Responses to Submitted Questions for the Record
Senate Judiciary Committee Hearing on "Arbitration in America"

Hearing held April 2, 2019
Dirksen Senate Office Building, Room 226

Responses to Questions from Senator Chuck Grassley

1. Both of you mentioned in your testimony the fact that courts can invalidate unlawful arbitration agreements. Can you explain in a bit more detail how courts are already capable of doing this?

Response:

Most employers seek to provide employees with arbitration agreements that incorporate fair procedures, such as the special employment arbitration rules applied by the American Arbitration Association (AAA)[1] and JAMS.[2] In the rare situation in which an employment arbitration agreement contains provisions that are unfair, courts can and do step in and declare those provisions unenforceable.

The Federal Arbitration Act (FAA) expressly permits courts to invalidate arbitration agreements on grounds that would allow for the "revocation of any contract."[3] This means, as the U.S. Supreme Court has explained, that arbitration agreements are subject to "'generally applicable contract defenses, such as fraud, duress, or unconscionability.'"[4]

The doctrine of unconscionability, which allows courts to refuse to enforce a contract that is deemed to be unfair, is a particularly powerful tool for courts in reviewing arbitration agreements. For example, under the doctrine of unconscionability, courts have invalidated arbitration provisions that: purported to limit claimants' entitlement to remedies available to them under state and federal law; required claimants to pay excessive fees to access the arbitral forum; unreasonably shortened applicable statutes of limitations; required arbitration to take place in inconvenient locations for claimants; required claimants to pay the full costs of the arbitration, regardless of who wins; unduly limited the discovery available to claimants; or provided for unfair procedures for selecting arbitrators. Courts have also invalidated arbitration provisions that purported to impose "gag orders" on claimants and to prevent them from discussing their claims publicly, or with law enforcement officials.

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[1] *See* Am. Arbitration Ass'n, *Employment Arbitration Rules and Mediation Procedures*, *available at* perma.cc/3DK8-4K42.

[2] *See* JAMS, *JAMS Employment Arbitration Rules & Procedures* (July 1, 2014), *available at* perma.cc/N5CX-CTB8.

[3] 9 U.S.C. § 2.

[4] *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 339 (2011) (quoting *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 687 (1996)).

In short, businesses have a powerful incentive to ensure that the arbitration agreements they use are fair to individuals—both because it is good business and the right thing to do, and also because unfair provisions will not be enforced by the courts.

2. Some of the witnesses at the hearing said that arbitration agreements harm consumers by preventing them from joining a class action. Used appropriately, class actions can create efficiencies and ensure justice. But they can also be abused. One of the goals of the bipartisan Class Action Fairness Act of 2005, which I authored, was to make sure that class members actually get compensation and aren't taken advantage of by their lawyers.

   However, one of the witnesses, Professor Gilles, wrote in a law review article, "Class action plaintiffs' lawyers are indeed independent entrepreneurs driven by the desire to maximize their gain, even at the expense of class members' compensation. Where the conventional wisdom has gone wrong, however, is in condemning this as a bad thing…."[5] She goes on to say, "there is generally no legitimate utilitarian reason to care whether class members with small claims get compensated at all. Nor is there any economic reason to fret that entrepreneurial plaintiffs' lawyers are being overcompensated."[6]

   a. Do you agree with Professor Gilles that there's no reason to care whether members in a class action get compensated at all?

Response:

I respectfully disagree with Professor Gilles' view that there is no reason to care whether members in a class action obtain compensation (or whether plaintiffs' lawyers are overcompensated via class actions). The fundamental purpose of a class action is to provide a mechanism for redress for harms to groups of individuals who experienced those harms in the same or similar manner. The reason why the class action device was adopted was the theoretical view that individuals with relatively modest monetary claims, who would likely not be able to pursue litigation in court individually, could join together to obtain a recovery.

The class action device has never been a tool designed to encourage entrepreneurial plaintiffs' lawyers to bring lawsuits regardless of whether class members actually benefit. In fact, the clear trend in the law with respect to class actions has been to *prevent* plaintiffs' lawyers from reaping the lion's share of monetary benefits at the expense of class members. As you stated, a key objective of the Class Action Fairness Act of 2005 was to help ensure that class members actually obtain compensation and are not taken advantage of by plaintiffs' lawyers. Amendments over the past several decades to Federal Rule of Civil Procedure 23 governing class actions similarly seek to protect class members against potential abuse by class counsel.[7]

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[5] Myriam Gilles & Gary B. Friedman, *Exploding the Class Action Agency Costs Myth: The Social Utility of Entrepreneurial Lawyers*, 155 U. Pa. L. Rev. 103, 104 (2006).

[6] *Id*. at 105.

[7] *See* Fed. R. Civ. P. 23 (explaining in Committee Notes to various rule amendments changes designed to improve the adequacy of class counsel selection and representation, and the determination of reasonable attorney fees and notice to class members).

The fact that many class members still end up receiving nothing at all in a "successful" class action is an enormous problem that should be addressed by courts or through legislation. Lawyers should use the litigation system to represent clients, not themselves. As I noted in my testimony, the CFPB itself recognized that nearly 88% of the class actions it studied delivered no benefits to class members whatsoever, and that in the remaining 12%, the "weighted" claims rate was 4%—meaning that 96% of class members did not benefit in those so-called "successful" class actions. That should not be treated as an acceptable outcome. The substantial inefficiencies on display in many modern class actions provide strong support for the use of arbitration as a simpler, fairer, and faster means of dispute resolution.

One legislative reform approach that might be considered to better align the incentives of class action lawyers with class members is to set plaintiffs' lawyer legal fees based on amounts actually collected by class members.[8]

Responses to Questions from Senator John Kennedy

1. I will be introducing the Stop Blaming Victims Act to address the problem of Nondisclosure agreements being used to protect government employees who sexually harass others. It would limit the ability of government employees to hide behind non-disclosure agreements. NDA's are dangerous because they are often mandatory elements of a settlement that prevent victims from speaking out later on when they see similar abuses repeated. How are mandatory NDA's used in forced arbitration? Are they also used to silence wronged parties who might seek to expose wrongdoing at a powerful company?

Response:

As stated in my written testimony, claimants subject to a pre-dispute arbitration agreement are free to discuss their claims publicly and to report alleged wrongdoing to law enforcement officials. If an arbitration agreement purported to impose a "gag order," that restriction is likely to be invalidated in court.[9]

The use of an NDA as a condition of the *settlement* of an arbitration proceeding, just like a settlement of a threatened or filed lawsuit in court, presents an entirely different legal situation. Here, the claimant has the choice of whether he or she wants to settle the dispute on the terms offered by the defendant. The claimant is under no obligation to accept terms in which he or she agrees not to discuss the dispute with others. The inclusion of an NDA is simply one factor, among others such as the amount of compensation at issue, that the claimant would weigh in deciding whether to agree to a proposed settlement. If the claimant values sharing his or her story publicly with the media or others more than what is offered in exchange for agreeing not to

[8] *See, e.g.*, H.R. 985, 115th Cong. (2017) (passed House; not acted on by Senate).

[9] *See, e.g.*, *Davis v. O'Melveny & Myers*, 485 F.3d 1066 (9th Cir. 2007), *overruled on other grounds by Kilgore v. KeyBank, Nat'l Ass'n*, 673 F.3d 947 (9th Cir. 2012); *Longnecker v. Am. Express Co.*, 23 F. Supp. 3d 1099 (D. Ariz. 2014).

share that information, the case would not settle. Thus, a defendant is not forcing anything on anyone; the claimant is engaging in an arms-length settlement negotiation.

Significantly, the inclusion of NDAs (or confidentiality provisions) in *settlement agreements* has nothing to do with arbitration whatsoever. As you know, most lawsuits filed in court that are not dropped or dismissed are settled, and many of those settlements (in all sorts of contexts, not sexual harassment alone), are subject to confidentiality provisions.

Moreover, the particular problem you mention—of confidential settlements of claims that government employees have engaged in sexual harassment—is one that arises in the context of the court system, not arbitration, because government employees often do not enter into employment arbitration agreements.

2. Courts consistently rule that claims under the Uniformed Services Employment and Reemployment Rights Act, which protects the employment rights of members of the armed forces, are subject to arbitration under the Federal Arbitration Act. We should be ensuring that our military men and women are adequately protected. How is it fair that an employer can fire an employee who leaves for combat and often times their only recourse is arbitration? What in your opinion needs to be done to correct this?

Response:

There is an underlying presumption in this question, with which I respectfully disagree, that arbitration is somehow unfair or less fair than litigation as a means of adjudicating a dispute. As stated in my written testimony, I believe (and numerous studies show) that arbitration provides claimants with even-handed justice, and often does so more quickly and at a lower cost. These benefits include the arbitration of employment disputes involving a member of our armed services.

In fact, the arbitration of an employment dispute may provide significant benefits compared to civil litigation where the dispute involves a member of the military stationed overseas or deployed in an active combat zone. Arbitration proceedings typically involve less rigid procedures and less time investment on behalf of claimants, which is an important consideration for someone involved in active military service. The comparative flexibility of arbitration proceedings also allows for greater accommodations and convenience for a member of the military, for instance participation in the adjudication via video conferencing as opposed to having to take leave and appear in a court proceeding in the United States (which may not be an option for an overseas service member).

3. In the past couple of years, more and more companies have eliminated forced arbitration. Over the last year, Uber, Lyft, Facebook, and Google and many others have scrapped their arbitration policy. Why do you think we are seeing this uptick in companies ending their forced arbitration policy?

Response:

I believe the decision by some companies to curtail the use of pre-dispute arbitration agreements reflects ordinary market forces at work. As stated in my written testimony, there are, in many instances, marketplace alternatives for consumers and employees to choose to purchase a product or service, or choose to apply for a job, that would not involve agreeing to arbitrate a subsequent dispute. If prospective employees in the tech industry, or any other industry, place value on working for an employer that does not include a pre-dispute arbitration agreement as a condition of employment, employers in a competitive marketplace will typically adjust and offer that option. Ultimately, consumers and employees benefit from greater options. The decisions by companies such as Uber, Lyft, Facebook, and Google demonstrate that ordinary market forces can and should be relied upon, and that banning or otherwise restricting the use of pre-dispute arbitration agreements is not needed or justified.

Responses to Questions from Senator Thom Tillis

1. This Committee is acutely aware of the backlog in today's federal courts. And, my understanding is that the state courts are even worse. Can you give us a sense of how individuals that have big enough claims to actually hire a lawyer and go to court fare in court versus employees and consumers who go through arbitration? How long does it typically take to go through arbitration versus the court system?

Response:

As your question suggests, the civil litigation system can be very impractical for consumers and employees to obtain justice. Studies show that plaintiffs' lawyers typically will not take a case in which the expected value is less than a hundred thousand dollars or more. This fact is understandable as plaintiffs' lawyers working under a contingency fee agreement are compensated only if they win and litigation may consume many hours of a lawyer's time as well as resources that could be used elsewhere. As a result, plaintiffs' lawyers are likely only to take cases involving substantial damages and a high probability of success. These "real life" factors create a major barrier to entry for a claimant with a comparatively modest and individualized harm. Accordingly, any comparison between the civil litigation system and arbitration system must begin with the understanding that the arbitration system adjudicates many claims that would have been weeded out by the civil litigation system purely on account of economic considerations.

When claimants are able to attract the assistance of a lawyer and obtain access to the courts, studies show they fare about the same as claimants proceeding in arbitration. As a study published in the Stanford Law Review, which analyzed other arbitration studies, found, "there is no evidence that plaintiffs fare significantly better in litigation" than arbitration, and "[i]n fact, the opposite may be true."[10] Thus, the clear takeaway from the empirical evidence is that claimants fare at least as well in arbitration as they would in the civil litigation system.

[10] David Sherwyn et al., *Assessing the Case for Employment Arbitration: A New Path for Empirical Research*, 57 Stan. L. Rev. 1557, 1578 (2005).

Claimants in arbitration proceedings are also able to obtain even-handed justice in a far more timely manner compared to civil litigation. The most recent federal court case management statistics state that the median time between the filing of a civil case and trial is 27.5 months (i.e. more than two years).[11] The percentage of federal civil cases more than three years old has also more than doubled in the last five years, from 8.8% of cases in 2013 to 18.3% of cases in 2018.[12] Studies of arbitration, in comparison, show that disputes are typically resolved in four to seven months.[13] Hence, the data show that arbitration often shaves months or years off the resolution time of a claim.

2. I routinely hear that courts have no ability to review arbitration agreements. Is that accurate?

Response:

No. As detailed in my response to a similar question by Senator Grassley at the beginning of this document, courts have a variety of tools in which to evaluate and potentially invalidate pre-dispute arbitration agreements. The contract doctrine of unconscionability, for example, is often invoked by claimants challenging any arbitration contract term that may be unduly harsh or unfair.

3. I understand that the American Arbitration Association (AAA), the country's largest arbitration provider, developed an Employment Due Process Protocol that articles key principles for ensuring fairness in arbitration. Can you describe some of those due process protections for the Committee?

Response:

The AAA's Employment Due Process Protocol sets forth basic rights, responsibilities, and qualifications of entities involved in an employment arbitration to ensure fairness in the proceeding.[14] The Protocol is the product of engagement by a multiplicity of stakeholders, including those representing businesses, arbitrators, labor unions, lawyers, and other professionals. One of the basic rights set forth in the Protocol is that employees may be represented by an attorney or spokesperson of their own choosing in any arbitration proceeding. The Protocol also states that employees or their representative should be provided reasonable

[11] *See United States District Courts – National Judicial Caseload Profile* (2018), at https://www.uscourts.gov/statistics-reports/analysis-reports/federal-court-management-statistics.

[12] *See id.*

[13] *See* Consumer Arbitration Before American Arbitration Association, Searle Civil Justice Inst., xiii, 8 (2009), *available at* https://www.adr.org/sites/default/files/document_repository/Searle%20Civil%20Justice%20Institute%20Report%20on%20Consumer%20Arbitration.pdf (discussing results of arbitration study as well as results of other empirical studies).

[14] *See* Employment Due Process Protocol, Am. Arbitration Ass'n (1995), *available at* https://www.adr.org/sites/default/files/document_repository/Employment%20Due%20Process%20Protocol_0.pdf.

access at all times to information and documentation at issue in the arbitration proceeding. It additionally provides that the arbitrator should have the authority to order fee reimbursement, in whole or in part, as part of an employee's remedy in accordance with the applicable law or in the interests of justice.[15]

In addition, the Protocol states that impartial arbitrators should be selected to preside over any employment dispute, and that a selected arbitrator should be knowledgeable about the conduct of hearings and the issues at stake, and possess familiarity with the workplace and employment environment. The Protocol further encourages training programs to educate arbitrators on substantive laws and procedural and remedial issues governing the employment relationship to improve consistency and due process in proceedings.

The Protocol additionally provides recommendations regarding the selection of arbitrators from a roster, pool, or selection panel to eliminate potential bias or conflicts of interest. It reaffirms an arbitrator's duty to disclose any relationship that might reasonably constitute or be perceived to create a conflict of interest, and that an arbitrator should be required to sign an oath affirming the absence of such present or preexisting ties. Finally, the Protocol states that the arbitrator should be bound at all times by the applicable agreements, statutes, regulations and relevant rules of procedure, and should issue an opinion summarizing the disputed issue and basis for disposition of the claim. All of these elements of the Protocol exist to protect due process interests and ensure a just outcome.

4. The Consumer Financial Protection Board during the Obama Administration in a 2015 study found that in 562 class action cases filed from 2010 to 2012, the consumer received nothing, mostly because trial lawyers negotiated settlements that paid their fees without any cash payment for the consumer.

   Is it not common in many class action settlements for consumers to fail to recover a single penny because of the demands of trial lawyers to satisfy their contingency fee arrangements before any recovery for the consumer?

Response:

As your question suggests, many class action settlements today do not advance the interests of consumers. Instead, the lawyers who bring consumer class actions are the real beneficiaries because they control the settlement negotiations on behalf of the class and can orchestrate the payment of substantial attorney fees.[16] Consumers swept into a class, at times without realizing

[15] In cases in which an employee initiates arbitration against the employer under the employer's arbitration plan, the AAA's Employment Rules cap the employee's filing fee at $300—less than the cost of initiating a lawsuit in federal court. *See* Am. Arbitration Ass'n, *Employment/Workplace Fee Schedule* at 1 (Oct. 1, 2017), at https://www.adr.org/sites/default/files/Employment_Fee_Schedule.pdf.

[16] *See, e.g.*, Joanna Shepherd, *An Empirical Study of No-Injury Class Actions* 2, 5 (Emory Univ. Sch. of L., Legal Studies Research Paper Series No. 16-402, Feb. 1, 2016), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2726905 (finding in study of 432 class

they are "in" a class action, may be entitled to some small measure of compensation, but frequently remain absent and recover nothing at all. Consumers, for instance, may not want to bother filling out complex paperwork to collect only a small sum. Numerous studies have reported average claims rates in consumer class actions of single-digit percentages, meaning the vast majority of class members obtain no benefit.[17] Even the CFPB's analysis reported a "weighted average claims rate" in class actions of just 4%—meaning that 96% of class members did not benefit.[18]

The costs incurred to effectuate such a transfer of funds to a class of consumers can be enormous. A business involved in a class action may incur millions of dollars in legal fees and other expenses in addition to the settlement funds paid, which, in turn, will be passed on to consumers. As a result, in the "real world," many consumers may end up worse off when a plaintiff and his or her lawyer "win" a class action.

5. Some say that companies prefer arbitration because arbitration is skewed against the claimant, meaning the company is more likely to prevail on the matter, and even if they don't win, they will have to pay a lesser amount in damages than if the matter was litigated. Is there any evidence to support the claim that employees and consumers are likely to make out better through litigation – both in terms of prevailing in the suit and the amount recovered?

Response:

As discussed in my response to the first question about how claimants fare in civil litigation versus arbitration, empirical studies find "no evidence that plaintiffs fare significantly better in litigation."[19] "In fact, the opposite may be true" that claimants fare better in arbitration because a "critical question is not what happens at the final stage, but instead what happens to the claims that never make it that far."[20]

As explained previously, a comparison of outcomes in the civil litigation system and arbitration system must begin with the understanding that the arbitration system adjudicates many claims that would have never seen the light of day if pursued in the civil litigation system because no lawyer would agree to take the case. A lawyer might decline to do so because the expected value of the case is too low to justify his or her investment of time and resources, or because the claim is of a less certain nature (or both). The availability of arbitration in such situations is a

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action settlements from 2005-2015 that approximately 38% of settlement proceeds was allocated to attorney fees and that class members ultimately received less than 9% of settlement funds).

[17] *See id.*; Mayer Brown LLP, *Do Class Actions Benefit Class Members? An Empirical Analysis of Class Actions* 7 (Dec. 11, 2013), *available at* https://www.mayerbrown.com/files/uploads/Documents/PDFs/2013/December/DoClassActionsBenefitClassMembers.pdf.; *see also* Linda Mullenix, *Ending Class Actions as We Know Them: Rethinking the American Class Action*, 64 Emory L. J. 399 (2014).

[18] *See* Consumer Fin. Pro. Bureau, *Arbitration Study: Report to Congress 2015* 30 (Mar. 2015).

[19] Sherwyn, *supra* note 10, at 1578.

[20] *Id.*

testament to greater access to justice for the claimant even if the defendant prevailed in a comparatively greater number of these types of cases.

With respect to amounts recovered in civil litigation versus arbitration, it is difficult to make a direct comparison. Civil litigation generally involves a greater investment of time and resources than arbitration (which is one of the reasons arbitration may be preferable), so the amount of compensation obtained in litigation would presumably need to be greater as well to account for those expenditures. Also, the vast majority of litigations involve representation by an attorney, whereas many arbitrations do not involve an attorney who would be paid out of any recovery. Attorneys operating under a contingency fee agreement may take one-third or more of any recovery (as well as expenses), so a claimant obtaining a 25% greater recovery in the litigation system could end up with less after paying his or her attorney compared to an arbitration that either did not involve an attorney or involved an attorney with a relatively low hourly fee. Further, the cases pursued in the litigation system by contingency fee lawyers are those the lawyer feels confident of a "win" through a substantial judgment or settlement, whereas arbitration opens the door to adjudication for persons with more uncertain claims involving lower amounts at issue and expected recoveries. Thus, any dollar for dollar comparison could present a misleading picture of how well the consumer actually fares.

That said, even with those caveats, the available data show that the outcomes that claimants achieve in arbitration are as good or better as those achieved in court. One empirical analysis, for example, showed that employees who arbitrate are more likely to win their disputes than those who litigate in federal court (46% in arbitration as compared to 34% in litigation); that the median arbitral awards that the employees obtained were typically the same as, or larger than, the amount obtained in court; and their arbitrations were resolved 33% faster than in court.[21] Another study examined AAA awards and determined that, for higher-income employees' claims, there was no statistically significant difference in win rates or amounts between discrimination and non-discrimination claims.[22] As an article published in the Stanford Law Review surveying the empirical research on arbitration concluded, "[w]hat seems clear from the results of these studies is that the assertions of many arbitration critics were either overstated or simply wrong."[23]

[21] *See* Michael Delikat & Morris M. Kleiner, *An Empirical Study of Dispute Resolution Mechanisms: Where Do Plaintiffs Better Vindicate Their Rights?*, 58 Disp. Resol. J. 56, 58 (Nov. 2003-Jan. 2004).

[22] *See* Theodore Eisenberg & Elizabeth Hill, *Arbitration and Litigation of Employment Claims: An Empirical Comparison*, 58 Disp. Resol. J. 44, 45-50 (Nov. 2003/Jan. 2004).

[23] Sherwyn et al., *supra* note 10, at 1567.