

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

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	:	
JUSTIN A. KUEHN, on behalf of himself	:	
and all others similarly situated,	:	
	:	
Plaintiff,	:	
	:	12 Civ. 3287 (DLC)
-v-	:	
	:	<u>OPINION AND ORDER</u>
CITIBANK, N.A., THE SUTDENT LOAN	:	
CORPORATION, and DISCOVER BANK,	:	
	:	
Defendants.	:	
	:	
-----	X	

Appearances:

For the Plaintiff:

Stephen Rabin  
Joseph V. McBride  
Rabin & Peckel LLP  
885 Third Avenue, 30th Floor  
New York, NY10022

For the Defendants:

Joseph E. Strauss  
Stroock & Stroock & Lavan LLC  
180 Maiden Lane  
New York, NY 10038

DENISE COTE, District Judge:

Defendants Citibank, N.A. ("Citibank"), The Student Loan Corporation ("SLC"), and Discover Bank ("Discover") move pursuant to the Federal Arbitration Act to compel plaintiff Justin A. Kuehn ("Kuehn") to arbitrate his claims for breach of contract, violation of N.Y. Gen. Bus. L. § 349, and N.Y. Gen.

Bus. L. § 350 against the defendants. Kuehn argues that the arbitration agreement contained in his loan agreement is unconscionable and thus unenforceable. For the following reasons, the defendants' motion to compel arbitration is granted and this action is stayed pending resolution of the arbitration.

#### BACKGROUND

On November 13, 2007, Kuehn electronically submitted a Private Consolidation Loan Application with SLC. In this application, Kuehn sought to consolidate four private student loans. As part of the on-line application process, the plaintiff was required to view the application itself, a promissory note and a conditional approval letter. The application contained a section entitled "Signatures" directly above the signature box where the customer was permitted to electronically sign the application by clicking on a box. The "Signatures" section provided as follows:

I promise to pay Citibank, N.A. or any other holder of the accompanying promissory note (the "Note") all sums disbursed under the terms of this application (the "Loan") plus interest, fees and other charges which may become due as provided for by the Note. The terms and conditions of this application, the Note, any Conditional Approval Letter and any other disclosures collectively constitute the entire agreement between you and me.

The plaintiff submitted the loan application on November 13, 2007. In an approval letter dated December 7, 2007, Citibank approved the plaintiff's application. The approval letter

stated that "[t]his approval letter, together with your Application/Promissory Note, constitutes the entire agreement between you and us with respect to your Private Consolidation Loan that you requested."

The parties do not dispute that the promissory note is part of the loan agreement between the parties. The parties also do not dispute that the promissory note contains an arbitration agreement. The arbitration agreement contains the following language:

Agreement to arbitrate:

You and I agree that either you or I may, without the other's consent, require that any Claims between you and me be submitted to mandatory, binding arbitration except for certain matters excluded below. This arbitration provision is made pursuant to a transaction involving interstate commerce, and shall be governed by, and enforceable under, the Federal Arbitration Act (the "FAA"), 9 U.S.C. §1 et seq., and (to the extent State law is applicable), the State law governing this transaction.

Claims subject to Arbitration include, but are not limited to:

Claims relating to . . . the application, enforceability or interpretation of my Account, including this arbitration provision.

(Emphasis supplied.) The arbitration agreement defines the word "claim" to mean "any case, controversy, dispute, tort, disagreement lawsuit or claim now or hereafter existing between you and me arising out of or in connection with my loan," and the word "account" to mean "my agreement with you as evidenced

by the loan application and Note along with any and all records or transactions related thereto.”

The original balance of the Consolidated Private Student Loan was \$99,148.19 with an annual interest rate of 9.55%. The plaintiff enrolled in an auto-debit payment program offered by Citibank and SLC. Pursuant to this program, the plaintiff’s monthly payments under the Consolidated Private Student Loan are automatically deducted from the plaintiff’s checking account each month. The plaintiff began making monthly payments on the Consolidated Private Student Loan of \$845.72 in either December 2007 or January 2008. In addition to his monthly payments, the plaintiff made three large payments by check to SLC towards the principal of the Consolidated Private Student Loan. These payments, which were made in April 2008, June 2008, and June 2009, totaled \$25,000. Following June 2009, the plaintiff has not made a payment in excess of the auto-debited monthly minimum payment. In late 2011, the plaintiff received a notice from Citibank that his Consolidated Private Student Loan had been sold to Discover, but that Citibank would remain the loan’s servicer.

In January of 2012, the defendants reduced the plaintiff’s auto-debited monthly payment from \$845.72 to \$539.27. The plaintiff’s January 2012 monthly statement from SLC provided the following notification: “The variable interest rate on your

student loan has changed. Your monthly payment has been adjusted to reflect the new interest rate, as stated above." On at least two occasions, the plaintiff requested an explanation from SLC of why his auto-debit payments were reduced. Sometime in January 2012, the plaintiff received a letter from Citibank with the following explanation:

Prior to your loan payment amount being adjusted in December 2011, your payment schedule was last changed in January 2008. Between those two adjustments, we received three payments larger than your monthly minimum due totaling approximately \$25,000.00. Your payment schedule was then systematically adjusted in December 2011 for the full remaining repayment term with a payment amount based on the reduced principal balance.

On April 25, 2012, the plaintiff filed a complaint in this court against the defendants. The complaint asserts claims for breach of contract, and violations of New York General Business Law §§ 349 and 350. The plaintiff alleges that the defendants are engaged in a scheme to collect additional interest at the expense of borrowers of student loans by deceiving borrowers into believing that their monthly payments have been reduced because of an interest rate reduction, when in fact, the majority of the payment reduction is due to a reduction in the amount of principal being repaid each month. On August 16, the defendants filed a motion to compel arbitration of the plaintiff's claims and to stay the action pending completion of the arbitration proceedings. In their motion, the defendants

argue that not only are the plaintiff's substantive claims subject to the arbitration agreement, but the question of the arbitration agreement's enforceability is itself subject to arbitration.

#### DISCUSSION

Pursuant to Section 2 of the Federal Arbitration Act ("FAA") "a written provision in . . . a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. The FAA was enacted to counteract "widespread judicial hostility to arbitration agreements." AT&T Mobility LLC v. Concepcion, 131 S.Ct. 1740, 1745 (2011). The Supreme Court and Second Circuit have repeatedly emphasized that the Act "declares a national policy favoring arbitration." See e.g., Nitro-Lift Technologies, L.L.C. v. Howard, --- S.Ct. ---, 2012 WL 5895686, \*2 (2012)(citation omitted); Perry v. Thomas, 482 U.S. 483, 489 (1987); Schnabel v. Trilegiant Corp., 697 F.3d 110, 118 (2d Cir. 2012). Consistent with this policy, "[a] party to an arbitration agreement seeking to avoid arbitration generally bears the burden of showing the agreement to be inapplicable or invalid." Harrington v. Atlntatic Sounding Co., Inc., 602 F.3d

113, 124 (2d Cir. 2010); see also Green Tree Fin. Corp.-Ala. V. Randolph, 531 U.S. 79, 91-92 (2000). Under the FAA, when the court is "satisfied that the issue involved in such suit or proceeding is referable to arbitration under" the arbitration agreement, it must stay the action and compel arbitration. 9 U.S.C. §§ 3-4; see also Progressive Cas. Ins. Co. v. C.A. Reaseguradora Nacional De Venezuela, 991 F.2d 42, 45 (2d Cir. 1993).

In many cases, the threshold question of the enforceability of the arbitration agreement as a whole is resolved by the court and not by an arbitrator. See Cap Gemini Ernst & Young, U.S., L.L.C. v. Nackel, 346 F.3d 360, 365 (2d Cir. 2003). The Supreme Court has recognized, however, that parties can also agree to delegate this "gateway" question to an arbitrator. Rent-A-Center, West, Inc. v. Jackson, 130 S.Ct. 2772, 2777 (2010); cf. PaineWebber Inc. v. Bybyk, 81 F.3d 1193, 1198-99 (2d Cir. 1996). "An agreement to arbitrate a gateway issue is simply an additional, antecedent agreement the party seeking arbitration asks the federal court to enforce, and the FAA operates on this additional arbitration agreement just as it does on any other." Rent-A-Center, West, Inc., 130 S.Ct. at 2777-78. Thus, when an arbitration agreement contains an antecedent agreement delegating the question of the agreement's enforceability to an arbitrator (the "delegation agreement"), this antecedent

agreement itself is "valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2; see also Rent-A-Center, West, Inc., 130 S.Ct. at 2778. In other words, in light of a delegation agreement, a party's challenge to the arbitration agreement on unconscionability grounds is a dispute that must be resolved by arbitration unless the party opposing arbitration demonstrates that the delegation agreement itself is unenforceable. Rent-A-Center, West, Inc., 130 S.Ct. at 2779. Accordingly, a party seeking to avoid arbitration on unconscionability grounds must demonstrate that the delegation agreement in particular, rather than the arbitration agreement as a whole, is unconscionable. Id. at 2779-81.

The arbitration agreement in this case contains a provision delegating questions about the enforceability of the arbitration agreement to an arbitrator. Because the plaintiff has failed to demonstrate that the delegation agreement is unconscionable, the defendants' motion to compel arbitration is granted.

The arbitration agreement between the parties in this case provides that "[c]laims relating to . . . to application, enforceability or interpretation of my Account, including this arbitration provision" are subject to arbitration. (Emphasis supplied.) This provision plainly delegates resolution of questions about the arbitration agreement's enforceability to an

arbitrator. Under the FAA, and as explained by the Supreme Court in Rent-A-Center, West, Inc., 130 S.Ct. 2772, the Court must enforce this delegation agreement unless the plaintiff has shown that the delegation agreement itself is unenforceable.

The enforceability of the delegation agreement, like the enforceability of the arbitration agreement as a whole, is governed by state law. See e.g., id. at 2780; see also Cap Gemini Ernst & Young, U.S., L.L.C., 346 F.3d at 365. The parties agree that Nevada law is the applicable state law. Under Nevada law, a contract provision is unconscionable only if it is both procedurally and substantively unconscionable. Gonski v. Second Judicial Dist. Court of State ex rel. Washoe, 245 P.3d 1164, 1169 (Nev. 2010). Procedural unconscionability exists "when a party has no meaningful opportunity to agree to the clause terms either because of unequal bargaining power, as in an adhesion contract, or because the clause and its effects are not readily ascertainable upon a review of the contract." Id. (citation omitted). Substantive unconscionability relates to a contract provision's one-sidedness or oppressiveness. Id. The plaintiff has failed to demonstrate that the delegation provision contained in the arbitration agreement is substantively unconscionable.

Like the plaintiff in Rent-A-Center, West, Inc., Kuehn has directed his unconscionability arguments at the arbitration

agreement as a whole, rather than the antecedent delegation agreement. This is problematic for the plaintiff, because, as the Supreme Court has recognized, some unconscionability arguments will be more difficult to sustain with respect to the delegation agreement than they would be with respect to the arbitration agreement as a whole. Rent-A-Center, West, Inc., 120 S.Ct. at 2780.

The plaintiff argues that the arbitration agreement is substantively unconscionable.<sup>1</sup> In support of this argument, the plaintiff points out that the arbitration agreement's fee-splitting scheme requires the plaintiff to pay for half of the arbitration costs less the cost of the first day of a hearing. The plaintiff estimates that arbitration of his claims could cost as much as \$25,000. The plaintiff suggests that the cost of arbitration will therefore be prohibitively expensive for him. Once again, however, the plaintiff's focus on the arbitration agreement as a whole, rather than the delegation agreement, misses the mark. "[T]he unfairness of the fee-splitting arrangement may be more difficult to establish for the

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<sup>1</sup> The plaintiff has also argues that the arbitration agreement is procedurally unconscionable. Because the plaintiff has failed to demonstrate that the delegation agreement is substantively unconscionable, the Court does not reach this issue. Although it is true that "a strong showing of procedural unconscionability means that less substantive unconscionability [is] required," Nevada law still requires "a showing of both types of unconscionability . . . before an arbitration clause will be invalidated." Gonski, 245 P.3d at 1169.

arbitration of enforceability than for arbitration of more complex and fact-related aspects” of the plaintiff’s substantive claims. Id. The plaintiff’s cost estimates appear to refer to the arbitration of the plaintiff’s substantive claims against the defendants. There is no indication in the plaintiff’s submissions that the costs of having an arbitrator decide the question of the arbitration agreement’s enforceability will itself be prohibitively expensive due to the fee-splitting scheme. When “a party seeks to invalidate an arbitration agreement on the ground that arbitration would be prohibitively expensive, that party bears the burden of showing the likelihood of incurring such costs.” Green Tree Fin. Corp.-Ala. V. Randolph, 531 U.S. 79, 92 (2000). In this case, the plaintiff has failed to demonstrate that he is likely to incur prohibitive costs by arbitrating the question of the arbitration agreement’s enforceability.<sup>2</sup>

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<sup>2</sup> The defendants have also volunteered to advance the plaintiff’s portion of any arbitration fees for arbitration before the AAA or JAMS.

CONCLUSION

The defendants' August 16 motion to compel arbitration is granted. This action is stayed pending resolution of the arbitration proceeding.

SO ORDERED

Dated: New York, New York  
December 6, 2012

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*Denise Cote*  
DENISE COTE  
United States District Judge