Editor's Note: *In July of 2011 the NYSBA Dispute Resolution Section submitted Comments to the Consumer Financial Protection Bureau in Connection with its Review of Arbitration for Consumer Financial Products or Services. The comments were submitted to provide background and highlight issues the Bureau may wish to consider in fulfilling its charge under the Dodd-Frank Act to review consumer arbitration in the financial sector. The report takes no position as to the appropriate treatment of consumer disputes, but supports a thorough examination of dispute resolution processes to ensure that they are in the public interest and fair to consumers. This article summarizes some of the issues highlighted for the Bureau's attention. The reader is invited to review the full text of the comments which cover these and other issues. The comments can be found at www.nysba.org/doddfrank.*

The Dodd-Frank Act: Seeking Fairness and the Public Interest in Consumer Arbitration

By Edna Sussman

The April 2011 Supreme Court decision in *AT&T v. Concepcion*, 131 S. Ct. 1740 (2011), intensified earlier concerns about the fairness of pre-dispute arbitration agreements in consumer contracts. In the *AT&T* case the court held that California state contract law, which deems class-action waivers in arbitration and other agreements unenforceable when certain criteria are met, is preempted by the Federal Arbitration Act as applied to arbitration clauses. Thus, California must enforce arbitration agreements even if the agreement requires that consumer complaints be arbitrated individually instead of on a class-action basis.

"[T]he Consumer Financial Protection Bureau…was directed to conduct a study…on the use of agreements providing for arbitration of future disputes between covered persons and consumers in connection with consumer financial products or services."

How *AT&T v. Concepcion* will be interpreted by the courts remains to be seen, but it has already motivated action to afford consumers more protection. The Arbitration Fairness Act which would invalidate pre-dispute arbitration agreements for consumers and employees was reintroduced in Congress on the heels of the decision. Senator Franken said when he reintroduced the bill: "This ruling is another example of the Supreme Court favoring corporations over consumers. The Arbitration Fairness Act would help rectify the Court's most recent wrong by restoring consumer rights." The Arbitration Fairness Act is not likely to progress in Congress this year but Congress has already enacted legislation with respect to arbitration which may ultimately be a game-changer for consumer arbitration. The Wall Street Reform and Consumer Protection Act of 2009, H.R. 4173, 111th Cong. § 1028 (2009), commonly known as the "Dodd-Frank Act, has attracted considerable press coverage with respect to various required changes in practices by financial institutions, but the Act's provisions requiring a review of arbitration have drawn little attention.

The examination of arbitration for consumers in the financial sector called for in the Dodd-Frank Act was first recommended in the Obama Administration's white paper on financial reform. Adopting the recommendation, the Consumer Financial Protection Bureau (the "Bureau") established by Congress was directed to conduct a study and provide a report on the use of agreements providing for arbitration of future disputes between covered persons and consumers in connection with consumer financial products or services. The Act further authorized the Director of the Bureau to prohibit or impose conditions or limitations on such arbitration agreements by regulation if it would be in the public interest, for the protection of consumers, and consistent with the study performed.[1]

The Bureau's task will not be an easy one. There have undoubtedly been abuses of arbitration for consumers. Indeed, the courts have struck many unfair provisions in arbitration agreements as unconscionable, including unfair arbitrator selection, discovery limitations, distant forums, limitations of remedies, shortening time to file from applicable statutes of limitations, and burdensome costs. On the other hand arbitration is viewed by many as affording a more user-friendly, cheaper and faster forum and as offering many advantages over litigation. Accordingly, there are a host of considerations that should be analyzed and reviewed by the Bureau in the development of the mandated study.

The Bureau's final study and conclusions are likely to have great influence on subsequent legislation and regulation of consumer arbitration not only for the financial services sector that are the subject of the Dodd-Frank Act but also for other sectors of the economy. This article does not urge any specific outcome but discusses some of the issues and highlights some of the impacts which the Bureau should consider before making its final determination.

I. Prior Studies of Arbitration for Consumers

There have been a great many studies of consumer arbitration addressing various questions including win rates, and cost and time factors.[2] However, none of them appear to address the question of when mandatory arbitration is or is not "in the public interest," a finding that the Bureau must make as part of its analysis of consumer arbitration.

The Federal Trade Commission ("FTC") conducted a comprehensive study of consumer debt collection,[3] to date the market segment that has garnered the most intensive study, undoubtedly due to the very large number of such cases and the perceived inequities in dispute resolution processes of such claims. In its study the FTC recognized that consumer credit is a critical component of today's economy and that debt collection is essential to keep credit available and its cost as low as possible.[4] The FTC, following comprehensive hearings and a review of the literature, concluded "that neither litigation nor arbitration currently provides adequate protection for consumers. The system for resolving disputes about consumer debts is broken."[5] To fix the system, the FTC found that a variety of significant reforms were necessary in both litigation and arbitration to make the system both efficient and fair.

Any assessment of consumer arbitration must examine the litigation alternative to arbitration since without arbitration disputes will have to be resolved in court. Arbitration results alone without such a comparison signify nothing and cannot be the basis for evaluating the process as the challenges in certain contexts may be endemic to the nature of the disputes in question, creating problems in the context of both arbitration and litigation as the FTC already found. Illustrating this point, one study found that in California, over a 4-year period, in more than 19,000 credit card cases heard by arbitrators, the credit card company prevailed 94 percent of the time, suggesting a bias in favor of the claimants.[6] A subsequent study reported that in court programs, creditors won relief in 98-100 percent of the debt collection cases that went to judgment. Meanwhile, in the American Arbitration Association debt collection cases, the rates were 97.1 percent for the debt collection program run by the AAA and 86.2 percent in the individual AAA debt collection cases. In a significant portion of the cases, both in court and in arbitration, the consumer defaulted.[7] It is this kind of comparison with respect to all relevant factors that is required to arrive at the optimal solution.

II. Access to the Courts

Court congestion and the recent cutbacks in judicial budgets are also relevant to the analysis as they affect access to the courts for the resolution of disputes. Data for 2009 regarding disposition of civil cases show a median of 23.4 months through trial in the federal courts, with the median in various districts ranging from 14.9 to 57.3 months. The median through appeal was 32.1 months.[8] The Bureau of Justice Statistics reports that for state court contract cases in the 75 largest U.S. counties, the average length of time from case filing to trial in jury cases was 25.3 months and for bench trials was 18.4 months.[9] Delays for appeals similar or lengthier than in federal court are likely to be found for state court appeals, a statistic that is not reported. These statistics are likely to deteriorate with the current budget crises.

Empirical research has also been conducted on the length of time required to complete a dispute in arbitration. One study found that the average time from the filing of the demand to the final award was 6.9 months.[10] As discussed below, delays in resolution of disputes not only has a negative impact on people's lives as they await resolution but also has real economic, dollars and cents, consequences. Justice delayed is indeed justice denied. Consideration may also be given to whether parties feel pressured to settle and accept terms not wholly acceptable in order to avoid long delays.

Recent cutbacks in funding of the judiciary in light of today's hard pressed state and local governments are leading to further delays in court. State after state reports cutbacks in funding for the judicial branch with 65 percent of states reporting reductions for fiscal year 2010 and 57 percent of states reporting reductions for fiscal year 2011,[11] with consequent reductions in access to justice. For example, the Los Angeles Superior Court, the nation's largest trial court system, predicts anticipated layoffs of roughly one-third of its personnel, and the closure of 139 courtrooms used as civil courtrooms out of its total courtroom count of 605 for all cases. Civil caseload clearance capacity is expected to fall by no less than 35 percent by 2013.[12] Florida reports a rapidly growing caseload coupled with funding which peaked in 2004-2005, forcing courts to slow or suspend the processing of civil cases.[13] Iowa reports a 9.3 percent reduction in staffing, ten days of court closure, and a delay in processing, *inter alia*, small claims cases.[14] Many consumer cases are low-dollar value cases which, with the more limited resources of the courts, may suffer disproportionately long delays and lack of attention as courts focus on their criminal and larger stakes civil matters.

III. The Economic Impacts of Elimination of Consumer Arbitration

The analysis of the "public interest" should include an examination of the financial implications of any action taken with respect to arbitration. The Supreme Court has recognized that the contractual selection of the dispute resolution forum can be a factor in pricing.[15] Thus whether the elimination of arbitration will lead to increased costs for the consumer must be explored.

Furthermore, delayed recoveries have a real monetary cost to the recovering party. As discussed above, there is considerable support for the proposition that resolution is approximately three times faster in arbitration as compared to court. The economic impact of a delay in resolution on an individual recovery for the consumer or the opposing party can be meaningful. To illustrate: assuming a successful claim for $10,000 and a delay of twelve months until resolution, a discount rate, a tool typically used to account for the time value of money, can be applied. Applying a 10 percent discount rate with respect to the $10,000 claim on which recovery is delayed by twelve months yields a loss in the real value of the recovery of about $900, or almost 10 percent of the recovery. In other words, the present value of the recovery received twelve months later on a claim of $10,000 is $9,090, thus reducing the value of the recovery by almost 10 percent.[16] The longer the wait the less the value to the party.

The impact on the broader economy of including all consumer cases in the court caseload cannot be overlooked either. The delays in the judicial system caused by the influx of the hundreds of thousands of consumer cases could be significant and could cause enormous economic losses for the broader society.[17] The County of Los Angeles conducted an analysis to predict the economic impact of the increased duration of litigation due to lost operating capacity driven by the budget constraints. It projected a $30 billion drop in economic output, translating to more than 150,000 jobs and $1.6 billion in tax revenue.[18] Findings from a similar study conducted in Florida showed that the total adverse economic impact of the projected increased civil court case delays on the Florida economy would be almost $17.4 billion annually and lead to an adverse impact on 120,000 jobs.[19]

IV. Pro Se Appearances

In late 2009, the American Bar Association Coalition for Justice undertook a study of judges throughout the United States to determine the effect of the economic downturn. The judges reported that self-representation had increased significantly. Sixty two (62) percent of all judges said that outcomes were consequently worse. When asked how parties were negatively impacted, ninety-four (94) percent of those responding stated that the failure to present necessary evidence was the most common problem. Eighty-nine (89) percent said that parties were impacted by procedural errors. Ineffective witness examination (85 percent) and failure to properly object to evidence (81 percent) were both cited as issues by more than four-fifths of the judges. Seventy-seven (77) percent of the judges cited ineffective arguments. Several judges noted that even when parties won at hearing, they were not able to proffer an order or judgment in a form that could be enforced to the court.[20]

Consideration should be given to whether in arbitration, with its more informal setting and expectations, these obstacles would have a less detrimental impact on a *pro se* representation. For example, are procedural errors less likely as arbitration procedures are less rigid and can be set out in simple, short arbitration rules? Is the arbitration process more easily accessible and easier to explain to the *pro se* litigant when the arbitrator and the case managers are involved? Is failure to object to evidence properly and the proper introduction of evidence less of a concern in arbitration as the rules of evidence are not strictly adhered to in arbitration and arbitrators are likely to consider the weight to be given to evidence based on its trustworthiness, whether or not a formal objection is lodged? Are issues concerning the provision of an enforceable order or judgment alleviated because parties generally need not present an order or judgment to the arbitrator since the arbitrators draft the award? It would seem that inquiry along these lines as to the ability of individuals to represent themselves effectively in court versus arbitration should be considered.

V. Online Dispute Resolution—Domestic and International

Many scholars have suggested that arbitration in the form of an online dispute resolution ("ODR") process could be most useful for consumers. E-commerce between business and consumers is growing rapidly. ODR involves the use of the Internet, e-mail, and other information technologies in lieu of the traditional face-to-face dispute resolution model. It offers efficiency, cost savings, and convenience for the disputing parties, while relieving the courts of an additional caseload. For smaller claims in particular, not having to take days off from work, or find coverage at home in order to attend to a dispute, can be of enormous benefit to consumers. Thus, use of such ODR arbitration processes may be a benefit for consumers.

The Congressional mandate under the Dodd- Frank Act does not distinguish between international and domestic transactions, and does not direct the Bureau to conduct a separate analysis of arbitration in these two different settings. ODR can be of special benefit to the consumer in the international context. Efforts on several fronts have been pursued to develop ODR for cross-border disputes involving consumers. One such effort by the United Nations Commission on International Trade Law (UNCITRAL) is progressing.[21] The Department of State, Office of Legal Adviser, Office of Private International Law, is actively engaged with UNCITRAL in its ODR initiatives.[22] Special attention should be given to cross border consumer disputes in this increasingly global economy.

VI. Standards for Consumer Arbitration

Regulation that would impose consumer protection standards in arbitration is a solution that must be examined. The private sector community that offers arbitral services has devoted considerable attention to the concerns about consumer arbitration. For example, in 1998, the American Arbitration Association issued a Consumer Due Process Protocol[23] that has guided the conduct of consumer arbitration at the AAA. It requires such measures as qualified, independent, and impartial neutrals chosen by an equal voice of the parties, an independent administration, reasonable cost which may require the business rather than the consumer to pay, a reasonably convenient location, reasonable time limits, a right to representation, encouragement of mediation, clear notice of the arbitration provisions and their consequences, access to information to ensure a fair hearing, a fair hearing, availability of all remedies that would be available in court, application by the arbitrator of pertinent contract terms, statutes and legal precedents and, on request, the provision of an explanation of the basis for the award. In addition, it provides that consumers retain the ability to take matters to small claims court that fall within small claims court jurisdiction.

An AAA-led Task Force released additional standards for consideration in a Consumer Debt Collection Due Process Protocol Statement of Principles which supplement the Consumer Due Process Protocols.[24] These additional Protocols include requirements that the commencement of the arbitration be in a manner that provides substantial certainty that the debtor will receive notice, that all communication be drafted in a manner easy to understand, including communicating in the consumer's primary language where known, that claims be accompanied by sufficient documentation to establish a prima facie case, that a procedure be established to identify time-barred claims, that the answer to the demand for arbitration be simplified, that the appointment of the arbitrator be done in a manner that enhances the perception of neutrality, and that participants take advantage where appropriate of technology such as e-mail, telephonic, or videotaped hearings and proceedings to save time and expense.

There has to date been no resolution of the debate as to class action waivers in the development of consumer arbitration fairness protocols because no consensus has been reached by the groups that have studied the issue. In the wake of the *AT&T v. Concepcion* decision, class action waivers will be an important issue for the Bureau to review. However, the Bureau's conclusion as to such waivers should not drive its broader conclusion as to arbitration. Regulation as to the validity of a class action waiver can simply be part of the development of a regulatory scheme that would ensure fairness in arbitration for consumers.

Conclusion

The Bureau has before it an important and difficult task in responding to the Congressional mandate under the Dodd-Frank Act. The conclusions reached in its study may influence future discussions of arbitration for consumers not only in the financial sector covered by the Dodd-Frank Act but also influence future consideration of consumer arbitration in legislation for a host of economic sectors. A thorough analysis of all of the pros and cons of arbitration for consumers and of the impact of any decision reached on the broader public interest should lead to a thoughtful and informed conclusion.

Endnotes

1. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1028, 124 Stat. 1376, (2010) (definitions for "covered person" and "consumer financial products or services" are provided in § 1002). The Dodd-Frank Act also authorizes the Securities and Exchange Commission to engage in rulemaking with respect to arbitration agreements.
2. For a listing of prior studies, *see* Comments to the Consumer Financial Protection Bureau in Connection with its Review of Arbitration for Consumer Financial Products or Services, adopted by the Dispute Resolution Section of the New York State Bar Association, Appendix A, April 2011, *available at* www.nysba.org/doddfrank.
3. Federal Trade Commission, *Repairing a Broken System: Protecting Consumers in Debt Collection Litigation and Arbitration* 37–71 (Jul. 2010), *available at* http://www.ftc.gov/os/2010/07/debtcollectionreport.pdf [hereinafter *Repairing a Broken System*].
4. Federal Trade Commission, *Collecting Consumer Debts: The Challenges of Change—A Workshop Report* iii (2009), *available at* http://www.ftc.gov/bcp/workshops/debtcollection/dcwr.pdf [hereinafter *Collecting Consumer Debts*].
5. *Repairing a Broken System*, *supra* note 3, at I.
6. *See* Public Citizen, *The Arbitration Trap: How Credit Card Companies Ensnare Consumers* (Sept. 2007), *available at* http://www.citizen.org/documents/ArbitrationTrap.pdf.
7. *See* Searle Center on Law, Regulation and Economic Growth, *An Empirical Study of AAA Consumer Arbitrations* (Mar. 2009) (hereinafter *Searle Consumer Arbitrations*); Searle Center on Law, Regulation and Economic Growth, *Creditor Claims in Arbitration and in Court, Interim Report No. 1*, 27 (Nov. 2009).
8. *See Judicial Business of the United States Courts, 2009 Annual Report of the Director*, *available at* http://www.uscourts.gov/uscourts/Statistics/JudicialBusiness/2009/JudicialBusinespdfversion.pdf.
9. Bureau of Justice Statistics, *Civil Justice Survey of State Courts (CJSSC), Bureau of Justice Statistics 2005*, *available at* http://bjs.ojp.usdoj.gov/index.cfm?ty=dcdetail&iid=242 (this is the most recent compilation of data by this source).
10. *Searle Consumer Arbitrations*, *supra* note 7, at 2.
11. National Center for State Courts, *Budget Shortfalls by State*, *available at* http://www.ncsc.org/information-and-resources/budget-resource-center/states-activities-map.aspx.
12. *See* B. Roy Weinstein & Stevan Porter, *Economic Impact on the County of Los Angeles and the State of California of Funding Cutbacks Affecting the Los Angeles Superior Court* (Dec. 2009), *available at* http://www.micronomics.com/articles/LA_Courts_Economics_Impact.pdf.
13. *See* The Washington Economics Group, Inc., *The Economic Impacts of Delays in Civil Trials in Florida's State Courts Due to Under-*

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Funding (Feb. 2009), *available at* http://www.floridabar.org/TFB/TFBResources.nsf/Attachments/1C1C563F8CAFFC2C8525753E005573FF/$FILE/WashingtonGroup.pdf?OpenElement.

14. *See Justice in the Balance: The Impact of Budget Cuts on Justice, Iowa Judicial Branch* (Jan. 13, 2010), *available at* http://www.iowacourts.gov/wfData/files/StateofJudiciary/JusticeInTheBalanceJan2010.pdf.
15. *See, e.g., Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972).
16. The award of pre-judgment interest, permissible in some cases, may compensate for all or part of this impact depending on the interest rate allowed and the appropriate discount rate to use.
17. The number of cases involved in consumer disputes is not *de minimis*. In 2006, approximately 320,000 consumer debt collection cases were filed in New York City alone. This number is comparable to the total number of civil and criminal cases filed in the federal trial courts nationwide that year. *See* THE URBAN JUSTICE CENTER, *Debt Weight: The Consumer Credit Crisis in New York City and its Impact on the Working Poor* 3 (Oct. 2007), *available at* www.urbanjustice.org/pdf/publications/CDP_Debt_Weight.pdf. Sixty percent of the 120,000 small claims cases filed in Massachusetts in 2005 were filed by debt collectors. In Cook County Circuit Court in Chicago, 119,000 cases against debtors were pending as of June 2008. *See Collecting Consumer Debts, supra,* note 4 *at* iii.
18. *See* Weinstein & Porter, *supra* note 12, at 1.
19. *See* The Washington Economics Group, *supra* note 13, at 12–17.
20. *See* AMERICAN BAR ASSOCIATION COALITION FOR JUSTICE, *Report on the Survey of Judges on the Impact of the Economic Downturn on Representation in the Courts* (Preliminary) (Jul. 12, 2010), *available at* http://new.abanet.org/JusticeCenter/PublicDocuments/CoalitionforJusticeSurveyReport.pdf.
21. UNCITRAL, Working Group III (Online Dispute Resolution) 22nd Session, 13-17 December 2010, Vienna, *available at* http://www.uncitral.org/uncitral/commission/working_groups/3Online_Dispute_Resolution.html.
22. U.S. Department of State Advisory Committee on Private International Law (ACPIL): Online Dispute Resolution (ODR) Study Group, 75 Fed. Reg. 66420 (Oct. 28, 2010), *available at* http://edocket.access.gpo.gov/2010/pdf/2010-27297.pdf.
23. *See* AMERICAN ARBITRATION ASSOCIATION, *Consumer Due Process Protocol*, *available at* http://www.adr.org/sp.asp?id=22019.
24. *See* AMERICAN ARBITRATION ASSOCIATION, National Task Force on the Arbitration of Consumer Debt Collection Disputes, *Consumer Debt Collection Due Process Protocol Statement of Principles* (Oct. 2010), *available at* http://www.adr.org/si.asp?id=6248.

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