QUESTION FOR THE RECORD

FROM SENATOR CHARLES GRASSLEY TO VICTOR E. SCHWARTZ

FOLLOWING THE SENATE JUDICIARY COMMITTEE HEARING:

"ARBITRATION: IS IT FAIR WHEN FORCED?"

OCTOBER 13, 2011

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

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

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

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

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

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

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

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

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