AUTOMOBILE ARBITRATION FAIRNESS ACT OF 2008

HEARING

BEFORE THE

SUBCOMMITTEE ON
COMMERCIAL AND ADMINISTRATIVE LAW

OF THE

COMMITTEE ON THE JUDICIARY
HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

SECOND SESSION

ON

H.R. 5312

MARCH 6, 2008

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AUTOMOBILE ARBITRATION FAIRNESS ACT OF 2008

THURSDAY, MARCH 6, 2008

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMMERCIAL
AND ADMINISTRATIVE LAW,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Subcommittee met, pursuant to notice, at 9:37 a.m., in room 2237, Rayburn House Office Building, the Honorable Linda Sánchez (Chairwoman of the Subcommittee) presiding.

Present: Representatives Sánchez, Johnson, Watt, Smith, and Cannon.

Staff present: Norberto Salinas, Majority Counsel; Daniel Flores, Minority Counsel; and Adam Russell, Majority Professional Staff Member.

Ms. SÁNCHEZ. This hearing of the Committee on the Judiciary, Subcommittee on Commercial and Administrative Law will now come to order, and I will recognize myself for a short statement.

During the last session, this Subcommittee held two hearings focusing on arbitration. Our first hearing in June provided the Subcommittee with a basic knowledge of the history of arbitration, and its benefits and problems. We revisited arbitration during a hearing in October in which we reviewed H.R. 3010, the "Arbitration Fairness Act of 2007," authored by Congressman Hank Johnson. During those hearings we learned that an increasing number of businesses and employers have begun to utilize arbitration to the detriment of others, especially consumers.

Today we hold this legislative hearing on H.R. 5312, the "Automobile Arbitration Fairness Act of 2008" to respond to a significant problem with arbitration: the take-it-or-leave-it approach of pre-dispute binding mandatory arbitration clauses. This legislation targets certain arbitration clauses solely related to motor vehicle purchase or lease contracts. It would grant to automotive consumers what Congress extended to motor vehicle dealers in 2002: protection from mandatory binding arbitration clauses.

[The bill, H.R. 5312, follows:]

I

110TH CONGRESS
2D SESSION

H. R. 5312

To amend chapter 1 of title 9 of the United States Code with respect to arbitration of certain controversies.

IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 7, 2008

Ms. LINDA T. SÁNCHEZ of California (for herself, Mr. CONYERS, Mr. COHEN, Mr. WATT, Ms. ZOE LOFGREN of California, Mr. JOHNSON of Georgia, Mr. KUCINICH, Ms. WASSERMAN SCHULTZ, Mr. WEXLER, and Mr. DELAHUNT) introduced the following bill; which was referred to the Committee on the Judiciary

---

A BILL

To amend chapter 1 of title 9 of the United States Code with respect to arbitration of certain controversies.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Automobile Arbitration Fairness Act of 2008".

SEC. 2. AMENDMENTS.

(a) REQUIREMENTS FOR ARBITRATION OF CERTAIN CONTROVERSIES.—Chapter 1 of title 9, United States Code, is amended by adding at the end the following:

"§ 17. Requirements applicable to certain controversies

"(a) DEFINITIONS.—For purposes of this section—

"(1) the term 'motor vehicle' has the meaning given such term in section 30102 of title 49; and

"(2) the term 'motor vehicle consumer sales or lease contract' means a contract under which a person regularly engaged in the business of selling motor vehicles sells or leases a motor vehicle to an individual.

"(b) REQUIREMENTS.—

"(1) REQUIRED CONSENT.—Notwithstanding any other provision of this chapter or of any other law (excluding chapters 2 and 3 of this title), a controversy described in subsection (c) may not be settled by arbitration unless, after such controversy arises, all the parties to such controversy agree in writing to settle such controversy by arbitration.

"(2) REQUIRED EXPLANATION OF ARBITRATION AWARD.—Notwithstanding any other provision of this chapter or of any other law (excluding chapters 2 and 3 of this title), at the request of any of such parties made after such controversy arises and before an award is made in an arbitration agreed to in accordance with paragraph (1), such award shall include a brief, informal discussion of the factual

1 and legal basis for the award, but formal findings of
2 fact or conclusions of law shall not be required.
3 "(c) CONTROVERSY DESCRIBED.—Subsection (b)
4 shall apply with respect to a controversy arising out of
5 a motor vehicle consumer sales or lease contract as en-
6 tered into, amended, altered, modified, renewed, or ex-
7 tended on or after the date of the enactment of the Auto-
8 mobile Arbitration Fairness Act of 2008, or out of a re-
9 fusal to perform the whole or any part of such contract.".
10 (b) CONFORMING AMENDMENT.—The table of sec-
11 tions in chapter 1 of title 9, United States Code, is amend-
12 ed by adding at the end the following:

"17. Requirements applicable to certain controversies.".

○

Ms. SÁNCHEZ. Since then, automobile manufacturers have been prohibited from requiring automobile dealers to accept pre-dispute mandatory binding arbitration clauses in their franchise contracts. It seems only fair that consumers receive the same protection afforded to automobile dealers.

H.R. 5312 would give consumers the choice to settle a dispute related to their purchase or lease of a motor vehicle through arbitration or in court. As a result of this simple change, consumers would be able to consider the advantages and disadvantages of choosing to arbitrate with the specifics of their own case in mind. They could negotiate with the dealer or financier the terms of the arbitration agreement, should they decide to arbitrate.

Most importantly, arbitration could still be an avenue to resolve a dispute, but one to which all the parties would agree to voluntarily, fairly, and with full knowledge of the potential costs and benefits.

Today we gather to hear testimony from several individuals with knowledge of the arbitration process and consumer automobile contracts. I want to emphasize that today's testimony is very important for our understanding of the legislation. Accordingly, I very much am looking forward to hearing today's testimony, and I welcome a thorough discussion of the issues and legislation.

At this time I would now like to recognize my colleague, Mr. Cannon, the distinguished Ranking Member of the Subcommittee, for his opening remarks.

Mr. CANNON. Thank you, Madam Chair. I look forward to the testimony today. As we talked about earlier, there is a markup in Courts and Intellectual Property shortly after this, and I am a Member of that Subcommittee and so in the interest of time I would ask unanimous consent to submit my opening statement to the record——

Ms. SÁNCHEZ. Without objection.

[The prepared statement of Mr. Cannon follows:]

PREPARED STATEMENT OF THE HONORABLE CHRIS CANNON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF UTAH, AND RANKING MEMBER, SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW

Thank you Madam Chair and welcome to our witnesses.

This hearing marks the third time this Congress we have met to consider the question of mandatory binding arbitration.

I welcome the opportunity to talk about arbitration, because its wide availability is one of the most important features of our modern dispute resolution system.

It is a fact that our courts are overburdened, and arbitration has provided an escape valve for citizens hoping to avoid an unresponsive judicial system.

We should do everything we can to protect it.

Part of protecting it is overseeing it to assure that the abuse we have seen in the judicial system does not creep into the arbitration system.

Opponents of arbitration allege that mandatory binding arbitration clauses are abusive, and in response we have seen the introduction of H.R. 5312 in the auto sector, and we have seen the introduction of H.R. 3010 in the broader area of consumer, employment, franchise and other contracts.

One thing we have not seen, though, is hard, representative and credible evidence that mandatory binding arbitration is being widely abused.

On the contrary, the evidence we have seen is that mandatory binding arbitration produces fair results, prompt results, and lower costs of goods and services.

And we have seen that, to make the arbitration system ever better, companies asking their customers to consent to mandatory binding arbitration are offering those costumers pro-consumer contract clauses. These are known as "fair clauses."

They provide important innovations, such as opt-outs, off-ramps to small claims court, and fee-shifting so that consumers don't bear the costs of arbitration.

Although we have not seen much evidence concerning the use of mandatory binding arbitration in the auto purchase and lease field, I think there is every reason to believe that the same scenario exists in that sector.

Competition between dealers for customers is intense. Many dealers are bending over backward to make customers happy. Manufacturers are as well, as can be seen in the wave of high-mileage, multi-year warranties accompanying new car sales.

Solicitousness towards customers should be especially strong in the auto lease market—where so much depends on whether a dealer can keep a happy customer coming back every few years for a new lease.

The composition of today's witness panel—doubled up with consumer advocates, complemented by an individual witness and the arbitration sector—means we won't be able to hear from the auto dealers or any of the companies that write the peripheral contracts associated with car sales like financing agreements or insurance agreements.

That is unfortunate. We, for one, tried to obtain a witness from the auto finance sector, which works arm-in-arm with dealers on most any auto sale or lease in the country, but due to the size of the panel the majority could not accommodate that request.

The reason why we were interested in having the auto finance sector was related to their concerns that H.R. 5312 would include their contracts. It is my understanding that the Chair and the other sponsors present indicated that their intent is not to cover auto finance contracts, other peripheral contracts associated with an auto sale or lease, or even rental-car agreements so without their testimony we will presume that is the case.

I expect today that we will hear a good deal about how H.R. 5312 simply seeks to impose parity in contracts involving auto dealers. Under a 2002 law, dealers cannot be forced into mandatory binding arbitration with auto manufacturers. H.R. 5312, its proponents argue, would simply give the same benefit to consumers when they contract with dealers.

I find that argument unpersuasive. Because we limited arbitration in a particular sector in 2002 doesn't provide enough of a record for action here today.

When we are done today, I suspect we will be at the same place we were when we started—staring at a record that tells us that arbitration works, and that we should do nothing to limit buyers' and sellers' freedom to enter into it.

And I am left wondering whether there is anyone that would benefit from the proposed legislation other than trial lawyers.

I yield back the remainder of my time.

Mr. CANNON [continuing]. And just point out that we have been through several of these hearings and discussions about arbitration, but I would only make the point that there is a huge difference, just in nature, between dealers and consumers. We ought to focus on that during the course of this hearing.

With that, Madam Chair, I am happy to yield back.

Ms. SÁNCHEZ. I thank the gentleman for his statement.

Without objection, other Members' opening statements will be included in the record. And without objection, the Chair will be authorized to declare a recess of this hearing at any point.

[The prepared statement of Mr. Conyers follows:]

PREPARED STATEMENT OF THE HONORABLE JOHN CONYERS, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MICHIGAN, CHAIRMAN, COMMITTEE ON THE JUDICIARY, AND MEMBER, SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW

Properly used, arbitration can help parties avoid the delay and costs of protracted litigation.

But unfortunately, as we have heard in prior Subcommittee hearings, some businesses are insisting on mandatory arbitration clauses in their consumer contracts, with consumers who have no practical choice but to go along, because of their unequal bargaining position.

These mandatory arbitration clauses are written by the business's lawyers, and quite naturally often favor the business.

Some of the procedural requirements they impose can make it exceedingly difficult, even cost- prohibitive for consumers to protect their rights under the law.

At their essence, these mandatory arbitration clauses, when imposed on consumers who have no power to refuse them, force consumers to give up their constitutional right to a jury trial.

Chairwoman Sánchez has introduced H.R. 5312, the "Automobile Arbitration Fairness Act of 2008," to address these concerns in one specific area, automobile sales and leases. This bill would give consumers who have a legal claim against an automobile dealer the right to *choose—after* the problem arises—whether to resolve the claim through arbitration, or in court.

The auto dealers obtained this same relief from Congress a few years ago, when we decided that in light of the unequal bargaining position auto dealers faced against manufacturers in their franchise agreements, it was not fair to permit the manufacturers to impose mandatory arbitration clauses.

It is now time to take this same step on behalf of fundamental fairness with the automobile dealer- consumer relationship.

I commend Chairwoman Sánchez for her leadership in authoring this legislation, which is supported by a majority of the Subcommittee's Members.

And I look forward to the testimony from today's witnesses.

[The prepared statement of Mr. Johnson follows:]

PREPARED STATEMENT OF THE HONORABLE HANK JOHNSON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF GEORGIA, AND MEMBER, SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW

- Thank you Madame Chairwoman for holding this important hearing today on H.R. 5312, the Automobile Arbitration Fairness Act of 2008.
- And many thanks to our witness for coming before the Committee.
- Fairness is the key word in the title of this bill and fairness is the underlying issue that brings us here today.
- In 2002, with bipartisan support and over 250 co-sponsors Congress passed the "Motor Vehicle Franchise Contract Arbitration Fairness Act."
- At that time, auto dealers sought relief because they were saddled with mandatory binding arbitration agreements in franchise contracts. They rightly cited the inherent unfair nature of such agreements.
- The 2002 Bill, introduced by Representative Mary Bono, granted relief by making such agreements voluntary. It was a sensible, no nonsense solution to a heavy-handed practice. It leveled the playing field for auto dealers.
- It is a bill that makes perfect sense. The Congress overwhelmingly supported the idea.
- Fast forward to 2008 and H.R. 5312, a bill that would extend to automobile consumers the same fairness that the automobile dealers now enjoy.
- We are all familiar with purchasing a car; it is often an arduous and complicated process, filled with stacks of papers to sign, complicated financial terms, and wait times that can last for hours,
- And when consumers finally walk away—worn out—but usually happy with a vehicle their families will depend on to get to work, school, and home; they are totally unaware that tucked away in the "mice print" of all those financial terms and "legalese" is a provision that strips them of a constitutional right.
- For the average American the right to a day in court is a dearly held right one that is automatically assumed, one that is deeply embedded in the Bill of Rights.
- Yet there are thousands of citizens, who unknowingly have given away their right to a trial by signing consumer contracts when they purchase a vehicle.
- And more ironically they have done so because of the heavy-handed tactics of the very auto dealers who just six short years ago came before Congress to have that right restored to them.
- Later, for those consumers who have a problem with their vehicle or the dealership the small "mice print" clause becomes a ticking time bomb that explodes when they seek relief.
- These clauses are a very unpleasant surprise to consumers who never realized that their consumer dispute would be forced to go to a private, closed system with no oversight, no chance of appeal and no real justice.

- So we are back to a simple matter of fairness— Good for the goose, good for the gander. Automobile dealers must extend the same terms to their customers that they so rightfully claimed for themselves.
- As most of you are aware, in the last session, I introduced, H.R. 3010, the Arbitration Fairness Act, which would do away with pre-dispute mandatory arbitration agreements in all consumer, medical, employment, and franchise contracts.
- I did that because fair is fair and the fundamental feature of a fair justice system is that both sides to a dispute are on equal footing in a public court of law, governed by the civil rules of procedure.
- The imminent associate Supreme Court Justice the late William J. Brennan once put it very succinctly

"The Framers of the Bill of Rights did not purport to "create" rights. Rather they designed the Bill of Rights to prohibit our Government from infringing rights and liberties presumed to be preexisting."

Clearly, the right to a trial is a widely presumed, preexisting liberty and we must ensure that it is preserved and protected for all Americans.

- So, I return to my previous statement, "Fairness is the key word in this Bill and fairness is the underlying issue that brings us here today—and—there is no time like today—to restore fairness to the people!
- Thank you Madame Chairwoman and I yield back.

Mr. SMITH. Madam Chair, I would like to be recognized, just very briefly.

Ms. SÁNCHEZ. Absolutely. I would recognize our distinguished Ranking Member of the full Committee, Mr. Smith, for opening remarks.

Mr. SMITH. Thank you, Madam Chair. Actually, I don't have an opening statement and I will certainly concur with the precedent that has been set about putting it in the record. I just wanted to say that I think the subject of today's hearing is a very important one.

I tend to lean toward appreciating the value of arbitration, and perhaps I ought to confess to a slight bias. Long ago and far away when I was a county commissioner in Bexar County in San Antonio, Texas, I actually started the first mediation center in that county. So I think that that could have real value. Although I also recognize that there are two sides to the issue and that is what is going to be explored at this very interesting hearing today.

I also want to follow up on what the Ranking Member, Mr. Cannon, said. I, too, have to be in 20 minutes at the mark-up of a bill in the IP Subcommittee, and I just hope, Madame Chair that you will pass along to those who make decisions as to when Subcommittee hearings and mark-ups are scheduled that, many times, it puts Members in the untenable position, where we would like to be at a hearing, and we would like to be at a mark-up. And it is probably helpful to Members not to have both scheduled concurrently, just because it does put us in the position of having to choose.

So I just make that statement for the record and hope that those who schedule these kinds of hearings and other mark-ups can consider that in the future. And with that I will yield back.

Ms. SÁNCHEZ. I thank the gentleman for his comments, and I am mindful of the concern of concurrent hearings and mark-ups.

Now, I am pleased to move on and introduce the witnesses for today's hearing. Our first witness is Rosemary Shahan. Did I pronounce that correctly?

Ms. SHAHAN. Yes, thank you.

Ms. SÁNCHEZ. Okay. Ms. Shahan is the president of Consumers for Auto Reliability and Safety, otherwise known as CARS. In 1979 she initiated California's Auto Lemon Law and worked as a volunteer for enactment of the law from 1979 to 1982. This legislation became the model for similar laws in all 50 states.

Ms. Shahan has continued her consumer advocacy work and has been a major force in the adoption of Federal Motor Vehicle Safety Standards to require airbags. She spearheaded Federal Motor Vehicle Safety Standards adopted by the National Highway Traffic Safety Administration to improve vehicle safety recalls and improve seatbelts for smaller adults and children. Ms. Shahan also assisted in the enactment of major landmark auto safety and antifraud legislation.

Our second witness is Erika Rice. Ms. Rice was born and raised near Dayton, Ohio, and now lives in the town of Arcanum, Ohio, is that correct?

Ms. RICE. Yes, it is.

Ms. SÁNCHEZ. She has an associate's degree in social work, and has been working for more than 3 years with children with emotional, behavioral, and mental health disorders. Ms. Rice is here today to tell us about her experience with mandatory binding arbitration in an automobile contract.

Our third witness is Richard Naimark. Mr. Naimark is senior vice president of American Arbitration at the International Center for Dispute Resolution Research. He is the founder and former executive director of the Global Center for Dispute Resolution—which conducted research in arbitration and alternative dispute resolution for business disputes in cross-border transactions.

Mr. Naimark is an experienced mediator and facilitator, having served in a wide variety of business and organizational settings. Since joining the association in 1975, Mr. Naimark has conducted hundreds of seminars and training programs on dispute resolution and published several articles on alternative dispute resolution.

Welcome to you, Mr. Naimark.

Our final witness on the panel is Hallen Rosner. Mr. Rosner is a partner at Rosner & Mansfield, LLP, specializing in auto fraud. He also represents the National Association of Consumer Advocates, a nonprofit corporation whose primary focus involves the protection and representation of consumers.

Over the past 23 years Mr. Rosner's firm has represented thousands of consumers and, in particular, servicemen and women who serve in the armed services. In 2007 his firm was awarded the Public Service Award by the San Diego Bar Association, recognizing over two decades of helping consumers.

Mr. Rosner teaches military, legal aide and volunteer attorneys, among others, about how to understand vehicle contracts and recognize the most common forms of auto fraud. He is a board member for EPIC, the Energy Policy Initiative Center, and has acted for many years as legal counsel for the consumer organization UCAN, the Utility Consumer's Action Network. Mr. Rosner writes "Ask Hal," an Internet auto-fraud advisory column that gets over 10,000 hits a month from across the country.

I want to thank you all for your willingness to participate in today's hearing. Without objection, your written statements will be

placed into the record in their entirety, and we are going to ask that you please limit your oral testimony today to 5 minutes.

You will note that we have a lighting system, and when your time begins you will receive a green light on the lighting system. After 4 minutes of testimony you will get the yellow warning light that you have about a minute to finish your testimony. And when the light turns red, of course, your time has expired and we would ask that you finish off any final thoughts so that we can move on to our next witness.

After each witness has presented his or her testimony, Subcommittee Members will be permitted to ask questions subject to the 5-minute limit.

With that I will invite Ms. Shahan to please proceed with her testimony.

TESTIMONY OF ROSEMARY SHAHAN, PRESIDENT, CONSUMERS FOR AUTOMOBILE RELIABILITY AND SAFETY, SACRAMENTO, CA

Ms. SHAHAN. Thank you, Chairwoman Sánchez and Members of the Committee, and Ranking Member Mr. Cannon, for the invitation to testify today in support of H.R. 5312, the "Automobile Arbitration Fairness Act of 2008."

I am Rosemary Shahan, president of Consumers for Auto Reliability and Safety. We are based in Sacramento, and we are delighted to have the opportunity to support this desperately needed legislation that will improve protections for consumers and also benefit honest businesses by freeing car buyers from having mandatory pre-dispute arbitration imposed on them as a condition of selling or leasing a vehicle.

H.R. 5312 will allow consumers and auto dealers to resolve disputes through arbitration if they choose after a dispute has arisen. Thus, it will make participation in arbitration more informed and voluntary. H.R. 5312 will ensure that a consumer's rights are protected against a fraudulent auto dealer who seeks to use a binding mandatory arbitration clause buried in a purchase contract to take advantage of the consumer. The bill will also give auto consumers the same right to be free from binding mandatory arbitration agreements that auto dealers currently enjoy.

First I should tell you, I am not an attorney. I am a former college English teacher who had a horrendous car experience at a car dealership in Lemon Grove, California, and as well, my family was stationed on active duty with the United States Navy.

And that led me to get active on behalf of car owners and initiate California's Auto Lemon Law that was authored by Assemblymember Sally Tanner that became the model for similar laws in all 50 states. Our organization is dedicated to preventing motor vehicle related fatalities, injuries, and economic losses, and we see this as one of the most important bills pending before Congress to help consumers across the country.

Pre-dispute mandatory binding arbitration deprives consumers of access to justice. Since 1979, I have listened to complaints of consumers all over the country who are harmed due to illegal practices perpetrated by car dealers. The victims run the gamut. Most of them are pretty sophisticated; they don't have problems with other

kinds of financial transactions but they are no match for car dealers who sometimes engage in very sophisticated forms of fraud.

Some of the consumers have been students who had to drop out of school because their vehicles kept breaking down, even though when they bought them they were promised they were in mint condition. Others are active duty members of our Armed Forces and their families, who are often targeted by unscrupulous auto dealerships. And this is a problem nationally; if you ask the military about it they can tell you more.

For decades I have been able to offer consumers hope that they could recover from their losses and be made whole if they simply persisted in pursuing their rights. We actually have really good laws on the books, on the Federal level and on the state level, to protect consumers, but over the past several years it has become increasingly difficult for consumers to have access to justice under those laws due to the imposition of pre-dispute binding mandatory arbitration.

Pre-dispute binding arbitration is inherently unfair. As Members of Congress argued in favor of granting auto dealers access to courts for resolving disputes with auto manufacturers, the contracts are take-it-or-leave-it, boiler plate contracts of adhesion. There is no opportunity to negotiate, especially since the majority of car dealers now use these clauses in their contracts.

The parties to the contracts are on an unequal footing; the arbitrators are inherently biased in favor of repeat customers like the car dealers, who contract their decisions and have the advantage of knowing which arbitrators or which arbitration processes tend to rule in their favor. Arbitrators are not required to apply the law or adhere to judicial precedent.

Even if the arbitrators totally disregard the law, there is rarely any review, little or no check on their power; there is usually not even a record that would be subject to review. Discovery is very, either nonexistent or very limited, and without discovery consumers are severely disadvantaged.

H.R. 5312 will provide consumers with the same protections already enjoyed by car dealers. The same arguments that were made by auto dealers in Congress in favor of preserving their rights apply equally to consumers, if not more. As Senator Hatch stated when he introduced S. 1140, the Motor Vehicle Franchise Contract Arbitration Fairness Act of 2001, "The new law was needed to protect car dealers from having mandatory arbitration clauses imposed on them by automakers due to their unequal bargaining power."

And I would be happy to answer any questions that you or the Committee may have.

[The prepared statement of Ms. Shahan follows:]

PREPARED STATEMENT OF ROSEMARY SHAHAN

United States House of Representatives
Committee on the Judiciary
Subcommittee on Commercial and Administrative Law

Honorable Linda Sanchez, Chairperson

March 6, 2008

Testimony
Presented by

Rosemary Shahan
President, Consumers for Auto Reliability and Safety

In Support of Passage of H.R. 5312 The Automobile Arbitration Fairness Act

Consumers for Auto Reliability and Safety
1303 J Street, Suite 270
Sacramento, CA 95814
530-759-9440

Chairwoman Sanchez and Members of the Committee:

Thank you for the opportunity to testify today in support of HR 5312, the Automobile Arbitration Fairness Act of 2008. This desperately needed legislation will improve protections for consumers and also benefit honest businesses by freeing car buyers from being compelled to surrender their constitutional rights as a condition of purchasing or leasing a motor vehicle. We applaud your leadership in authoring this important consumer protection measure and also greatly appreciate the co-sponsorship of Members of this Subcommittee.

H.R. 5312 will allow consumers and auto dealers to resolve disputes through arbitration, if they choose, after a dispute has arisen. Thus, it will make participation in arbitration more informed and voluntary. H.R. 5312 will ensure that a consumer's rights are protected against a fraudulent auto dealer who seeks to use a binding mandatory arbitration clause buried in a purchase contract to take advantage of that individual. The bill will also give auto consumers the same right to be free from binding mandatory arbitration agreements that auto dealers currently enjoy.

Background about Consumers for Auto Reliability and Safety

First, a disclaimer. Unlike others who may testify, I am not an attorney. I am a former college English teacher who had a horrendous car problem at a car dealership in Lemon Grove, California, while my family was stationed on active duty with the United States Navy in San Diego, in 1979. That experience led me to initiate California's auto lemon law for car buyers, authored by Assemblywoman Sally Tanner, which became the model for similar laws in all 50 states.

Our organization, Consumers for Auto Reliability and Safety (CARS), is a national, award-winning non-profit auto safety and consumer advocacy organization based in Sacramento. CARS is dedicated to preventing motor vehicle-related fatalities, injuries, and economic losses. CARS has a long history of pro-consumer advocacy that has led to the enactment of numerous state laws and national regulations to improve vehicle safety, make our roads and highways safer, and make the automotive marketplace fairer, including several landmark measures signed into law by Governors from both major parties.

In the aftermath of Hurricanes Katrina, Wilma, and Rita, I was invited by the Senate Committee on Commerce, Science and Transportation Subcommittee on Consumer Affairs, Product Safety, and Insurance, Chaired by former U.S. Senator George Allen, to testify regarding flood and salvage vehicle frauds, which cost American car buyers billions each year and threaten the public health and safety.

In 2004 and 2005, CARS led efforts to make California's Car Buyers Bill of Rights as strong as possible for consumers. That legislation (AB 68, Montañez), which

reflects a compromise struck among key legislators, the Governor, and auto dealers, was spurred by a stronger ballot initiative proposed by CARS that polled at over 80% support statewide. AB 68 passed with overwhelming bi-partisan support and was signed into law by Governor Schwarzenegger in 2005. It took effect on July 1, 2006. While the law is seriously flawed, its enactment is evidence of widespread support for reforming auto sales in the nation's largest automotive marketplace.

The most recent legislation CARS sponsored in California, SB 234, authored by Senator Ellen Corbett, passed unanimously and was signed into law by Governor Schwarzenegger. That new law extends protections under California's auto lemon law to active duty members of our nation's armed forces, regardless where they purchase or register their vehicles.[1]

Pre-dispute mandatory binding arbitration deprives consumers of access to justice

Since 1979, I have listened to complaints from consumers around the nation who were harmed due to illegal practices perpetrated by auto dealers. The victims run the gamut. Most are fairly sophisticated and savvy consumers who succeeded in navigating other complex financial transactions, but were no match for unscrupulous auto dealers. Others are struggling students who just bought their first cars. Some of the students had to drop out of school because their vehicles kept breaking down, despite ads promising they were in "mint condition." Others are active duty members of our Armed Forces and their families, who are often targeted by unscrupulous auto dealerships.[2]

For decades, I have been able to offer consumers hope they could recover from their losses and be made whole, if they simply persisted in pursuing their rights. But over the past several years, that has changed. The laws are still on the books, but millions of consumers are enduring injustices without any meaningful recourse, due to the imposition of pre-dispute binding mandatory arbitration.

Pre-dispute binding arbitration is inherently unfair

As Members of Congress argued in favor of granting auto dealers access to courts for resolving disputes with auto manufacturers:

- The contracts are take-it-or-leave it, boiler-plate contracts of adhesion. There is no real opportunity to negotiate.

- The parties to the contracts are on an unequal footing.

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[1] See report posted on CARS' website, at: http://www.carconsumers.com/SB234_LL.html

[2] According to the Armed Forces themselves, auto-related frauds are a serious problem that adversely impacts morale, readiness, and the ability of our troops to accomplish their mission. More details, including links to news reports, are posted at: http://www.carconsumers.com/military_ripoffs.html.

- Arbitrators are inherently biased in favor of repeat customers, who can track their decisions and have the advantage of knowing which arbitrators have ruled in their favor in the past.

- Arbitrators are not required to apply the law or adhere to judicial precedents.

- Even if the arbitrators totally disregard the law, there is little or no review, and rarely any check on their power. There is seldom even any record that would be subject to review.

- Discovery is either non-existent or very limited. Without discovery, consumers are severely disadvantaged. This enables crooked dealers to conceal material facts from their victims and from the arbitrators.

- Arbitrations occur in a vacuum. They almost always operate in secret. If a dealer has engaged in widespread violations of the law, it may never come to the attention of law enforcement agencies or policymakers, who might otherwise act to protect the public.

HR 5312 will provide consumers with the same protections already enjoyed by auto dealers.

The same arguments that were made by auto dealers and Congress in favor of preserving the rights of auto dealers apply equally to consumers, if not more.

As Senator Hatch stated when he introduced S. 1140, "The Motor Vehicle Franchise Contract Arbitration Fairness Act of 2001," the new law was needed to protect auto dealers from having mandatory arbitration clauses imposed upon them by auto manufacturers, due to their "unequal bargaining power."[3]

As Senator Grassley, speaking in support of S. 1140, stated:

> "While arbitration serves an important function as an efficient alternative to court, some trade-offs must be considered by both parties, such as limited judicial review and less formal procedures regarding discovery and rules of evidence. When mandatory binding arbitration is forced upon a party, for example when it is placed in a boiler-plate agreement, it deprives the weaker party the opportunity to elect another forum. As a proponent of arbitration I believe it is critical to

[3] Statements on Introduced Bills and Joint Resolutions, United States Senate, June 29, 2001. Statement by Senator Hatch of Utah.

> ensure that the selection of arbitration is voluntary and fair…Unequal bargaining power exists in contracts between automobile and truck dealers and their manufacturers. The manufacturer drafts the contract and presents it to dealers with no opportunity to negotiate…The purpose of arbitration is to reduce costly, time-consuming litigation, not to force a party to an adhesion contract to waive access to judicial or administrative forums for the pursuit of rights under State law."[4]

Senator Grassley also stated that:

> "This legislation will go a long way toward ensuring that parties will not be forced into binding arbitration and thereby lose important statutory rights. I am confident that given its many advantages arbitration will often be elected. But it is essential for public policy reasons and basic fairness that both parties to this type of contract have the freedom to make their own decisions based on the circumstances of the case."[5]

While S. 1140 did not pass, auto dealers were given an exemption from the FAA, in order to preserve their rights, via passage of H.R. 2215 in 2002. That act, now codified at 15 U.S.C. section 1226, prohibits auto manufacturers from including any type of pre-dispute arbitration clause in franchise contracts with auto dealers. Specifically, it provides that arbitration may be used to settle a controversy arising out of a motor vehicle franchise contract only if both parties consent, in writing, and only after the dispute arises.

Unequal bargaining power exists between consumers and dealers

Clearly, consumers are in an even less equal bargaining position vis-à-vis auto dealers than are dealers, vis-à-vis auto manufacturers. It is now the norm for franchised auto dealers and the largest auto dealership chains to use pre-printed contracts that include mandatory pre-dispute binding arbitration. Lenders have informed auto dealers that they will not accept retail installment contracts for auto loans unless the dealers include binding mandatory arbitration clauses in the contracts.

Consumers are inherently in an unequal bargaining position, where they have little choice but to enter into a contract that deprives them of their rights, in order to obtain transportation. This is particularly true if they cannot afford to pay cash and must

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[4] Statements on Introduced Bills and Joint Resolutions, United States Senate, June 29, 2001. Statement by Senator Grassley of Iowa.

[5] Statements on Introduced Bills and Joint Resolutions, United States Senate, June 29, 2001. Statement by Senator Grassley of Iowa.

be approved for a loan, since lenders now refuse to accept contracts without binding mandatory arbitration clauses.

Thanks to franchise laws in all 50 states that grant auto dealers a special monopoly, consumers who wish to purchase a new vehicle are virtually captive to franchised auto dealers to make their purchase. They have no choice. They have to buy the car from a franchised auto dealer, or go abroad to buy direct from the factory.

Used car buyers have more choices, including purchasing from individuals and over the internet. In the past, consumers who chose to purchase vehicles from licensed dealers had a reasonable expectation that if there was a major problem, they would be protected by various state and federal laws. Now, due to the imposition of arbitration in dealer contracts, consumers may actually get LESS protection than if they bought the car from an individual.

Not only are the stakes high for consumers in terms of sheer dollar amounts, but they are also high in terms of the potential impact on their entire future. Worst case scenario: if the vehicle has serious hidden, undisclosed defects, it can kill them and/or members of their family, as well as others who happen to share the roads. A bad car deal can also cost them their job, destroy their credit, and saddle them with added debt.

Among the factors that create the vast inequality in bargaining position:

- Dealers and their attorneys prepare the contracts and present them to the consumer. They are contracts of adhesion, presented on a take-it-or-leave-it basis, and many of the terms are not negotiable.

- The contracts are lengthy and complex. The language is highly legalistic. Even highly-educated consumers find the contracts to be intimidating and confusing. This is particularly true of lease transactions.

- Consumers generally lack access to legal counsel specializing in auto sales transactions. Dealers typically have attorneys on retainer. They also belong to trade associations that employ full-time high-powered legal talent.

- Consumers are led to believe that when they purchase or lease a vehicle from a licensed auto dealership they have a reasonable expectation that the business practices are legitimate. To some extent, their guard is down.

- Most consumers purchase a vehicle only two or three times a decade. More consumers are keeping their vehicles longer, making the length of time between purchases longer. Dealers typically buy and sell vehicles on a daily basis. They are pros.

- When the product is a used car, auto dealers have superior knowledge of the history and condition of the product. For example, they know whether they bought the car at a deep discount from a "salvage" auction, where frame damage and other faults are openly announced.

- For most car buyers, purchasing a vehicle is unlike any other transaction they have ever experienced. School curriculums typically do not prepare students for the high-stakes negotiations. Other purchasing experiences do not prepare car buyers for the unique challenges of buying a car.

- Sales and finance and insurance (F & I) personnel receive intensive training in how to maximize profits for the dealership. They typically receive bonuses and perks based on their performance, so have strong incentives to get the most out of each transaction. Some F & I managers are paid $300,000 or more per year, mostly in bonuses, based on how much they extract from each customer.

- Auto sales scams have gone high-tech. The practices are increasingly sophisticated, and are challenging for even high-tech crime specialists to identify.

- Typically, pre-dispute binding arbitration contracts allow dealers to select the forum and decide on the terms. This loads the dice in favor of defendants, who are in a superior position to select forums that will rule in their favor.

- Some arbitration forums allow arbitrators to charge high fees, such as $500 to $1,000 per hour, plus administrative charges. The vast majority of consumers, who have to stretch their budgets to purchase a vehicle, are in no position to shell out another $20,000 or more to obtain a biased decision.

- Some arbitration forums allow arbitrators to inflate their charges by requiring briefings and hearings for even minor disputes between counsel. In court, minor disputes are discouraged by code, which requires or allows judges to award sanctions.

Overview: scope and types of auto sales scams; private enforcement is essential

Last year, American car buyers purchased 57,500,000 vehicles. Of those, 16,100,000 were new and 41,400,000 were used.[6] For most consumers, a motor vehicle

[6] "Keys to Buying a Used Car," by Ken Bensinger, *Los Angeles Times*, March 2, 2008. The *Los Angeles Times* cites CNW Marketing Research Inc.as its source.

is the second-largest purchase they make, second only to a home. The average price of a new vehicle is now estimated to be over $27,800, and used cars average about $13,900.[7]

Given the immense size of the automotive marketplace, and the vast sums involved, private enforcement of federal and state consumer protection laws is essential to deter massive fraud. No federal, state, or county agency has the staff or resources necessary to police the tens of millions of transactions that occur each year. Typically, law enforcement agencies act only when there is a pattern and practice of rampant lawbreaking that comes to their attention. Especially in the aftermath of 9/11, state motor vehicle departments, which license auto dealers, have other priorities. To a great extent, consumers are on their own.

Making matters worse, the most-prevalent auto sales-related crimes are increasingly sophisticated, involve high-tech prowess, and often cross state lines. Prosecuting those crimes has become increasingly challenging and costly for public law enforcement agencies at a time when they are strapped for resources.

Here in California, passage of Proposition 64, backed largely by auto dealers, eliminated the ability of non-profit organizations to represent the public interest in curbing widespread violations of state laws, creating a huge enforcement vacuum. Then Governor Schwarzenegger vetoed SB 1489 (authored by Senator Ducheny), which would have allowed the Attorney General to continue to be able to recoup the costs incurred in litigating against corrupt corporations with enormous resources, on behalf of the citizens of California, when the Attorney General prevails. That has inevitably lessened the ability of our state's top cop to address all but the most pressing cases.

Counties are also reeling from the downturn in the economy, and District Attorneys generally tend to emphasize violent crimes over property crimes.

At the same time, **the public interest in curbing auto sales frauds has never been clearer or stronger.** According to the U. S. Department of Justice, auto-related frauds rank among the nation's top property crimes. To give some sense of the scope of just part of the auto sales problem: According to a report commissioned by the U.S. DOJ, completion of a national database system to help curb illicit activity involving stolen and damaged autos would save the American public between $4 billion and $11.3 billion per year.[8]

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[7] Edmunds.com. See website at: http://www.edmunds.com/advice/buying/articles/45310/article.html

[8] "In 2001, at the request of the Department of Justice, the Logistics Management Institute (LMI) submitted a report to DOJ's National Institute of Justice, found that: "...NMVTIS-if it is fully implemented in all 50 states and the District of Columbia, and if it is 100 percent effective-can achieve benefits in the range of $4 billion to $11.3 billion annually."—US Department of Justice website, at: http://www.ojp.gov/BJA/grant/nmvtis.html The cost-benefit analysis is posted at: http://www.ojp.gov/BJA/pdf/LMI_NMVTIS.pdf

According to the National Highway Traffic Safety Administration, odometer fraud costs consumers over $1 billion a year, based solely on the difference between the price car buyers pay and the actual value of the vehicles with rolled-back odometers. The agency has also found that the incidence of odometer fraud is escalating.

Frauds involving the illegal sales of damaged autos cost American consumers billions of dollars each year. According to Experian Automotive, approximately 7 million vehicles that were deemed to be a total loss because they sustained severe damage in wrecks or floods are now re-registered and being driven our roads.[9] Many millions more have sustained major damage, but were not totaled. Dealers themselves acknowledge that auto salvage frauds, including "title washing" across state lines, is a serious problem that needs to be addressed.

In California alone, more than 1,690,000 vehicles currently registered for use on our roads have had their titles branded as "salvage," indicating they were so severely damaged it would not pay to fix them properly.[10]

Damaged auto frauds also pose a serious threat to the public health and safety. For example, shady rebuilders often fail to replace deployed air bags, which can be expensive. Instead, they stuff the compartments where the air bags belong with shop rags, paper, or whatever else is handy. In some cases, consumers are killed or suffer debilitating injuries when they are sold rolling wrecks that are structurally unsound. Some vehicles, known as "chop jobs," are literally halves of two different cars, welded together. On impact, they split apart, spilling their hapless occupants onto the highway.

Auto "lemon laundering" of seriously defective lemon vehicles, previously repurchased by the manufacturers due to incurable defects, then resold to unsuspecting used car buyers, costs consumers at least another $1 billion per year. It also exposes car buyers and their families to life-threatening safety defects including faulty brakes and steering, electrical fires, engines that intermittently stall in traffic without warning, wheels that fall off, and other hazards.

Other common scams perpetrated by auto dealers that cost American consumers billions more:

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[9] "Citing 15-Year Delay, Suit Seeks Action on Rebuilt Wrecks," by Christopher Jensen, The New York Times, February 10, 2008. "Experian automotive, an Illinois company that sells information gathered from state motor vehicle departments, said its records showed that there were about seven million vehicles on the road that at one time were damaged so badly that the titles were marked as 'junked, scrapped, unrebuildable, salvage, or rebuilt.'"

[10] Source: California Department of Motor Vehicles. Based on number of vehicles with "salvage" titles as of July 1, 2007. Note: this figure is artificially low, as it fails to include vehicles that were never properly branded or have had their titles "washed," a very common form of fraud.

- Charging excessive hidden dealer "markups" ("markups" are kickbacks dealers receive from lenders in return for raising the interest on auto loans, above the rate the consumer qualifies for, based on their credit history)
- Falsifying signed credit applications to exaggerate income
- Engaging in "yo-yo" financing to gouge purchasers (misleading or intimidating consumers into accepting worse terms, after the consumer has taken possession of their new purchase)
- Engaging in loan packing of unwanted items (adding high-profit extras while misrepresenting their cost to the buyer, in a sophisticated shell game)
- Forging documents
- Selling used cars or "demonstrators" as new cars
- Concealing prior status as a daily rental, police vehicle, or taxicab
- Taking vehicles in trade and failing to pay off the liens, as promised
- Failing to disclose "negative equity" from prior transactions that is rolled over into new loans
- Engaging in high-pressure sales tactics, such as refusing to return keys for buyers' vehicles after they are test-driven, until they purchase another vehicle
- Altering VIN numbers to disguise vehicle histories
- Altering vehicle history reports to conceal prior damage and odometer rollbacks
- Selling stolen vehicles

From a macro-economic perspective, auto sales and lending practices are shrinking the market for homes and other products by soaking up a disproportionate share of consumers' take-home pay. Except for unjustifiably inflated auto loans, millions more consumers would qualify to purchase a home.

Auto loans are increasingly disproportionate to the value of the vehicles. This is particularly likely to occur when the true value is concealed from the buyer.[11] In order to make the artificially inflated monthly payments affordable, auto loans are getting longer. The median auto loan is now over 60 months, with increasing numbers stretching into 7 or 8 years. As a consequence, consumers trade in their cars long before the loan is paid off. Between roughly 30% to 40% of car buyers are now "upside down" – burdened with "negative equity" -- when they purchase their next vehicle. That debt is then rolled over into the next transaction. Car buyers are sinking deeper into debt for a product that depreciates the moment they drive it off the lot.

[11] Changes in federal bankruptcy law, backed by auto dealers and signed into law by President Bush, shifted substantial risk from lenders and dealers to consumers. Unlike before, when consumers were liable only for the fair market value of their vehicles, they are now being held liable for the entire amount of loans, even when the vehicle is worth far less than the amount they owe, due to undisclosed prior damage or odometer rollbacks.

All 50 states have tried to protect car buyers from these scams, but the illegal activity can still flourish and individuals are severely harmed when consumers are denied their rights due to the imposition of pre-dispute binding arbitration agreements.

The good news is that by adopting H.R. 5312, and empowering individual consumers to obtain relief and deter auto scams, Congress can make a major, tangible improvement in the lives of tens of millions of Americans and their families.

States rely on Congress to address arbitration abuses

Speaking in support of passage of S. 1140, to improve access to the courts for auto dealers, Senator Grassley explained that:

> "In 1925, when the [Federal Arbitration Act] FAA was enacted to make arbitration agreements enforceable in Federal courts, it did not expressly provide for preemption of State law. Nor is there any legislative history to indicate Congress intended to occupy the entire field of arbitration. However, in 1984 the Supreme Court interpreted the FAA to preempt state law in Southland Corporation v. Keating. Thus, State laws that protect weaker parties from being forced to accept arbitration and to waive State rights, such as Iowa's law prohibiting manufacturers from requiring dealers to submit to mandatory binding arbitration, are preempted by the FAA."[12]

Because the FAA has been interpreted to preempt state law, states are hamstrung in their ability to protect their citizens from the pitfalls of arbitration.

In 2004, California legislators considered AB 2656, The Car Buyer's Legal Equality Act of 2004, authored by former Assemblymember Hannah-Beth Jackson. It would have ensured that consumers who enter into agreements with franchised auto dealers, to waive rights or procedures under state laws, do so voluntarily. It would also have deemed any agreement to waive rights under state law that was not knowing and voluntary to be unconscionable, against public policy, and unenforceable.

Opponents argued that AB 2656 was preempted by the FAA. While the author and proponents disagreed, it ultimately failed to pass. The defeat of AB 2656 makes it all the more important for Congress to assert its leadership on this issue. Taking at face value the opponents' argument that states' hands are tied, they themselves make the case that it is entirely up to Congress to act.

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[12] Statements on Introduced Bills and Joint Resolutions, United States Senate, June 29, 2001. Statement by Senator Grassley of Iowa.

Enactment of HR 5312 will benefit consumers, honest business, and the nation

Passage of HR 5312 will go a long way toward curbing a whole host of shady practices that harm not only the individuals who purchase the vehicles; but also their families; their employers; honest auto dealers that are at a competitive disadvantage; other businesses that suffer collateral damage due to auto frauds, which drain dollars that could be spent on other legitimate products and services; and the entire nation.

Case study: Odometer fraud flourishes under mandatory arbitration clauses

Most people mistakenly believe that odometer fraud is a rare occurrence. However, in reality, odometer fraud is rampant. It is now one the leading property crimes in the nation. Unscrupulous auto dealers traffic in vehicles with rolled back odometers, either altering the odometers themselves or purchasing them from criminals who simply reprogram the odometers, a crime that is difficult to trace.

Consumers who purchase vehicles with altered odometers face severe losses. The difference in value between what they pay and the vehicle's true worth is usually thousands of dollars. In addition, they face unanticipated expenses which can mount up and add thousands of extra charges, such as engine and/or transmission replacements. They may also experience safety issues when brakes and other safety-related parts fail sooner than expected. To make matters worse, any warranty or service contract they purchase may be void, due to the altered odometer. This is a triple whammy for victims of odometer fraud.

The Federal odometer law, 49 U.S.C. Chapter 327 (Public Law 103-272), prohibits the disconnection, resetting, or alteration of a motor vehicle's odometer with intent to change the number of miles indicated thereon. But having a law on the books and having it actually enforced are two different things.

According to the National Highway Traffic Safety Administration's Office Of Odometer Fraud Investigation, "Odometer tampering continues to be a serious crime and consumer fraud issue. In 2002, NHTSA determined this crime allows more than 450,000 vehicles to be sold each year with false odometer readings, milking American car buyers out of more than $1 billion annually… The increased cost consumers pay to purchase passenger vehicles with odometer rollback of $1,056,000,000 per year makes odometer fraud one of the top crimes against property in the United States"[13]

The agency currently estimates that odometer fraud costs each victim approximately $4,000. That figure does not count the costs of unanticipated major repairs; job loss due to faulty vehicles that break down and become inoperable and/or

[13] National Highway Traffic Safety Administration Report Number DOT HS 809 441, April, 2002.

unsafe to drive; or losses incurred when roll-back vehicles are traded in, the true mileage is discovered, and the buyer owes far more than the car is worth.

More recently, NHTSA found that the problem has become even worse. "From 2002 to 2005, we have seen a definite escalation of odometer fraud. New car prices, coupled with the increased demand for late-model, low-mileage used cars, has made odometer fraud more profitable than ever."

On its website, NHTSA states that "Violations of any of the [Federal odometer law] may subject the violator to civil liability if it is determined that his/her actions were intended to defraud the purchaser. The law makes available to the buyer a remedy in the amount of $1,500 or treble damages, whichever is greater, together with attorney's fees. To obtain this remedy, Section 32710 of the law permits the buyer to bring a private civil action in State or Federal court. He may do this by contacting his own attorney or the State Attorney General. The Federal Government has the authority to bring actions for civil and criminal penalties; however, it cannot bring actions on behalf of consumers. We strongly recommend that you consult your own private attorney to determine your legal rights and remedies in this matter."

NHTSA reports that is has a total of 5 criminal investigators and 4 support staff who handle odometer fraud cases for the entire nation. That translates into less than one NHTSA field investigator per 11.5 million vehicle sales, each year. While some states have officers who work with NHTSA on occasion to curb odometer fraud, usually on a part-time basis, they lack the resources to focus on any but the largest odometer fraud rings. NHTSA found that only 4 states have taken even the most basic steps to track odometer fraud and that fewer than 10 states routinely reported suspected odometer fraud to the federal authorities. [14]

Given the sheer volume of transactions and the seriousness of the crime, Congress saw fit to provide for strong sanctions to encourage victims of odometer fraud to pursue their rights, to police the marketplace on behalf of the motoring public and to help foster confidence in car purchasing from licensed dealers. Accordingly, our nation depends almost entirely upon the civil justice system to curb this illegal practice, which is a particularly pernicious form of theft. However, due to the imposition of binding mandatory arbitration, odometer fraud can easily flourish, leaving hapless victims with little or no recourse.

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[14] National Highway Traffic Safety Administration Report Number DOT HS 809 441, "Preliminary Report: The Incidence Rate of Odometer Fraud," April, 2002. Note: these figures do not reflect other costs inflicted on victims of odometer fraud, including: costs of repairs, diminished value upon resale, lost work due to vehicle failures, and related costs. It also fails to include vehicles with altered odometers that did not appear in the Carfax database, which NHTSA acknowledges is far from complete.

All an unscrupulous dealer needs to do, in order to get away with the crime, is to insert an arbitration clause in the contract. Suddenly, the consumer no longer has access to the remedies intended by Congress. Instead of being able to seek damages, including penalties and attorneys fees, victims may be eligible to receive only a refund. Their fate is in the hands of an inherently biased arbitrator who depends on the auto dealer for repeat business. The process is not open and the decision is only rarely subject to review. Thus, the deterrent effect of the Odometer Act is defeated by the arbitration clause.

Also, because of limited discovery, and the secrecy inherent in arbitration, someone who is a victim of odometer fraud may never find out they are one of 100 who were similarly cheated. This means that even if individual consumers prevail in arbitration, dealers who deliberately engage in a pattern and practice of committing odometer fraud may never be brought to justice for their crimes, even if they are serial fraudsters.

In addition, the secrecy inherent in the arbitration means that ultimately the free market cannot work to reward legitimate businesses and give them a competitive advantage. Instead, it allows crooked enterprises to flourish, shielded from public scrutiny, giving them an unfair competitive advantage.

New and growing problem: dealers going out of business, fail to pay off liens

As the auto market softens and auto manufacturers consolidate dealerships, more auto dealers are going out of business, leaving their customers holding the bag. One of the worst scams: increasing numbers of dealers are taking consumers' vehicles in trade, with a promise they will pay off the liens. Then they fail to follow through on that obligation. This has reached epidemic proportions, and involves some long-established franchised auto dealerships. Consumers have been saddled with millions of dollars in unpaid liens and other losses, forcing some consumers into bankruptcy.

In response, California enacted SB 729, authored by Senator Alex Padilla, to establish a restitution fund to provide relief to victims of auto dealers who go out of business. The new law will assess a fee that is paid by each dealer, based on the number of vehicles sold, to provide assets for the restitution fund.[15] However, the California fund is unique and other states have failed to act.

Conclusion

[15] For examples of losses inflicted on consumers by dealers that went out of business, see California Senate Judiciary Committee analysis for SB 729 (Padilla), at: http://info.sen.ca.gov/pub/07-08/bill/sen/sb_0701-0750/sb_729_cfa_20070425_141418_sen_comm.html

We strongly urge adoption of H.R. 5312. This measure is urgently needed to allow car buyers to enforce important rights under existing federal and state laws. Passage of H.R. 5312 will achieve important public policy goals, help protect the public from some of the worst property crimes, increase healthy competition, and improve auto safety.

Thank you again for the opportunity to testify in support of this important consumer protection measure.

Ms. SÁNCHEZ. Thank you. Again, we appreciate your testimony.

At this time I would invite Ms. Rice to please share her testimony.

TESTIMONY OF ERIKA RICE, ARCANUM, OH

Ms. RICE. Good morning. I would like to get started by thanking Chairwoman Sánchez, Ranking Member Cannon, and the rest of the Members of the Subcommittee for hearing my testimony today. I am hoping that when this bill becomes a law, other families will be protected from what has happened to us.

My name is Erika Rice, and I am a mother of two from Arcanum, Ohio. My husband and I were taken advantage of by a car dealership that used a clause that was buried in some fine print. I later learned that this clause could take away my right to hold the dealership responsible for their actions.

In November of 2006, my husband, daughter, and I went to a car dealership with the intention of buying a safe car that would last us for a number of years. After being there for almost 4 hours, the dealer finally sat us down and in just a few minutes, hurried us through a mountain of documents. Because it was 45 minutes past the closing time of the dealership, I was not given the chance to read the unending lines of fine print; instead, the dealer just pointed and said, "Sign here, sign here," not answering any of my questions.

The dealer assured me that the car had undergone quality assurance inspections, and I was led to believe that the car had never been in an accident or been damaged. I learned later that in fact, the car had been in a crash where the airbags had deployed and the car was seriously damaged. In short, they had sold me a rebuilt wreck.

During the whole process of buying the car, the word "arbitration" was never mentioned. I didn't even know what the word meant until I was forced to file a claim against the dealership due to their lack of responsiveness. The dealer never explained the term or explained that by signing certain documents I might be giving up my right to hold them accountable for what I later learned was a complete scam.

That night as I was driving home it began to rain, and my windshield wipers in my new car quit working. Here I was, driving with my 6-year-old, on the interstate in a rainstorm, and the windshield wipers quit working. Needless to say, I wasn't happy with the car.

The next morning I drove the car back to the dealer. On the way there, the "check engine" light came on. When I got to the dealer I informed them that I wanted another car because of the obvious problems with the car they had just sold me hours before.

They told me they couldn't help me; my pleas fell on deaf ears. I told them that I still wanted to buy a car and I would be willing to buy that car from them, only I didn't want a car that had problems within minutes of driving it.

After a few weeks had passed, the car had spent more time in the shop being fixed than being driven by myself or my husband. I was getting nowhere with the dealer, and so I told them that I was looking into hiring an attorney, thinking that if perhaps they

knew how serious I was about the situation they would actually try to rectify it.

Instead, the people at the dealership literally laughed at me. They said, "Bring it on." What they knew, that I didn't at the time, is that I might be unable to hold them accountable by the fine print: the binding mandatory arbitration clause.

The worst part about my case is that the box that said I would be bound under my contract for arbitration was never even checked. This alone should allow me to pursue my claim in court. Let me clarify: My purchase agreement for the car has a provision in it which states, "Buyer acknowledges that if this box is checked, this agreement contains an arbitration clause." Right next to that statement is a checkmark box, but the box is not checked on my contract.

So even though the box is not checked, the dealer's lawyers have filed a motion to force me to go to arbitration with the AAA. This motion has been pending for over a year.

You may be asking yourself, "Why don't I just submit to the arbitration and try to get a good settlement that will allow me to buy a car that works?" First of all, I know there is not much of a chance that I will win in arbitration. I have learned about the thousands of other car buyers who have paid thousands of dollars in arbitration fees believing that the arbitrator would be fair, only to find out otherwise.

Secondly, I can't even afford the cost of going through with the arbitration process. In order to just start that process, I would have to pay half or more of all the cost of arbitration. I have learned that arbitrator's fees usually range from at least $700 to $1,800 per day with an average of $1,300. In addition to the arbitration fees, I would also have to pay half of the administrative fees. I know that the cards are totally stacked against me.

What upsets me the most is that all of this could have been prevented. If the dealers were not allowed to use mandatory arbitration clauses in their contracts, perhaps they would have treated me right from the start. I would never have been forced to get a lawyer and spend all my time and money just to get a judge to hear my concerns. It has been a very stressful situation.

I went to a dealership excited to get a new car. Instead, I was scammed and lied to. If the dealer was never allowed the opportunity to try and force me into an unfair, secret, and expensive arbitration system, all of this could be avoided.

Thank you for hearing my testimony.

[The prepared statement of Ms. Rice follows:]

PREPARED STATEMENT OF ERIKA RICE

United States House of Representatives
Committee on the Judiciary
Subcommittee on Commercial and Administrative Law

Honorable Linda Sanchez, Chairperson

March 6, 2008

Testimony
Presented by

Erika Rice
Automobile Consumer

In Support of Passage of H.R. 5312 The Automobile Arbitration Fairness Act

Good Morning.

I would like to get started by thanking Chairwoman Sanchez, Ranking Member Cannon, and the other members of this subcommittee for giving me the opportunity to appear before you today to share my story. I also would like to thank Congresswoman Sanchez for introducing The Automobile Arbitration Fairness Act. Hopefully this bill will become a law, and other families will be protected from having to go through what my family has been through.

My name is Erika Rice and I am a mother of two from Arcanum, Ohio. My husband is also here with me today. We were taken advantage of by a car dealership that used a clause buried in the fine print. I later learned that this clause could take away my right to hold the car dealership responsible for their actions.

In November of 2006, my husband, my oldest daughter, and I went to a car dealership with the intention of buying a safe car that would last our family for a number of years. We got there at 6:00 in the evening and despite knowing we wanted to buy a car, we weren't allowed to sit down to sign any paper work until 9:45, forty-five minutes after the dealership was to have closed.

In just a few minutes, the dealer hurried us through a blizzard of documents. I had no time or chance to read over the seemingly unending lines of fine print – instead, the dealer just pointed where to "sign here," or "initial here."

The dealer assured me that the car had undergone quality assurance inspections and I was led to believe that the car had never been in an accident or been damaged. I learned later that in fact, the car had been in a crash where the air bags deployed and the car was seriously damaged. In short, they had sold me a rebuilt wreck.

During the whole process of buying the car, the word "arbitration" was never mentioned. I didn't even know what the word meant until I was forced to file a claim against the dealership due to their total lack of responsiveness. The dealer never explained the term or explained that by signing certain documents, I could be giving up my right to hold them accountable for what I later learned was a complete scam.

That night, as I was driving my newly purchased car home, it began to rain. I went to flip on the windshield wipers, but they didn't work. Here I was driving my six-year old daughter in a car with just 50,000 miles on it, through a rain storm on the interstate, with no windshield wipers.

Needless to say, I wasn't happy with the car the dealer sold me. The next morning I drove the car back to the dealer. On the way there, the "Check Engine" light flickered on. So, when I arrived at the dealer, I informed them that I had changed my mind and that I wanted to buy a new car from them, because of the obvious problems with the used car they had sold me just the previous night.

They told me they couldn't help me. My pleas fell on deaf ears. I told them that I still wanted to buy a car and I still wanted to buy a car from them, but that I didn't want a car that had these problems with it only moments after I started driving it. Instead, they pushed me back and forth between different people at the dealership and gave me different explanations about the car and how they could "help" me.

After a few weeks had passed, the car had spent more time in the shop being "fixed" than being driven by myself or my husband. I was getting nowhere with the dealer, so I told them that I was looking into hiring an attorney, thinking that perhaps if they knew I was very serious about solving this problem, they would actually try to rectify the situation.

Instead, the people at the dealership literally laughed at me, and told me to "bring it on." What they knew, and I didn't at that time, is that I might be unable to hold them accountable by the fine print – the binding mandatory arbitration clause.

The worst part about my case is that I didn't even check the box that said I would be bound, under my contract, to arbitration. This fact alone should allow me to pursue my claims in court.

Let me clarify: my purchase agreement for the car has a provision in it which states, "Buyer acknowledges that if this box is checked, this agreement contains an arbitration clause." Right next to that statement is a check-mark box, but the box is not checked on my contract. So even though the box is not checked, the dealer's lawyers have filed a motion to force me to go to arbitration. This motion is currently pending.

But even if I am one of the few lucky car buyers to somehow stay out of arbitration, the cost to fight the arbitration clause is very high, a cost my family cannot easily afford. And it's taken over a year so far.

You may be asking yourselves, why don't I just submit to arbitration and try to get a good settlement that will allow me to buy a car that works?

First of all, I know there is not much of a chance I will win in arbitration. I have learned about the thousands of other car buyers who paid thousands of dollars in arbitration fees believing that the Arbitrator would be fair, only to find out otherwise.

Secondly, I can't even afford the cost of going through with the arbitration process the dealer is demanding. In order to just start the process of arbitration, I would have to pay half or more of all the costs of arbitration.

I have been told that arbitrators' fees usually range from at least $700 - $1800 per day, with an average of $1300. In addition to the arbitration fees, I would also have to pay half of the administrative fees. But, these rules are so unclear on this cost that not even my lawyer can figure out which fees would actually apply to me and exactly how much I would have to pay.

I know that the cards are totally stacked against me in the arbitration process that the dealers want me to go through.

What upsets me the most is that all of this could have been prevented. If the dealers were not allowed use binding mandatory arbitration clauses in their contracts with people like me, perhaps they would have treated me right from the start. I would never have been forced to get a lawyer and spend all of this time and money just trying to get a judge to hear to my concerns.

If we lose and are forced to go to arbitration, our credit could be ruined (my credit is actually currently suffering due to the fact that I had to buy another car, so it looks like I have two car loans (bad for debt to income ratio) and the fact that the bank reports negative information even though, due to the lawsuit, they had agreed not to), the bank could repossess the car, and I fear that all this will only be the beginning of our nightmare.

I went to a dealership excited to get a new car and instead, I was scammed and lied to. If the dealer was never allowed the opportunity to try and force me into an unfair, secret, and expensive arbitration system, all of this could have been avoided.

I never wanted to be involved in a lawsuit; all I wanted was to buy a car that was safe and that worked the way it was supposed to work.

How can it be possible for dealers to do things like this to people every day and be protected by this arbitration system? If no one is going to hold these dealerships accountable, why would they ever change the deceitful way they do business? Congress must act to protect other families like me, who simply want the right to be treated fairly by car dealerships.

Thank you again, Madam Chair and other members of the committee, for giving me a chance to tell you my story. I hope my situation will help you to understand that this is not just some meaningless change in a contract, but a change that will have a profound impact on future car buyers across the country and will prevent them from ending up in a situation like ours.

Thank you.

Ms. SÁNCHEZ. We are sorry for the trouble that you obviously encountered in your experience, but we appreciate very much the fact that you took the time to attend today. At this time I would like Mr. Naimark to speak.

TESTIMONY OF RICHARD NAIMARK, SENIOR VICE PRESIDENT, AMERICAN ARBITRATION ASSOCIATION, WASHINGTON, DC

Mr. NAIMARK. Good morning, Madam Chair, Congressman Cannon, all the Members of the Committee. I am Richard Naimark; I am senior vice president of American Arbitration Association, and we appreciate the opportunity to testify before the Subcommittee today.

May I say at the outset that the AAA is a not-for-profit public service organization with over 80 years of experience in the field. Arbitrators who hear cases that are administered by the AAA are not employees of the AAA, but are independent, neutral, screened, and trained, and in the consumer context are virtually always attorneys.

The AAA does not represent an industry, per se. It does not represent the ADR or arbitration industry or other arbitral institutions. And our primary concern today, and reason for attending, is concern about the health and integrity of the arbitration process in particular.

I will note that there is a marked irony in the hearing today and in the bill that is being proposed, as already has been noted in some of the submitted testimony: The automobile dealers themselves were successful in securing a provision and law that allows them to circumvent the arbitration provisions in their contracts with automobile manufacturers, and now we have sort of the other end of the spectrum, which I think is a rather ironic situation. Nonetheless, let me say that we have two primary suggestions that we would like to propose to the Subcommittee—to the Committee—changes to H.R. 5312 that would preserve the objectives but would not have extensive potential unintended impacts that might be undesirable.

And the first thing I want to say is that this is largely, in many respects, as has already been said, an issue of access to justice. The reality is that for most Americans, consumers don't have ready access to justice. Studies have shown difficulty for consumers, individuals, for claims typically less than $65,000, in obtaining legal representation, unless they can finance the lawsuits themselves; and for pro se, self-representation in court is often extremely difficult to manage. The court process was not designed for easy access.

So I want to say, in that context, that arbitration can provide a fair, balanced dispute resolution in the consumer context if it incorporates principles like due process protocols, which require some fair play in the process.

Very briefly, some highlights of the due process protocols which are part of the AAA process in the consumer setting. They provide for things like:, consumers and businesses have a right to independent, impartial neutrals to decide their disputes; consumers always have a right to representation; costs of the process must be reasonable; the location of the proceeding must be reasonably ac-

cessible; no party may have a unilateral choice of arbitrator; there should be full disclosure by arbitrators of any potential conflict or previous contact with any of the parties; and perhaps most importantly of all, there should be no limitation of remedy that would otherwise be available in court.

And in this way, you preserve safeguards. There are other aspects, certainly, of the protocols.

Now, the other thing I want to stress is that it would be a mistake to amend the Federal Arbitration Act. The so-called Dealers' Day in Court did not amend the FAA; it was a piece of, sort of, collateral legislation. The reason we talk about that is, the arbitration world context is extremely large. There are all kinds of business-to-business arbitrations, there are international arbitrations, there are some arbitrations involving governmental bodies, there are lots of arbitrations involving unions and management.

The alterations of the FAA potentially impact over 80 years of judicial wisdom, which have built up the contours and the confines of how arbitration ought to be properly conducted. So rather than doing something like that, we would suggest not amending the FAA, but thinking about sort of a collateral piece of legislation.

Thank you.

[The prepared statement of Mr. Naimark follows:]

PREPARED STATEMENT OF RICHARD NAIMARK

Statement on H.R. 5312 by the American Arbitration Association
Submitted to the
Subcommittee on Commercial and Administrative Law
Committee on the Judiciary
United States House of Representatives

Thursday, March 6, 2008

Good afternoon, Madam Chair, Congressman Cannon and Members of the Subcommittee. I am Richard Naimark, Senior Vice President of The American Arbitration Association. We appreciate the opportunity to testify before the Subcommittee today on H.R. 5312, the "Automobile Arbitration Fairness Act of 2008."

AAA is a not-for-profit public service organization with over 80 years of experience in the administration of justice. Arbitrators who hear cases that are administered by the AAA are not employees of AAA, but are independent neutrals screened and trained. AAA does not represent the ADR industry or other arbitral institutions.

As the world's largest provider of alternative dispute resolution ("ADR") services, including arbitration, the AAA has pioneered the development of arbitration rules, protocols and codes of ethics, which may be helpful to the Subcommittee as it works to address issues relating to the use of arbitration in motor vehicle purchase and lease contracts.

As has already been noted, automobile dealers in 2002 were successful in securing a provision in law that allowed them circumvent arbitration clauses in their contracts with automobile manufacturers. We held at the time that this is an ill-advised approach to addressing this and other issues in business-to-business contractual arrangements. Of particular concern were bills that would have amended the Federal Arbitration Act, the cornerstone of arbitration and the rich body of judicial decisions that have evolved since 1923. Fortunately, the provision that ultimately passed did not amend the Federal Arbitration Act.

We suggest some changes to H.R. 5312 that would preserve its objectives, but in a manner that would not have extensive potential unintended impacts on the broader world of business-to-business and international arbitration.

First, we recommend incorporating into the legislation a series of concrete due process and procedural requirements to ensure fairness in arbitration contracts imposed on consumers. These provisions should parallel the protections and standards articulated in the *Due Process Protocol for Mediation and Arbitration of Consumer Disputes*, developed a decade ago by the National Consumer Disputes Advisory Committee. This is, of course, a more complex undertaking than simply prohibiting pre-dispute arbitration, and we stand ready to assist in the development of appropriate language.

Second, any legislation to address consumer arbitration issues should not amend the Federal Arbitration Act, but rather a more pertinent section of the U.S. Code. Since initial passage in 1923, the Federal Arbitration Act has formed the basis of the vast majority of business-to-business, international, and other types of arbitration. What is more, the shaping of the Act has been consistent with international standards of practice in arbitration, making the U.S. a jurisdiction successfully aligned with this predominant cross border system of justice. Just as the 2002 automobile dealer legislation amended the Dealer Day In Court Act, and has been effective, so too can this bill achieve its objectives without amending the Federal Arbitration Act. In fact, appending consumer protections to the 2002 amendments to the Dealer Day in Court Act might be seen as particularly apropos.

The Consumer Due Process Protocols

Recognizing that the use of arbitration in consumer agreements presented some unique issues, nearly a decade ago a group of representatives of consumer, academic, government, and industry groups was convened to examine these issues. This National Consumer Disputes Advisory Committee ultimately issued the *Due Process Protocol for Mediation and Arbitration of Consumer Disputes*. The AAA and a few other organizations have implemented this Protocol, but others have not. Courts have repeatedly referred to the Protocols as a standard of fair play in this context.

Key Elements of the Consumer Due Process Protocol:

- Consumers and businesses have a right to an independent and impartial neutral and independent administration of their dispute.
- Consumers and employees always have a right to representation
- Costs of the process must be reasonable.
- Location of the proceeding must be reasonably accessible.
- No party may have unilateral choice of arbitrator.
- There shall be full disclosure by arbitrators of any potential conflict or appearance of conflict or previous contact between the arbitrator and the parties. The arbitrator shall have no personal or financial interest in the matter.
- There shall be no limitation of remedy that would otherwise be available.
- Small claims may opt out where there is small claims court jurisdiction
- Parties to the dispute must have access to information critical to resolution of the dispute.
- The use of mediation to foster voluntary resolution of the matter.
- Clear and adequate notice of the arbitration provision and its consequences, including a statement of its mandatory or optional character.

Ms. SÁNCHEZ. Thank you, Mr. Naimark.

At this time I would like to invite Mr. Rosner to provide his testimony.

TESTIMONY OF HALLEN D. ROSNER, ROSNER & MANSFIELD, LLP, SAN DIEGO, CA

Mr. ROSNER. I agree with Mr. Conner, what we need to do today is focus on the car dealer context.

And Mr. Smith, while you are leaving, I did want you to see, I brought a car contract here today. I kept one thing just to flash you with as you leave. This is the standard retail installment sales contract that a consumer gets.

This is what they see after they have been at the dealership for 3 or 4 hours and been shown paperwork that would take hours to read; there have been various studies done. This is what comes at the end. They have already signed 10 times that they are going to buy. Then they get the retail installment sales contract.

In this contract is one single line on the front page that mentions arbitration. I have two for you; I would like to submit them at the end of my testimony. If you want to play "look for the needle in the haystack," try and find the one line on the front of a contract that mentions arbitration.

It actually beautifully blends in, and I will give you a clue: The one line that mentions arbitration is where they have the consumer, after spending 4 hours, after being told, "Here is where you sign," and they finally just want to be out of there, the one line is the line where they promise that they thoroughly read the front and back of the contract, which, of course, they wouldn't know that they are acknowledging that because no one reads the front and back of the contract.

I brought two agreements for a reason. One is a 2006; one is a 2004. The front side has 2,000 words, there are over 100 clauses—there you will find the arbitration clauses. The reason I brought two is that the 2004 version had a group called JAMS, that is Judicial Arbitration Mediation Services—highly respected ex-judges. They instituted rules such as proposed by AAA.

The result was, they were disqualified and taken out of the contracts as a provider because the put in rules of fairness. I was unfortunately having to explain that AAA is right now rumored, because they put in some better consumer protections recently, that they are going to be taken out of the dealer contracts. The only improvement they want is the National Arbitration Forum, and in my testimony and others there has been quite a lot of documentation about the nature of that organization.

So if you did read the back of the contract, and I did a whole section in my written statement here about how people buy cars. This is something you end up doing after many, many hours. It is the last thing you sign. They have already had you sign that you are going to buy it.

You wouldn't know what you are agreeing to because this tells you to go to a Web site to learn the rules of the organizations that are involved in what you are doing. So if you happen to have your laptop and you go to the Web site, you can then pull up United

States Code and read the other 100 pages of regulations governing the agreement that you are entering into.

What we propose here, and this is—arbitration should be knowing and voluntary. It is never, never knowing and voluntary in the car context because the people, first, don't know it exists; that is the reality. The second, if you knew it existed you wouldn't know the rules because it is not in the agreement.

There was a comment here about the importance of access to justice. The reality is, arbitration is right now precluding access to justice. There is no problem getting representation if you are a consumer of a $10,000 car if your case has merit. Anyone in my state can get me to represent them if their case has merit because we have consumer laws that, if the consumer's car should be brought back, the dealership has to pay their fees.

But what I get on my column, from across the country, is people can't get lawyers. They won't take arbitration cases with arbitration clauses. The same lawyer who will represent you in court, not charge you one penny up front, won't take the arbitration because among the clauses here is a clause that takes away, potentially, that right to get paid to represent the consumer. These rules aren't fair.

And I guess I ask you to consider this fact: Would the same car dealer who sells you a wrecked car, who took advantage of this young lady here, hesitate to maybe tilt the field a little bit in a document like this, in writing the rules and regulations? They get to pick the organization you have to go to. We run into the repeat-player bias and other difficulties.

I noted in the written statement submitted by the gentleman from AAA, he says, "No party should have a unilateral choice of arbitrator." I would like to amend to that, "Or group or arbitration system." Of course, everyone spreads butter different. When you have groups that send out mass solicitations, like the National Arbitration Forum, saying, "Choose us and we will make your bottom line better. We will take care of you," and that is what they do, then tell you how to write in clauses, that is not where you as a consumer want to have your dispute heard.

The problem is access to justice. And the other biggest problem is the inability to do discovery and stop it. It promotes widespread fraud because it is all done in secrecy, versus, I detailed how one lady changed the law for millions by doing it in a court proceeding because it became public, it became a record, it because a law.

Arbitration is secret. It promotes continued fraud and predatory practices against consumers, and I think that is one of the major problems we have.

[The prepared statement of Mr. Rosner follows:]

PREPARED STATEMENT OF HALLEN D. ROSNER

United States House of Representatives
Committee on the Judiciary
Subcommittee on Commercial and Administrative Law

Honorable Linda Sanchez, Chairperson

March 6, 2008

Testimony
Presented by

Hallen D. Rosner
Partner, Rosner & Mansfield LLP
Also on Behalf of National Association of Consumer Advocates[1]

In Support of Passage of H.R. 5312 The Automobile Arbitration Fairness Act

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[1] The National Association of Consumer Advocates (NACA) is a non-profit corporation whose members are private and public sector attorneys, legal services attorneys, law professors, and law students, whose primary focus involves the protection and representation of consumers. NACA's mission is to promote justice for all consumers.

Hallen ("Hal") Rosner is one of the leading experts in the country on Auto Finance Fraud, and other areas involving the purchase of vehicles. He teaches military legal aid, public legal aid, volunteer attorneys, and others how to understand vehicle contracts and recognize the most common auto frauds. He regularly consults with the Legal Aid office at Camp Pendleton Marine Base. On February 1, 2008 he taught on these subjects to Marine attorneys from West of the Mississippi. Mr. Rosner's firm represents servicemen and women who have been cheated, regardless of the economics. Mr. Rosner's vehicle case involved his own vehicle in 1982. He started his practice with Professor Robert Fellmeth, one of the two original Naders Raiders and opened his own practice in 1985. Over the past 23 years, the firm now named Rosner and Mansfield, LLP's Auto Fraud Legal Center has represented thousands of consumers. Mr. Rosner was both trial counsel and appellate counsel in the case that changed vehicle sales across the country, *Thompson v. 10,000 RV*. In 2007, his firm was awarded the Public Service Award by the San Diego Bar Association, recognizing over two decades of helping consumers. He also writes "Ask Hal", an internet auto fraud advisory column that gets over 10,000 hits a month from across the country.

OPENING STATEMENT

Chairperson Sanchez and Members of the Committee, I am proud to be here to testify today in support of enacting HR 5312. Almost everything written in support of arbitration is completely untrue in the context of modern day vehicle purchase contracts with arbitration clauses usually found on the back of these lengthy contracts. These clauses are carefully written, to put it blunty, to cheat and victimize consumers while protecting Car Dealers. Such arbitration is not "voluntary" and is not "fair" or meant to be so. Arbitration promotes continued fraudulent/illegal activities by Car Dealers and eliminates the widespread stopping of these activities as has and can be achieved in

Court actions.

I. INTRODUCTION

Car dealer arbitration clauses are a fairly recent phenomenon. Only after car dealers learned how affective arbitration clauses could be at denying people their rights did they on a massive national level begin to insert them onto the backs of their Retail Installment Sale Contracts (RISCs)[2].

Today, arbitration clauses in vehicle contracts are standard, utilizing the most effective language aimed at limiting consumers rights and requiring arbitration only before the most dealer-influenced organizations. All while discouraging any action at all by making the process expensive, anti-consumer and difficult for consumers to obtain an attorney.

In California, the initial dealer arbitration clauses included one of the country's most respected arbitration providers, JAMS, an organization composed of former judges. In response, JAMS created consumer arbitration rules that attempted to create a fairer playing field for consumers. This led to the state's auto dealers acting in concert to eliminate the option of JAMS from all arbitration clauses. There is even talk that the AAA (American Arbitration Association) may be excluded and that future clauses will only list the thoroughly discredited National Arbitration Forum (NAF).

Sadly, even changing arbitration panel selection clauses will not change the essential fact that all industry-wide arbitration is inherently flawed and subject to business leanings and manipulation. Even JAMS changed its rules enacted to "ensure fairness" when leaned on by large business clients[3].

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[2] The irony of the Car Dealers getting an exemption for themselves as to their franchise agreements with manufacturers based on arguments that such clauses were not voluntary or fair, and then turning around and adding them to their contracts with consumers, is hard to miss.

[3] After JAMS announced rules to "ensure fairness", Citibank, Discover Card and American Express wrote JAMS out of their agreements, as the Cars Dealers have. Within months, JAMS reversed their policies. Eric Berkowitz, IS Justice Served, LA Times Magazine, October 22, 2006.

Dealers can make their arbitration clauses as one-sided and abusive as they want as almost all consumers do not even know the clauses exist. Even if seen, the arbitration rules are not even in the contracts. A consumer must go to a website to learn what the rules are. Voluntary and knowing consent to arbitration is a fiction after consumers spend hours at a car dealer, sign voluminous paperwork, and are handed a 24-inch contract with small print, over a hundred clauses, and a backside requiring a law degree to decipher. The arbitration clause is located on the back of the contract and requires no initials.

The arbitrations provided for are expensive and highly risky for consumers, costing thousands of dollars with the risk of owing the dealer more than the price of the vehicle.

Illegal dealer practices cannot be stopped by arbitration which does not allow for injunctions to stop illegal practices. The secrecy and non-public nature of the arbitration process promotes continued illegal practices which remain highly profitable. An example of how a single Court action can protect millions of consumers, as well as the financial market, is provided in this testimony.

II. SUMMARY

I do a lot of teaching. For many years, I have worked with attorneys from the armed services to protect our servicemen and servicewomen from Car Dealers. These Dealers will advertise their patriotism while blatantly cheating our service personnel. I also teach and work with volunteer lawyers and legal aid attorneys.

To understand Car Dealer abuses and how to deal with them, there are a few very valuable things to learn about first. This includes: who they victimize; what is the "selling system" utilized (meaning how are the cars sold), what their basic contract is (vehicle contracts are entitled Retail Installment Sale Contracts, commonly known as RISCs), and how it is utilized in the sales process.

Once the sales process, including the contract used, is understood, the fact that consumers

do not voluntarily enter into arbitrations clauses is clear.

I will also in this testimony examine the standard arbitration clause and point out its deliberate one-sided nature and blatant unfairness.

Finally, I will address what might be the most important point. Arbitration promotes continued illegal and predatory practices, and prevents changing Car Dealer conduct.

III. CAR BUYERS

Of course with millions of vehicle sales, vehicle buyers are a varied group. For many vehicle buyers, a vehicle is a necessity like food or shelter. Without a car people cannot get to work or school, or even function in today's society. When car deals go bad, it can literally wreck someone's life. Just two weeks ago I resolved the case of Nellie Favella. She was sold a car that listed a phony downpayment she did not make and could not afford to make. After the sale, the Car Dealer then asked for the downpayment, and she tried to give the car back. Instead, they sued Ms. Favella in small claims court (as allowed in one-sided arbitration agreements on the back of contracts). The Dealer won the downpayment amount, a large penalty and started garnishing on her wages. This left her no longer able to afford shelter, leaving her and her daughter homeless. Ms. Favella is now returning the car, having it paid off, getting all her wage garnishments back, her credit repaired, and other monies. She was lucky we met her crying while she was at Court trying to reduce the garnishment.

Second, there is the case of Marine Nicholas Schwenk. His family's life was disrupted for years due to a dishonest dealer. All he wanted was a car for his family. The car he bought soon developed serious problems and the dealer told him to bring it to a specified repair shop. Mr. Schwenk told the car dealer he would be out on training for two weeks. When he returned, the car had been repossessed. All dealer arbitration clauses let the dealers use self help, which includes

repossession or even stealing cars, while denying Court access for consumers. The repair shop falsely called in the car as abandoned. The repossession company took the car and demanded $2,500.00 even though no payments were even due. They would not return the car to the young Marine. He was so badly threatened and scared he was convinced to keep paying on the damaged car they had taken from him. After years of paying and leaving his family broke, his Sergeant learned of all this and told him to stop paying. He was then later sued for all money owing on the car that had been auctioned for almost nothing. He went to Marine Legal who asked if we could help. His case, at that point over 6 years from purchase, did not have an arbitration clause. The threat of Court action, including an injunction and other remedies, allowed us to persuade them to not only drop the suit, but to give him all the years of payments back. This would be a highly unlikely result with an arbitration clause.

On my internet column, I get horror stories daily, many from outside California. It is tragic how so many consumers cannot get legal help as they are told by attorneys that they do not take dealer cases that have arbitration clauses. For these people, arbitration clauses that they never knew existed when they bought their cars, now stop them from seeking any justice and allow the predatory acts to continue.

People who learn that they have been cheated by a dealer often describe their feeling of having been discriminated against because they were young, a woman, black, a Latino, a senior citizen, etc. My experience is that dealers try to cheat everyone and would do so if you were pink with polka dots. On the other hand, it is very clear that the most vulnerable members of our society are victimized far more and at a higher rate.

I practice in a military city with a significant Latino population. These young servicemen and women are easy prey and experience a long list of Car Dealer abuses. I have spent a lot of time with

military legal aid, and car dealer abuse is a major issue they deal with. In my teaching and on my website, I detail a list of the most common auto frauds. What happens to the Latino community is truly amazing. While it is not uncommon for consumers to have been victimized by more than one practice, we have cases involving Latinos where the dealers have committed a laundry list of illegal practices.

The fact is, dealer unlawful practices are way under-reported. In the movie The Sting, Paul Newman explains to Robert Redford that in a good sting (another word for a con involving cheating someone) the mark never knows he has been had. The mark, of course, means the victim. Most people never know they were cheated. Very few of our auto fraud clients initially call about being cheated. They call because their vehicle is not working right. We then check the history and may find the car was a wreck, a rental, flood damaged, a prior lemon or has other negative history. We later look at the paperwork and may find illegal charges, "packing" where consumers were charged for things they did not want, along with a wide variety of other illegal practices. I once talked to a lawyers group and had them bring their car contracts. They were surprised when I showed them how they had been taken. Even the lawyers did not read the backs of their contracts.

The fact that consumers do not enter into arbitration on a voluntary basis is clear upon understanding how cars are sold and the contracts utilized.

IV. THE SELLING OF A VEHICLE[4]

I most recently presented these materials before the Marine attorneys of the Western States on February 1, 2008. A copy of my brief outline on car dealer fraud is included as attachment A to

[4] I fully acknowledge the fine work of Ronal Burdge, Esq. of Dayton, Ohio. He is one of the Country's true consumer champions. My teaching and writing on this subject freely uses his teaching and materials. Over the years I have updated his materials based on my experiences and client communications – all with his knowledge and blessing.

this testimony. I find that very few people really understand how vehicles are sold.

Dealers use a very sophisticated selling system developed at great expense. I noted for my Marine attorneys the similarity to Military combat tactics. The fact is, the average consumer has as much chance against these systems as weekend athletes would in combat with Marines.

Understanding these selling systems is key to understanding why the arbitration clauses put onto the back of the Retail Installment Sales Contracts are not voluntarily entered into and why, even if one did read the entire 24-inch contract front and back, it would still be impossible to know how blatantly unfair these clauses are. Few, if any, consumers know the clauses exist until after they seek legal help for being cheated.

The typical sales process is a multi-hour affair. Only after price and payments are agreed to, and the consumer has committed to buying the car, often signing "I agree I will buy for this price today" do they then get taken to the finance office. This is where modern dealers really go to work and make their profits and commit a variety of frauds. This is the area of the law where my firm has succeeded in changing at least some dealer practices nationally because of the Court system; changes that cannot happen with arbitration.

The customer arrives in the finance department, usually tired and exhausted and, yes, excited. They think the deal is done. Here they do what is called "smoking the paperwork". Various estimates have been made as to how many hours it would take to read all the paperwork. As explained below, form after form is signed, each form making the customer feel more committed. After all, they have already signed to buy the vehicle. Their trade-in vehicle is long gone, and after all these hours, it is just paperwork.

Finally, after all the hours spent often involving lots of sitting around (as dragging out the sales process is part of the selling system) and after all the paperwork has been signed, comes the

RISC. A 24-inch front and back form with lots of small print. The dealer usually just says sign and people are happy to sign and be done. Some dealers may point out price or payments. Usually it is sign here, here, and here. In the customers mind, this is already a done deal referring back to when they agreed to buy with the salesman. While the contract states it includes all terms, this is false regarding arbitration. Later in this testimony I will examine the arbitration clause, which include tens of pages of terms only found on websites, or in federal code books.

No one reads the back, and if it is read it is done so incompletely. Everything about how car sales are done creates a situation where the final signing is a quick and final event. The dealers do not talk about arbitration and nowhere does the consumer even initial the arbitration clause. Only one small mention of arbitration is found on the front in a place designed to blend in and be unnoticed.

A shortened version of how cars are sold is provided:

Step 1: Sales Meetings at Dealership

Before the customer ever steps foot on the lot, the dealership management has been conducting their periodic sales meeting. Designed to "push" the sales staff to sell, topics include targeting of specific vehicles that are "stale". Leading sales persons are recognized in front of the group and "slow" sales are also pointed out, chastised and motivated to sell harder.

Step 2: Meet and Greet the Customer

The sales routine usually starts out the same way: greet the customer. The sales person cannot sell until he greets the customer, preferably in a warm and friendly way. A warm handshake, and establishing eye contact, is the first step to getting a customer's trust. The second is to begin looking for that "common ground" between the sales person and the customer. Something they have in common, like children, grandchildren, sports, hobbies, membership in social organizations (the

VFW Post, Masonic Lodge, etc.), or anything else – without being obvious about it. That's why in many sales personnel offices you will find a picture of the family on the desk or an award or plaque on the wall. A lapel pin or Lodge ring, etc., can establish a connection without ever saying a word. Dealers near military areas have lots of veterans and flags. In Latino neighborhoods, they have Latino salespersons, etc.

Step 3: The Trade In

For today's testimony, I am omitting this section, as I did with the section on dealer preparation, and post sales activities.

Step 4: Qualify the Customer

Sooner or later the cost issue comes up. To take the "sting" out of the discussion, many dealers will focus on monthly payments and avoid all price discussions. When asked what a vehicle costs, many times the answer will be another question like "what kind of monthly payment were you looking for?"

Step 5: Land the Customer on a Car

While this should be the customers choice, many dealers who specialize in the "hard to finance" tell customers which vehicle that they can buy.

Step 6: Work the Deal and the Customer (puts the customer in ether)

The sales person emphasizes all the attributes of the new(er) car and all the negative aspects of the old(er) car while working the deal. All the usual factors are in play: mileage, age, options, equipment, plus the usual personal factors that are customer-specific. The idea is to get the customer so wrapped up in the idea of getting the new car, and how much it will improve their life, be the envy of others, improve family harmony, increase their peer reputation, etc., that they lose track of the numbers in the deal. This is called putting the customer in the "ether". The deeper the ether, the

higher the gross profit on the deal. The objective at this stage is to get the customer firmly committed to the deal. That is why getting the customer to say "yes" is so important at this stage of the sales process. Part of that "yes" psychology is getting the customer to sign their name to a worksheet or other form of early commitment. Something, almost anything, has to be signed by the customer before the Turnover takes place. Committed to the deal, the customer will be less suspicious, more trusting, and easier to deceive when he/she is "t.o.'ed" to "F & I".

This also means that some sort of payment amount must be agreed to before the "Turnover". It often starts with the sales person presenting three numbers written on the worksheet. It often looks something like this:

700/-0- down 600/1k down 500/5k down

The numbers don't necessarily have anything to do with reality. What the salesperson often says when presenting the number is something like "with no down payment, your monthly payment is going to be about $700. If you put $1,000 down, I can get your payment down to $600. But if you really want to pay less each month, then I have to have $5,000 down on the financing." The psychological motive is, obviously, to "scare up" as much down payment money as possible by putting a huge monthly payment right in the customer's face.

Notice that the sales person may have said nothing at all about how long the loan will be for. The customer doesn't know if they are talking about a 3 year loan, a 4 year loan, or a 5 year loan. The absence of that information gives the F& I department more flexibility to determine what the interest rate and price will end up being, and just how much of the "soft add-on's" they can pack into the deal's numbers. Soft add-on's are high-profit items like credit life insurance, disability insurance, Gap Insurance, rust-proofing, fabric protection, paint protection, etc. The idea is that the sales person creates the room in the monthly payment for these things to be packed into the deal by

the F& I department after the Turnover.

This is called "leg". In deposition a finance manager explained how they trained and had contests as to who could generate the most "leg". If a car can be bought, for example, at $250.00 per month and you commit the customer to $300.00 per month, you have $50.00 per month "leg" over the life of a five year loan. This translates to $3,000.00 over the 60 month period. The dealership then can include lots of high profit items in the deal for "free", or just show them in the finance paperwork without ever telling the customer. This practice is called "packing".

Of course, the sales person often has no real intention of ending up with a $700 monthly payment, but they know that if they start out with a "500-400-300" set of numbers, there will be less chance of landing the customer on a higher number in the first place. By presenting the "700-600-500" numbers, the sales person has already conditioned the customer to expect that the monthly payment is going to be much higher than they thought. Having accepted that as the reality of the situation (after all, the sales person deals with these numbers every day so they must be right), the Dealer now has more room (and leverage) to actually end up with a higher number.

Once a payment number has been agreed to (usually with the customer initialing or signing the worksheet number that they go along with), the customer is ready for the Turnover. The worksheet, as mentioned, usually contains a statement like "I will buy for this amount, today."

Step 7: The Turnover

At the height of the ether, the customer is "t.o.'ed" (turned over to the Dealership Finance Manager). This person's job is to close the deal and maximize the profit in the process. If done really well, the customer will never know what a bad deal they received.

Much like passing the baton in a relay race, the smoother the Turnover is executed, the less likely it is that the customer thinks the hard part is over with and that all they have to do is sign some

papers. After all, that's what the sales person said they were going to do next. Actually, the selling process is still going on. The customer has just arrived at "part two".

The F & I manager can also be called a "Business Manager" or something similar. The reality, however, is that they are just another salesperson in the chain. Their job is two fold: first, to get all the paperwork signed; second, to sell (or pack) soft add-on's into the deal. This is where knowing the customer's background can be extremely useful. If the customer is married, credit life and disability insurance become much easier to sell ("gosh, you wouldn't want the bank to come and take your car and leave you wife/husband stranded if something suddenly happens to you, would you?" is a question that is most effective when asked right in front of the other spouse). If the customer had a trade in with "negative equity" (a phrase invented by the car sales business), it is easy to convince them that they really do need Gap insurance.

Step 8: F & I Smokes the Paperwork

Of course, some dealerships just "pack" soft add-on's into the deal without making the customer fully aware of the additional cost for these items by using the "just sign here, and here, and here" approach to the closing process, with the documents all stacked up one on top of another and the friendly Business Manager holding the stack still with one hand while turning the pages one at a time with the other hand and pointing to the signature line (often marked ahead of time with an "x"). "I'll give you a copy of all this paperwork right after I process it" is a good line to trivialize the event in the customer's mind. This kind of "five finger close", when done nonchalantly and smoothly, can generate hundreds or even thousands of extra dollars in profit for a dealership. In fact, a "successful" dealership will make more money in F & I sales than on the sale of the vehicle itself. Ward's Auto Online (http://www.wardsdealer.com/) is a great source for such information on the 500 biggest car dealers in the country.

"Smoking the paperwork" is a phrase that means the paperwork slides by the customer so fast that the friction of it sliding across the table, so to speak, makes it "smoke".

At the end of the process, the F & I person will usually tear out the customer copies of the papers, line up the corners in the stack, staple them together, fold them all up, and put them in an envelope. Then the envelope is usually given to the customer with the admonition that the papers are important and they should put them in a safe place and keep them. Of course, doing all of that discourages the customer from looking closely at the papers on the way home. Putting them into a safe place at home also discourages the customer from looking too closely at the papers, or for too long, at home. This way, the customer is less likely to discover anything that is not quite what they expected until weeks or months later.

The last thing a customer ever suspects when buying a car is that they have given up their constitutional right to a jury trial, and agreed to an unfair expense and biased arbitration system. Car contracts are so long they cannot be attached as is and take pages to copy (see exhibit B). The full 24-inch version will be brought to the hearing.

V. THE ARBITRATION CLAUSE

Usually there is a one sentence mention of arbitration on the front of RISCs which contain front and back over 100 disclosures, and 2,000 words just on the front side. The single arbitration sentence appears with two untrue facts. First, Dealers have people confirm they were given the contract before being asked to sign it. Second, they have people agree that they read the entire contract front and back. Dealers do not direct peoples' attention to this clause or have it initialed; it just blends in. Of course, if what is said is untrue, the consumer would not know it because they never read that they agreed they read everything. All dealers know, after the long sales process, this final act of the pen is quick. So, in one paragraph off to the side, one sentence appears in the middle

of a paragraph and says, "You acknowledge you have read both sides of this contract including the arbitration clause on the reverse side."

Now to the arbitration clause on the reverse side. Even if this clause was read, only a select few people in the entire country would know all the terms, as they are not included in the RISC.

A. The rules and law are not disclosed

Virtually all car dealer arbitration clauses require consumers use an arbitration group the dealers pick. Let us put aside that letting one side pick who decides is offensive and unfair on its face and let us put aside the dealers only pick organizations with a heavy leanings towards them. After requiring that the consumer pick a dealer selected or approved organization to arbitrate, the clause reads, "You may get a copy of the rules of these organizations by contacting the arbitration organization or visiting its website." So lets get this straight. After hours of negotiation and signing papers that would take hours to read, a consumer needs to contact an organization or go to a website to know what they are agreeing to. So, no consumer ever knows what they are agreeing to.

It gets worse. Because California law might protect consumers or require some degree of fairness, it has been written out of these arbitration clauses which require use of the FAA (Federal Arbitration Act). Consumers, of course, are all familiar with the FAA. Here, the standard language is, "Any arbitration under this Arbitration Clause shall be governed by the Federal Arbitration Act (9 U.S.C. §1 et seq.)". If a consumer has a copy of the U.S. Code on hand, they can quickly look it up. The "et seq" means a lot of sections that follow.

B. Only consumers must arbitrate against third parties

Car Dealer arbitration clauses also require consumers to arbitrate any dispute they have with people who did not sign the contract if the dispute in any possible way relates to the vehicle. The arbitration agreement states it applies to "third parties who do not sign this agreement". If these third

parties did not sign, could the consumer enforce arbitration, say, against the prior owner, or a body shop, etc.? Highly unlikely.

A key driving force in inserting these provisions are groups who finance cars. Arbitration has helped them exploit consumers. So why not require it in car contracts?

C. The agreements are cost prohibitive

Except for a maximum up-front payment of $1,500 for administrative fees by the dealer, the consumer is required under the agreement to pay all their own fees and costs. Standard arbitrator fees, at least in California, are $300 - $600 per hour. The average consumer is required to pay an hourly fee equal in most cases to their car payment. Only the wealthiest purchasers can afford this. State law lets a party recover attorneys fees and costs so a consumer can afford to hire an attorney. Such recovery is mandatory under state law, but the arbitration agreement states reimbursement is "at the arbitrators discretion". Attorneys are reluctant to risk that even if they win, an arbitrator (who gets his income from the car industry), will award any attorney fees let alone fair fees. The one organization that provides rules that recognize the limited resources on consumers was written out of the agreements (see earlier discussion of JAMS).

It is no wonder readers of Ask Hal cannot get attorneys to sue dealers with arbitration clauses. Anyone who says arbitration is cheaper is dead wrong in the consumer law arena, especially with respect to car dealer arbitrations.

D. The car dealers do not use arbitration when they are the aggrieved party

In thousands of cases over 20 plus years, I have never had a car dealer use arbitration when they felt they were owed something. The agreements are written so that only consumers must arbitrate.

For instance, on both a State and National basis, one of the problems I encounter most is

violation of the "ten-day rule". After a RISC is signed, it is final and binding unless cancelled by notice in 10 days by the dealer because no financing is obtained. The dealer does not have to cancel, but if they do not, they must finance the vehicle if they cannot find someone else to do so. I have case after case where even months later dealers demand a car back. This is, of course, illegal. If the consumer does not give it back, the Dealer simply steals the car, and calls it a repo. The arbitration clauses allow the car dealers to do any "self-help" they want, stating, "you and we retain the rights to self-help remedies such as repossession". Despite saying "you and we", the clear intent is to enable Dealers, not consumers. Once the dealer steals the car, arbitration cannot get it back; such remedies are equitable and require injunctive relief not available in arbitration.

E. The organizations used to hear car arbitrations are inherently biased

Across the Country dealers favor the National Arbitration Forum. After all, who would not like a group that solicits your business and promises to be on your side. NAF makes money doing arbitrations as do all arbitrations groups, such as AAA and others. NAF promises they "*will make a positive impact on the bottom line*" (emphasis in original). They promise, in huge print, to be "The alternative to the million dollar lawsuit". Many abuses have been documented against NAF by Public Justice (formerly Trial Lawyers for Public Justice). Similar advertising, as well as abuses, by AAA have also been documented. Extensive testimony on this subject was supplied by Paul Bland in his December 12, 2007 testimony before the Subcommittee on the Constitution of the United States Senate Judiciary Committee on S. 1782, the Arbitration Fairness Act of 2007.

When our office recently had a case before NAF, they were outright hostile. They would not even give us a list of arbitrators unless we agreed to keep the list secret. What a surprise the list had no Plaintiff attorneys. One of the benefits of arbitration for the dealers, as will be discussed in my final section, is the secrecy. Even if an isolated attorney takes a case to arbitration, they are free to

continue doing more of the same.

While the two arbitration panels selected by Car Dealers in California have inherent bias towards Car Dealers, I will not go on and on with examples. It is sad that we often represent consumers under the Automobile Sales Finance Act, and we have not been able to get Arbitrators to follow the act. In the case of Mrs. Woodly we had a dealer who denied any illegal conduct. When it became clear their acts were illegal, they claimed the defense of mistake (i.e. that this was a one time isolated event). A claim that in Court would have been laughable given their prior position and a right to investigate - meaning to do discovery. In arbitration, the Arbitrator denied us any right at all to discovery, such as seeing the other files. The Arbitrator in the unrecorded proceeding made clear his dislike of the law on this subject. In his written decision, however, he found the conduct illegal and then ruled it was a mistake because we had no evidence of other acts, which of course he stopped us from getting. He then awarded fees and costs against our consumer. He then tried to rewrite the arbitration agreement to prevent any review at all of his decision. As set forth in a later section, when we later faced the same attorney and defense in a Court case, their defense of "mistake" was exposed as a big lie and the consumer won.

In the end, no fix is available. Arbitration forums are businesses. Arbitrators make money arbitrating. The effects of repeat player bias have been well documented. Arbitrators and arbitration organizations favor companies they see a lot and who give them lots of business. Arbitrators who rule against companies quickly get disqualified and black-balled. All of which again makes it difficult for consumers to get attorneys to represent them in arbitration with Car Dealers. I stand willing and able to provide documentation on these issues, although groups such as Public Justice have made far more extensive studies. My world is almost all auto cases, and arbitration, simply put, is not fair or in any way helpful to consumers.

VI. ARBITRATION PROMOTES DEALER FRAUD, WHILE COURT PROCEEDINGS DISCOURAGE IT

One widowed senior changed the way cars are sold in this country, got refunds of excess charges for 180 other consumer, and perhaps helped lessen the financial negative equity crisis in the financial markets. The lady is Rita Thompson, and the case where I was Trial and Appellate counsel is *Thompson v. 10,000 RV Sales, Inc.* 130 Cal. App. 4th 950 (2005).

Rita Thompson sought help because she had traded in her used motor home for what she thought was a better used motor home. She paid thousands for a service contract to cover repairs. Her motor home turned out to be a disaster with many problems. The dealer would not fix any of these problems and the service contract company would not pay for any repairs. It later turned out the Dealer sold her the wrong service contract, selling her one for a new motor home instead. So, the service contract company would not fix anything, and no one told Rita or even offered her a different service contract. Rita did later obtain a significant verdict on this issue in the Judge trial that took place.

In going through the paperwork it was clear Rita had overpaid for her motor home. It was proven that the Dealer had manipulated the numbers to get her financing. Rita owed more on her trade in than it was worth; a common problem in this Country. This is called negative equity. A person who has a trade-in with $10,000.00 may owe $15,000.00 on the loan. They are $5,000.00 upside down with negative equity. To get her financed, the Dealer not only gave her trade in for the higher amount of what her loan balance was, but also paid her $14,000.00 more so this could be listed as a downpayment. Then they took this extra money they paid on the trade-in and added it to the purchase price. This has the effect of defrauding not only the lender but the financial markets where the loan is sold. Also, sales tax and registration is paid on the negative equity. Another effect

was brought home by the testimony of another widow.

Mrs. G. testified that she and her husband would buy a new motor home if they did not lose too much on their trade-in. When buying the motor home, her husband was still alive. The Dealer gave them a great trade-in and simply added $60,000.00 to the purchase price. When her husband died shortly after, she was stuck with a motor home she could not sell, given the debt, and did not know how to drive it. We later represented her and took car of the problem.

The key to this case is we got an injunction. An injunction is a Court order making a Dealer stop doing an illegal activity. The Dealer was ordered to stop adding the negative equity into purchase prices. From now on, contracts would have to show what the dealer was really paying for trade-ins.

In California, the Court above the Trial Court is the Appellate Court. The decisions of this Court may be published and become law to be followed by other Courts. This caused concern across the Country for auto dealers. Unlike arbitration, a published Court opinion could stop the illegal practice. Lengthy legal briefs by large law firms were filed on behalf of the vehicle and RV industries. In the end, the Appellate Court published a lengthy opinion finding this conduct illegal and to deceive both customers and the financial markets who buy these loans.

The case was featured in the Wall Street Journal. The Dealer magazines interviewed me and published the results on a National basis. Attorneys also learned of the ruling. A case of negative equity became named after Rita as a "Thompson cause of action". Other states have since followed the decision. Best of all, Dealers across the Country now show the negative equity on the contracts, giving full information to consumers and lenders.

So, what if Rita had an arbitration clause? Everything would have been handled in secrecy. We probably would never have seen the papers that showed what had happened as we got those in

discovery. Arbitrators do not, and in all states I know of cannot, order injunctions. Given our prior history, we probably would have lost this part of Mrs. Thompson's case. The end result would be the practice would still be happening in hundreds of thousands, if not millions, of car deals. Which, in the end, may be why dealers love arbitration so much.

VII. CONCLUSION

I admit to having very strong feelings on this subject. I talk or write to consumers almost every working day and, per my wife, too many weekends. The widespread use of arbitration clauses has turned the consumer world upside down. Dealers who have arbitration clauses have a very different attitude toward making things right or correcting problems. Earlier I mentioned an arbitration where the Judge ruled against us on the issue of mistake. The same attorney tried the same thing recently in another case, this one in the Court system. This time, we were able to prove the Dealer lied, and the overwhelming evidence was that the illegal practice was done time and again. I have to wonder what would have been the result in arbitration. With 50 million vehicle sales per year, I hope you act to provide a fair system.

Defend consumers constitutional rights and the ability to make a difference with access to the Court system. Thank you again for this honor.

Hallen D. Rosner

EXHIBIT A

U.S. MARINES – PERSONNEL TRAINING
FEBRUARY 1, 2008
Training by Hal Rosner, Senior Partner, Rosner & Mansfield, LLP

CAR DEALER FRAUD AND LEMON LAW 101

Brought to you by Rosner and Mansfield, the Auto Fraud Legal Center.*

AUTO FRAUD 101

Automobile fraud occurs when a retailer seller misrepresents or fails to disclose material facts regarding a new or used vehicle.

There are many categories of automobile fraud, including: violating the "single document rule;" requiring a deferred down payment with improper procedures; including "negative equity"/"over-allowance" in the sale; sale of wrecked vehicles; sale of previously repurchased "lemon" vehicles; odometer fraud; and various other financial frauds that occur in the advertising or at the time of sale or lease of the vehicle. The defendants in auto fraud cases may include insurance companies, car dealers, car manufacturers, and car finance companies.

The **following are some types of auto fraud that we frequently see** during our daily interaction with vehicle consumers:

Single Document Rule:

The Automobile Sales Finance Act (AFSA) provides that all obligations of both parties in a transaction must be contained in a single document (which explains why purchase agreements are so long in the auto industry). Often, however, dealerships will have customers sign additional documents, such as trade-in forms stating that the customer agrees to pay any difference between the value of their trade-in vehicle and the amount owed on that vehicle. Or, the dealership will agree to make payments on a trade-in vehicle but not include the trade-in vehicle in the purchase agreement. Another example is a "hold check agreement" (see below) whereby the customer agrees to pay additional money towards the down payment on a later date. Each of these documents violates the one document rule.

Hold Check Agreement/Deferred Down Payment:

Many dealership customers are unable to pay the entire down payment at the time the purchase contract is signed. Often dealerships will allow the customer to make a down payment in payments (called deferred down payments). Although the vehicle code recognizes these deferred down payments, they must be itemized in the purchase contract, including the amounts and due dates for the deferred payments. Some dealerships, however, will have customers write checks for the deferred down payments and then agree not to deposit the checks until an agreed upon date. The customer is then made to sign a separate agreement that lays out the dates on which the checks will be cashed and additional provisions regarding any returned checks – thus creating additional obligations that are not included in the purchase agreement.

Sticker Price:

The vehicle code states that a dealership cannot sell a new vehicle for more than sticker price (a.k.a. the manufacturer's suggested retail price, or MSRP) unless there is a dealer addendum sticker disclosing itemized costs above MSRP physically affixed to the car. Inflating the cash price of a vehicle – as in the case of a negative equity deal (see above) often results in selling a vehicle for higher than the MSRP, while also affecting the amount charged for taxes, licensing & registration and finance charges.

Spanish Language:

Civil Code § 1632 provides that if certain transactions, including lease/purchase of a vehicle, is primarily negotiated in Spanish, then a Spanish translation of the contract must be provided to the customer prior to signing the English language contract. This law was recently expanded to include Chinese, Vietnamese, Tagalog and Korean. Failure to comply gives the customer the right to rescind the transaction.

Used Vehicle Disclosures/Misrepresentation:

Dealerships are required to disclose material known facts about a used vehicle, such as if it was:

- involved in a prior accident (that caused substantial damages) [*See below* for more information on this issue]
- a prior rental vehicle
- a lemon law 'buy back,' meaning the vehicle was repurchased by either the manufacturer or dealer under the lemon law because of a defect
- subject to odometer tampering/malfunction

New/Used/Demo/Unwind:

The AFSA requires that a dealership describe the vehicle being purchased as either "new" or "used." Although the "used" designation applies to demonstrator vehicles (a.k.a. "demos," vehicles used by manufacturer or dealership representatives) and "unwinds" (vehicles previously sold, then returned, usually because of financing problems), these vehicles are often represented as "new" to customers.

Negative Equity/Over-Allowance:

Arises in a transaction that includes a trade-in vehicle. Generally, the customer is led to believe that the dealership is valuing the trade-in vehicle at the same amount that's owed (so that the customer doesn't appear to owe anything on the trade-in). In reality, however, the actual cash value given by the dealership is less than the amount owed, and the difference is added to the cash price of the vehicle being purchased. If this is done it is illegal, even if the customer knows and agrees to it. The extra amount cannot be added to the vehicle line 1(a)1 per our precedent-setting case of Thompson v. 10,000 RV's.

Packing:

In a "packing" case the customer is quoted an inflated monthly payment. If he or she accepts this amount, the dealership adds accessories (alarms, service contracts, GAP insurance, paint/fabric protection, etc.) to the purchase contract to reach the inflated quoted price. The customer doesn't realize that the accessories are optional nor that they're paying extra for the accessories, which are often represented as "included" with the vehicle.

Rewritten Contract/Backdating:

Often a customer won't qualify for financing under the terms of the first purchase contract and may be required to increase a down payment, APR, etc. to quality for a loan. The dealership then has the customer sign a second contract with the new terms but backdates it with the date of the first contract, sticking the customer with financing charges for a period during which the contract wasn't yet in effect. In addition to making a material misrepresentation of when the customer takes the obligation of the new contract, a backdated contract often violates the single document rule (see below) because another form, usually called "Acknowledgment of the Rewritten Contract," has the actual date when the contract was signed. In addition, many customers aren't informed that they can opt to cancel the contract and return the new vehicle and have the down payment and trade-in vehicle refunded, rather than signing a second contract with less favorable financing terms.

Forgery:

Dealerships sometimes forge the signature of customers on subsequent contracts that change the terms of the original signed contract (especially if the customer refuses to sign the new contract). Other commonly forged documents include: credit applications (with fraudulent representations about income, etc.), as well as buyer's guides and disclosure forms (to prevent buyers from reading their buyers' rights and/or information that may cause them to reconsider their purchase decisions).

Certified Used Vehicles:

Many manufacturers and dealerships advertise used vehicles as "certified pre-owned," supposedly guaranteeing to the customer that the vehicle is in good working order and free from major structural damage, including previous accidents. Often times, however, dealerships misrepresent used vehicles that have suffered previous accidents, structural damage (or other conditions that would preclude certification under the dealership's advertised standards) as "certified" vehicles – misleading customers into paying a premium price for a damaged product.

EXHIBIT B

RETAIL INSTALLMENT SALE CONTRACT - SIMPLE INTEREST FINANCE CHARGE

Dealer Number _____ Contract Number _____ R.O.S. Number _____ Stock Number 473446

Buyer (and Co-Buyer) Name and Address (Including County and Zip Code)	Creditor - Seller (Name and Address)
	ENCINITAS FORD 1424 ENCINITAS BLVD ENCINITAS CA 92024-0245

You, the Buyer (and Co-Buyer, if any), may buy the vehicle below for cash or on credit. By signing this contract, you choose to buy the vehicle on credit under the agreements on the front and back of this contract. You agree to pay the Creditor - Seller (sometimes "we" or "us" in this contract) the Amount Financed and Finance Charge according to the payment schedule below. We will figure your finance charge on a daily basis. The Truth-In-Lending Disclosures below are part of this contract.

New Used	Year	Make and Model	Odometer	Vehicle Identification Number	Primary Use For Which Purchased
USED	2004	FORD F-250 SD	43990		☒ personal, family or household ☐ business or commercial

FEDERAL TRUTH-IN-LENDING DISCLOSURES

ANNUAL PERCENTAGE RATE The cost of your credit as a yearly rate.	FINANCE CHARGE The dollar amount the credit will cost you.	Amount Financed The amount of credit provided to you or on your behalf.	Total of Payments The amount you will have paid after you have made all payments as scheduled.	Total Sale Price The total cost of your purchase on credit, including your down payment of $ 700.00 is
9.40 %	$ 9,353.10 (e)	$ 29,960.34	$ 39,313.44 (e)	$ 40,013.44 (e)

(e) means an estimate

YOUR PAYMENT SCHEDULE WILL BE:

Number of Payments:	Amount of Payments:	When Payments Are Due:
One Payment of	N/A	
One Payment of	N/A	
71 Payments	546.02	Monthly, Beginning 12/16/2006
Payments	N/A	Monthly, Beginning
One Final Payment	546.02	11/16/2012

Late Charge. If payment is not received in full within 10 days after it is due, you will pay a late charge of 5% of the part of the payment that is late.
Prepayment. If you pay off all your debt early, you may be charged a minimum finance charge.
Security Interest. You are giving a security interest in the vehicle being purchased.
Additional Information. See this contract for more information including information about nonpayment, default, any required repayment in full before the scheduled date, and security interest, late charges, and prepayment refunds.

ITEMIZATION OF THE AMOUNT FINANCED

1. Total Cash Price — $ 28250.00 (A)
   A. Cash Price of Motor Vehicle and Accessories
      1. Cash Price Vehicle $ 28250.00
      2. Cash Price Accessories $ N/A
      3. Other (Nontaxable)
         Describe $ N/A
         Describe $ N/A
   B. Document Preparation Fee (not a governmental fee) $ 85.00 (B)
   C. Smog Fee Paid to Seller $ N/A (C)
   D. Theft Deterrent Device $ N/A (D)
   E. Theft Deterrent Device $ N/A (E)
   F. Surface Protection Product $ N/A (F)
   G. Surface Protection Product $ N/A (G)
   H. Sales Tax (on taxable items in A through G) $ 2334.34 (H)
   I. Optional DMV Electronic Filing Fee* $ N/A (I)
   J. (Optional) Service Contract (to whom paid)* $ N/A (J)
   K. (Optional) Service Contract (to whom paid)* $ N/A (K)
   L. Prior Credit or Lease Balance paid by Seller to $ N/A (L)
      (see downpayment and trade-in calculation)
   M. (Optional) Gap Contract (to whom paid)* $ N/A (M)
   N. (Optional) Used Vehicle Contract Cancellation Option Agreement $ N/A (N)
   O. Other (to whom paid)* $ N/A (O)
      For
   Total Cash Price (A through O) $ 30629.34 (1)
2. Amounts Paid to Public Officials
   A. License Fees ESTIMATED $ 23.00 (A)
   B. Registration/Transfer/Titling Fees $ N/A (B)
   C. California Tire Fees* $ N/A (C)
   D. Other $ N/A (D)
   E. Other $ N/A (E)
   Total Official Fees (A through E) $ 23.00 (2)
3. Amount Paid to Insurance Companies
   (Total premiums from Statement of Insurance column a + b)* $ N/A (3)
4. Smog Certification or Exemption Fee Paid to State $ 8.00 (4)
5. Subtotal (1 through 4) $ 30660.34 (5)
6. Total Downpayment
   A. Agreed Upon Value [illegible] $ [illegible] (A)
      Year 2001 Make [illegible]
      Model 4251 Body [illegible]
      VIN WBADV33412P655423
   B. Less Prior Credit or Lease Balance $ 13300.00 (B)
   C. Net Trade-In (A less B) (indicate if a negative number) $ 700.00 (C)
   D. Deferred Downpayment $ N/A (D)
   E. Manufacturer's Rebate $ N/A (E)
   F. Other $ N/A (F)

STATEMENT OF INSURANCE

NOTICE. No person is required as a condition of financing this purchase of a motor vehicle to purchase or negotiate any insurance through a particular insurance company, agent or broker. You are not required to buy any other insurance to obtain credit. Your decision to buy or not buy other insurance will not be a factor in the credit approval process.

Vehicle Insurance

	Term	Premium
$ N/A Bod Comp, Fire & Theft	N/A Max.	$ N/A
$ N/A Bod Collision	N/A Max.	$ N/A
Body Injury $ N/A Limits	N/A Max.	$ N/A
Property Damage $ N/A Limits	N/A Max.	$ N/A
Medical N/A	N/A Max.	$ N/A
	N/A Max.	$ N/A
Total Vehicle Insurance Premium		$ N/A

UNLESS A CHARGE IS INCLUDED IN THIS AGREEMENT FOR PUBLIC LIABILITY OR PROPERTY DAMAGE INSURANCE, PAYMENT FOR SUCH COVERAGE IS NOT PROVIDED BY THIS AGREEMENT.

You may buy the physical damage insurance this contract requires (see below) from insurer you choose who is acceptable to us. You are not required to buy any other insurance to obtain credit.

Buyer X [redacted]
Co-Buyer X
Seller X

If any insurance is checked below, policies or certificates from the named insurance companies will describe the terms and conditions.

Application for Optional Credit Insurance

☐ Credit Life: ☐ Buyer ☐ Co-Buyer ☐ Both
☐ Credit Disability (Buyer Only)

	Term	Exp.	Premium
Credit Life	N/A Max.		$ N/A
Credit Disability	N/A Max.		$ N/A
Total Credit Insurance Premiums			$ N/A

Insurance Company Name N/A
Home Office Address N/A

Credit life insurance and credit disability insurance are not required to obtain credit. Your decision to buy or not buy credit life and credit disability insurance will not be a factor in the credit approval process. They will not be provided unless you sign and agree to pay the extra cost. Credit life insurance is based on your original payment schedule. This insurance may not pay all you would owe if a contract is paid ahead of its regular payment. Credit disability insurance does not cover any increase in your payment or in the number of payments. Coverage for credit life insurance and credit disability insurance ends on the original due date for the last payment unless a different term for the insurance is stated above.

You are applying for the credit insurance marked above. Your signature below means that you agree that: (1) You are not eligible for insurance if you have reached your 65th birthday; (2) You are eligible for disability insurance only if you are working for wages or profit 30 hours a week or more on the Effective Date; (3) Only the Primary Buyer is eligible for disability insurance. DISABILITY INSURANCE MAY NOT COVER CONDITIONS FOR WHICH YOU HAVE SEEN A DOCTOR OR CHIROPRACTOR IN THE LAST 6 MONTHS (Refer to "Total Disabilities Not Covered" in your policy for details).
You want to buy the credit insurance.

Date X Buyer Signature Age
Date X Co-Buyer Signature Age

OPTIONAL GAP CONTRACT. A gap contract (sometimes called a gap waiver or debt cancellation contract) is not required to obtain credit and will not be provided unless you sign below and agree to pay the extra charge. If you choose to buy a gap contract, the charge is shown in Item 10A. See your gap contract for details on the protection it provides. Is a part of this contract.
Term N/A Max. N/A Name of Gap Contract
You want to buy a gap contract.
Buyer X

C. California Tire Fees* $ N/A (C)
D. Other $ N/A (D)
E. Other $ N/A (E)
Total Official Fees (A through E) $ 23.00 (2)
3. Amount Paid to Insurance Companies
[Total premiums from Statement of Insurance columns a + b]* $ N/A (3)
4. Smog Certification or Exemption Fee Paid to State $ 8.00 (4)
5. Subtotal (1 through 4) $ 30560.34 (5)
6. Total Downpayment
A. Agreed Trade-in Value Yr. 2002 Make BMW
Model 325I Color 65508
VIN WBAEV3341 2PD55423 $ 14000.00 (A)
B. Less Prior Credit or Lease Balance $ 13300.00 (B)
C. Net Trade-in [A less B] (find cash if a negative number) $ 700.00 (C)
D. Deferred Downpayment $ N/A (D)
E. Manufacturer's Rebate $ N/A (E)
F. Other $ N/A (F)
G. Cash $ N/A (G)
Total Downpayment (C through G) $ 700.00 (6)
(If negative, enter zero on line 6 and enter the amount less than zero as a positive number on line 10, above)
7. Amount Financed (5 less 6) $ 29860.34 (7)
*Seller may keep part of these amounts.

Disability Insurance. DISABILITY INSURANCE MAY NOT COVER CONDITIONS FOR WHICH YOU HAVE SEEN A DOCTOR OR CHIROPRACTOR IN THE LAST 6 MONTHS (Refer to "Total Disabilities Not Covered" in your policy for details).
You want to buy the credit insurance.
X Date Buyer Signature Age
X Date Co-Buyer Signature Age

OPTIONAL GAP CONTRACT A gap contract (debt cancellation contract) is not required to obtain credit and will not be provided unless you sign below and agree to pay the extra charge. If you choose to buy a gap contract, the charge is shown in Item 1K. See your gap contract for details on the protection it provides. It is part of this contract.
Term N/A Mos. N/A Price of Gap Contract
You want to buy a gap contract.
Buyer X

OPTIONAL SERVICE CONTRACT(S) You want to purchase the service contract(s) written with the following company(ies) for the period(s) shown below for the charge(s) shown in Item 1J and/or 1K above.
1J Company N/A
Term Mos. or Miles
1K Company N/A
Term Mos. or Miles
Buyer X

BELLER ASSISTED LOAN
BUYER MAY BE REQUIRED TO PROVIDE SECURITY FOR THE LOAN, AND WILL BE OBLIGATED FOR THE INSTALLMENT PAYMENTS ON BOTH THIS RETAIL INSTALLMENT SALE CONTRACT AND THE LOAN.
Proceeds of Loan From: N/A
Amount $ N/A Finance Charge $ N/A
Total $ N/A Payable in N/A
Installments of $ N/A
from this Loan is shown in Item 6D.

AUTO BROKER FEE DISCLOSURE
If this contract reflects the retail sale of a new motor vehicle, the sale is not subject to a fee received by an autobroker from us unless the following box is checked:
☐ Name of autobroker receiving fee, if applicable:
N/A

HOW THIS CONTRACT CAN BE CHANGED. This contract contains the entire agreement between you and us relating to this contract. Any change to the contract must be in writing and both you and we must sign it. No oral changes are allowed.
Buyer Signs X
Co-Buyer Signs X

SELLER'S RIGHT TO CANCEL. Buyer and Co-Buyer sign here, the provisions of the Seller's Right to Cancel section on the back of this contract. Sign only if Seller cancel if Seller is unable to assign the contract to a financial institution at cost.
X Buyer X Co-Buyer

OPTION: ☒ You pay no finance charge if the Amount Financed, Item 7, is paid in full on or before 11-22 Year 06 SELLER'S INITIALS

THE MINIMUM PUBLIC LIABILITY INSURANCE LIMITS PROVIDED IN LAW MUST BE MET BY EVERY PERSON WHO PURCHASES A VEHICLE. IF YOU ARE UNSURE WHETHER OR NOT YOUR CURRENT INSURANCE POLICY WILL COVER YOUR NEWLY ACQUIRED VEHICLE IN THE EVENT OF AN ACCIDENT, YOU SHOULD CONTACT YOUR INSURANCE AGENT.
WARNING:
YOUR PRESENT POLICY MAY NOT COVER COLLISION DAMAGE OR MAY NOT PROVIDE FOR FULL REPLACEMENT COSTS FOR THE VEHICLE BEING PURCHASED. IF YOU DO NOT HAVE FULL COVERAGE, SUPPLEMENTAL COVERAGE FOR COLLISION DAMAGE MAY BE AVAILABLE TO YOU THROUGH YOUR INSURANCE AGENT OR THROUGH THE SELLING DEALER. HOWEVER, UNLESS OTHERWISE SPECIFIED, THE COVERAGE YOU OBTAIN THROUGH THE DEALER PROTECTS ONLY THE DEALER, USUALLY UP TO THE AMOUNT OF THE UNPAID BALANCE REMAINING AFTER THE VEHICLE HAS BEEN REPOSSESSED AND SOLD.
FOR ADVICE ON FULL COVERAGE THAT WILL PROTECT YOU IN THE EVENT OF LOSS OR DAMAGE TO YOUR VEHICLE, YOU SHOULD CONTACT YOUR INSURANCE AGENT.
THE BUYER SHALL SIGN TO ACKNOWLEDGE THAT HE/SHE UNDERSTANDS THESE PUBLIC LIABILITY TERMS AND CONDITIONS.
SIS X X

Representations of Buyer. Seller has relied on the truth and accuracy of the information provided by you in connection with the Trade-in Vehicle. You represent that you have given a true payoff amount on the vehicle traded in. If the payoff amount is more than the amount shown above in Item 6B as "Prior Credit or Lease Balance," you must pay Seller the excess on demand. If the actual amount is less than the amount shown above in Item 6B as "Prior Credit or Lease Balance," Seller will refund the difference to you.
Buyer X Co-Buyer X

Notice to Buyer: (1) Do not sign this agreement before you read it or if it contains any blank spaces to be filled in. (2) You are entitled to a completely filled in copy of this agreement. (3) You can prepay the full amount due under this agreement at any time. (4) If you default in the performance of your obligations under this agreement, the vehicle may be repossessed and you may be subject to suit and liability for the unpaid indebtedness evidenced by this agreement.

If you have a complaint concerning this sale, you should try to resolve it with the seller.
Complaints concerning unfair or deceptive practices or methods by the seller may be referred to the city attorney, the district attorney, or an investigator for the Department of Motor Vehicles, or any combination thereof.
After this contract is signed, the seller may not change the financing or payment terms unless you agree in writing to the change. You do not have to agree to any change, and it is an unfair or deceptive practice for the seller to attempt to impose a change.
Buyer Signature X Co-Buyer Signature X

The Annual Percentage Rate may be negotiable with the Seller. The Seller may assign this contract and retain its right to receive a part of the Finance Charge.

THERE IS NO COOLING OFF PERIOD UNLESS YOU OBTAIN A CONTRACT CANCELLATION OPTION
California law does not provide for a "cooling off" or other cancellation period for vehicle sales. Therefore, you cannot later cancel this contract simply because you change your mind, decide the vehicle costs too much, or wish you had acquired a different vehicle. After you sign below, you may only cancel this contract with the agreement of the seller or for legal cause, such as fraud.
However, California law does require a seller to offer a 3-day contract cancellation option on used vehicles with a purchase price of less than $4,000, subject to certain statutory conditions. This contract cancellation option requirement does not apply to the sale of a motorcycle or an off-highway motor vehicle subject to identification under California law. See the vehicle contract cancellation option agreement for details.

YOU AGREE TO THE TERMS OF THIS CONTRACT. YOU CONFIRM THAT BEFORE YOU SIGNED THIS CONTRACT, WE GAVE IT TO YOU, AND YOU WERE FREE TO TAKE IT AND REVIEW IT. YOU ACKNOWLEDGE THAT YOU HAVE READ BOTH SIDES OF THIS CONTRACT, INCLUDING THE ARBITRATION CLAUSE ON THE REVERSE SIDE, BEFORE SIGNING BELOW. YOU CONFIRM THAT YOU RECEIVED A COMPLETELY FILLED IN COPY WHEN YOU SIGNED IT.

Buyer Signature X Date 11/16/2006 Co-Buyer Signature X Date 2006

Co-Buyer and Other Owner: A co-buyer is a person who is responsible for paying the entire debt. An other owner is a person who is name on the title to the vehicle but does not have to pay the debt. The other owner agrees to the security interest in the vehicle given to us in this contract.

Other Owner Signature X Address

GUARANTY: To induce us to sell the vehicle to Buyer, each person who signs as a Guarantor individually guarantees the payment of this contract. If Buyer fails to pay any money owing on this contract, each Guarantor must pay it when asked. Each Guarantor will be liable for the total amount owing even if other persons also sign as Guarantor, and even if Buyer has a complete defense to Guarantor's demand for reimbursement. Each Guarantor agrees to be liable even if we do not or have not: (1) sue the Buyer or force Buyer to pay any or more payments; (2) give a full or partial release to any other Guarantor; (3) release any security; (4) accept less from the Buyer than the total amount owing; or (5) otherwise reach a settlement relating to this contract or extend the contract. Each Guarantor acknowledges receipt of a completed copy of this contract and guaranty at the time of signing.
Guarantor waives notice of acceptance of this Guaranty, notice of the Buyer's non-payment, non-performance, and default, and notices of the amount owing at any time, and of any demands upon the Buyer.

Guarantor X Date Guarantor X Date
Address Address

Seller Signs ENCINITAS FORD Date 11/16/2006 By X Title F&I

LAW FORM NO. 563-RA-RS (Rev. 10/06) Page 1 of 2

1. **FINANCE CHARGE AND PAYMENTS**
   a. **How we will figure Finance Charge.** We will figure the Finance Charge on a daily basis at the Annual Percentage Rate on the unpaid part of the Amount Financed. Creditor Seller may receive part of the Finance Charge.
   b. **How we will apply payments.** We may apply each payment to the earned and unpaid part of the Finance Charge, to the unpaid part of the Amount Financed and to other amounts you owe under this contract in any order we choose.
   c. **How late payments or early payments change what you must pay.** We based the Finance Charge, Total of Payments, and Total Sale Price shown on the front on the assumption that you will make every payment on the day it is due. Your Finance Charge, Total of Payments, and Total Sale Price will be more if you pay late and less if you pay early. Changes may take the form of a larger or smaller final payment or, at our option, more or fewer payments of the same amount as your scheduled payment with a smaller final payment. We will send you a notice telling you about these changes before the final scheduled payment is due.
   d. **You may prepay.** You may prepay all or part of the unpaid part of the Amount Financed at any time. If you do so, you must pay the earned and unpaid part of the Finance Charge and all other amounts due up to the date of your payment. As of the date of your payment, if the minimum finance charge is greater than the earned Finance Charge, you may be charged the difference; the minimum finance charge is as follows: (1) $25 if the original Amount Financed does not exceed $1,000, (2) $50 if the original Amount Financed is more than $1,000 but not more than $2,000, or (3) $75 if the original Amount Financed is more than $2,000.

2. **YOUR OTHER PROMISES TO US.**
   a. **If the vehicle is damaged, destroyed, or missing.** You agree to pay us all you owe under this contract even if the vehicle is damaged, destroyed, or missing.

   > **GAP LIABILITY NOTICE**
   > In the event of theft or damage to your vehicle that results in a total loss, there may be a gap between the amount you owe under this contract and the proceeds of your insurance settlement and deductible. THIS CONTRACT PROVIDES THAT YOU ARE LIABLE FOR THE GAP AMOUNT. An optional gap contract (debt cancellation contract) for coverage of the gap amount may be offered for an additional charge.

   b. **Using the vehicle.** You agree not to remove the vehicle from the U.S. or Canada, or to sell, rent, lease, or transfer any interest in the vehicle or this contract without our written permission. You agree not to expose the vehicle to misuse, seizure, confiscation, or involuntary transfer. If we pay any repair bills, storage bills, taxes, fines, or charges on the vehicle, you agree to repay the amount when we ask for it.
   c. **Security Interest.**
      You give us a security interest in:
      - The vehicle and all parts or goods installed on it;
      - All money or goods received (proceeds) for the vehicle;
      - All insurance, maintenance, service, or other contracts we finance for you; and
      - All proceeds from insurance, maintenance, service, or other contracts we finance for you. This includes any refunds of premiums or charges from the contracts.

      This secures payment of all you owe on this contract. It also secures your other agreements in this contract as the law allows. You will make sure the title shows our security interest (lien) in the vehicle.
   d. **Insurance you must have on the vehicle.**
      You agree to have physical damage insurance covering loss of or damage to the vehicle for the term of this contract. The insurance must cover our interest in the vehicle. If you do not have this insurance, we may, if we choose, buy physical damage insurance. If we decide to buy physical damage insurance, we may either buy insurance that covers your interest and our interest in the vehicle, or buy insurance that covers only our interest. If we buy either type of insurance, we will tell you which type and the charge you must pay. The charge will be the premium for the insurance and a finance charge equal to the Annual Percentage Rate shown on the front of this contract or, at our option, the highest rate the law permits. If the vehicle is lost or damaged, you agree that we may use any insurance settlement to reduce what you owe or repair the vehicle.
   e. **What happens to returned insurance, maintenance, service, or other contract charges.** If we get a refund of insurance, maintenance, service, or other contract charges, you agree that we may subtract the refund from what you owe.

[illegible] PROMISES
   a. **You may owe late charges.** You will pay a late charge on each late payment as shown on the front. Acceptance of a late payment or late charge does not excuse your late payment or mean that you may keep making late payments. If you pay late, we may also take the steps described below.
   b. **You may have to pay all you owe at once.** If you break your promises (default), we may demand that you pay all you owe on this contract at once, subject to any right the law gives you to reinstate this contract.

      providing proof of insurance, and/or taking other action to cure the default. We will provide you all notices required by law to tell you when and how much to pay and/or what action you must take to redeem the vehicle.
   f. **We will sell the vehicle if you do not get it back.** If you do not redeem, we will sell the vehicle. We will send you a written notice of sale before selling the vehicle.
      We will apply the money from the sale, less allowed expenses, to the amount you owe. Allowed expenses are expenses we pay as the direct result of taking the vehicle, holding it, preparing it for sale, and selling it. Attorney fees and court costs the law permits are also allowed expenses. If any money is left (surplus), we will pay it to you unless the law requires us to pay it to someone else. If money from the sale is not enough to pay the amount you owe, you must pay the rest to us. If you do not pay this amount when we ask, we may charge you interest at the Annual Percentage Rate shown on the face of this contract, not to exceed the highest rate permitted by law, until you pay.
   g. **What we may do about optional insurance, maintenance, service, or other contracts.** This contract may contain charges for optional insurance, maintenance, service, or other contracts. If we repossess the vehicle, we may claim benefits under these contracts and cancel them to obtain refunds of unearned charges to reduce what you owe or repair the vehicle. If the vehicle is a total loss because it is confiscated, damaged, or stolen, we may claim benefits under these contracts and cancel them to obtain refunds of unearned charges to reduce what you owe.

4. **WARRANTIES SELLER DISCLAIMS**
   If you do not get a written warranty, and the Seller does not enter into a service contract within 90 days from the date of this contract, the Seller makes no warranties, express or implied, on the vehicle, and there will be no implied warranties of merchantability or of fitness for a particular purpose.
   This provision does not affect any warranties covering the vehicle that the vehicle manufacturer may provide. If the Seller has sold you a certified used vehicle, the warranty of merchantability is not disclaimed.

5. **Used Car Buyers Guide. The information you see on the window form for this vehicle is part of this contract. Information on the window form overrides any contrary provisions in the contract of sale.**
   Spanish Translation: Guía para compradores de vehículos usados. La información que ve en el formulario de la ventanilla para este vehículo forma parte del presente contrato. La información del formulario de la ventanilla deja sin efecto toda disposición en contrario contenida en el contrato de venta.

6. **Applicable Law**
   Federal law and California law apply to this contract. If any part of this contract is not valid, all other parts stay valid. We may delay or refrain from enforcing any of our rights under this contract without losing them. For example, we may extend the time for making some payments without extending the time for making others.

7. **Warranties of Buyer.** You promise you have given true and correct information in your application for credit, and you have no knowledge that will make that information untrue in the future. We have relied on the truth and accuracy of that information in entering into this contract. Upon request, you will provide us with documents and other information necessary to verify any item contained in your credit application.

You waive the provisions of Calif. Vehicle Code Section 1808.21 and authorize the California Department of Motor Vehicles to furnish your residence address to us.

CREDIT DISABILITY INSURANCE NOTICE
CLAIM PROCEDURE

If you become disabled, you must tell us right away. (You are advised to send this information to the same address to which you are normally required to send your payments, unless a different address or telephone number is given to you in writing by us as the location where we would like to be notified.) We will tell you where to get claim forms. You must send in the completed form to the insurance company as soon as possible and tell us as soon as you do.

If your disability insurance covers all of your missed payment(s), WE CANNOT TRY TO COLLECT WHAT YOU OWE OR FORECLOSE UPON OR REPOSSESS ANY COLLATERAL UNTIL THREE CALENDAR MONTHS AFTER your first missed payment is due or until the insurance company pays or rejects your claim, whichever comes first. We can, however, try to collect, foreclose, or repossess if you have any money due and owing us or are otherwise in default when your disability claim is made or if a senior mortgage or lien holder is foreclosing.

If the insurance company pays the claim within the three calendar months, we must accept the money as though you paid on time. If the insurance company rejects the claim within the three calendar months or accepts the claim within the three calendar months on a partial disability and pays less than for a total disability, you will have 35 days from the date that the rejection or the acceptance of the partial disability claim is sent to pay past due payments, or the difference between the past due payments and what the insurance company pays for the partial disability, plus late charges. You can contact us, and we will tell you how much you owe. After that time, we can take action to collect or foreclose or repossess any collateral you may have given.

If the insurance company accepts your claim but requires that you send in additional forms to remain eligible for continued payments, you should send in these completed additional forms no later than required. If you do not send in these forms on time, the insurance company may

charge equal to the Annual Percentage Rate shown on the front of this contract or, at our option, the highest rate the law permits. If the vehicle is lost or damaged, you agree that we may use any insurance settlement to reduce what you owe or repair the vehicle.

e. **What happens to returned insurance, maintenance, service, or other contract charges.** If we get a refund of insurance, maintenance, service or other contract charges, you agree that we may subtract the refund from what you owe.

3. **IF YOU PAY LATE OR BREAK YOUR OTHER PROMISES**

a. **You may owe late charges.** You will pay a late charge on each late payment as shown on the front. Acceptance of a late payment or late charge does not excuse your late payment or mean that you may keep making late payments. If you pay late, we may also take the steps described below.

b. **You may have to pay all you owe at once.** If you break your promises (default), we may demand that you pay all you owe on this contract at once, subject to any right the law gives you to reinstate this contract.

Default means:

- You do not pay any payment on time;
- You start a proceeding in bankruptcy or one is started against you or your property;
- The vehicle is lost, damaged or destroyed; or
- You break any agreements in this contract.

The amount you will owe will be the unpaid part of the Amount Financed plus the earned and unpaid part of the Finance Charge, any late charges, and any amounts due because you defaulted.

c. **You may have to pay collection costs.** You will pay our reasonable costs to collect what you owe, including attorney fees, court costs, collection agency fees, and fees paid for other reasonable collection efforts. You agree to pay a charge not to exceed $15 if any check you give to us is dishonored.

d. **We may take the vehicle from you.** If you default, we may take (repossess) the vehicle from you if we do so peacefully and the law allows it. If your vehicle has an electronic tracking device, you agree that we may use the device to find the vehicle. If we take the vehicle, any accessories, equipment, and replacement parts will stay with the vehicle. If any personal items are in the vehicle, we may store them for you at your expense. If you do not ask for these items back, we may dispose of them as the law allows.

e. **How you can get the vehicle back if we take it.** If we repossess the vehicle, you may pay to get it back (redeem). You may redeem the vehicle by paying all you owe, or you may have the right to reinstate this contract and redeem the vehicle by paying past due payments and any late charges, the insurance company pays or rejects your claim, whichever comes first. We can, however, try to collect, foreclose, or repossess if you have any money due and owing us or are otherwise in default when your disability claim is made or if a senior mortgage or lien holder is foreclosing. If the insurance company pays the claim within the three calendar months, we must accept the money as though you paid on time. If the insurance company rejects the claim within the three calendar months or accepts the claim within the three calendar months on a partial disability and pays less than for a total disability, you will have 30 days from the date that the rejection or the acceptance of the partial disability claim is sent to pay past due payments, or the difference between the past due payments and what the insurance company pays for the partial disability, plus late charges. You can contact us, and we will tell you how much you owe. After that time, we can take action to collect or foreclose or repossess any collateral you may have given.

If the insurance company accepts your claim but requires that you send in additional forms to remain eligible for continued payments, you should send in these completed additional forms no later than required. If you do not send in these forms on time, the insurance company may stop paying, and we will then be able to take action to collect or foreclose or repossess any collateral you may have given.

Seller's Right to Cancel

a. Seller agrees to deliver the vehicle to you on the date this contract is signed by Seller and you. You understand that it may take a few days for Seller to verify your credit and assign the contract. You agree that if Seller is unable to assign the contract to any one of the financial institutions with whom Seller regularly does business under an assignment acceptable to Seller, Seller may cancel the contract.

b. Seller shall give you written notice (or in any other manner in which actual notice is given to you) within 10 days of the date this contract is signed if Seller elects to cancel. Upon receipt of such notice, you must immediately return the vehicle to Seller in the same condition as when sold, reasonable wear and tear excepted. Seller must give back to you all consideration received by Seller, including any trade-in vehicle.

c. If you do not immediately return the vehicle, you shall be liable for all expenses incurred by Seller in taking the vehicle from you, including reasonable attorney's fees.

d. While the vehicle is in your possession, all terms of the contract, including those relating to use of the vehicle and insurance for the vehicle, shall be in full force and you shall assume all risk of loss or damage to the vehicle. You must pay all reasonable costs for repair of any damage to the vehicle until the vehicle is returned to Seller.

ARBITRATION CLAUSE
PLEASE REVIEW - IMPORTANT - AFFECTS YOUR LEGAL RIGHTS

1. EITHER YOU OR WE MAY CHOOSE TO HAVE ANY DISPUTE BETWEEN US DECIDED BY ARBITRATION AND NOT IN COURT OR BY JURY TRIAL.
2. IF A DISPUTE IS ARBITRATED, YOU WILL GIVE UP YOUR RIGHT TO PARTICIPATE AS A CLASS REPRESENTATIVE OR CLASS MEMBER ON ANY CLASS CLAIM YOU MAY HAVE AGAINST US INCLUDING ANY RIGHT TO CLASS ARBITRATION OR ANY CONSOLIDATION OF INDIVIDUAL ARBITRATIONS.
3. DISCOVERY AND RIGHTS TO APPEAL IN ARBITRATION ARE GENERALLY MORE LIMITED THAN IN A LAWSUIT, AND OTHER RIGHTS THAT YOU AND WE WOULD HAVE IN COURT MAY NOT BE AVAILABLE IN ARBITRATION.

Any claim or dispute, whether in contract, tort, statute or otherwise (including the interpretation and scope of this clause, and the arbitrability of the claim or dispute), between you and us or our employees, agents, successors or assigns, which arise out of or relate to your credit application, purchase or condition of this vehicle, this contract or any resulting transaction or relationship (including any such relationship with third parties who do not sign this contract) shall, at your or our election, be resolved by neutral, binding arbitration and not by a court action. Any claim or dispute is to be arbitrated by a single arbitrator on an individual basis and not as a class action. You expressly waive any right you may have to arbitrate a class action. You may choose one of the following arbitration organizations and its applicable rules: the National Arbitration Forum, Box 50191, Minneapolis, MN 55403-0191 (www.arbitration-forum.com), the American Arbitration Association, 335 Madison Ave., Floor 10, New York, NY 10017-4605 (www.adr.org), or any other organization that you may choose subject to our approval. You may get a copy of the rules of these organizations by contacting the arbitration organization or visiting its website.

Arbitrators shall be attorneys or retired judges and shall be selected pursuant to the applicable rules. The arbitrator shall apply governing substantive law in making an award. The arbitration hearing shall be conducted in the federal district in which you reside unless the Creditor-Seller is a party to the claim or dispute, in which case the hearing will be held in the federal district where this contract was executed. We will advance your filing, administration, service or case management fee and your arbitrator or hearing fee all up to a maximum of $1500, which may be reimbursed by decision of the arbitrator at the arbitrator's discretion. Each party shall be responsible for its own attorney, expert and other fees, unless awarded by the arbitrator under applicable law. If the chosen arbitration organization's rules conflict with this clause, then the provisions of this clause shall control. The arbitrator's award shall be final and binding on all parties, except that in the event the arbitrator's award for a party is $0 or against a party is in excess of $100,000, or includes an award of injunctive relief against a party, that party may request a new arbitration under the rules of the arbitration organization by a three-arbitrator panel. The appealing party requesting new arbitration shall be responsible for the filing fee and other arbitration costs subject to a final determination by the arbitrators or a fair apportionment of costs. Any arbitration under this Arbitration Clause shall be governed by the Federal Arbitration Act (9 U.S.C. § 1 et seq.) and not by any state law concerning arbitration.

You and we retain any rights to self-help remedies, such as repossession. You and we retain the right to seek remedies in small claims court for disputes or claims within that court's jurisdiction, unless such action is transferred, removed or appealed to a different court. Neither you nor we waive the right to arbitrate by using self-help remedies or filing suit. Any court having jurisdiction may enter judgment on the arbitrator's award. This clause shall survive any termination, payoff or transfer of this contract. If any part of this Arbitration Clause, other than waivers of class action rights, is deemed or found to be unenforceable for any reason, the remainder shall remain enforceable. If a waiver of class action rights is deemed or found to be unenforceable for any reason in a case in which class action allegations have been made, the remainder of this arbitration clause shall be unenforceable.

NOTICE: ANY HOLDER OF THIS CONSUMER CREDIT CONTRACT IS SUBJECT TO ALL CLAIMS AND DEFENSES WHICH THE DEBTOR COULD ASSERT AGAINST THE SELLER OF GOODS OR SERVICES OBTAINED PURSUANT HERETO OR WITH THE PROCEEDS HEREOF. RECOVERY HEREUNDER BY THE DEBTOR SHALL NOT EXCEED AMOUNTS PAID BY THE DEBTOR HEREUNDER.

The preceding NOTICE applies only if the "personal, family or household" box in the "Primary Use for Which Purchased" section of this contract is checked. In all other cases, Buyer will not assert against any subsequent holder or assignee of this contract any claims or defenses the Buyer (debtor) may have against the Seller, or against the manufacturer of the vehicle or equipment obtained under this contract.

Seller assigns its interest in this contract to _____ (Assignee) at (address) _____ under the terms of Seller's agreement(s) with Assignee.

☐ Assigned with recourse ☐ Assigned without recourse ☐ Assigned with limited recourse

Seller _____ By _____ Title _____

Form No. 559-CA-ARB 7/09

Ms. SÁNCHEZ. Thank you. Your time, unfortunately, has expired.

And we want to thank all of the witnesses for their testimony, and we are going to now begin our round of questioning. And I will begin by recognizing myself for 5 minutes.

My first question is for Ms. Shahan. One section of the proposed legislation that we are talking about today requires that arbitrators provide a written decision if either party to the arbitration requests one. I want you to please explain why that language is important.

Ms. SHAHAN. Yes. Thank you, Congresswoman.

That is one of the best provisions in the bill, and we see that as a real benefit because right now, when consumers are going to these arbitration programs, there is no requirement that there be any record at all. And I think that it is very carefully crafted so that it is not overly burdensome. It doesn't require formal findings of fact; it requires simply that the arbitrator provide an informal explanation of how they arrived at their decision.

And that will help other consumers. It will also help, I hope, policymakers decide how these decisions are being rendered and why, so that if there is a need to improved this system, that can be done.

Ms. SÁNCHEZ. In your prepared statement, you state that lenders will not accept retail installment contracts for auto loans unless the dealers include binding mandatory arbitration clauses in the contract, and I would like you to please explain that.

Ms. SHAHAN. Yes. This has been a real concern because some dealers were not imposing mandatory binding arbitration, pre-dispute, but lenders insist on it. And so consumers, especially consumers who aren't paying cash for a car and have to get a loan and use a retail installment contract, are having arbitration forced on them by virtually all the dealers.

If you are a consumer, you have very limited options. If you are buying a new car, you have to go to a franchise car dealer unless you are going overseas and getting it directly from the manufacturer, because they have a monopoly in all 50 states. That is the only place you can go to get a new car.

And if you are buying a used car and you want to go to a reputable dealership that is licensed by the state, where you have some expectation that they are a legitimate business, you really don't expect that they can engage in massive fraud and get away with it. And so consumers' guard is down, their options are limited, and the lenders are forcing dealers who might not be inclined to use these provisions to do it.

Ms. SÁNCHEZ. Thank you.

Ms. Rice, and again, I am sorry for the experience that you have had, but we are still thankful that you are here to talk about your experience in this field. One of the many arguments that are used for mandatory binding arbitration is that it is less costly than litigating in the traditional court system. And I wanted to know whether you found that to be true in your situation, that having to arbitrate your issue would be less costly than it would be to pursue that claim in court.

Ms. RICE. There aren't set fees; there aren't set limitations on how much a private person can charge a consumer in regards to arbitration. There is no way for me to research that and to come

up with a number that says, "Okay, this is, you know, where it is at, and what it is going to cost me."

You know, my lawsuit has cost me some money, but if the dealership would have just done the right thing at the beginning, it wouldn't have come to this; I wouldn't be sitting in front of all of you today and telling you this story. It would be, "This dealership did me right, and everything is great and wonderful." So, I mean, short of having my attorney here to tell you the difference between what she is going to charge me versus what arbitration is going to cost, I mean, there is really no way to come up with the correct answer on that.

Ms. SÁNCHEZ. Thank you.

Mr. Rosner, maybe you can provide a little bit of information on the cost to the consumer between arbitration versus court.

Mr. ROSNER. Obviously, the cost of a court proceeding in a case with my firm, for a consumer, is zero. There is a complaint fee of $300; the court system if free. In the court system we have arbitration available, but those arbitrators are people who donate their time, don't do it as a regular business, and we pay them a minimal fee and they will hear disputes. We also have mediation, and there is no cost during it.

If they want to go to arbitration, you are lucky if you get an arbitrator whose fees are limited to $300 to $600 per hour. Plus, I have to look to a consumer and say, "Despite the fact that California law says that you will not have to pay the dealer's attorneys fees in these consumer cases," because they know no one will bring—they can't afford it. The risk is too high. Even if there is a 10 percent chance they lose, they can't afford to spend more than a car.

But in arbitration, they can get awarded the fees of the dealership. So they have to risk losing everything they have, and they are in for paying large fees, and arbitration is often very expensive—$300 to $600 an hour. And the way I put it is, they are being asked to contribute to someone per hour, a fee equal to their car payment per month. This is outside of their area.

So there are firms like mine that will advance fees for consumers. It limits what cases we can take, and it leaves tremendous numbers of consumers begging for legal representation because the consumer can't pay the arbitration fee, and there is not a lot of lawyers who could afford to advance that without going broke and otherwise take those sorts of risks.

So this is why I say this denies access to people, it does not encourage it. And there is no rational base for saying it is cheaper. It flat out isn't.

Ms. SÁNCHEZ. Thank you. My time is expired, but Mr. Cannon has generously agreed to allow me to ask one last question, and it is also a question for you, Mr. Rosner.

Mr. Naimark has suggested that Congress incorporate into this legislation due process and procedural protocols which are aimed at protecting consumers. And my question for you is, are these protocols sufficient to actually protect consumers?

Mr. ROSNER. They really aren't. They are hard to enforce, they are hard to put down, but you can achieve his objective. If you make people have to enter into arbitration voluntarily and know-

ingly, then people won't enter into it unless you make the system fair.

So if you set up things like—I use core arbitration all the time; arbitration is not inherently bad. But if you take the first step, and make it knowing and fair. So if the consumer doesn't have to enter into it until the dispute arises, to where they haven't sat in a car dealership for 6 hours, if they want consumers to go to arbitration, if they present a fair system, then there may be the possibility of arbitration.

So the way to get the protocols isn't to try and make car dealers rewrite their contracts and create a huge board and bureaucracy, it is to create a knowing and fair system. And if people have to be knowing and voluntary, then you are going to have to be encouraged to create a fair system so they want to go. That is very American; it is the marketplace of ideas.

If you offer them a better alternative to the court system, they shall take it. But if you unilaterally impose it on the back of a huge contract or let the car dealers write the agreements—so let us use your legislation will result in these results without having to go through creating an unenforceable system. And these are good things that should happen; they are not happening, and if they do the car dealers won't use the system.

So we can achieve the results by making it knowing and voluntary. We are not saying no arbitration; we are saying knowing and voluntary.

Ms. SÁNCHEZ. Thank you. I think that is a very important distinction with respect to the legislation we are discussing today. I thank you all for your answers. And now I would like to recognize Mr. Cannon for 5 minutes of questions.

Mr. CANNON. Thank you, Madam Chair.

Thank you for being here, Ms. Shahan. You are sort of like this embodiment of this great hero in my life, and it is nice to know who you are and see you here. I think the Lemon Law was actually a remarkably good thing. And, by the way, did you call it the Lemon Law because you lived in Lemon Grove, which I always thought of as sort of a sweet place. I have a brother-in-law and sister-in-law who live there.

Ms. SHAHAN. I love Lemon Grove.

Mr. CANNON. It doesn't really relate to the fact that you buy a lousy car——

Ms. SHAHAN. That is right. The nomenclature came from the sour taste it leaves in people's mouths.

Mr. CANNON. Let me just ask one question, Mr. Rosner. If you essentially cost zero to your clients, do you tell them that they don't need to pay you for the filing fees, that sort of thing?

Mr. ROSNER. Yes.

Mr. CANNON. And California then, I take it, it is——

Mr. ROSNER. It is completely permissible. In California, to be honest, sir, after a few thousand cases I am a pretty good judge of how things will go in court. The results have been very—the same cases I have never lost in court I find myself losing in arbitration, but I pay everything.

Mr. CANNON. You are comfortable getting paid back for the risk, but you don't put that risk on the client, right?

Mr. ROSNER. That is correct, sir.

Mr. CANNON. Different laws, different states. It is an interesting fact.

I actually want to—I don't often do this, but I actually want to lecture here a little bit. And you guys are stuck, and I apologize—— [Laughter.]

The Chair has apologized twice to Ms. Rice for the problem that she has had, and on the other hand, you have Mr. Naimark, who talks about the cost of litigation and why it is not worth litigating. I personally have passed up a number of lawsuits in my life because I am not going to get paid back as much as it is going to cost me to do the litigation.

And I think there is a philosophical gap here that I think we ought to explore. I think the Chair would agree with me that the reason she apologizes to Ms. Rice is because she believes there is an obligation, by the system, to you as a person.

And I think that philosophy derives from a guy named Kant, who wrote a book called "The Social Contract," a French author some time back. And his premise was that society, as human beings, we owe each other something, and that is an attractive idea—I read the book when I was 18 or 19 and I was interested in the idea. And it is a good idea; I think that people do actually owe each other things.

The problem is, who gets to decide who owes what to whom? And that is the fundamental concept that we are actually dealing with here. This is a fundamental philosophical discussion, and I think it ought to be considered in the context of philosophy, because that allows us to make decisions, instead of in sympathy, in a context that allows us to create a system that actually works.

So, somewhere between your problem, which is very serious and a clear problem, and, for instance, Ms. Shahan's dramatic impact on the law by getting the California Lemon Law enacted, and Mr. Naimark's fairly dry and clear statement about the cost that we are incurring to society. I think were talking about philosophy and what we are doing that makes a big difference.

So if you say that we have an obligation to each other as individuals, that is like a good Christian, or Jewish, or Muslim, or any other kind of religious view that elevates our obligations to other people. If you say government should take a role, then you take an additional responsibility because government has to make decisions.

And, in fact, if we decide that you have been wronged and government should step in, then you might actually find yourself in a position where the government can reimburse you for the foulness of the dealer who cheated you. And that would be okay if God were the guy who was making those kinds of decisions, but to do that kind of a payment to you, you would need to take money from other people to make it available. And so the idea behind socialism is that there is force in government to take money and reallocate it.

And in fact, the recent debate between Senator Obama and Senator Clinton in Ohio—a large part of that debate was about which program required more force by government. And, a remarkable debate because in America, you see, we have never had success with

the Socialist Party, and a large part of the reason for that failure or success is that communism, which is just socialism with force, has had such an awful rap in the world today.

So as we look at these things, and I see my time is running; I am not going to go over that time. But what we are talking about here is how we use the system. In America we don't do socialism; in America we have what I like to call Anglo-American constitutionalism. We have a Constitution that has principles; we build a superstructure over that of law. And that way, it doesn't matter what your background is or your context is, whether you are a millionaire or a pauper, Ms. Rice, you get the same protection, theoretically, in front of the law.

And Mr. Rosner is absolutely right when he is thinking, and I know this is going through his mind, that people that are poor don't get the same kind of shake that people that are rich get. And that is a reasonable conclusion. And so our job is to create a system where people, regardless of their economic circumstances, their educational circumstances, their other inherent differences, have the same rights or the same opportunities, without saying we are going to substitute our judgment for a legal system and reach into some people's pocket and put it into other people's.

And in the end, that is what this bill is about. This bill that is before us is about how we reallocate resources in society to protect some. And I would just tell you, if you want protection from the government you ought to think twice. Because the people that end up being protected tend to be the elite, rich, the corporations that have vast resources, and they can use the law to benefit their interests and not others.

And so while I sympathize heavily, Ms. Rice, with your circumstance, I want a system that is most likely to create an environment where you are better served. And by the way, I think you should tell all your friends what a creep the guy was you bought the car from and tell them not to go there. And that is the ultimate defense, because creepy people do creepy things, and in our lives we have a choice of getting on with our lives or spending money. And I read part of—if you will allow me another moment——

Ms. SÁNCHEZ. If you would yield to me when you are done.

Mr. CANNON. Absolutely. Absolutely.

In your circumstance, you are facing the worst of all choices. You have got arbitration that costs a great deal of money; you hire a lawyer, it costs a lot of money. No lawyer is going to step in because of the legal context that you are in. You face some really ugly choices. And you end up saying to yourself, and I hate the fact that this is the case, but you say to yourself, "Look, how much is this lousy car going to cost me? What can I do with it? How do I get out of it? How can I get on with my life?"

Because you were talking about $1,800 or $1,300 a day, I think you said was the average cost. You know, it doesn't take many days before you say, "I am just going to pay this off, find a dealer I can trust, get a car that is reliable, and go on with my life." And the only alternative to that is to say, "I want the government to take care of it," and that comes with burdens and costs that I think that you probably are not ready to ask for.

And with that, I would be happy to yield.

Ms. SÁNCHEZ. Thank you. I would just like to make a couple of brief comments. Number one, my apology to Ms. Rice was for her having gone through such a bad experience. I am not assessing blame in her particular situation, but I can empathize with the idea of being excited about getting a brand new car, and then finding out that it doesn't function just minutes after you have driven it off the lot.

Secondly, with respect to some of the arguments that you were making, Mr. Cannon, about asking government to step in and who bears the cost. I don't think that we are asking government to reimburse Ms. Rice for her bad experience or for the lemon that she bought. We are certainly not asking taxpayers to come to her rescue and bail her out of what ended up being a very unfortunate circumstance for her.

I think what we are asking for is what Mr. Rosner said, is some fairness in a system, and not getting rid of arbitration, but merely making it a knowing, willing, informed, and voluntary decision on the part of a consumer, whether or not they choose to pursue what they think is their due in the arbitration system, or whether or not they choose to go the route of the traditional court system.

And I think that is what this bill ultimately is about, is ensuring that there are safeguards that people aren't reading or missing—that would be a better word, missing a mandatory binding arbitration clause in a lengthy contract that comes at the end of a very heavy negotiating session over price and mountains of paperwork.

Mr. CANNON. Reclaiming my time, let me just say that I agree with the gentlelady and that you explained your view and your nature of your apologies, I think, perfectly. I would only just add this, that our decision today is not a decision about solving Ms. Rice's problem; it is about solving a societal problem. We are in the position we are in because we have looked at the costs and the best ways to get to it over a very long period of time. And the bill that you have introduced fits within the structure of the Anglo-American constitutional system.

It is not a matter of, the bill you introduced is not a socialistic bill; I would not suggest that. But rather, I talked about Ms. Rice's circumstances to point out that what we are really doing in Congress is trying to create the system that is the most efficient for her and for other consumers to keep prices down, costs down, interest rates down, and give her the mobility to move back and forth between.

If you change the system and create another system, it may actually benefit Ms. Rice because she can go to Mr. Rosner and get a lawyer to work the system. But I believe, this is my personal belief in this regard, that that is not wise, because what it ends up doing is raising the cost to all consumers, because now lawyers can get all the complicated and expensive system in a way that they benefit an individual but costs the entire system a great deal more. That is the ongoing debate we have had about these arbitration clauses.

And with that, Madam Chair, I would be happy to yield.

Ms. SÁNCHEZ. Will you yield to me?

The only comment that I would have to your final concluding remarks is that, with respect to fixing Ms. Rice's problem and mak-

ing the system more expensive by allowing her to perhaps choose to go the traditional court system, perhaps what we will also do is with these dealers who are engaging in this practice find it is too expensive to continue to try to sucker people into buying bad cars. Maybe they will reform their behavior and actually sell the product that they are representing to the customer, that the customer wants to buy when the customer goes in and plunks down their money, and maybe we actually will get a change in behavior so that this doesn't happen on a widespread basis.

Mr. ROSNER. I would love a 1-minute response to Mr. Cannon's question on obligation if I—I don't know if that is asking for too much. Mr. Cannon asked, "Where is the obligation to this young lady?" if you would. The obligation is the Constitution of the United States, which had guaranteed her a right to a jury trial and to have her grievances heard. It is the government that took away that right through various arbitration provisions and put her into an unfair system.

The right, here, is to have compensation to her. In Ms. Shahan's testimony she talked about $10 billion consumers lose buying bad cars. We help the good car dealers if we go ahead and make the other car dealers pay the price for what they do. And as I point out in my testimony, the advantage of a court system is, one single lady, like I pointed out Rita Thompson, changed the way millions of cars are sold. That can't happen in arbitration, which cloaks everything in secrecy, which tells the car dealer, even if he loses a secret arbitration to her, it is profitable to keep doing it. So we protect society, and the cost is to the people doing the wrong where it should be.

Mr. CANNON. Reclaiming my time, and I hope this will be final. In fact, Mr. Rosner makes a very good point. I don't think that good car dealers would object to having bad car dealers driven out of business. But I think if you look at the overall system, the cost of litigation is much, much higher, and the effectiveness of telling your friends what a creepy dealer you went to is much better.

With that, Madam Chair, I yield back.

Ms. SÁNCHEZ. I thank the gentleman, and I want to thank, again, all of the witnesses for their testimony today.

Without objection, Members will have 5 legislative days to submit any additional written questions, which we will forward to the witnesses and ask that you answer as promptly as you can so that they can be made a part of this record as well. And without objection, the record will remain open for 5 legislative days for the submission of any additional material.

Again, I thank everybody on the panel for their time and patience, and this hearing of the Subcommittee on Commercial and Administrative Law is adjourned.

[Whereupon, at 10:27 a.m., the Subcommittee was adjourned.]

APPENDIX

Material Submitted for the Hearing Record

PREPARED STATEMENT OF THE AMERICAN FINANCIAL SERVICES ASSOCIATION (AFSA)

HOUSE OF REPRESENTATIVES
COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW

H.R. 5312, The Automobile Arbitration Fairness Act of 2008

Thursday, March 6, 2007

WRITTEN TESTIMONY OF
THE AMERICAN FINANCIAL SERVICES ASSOCIATION

The American Financial Services Association ("AFSA") thanks Subcommittee Chair Sanchez and the Subcommittee on Commercial and Administrative Law for holding this hearing and is pleased to provide its views on how H.R. 5312, *The Automobile Arbitration Fairness Act of 2008*, which will impact resolution of customer disputes. Although the Act is portrayed as simply returning "fairness" to the arbitration process, it would effectively abolish all pre-dispute arbitration agreements in the sale or lease of a motor vehicle contract.

AFSA, the national trade association for the consumer credit and finance industry, represents lenders that provide access to credit for millions of Americans. AFSA's 350 member companies include consumer and commercial finance companies, "captive" auto finance companies, credit card issuers, mortgage lenders, industrial banks, and other financial service firms that lend to consumers and small businesses.

Arbitration Overview

Arbitration is beneficial due to its affordability, accessibility and efficiency. Mandatory arbitration is a key tool in resolving customer disputes in a way that is fair and cost efficient for both the customer and the company. Arbitration organizations such as the National Arbitration Forum, the American Arbitration Association, and JAMS all conduct their proceedings according to well recognized and detailed procedural rules that allow for fair and timely consideration of the claims by experienced and impartial arbitrators. We firmly believe, and it is our experience, that arbitrations are fair and beneficial to borrowers who have meritorious claims, and that arbitration clauses do not deter such borrowers from pursuing their claims.

A recent Ernst and Young study showed, for example, that 55% of arbitrations that went to hearing were resolved in the consumer's favor; 79% of all arbitrations (including those that settled) were resolved in favor of the consumer; 69% of consumers surveyed indicated they were satisfied or very satisfied with the arbitration process. Numerous other studies have confirmed these results. A Harris Interactive poll in 2005 found that 75% of arbitration participants are satisfied with the fairness of the process and 74% with the fairness

of the outcome.[1] The Georgia State Law Review in 2003 found that 71% of individuals won claims against corporate entities before the National Aribitration Forum, compared to an individual winning less than 55% of claims brought against corporate entities in federal court.[2]

Most Americans welcome arbitration as an alternative to suing to settle disputes, according to a 1999 Roper Starch survey conducted for the Institute for Advanced Dispute Resolution and the National Arbitration Forum. The Roper poll found that 59% of Americans would choose arbitration over a lawsuit if the disputed amount of money were significant. When informed that arbitration would cost 75% less than a lawsuit, 82% of adults said they would opt for arbitration, according to the study.

Further, numerous courts have found arbitrations to be fair proceedings. The Maryland Court of Special Appeals in 2005 noted that the arbitration would likely be more expedient and less procedurally cumbersome for petitioners than would a circuit court trial.[3] The U.S. Supreme Court stated that national arbitration organizations have developed similar models for fair cost and fee allocation.[4] Finally, the Northern District of Texas Court of Appeals in 2000 stated they were "satisfied that NAF will provide a reasonable, fair, and impartial forum within which Plaintiffs may seek redress for their grievances."[5]

AFSA's Leaderships on Arbitration

In 2000, AFSA's member companies adopted a voluntary standard setting out certain arbitration guidelines to use when resolving borrower-lender disputes. The intent of AFSA's voluntary standard is to ensure all involved parties receive fair treatment throughout the arbitration process. The standard establishes the minimum expected from our members. We have encouraged companies to develop and implement additional mechanisms that support the standard's goal of an arbitration process free and clear of any bias and unfairness.

The standard outlines 14 core principles for AFSA companies to apply to their arbitration programs (also known as Alternative Dispute Resolution or ADR programs), along

with recommended procedures to implement each principle. Among the principles are: consumer access to full and accurate information about ADR programs; use of independent and impartial "neutrals" and independent ADR institutions; establishment of reasonable cost, location and time limits; and notification of participating parties about their right to representation and mediation. Also included is a call for lenders to provide "clear and adequate notice of the arbitration provision and its consequences, including a statement as to whether or not a provision is a mandatory or optional character."

The federal law governing the nation's arbitration system is the Federal Arbitration Act (FAA), which recognizes arbitration and establishes the "validity, irrevocability and enforcement" of arbitration agreements. AFSA's voluntary standard goes far beyond what's required by law and fills in many gaps left by the FAA, since it does not mandate detailed standards for conducting arbitration proceedings. A copy of AFSA's voluntary standard has been submitted along with this testimony.

H.R. 5312 Will Have a Detrimental Effect on Consumers and the Economy

There are several reasons why Congress should not pass this bill. First, the Act's overly vague language will introduce widespread uncertainty into the economy and the courts. Second, the Act would largely nullify the arbitration system for automobile sales or leases, even though proponents have failed to establish the need for this drastic action. Third, if the Act becomes law, it will eliminate any possibility that consumers will be able to obtain a remedy for the claims they are most likely to have—those involving individualized facts and damage less than $75,000. Last, the Act ignores the numerous existing protections against unfair arbitration provisions. We will elaborate on each of these points below.

In increasingly uncertain economic times, market liquidity is the key to lenders' ability to provide affordable credit to consumers. When credit is tight, the interest rates that lenders can offer consumers rise. After the credit crisis last August, many borrowers with less-than-perfect credit found getting an auto loan more expensive. However, the Federal Reserve Board's recent rate cuts have improved liquidity and made credit more affordable. Part and

parcel of maintaining liquidity is providing certainty to investors about the nature of the products to which they are committing their capital. Proposals to address the current economic conditions in the credit market that would impose the renewed threat of costly litigation by plaintiffs would force auto lenders to price for that risk. H.R. 5312, *The Automobile Arbitration Fairness Act* would do just that.

H.R. 5312 would leave automobile consumers in a no-win situation of either attempting to find a lawyer to file suit in court, or abandoning any realistic hope of resolving a dispute. The fact is plaintiffs' lawyers will not take a case without a certain level of expected recovery. One survey of plaintiffs' attorneys revealed a required minimum of $60,000 in provable damages, a retainer and required payment of a 35% contingency fee.[6] By another estimate a consumer would need to have a claim of at least $75,000 before litigation became cost-effective for an attorney.[7] Most automobile claims are far less than these figures, leading customers to search in vain for a lawyer. In addition, even when consumers do find an attorney, empirical evidence shows that the vast majority of filed lawsuits never make it to a trial, by jury or otherwise.[8] To the extent there is a problem, the data suggest that the problem is not a systemic one with arbitration but rather stems from difficulties that an individual encounters obtaining access to counsel in our civil justice system.

Amid the rhetoric and misleading assertions, the truth about arbitration has been obscured. But while opponents of arbitration are entitled to their opinions, they are not entitled to their own facts. Congress should not pass the proposed Automobile Arbitration Fairness Act (H.R. 5312) without considering the reality of how arbitration works.

Studies show that arbitrators are not biased, and safeguards, including strict disclosure requirements, protect against the risk of bias. Arbitration is usually less expensive than litigation for consumers and employees. Discovery limitations and the informal nature of arbitration make arbitration quicker and more accessible for consumers and employees. Arbitration agreements generally do not forbid a consumer from retaining counsel. Many arbitration agreements do require that disputes be resolved on an individual basis. The vast

majority of arbitration provisions do not require arbitration in an inconvenient location, and if forum-selection clauses are unfair, courts will refuse to enforce them.

The assumption that it is bad for arbitration to be confidential is flawed: many consumers in fact do not want their personal disputes and private information to become part of the public record. In any event, many arbitration agreements do not mandate confidentiality.

The FAA does permit appeals from arbitration awards in certain, albeit limited, situations. After a dispute arises, a consumer and a company will rarely agree to seek arbitration if they have not already agreed to do so. The FAA was not intended to apply only to sophisticated business-to-business contracts. It was specifically designed to include consumer contracts. Arbitration provisions are part of contracts that consumers and businesses freely enter into. Arbitration does not require consumers to give up the right to a trial by jury.

In conclusion, critics of arbitration assert that arbitration is broken—that is the premise that underlies the proposed Automobile Arbitration Fairness Act. Relying on anecdotes, the opponents of arbitration claim that arbitration is unfair, expensive, and biased in favor of companies. In light of the drastic changes that the Act would entail, the opponents of arbitration bear the burden of demonstrating that such changes are needed. When the data are examined, however, it is clear that arbitration's opponents have failed to make their case. Instead, studies show that arbitration is beneficial to consumers. It is cheaper than litigation and more likely to result in positive outcomes for consumers.

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[1] *Arbitration: Simpler, Cheaper and Faster Than Litigation*, Harris Interactive, 2005

[2] Eric J. Mogilnicki and Kirk D. Jensen, *Arbitration and Unconscionability*, 19 Ga. St. L. Rev. 764(2003)

[3] Walther v. Sovereign Bank, 386 Md. 412, 441-42 (Md. App. 2005)

[4] Green Tree Fin. v. Randolph, 531 U.S. 79, 95, n.2 (2000)

[5] Marsh v. First USA Bank, 103 F.Supp.2d 909, 925 (N.D. Tex. 2000)

[6] Elizabeth Hill, *Due Process at Low Cost: An Empirical Study of Employment Arbitration Under the Auspices of the American Arbitration Association*, 18 Ohio St. J. on Disp. Resol. 777 (2003)

[7] *Employment Arbitration: What Does the Data Show?, supra note 3; Michael A. Perino, Report to the Securities and Exchange Commission Regarding Arbitrator Conflict Disclosure Requirements and NASD and NYSE Securities Arbitrations 7 (Nov. 4, 2002), available at* http://www.sec.gov/pdf/arbconflict.pdf.

[8] Michael Delikat & Morris M. Kleiner, *An Empirical Study of Dispute Resolution Mechanisms: Where do Plaintiffs Better Vindicate Their Rights?* Disp. Resol. J. (Nov. 2003-Jan. 2004); see also 23-9 Insurance Times (Apr. 29, 2003)

AFSA Voluntary Standard on Alternative Dispute Resolution

In the event that a member adopts an Alternative Dispute Resolution (ADR) process, the following principles [1] shall apply:

PRINCIPLE 1. FUNDAMENTALLY FAIR PROCESS

All reasonable efforts shall be made to ensure that all parties are subject to a fundamentally fair ADR process. As embodiments of fundamental fairness, these Principles should be observed in structuring ADR Programs.

PRINCIPLE 2. ACCESS TO INFORMATION REGARDING ADR PROGRAM

Providers of goods or services should undertake reasonable measures to provide Consumers with full and accurate information regarding Consumer ADR Programs. At the time the Consumer contracts for goods or services, such measures should include (1) clear and adequate notice regarding the ADR provisions, including a statement indicating whether participation in the ADR Program is mandatory or optional, and (2) reasonable means by which Consumers may obtain additional information regarding the ADR Program. After a dispute arises, Consumers should have access to all information necessary for effective participation in ADR.

PRINCIPLE 3. INDEPENDENT AND IMPARTIAL NEUTRAL; INDEPENDENT ADMINISTRATION

1. Independent and Impartial Neutral. Independent and impartial neutrals shall be used in an ADR proceeding.

2. Independent Administration. If participation in mediation or arbitration is mandatory, the procedure should be administered by an Independent ADR Institution. Administrative services should include the maintenance of a panel of prospective Neutrals, facilitation of Neutral selection, collection and distribution of Neutral's fees and expenses, oversight and implementation of ADR rules and procedures, and monitoring of Neutral qualifications, performance, and adherence to pertinent rules, procedures and ethical standards.

3. Standards for Neutrals. The Independent ADR Institution should make reasonable efforts to ensure that Neutrals understand and conform to pertinent ADR rules, procedures and ethical standards.

4. Disclosure and Disqualification. Beginning at the time of appointment, Neutrals should be required to disclose to the Independent ADR Institution any circumstance likely to affect impartiality, including any bias or financial or personal interest which might affect the result

of the ADR proceeding, or any past or present relationship or experience with the parties or their representatives. The Independent ADR Institution should communicate any such information to the parties and other Neutrals, if any. Upon objection of a party to continued service of the Neutral, the Independent ADR Institution should determine whether the Neutral should be disqualified and should inform the parties of its decision. The disclosure obligation of the Neutral and procedure for disqualification should continue throughout the period of appointment.

PRINCIPLE 4. QUALITY AND COMPETENCE OF NEUTRALS

Competent, qualified Neutrals shall be used in an ADR proceeding. Independent ADR Institutions are responsible for establishing and maintaining standards for Neutrals in ADR Programs they administer.

PRINCIPLE 5. REASONABLE COST

1. Reasonable Cost. Providers of goods and services should develop ADR programs which entail reasonable cost to Consumers based on the circumstances of the dispute, including, among other things, the size and nature of the claim and the nature of goods or services provided. In some cases, this may require the Provider to subsidize the process.

2. Handling of Payment. In the interest of ensuring fair and independent Neutrals, the making of fee arrangements and the payment of fees should be administered on a rational, equitable and consistent basis by the Independent ADR Institution.

PRINCIPLE 6. REASONABLY CONVENIENT LOCATION

In the case of face-to-face proceedings, the proceedings should be conducted at a location which is reasonably convenient to both parties with due consideration of their ability to travel and other pertinent
circumstances. If the parties are unable to agree on a location, the determination should be made by the Independent ADR Institution or by the Neutral.

PRINCIPLE 7. REASONABLE TIME LIMITS

ADR proceedings should occur within a reasonable time, without undue delay. The rules governing ADR should establish specific reasonable time periods for each step in the ADR process.

PRINCIPLE 8. RIGHT TO REPRESENTATION

All parties participating in processes in ADR Programs have the option, at their own expense, to be represented by a spokesperson of their own choosing. The ADR rules and procedures should so specify.

PRINCIPLE 9. MEDIATION

The use of mediation is strongly encouraged as an informal means of assisting parties in resolving their own disputes.

SPECIAL PROVISIONS RELATING TO BINDING ARBITRATION

PRINCIPLE 10. AGREEMENTS TO ARBITRATE

Consumers should be given:

1. Clear and adequate notice of the arbitration provision and its consequences, including a statement of its mandatory or optional character;

2. Reasonable access to information regarding the arbitration process, including related costs and assistance as to where they may obtain more complete information regarding arbitration procedures; and,

3. A clear statement of the means by which the Consumer may exercise the option (if any) to submit disputes to arbitration.

PRINCIPLE 11. ARBITRATION HEARINGS

1. Fundamentally Fair Hearing. All parties are entitled to a fundamentally fair arbitration hearing. This requires adequate notice of hearings and an opportunity to be heard and to present relevant evidence
to impartial decision- makers. In some cases, such as some smaller claims, the requirement of fundamental fairness may be met by hearings conducted by electronic or telephonic means or by a submission of
documents. However, the Neutral should have discretionary authority to require a face-to-face hearing upon the request of a party.

2. Confidentiality in Arbitration. Consistent with general expectations of privacy in arbitration hearings, the arbitrator should make reasonable efforts to maintain the privacy of the hearing

to the extent permitted by applicable law. The arbitrator should also carefully consider claims of privilege and confidentiality when addressing evidentiary issues.

PRINCIPLE 12. ACCESS TO INFORMATION

Consumer ADR agreements which provide for binding arbitration should establish procedures for arbitrator-supervised exchange of information prior to arbitration, bearing in mind the expedited nature of arbitration.

PRINCIPLE 13. ARBITRAL REMEDIES

The arbitrator should be empowered to grant whatever relief would be available under applicable law.

PRINCIPLE 14. ARBITRATION AWARDS

1. Final and Binding Award; Limited Scope of Review. If provided in the agreement to arbitrate, the arbitrator's award should be final and binding, but subject to review in accordance with applicable statutes governing arbitration awards.

2. Standards to Guide Arbitrator Decision-Making. In making the award, the arbitrator should apply any identified, pertinent contract terms, statutes and legal precedents.

[8][1] These principles are intended to serve as minimum standards for ADR programs. AFSA members using ADR programs are encouraged to develop and implement processes which further the goal of ensuring fundamental fairness to all parties.

LETTER FROM THE ALLIANCE OF AUTOMOBILE MANUFACTURERS

March 14, 2008

The Honorable Linda Sanchez
Chairwoman
Subcommittee on Commercial and
Administrative Law
Committee on the Judiciary
United States House of Representatives
Washington, DC 20515

The Honorable Chris Cannon
Ranking Member
Subcommittee on Commercial and
Administrative Law
Committee on the Judiciary
United States House of Representatives
Washington, DC 20515

Dear Chairwoman Sanchez and Ranking Member Cannon:

The Alliance of Automobile Manufacturers and its ten member companies respectfully write in opposition to H.R. 5312, the Automobile Arbitration Fairness Act of 2008. We agree with the purpose of the legislation – to ensure that consumers are protected and have a means to address their grievances -- however, we are concerned that this bill would upend and replace longstanding consumer practices that enable consumers to obtain expeditious action on their complaints, in an uncomplicated fashion.

Proponents of this legislation have argued that the arbitration process provides businesses an unfair advantage and eliminates consumer due process within the legal system. Respectfully, we must strongly disagree. The reality is that arbitration has a proven track record of success and provides meaningful protections for consumers throughout the process. Neither "side" has an advantage, and neither side is disadvantaged. For example, studies of arbitration in California have shown that two thirds of all arbitrated disputes have resulted in awards favoring consumers. In addition, for those decisions that are adverse to the consumer, Section 2 of the Federal Arbitration Act permits courts to exercise their authority to review arbitration agreements for compliance with general state-law contract principles, including whether they are fair under state law. Furthermore, The American Arbitration Association has implemented a Consumer Due Process Protocol to ensure the fairness of consumer arbitration and strictly enforces arbitrator qualifications and neutrality. As a result, we believe the current system works, and provides the types of checks and balances that are needed to ensure a fair process.

Arbitration was created and implemented to provide both buyers and sellers expedited solutions to non-intense disputes, and at a reasonable cost to both sides. Arbitration minimizes protracted, expensive legal battles, and provides consumers with relatively immediate results.

As leaders in the community and on Capitol Hill, we urge you to reconsider such legislation. We stand ready to assist you in your efforts to ensure that both consumers and businesses in your districts and throughout the country are protected.

Sincerely,

Shane Karr
Vice President, Federal Government Affairs
Alliance of Automobile Manufacturers

Responses to Questions for the Record
Regarding HR 5312, The Automobile Arbitration Fairness Act
Hearing before Committee on the Judiciary
Subcommittee on Commercial and Administrative Law
March 6, 2008

Provided by
Witness Rosemary Shahan, President
Consumers for Auto Reliability and Safety

Responses to Questions for the Record
From U.S. Representative Linda T. Sanchez, Chairwoman
Subcommittee on Commercial and Administrative Law

1. **If arbitration truly benefits businesses as you and other consumer advocates have claimed, then would not those benefits apply equally to voluntary, post-dispute arbitration systems? Would not the costs of arbitration be the same whether the agreement to arbitrate was entered into before or after the dispute arose?**

Mandatory arbitration unfairly benefits businesses because they choose arbitration firms that favor them and disadvantage consumers. If consumers are given a choice, after disputes arise, they will have at least some opportunity to avoid the current pitfalls, such as excessive secrecy, limited discovery, pay-to-play rules, loser-pays rules, an arbitrator chosen by the opposing party, and virtually no appeal to a real court. Instead, consumers would be free to select fairer systems, which would not benefit businesses as much as firms chosen by businesses specifically because they are biased in their favor.

Setting aside the fact that the results would be fairer, overall operating costs may be roughly the same. Businesses' insistence on mandatory pre-dispute arbitration is not really about the cost and efficiency of the dispute resolution process itself, but about other goals entirely--namely, forcing consumers into a system that insulates them from effective enforcement of consumer protection laws.

2. **Witnesses from our previous hearings on arbitration have testified that the Federal Arbitration Act preempts state provisions that attempt to protect their residents from binding mandatory arbitration clauses. Would you please provide us with some examples of what states have tried to do to**

address the problem of binding mandatory arbitration and the result of those attempts?

In 2004, California legislators considered AB 2656, The Car Buyer's Legal Equality Act of 2004, authored by former Assemblymember Hannah-Beth Jackson. It would have ensured that consumers who enter into agreements with franchised auto dealers, to waive rights or procedures under state laws, do so voluntarily. It would also have deemed any agreement to waive rights under state law that was not knowing and voluntary to be unconscionable, against public policy, and unenforceable.

Opponents argued that AB 2656 was preempted by the FAA. While the author and proponents disagreed, it ultimately failed to pass. The defeat of AB 2656 makes it all the more important for Congress to assert its leadership on this issue. Taking at face value opponents' argument that states' hands are tied, they themselves make the case that it is entirely up to Congress to act.

3. **Opponents of this legislation may argue that state laws already exist to protect consumers and therefore this bill is unnecessary. Are these state laws sufficient or do we still need enactment of this legislation?**

This legislation is desperately needed to restore the ability of consumers to enforce their rights under the existing state and federal laws. Otherwise, dealers will continue to be permitted to ignore the laws, secure in the knowledge their victims lack recourse to a court of law where those laws may be applied.

4. **Would you provide statistics, if any, concerning the percentage of retail installment contracts in motor vehicle purchases and leases which contain arbitration clauses?**

It is CARS' understanding that lenders demand the inclusion of binding mandatory arbitration clauses, and that nearly all dealers now include them in their contracts of adhesion.

Responses to Questions for the Record From Ranking Member Rep. Chris Cannon

1. **The stability and efficiency of arbitration as a dispute resolution option helps keep car sales and lease prices down. Don't lower prices help your consumer constituents?**

On the contrary, allowing unscrupulous auto dealers to impose mandatory pre-dispute binding arbitration on their victims makes it easier for crooked car dealers to violate federal and state laws, costing consumers billions and exposing them to unsafe, seriously defective vehicles with little real recourse. This raises the price of car purchasing, instead of lowering it.

This question assumes that arbitration is cheaper and more efficient than litigation. However, in reality, arbitration is often far more expensive. For example, consumers typically pay a one-time filing fee of less than $400 in court, but arbitrators charge filing fees ranging between $1,750-6,000, then charge several other fees throughout a proceeding, plus steep fees for the arbitrators' time. *See* Public Citizen, *The Arbitration Trap*, 34–37, available at:

http://www.citizen.org/documents/Final_wcover.pdf.

Therefore, in addition to reducing quality by making it easier for car dealers to violate the law, mandatory pre-dispute binding arbitration actually raises prices, forcing consumers to pay more for less.

2. **Consumer groups like yours are ideally situated to arm consumers with education about how to negotiate better deals and protect themselves from abuse. Why doesn't your organization do more to promote those efforts, rather than try to eliminate dispute resolution choices?**

With all due respect, this question misrepresents both HR 5312 and CARS' position. HR 5312 does not "eliminate dispute resolution choices." Exactly the opposite. HR 5312 frees consumers to choose where to have their dispute resolved, in court or in arbitration, after a dispute arises. Thus, it expands the options available to consumers.

Regarding providing education for consumers, CARS continues to work to educate the public about how to avoid common auto dealer scams, including generating news reports in major media that reaches millions of consumers. We also provide information on our website. Of course, the best way to avoid auto dealer scams is to purchase used vehicles from legitimate individuals, and never set foot on a dealer's lot. More consumers are choosing that option, particularly as consumer confidence in the automotive market and overall economy declines. (Of course, this is not possible with new vehicles, due to auto dealers' monopoly.)

One of the challenges consumer groups face, when we attempt to educate the public about how to avoid dealer scams, is that auto dealers and manufacturers are notorious for pulling their ads in retaliation for even the most mild, totally legitimate criticisms of their practices. For example, auto dealers in the San Jose pulled over $1 million in ads from the *San Jose Mercury News*, after that paper published a quite innocuous report with advice for car buyers. General Motors and its dealers pulled approximately $10 million in ads from the *Los Angeles Times*, after that publication criticized GM products and a GM executive. Auto interests pulled ads from the *Orange County Register* in retaliation for a series of articles that exposed discriminatory and illegal practices that led to appropriate action by law enforcement officials including license revocation. Auto interests also pulled ads from a Los-Angeles area TV station after it ran a series exposing practices that

led to criminal convictions of numerous dealership employees and suspension of the dealership's license, as well as millions in restitution for victims.

Surveys of news media organizations have found that consistently, auto interests are by far the worst in exerting advertiser pressure in an effort to censor the news. Recently auto interests reportedly complained when comedian Jay Leno merely mentioned a product purely in jest.

It is quite hypocritical for auto dealers to claim that public education is the sole solution, then bludgeon news organizations for providing solid, accurate information and advice.

Rather than try to eliminate arbitration options and deliver consumers into the hands of congested courts and trial lawyers, why doesn't your organization join with organizations like the AAA to promote fairer arbitration clauses and practices?

With all due respect, this question misrepresents both HR 5312 and CARS' position. HR 5312 frees consumers to choose where to have their dispute resolved, in court or in arbitration, after a dispute arises. It does not eliminate arbitration options. On the contrary, it expands the options available to consumers.

This question mistakenly assumes that parties to arbitration cannot hire lawyers –which would make binding pre-dispute mandatory arbitration even more unfair to consumers than it already is. It also wrongly assumes that consumers do not *want* lawyers to represent them in legal proceedings. Virtually everyone in a legal dispute is better off with legal representation than without. In courts, consumers who would otherwise not be able to afford a lawyer can often retain one on a contingency basis, with the consumer paying little or nothing unless he or she wins. In contrast, binding pre-dispute mandatory arbitration often forecloses this possibility with "pay-to-play" rules that require consumers to pay hefty expenses throughout the proceeding, and sometimes even loser-pays rules that require consumers who lose to pay the other side's costs. This substantially increases the costs and risks for consumers.

CARS believes that when consumers regain their lost freedom to choose the forum they prefer, market forces will promote fairer arbitration clauses and practices. More importantly, victims will regain their ability to protect themselves against unscrupulous auto dealers, helping deter widespread fraud and predatory practices from occurring in the first place.

3. **Don't you agree that if more dispute resolution services and providers are available to consumers, the costs of dispute resolution will go down? Isn't that good for consumers?**

While the imposition of binding mandatory arbitration has expanded rapidly in recent years, there is no evidence that it has become more affordable. This question appears to assume that arbitration costs would go down as a result of increased competition among

arbitration providers. Competition among arbitration providers influences arbitration procedures and costs, but this competition cuts against consumers, not for them. Businesses that force consumers into arbitration get to choose the arbitration firms. Therefore, arbitration firms compete to please businesses, not consumers – and they do so by making arbitration more onerous and costly for consumers.

It is important to keep in mind that consumers already pay for a system to provide them with a fair, just resolution---in the form of taxes, to support the judicial system. When dealers impose binding mandatory arbitration on their victims, that not only wastes those tax dollars by denying consumers access to the process they have already paid for, it also imposes a "mandatory arbitration tax" in the form of added costs borne by consumers who are compelled to submit to privatized, rigged processes chosen by the wrongdoers.

RESPONSES TO POST-HEARING QUESTIONS FROM ERIKA RICE, ARCANUM, OH

Erika Rice

1. Please describe where in the litigation process your case currently resides:

My case is still pending in Indiana court of law, we had a hearing on March 20th or so to determine if I was bound to arbitration. The other attorney produced the original top copy of the contract that I had signed that "mysteriously" had the arbitration box checked, when my carbon copy does not have the box checked, the judge said that he would decide this month if I was bound to arbitration. We still don't know as of today's date.

How likely will your current attorney represent you if you have to arbitrate your claims?

My attorney accepted my case because she thought that I have a good argument against the enforceability of binding arbitration. She was aware of the arbitration clause upon receipt of my paperwork. She would not have taken my case if she thought there was a strong chance I would be forced to arbitrate.

2. Automobiles are important to many individuals who must drive to work, to the doctor, to drop off their children at school. What impact did the loss of your vehicle have on your lifestyle and your family? Please explain and provide examples if any.

When we bought our rebuilt wreck in November of 2006, we traded in a good sound car. We were then given a loaner while the car we had bought was in the shop, after they returned the car to our house and took the loaner back, we parked the rebuilt wreck because we do not feel safe driving it and because of issues with the reliability of the vehicle. Therefore, we are forced to have two cars. I had to purchase another car so that I could get to work and take care of our family and so that my husband could get to work as well. Therefore, I had/have two cars on my credit report, which really screws up my income to debt ratio not to mention my credit as the financial company of the car we bought from the dealership was reporting negative information, when they weren't supposed to report any negative information regarding the account per their agreement with my attorney. It is very important for us to have a safe, reliable car since we have two small children. *Also, in my job as a case manager, I do home visits, school visits, etc, and it is very important for me to have a reliable car. If I don't, than I cannot do my job and my family cannot count on me.*

My response to questions from Congressman Cannon,

1. **If you did not check the box on your contract that pertained to the arbitration clause, don't you think you'll be able to prevail in court, and stay out of arbitration?**

I would have liked to think that we wouldn't have had to go to court at all. I gave the dealership plenty of time, more than a year, to simply put me back in the position I was in before I ever

walked into their dealership. I gave them a month before I even sought legal counsel and I communicated my issues with the car they had sold me and how they could make it right to both the dealership and the corporation. I also warned them that if they were not going to fix the issue, I was going to seek legal counsel. Yet, they did NOTHING. I did not check the box on my contract, and neither did they. However, at the time of the most recent hearing on my case, the attorney for the dealership produced a contract where the box WAS checked, which is impossible, since my copy is a carbon copy and it is NOT checked. I wish it was as simple as the box wasn't checked, so I'm not bound to arbitration, however, over a year of legal battling over JUST the arbitration issue has proved otherwise.

2. **If the court doesn't decide the case in your favor, why would you think you'd ever be better off in a court than in arbitration?**

I tried to resolve this matter informally. The dealership forced me to seek legal recourse. I never agreed to arbitrate. When I learned that the dealership lied to me, and sold me a rebuilt wreck, they added insult to injury and tried to strip me of my constitutional right to have a jury hear my case. The thing about arbitration, is that in theory, it is a great idea. However, it has some serious flaws. This car dealership uses an arbitration company many times, which makes the arbitration company money, which in turn, the arbitration company knows that good business is to keep business which is repeat business. Arbitration is essentially paid private judging, and not an unbiased system, like a court of law. Why would a dealership want to return to an arbitration company who when it is in the interest of the consumer, rules in favor of the consumer? As a matter-of-fact, the dealership counsel in my case said the dealership representative stated that "our worst day in arbitration was better than our best day in court."

The bottom line for me, in regards to this situation, is that I never wanted to be involved in a court, let alone an arbitration. If I could go back and change things, I would have never walked into that dealership. But my rights shouldn't be taken away and a jury of my peers should get to say whether or not the car dealership has behaved negatively and done me wrong, not some lawyer or judge who is acting as an arbitrator on the side making $200-$400 dollars an hour.

3. You've had one unpleasant experience with one dealer, with whom you believe you did not contract for mandatory binding arbitration. I understand how you feel about your transaction, but how does that one experience give the United States Congress a sufficient basis to climate mandatory binding arbitration for every auto sale or lease in the country?

Congressman Cannon, to answer this question quite simply, the dealers wanted and won having mandatory binding arbitration banned from their contracts with the manufacturers. How is it fair that we, the consumers, the public, who actually KEEP the economy going, have our rights taken away from us? I think that arbitration could be a great thing, if it is something that a consumer understood, had a choice about, and knowingly agreed to; not something hidden in fine print that they learned about for the first time after their problem arose and the dealership refused to stand behind its promises, not forced into. I think that this could keep businesses from

conducting bad business as well, which would further help the economy.

4. An abundant body of evidence tells us that many consumers across the country have had a positive experiences in arbitration, including mandatory binding arbitration, and are satisfied with its results. Knowing that, do you think we should deny all auto sales and lease customers the same possibility of obtaining faster, cheaper, better results than can be had in court?

As far as I know there is nothing in the proposed legislation that would prevent a consumer from entertaining informal dispute mechanisms, such as arbitration if the parties felt it would hasten a resolution after the dispute arose. Again, this should be a choice, not part of form contracts drafted in fine print by the dealership, to which the consumer has no understanding. In all respect, Congressman, I would love to see this abundant evidence, as far as I can see and research, nothing points to what you have stated and there is probably abundant evidence to the contrary as well.

What is the measure of a "better" result? A consumer lied and defrauded would prefer a fair result than a fast, cheap one. After all, it is the consumer who is stuck with the defect-ridden vehicle during the legal process. In regards to denying all auto sales and lease customers the same possibility of obtaining faster, cheaper, better results than can be had in court? I think what you meant to state is ***denying all auto dealerships, not consumers faster cheaper, better results****. What's good for the goose is good for the gander, correct? So why can't consumers have the same protection as the dealerships in regards to mandatory binding arbitration. The key word there is MANDATORY. Let the consumers agree to this and make the decision on their own, just as the dealerships can do.*

RESPONSES TO POST-HEARING QUESTIONS FROM RICHARD NAIMARK, SENIOR VICE PRESIDENT, AMERICAN ARBITRATION ASSOCIATION, WASHINGTON, DC

RESPONSES FOR THE RECORD
FROM RICHARD NAIMARK, THE AMERICAN ARBITRATION ASSOCIATION

QUESTIONS FROM THE HON. LINDA T. SÁNCHEZ, CHAIR
SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW
COMMITTEE ON THE JUDICIARY
UNITED STATES HOUSE OF REPRESENTATIVES

SUBCOMMITTEE HEARING HELD ON MARCH 6, 2008

Question 1: In your written statement for the hearing, you indicated that "any legislation to address consumer arbitration issues should not amend the Federal Arbitration Act." Is it safe to assume that AAA's opposition to H.R. 5312 is strictly because of what is amended and not the objective of the bill? If not, please explain.

Answer: The AAA opposes legislation that would amend the Federal Arbitration Act (Chapter 1 of Title 9 of the U.S. Code). Since initial passage in 1923, the Federal Arbitration has formed the basis of the vast majority of business-to-business, international, and other types of arbitration. What is more, the shaping of the Act has been consistent with international standards of practice in arbitration, making the U.S. a jurisdiction successfully aligned with this predominant cross border system of justice. Amending the FAA, even for laudable objectives, could have severe unintended consequences.

As noted in our testimony, the 2002 automobile dealer legislation amended the Dealer Day In Court Act (15 USC 1226). So too can H.R. 5312 achieve its objectives without amending the Federal Arbitration Act. In fact, appending consumer protections to the 2002 amendments to the Dealer Day in Court Act might be seen as particularly apropos.

Nevertheless, the AAA does not believe the approach taken by H.R. 5312 is the most effective means to enhance consumer protections. We have for years recommend codifying a series of concrete due process and procedural requirements to ensure fairness in arbitration contracts imposed on consumers. These provisions should parallel the protections and standards articulated in the *Due Process Protocol for Mediation and Arbitration of Consumer Disputes*, developed a decade ago by the National Consumer Disputes Advisory Committee.

Question 2: You suggested in your written statement for the hearing that H.R. 5312 should incorporate "concrete due process and procedural requirements to ensure fairness in arbitration contracts imposed on consumers." How would these suggested requirements ensure that costs to arbitrate are not prohibitively high for consumers? And ensure that parties receive full discovery to prepare for a fair and open arbitration proceeding?

Answer: Under the AAA's arbitration rules for consumer disputes, the maximum cost to the consumer is either $125 (for claims/counterclaims of up to $10,000) or $375 (for

claims or counterclaims above $10,000 but not exceeding $75,000). These amounts are to pay for a portion of the arbitrator's compensation. The consumer is not responsible for any AAA filing fees – these costs, as well as additional arbitrator compensation costs, are the responsibility of the non-consumer party. The non-consumer party is responsible for payment of AAA filing and case service fees.

For amounts above $75,000, the AAA's standard commercial rules and fee schedules would apply. In the context of consumer automobile purchase and lease transactions, the vast majority would likely fall under the consumer rules, given the cost of most automobiles.

While the AAA has taken a leadership role in limiting costs for consumer disputes, our actions have been entirely voluntary and have not necessarily been mirrored by other ADR providers. Congress can look to our consumer rules, as well as the relevant Protocols, to design mandatory standards that would ensure costs to arbitrate are reasonable for consumers.

Question 3: Mr. Rosner mentioned in his written statement for the hearing that JAMS has already been eliminated as an option from motor vehicle arbitration clauses because it had attempted to create a fairer playing field for consumers. Apparently AAA may be excluded as an option too, in favor of the National Arbitration Forum. If Mr. Rosner is correct, does this not show that H.R. 5312 is necessary litigation to ensure a level playing field for consumers?

Answer: What this indicates is a need for the current voluntary standards to be made mandatory. The Consumer Due Process Protocol was developed a decade ago by the National Consumer Disputes Advisory Committee, which included consumer advocates, government representatives, and other interested parties. Codification of these standards would ensure a level playing field while preserving arbitration as a viable option.

Question 4: Mr. Rosner describes a story about Rita Thompson, an individual who purchased a used mobile home, not knowing about the many problems with it. Ms. Thompson was able to take her case to court and won, with the result that dealers across the country now have to show the negative equity on contracts for trade-ins, which protects both consumers and lenders. How would allowing mandatory binding arbitration in motor vehicle purchase or lease contracts protect the public, in the same manner as Ms. Thompson's lawsuit, when arbitration decisions are often secretive and do not provide injunctive relief?

Answer: With respect to an arbitrator's authority, under the AAA's consumer rules, "The arbitrator may grant any remedy, relief or outcome that the parties could have received in court." While the authority of an arbitrator may vary from state to state, generally an arbitrator may enjoin either party to a dispute in the same manner as a judge. The AAA also publishes information on consumer cases, including information on the parties, relief, and other relevant data.

Similarly, Rule 34 of the AAA's Commercial Rules, which apply to many consumer arbitrations, arbitrators are explicity authorized to provide for injunctive relief."

Cases administered by the AAA are provided with confidentiality on the part of the arbitrator and the AAA as administrator. Unless the parties have otherwise agreed (through, for example, a nondisclosure agreement), no such confidentiality requirement applies to the parties themselves. A major exception to the AAA's confidentiality is the publication of extensive information on consumer cases, as required under California law. Further, the AAA publishes information required under California law for all consumer cases throughout the United States.

Similarly, a relatively new development related to alternative dispute resolution in the consumer arena is the advent of class action arbitrations. In response to a 2003 decision by the United States Supreme Court, the AAA developed its *Supplementary Rules for Class Arbitration.* A component of the Class Arbitration Rules is the creation of a class arbitration docket, where briefs, awards and other information about the AAA's class actions is publicly available on the internet.

Court rulings on the arbitrability of injunctive claims have been mixed, with some finding that injunctive claims are severable from other aspects of the consumer's claim.

Question 5: An argument that dealers and their lenders offer is that mandatory binding arbitration agreements are a defense against litigation and therefore keep costs down for them. How neutral are mandatory arbitration agreements if such clauses are seen as a defense to lawsuits? And may not this "defense" argument have a chilling effect on consumer protection?

Answer: Arbitration can be less expensive than litigation. With appropriate due process protections and cost limitations on the consumer party, as required by the AAA under its consumer rules, the reduced cost can benefit all parties to the dispute. Also, it should be noted that the AAA's consumer rules allow the consumer to "opt-out" and seek relief in a small claims court for disputes or claims within the scope of its jurisdiction, even in consumer arbitration cases filed by the business.

A preliminary analysis of the 198 cases filed in 2007 with the AAA involving consumers and car dealers yields some important information:

- 78% (174) of these cases were filed by the consumer
- 65% of cases filed by the consumer resulted in the consumer receiving a favorable outcome (monetary award or settlement)

These figures, combined with the reasonable total maximum costs for the consumer under the AAA consumer rules ($125 or $375, depending on the amount of the claim), show that arbitration can be a fair, fast, and cost-effective mechanism for consumers to resolve their disputes.

Question 6: How can AAA, or other arbitration groups, ensure that the costs of proceeding with arbitration are in fact lower for consumers, such as Ms. Rice, than using the traditional court system?

Answer: Two mechanisms help ensure costs to the consumer are reasonable: first, the caps imposed by the AAA's consumer rules on the consumer's share of costs of arbitration ($125 or $375), and second, the inherent efficiencies of alternative dispute resolution.

Question 7: Does AAA or any other arbitration group keep statistics on the number of claims it has arbitrated involving motor vehicle purchases or leases? If yes, please provide a breakdown of the statistics including the results of arbitration decisions, year, and any other pertinent information.

Answer: The AAA maintains and publishes on its website (www.adr.org) information on all consumer cases nationally, based on the standards and requirements of California law. As noted above, a preliminary analysis of 2007 data indicates that 198 cases involving consumers and car dealers were filed with the AAA. Of these, 78% were filed by the consumer, and in 65% of those cases, the result was an outcome favorable to the consumer.

Information published by the AAA for consumer cases include the following data when available:

- Name of Non-Consumer Party
- Type of Dispute
- Salary Range (reported only on employment cases)
- Prevailing Party (as reported by arbitrator)
- Consumer Self Represented (indicates whether the consumer represented himself or herself in the arbitration proceeding)
- Filing Date
- Disposition Date
- Type of Disposition (Awarded, Settled, Withdrawn)
- Amount of Claim
- Total Fee (total amount of arbitrator's fees and expenses charged on the case)
- Fee Allocation (percentage of the Total Fee borne by the consumer and non-consumer parties)
- Name of Arbitrator
- Award Amount (monetary amount awarded on the claim, if any)
- Other Relief

RESPONSES FOR THE RECORD
FROM RICHARD NAIMARK, THE AMERICAN ARBITRATION ASSOCIATION

QUESTIONS FROM THE HON. CHRIS CANNON, RANKING MEMBER
SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW
COMMITTEE ON THE JUDICIARY
UNITED STATES HOUSE OF REPRESENTATIVES

SUBCOMMITTEE HEARING HELD ON MARCH 6, 2008

Question 1: In other contexts, the market has witnessed the voluntary evolution of more and more "fair clauses," which include due-process-like protections such as those you advocate. Please explain what the benefits would be of fostering voluntary movement in this direction in the automobile sale and lease sector, rather than imposing a legislative mandate that could shut off further innovation.

Answer: It is true that legislative mandates can create a static environment that does not encourage evolution regarding the further development of fairness standards in arbitration. However, the AAA believes that concrete due process and procedural requirements to ensure fairness in consumer arbitration agreements should be codified through legislation at the federal level. These provisions should be modeled on the protections and standards articulated in the *Due Process Protocol for Mediation and Arbitration of Consumer Disputes*, developed a decade ago by the National Consumer Disputes Advisory Committee. These would be minimum standards, and should not prevent further voluntary evolution of practices that would contribute to fair and efficient arbitration procedures being made available to consumers.

Question 2: Could you please explain in more detail why you believe the H.R. 5312 should not attempt to amend the Federal Arbitration Act?

Answer: The AAA strongly opposes legislation that would amend the Federal Arbitration Act (Chapter 1 of Title 9 of the U.S. Code). Since initial passage in 1923, the Federal Arbitration Act has been considered the cornerstone business-to-business, international, and other types of arbitrations. In addition, the shaping of the Act has been consistent with international standards of practice in arbitration, making the U.S. a jurisdiction successfully aligned with this predominant cross-border system of justice. Amending the FAA, even for laudable objectives, could have severe unintended consequences. For example, the United States could become known as a jurisdiction that is hostile to arbitration, and as a result, American companies entering into agreements with foreign corporations could be disadvantaged as they attempt to negotiate issues such as the applicable law and the venue that would govern a dispute.

Question 3: Do you believe that market incentives for auto dealers to keep customers happy and returning for business, especially in the lease sector, should significantly dampen the potential for auto dealers to abuse mandatory arbitration clauses?

Answer: While the AAA does not have the expertise to comment on the nature of the exact relationship between automobile dealers and their customers, it is certainly the AAA's observation that whenever parties anticipate having an ongoing business or other type of relationship, they will work hard to minimize and contain disputes among them. Consequently, if automobile dealers have a substantial interest in maintaining positive and ongoing customer satisfaction and relationships, then it would be fair to assume that automobile dealers would also want to ensure that the agreed upon dispute resolution procedures are also viewed as fair by customers.

Question 4: Do you have any evidence that auto dealers tend to abuse mandatory binding arbitration clauses, rather than make fair and appropriate use of them?

Answer: The AAA can only address cases in which it is involved. Because the AAA conforms to the *Consumer Due Process Protocol*, declines to administer arbitrations arising out of agreement that do not comply with that Protocol, and has developed rules to ensure fair play and limit the costs to consumers, those who seek to abuse the process are unlikely to name the AAA in their contract provisions.

Question 5: Does the AAA have means already at its disposal to assure that procedures such as those in the Due Process Protocol are used in mandatory binding arbitration in the auto sales sector?

Answer: The AAA already implements the *Consumer Due Process Protocol* in cases between automobile dealers and their customers. The AAA provides extensive information on alternative dispute resolution, especially with regard to consumer cases. The AAA developed its consumer rules to ensure fairness for consumer cases, and requires parties to conform to these rules if a case is filed that fits our definition of a consumer dispute. If a party refuses to conform to the rules, our only option is to refuse to administer the case.

Question 6: Do you know whether the availability of arbitration in the auto sales sector tends to lower auto purchase and lease prices?

Answer: The AAA has no data on this. In general, alternative dispute resolution provides a fast and cost-effective alternative to litigation, but we do not have any means to develop objective data with regard to this sector.

RESPONSES TO POST-HEARING QUESTIONS FROM HALLEN D. ROSNER, ROSNER & MANSFIELD, LLP, SAN DIEGO, CA

United States House of Representatives
Committee on the Judiciary
Subcommittee on Commercial and Administrative Law

Honorable Linda Sanchez, Chairperson

April 14, 1008

Answers to Supplemental Questions

by

Hallen D. Rosner
Partner, Rosner & Mansfield, LLP
[With assistance from Cecilia Brennan, Associate at Rosner & Mansfield, LLP;
also on Behalf of National Association of Consumer Advocates]

In Support of Passage of H.R. 5312 The Automobile Arbitration Fairness Act

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Questions for Hal Rosner
From Linda T. Sanchez, Chair

1. In her written testimony Ms. Shahan noted that the National Highway Traffic Safety Administration has just a handful of staff to investigate odometer fraud. How does allowing consumers the opportunity to file a complaint in court further the interest of the Federal Government in stamping out odometer fraud, and other illegal actions by dealers?

American consumers purchase more than 57 million vehicles a year, as set forth in Ms. Shahan's testimony. The Federal Government lacks the staff and resources to police those transactions, and relies heavily on private litigation to rein in and deter predatory practices against consumers, including engaging in odometer and salvage frauds. A fundamental difference exists between filing a complaint in court and private arbitration. Complaints in court are public records, easily accessible to other litigants and both state and federal entities. Injunctions can be obtained in court proceedings to stop illegal conduct, as well as penalties imposed to deter such acts. A dealer in a court proceeding may have to face members of the community in a jury trial and the result of such trials are well-published. All of this creates deterrence and stops repeat offenses.

Arbitrations, by comparison, are highly secretive, with no public record and more limited remedies; for example, injunctions are not available in the arbitration process. Further, the people who make their money doing arbitrations often know that a negative result for the auto industry, or even awarding a penalty, means the end of their livelihood. If all a dealer faces is a secretive, non-public action without penalties, it is simply good business to keep cheating people. [My thanks to Rosemary Shahan and Martin Anderson, a California attorney, for their assistance with this answer.]

2. What remedies do automobile purchasers lose when they have to argue their claim in arbitration?

Automobile purchasers may lose ALL of their remedies when they are forced into binding mandatory arbitration ("BMA"). Dealers contract with biased arbitration companies who cater to them. The arbitration agreements and/or the rules of the arbitration company may limit and exclude remedies. They may also both limit the right for consumers to win attorney fees and costs while creating risk to consumers of having to pay the car dealers fees and costs if they lose. As arbitrations are very expensive, this has a number of effects. Consumers are intimidated into taking no action at all because of the risk. Further, because attorneys may not get paid and because they view arbitration as a rigged game, they are less likely to take cases where contracts contain arbitration clauses. As mentioned in response to your first supplemental question, injunctions cannot be obtained in arbitration. Furthermore, for all practical purposes, penalties/punitives are nonexistent or very limited.

3. How common are binding mandatory arbitration clauses in automobile purchase agreements?

The use of arbitration clauses in purchase agreements is moving from over 75% towards 100%. The lending institutions have for years used arbitration clauses to cheat and abuse consumers and are now insisting as a condition for financing that such clauses be in all contracts. In California, virtually all dealers use the Reynolds and Reynolds LAW form for vehicle sales. The LAW 533-CA-ARB form contains a standard arbitration form. [Martin Anderson as well as John Hanson from my office contributed to this response.]

4. You stated in your written statement that the Federal Arbitration Act preempts state provisions that attempt to protect their residents from binding mandatory arbitration clauses. Please provide us with some examples of what states have tried to do to address the problem of binding mandatory arbitration and the result of those attempts.

I asked for comments on this question, and attorneys across the country agree that the Federal Arbitration Act ("FAA") has stopped states trying to help consumers from being forced into unfair binding mandatory arbitration. This has happened either through court rulings, or through state legislation being stopped because it would be a waste of time, *i.e.* where it would be preempted. For example, Ray Johnson, an attorney from Iowa, wrote me that Iowa had passed a law prohibiting mandatory pre-dispute arbitration clauses in adhesion contracts. However, in *Heaberlin Farms, Inc. v. IGF Ins. Co.*, 641 N.W.2d 816 (Iowa 2002), the Iowa Supreme Court concluded that Federal preemption rendered those Iowa statutes unenforceable. Even more common is the situation in New Jersey. The prior co-chairman and present member of the New Jersey State Bar Consumer Committee, Jonathon Rudnick explained to me that his group has talked many times about the need for legislation regarding arbitration clauses. They have not moved forward because their efforts would be "fruitless," because any attempt to limit the FAA would be preempted. In California, Rosemary Shahan notes that A.B. 2656, the Car Buyers Equality Act of 2004, sought to level the playing field and prohibit making consumers waive rights under the state law. The opponents succeeded in killing the bill arguing that it was preempted by the FAA. [Ray Johnson, Jonathon Rudnick, and Rosemary Shahan contributed to this response.]

Questions for the Record by Ranking Member Chris Cannon
For Hal Rosner

1. You believe that educating Congress will cause us to do something about alleged dealer abuses. Do you agree that doing more to educate consumers and to promote vigilant consumer practices in automobile sales and lease transactions would help to curb alleged dealer abuses? Please explain.

This question seems to reflect a belief in blaming the consumer and stopping all court actions. I can only hope that educating Congress will lead to basic fairness by limiting binding mandatory arbitration ("BMA"). I would urge Congress to look at the European Union Nations – who have essentially prohibited BMA in consumer contracts – for guidance here.

In response to the idea that educating consumers would help curb dealer abuses, you can educate consumers all you want about BMA but it would not change the pro-dealer bias in the arbitration system. Even these same car dealers are protected by Congress from being subject to manufacturer arbitration clauses. Further, most consumers who purchase or lease new automobiles make such purchases every 2 to 5 years. It is unlikely that a consumer who is educated today about dealer abuses would even remember what they were told the next time that they buy an automobile. Additionally, the techniques used by dealers to deprive consumers of their rights, including inserting an arbitration clause in the sales contract or lease agreement, involve facts and laws that are not understood by most lawyers. It would be unreasonable to expect consumers to know and understand these rights when most lawyers and even our elected officials do not. Even if consumers did understand the impact of an arbitration clause, it is often impossible to refuse one when purchasing or leasing a vehicle (anecdotally, one of my firm's partners, well-aware of the clauses and their impacts, recently tried to buy a car without a BMA and found out he could not). Furthermore, it would greatly increase the cost of purchasing or to lease an automobile if we expected consumers to consult a lawyer before making such a purchase.

Finally, in its current form, the arbitration provision in the LAW printing form is on the back of a 24-inch long contract. Most consumers never read this lengthy agreement, and thus never realize that they are signing an arbitration agreement. Furthermore, the boilerplate language on the contract is never open to negotiation, and thus, reading it would offer consumers no ability to reject the offending language.

In contrast, since automobile dealers engage in these types of transactions every day, and since they already retain lawyers to assist them in complying with the various state and federal regulations that govern the process, it is vastly more economical to educate dealers and to prohibit improper practices at dealership level. [Martin Anderson is again thanked for his contribution to this answer.]

2. Do you agree that a system filled with well-armed consumers offers benefits over a system that paternalistically limits consumers' freedom to contract for alternative dispute resolution options?

The question itself shows a bias and contains an untruth. The present system protects car dealers and prevents consumers from having any freedom to contract. As explained, consumers are forced, without any choice at all, to agree to BMA. The proposed legislation allows both consumers and car dealers to choose arbitration should a dispute arise.

3. Don't law firms like your stand to gain trial business if consumer options for arbitration are shut down?

The statement that H.R. 5312 shuts down consumers' options is an untruth and a blatant distortion of the legislation. The present systems forces consumers, without any choice, into unfair, rigged arbitration controlled by car dealers. The proposed legislation allows for choice by both dealers and consumers. As I explained in my testimony, a fair system helps everyone. Very few cases go to trial. The reason is the lawyers in a fair system can usually tell what the result will be. The present biased unfair arbitration system creates more litigation and discourages settlement. Even a car dealer who has blatantly violated the law may proceed with arbitration. We have even seen them encourage the arbitrators to not follow the law, and they sometimes succeeded.

If the questioner believes in a system of fair choice, he would himself have no choice but to fully support this legislation. [This answer is all my own.]

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