Auto Safety Group • Congress Watch • Energy Program • Global Trade Watch • Health Research Group • Litigation Group
Joan Claybrook, President

June 15, 2007

The Honorable Mary M. Cheh
1350 Pennsylvania Avenue NW
Suite 108
Washington, DC 20004

Re: B17-050, Arbitration Amendments Act of 2007

Dear Councilmember Cheh,

We write to address the objections and concerns that have been raised to B17-50, the Arbitration Amendments Act of 2007. We would welcome the opportunity to meet with you in the near future to discuss the consumer-friendly aspects of the bill.

B17-50 Was Rightly Adapted To Protect Consumers From Abusive Arbitration Practices

Some have noted a concern that, as a general matter, altering a model bill lessens uniformity and that uniformity is a positive goal. Yet model bills are routinely altered by state legislatures to better reflect the will of its residents. Thus, a mere preference for uniformity should not take precedence over the right of the District to adapt model bills to address the particular circumstances within its jurisdiction. As the District Councilmembers know all too well, self-governance is the essence of democracy.

Indeed, it is not out-of-the-ordinary that the model arbitration bill, the Uniform Arbitration Act of 2000 ("RUAA")[1], has been altered. The changes attempt to re-balance, to the extent possible given the overlay of the Federal Arbitration Act ("FAA"), the very unfair playing field faced by consumers forced into arbitration. These much-needed changes are a legitimate effort to respond to the state of consumer arbitration in the District and should be applauded, not opposed. We would note that other changes, distinct from those helping consumers, were made to the model bill,[2] particularly one advanced by insurers in the District for the benefit of insurers.[3]

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[1] The RUAA was drafted by the National Conference of Commissioners on Uniform State Laws (NCCUSL) in 2000.
[2] Section 16-4429 is altered from the RUAA model bill to accommodate the District's electronic practices, while the RUAA provision on venue is deleted, given the nature of the District.
[3] Section 16-4404(c) states:

> if there is an agreement to arbitrate disputes over insurance obligations by two or more insurers, reinsurers, self-insurers, or reinsurance intermediaries, or any combination of them, the parties to the agreement may waive the right to vacatur under § 16-4423.

Importantly, several states that have adopted the RUAA[4] made changes to the model bill – changes that are wide-ranging – demonstrating that state legislative bodies typically adapt model bills to address the concerns playing out within their jurisdictions. For example:

- Colorado added protections to ensure important procedures could not be waived by an arbitration agreement which covers future disputes;[5]
- New Jersey added disclosure requirements for arbitrators;[6]
- Oregon added a provision protecting the right to a jury trial in some circumstances;[7]
- New Mexico voids all clauses written into form contracts that would modify or limit procedural rights useful to consumers.[8]

The District clearly has the ability to attempt to remedy the terrible environment that exists now for consumers, who are stuck arbitrating disputes because of pre-dispute binding mandatory arbitration ("BMA") clauses in standardized form contracts for the purchase of many goods and services. The Council should seize this opportunity to provide much-needed consumer protections from abusive arbitration practices rather than endorsing broad and unhelpful generalizations about uniformity. Fairness to District residents should not be sacrificed for the sake of uniformity. Simply stated, any model bill – and particularly a bill, like the arbitration model law, that is yet to be adopted in any form by most states and has been altered by several states that have adopted it – should not trump a strong bill that would help to level the playing field for consumers.

The Bill Protects District Residents by Banning Pre-Dispute BMA Clauses in Insurance Contracts

Without a doubt, the District has the legal authority to protect residents from being forced into arbitration by insurers to resolve disputes over the extent of health care coverage, nursing home care or auto coverage. Twenty-three states have enacted laws or regulations that ban pre-dispute binding mandatory arbitration clauses ("BMA") from all or some insurance contracts.[9] *See attached Letter from the Center for Responsible Lending (Apr. 6, 2007) to the Honorable Phil Mendelson at 3 and n. 4 and Attachment 1 (Supplement to the Record of the Hearing on B17-500).* In every state where this issue has been litigated, these exclusionary provisions were upheld and found not to be pre-empted by the force and effect of the FAA. *Id.* at 3, n. 6. In these cases, the courts have held that state laws regulating insurance cannot be pre-empted by the FAA because a federal law, the McCarran-Ferguson Act, expressly gives states authority to regulate the business of insurance, which no federal law unrelated to insurance can defeat.[10] As the FAA is unrelated to insurance, the courts have held that the

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[4] *See* Uniform Law Commissioners: The National Conference of Commissioners on Uniform State Laws, "A Few Facts About The Uniform Arbitration Act of 2000," available at http://www.nccusl.org/Update/uniformact_factsheets/uniformacts-fs-aa.asp

[5] COLO. REV. STAT. § 13-22-204(2).

[6] N.J. STAT. ANN. § 2A:23B-12 (f).

[7] OR. Rev. Stat. § 36.625(8).

[8] N. M. STAT. § 44-7A-5.

[9] Arkansas, Georgia, Hawaii, Iowa, Kansas, Kentucky, Louisiana, Maryland, Mississippi, Missouri, Montana, Nebraska, Nevada, New Mexico, Oklahoma, South Carolina, South Dakota, Tennessee, Utah, Virginia, West Virginia, Washington, Wyoming.

[10] The McCarran-Ferguson Act expressly states that no federal law shall invalidate or impair any state law that regulates insurance unless the federal law specifically relates to insurance. 15 U.S.C. § 1012(b).

FAA cannot nullify a state law banning pre-dispute binding mandatory arbitration clauses in insurance contracts.

It is also readily apparent that there are several reasons why it would be good policy for the District to protect consumers from being forced to arbitrate disputes against insurance companies (which mostly have a national presence) when dangerous or defective products or services cause significant physical or monetary harm. As an initial matter, there is no reason to believe that such a ban would limit the ability of District residents to obtain insurance. The District is a very lucrative market which insurers would not likely turn away from. Insurance remains widely available in states that have instituted complete or partial bans. *Id*. at 3 and Attachment 2.

Moreover, District consumers today cannot "just say no" to pre-dispute binding mandatory arbitration when insurance is required by law – including for products like car insurance, homeowners' insurance (often required as a condition of receiving a loan to purchase the home), or health insurance (often a non-negotiated part of an employment benefits package) – or insurance otherwise essential to daily living. Given the much more powerful position insurance companies occupy in the marketplace, special attention must be given to contracts of adhesion in that industry.

In addition, a ban on BMA clauses in consumer insurance contracts would mean that insurers could no longer insulate themselves from the oversight that benefits District residents. Currently, District insurance regulators cannot determine if an insurer operating in the District is complying with the District laws and regulations when BMA clauses are included in a contract because arbitration results are secret.[11] Indeed, lawsuits show that insurers do deny many valid claims or fail to investigate claims appropriately, as we have seen most recently in the conduct of State Farm Insurance (an insurer doing business in the District) in the aftermath of hurricane Katrina. *Id*. at 2, n. 2.

Importantly, insurers would remain free to enter into arbitration agreements with customers *after* a dispute arises. Section 16-4403(c) would only apply when insurers make arbitration of any future dispute a condition of purchasing the insurance. Thus, consumers and insurers in the District could still agree to arbitration after an actual dispute occurs. Consumers could assess whether arbitration is appropriate and in their best interest. Many consumers may in fact opt for arbitration for more minor claims. But where substantial physical or monetary harm occurred, a consumer could decide to exercise their constitutional right to a jury trial.[12] Right now, that fundamental constitutional guarantee is, in effect, eviscerated.

Finally, some have indicated a concern that this ban on pre-dispute BMA clauses would "flood" the courts with litigation.[13] This claim should be disregarded entirely. There is no evidence to show that for the 23 states – nearly half of the country – that ban BMA clauses from some or all insurance contracts, there was a stampede to the courts. Indeed, Chief Judge Rufus G. King, III, of the Superior Court of the District of Columbia submitted a written statement to the Committee of the

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[11] The grounds for overturning or modifying an arbitration award are quite narrow. *See Lessin v. Merrill Lynch, 481 F.3d 813, 821 (D.C. Cir. 2007), citing to LaPrade v. Kidder, Peabody & Co., 246 F.3d 702, 706 (D.C.Cir. 2001)*(rejecting claim alleging arbitration award made in manifest disregard of law*); see also* 9 U.S.C. § 10.

[12] While not all disputes necessarily would give rise to the constitutional right to a jury trial under the 7th Amendment, clearly many matters would be encompassed by that amendment's guarantee to a jury trial.

[13] Some insurers like the Property Casualty Insurers Association of America also have expressed this same concern. *See* Property Casualty Insurers Association of America, *PCI Comments to Proposed Bill DC B 17-50* (Mar. 23, 2007).

Judiciary in support of the bill.[14] As noted above, insurers are free to negotiate with customers to arbitrate any dispute and it is likely that consumers would do so in some cases.

If arbitration is as fair, speedy and inexpensive as insurers suggest, then they should have no fear because consumers will choose arbitration when presented with a choice. If, on the other hand, arbitration is in reality, as we believe, unfair, the D.C. Council should approve a bill that levels the playing field for consumers by banning pre-dispute BMA clauses in all consumer insurance contracts written in the District.

Section 16-4403(d) Is Valid, Appropriate and Should Be Retained

One councilmember objected in public remarks to section 16-4403(d), which would ensure that future changes to the FAA could immediately take effect in the District, that is to say, changes to federal law would be self-executing in the District. This as a critical adjustment to the bill because it immediately would provide District residents with the benefit of pro-consumer changes to the FAA. Imagine, for instance, that Congress bans pre-dispute BMA clauses in consumer contracts for the purchase of automobiles. Yet District rules continue independently to allow pre-dispute arbitration clauses to be foisted onto District auto buyers – despite a clear Congressional recognition that compelling auto buyers to arbitrate disputes as a condition of purchasing an automobile is grossly unfair.

At least in some circumstances, Congress has indicated its belief that pre-dispute BMA clauses are unfair and must be banned. In 2002, Congress excluded pre-dispute BMA clauses from contracts between automobile dealerships and manufacturers after auto dealers convinced Congress that "large multinational motor vehicle manufacturers will continue to be able to unilaterally deny small business automobile and truck dealers rights under state laws that are designed to bring equity to the relationship between manufacturers and dealers." *See attached Letter from the National Automobile Dealers Association to the Congressman Nadler* (Jul. 12, 2000). That law provides that arbitration agreements between auto dealers and auto manufacturers may only be entered into *after* a dispute arises. 15 U.S.C. § 1226(a)(2).[15]

In 2006, Congress passed a statute that bans BMA clauses (both pre- and post-dispute) in consumer loan contracts entered into by members of the military and their dependents. *See* 10 U.S.C. §987(e)(2)-(4); (f)(1). This statute actually makes it a misdemeanor crime for a creditor to require

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[14] *See* Council of the District of Columbia Committee on Public Safety and the Judiciary, *Report on Bill 17-50, the "Arbitration Amendments of 2007"* (June 4, 2007). We note that Chief Justice King gave unqualified support for B17-50, which included the insurance exemption.

[15] Regrettably, car dealers continue to impose their unequal bargaining power – through BMA clauses in consumer auto purchasing contracts – upon individual auto purchasers. For an example of the problems occurring in that area, we direct you to the testimony of attorney Brad Blower who represents several African Americans forced to arbitrate racial discrimination claims against a large auto dealer in the area, Jim Koons Automotive Companies. *See attached: Letter from Public Citizen to Chairman Phil Mendelson: Supplement to March 23rd Hearing on the Arbitration Amendments Act of 2007* (Apr. 5, 2007) at 6-7, n. 5.

members of the military or their dependents to waive or severely burden their rights by the use of BMA clauses and thereby cut off access to the courts.[16]

Section 16-4403(d) would not put the District in the position of forcing individuals and small businesses into arbitration against powerful and entrenched interests after the Congress curtails, out of fairness, application of the FAA. Section 16-4403(d) ensures that any changes Congress might enact to the FAA to prohibit enforcement of arbitration clauses also would extend to District residents. Without it, the District would have to go through a lengthy and cumbersome process of amending its rules to merely assure that treatment in the District does not vary from the national norm.

While the FAA embodies a policy of enforcing agreements to arbitrate, it was not enacted to force parties into arbitration but to enforce voluntary agreements between parties to arbitrate. Indeed, the legislative history suggests that the FAA was primarily intended to govern disputes between merchants.[17] Unfortunately, in more recent times, application of the FAA expanded to cover standardized boilerplate contracts involving all kinds of consumer transactions.[18] Legal commentators and dissenting Supreme Court justices recognize that "the [Supeme] Court's interpretation of the Act has given it a scope far beyond the expectations of the Congress that enacted it." *Southland Corp. v. Keating*, 465 U.S. 1, 25-29 (1984) (O'Connor, J. dissenting, joined by Rehnquist, J.). The courts generally have failed to consider the harmful impact of BMA on individual consumers and consumer protection laws.[19] *See attached* Public Citizen Fact Sheet: "*D.C. Arbitration Bill Provides Much-Needed Protections for Consumers Against Abusive Arbitration Practices.*"

The Council for the District now has an historic opportunity to level the playing field for consumers and to right many of the wrongs which occur in pre-dispute binding mandatory arbitration. We strongly urge you to support B17-50 in its entirety.

Sincerely,

Laura MacCleery
Director, Congress Watch

Linda Andros
Legislative Counsel

[16] Congress continues to consider additional categories for exemption from the FAA, notably the Consumer Fairness Act of 2007 (H.R. 1443), the American Homebuyers Protection Act (H.R. 1519), and the Fair Contracts for Growers Act (S. 221). *See attached Letter from the Center for Responsible Lending (Apr. 6, 2007) to the Honorable Phil Mendelson at 4.*

[17] *See* Hearing on S. 4213 and S. 4214 Before the S. Comm. on the Judiciary, 67th Cong. 9 (1923).

[18] *Perry v. Thomas*, 482 U.S. 483, 493-94 (1987) (Stevens, J. dissenting). *See Allied-Bruce Terminix Companies, Inc. v. Dobson*, 513 U.S. 265, 286 (1995) (Thomas, J. dissenting, joined by Scalia, J.).

[19] In fact, the Department of Consumer & Regulatory Affairs initially advocated for a provision to exempt the District's consumer protection laws from being determined by arbitrators under pre-dispute BMA clauses, but such a provision was viewed as likely being preempted by the FAA, so that provision has been removed from B17-50.