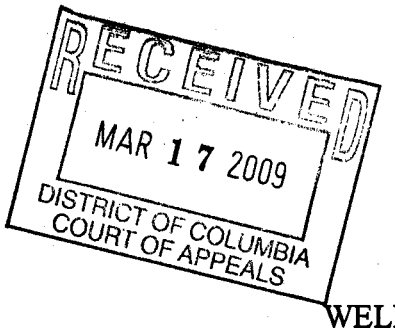
DISTRICT OF COLUMBIA COURT OF APPEALS



No. 08-CV-990

BONITA KEETON,
Plaintiff/Appellant

v.

WELLS FARGO CORP., *et al.*,
Defendants/Appellees.

On Appeal from the Superior Court of the District of Columbia
(The Hon. Jennifer Anderson)
Case No. CAB-2622-08

BRIEF OF THE LEGAL AID SOCIETY OF THE DISTRICT OF COLUMBIA AS *AMICUS CURIAE* SUPPORTING REVERSAL

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

STATUTES AND RULES

OTHER AUTHORITIES

INTEREST OF AMICUS

The Legal Aid Society of the District of Columbia (Legal Aid) was formed in 1932 to "provide aid and counsel to indigent persons in civil law matters and to encourage measures by which the law may better serve their needs." Legal Aid By-Laws, Art. II. It is the oldest general civil legal service program in the District of Columbia and represents hundreds of litigants each year before the District's courts and administrative agencies.

Legal Aid's staff members work on a range of legal issues affecting persons living in poverty in the District. The program's principal practice areas are housing, family, public benefits, and consumer law. Its consumer practice, founded in 2008, seeks to protect low-income residents of the District of Columbia from unconscionable, exploitative, or otherwise unlawful consumer practices. These may include the use of procedurally or substantively unconscionable clauses in consumer contracts, which frequently have a disproportionate adverse impact on unsophisticated, low-income residents. A Motion for Leave to File pursuant to D.C. Ct. App. R. 28(a) has been submitted herewith.

SUMMARY OF ARGUMENT

Since the landmark case of *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445 (D.C. Cir. 1965), this Court has policed consumer sales and lease contracts which are "unconscionable" because they do not represent a bargained-for exchange; are grossly unfair; or both. Certain types of consumer arbitration clauses – which are inescapable in the auto industry – present issues such as prohibitive cost, arbitrator bias, and "one-way" provisions which require arbitration only by the consumer, and are thus unconscionable in many instances. An appropriate rule for consumer arbitration clauses (whose enforceability must typically be decided case by case) would require the consumer to prove both lack of informed choice by the consumer (because, for example, there is no alternative in the marketplace) and also that at least one

substantive term in the arbitration clause was materially unfair (because of excessive cost, arbitrator bias, or similar reasons).

Easterns' clause raises all of these concerns: Easterns chooses the arbitrator, who charges $200 per hour to decide Easterns' cases (the consumer must pay at least half, and potentially all, of the arbitrator's charges); Easterns is a "repeat player" with superior knowledge and leverage over the arbitration process (including the right to pick any arbitrator or arbitration provider it wishes, without restriction); and Easterns' clause requires only claims by the consumer (not Easterns) to be arbitrated. In this case, Easterns did not identify the arbitration provider, the arbitrator, or the high costs imposed, until filing a reply memorandum in support of Easterns' motion to compel arbitration, which handicapped plaintiff's efforts to prove the clause was unenforceable.

The lower court's suggestion that the validity of the arbitration clause should be decided by the arbitrator, rather than the court, was error. In cases like this, where there is a direct challenge to the enforceability of the arbitration clause itself (including unconscionability), settled law requires that this challenge be decided by the court, not the arbitrator.

If this Court finds that there is insufficient evidence in the record to determine unconscionability, then it should remand for discovery and a fresh decision applying the correct rules. Deciding the enforceability of an arbitration clause is akin to a summary judgment proceeding, in which both sides are entitled to take any necessary discovery before the court decides a motion which could cut off the plaintiff's right to proceed in court.

ARGUMENT

THE FORM ARBITRATION CLAUSE IN THE EASTERNS MOTORS BUYER'S ORDER IS UNCONSCIONABLE

Defendants' one-sided, overreaching arbitration clause cannot be understood or examined in isolation, but only in the broader context of (1) the dynamics of Defendants' own business and their customers, such as Ms. Keeton, and (2) the move to impose similar clauses in a broad array of consumer and employment agreements. The transaction between Ms. Keeton and Easterns, as described in the complaint, involves the same kind of exploitation of unsophisticated consumers with few options in the marketplace as the Circuit Court's historic decision in *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445 (D.C. Cir. 1965). In *Walker-Thomas*, the consumer signed a contract allowing the company to repossess everything she had purchased on installments if she missed a payment. That financing structure gave the company an incentive to push items the consumer could not afford:

> [A]t the time of this and the preceding purchases, appellee was aware of appellant's financial position. The reverse side of the stereo contract listed the name of appellant's social worker and her $218 monthly stipend from the government. Nevertheless, with full knowledge that appellant had to feed, clothe and support herself and seven children on this amount, appellee sold her a $514 stereo set. [*Id.* at 448.]

Just so, Ms. Keeton's complaint alleges that she brought her paystub in to Easterns, seeking a $200 monthly car payment. Yet she left with what Easterns knew was an overpriced car and payments she could not afford.

Beyond its application of the legal principle of unconscionability, *Walker-Thomas* stands for the proposition that the unconscionability standard must be applied not to the idealized abstractions of contract theory, but to the gritty reality of consumer transactions. Bargaining power and consent must be assessed in terms of the real options open to people living in poverty,

and their actual understanding of contractual boilerplate. *Id.* at 449-450. Just as no consumer who really had a choice would have agreed to Walker-Thomas's onerous financing terms, no consumer who really had a choice would buy a used car from Easterns at new car prices.

Today, of course, the Walker-Thomas contract would have an arbitration clause designed (like Easterns') to keep its customers away from the courthouse. But this Court should be no less practical and realistic about arbitration clauses than the Circuit Court was in *Walker-Thomas* about the substantive terms of the contract. Unlike commercial arbitration agreements intended to divert disputes between sophisticated parties to panels with industry expertise, arbitration clauses like the one set forth in the Easterns buyer's order are designed to prevent customers from seeking redress.

As *Walker-Thomas* and its progeny make clear, the issue of unconscionability is one decided on a case-by-case basis, calibrated to the facts of the transaction and the parties to the contract. Here, *amicus* addresses the standards which will govern the unconscionability analysis for arbitration clauses which now appear in many, if not most, consumer sales transactions. Although those transactions vary as to the subject of the consumer purchase, the parties involved, and the arbitration clauses themselves, it is essential that this Court establish "rules of the road" so that the legality of such clauses may readily be determined.

Ms. Keeton's case presents compelling evidence of both procedural (her limited education and means, and the near-universal use of arbitration clauses in auto sales contracts) and substantive (at least three aspects of the clause are materially unfair, as detailed below) unconscionability. In the case of arbitration clauses specifically, *amicus* suggests that an appropriate rule would (at a minimum) prohibit enforcement of any arbitration clause between a merchant and a consumer in which the consumer can demonstrate both (1) lack of informed

choice by the consumer, either because of (a) the consumer's lack of education or sophistication, (b) no alternative in the marketplace, because arbitration is a condition of sale in all or substantially all similar transactions, or (c) the effective concealment of the arbitration provision (not an issue in this case), and (2) at least one substantive item in the clause that is materially unfair (whether it is excessive cost, biased arbitrators, a one-way arbitration requirement – as here – or other defects such as a shortened statute of limitations, unfair venue, or a ban on class actions).

A. THE BUSINESS OF EASTERNS MOTORS

Easterns is a regional used car empire, with seventeen locations in the District, Maryland and Virginia (an eighteenth sells new Hyundais). Easterns reports itself to be "one of the largest and fastest growing auto dealer groups on the East Coast"[1] and boasts the official motto "Where your job is your credit."[2] The company's home page invites customers to "[a]pply now for instant credit,"[3] and an interview last year of the company's owner notes that "[h]e quickly established the Eastern Motors brand as the place for 'second-chance' credit and began adding stores in 1992." The company's TV and radio advertising, which one writer described as "rivaled by only 'It's a Small World' for its ability to get stuck in your head," airs approximately 300 times a day and "has been a Washington area staple since it debuted on local radio stations in 1995."[4]

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1 Http://geebo.com/atl.cgi?ct=6&md=2&id=20115553 (last visited 3/8/09).

2 Http://easternmotors.ylmnd.com (last visited 3/16/09).

3 Http://www.easterns.com/easterns/default.aspx (last visited 3/5/09).

4 The Examiner, 11/3/06 (available at http://www.examiner.com/a-376995~Eastern%20Motors%20founder%20Bassam%20finds%20fortune%20with%20second-chance%20financing.html (last visited 3/16/09).

In short: Easterns' business is based on sales to lower-income, less-educated auto buyers with poor credit or a limited credit history. These are buyers with few auto-buying options, who come to Easterns precisely because (as intended) Easterns' advertising gives them confidence they will not be turned away. These are exactly the sorts of consumers at whom this Court's unconscionability doctrine should be aimed. And this means that Ms. Keeton's case was not exceptional, but was the result of Easterns' regular business practices, indeed its business model.

Easterns drew Ms. Keeton to one of its dealerships with its televised advertising. App. 3, Comp. ¶ 6. Ms. Keeton alleges in her complaint that Easterns sold her a car on unconscionable terms. The terms and circumstances of the transaction, as alleged in the complaint, show a gross imbalance in the sophistication and bargaining power of the parties. *See, e.g.,* App. 4, Comp. ¶¶ 15-16. Although she went to Easterns looking for a car she could afford on her school bus driver's salary. App. 3, Comp. ¶ 9. Ms. Keeton ultimately agreed to make monthly payments nearly double what she had sought. She also agreed to a 9.3% interest rate and numerous add-on fees. Although her car has been repossessed, she likely faces thousands of dollars in liability because it was worth so much less than she agreed to pay. And, instead of being able to proceed in court *in forma pauperis*, as she has been permitted to do on appeal, she faces hundreds or thousands of dollars in arbitration costs in a proceeding before an arbitrator chosen by Easterns, even though Easterns and its assignees are free to sue her.

B. CONSUMER ARBITRATION CLAUSES ARE UBIQUITOUS, AND PRESENT ISSUES OF COST AND UNFAIRNESS

The starting point for analysis is the fact that form arbitration clauses such as Easterns' are now the rule, not the exception, in consumer sales and credit transactions such as auto purchases. Testimony of Sen. Feingold (D-Wis.), *S. 1782, The Arbitration Fairness Act of 2007*, Sen. Hrg. 110-396, U.S. Sen. Comm. on Judiciary, Dec. 10, 2007 ("2007 Senate Hearings") at 2;

see also id. at 1 ("large and growing number" of corporations require arbitration); at 10 ("Today, most consumer credit contracts contain an arbitration provision") (testimony of Richard Alderman, Univ. of Houston). "[I]t appears that in the last four years the vast majority (if not nearly all) car dealers in the United States have inserted binding arbitration clauses into their . . . sales contracts." 2007 Senate Hearings at 56 (testimony of Paul Bland, Public Justice). And this is a recent phenomenon: "In 2000, almost no car dealers had arbitration clauses." *Id.* at 27.

This overnight transformation in consumer sales transactions is not, of course, the result of consumer demand, or negotiations between consumers and merchants. "Questions have been raised about the true cost of arbitration, and its fairness. But no one disputes that consumer arbitration is imposed by the stronger party, not voluntarily agreed to." 2007 Senate Hearings at 45 (Alderman testimony). And given the ubiquity of business-drafted arbitration clauses – particularly in auto sales – buyers such as Ms. Keeton have no choice but to accept the terms demanded:

> Most consumers have little or no meaningful choice about submitting to arbitration. Few people notice or realize the importance of the fine print that strips them of rights; and because all the corporations in entire industries are adopting these clauses, people have no choice. They must give up their rights as a condition of buying a car, opening a bank account, or getting credit card[s], etc. [*Id.* at 51 (Bland testimony).]

Respected commentators agree: "Given the lack of information available to customers in predispute arbitration clauses, and the difficulty of obtaining and deciphering these clauses, it is likely that most consumers only become aware of what rights they retain and what rights they have waived after disputes arise." L. Demain and D. Hensler, *"Volunteering" to Arbitrate Through Predispute Arbitration Clauses: The Average Consumer's Experience,* 67 Law & Contemp. Probs. 55, 73-74 (Winter-Spring 2004).

Companies insist on arbitration clauses not because they see arbitration as a fairer way to resolve disputes, but because arbitration gives them a decided advantage in those disputes. Tellingly, although auto dealers such as Easterns have inserted arbitration clauses into virtually every consumer sales transaction, they have lobbied hard – and successfully – to prohibit by federal law the use of mandatory arbitration in disputes with auto manufacturers. In 2002, Congress passed a law doing just that. *See* 15 U.S.C. § 1226(a)(2). Thus, if Easterns had a dispute with Hyundai Motors (for which it is an authorized reseller of new vehicles), the dealership would have the right to insist on a jury trial in Superior Court. But when it comes to Ms. Keeton, Easterns claims the right to require arbitration, or to go to court – whichever gives it the biggest advantage in the dispute.

Because one-sided consumer arbitration clauses are a systemic problem, not limited to Ms. Keeton's case, it should come as no surprise that the defects designed-in to her clause – high cost, arbitrator bias, and one-way use – are broadly representative of other, unconscionable clauses. The net (and intended) effect is to place enormous barriers in the way of consumers seeking to enforce their statutory and common-law rights. Take the cost of arbitration as an example. At the recent Senate hearings, Sen. Feingold explained the problem:

> [T]he administrative fees—both to gain access to the arbitration forum and to pay for the ongoing services of the arbitrator or arbitrators—can be so high as to act as a de facto bar for many individuals who have a claim that requires resolution. [2007 Senate Hearings, p. 2]

To take another example, the evidence on arbitrator bias from clauses like Ms. Keeton's is especially impressive. This problem results from two facts. First, the business that demands the clause – like Easterns – is solely in charge of picking the arbitration forum, the rules that govern the arbitration, and the circumstances in which arbitration is required. (This, in turn,

results from the fact, just noted, that such clauses are imposed, not negotiated – consumers simply play no role in the design of the supposedly consensual arbitration system that can have such a powerful effect on their rights.) Second, a consumer like Ms. Keeton will use the arbitration system at most once with a given merchant. But the merchant – like Easterns, with its seventeen dealerships and thousands or tens of thousands of yearly transactions – will use arbitration again and again. Simply put, a business like Easterns is a "repeat player."

Repeat players benefit from their hand-selected arbitration systems in a number of ways. For one thing, businesses like Easterns know the track records of the potential arbitrators, while customers (faced with a "private" arbitration system) do not. Businesses can (and do) pick arbitrators with a good track record for their side. They are "'professional litigants,' [who] can make use of their superior knowledge of arbitrators past decisions to help ensure that their cases are heard by [a given tribunal's] arbitrators who will rule for them." 2007 Senate Hearings at 63 (Bland testimony).

In one District of Columbia case, the U.S. Court of Appeals found that this was a great risk, for reasons that extended well beyond the facts of that case and are plainly applicable here:

> Unlike the labor case, in which both union and employer are regular participants in the arbitration process, only the employer is a repeat player in cases involving individual statutory claims. As a result, the employer gains some advantage in having superior knowledge with respect to selection of an arbitrator. *See, e.g.,* Lewis Maltby, *Paradise Lost-How the* Gilmer *Court Lost the Opportunity for Alternative Dispute Resolution to Improve Civil Rights,* 12 N.Y.L. SCH. J. HUM. RTS. 1, 4-5 (1994) (arguing that individual employees are disadvantaged vis-à-vis employers in determining whether given arbitrator is truly neutral because employees lack financial resources to research arbitrator's past decisions); Sternlight, 74 WASH. U. L.Q. at 685 (arguing that "one-shot players" such as employees and consumers are less able to make informed selections of arbitrators than "repeat-player" companies); Getman, 88 YALE L.J. at 936 (same); Gorman, 1995 U. ILL. L. REV. at 656 (same); Reginald Alleyne, *Statutory*

> *Discrimination Claims: Rights "Waived" and Lost In the Arbitration Forum,* 13 HOFSTRA LAB. L.J. 381, 403, 426 (1996) (same).

Cole v. Burns Int'l Security Services, 105 F.3d 1465, 1476-77 (D.C. Cir. 1997).

But businesses do not only use their superior knowledge to pick *favorable* arbitrators: they also use their power to ensure that *unfavorable* arbitrators -- which is to say, ones who might see things the consumer's way on occasion – will never hear their cases. Research from California, the only state that requires certain business arbitration systems to disclose data about outcomes, demonstrates this point:

> One particularly troubling aspect of the repeat-player syndrome is the tendency of corporate repeat-players to blackball arbitrators who might rule against them. This tendency was revealed by a study of mandatory arbitration in managed care cases in California, which found a small number of cases in which an arbitrator awarded a plaintiff more than one million dollars against [an] . . . HMO. M. Nieto and M. Hosel, *Arbitration in California Managed Health Care Systems* 22-23 (2000). In each instance, that was the only HMO case that the arbitrator ever handled, suggesting that every time an arbitrator entered a substantial verdict against an HMO, the arbitrator was unable to get any further work from an HMO in the state. The same study found that arbitrators were far more likely than judges to enter summary judgment for defendant HMOs. [*Id.* at 61-62 (Bland testimony).]

And these are just examples of how businesses "game the system" as to *individual* arbitrators. In a regime where businesses like Easterns act as customers and get to choose among arbitration providers, providers will shape both their rules and their choice of arbitrators to the demands of their clients:

> There are a number of different private arbitration companies who compete to be selected by corporations in their standard form contracts with consumers and employees. Arbitration work is often very lucrative, and arbitrators know that if they rule against a corporate defendant too frequently or too generously . . . they will lose the work. [*Id.* at 60.]

The result is aptly characterized as a "race to the bottom," in which arbitration forums such as the American Arbitration Association lose out to newer competitors who can provide a greater assurance of pro-business results. *Id.* at 18. In this regard, Easterns has great flexibility, because its clause does not actually specify who is to perform the arbitration. And even from a "traditional" arbitration provider such as the AAA, it is common to find the following situation, whether a bank or an auto dealer is on the other side of the case:

> AAA says that one of the due process protocols is you will always get a neutral arbitrator. But when you get a list of who is going to be on your panel, there are seven names on the list. The vast majority of the time, every one of those names is a lawyer who specializes in defending that industry. [*Id.* at 19.]

Although data are hard to come by – due to the closed, secretive system that is one of arbitration's principal selling points to business[5] – "[t]here is some empirical evidence and a good deal of academic analysis showing that arbitrators have a tendency to favor 'repeat player' clients. In the consumer law context, the repeat player will generally be the corporate defendant." *Id.* at 61 (citing authorities); *see, e.g.*, L. Bingham and S. Sarraf, "Employment Arbitration Before and After the Due Process Protocol for Mediation and Arbitration of Statutory Disputes Arising Out of Employment: Preliminary Evidence that Self-Regulation Makes a Difference," *Alternative Dispute Resolution in the Employment Arena: Proceedings of the NYU 53rd Annual Conference on Labor* 303 (Estreicher and Sherwin eds. 2004) (employee win rate of 28% in employer-promulgated arbitrations, compared to 38% in all employment arbitrations). No surprise, then, that one observer testified recently that:

> [f]rom numerous conversations with lawyers both for corporations and advocates for individuals generally, and participation in

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[5] *Cole v. Burns, supra,* 105 F.3d at 1477 ("The unavailability of arbitral decisions also may prevent potential plaintiffs from locating the information necessary to build a case of intentional misconduct or to establish a pattern or practice of discrimination by particular companies.").

> multiple mediations and settlement negotiations, I can unequivocally testify that the nearly universal perception among both plaintiff-side and defense-side lawyers is that arbitrators are more likely to have a pro-defense attitude than are judges or juries. [2007 Senate Hearings at 60 (Bland testimony).]

C. EASTERNS' ARBITRATION CLAUSE IS TYPICAL OF INDUSTRY CLAUSES IN ITS PROHIBITIVE COST AND INHERENT ANTI-CONSUMER BIAS

Easterns' standard arbitration clause illustrates all the problems generally found in mandatory consumer predispute clauses, and then some. The array of defects in the clause makes clear that the real purpose here was to prevent consumers like Ms. Keeton from filing claims against Easterns in the first place, rather than to gain the theoretical advantages of the arbitration forum over the courtroom.

To begin with, the fact of grossly unequal bargaining power and no meaningful choice about the arbitration clause is hard to ignore, because it is all but impossible to buy a car without a dealer-drafted arbitration clause. *See supra* p. 7. Without any factual basis, however, the lower court held that "Here, no gross inequality of bargaining power existed because the plaintiff could have gone to another dealership." App. 67. But even if Ms. Keeton might have found another dealer who would not have sold her an overpriced *car*, that has nothing to do with the unconscionability of the *arbitration clause*. There was no basis on which to conclude that Ms. Keeton would have found a dealer that would not impose an arbitration clause. *See supra* p. 7. In any event, there was no factual basis for concluding that Ms. Keeton, a single mother with a limited income, really did have the wide choice of dispute resolution options the trial judge presumed. Because this error evidently played a key role in the court's rejection of the unconscionability defense, it is an independent ground for reversal.

Arbitrator selection and the "repeat player" phenomenon is another good example. The Easterns' clause states that all covered disputes (including those about "the validity of this

arbitration clause") "shall be resolved by binding arbitration by one arbitrator *selected by the Dealer* (or the assignee of any Retail Installment Sales contract) with the consent of the Purchaser." App. 21 (emphasis added). In using this language, Easterns has reserved to itself the right to choose any arbitrator (and any arbitration provider) it likes. It can pick from any list or roster, and select the individuals most likely to go Easterns' way, based on the arbitrator's track record in business-consumer cases, or the fact that the arbitrator routinely represents creditors, or both. Like the American Arbitration Association rosters described *supra*, for example, Easterns has a contractual "right" to pick only from lists of attorneys representing auto dealers. If a given arbitrator (or provider), despite Easterns' best efforts, proves to be pro-consumer, Easterns is free to blackball him or her in all future cases. Other arbitrators are likely to get the message: if you want business from one of the largest auto dealers on the East Coast, don't cross Easterns.

The lower court shrugged off these problems, holding that:

> The language gives the plaintiff the important power of vetoing the arbitrator the defendant selects. If the parties cannot agree on an arbitrator, the Uniform Arbitration Act provides that the court shall appoint the arbitrator. For that reason, the defendant does not have an unfair advantage over the plaintiff . . . [App. 70]

But this assumes that Ms. Keeton was in a position to know (or learn) anything about the arbitrators chosen by Easterns besides their names. For the reasons explained above, Easterns holds a monopoly on this information. *See Cole v. Burns*, *supra*, 105 F.3d at 1476-77. And the lower court in effect proposed that Ms. Keeton veto every arbitrator proposed by Easterns, *then* file an action in court to set aside Easterns' choices, *then* convince a judge that Easterns' list should be ignored in favor of a "neutral" appointment. Really, this was no solution at all.

Nor can the fact that Defendants specified – *after* the clause was challenged – an arbitrator from a regional arbitration provider (the McCammon Group) address this problem. It is inherent in every system in which one party has the right to name the arbitrator, and is a "repeat player" with the power to direct future business.[6] And like virtually every other large arbitration provider, the McCammon Group's clients "are primarily businesses, large commercial organizations, doctors, etc."[7]

But just as important, Defendants' "cure" could not, as a matter of law, solve the problems inherent in their unconscionable clause. In the first place, allowing one party to a contract to rewrite the agreement, after its enforceability is challenged, violates basic principles of contract law. As the Supreme Court has noted, the "primary purpose" of statutes permitting or encouraging arbitration is to ensure that "private agreements to arbitrate are enforced *according to their terms*."[8] *Volt Info. Sciences, Inc. v. Board of Trustees*, 489 U.S. 468, 479 (1989) (emphasis added). In the case of unconscionable contracts, comment b to § 184 of the *Restatement (2d) of Contracts* states that:

> a court will not aid a party who has taken advantage of his dominant bargaining power to extract from the other party a

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[6] The McCammon Group is a for-profit enterprise owned by Avitas Capital, a Richmond venture capital group which targets its investments to businesses with "strong margins, an established and diverse customer base, a strong management team, and growth potential." Http://www.avitascapital.com/portfolio/index.asp (last visited 3/8/09). As such it is vulnerable to the same market forces described *supra*, p. 10.

[7] Http://www.thehindubusinessline.com/2005/09/07/stories/2005090702440500.htm (interview with founder of the McCammon Group) (last visited 3/8/09).

[8] Too, by naming the arbitrator (and the arbitrator's employer) only *after* the dispute erupted and in their *reply memorandum* in support of Defendants' motion to compel arbitration, Defendants effectively prevented Ms. Keeton from taking discovery about the McCammon Group's practices. It is not unusual to learn that arbitration groups have a track record with particular industries, or market their services to those industries on the basis of pro-industry results. *See supra* p. 9.

> promise that is clearly so broad as to offend public policy by redrafting the agreement so as to make a part of the promise enforceable.

Similarly, as the lower court recognized, if "the element of unconscionability exists *at the time of contract formation*, the contract should not be enforced. *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445, 449 (D.C. Cir. 1965)." App. 64, emphasis added.

In the case of contractual arbitration clauses specifically, a number of courts have held that the drafter of the clause may not change its terms in an effort to salvage the clause. *See, e.g.*, *Alexander v. Anthony Intern., L.P.*, 341 F.3d 256, 271 (3d Cir. 2003); *Murray v. UFCW Int'l Union*, 289 F.3d 297, 304-05 (4th Cir. 2002) (rejecting effort to use substitute list of "neutral" arbitrators vs. defendant's list per agreement; "The arbitration agreement is unenforceable as written and Local 400 may not rewrite the arbitration clause and adhere to unwritten standards on a case-by-case basis in order to claim that it is an acceptable one."); *Perez v. Globe Airport Sec. Servs. Inc.*, 253 F.3d 1280, 1285-86 (11th Cir. 2001) (rejecting attempt to rewrite unenforceable arbitration clause in order to salvage it).

Second, Defendants' purported appointment of an arbitrator was actually a legal nullity. The McCammon Group's rules permit the parties to agree to use McCammon's services in advance, but only when the agreement expressly identifies the McCammon Group in advance:

> Alternatively, parties may obligate themselves to arbitrate by executing an external Agreement to Arbitrate not drafted by The Group. In such situations, The Group may serve as the arbitration service, but only in the following circumstances:
>
> 1. The provision *must specify* that The Group will provide the arbitration service. [Emphasis added.] (http://www.mccammongroup.com/arbitration-services/basics-of-arbitration.asp, last visited 3/5/09)

Similar problems flow from Easterns' requirement that "the cost of arbitration shall be borne equally between the parties, provided however, that the arbitrator may, in the interests of justice, order that the losing party pay the prevailing party's costs." App. 21. This means that Ms. Keeton must pay half the cost of an arbitrator who charges $200 an hour for preparing and hearing the case. In the Superior Court, by contrast, her filing fee was only $120, and she was eligible to proceed *in forma pauperis*, as she has been permitted to do on appeal. Even worse, she is liable for the *entire cost* of the arbitration proceeding if an arbitrator chosen by Easterns decides that Easterns was right. In Superior Court, by contrast, Ms. Keeton would at most be liable for statutory costs (filing fees and the like under Super. Ct. Civ. R. 54(d)(1)) if she lost; she would face liability for Easterns' attorneys' fees only in the unlikely event that her suit was found to be frivolous. *See* Super. Ct. Civ. R. 11.

Once again, Easterns identified the rate Ms. Keeton would be charged only *after* she challenged the arbitration clause, so that the record is sparse on the likely total cost of an arbitration by Ms. Keeton. But the clause as written gave the company a perfect right to charge as much as it liked, and the clause's legality, as explained above, must be judged at the time it was written. A reasonable estimate of the time required for a claim such as Ms. Keeton's is at least 10-20 hours, which implies a minimum arbitrator cost of $2,000-$4,000. Ms. Keeton is liable for at least half of that figure, and potentially all of it, if the clause is to be enforced. And the record is very clear that Ms. Keeton – a single mother of four, eligible for Medicaid, who is proceeding *in forma pauperis* in this Court – lacks the funds required to pay such an enormous amount. Under these circumstances, Sen. Feingold's prediction that arbitration fees "can be so high as to act as a de facto bar for many individuals" (2007 Senate Hearings, p. 2) appears to be exactly right.

The trial court's suggestion that Ms. Keeton did not suffer from the costly arbitration clause because she had volunteer legal help (*see* App. 69) was inexplicable, but in any event clearly wrong. Although Ms. Keeton was fortunate to receive *pro bono* legal assistance, it was preposterous to suggest that her lawyers (working from the legal clinic of a local law school) would (or could) advance the thousands of dollars in arbitrator fees required. In any event, the question is whether the clause was unconscionable as applied *to Ms. Keeton*, who plainly could not afford these fees.[9]

The last point is that Easterns' clause is so wholly one-sided that it may lack consideration in addition to being unconscionable. In the first place, the clause applies to any claim over $1,000 "whether contract, tort or other [a]rising from the negotiation of and terms of the" sale of Ms. Keeton's vehicle" (these are termed "Disputes"),

> Provided, however[,] that your failure to provide consideration to be paid by you (including your failure to pay a note, a dishonored check, failure to provide a trade title, or failure to pay deficiency resulting from additional payoff on trade) as well as our right to retake possession of the vehicle pursuant to this Buyer's Order shall not be considered a dispute and shall not be subject to arbitration. [App. 21]

Although it is unlikely that Ms. Keeton or most other laypersons could easily determine the meaning of this, its purpose is readily apparent to the lawyer. Ms. Keeton must arbitrate her claims against Easterns, but the company need not use arbitration when it sues her. And it

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9 Here too the lower court erred, by suggesting that it was required to "view the clause through the eyes of the typical litigant, not one who is fortunate enough to receive free legal assistance." App. 69. In fact, unconscionability must be determined based on the relationship between the two parties to the contract. See *Restatement (2d) of Contracts*, § 208 (1981) (If contract "is unconscionable at the time the contract is made," court may refuse enforcement.) On the same page, the lower court evidently recognized this rule, chiding Ms. Keeton for failure to provide "evidence of high costs that would preclude *her* from bringing *her* claims." *Id.* (emphasis added).

requires no great insight into the workings of used car dealers to know that a suit for money owed is just about the *only* conceivable claim that Easterns might file against its customers.

This makes Easterns' arbitration clause a classic one-way street. But it is one-way as well for a second, independent reason. As it did in this case, Easterns often assigns its sales contracts (together with the associated promissory note, security agreement, etc.) to a financial institution such as Wells Fargo. However, Easterns' arbitration clause does not bind its assignees, stating instead that "this arbitration provision, does not apply to and shall not be binding on any assignee thereof." App. 21. In other words, Easterns' assignees (who are likely in most cases, as here, to be in privity when the post-sales dispute arises) have at least as much flexibility as Easterns (and perhaps more – even Eastern cannot simply decide that the clause is "not binding") to pick arbitration or litigation, depending on what gives the assignee the biggest advantage.

The point of these one-sided terms in the arbitration clause is not simply that the clause is unfair or unconscionable. Rather, the drafting demonstrates that Easterns' goal was to prevent consumers from initiating actions against the company, not to choose arbitration because it was faster or more economical. For example, if Eastern or its assignee filed a collection case in Superior Court, a consumer could defend by way of set-off or counterclaim, and present the very same issues (fraud, deceptive trade practices) that Easterns now claims Ms. Keeton must bring to its hand-picked arbitrator. The fact that Easterns was willing to allow this to happen (so long as it retained the right to sue in court) leaves little doubt that Easterns' real motive here was to choke off consumer cases filed against it, not to save time or money or judicial resources.

D. THE ISSUE OF UNCONSCIONABILITY OF THE ARBITRATION CLAUSE IS SOLELY FOR THIS COURT TO DETERMINE

As an alternative ground for rejecting Ms. Keeton's unconscionability challenge, the lower court held that this claim must be presented to the arbitrator chosen by Easterns. The holding was contrary to established law (such issues are reserved exclusively for the court when there is a substantial claim of unconscionability), and the ruling confused important concepts under the law of arbitration. The trial court held:

> As to the last of plaintiff's arguments [regarding arbitrator bias], the arbitration clause provides that the "validity of this arbitration clause or the Agreement shall be resolved by binding arbitration." (Contract ¶ 17). The Supreme Court held in *First Options v. Kaplan* that the question, "who has primary power to decide arbitrability" turns upon what the parties agreed about *that* matter. *First Options v. Kaplan*, 514 U.S. 938, 945 (1995). Parties may agree to arbitrate the issue of arbitrability. The Contract clearly states that the arbitrator shall decide the validity of the arbitration clause itself. Therefore, since the parties agreed to arbitrate the issue of arbitrability, the arbitrator should hear this dispute rather than the court. [App. 71]

Unfortunately, the lower court mixed up two related, but distinct, arbitration concepts. *Arbitrability* means which disputes are covered by the arbitration clause, while *validity* refers to whether the clause is enforceable or not (for example, whether it is unconscionable under state law, or whether it is the result of forgery). Under some circumstances, as *First Options* suggests, arbitrability will be up to the arbitrator in the first instance – particularly when the parties have committed that decision to arbitration. But on the facts presented here, the validity of the clause itself will always be for the court to decide.

Here the dispute is over validity, not arbitrability. And on this point, regardless of what Easterns' clause says, no person may be required to arbitrate the validity of a clause that is unenforceable under state law. *See, e.g., Burden v. Check Into Cash of Ky.*, 267 F.3d 483 (6th Cir. 2001); *Matterhorn, Inc. v. NCR Corp.*, 763 F.2d 866, 867 (7th Cir. 1985). In Texas, for

example, where the state's Supreme Court once required arbitration of challenges based on unconscionability, the same court has subsequently made clear that courts must decide the issue. *See In re Halliburton Co.*, 80 S.W.3d 566, 572 (Tex. 2002). Similarly, in Alabama (despite a generally pro-arbitration reputation), the rule is that:

> Where the attack is addressed to the arbitration clause itself, as opposed to the contract as a whole, the court, and not the arbitrator, resolves the issue. Thus, the threshold issue of unconscionability of an arbitration clause is an issue for the court and not the arbitrator. [*Am. Gen. Fin., Inc. v. Branch*, 793 So. 2d 738 (Ala. 2000) (citations omitted).]

So too here, the question whether the arbitration clause is unconscionable under state law – because it requires arbitration of only party's claims, because it imposes great costs on the consumer which would not be required in court, and because of arbitrator bias – must be decided by the court.

E. IN THE ALTERNATIVE, THIS COURT SHOULD REMAND WITH INSTRUCTIONS TO PERMIT DISCOVERY INTO THE UNCONSCIONABILITY OF EASTERNS' ARBITRATION PROCEDURE

As noted above, the Buyer's Order was silent as to who was to conduct the arbitration and how much that person would charge. Easterns did not disclose this crucial information until filing a reply in support of its motion to compel arbitration, in which Easterns asserted the right to name an individual, Paul Sheridan, who charges $200 an hour to conduct arbitrations for Easterns. In disclosing Mr. Sheridan's name, Easterns asserted that

> the plaintiff cannot argue that arbitration costs and fees will be prohibitive unless the court compels arbitration and the parties actually proceed with the selection of an arbitrator. Absent such a selection, any evidence as to cost of arbitration sought to be presented by the Plaintiff will be purely speculative. [App. 44]

The lower court rejected Ms. Keeton's claim of excessive cost, reasoning that:

> Plaintiff has to provide affirmative evidence of high costs that would preclude her from bringing her claims, and the plaintiff did

> not do this. Plaintiff cited the costs of the American Arbitration Association ("AAA"), although the arbitration provision did not provide that the AAA would arbitrate any claims arising form the Contract. No further evidence was provided other than a conjecture that half of the arbitration fee would be much more than any court fees assessed. This assertion is too speculative to demonstrate prohibitive expenses that would prevent the plaintiff from successfully arbitrating her dispute. [App. 69]

Of course, the reason Ms. Keeton did not present such evidence[10] is the fact that Defendants did not identify the arbitration provider, or the proposed arbitrator, or his hourly fee, until filing the *reply memorandum* in support of their motion to compel arbitration. To the extent that more evidence is required, the solution was not to compel arbitration, but to permit discovery into the likely cost of Easterns' arbitration procedure, including the likelihood that Ms. Keeton might be required to pay the entire cost rather than only half of it. Similarly, the lower court turned aside challenges to the fairness of the arbitrator selection method, claiming that a "consumer veto" would solve the problem.

If this Court finds that there is a need for further evidence of unconscionability, then it would be appropriate to remand the case for discovery by Ms. Keeton into these matters, followed by a fresh decision on the enforceability of the arbitration clause, applying correct legal standards.

Indeed, given the fact that the arbitration clause was presented below in a motion to *dismiss* the complaint, it would be appropriate to require an opportunity for discovery in all such proceedings. Super. Ct. Civ. Rule 8(c) makes arbitration an affirmative defense, even if the

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[10] In cases subject to the Federal Arbitration Act, 9 U.S.C. §§ 1, *et seq.*, it is up to the party challenging the arbitration clause to provide evidence of cost. *Green Tree Fin. Corp. v. Randolph*, 531 U.S. 79, 92 (2000). *Green Tree,* however, did not have occasion to consider or decide the procedural posture in which such evidence must be presented, a question here of District of Columbia law. And although the procedural posture of this case prevented Ms. Keeton from doing so, she nonetheless improved on *Green Tree*, where the "record reveal[ed] only the agreement's silence on the subject." *Id.* at 81.

arbitration has already occurred and an award has been made. Consequently, a plaintiff such as Ms. Keeton has no duty to plead facts about the validity of an arbitration clause in her complaint, and the absence of such facts is not a ground for dismissal for failure to state a claim. In such cases, the defendant seeking dismissal is actually requesting the equivalent of summary judgment; if it succeeds, there will be no case left in court. A plaintiff in these circumstances has the right to take discovery on all issues related to the enforceability of the arbitration clause.

Treating a motion to dismiss in favor of arbitration as a summary judgment proceeding in which evidence outside the pleadings can be discovered and presented is also consistent with D.C. Code § 16-4302 (as interpreted by this Court), which reads:

> (a) On application of a party showing an agreement described in section 16- 4301, and the opposing party's refusal to arbitrate, the Court shall order the parties to proceed with arbitration, but if opposing party denies the existence of the agreement to arbitrate the Court shall proceed summarily to the determination of the issue so raised and shall order arbitration if found for the moving party, otherwise, the application shall be denied.
>
> (b) On application, the Court may stay an arbitration proceeding commenced or threatened on a showing that there is no agreement to arbitrate. Such an issue, when in substantial and bona fide dispute, shall be forthwith and summarily tried and the stay ordered if found for the moving party. If found for the opposing party, the Court shall order the parties to proceed to arbitration.

In *Haynes v. Kuder*, 591 A.2d 1286, 1290 (D.C. 1991), this Court construed § 16-4302 to require fact-finding into a client's allegation that her attorney had fraudulently induced her into executing an arbitration agreement by failing to disclose material facts about the arbitration process. Requiring the protection of a summary judgment style procedure (*Haynes* held that deciding the validity of the arbitration clause "mirrors the familiar summary judgment procedure" and that "the trial court correctly granted what amounts to summary judgment" on the issue, *id.*) will ensure that plaintiffs have a reasonable opportunity to present all necessary

proofs on the issue of arbitration, just as at summary judgment. Indeed, it would be strange to provide less rigorous fact-finding when a party seeks outright dismissal (as Easterns did in this case) than when a party seeks to compel arbitration. It would also conform D.C. law to the general practice in the federal courts under the Federal Arbitration Act, which is mirrored by the District's Uniform Arbitration Act (soon to be substantially revised), D.C. Code §§ 16-4301, *et seq*. *See Blair v. Scott Specialty Gases*, 283 F.3d 595 (3d Cir. 2002) (remand for discovery into cost of arbitration procedure); *Toppings v. Meritech Mortgage Svcs.*, 140 F. Supp.2d 683, 685 (S.D. W. Va. 2001) (both citing *Green Tree Fin. Corp.*) (same for arbitrator bias and unconscionability generally). Thus, if the record is deemed insufficient, a remand is the proper course. *See Owens v. National Health Corp.*, 263 S.W.2d 876, 889 & n.4 (Tenn. 2007) (remand to determine unconscionability "due to the limited nature of the factual record"; discovery required as to certain issues).

CONCLUSION

The judgment of the Superior Court dismissing the complaint and compelling arbitration should be reversed, and the case should be remanded with instructions to strike the arbitration clause as unconscionable and to return the case to the appropriate civil calendar for discovery and trial. In the alternative, the case should be remanded with instructions to (a) permit appropriate discovery into Ms. Keeton's unconscionability defense, including the cost and arbitrator selection procedures of Easterns' arbitration clause, and (b) apply the correct legal standards to unconscionability of the arbitration clause upon the completion of such discovery.

Dated: March 17, 2009

C V Smith/mle

Cyril V. Smith

Certificate of Service

I hereby certify that I caused a true and correct copy of the foregoing Brief of the Legal Aid Society of the District of Columbia as Amicus Curiae Supporting Reversal to be delivered by first-class mail, postage prepaid, this 17th day of March, 2009, to:

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