November 19, 2014

Richard Cordray
Director
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, D.C. 20552

RE: Study Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Section 1028(a) Regarding Pre-dispute Arbitration Agreements.

Dear Director Cordray:

On behalf of the undersigned State Attorneys General, we write to encourage the Consumer Financial Protection Bureau (the "Bureau") to exercise its specific statutory authority to regulate the use of pre-dispute mandatory arbitration clauses in consumer agreements for financial products or services. As the chief consumer protection officers in each of our respective States,[1] we are concerned about such clauses and the class action prohibitions often associated with them.

The need for regulations to protect the public interest has never been so great. Over the past decade, judicial decisions and business practices have diminished consumers' rights and bargaining power with respect to contracts for financial services. Today, the average consumer nominally assents to all kinds of contracts without any opportunity or bargaining power to negotiate better terms. In such an environment, it is incumbent upon regulators with the power to effect change, such as the Bureau, to ensure that consumers have meaningful avenues for redress against those with whom they contract to provide financial services. Without such protections, one of the only means for consumer redress will be through the enforcement efforts of State Attorneys General and other regulators (including the Bureau).

The Federal Arbitration Act ("FAA") as conceived in 1925 was intended to facilitate arbitration of disputes between commercial entities of similar sophistication and bargaining

[1] The Attorney General of Hawaii is the chief law enforcement officer of the State of Hawaii, has the authority to appear on behalf of the state in all civil and criminal matters, and has concurrent jurisdiction to enforce consumer protection laws with the State of Hawaii Office of Consumer Protection.

power.[2] In recent years, however, this premise has eroded. Companies routinely impose mandatory arbitration in a wide range of consumer contracts where the consumer has little bargaining power. Increasingly, large corporations present consumers with "take it or leave it" fine print contracts containing pre-dispute arbitration clauses in which consumers are required to waive their right to seek judicial resolution of future disputes (and appeal thereof) in federal or state court. Courts have found such language binding on the consumer even if he or she is not aware of the clause, never saw the provision, and had no opportunity to negotiate or reject the clause.[3] Such clauses have become prevalent in contracts for financial products and services.

Mandatory pre-dispute arbitration is procedurally unfair to consumers, and jeopardizes one of the fundamental rights of Americans; the right to be heard and seek judicial redress for our claims. These contractual requirements are neither voluntary nor readily understandable for most consumers. Often consumers do not recognize the significance of these provisions, if they are aware of them at all. Investigative studies have revealed that arbitrators have a powerful incentive to favor the dominant party in the arbitration (i.e., the corporation) that is more likely to send them future cases.[4] This "repeat player bias" is unfair to the consumer, who is bound by

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[2] Congress enacted the Federal Arbitration Act, 9 U.S.C. § 1 *et seq.*, "to place arbitration agreements upon the same footing as other contracts. Thus, arbitration agreements are enforceable 'save upon such grounds as exist at law or in equity for the revocation of any contract.' 9 U.S.C. § 2. Of course, courts should remain attuned to well-supported claims that the agreement to arbitrate resulted from the sort of...overwhelming economic power that would provide grounds for the revocation of any contract." *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 33 (1991) (internal citation omitted). *See also AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011) (dissent) ("When Congress enacted the Act, arbitration procedures had not yet been fully developed. Insofar as Congress considered detailed forms of arbitration at all, it may well have thought that arbitration would be used primarily where merchants sought to resolve disputes of fact, not law, under the customs of their industries, where the parties possessed roughly equivalent bargaining power.").

[3] Such agreements are often found to be procedurally unconscionable when challenged on such grounds. *See, e.g., Nino v. Jewelry Exchange, Inc.*, 609 F.3d 191, 201 (3rd Cir. 2010) ("We have consistently found that adhesion contracts — that is, contracts prepared by the party with greater bargaining power and presented to the other party for signature on a take-it-or-leave-it basis satisfy the procedural element of the unconscionability analysis.") (internal quotation marks omitted).

[4] For example, in 2009, the Minnesota Attorney General's Office, filed a lawsuit against the National Arbitration Forum – then the largest arbitration company in the country for consumer credit disputes – following a year-long investigation, alleging that it misrepresented its independence and hid its extensive ties to credit card companies, other creditors, and the collection industry from consumers and the public. The litigation resolved with a Consent Judgment, barring the company from the business of arbitrating credit card and other consumer disputes. *See* Complaint, *State of Minnesota by its Attorney General, Lori Swanson v. National Arbitration Forum, Inc., et al.*, Minn. Dist. Ct., Hennepin County (July 14, 2009), *available at* http://www.ag.state.mn.us/pdf/pressreleases/signedfiledcomplaintarbitrationcompany.pdf. *See also* Testimony of Lori Swanson, Minnesota Attorney General, to U.S. Judiciary Committee on October 13, 2011, "Arbitration: Is It Fair When Forced?", *available at* http://www.cpradr.org/Portals/0/Resources/10132011ArbFairnessSenateTestimony/Swanson%20Testimo

the arbitrator's decision, without the option of further appellate review. High arbitration costs[5] and inconvenient venues combined with class action waiver provisions, which prohibit collective arbitration, deter injured individuals from pursuing their rights. Indeed, it is often economically irrational for a consumer to seek redress when the amount at stake is far less than the cost of filing and pursuing a claim through arbitration.

The predictable result of such a situation is not only unfairness to the harmed consumers, but also a systemic failure to hold accountable those companies who abuse the trust placed in them by consumers. The few claims that actually do make it to arbitration are typically only adjudicated as to a single consumer, due to inclusion of class action prohibitions. This means that a decision in favor of the consumer will have no precedential value or binding effect against the company with respect to legal proceedings brought by other consumers. Thus, a corporation's loss in one arbitral proceeding simply becomes a cost of doing business rather than a mandate to change unlawful business practices. Moreover, the prevalence of arbitration lessens the opportunity to develop judicial precedents that can set preventive standards for corporate conduct. As a result, corporations are less likely to be held accountable for wrongdoing.

Despite the clear harm to consumers and the public interest from the increased use of these arbitration clauses, the result of recent U.S. Supreme Court rulings is that arbitration clauses in all forms are virtually impenetrable – from even state legislation.[6] In some cases, the aggregation of small consumer claims in the form of private class action lawsuits or at least class action arbitrations affords consumers the only opportunity to seek relief, due to the expense of individually bringing their own case or the inability to procure legal representation. Moreover, many of our respective consumer protection laws include private right of action provisions which

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ny.pdf. Anecdotal evidence supporting this "repeat player" bias is also discussed in, Costs of Arbitration Report, Public Citizen's Congress Watch (Apr. 2002), at p.68, *available at* http://www.citizen.org/documents/ACF110A.PDF.

[5] *See, e.g., Costs of Arbitration Report*, Public Citizen's Congress Watch (Apr. 2002), at p.1 ("The cost to a plaintiff of initiating an arbitration is almost always higher than the cost of instituting a lawsuit. Our comparison of court fees to the fees charged by the three primary arbitration provider organizations demonstrates that *forum costs* – the costs charged by the tribunal that will decide the dispute—can be up to five thousand percent higher in arbitration than in court litigation. These costs have a deterrent effect, often preventing a claimant from even filing a case."), *available at* http://www.citizen.org/documents/ACF110A.PDF.

[6] The combined impact of *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011) and *American Express Co., et al. v. Italian Colors Restaurant et al.*, 133 S. Ct. 2304 (2013), the U.S. Supreme Court's most recent holdings on this issue, is that contractual mandatory arbitration clauses containing class action waivers are enforceable even when they render it functionally impossible for plaintiffs to vindicate their rights or effectively insulate companies from accountability for consumer claims.

are often pursued through class actions.[7] Based on our experience, such litigation has the capability of providing real and meaningful benefit to harmed consumers and can result in injunctive relief mandating business reforms that are in the public interest. Our offices work together to ensure that such relief and redress are maximized.[8]

We are aware that the Bureau has devoted significant time and resources to the extensive study requested by Congress in Section 1028(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, 12 U.S.C. § 5518(a), and that the Bureau may use the study's findings to inform a decision on, as well as the substance of, rulemaking. As the chief consumer protectors in each of our respective States, we encourage the Bureau to use its statutorily prescribed powers to protect the public interest by imposing prohibitions, conditions, or limitations on the use of pre-dispute arbitration clauses in agreements for consumer financial products or services. While it is true that the issues associated with mandatory arbitration are wide-reaching and that further legislative action is required to fully address the problem, the Bureau has the unique opportunity to do something in the important area of consumer financial products or services. The time is ripe to do so.

The fundamental right of consumers to assert their claims in court should not be eroded through mandatory pre-dispute arbitration clauses included in adhesion contracts. If we can

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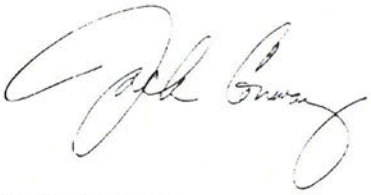
[7] California's Unfair Competition Law (UCL), Bus. & Prof.Code, § 17200 *et seq.* is one example. *See In re: Tobacco II Cases*, 46 Cal. 4th 298, 313 (2009), 207 P.3d 20, 30 (Cal. Sup. Ct. 2009) (stating that the UCL class action "is a procedural device that enforces substantive law by aggregating many individual claims into a single claim"); *Kraus v. Trinity Management Services, Inc.*, 23 Cal.4th 116, 126 (2000), 99 P.2d 718 (Cal. Sup. Ct. 2000) ("Class actions and representative UCL actions make it economically feasible to sue when individual claims are too small to justify the expense of litigation and thereby encourage attorneys to undertake private enforcement actions. Through the UCL a plaintiff may obtain restitution and/or injunctive relief against unfair or unlawful practices in order to protect the public and restore to the parties in interest money or property taken by means of unfair competition. These actions supplement the efforts of law enforcement and regulatory agencies. This court has repeatedly recognized the importance of these private enforcement efforts."), *modified by statute on other grounds as stated in Arias v. Superior* Court, 46 Cal.4th 969, 977-78, 209 P.3d 923, 928 (Cal. Sup. Ct. 2009).

[8] Pursuant to the Class Action Fairness Act of 2005 ("CAFA"), 28 U.S.C. § 1711, *et seq.*, each state Attorney General receives notice of proposed class action settlements filed in the federal courts. Together, through the National Association of Attorneys General ("NAAG"), we evaluate the substantive provisions of the settlements on a monthly basis and, in appropriate circumstances, our offices will reach out informally to class and defense counsel to discuss the settlement terms before deciding as a group whether a formal objection is required or feasible. As is often the case, the collective influence of the States through informal dialogue can lead settlement counsel to adjust the settlement terms in order to address our concerns. The consumer relief and injunctive terms afforded through these settlements, and the publicity stemming from them, can serve as a deterrent to the specific defendant as well as the greater business community or industry to combat otherwise unchecked unfair or deceptive business practices.

provide any further information or assistance related to the Bureau's study, or any other of our common objectives, please do not hesitate to contact us.

Respectfully Submitted,

Joseph R. Biden, III
Delaware Attorney General



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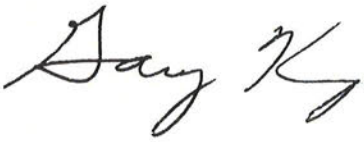

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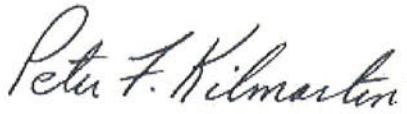

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