members. As I discussed in my testimony, my law firm conducted a study of class actions that showed that the vast majority of consumer class actions that are filed do not result in significant benefits to members of the proposed class. In the absence of any information, it is hard to tell whether Ms. Teske's class action fits with the majority of class actions that do not afford most class members significant benefits or instead would have stood as an exception to the rule.

In looking more broadly than the case mentioned by Ms. Teske and considering dispute resolution for service members overall, it is my view that arbitration can provide service members with an inexpensive and simple means of accessing justice. Because arbitration offers procedural flexibility, service members can pursue arbitration through conference call or by documentary submissions; arbitration rules also often permit, after the initial submission, subsequent submissions by email. Service members therefore would not have to take time off work to pursue their disputes. And, under most modern arbitration agreements, businesses pay most or all of the costs of arbitration—therefore subsidizing dispute resolution to a much greater extent than litigation in court.

Moreover, the government can—and I believe, has a special responsibility to—help service members whose legal rights may have been violated. It can do so in at least two ways.

First, the CFPB has supervision and examination powers that can help monitor potential violations of service members' rights, as well as enforcement authority with respect to consumer protection laws.[1] The CFPB has created an Office of Servicemember Affairs. That office, according to a letter on the CFPB's web site by Holly Petraeus, "will ask CFPB bank and non-bank examiners to keep an eye out for military-specific issues. When we find out about people breaking consumer financial protection laws to harm servicemembers, we'll help CFPB

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[1] *See* 12 U.S.C. § 5514(a)(1) (providing for supervisory authority over certain nonbank covered persons); *id.* § 5514(c) (enforcement authority); *see also* Defining Larger Participants of the Consumer Reporting Market, 77 Fed. Reg. 42,874 (July 20, 2012) (codified at 12 CFR Part 1090) (addressing scope of supervision authority over nonbank covered persons under § 5514).

enforcement teams take action against them. And we plan to make it easy for military personnel and their families to contact the CFPB with questions or complaints about consumer financial products and services."[2] Thus, especially if there were a systemic problem that adversely affected our service members, the CFPB possesses the authority and ability to assist them.

Second, the Judge Advocate General's Corps for the branches of the armed services provide legal assistance to service members and retirees; this legal assistance extends to providing advice about real property disputes and the Servicemembers' Civil Relief Act.[3]

In these ways, the government can help protect the legal rights of our service members without the burdens associated with class action litigation.

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[2] http://www.consumerfinance.gov/petraeus-letter/.

[3] For example, the Regional Legal Service Office, Naval District Washington, provides legal assistance to individuals in "Maryland, Northern Virginia, and the District of Columbia." Its website states that it allows "service members and their dependents, reservists on active duty for 30 days or more, and retirees, as resources permit" to obtain assistance in a number of areas, including "Real Property," "SCRA," and "Consumer/Financial Affairs" issues. *See* http://www.jag.navy.mil/legal_services/rlso/rlso_naval_district_washington.htm.

**"The Federal Arbitration Act and Access to Justice: Will Recent Supreme Court Decisions Undermine the Rights of Consumers, Workers, and Small Businesses?"**

**Questions for the Record Submitted by Ranking Member Charles E. Grassley December 20, 2013**

**Questions for Archis Parasharami**

1. **The Supreme Court has stated that class action waivers in an arbitration agreement will be enforced. However, there are alternatives to class actions such as cost sharing or cost shifting. These tools may allow individual claimants to pursue what would otherwise be cost-prohibitive small claims. Please explain how small, but costly, claims will proceed? Also, please describe the alternatives to class actions and how they are used.**

As I described in my written testimony (at pages 18-19), there are a variety of ways to pursue claims in individual arbitration that are relatively small in size but may be costly to prove.

Significantly, even the dissenting Justices in *American Express Co. v. Italian Colors Restaurant*[1] recognized that that class procedures are not necessary to vindicate small individual claims because "non-class options abound" for pursuing claims under federal law in individual arbitration.

For example, many arbitration provisions provide for some combination of (i) incentive or bonus payments designed to encourage the pursuit of small claims, and (ii) the shifting of expert witness costs and attorneys' fees to defendants when the consumer or employee prevails on his or her claim. The AT&T provision at issue in *AT&T Mobility LLC v. Concepcion*[2] contains such features. If a consumer obtains an arbitral award that is greater than AT&T's last settlement offer, he or she will receive a minimum recovery of $10,000 plus twice the amount of attorneys' fees that his or her counsel incurred for bringing the arbitration. In addition, under such circumstances, the company is required to reimburse such a customer for reasonable expert witness fees.

As the dissenting Justices in *American Express* acknowledged, when an arbitration provision "provide[s] [such] an alternative mechanism to . . . shift . . . the necessary costs" of proving a claim, that eliminates any concern about the ability of individual

[1] 133 S. Ct. 2304 (2013).

[2] 131 S. Ct. 1740 (2011).

plaintiffs to vindicate their rights in arbitration.[3] A number of companies have adopted approaches that are similar to AT&T's arbitration provision.

The *American Express* dissenting Justices further recognized that "informal coordination among individual claimants" would allow those claimants to share the same lawyer, experts, and costs of proof, thereby reducing the costs to each claimant.[4] For example, an entrepreneurial plaintiffs' lawyer can recruit large numbers of clients (via the internet, social media, or other similar means), file thousands of individual arbitration demands on behalf of those clients, and distribute common costs over all those claimants, making the costs for expert witnesses and fact development negligible on a per-claimant basis.

The litigants before the Supreme Court also recognized that cost-sharing can support the vindication of small claims in individual arbitration.

As mentioned at the first panel at the Hearing, the brief of the United States in *American Express* stated that companies can "adopt[] arbitration procedures that can feasibly be invoked even for small-value claims." The brief also stated that "many companies have modified their agreements to include streamlined procedures and premiums designed to encourage customers to bring claims."."[5]

In addition, counsel for Italian Colors Restaurant explained in its brief to the Supreme Court that although "[t]he cost-sharing available in class-action litigation provides one mechanism to address the high expert costs" necessary to prove their claim, "it is far from the only mechanism." Indeed, they explained, "[b]ilateral arbitration ***remains feasible*** if costs can be shared or shifted," as under the "arbitration clause at issue in *Concepcion*."[6]

With these principles in mind, some plaintiffs' lawyers are already beginning to institute multiple individual arbitrations or small claims actions—especially in view of the ability to reach multiple, similarly situated individuals using websites and social media. Indeed, this strategy for spreading litigation costs is an increasingly common means of pursuing disputes in arbitration:

- One of the lead counsel for the plaintiffs in *American Express* indicated at a Practicing Law Institute program that if the Supreme Court compelled arbitration the plaintiffs could, and would, pursue their claims through

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[3] 133 S. Ct. at 2318 (Kagan, J., dissenting).

[4] *Id.*

[5] Brief for the United States as Amicus Curiae Supporting Respondents at 24, 28, *American Express Co. v. Italian Colors Restaurant*, 133 S. Ct. 2304 (2013) (No. 12-133), 2013 WL 367051.

[6] Brief for Respondents at 17-18, 37, *American Express Co. v. Italian Colors Restaurant*, 133 S. Ct. 2304 (2013) (No. 12-133), 2013 WL 267025 (emphasis added).

individual arbitrations by using this cost-spreading approach.[7] While that counsel ultimately entered into a settlement, *Law360* later reported that, as part of the settlement, any claimant who pursued individual arbitrations would have "access to the entire litigation record from the nearly decade-long antitrust battle, as long as the merchant signs a confidentiality agreement." As counsel for the plaintiffs explained: "We fought really hard for that, to make the arbitration process as viable as it can be." He continued by acknowledging that "merchants representing 70 to 80 percent of AmEx's charge volume" would be able to "avail themselves" of the arbitration process.[8]

- The Internet and social media have made it easier than ever for aggrieved consumers to find each other. One lawyer "set up a website to recruit plaintiffs" to bring multiple small-claims cases alleging marketing of credit information.[9] Similarly, a former lawyer who sued an automaker in small-claims court after opting out of a class action set up a website along with profiles on Twitter and Facebook and a video on YouTube to publicize her case. She was as a result "contacted by hundreds of other car owners seeking guidance in how to file small claims suits if they opted out of" the class action.[10]

- After the decision in *American Express*, a member of a leading plaintiffs' firm recognized this new approach: "I think you'll continue to see firms like mine move into arbitration. If what large corporations want is to have thousands or tens of thousands of individual arbitrations as opposed to class actions ... then that's the direction we'll go in. It's a bit of 'be careful what you ask for.'"[11]

- At oral argument in *American* Express, Chief Justice John Roberts suggested that plaintiffs could use the resources of a common interest group, such as a small-merchant trade organization, to "get together and say we want to

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[7] *See* Gary B. Friedman, "Arbitration," *Consumer Financial Services Institute 2013*, Practicing Law Institute (Apr. 23, 2013), online at http://www.pli.edu/Content/OnDemand/Consumer_Financial_Services_Institute_2013/_/N-4nZ1z12p2h?fromsearch=false&ID=158662.

[8] Melissa Lipman, *AmEx To Spend Up To $79M In Surcharge Suit Settlement*, Law360.com (Dec. 19, 2013), online at http://www.law360.com/classaction/articles/497520.

[9] Sara Foley & Jessica Savage, *Court Filings Boost Revenue*, Corpus Christi Caller Times (Nov. 27, 2010), online at http://www.caller.com/news/2010/nov/27/court-filings-boost-revenue/

[10] Linda Deutsch, *Honda Loses Small-Claims Suit Over Hybrid MPG*, Associated Press (Feb. 1, 2012), online at http://www.msnbc.msn.com/id/46228337.ns/business-autos/t/honda-loses-small-claims-suit-over-hybrid-mpg/

[11] Melissa Lipman, *Plaintiff's Lawyers Still Hopeful After* AmEx *Ruling*, LAW360 (June 21, 2013), online at http://www.law360.com/articles/452294/plaintiffs-lawyers-still-hopeful-after-amex-ruling (quoting Jonathan Selbin).

prepare an antitrust expert report" that could be used in each of the subsequent arbitrations.[12]

- In other contexts, the pooling approach has helped plaintiffs lower their individual costs. As one study noted, "[a]n example of how such coordination can work is the large number of individual actions filed in litigation by common counsel for alleged violations of the Fair Debt Collection Practices Act, often against the same defendant."[13] In no small part because the fixed costs of proving a claim against the same defendant may be spread across many plaintiffs—and because attorneys' fees are provided by statute[14]—one newspaper reported that "[h]igh-volume consumer law firms are churning out [FDCPA] lawsuits as efficiently as the collectors they battle."[15]

In short, consumers, employees, and other potential plaintiffs have a wide array of tools for spreading litigation costs across a number of individual arbitrations. Social media and other technological innovations make it easier than ever for people who have common grievances to find each other and utilize common resources.

2. **Do you consider a class action proceeding as the best or most efficient way for individuals to have their claims adjudicated, whether or not in an arbitration proceeding?**

Class action proceedings are rarely the best or most efficient way for claims to be adjudicated—whether in arbitration or not.

To begin with, the overwhelming majority of disputes that consumers and employees may have would never qualify for class treatment because they are fact-specific and individualized—for example, if a consumer claims that a product he or she purchased does not work, or that particular charges appearing on a bill were not actually incurred.

Even in the minority of situations where a claim might qualify for class treatment, class actions are not efficient ways to deliver meaningful benefits to class members. Indeed, class actions are often troubling because they impose substantial costs without providing much in the way of benefits to most class members. My firm

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[12] Tr. of Oral Argument at 21, *American Express Co. v. Italian Colors Restaurant*, No. 12-133 (Feb. 27, 2013), online at http://www.supremecourt.gov/oral_arguments/argument_transcripts/12-133.pdf.

[13] Gregory C. Cook, *Why* American Express v. Italian Colors *Does Not Matter and Coordinated Pursuit of Aggregate Claims May Be a Viable Option After* Concepcion, MICH. J. L. REFORM ONLINE (Apr. 14, 2013), online at http://www.mjlr.org/2013/04/why-american-express-v-italian-colors-does-not-matter-and-coordinated-pursuit-of-aggregate-claims-may-be-a-viable-option-after-concepcion/#fnref-2132-14 (footnote omitted).

[14] *Id*. (citing 15 U.S.C. § 1692k).

[15] Chris Serres, *Debtors in Court – Suing Collectors*, MINN. STAR-TRIB. (Mar. 17, 2011), online at http://www.startribune.com/investigators/99676349.html?refer=y.

conducted a study of class action litigation that was attached as Exhibit A to my written testimony. As explained in that study, only about a third of cases settled on a class-wide basis; moreover, the settlements for which claims and/or distribution data were available showed that the lawsuits delivered funds to under 10% of the class—and sometimes under 1%. That is not surprising: many settlements require class members to submit a claim form—often with onerous documentation requirements—leading class members not to try to seek relief in the first place.

Arbitration on an individual basis affords consumers, employees, and small businesses with a mechanism that can be much more effective at delivering fair, easy, and quick access to a neutral decisionmaker at low cost. As the empirical research discussed in my written testimony reveals, arbitration is faster and cheaper than litigation, and is more likely to result in positive outcomes for consumers and employees.

3. **Professor Gilles stated that your law firm's study of class actions involved "cherry-picked" data. Please respond.**

Professor Gilles' unsupported assertion is false. The methodology for my firm's study is simple, straightforward, and transparent. Appendix C to the study provides details of that methodology, which I also explain here.

It was not possible to study all class actions; no other study has even come close. To make the study design manageable, we focused on cases filed in or removed to federal court because the dockets and case filings for federal courts are available online. By contrast, filings in state courts often are not searchable, let alone available, online.

We decided to study cases filed in or removed to federal court in a single year for three reasons. First, limiting the sample set to cases brought in a single year would ensure that the number of cases was manageable. Second, by selecting the year 2009, we were able to ensure that the Class Action Fairness Act of 2005 applied, which meant that most of the significant class actions that were alleged to be worth at least $5 million would proceed in federal court (and thus have the case files available online). Third, our experience suggested that most of the cases would have proceeded to a resolution over a four- to five-year period. Indeed, we found that 86% of the cases we studied were completed by 2013.

We also recognized that it would be impracticable to identify every putative class action filed in federal courts during 2009. There is no listing of class actions filed each year. And the federal courts' Public Access to Court Electronic Records (PACER) system does not offer an option for filtering cases, on a nationwide basis, to determine which lawsuits involve class allegations.

We therefore sought a neutral way of identifying class actions that were filed. We decided to review cases that were mentioned in two commercial publications: the *BNA Class Action Litigation Reporter* and the *Mealey's Litigation Class Action*

*Reporter*. Those publications cover a wide array of developments in class action litigation, and therefore provide a diverse sample of filed class action complaints. The publications have an incentive to report comparatively more significant class actions out of all class actions filed, without wasting readers' time and attention on minor or obviously meritless suits. If anything, that means the sample set of cases we reviewed would be skewed in favor of more significant class actions filed by prominent plaintiffs' attorneys – which, experience and logic would suggest, should be *more meritorious on average* than a sample generated randomly from all class actions filed.

Finally, we excluded three categories of cases that are not analogous to the types of disputes that would be covered by the proposed Arbitration Fairness Act—i.e., claims by consumers, employees, and small businesses. These exclusions had next to no effect on the results of our study.[16]

- We excluded class actions brought by the EEOC, which do not proceed under Federal Rule of Civil Procedure 23.[17]
- We also excluded Fair Labor Standards Act "collective actions," for which—in contrast with opt-out class actions typical of consumer and employee claims—similarly situated employees must provide consent in writing in order affirmatively to opt-in to the representative plaintiff's suit.[18]
- Finally, we also excluded securities class actions, which one academic study has described as being "managed under a set of class action rules distinct from" typical consumer and employee class actions, and under which "the plaintiffs with the largest losses have a significant role in the litigation."[19]

It is critically important for policymakers to base decisions on empirical data rather than anecdotes. For a long time, the debate about class actions has suffered from a lack of empirical information. Our study takes an important step forward in filling that gap, by reviewing a neutrally selected sample of cases. We are proud of and stand by the work done on our firm's study. At the same time, we welcome others to

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[16] Our 169-case sample set, which included these cases, resulted in 57% of cases dismissed, 14% pending, 28% settled on a class-wide basis, and 1% dismissed after an order compelling arbitration. After excluding them, our 148-case sample set resulted in 57% of cases dismissed, 14% pending, 28% settled on a class-wide basis, and 1% dismissed after an order compelling arbitration.

[17] *See, e.g., Gen. Tel. Co. of Nw., Inc. v. EEOC*, 446 U.S. 318 (1980).

[18] *See* 29 U.S.C. § 216(b).

[19] Nicholas M. Pace & William B. Rubenstein, *How Transparent are Class Action Outcomes? Empirical Research on the Availability of Class Action Claims Data* at 20, RAND Institute for Civil Justice Working Paper (July 2008), online at billrubenstein.com/Downloads/RAND%20Working%20Paper.pdf; *see, also e.g.,* Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-76, 109 Stat. 737 (1995); Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227 (1998).

take further steps in researching class actions to continue the work of replacing anecdotes with data.

4. **Last week, the Consumer Financial Protection Bureau announced its preliminary findings from the arbitration study Congress mandated in the Dodd-Frank Act. According to one report, there's concern the Consumer Financial Protection Bureau is preparing to write tough new rules restricting the use of arbitration clauses in consumer banking contracts. Please provide more information about the Consumer Financial Protection Bureau's study and what it means going forward.**

When the Bureau issued what it described as its "study results to date," its report included a number of important disclaimers that show why its "preliminary results" provide little information that is relevant to the central question that the Bureau must address: For the kinds of injuries that most consumers can suffer, what is the real-world accessibility, cost, fairness and efficiency of arbitration as compared to suing in court? And how will consumers be harmed if arbitration is prohibited or subjected to regulation that eliminates arbitration's availability. The Bureau stated:

- "Readers should not interpret this presentation as our assessment, preliminary or otherwise, of the relative importance of different areas to be covered in the statutory report to Congress. Rather, the subjects addressed here are those as to which we already have been able to obtain and analyze sufficient data in order to make some preliminary findings."

- "Because the Bureau's work on this study is ongoing, any of the findings presented here may be refined or modified when we issue our report to Congress."

- "This presentation focuses on the 'front-end' of formal disputes involving customers"—the nature of formal filings; "[i]n later work, we intend to address the 'back-end' of formal disputes: what happens, in how long, and at what cost."

The Bureau also identified a variety of areas not yet addressed, such as "the disposition of cases across arbitration and litigation (including class litigation), both in terms of substantive outcome and in terms of procedural variable like speed to resolution"; "consumer benefits and transaction costs in consumer class actions involving consumer financial services" including "whether class actions exert improper pressure on defendants to settle meritless claims"; and "the possible impact of arbitration clauses on the price of consumer financial products."

Especially with all of those issues—and more—left unresolved, the preliminary study does not even begin to answer the central questions that the Bureau must address.

To begin with, the number of formal claims filed by consumers in arbitration and in court—the principal focus of the Bureau's attention—says nothing about the relative accessibility and fairness of the two methods of dispute resolution. The Bureau compares the number of complaints filed in arbitration to a larger total number of potential customers, and seems to view the disparity as possible evidence that arbitration is not useful to consumers. Any such conclusion would be misguided for several reasons:

- *First*, consumers' claims often are resolved before the filing of a formal arbitration proceeding. Individuals who file arbitration demands—just like those who file small claims court cases or lawsuits in court—are almost always a very small group of consumers whose concerns were not resolved through the less-formal customer service mechanisms that precede the filing of an arbitration demand. The vast majority of customer concerns are resolved through informal channels, such as customer service processes, negotiation, or mediation, before a concern ripens into a dispute and a formal arbitration demand is filed.

  Moreover, because businesses subsidize most or all of the costs of arbitration—under AAA consumer rules, for example, a business must cover at least $1500 in filing fees—it is economically rational for every business to settle disputes of less than $2,000-5,000 before an arbitration is commenced. But that same incentive is lacking in court, where the cost burden falls on the consumer.

  What is more, many arbitration agreements create even greater incentives to settle claims before arbitration begins, such as through arbitration provisions that—like the provision at issue in *AT&T Mobility v. Concepcion*—contain potential bonus payments to customers who do better in arbitration than a company's last settlement offer. It is thus a straightforward matter of economics that, if a consumer has a dispute with a company of less than the bonus figure—and the claim is not frivolous or abusive—the company has every reason to settle by offering a payment (often for the full amount of the claim plus an amount for attorneys' fees) that satisfies the customer.

  Thus, as the Supreme Court explained in *Concepcion*, the consumers' claim in that case was "most unlikely to go unresolved" because the arbitration provision at issue provided that the company would pay the Concepcions a minimum of $7,500 and twice their attorneys fees if they obtained an award "greater than AT&T's last settlement offer."[20] And this self-imposed incentive to settle occurs not just at the stages of a formally commenced arbitration or the pre-arbitration negotiation period. Instead, large numbers of AT&T customers have their concerns resolved at a much earlier point by calling or

[20] 131 S. Ct. at 1753.

e-mailing AT&T's customer care department, which is remarkably effective: the record in *Concepcion* indicated that AT&T representatives awarded more than $1.3 billion in compensation to customers during a single twelve-month period in response to customer concerns and complaints.

Significantly, the Bureau's own preliminary results recognize that virtually all of the arbitration provisions studied require the company involved to pay all or nearly all of the arbitration costs and that many of the provisions include bonus provisions. Those agreements provide a very weighty incentive for pre-arbitration settlement of any non-frivolous consumer claim of $5,000 or less.

- *Second*, a concerted campaign to invalidate arbitration agreements was underway for the entire period studied by the Bureau. Plaintiffs' lawyers vigorously resisted arbitration (with success in certain "magnet" jurisdictions for class actions) before *Concepcion*. And after the Supreme Court held in *Concepcion* that class waivers in arbitration agreements are enforceable, the plaintiffs' bar has continued to search for ways to avoid their clients' agreements to resolve their disputes in arbitration. The unfortunate effect of these widespread efforts is that lawyers who represent consumers and their allies in consumer advocacy organizations have failed to encourage consumers to pursue their disputes in simplified, often cost-free arbitration.

- *Third*, the number of individuals who opt out of class action settlements shows nothing about the relative utility of arbitration and judicial litigation. The Bureau identified eight class actions in which the class members could choose to reject the benefits of the proposed settlement and instead file an individual arbitration claim. The failure of class members to do that, the Bureau seems to say, provides some evidence of the relative utility of arbitration and class actions. Put simply, any such contention makes no sense.

  A large number of consumers in these cases did nothing: they neither opted out, nor filed the forms required (in all but two of the cases) to obtain a share of the settlement. The most logical conclusion is that these consumers viewed the claim as spurious and/or the litigation process as a waste of their time.

  The fact that some consumers took advantage of a settlement offer says nothing about their view of the judicial litigation process—they may simply have concluded that it was worth obtaining what was offered—and absolutely nothing about their view of arbitration as an alternative.

  Finally, that some consumers opted out but did not pursue arbitration claims similarly offers no illumination about their views of arbitration as compared to litigation. Class members opt out of class actions for multiple reasons, as practitioners know well. True, some opt-outs may wish to pursue their own

claim separately, either by arbitration or small claims court. But other opt-outs may believe that the case is meritless and so they do not want to be part of the settlement class, and still others may object to class actions or to litigation in general. If (as is common) the class member who opted out has no quarrel with the company, then there is no reason that he or she would have chosen to initiate an arbitration. By suggesting otherwise, the Bureau appears to be assuming that (a) the claims at issue in the class action have merit; and (b) that the class members who opted out feel the same way. That thinking defies common sense and real-world experience.

- *Fourth*, the Bureau's definition of "small-value" claims presents a misleading picture of arbitration. The Bureau defines small-value claims as those involving $1,000 or less and then concludes that few consumers arbitrate small claims. But that definition is odd, given that—based on information compiled in Appendix E of the CFPB's own document—most state small-claims courts permit the assertion of claims of up to $10,000. Hopefully, the Bureau did not adopt this overly narrow definition in order to be able to assert, erroneously, that consumers do not use arbitration for small claims. In addition, of course, this analysis ignores entirely the fact, discussed above, that the terms of a growing number of arbitration agreements provide a very substantial incentive for the pre-arbitration settlement of such claims.

- *Fifth*, the Bureau has not yet addressed the critical question of how the resolution of consumers' claims in arbitration compares to the outcomes obtained in court. As the Bureau acknowledges, it has not yet compared the results that consumers obtain in arbitration and in court. But, as I explained in my written testimony, existing empirical research shows that consumers do at least as well – if not better – in arbitration than in court.

Furthermore, the Bureau's brief discussion of class actions provides no basis for any conclusion regarding their value to consumers – as the Bureau itself acknowledges.

The Bureau observes that most arbitration agreements preclude class actions and class arbitrations. That is not surprising because, as the Supreme Court explained in great detail in *Concepcion*, class actions are incompatible with arbitration, which traditionally has taken place on an individual (one-on-one) basis. The assumption underlying the Bureau's observation appears to be that consumers would be better off without these features of arbitration agreements. But that assumption is based on a theoretical opinion of how class actions function; as it turns out, the theory is diametrically opposed to how class actions work in practice.

Any legitimate study of dispute resolution—and certainly any regulation based on such a study—cannot rest on theoretical assumptions about the value of the class action device; instead, the study should examine the reality of how that procedure works. Thus, the question for the Bureau is whether the value of class actions outweighs the value that arbitration provides individual consumers by increasing

their ability to pursue their claims and obtain meaningful recoveries—not just through the formal arbitration process but also through informal resolutions that result from the greater incentives to settle that are generated by arbitration agreements.

The study my law firm conducted shows that in even in the minority of class actions that are settled on a classwide basis provide little, if any, tangible benefit to class members. In the cases where claims information was available, few class members—often fewer than 10 percent, and sometimes less than 1 percent—even bothered to submit claims.

While it is true that some class actions result in settlements where the parties agree to an "automatic distribution" of benefits to class members, such distributions are the exception rather than the rule. The Bureau's unrepresentative sample pointed to two automatic distributions out of eight possible settlements. While my law firm's broader study identified thirteen automatic distributions out of forty settlements studied, only one of the thirteen was a consumer case; ten involved claims by retirement plan participants in ERISA class actions where damages and eligibility could be ascertained easily from the plan's records. Thus, contrary to the implication in the Bureau's study, such settlements are exceptionally rare in the consumer context.

And the Bureau itself has acknowledged that it intends to study—among other areas that it has not yet addressed—"the disposition of cases across arbitration and litigation (including class litigation), both in terms of substantive outcomes and in terms of procedural variables like speed to resolution." It must do so by looking at a sample set that is greater than (a statistically insignificant) eight cases, and one that is selected on the basis of neutral factors rather than selected because class members obtained relief.

Finally, the Bureau's analysis provides strong evidence of the fairness of the arbitration process. The CFPB's review reveals:

- By far the leading choice of arbitration provider is the non-profit American Arbitration Association, which has long been recognized as the gold standard among arbitration administrators.
- Under most of the arbitration provisions studied, the business has agreed to pay all (or nearly all) of the costs of arbitration.
- All but one of the arbitration provisions studied ensured that the arbitration provider's rules would govern the selection of arbitrators using neutral criteria, and therefore did not create even an arguable risk of biased arbitrators.
- The Bureau states that arbitration clauses are "more complex than the rest of the contract." But there are many reasons for that.

*First*, arbitration provisions define procedures that will govern dispute resolution, and (by necessity) must be comprehensive because they apply in every dispute.

*Second*, even simplified legal procedures are likely to be more complicated than the "business" terms of consumer financial contracts. If companies were required to attach to their contracts the rules for dispute resolution in court, such as the Federal Rules of Civil Procedure, there is no doubt that those rules would be at least as hard to read—perhaps even harder—than the typical arbitration provision. (Indeed, the Federal Rules of Civil Procedure were so hard to read that they were substantially revised in 2007 solely to make them more comprehensible.)

*Third*, arbitration agreements have become longer and more complex over time in response to a wide variety of novel challenges raised by lawyers seeking to avoid those agreements. And courts that are hostile to arbitration have accepted some of those challenges, forcing the drafters of arbitration agreements to respond by adding further explanations (and, unfortunately, more length).

In short, the Bureau's "preliminary results" reveal that it has much more work to do. Congress has required that any regulation that the Bureau might propose must be consistent with the results of the study and justified by the public interest; the Bureau also "shall" consider "the potential benefits and costs to consumers and [businesses], including the potential reduction of access by consumers to consumer financial products or services resulting from" any such rule.[21] The study released on December 11 provides little information calculated toward answering those important questions, and even less information about how the Bureau plans in the next round of its study to address how arbitration and class actions work in reality, rather than in theory.

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

A number of issues were raised at the hearing that warrant a response.

*First*, Professor Gilles suggested at the hearing that the arbitration agreement in *American Express* precluded the parties from sharing the costs of proving their claims. She apparently relied on a contention in the *American Express* dissent that a confidentiality provision in the agreement prohibited "informal coordination

[21] 12 U.S.C. §§ 1028(b) & 1022(b)(2)(A)(i).

among individual claimants."[22] In fact, American Express contested that interpretation of the confidentiality provision at oral argument, and in any event a majority of the Supreme Court disagreed with the dissent's factual claim that the agreement at issue barred informal coordination among individual claimants.[23]

*Second*, it was suggested during the hearing that an individual employee or consumer who believes that he or she faced a biased arbitrator has no recourse *in court* to challenge that arbitrator's award. In fact, the Federal Arbitration Act allows such a consumer or employee to go to court to invalidate the arbitral award on the ground that the arbitrator was biased. Section 10 of the FAA states that "where there was evident partiality or corruption in the arbitrators"—*i.e.*, any arbitrator was biased—a party to the arbitral award may apply for "an order vacating the award." Moreover, even before arbitration commences, an individual may go to court to challenge the enforceability of the agreement if it lacks procedures for selecting a bias-free arbitrator. As I explained in my written testimony (at page 12), most consumer and employment arbitration agreements adopt fair and neutral mechanisms for selecting an arbitrator. But if an arbitration agreement fails to do so, courts have not hesitated to strike such agreements down. The U.S. Court of Appeals for the Ninth Circuit, for example, recently struck down an arbitration provision that "would always produce an arbitrator proposed by [the company] in employee-initiated arbitration[s]," and barred selection of "institutional arbitration administrators."[24]

*Third*, Professor Gilles stated that companies who adopt arbitration programs will "not have to be held accountable for any violations of the law." In addition, Professor Gilles stated that arbitrations are "private, sequestered, [and] individual," and that individual claimants thus have "no power to change" the defendant company's behavior on a broader scale. But these statements are based on assumptions that class actions are necessary deterrents to corporate wrongdoing—assumptions based on how class actions are supposed to work in theory that simply do not reflect the reality of class actions. As I discussed in my written testimony (at pp. 19-20), class actions do not deter corporate wrongdoing. That is because companies view class actions as a cost of doing business, rather than as a penalty for wrongdoing. The burdens of class action settlements fall on businesses against which plaintiffs' attorneys can present claims that survive a motion to dismiss and the standards for class certification—not against businesses that have engaged in wrongdoing.

New technology has provided individual claimants suffering from actual wrongdoing with new, extremely effective tools to hold corporations accountable. As

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[22] 133 S. Ct. at 2318 (Kagan, J., dissenting).

[23] *Id.* at 2311 n.4 (majority); *see also* Transcript of Oral Argument at 22-23, *American Express Inc. v. Italian Colors Restaurant*, 133 S. Ct. 2304 (No. 12-133), online at http://www.supremecourt.gov/oral_arguments/argument_transcripts/12-133.pdf.

[24] *Chavarria v. Ralphs Grocery Inc.*, 733 F.3d 916, 923-25 (9th Cir. 2013).

explained above (at p. 3), individuals with common grievances are increasingly using social media to target companies that they believe have aggrieved them.

*Finally*, although it has been suggested that the Arbitration Fairness Act would not prohibit consumer and employment arbitration altogether, in reality that would be the Act's effect if enacted. Companies that are told they must participate in the default system of litigation in court will not be willing to construct a second system of consumer or employee-friendly arbitration in which they subsidize the costs. As a result, they would abandon arbitration, leaving the vast majority of consumers and employees—whose claims tend to be small-value and not subject to certification in a class action—without any meaningful remedy. Those consumers and employees would undoubtedly be worse off, left to fend for themselves in our overburdened and underfunded courts.