

Ernst & Young LLP recently released a report discussing the outcomes of binding mandatory arbitration (“BMA”) in credit-related, consumer-initiated arbitration cases.¹ As an increasingly standard contract provision, consumers often unknowingly or feel compelled to accept pre-dispute BMA clauses in their contracts. These clauses strip consumers of their right to dispute claims in a court with a jury of their peers and provides corporations with substantial advantages to defend against their misdeeds. The Center’s evaluation of the Ernst & Young report questions the ability of the researchers to draw general conclusions about consumer arbitration based on its methodology and limited review of data. Further, our analysis shows that the report did not successfully demonstrate its claims that borrowers are not disadvantaged by BMA clauses or that they do well in arbitration versus litigation.

Lack of comparison with litigation cases misses key discussion point. The impact of BMA clauses pivots around whether consumers would be better off using arbitration as compared to litigation. Yet, the study does not examine outcomes for comparable cases in litigation. The report does not measure the differences between a decision from a jury of peers versus that of an arbitrator, monetary award amounts between litigation and arbitration, or the prohibitive costs of arbitration as compared with class action lawsuits.

Assumptions about prevailing party inaccurately portray outcomes. Consumer claimants are considered to prevail if the arbitration decision ruled in their favor, or if the case was dismissed at the claimant’s request or per party agreement. In at least one case in the study’s AAA data set, the consumer was considered to be the prevailing party because the arbitrator ruled in their favor without awarding any monetary compensation. It is flawed to assume that consumer dismissal equates to consumers prevailing when it is likely that consumers may be compelled to withdraw their claim or settle under negative circumstances. These assumptions do not take into account other mitigating factors, such as the consumer realizing their poor bargaining position within the arbitration process or consumers trying to avoid additional arbitration fees.

Assumptions about complaint success rates misguided. The report assumes that both parties would prevail approximately 50 percent of the time in arbitration hearings. It is imperative that the data reference complainant success rates in litigation and use this as comparison criteria to evaluate favorability of the arbitration process.

Limited data precludes general conclusions. The arbitration outcomes report reviews 226 cases filed with the National Arbitration Forum (“NAF”) between January 2000 and January 2004. The report does not indicate if this set of cases compiles all of the lending-related, consumer-initiated arbitration cases during that period or if it is a subset of a larger pool selected upon unknown criteria. Further, assuming that the data sample proportionally reflects the number of cases arbitrated, it excludes the

¹ Ernst & Young LLP, *Outcomes of Arbitration: An Empirical Study of Consumer Lending Cases*, November 30, 2004. The study was commissioned by Wilmer, Cutler, Pickering, Hale and Dorr LLP with funding provided by the American Bankers Association.

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larger pool of consumer claims that would have been brought except for the BMA clause. Costly arbitration fees, decreased award amounts, and difficulty in finding legal representation provide significant barriers for consumers to pursue claims. Therefore, the report's conclusions are misguided because of the limitations regarding which cases fall within the sample and by the impact of the questioned policy on the sample size.

Survey to determine consumer satisfaction inadequate. The report looks at an even smaller subset of the limited data pool to assess consumer satisfaction with the BMA process. Based on 29 responses, the survey purported to review whether consumers thought they required legal representation and their satisfaction with the magnitude of arbitration fees. Unfortunately, the survey questions did not accurately reflect the desired representations.

Inquiry into arbitration costs incomplete. The survey respondents were asked, "how they would characterize the costs associated with arbitration." This question makes no distinction between cases in which the company agreed ahead of time to pay for the costs of arbitration and cases in which the consumer paid. It also makes no distinction between court fees versus arbitration fees. Finally, the survey does not account for consumers who may have been eligible for lawsuits with contingency fees if there was no BMA clause or for consumers who were unaware of alternative, more affordable options that could have been available.

Legal representation conclusions misleading. Responses to whether or not consumers hired a legal representative does not lead to the report's suggestion that consumers may have found the process "straightforward enough not to require the assistance of legal representation." The question does not explore the reason why consumers did not have legal representation, such as cost or lack of familiarity with arbitration proceedings. It would have been more revealing to ask survey respondents without representation if they wished they had legal counsel in retrospect or if they were able to find legal counsel willing to represent them in arbitration.

This report is not compelling in its efforts to prove that BMA clauses are not biased toward business or less favorable to consumers. The problematic conclusions do not overcome arguments that pre-dispute, BMA clauses poses a serious threat to the ability of consumers to protect themselves against abusive practices.

- BMA clauses are contradictory to the expectation of most consumers that if they need redress against an abusive practice, they will have access to a court of law.
- BMA clauses typically limit the claims and defenses available to consumers allowed under law
- Arbitration is almost always a confidential process, which leads to unpredictability and disadvantage for consumers who lack adequate understanding of the process.
- Corporations are often repeat-players in arbitration leading to an advantage over newcomer consumers who do not have the established relationships existing between arbitration forums and corporate clients.
- The filing and administrative costs of arbitration are routinely more costly than court fees, deterring many meritorious claims.

Pre-dispute, BMA clauses remain detrimental to a consumer's ability to vindicate their legal rights and should be removed from contracts.