CONSUMER FINANCE PODCAST: WHAT IS MASS ARBITRATION AND HOW SHOULD COMPANIES PROTECT THEMSELVES?
HOST: CHRIS WILLIS
GUESTS: TONY KAYE AND JEREMY ROSENBLUM
POSTED: DECEMBER 8, 2022

Chris Willis:

Welcome to the Consumer Finance Podcast. I'm Chris Willis, the Co-Leader of Troutman Pepper's Consumer Financial Services regulatory practice. And I'm glad you've joined us for our episode today where we're going to talk all about the phenomenon of mass arbitrations in consumer finance litigation. But before we jump into that very serious topic, let me remind you to visit and subscribe to our blog, consumerfinancialserviceslawmonitor.com, where you'll see daily updates about all the important things that are happening in our industry. And while you're at it, check out our other podcasts, we have lots of them. We have the *FCRA Focus*, all about credit reporting, *The Crypto Exchange* about all things crypto and our Privacy and Data Security podcast called *Unauthorized Access*. All of those are available on all the popular podcast platforms that you might want to subscribe to them on. And if you like our podcast, let us know.

Leave us a review on your podcast platform of choice so that we know what you think about the podcast. Now, as I said, today we're going to be talking about mass arbitration, which is a phenomenon of recent years that has really been prevalent in private litigation, involving consumer financial services companies who routinely use arbitration clauses in their customer agreements. And I'm joined by two of my partners today to help talk about what's going on and what the potential remedies to the situation might be. So let me just thank my two partners, Jeremy Rosenblum, who's a partner in our Consumer Financial Services group in Philadelphia, and Tony Kaye, who's a partner in our Consumer Financial Services group and who lives in Salt Lake City.

Jeremy is primarily a regulatory and compliance lawyer who's been working in the industry for decades. Tony is primarily a litigator who's also been working in the industry for decades and the three of us have been working together for quite a long time too. So, I'm really glad that the two of you have joined us on the podcast to share your insights with the audience today. So, Jeremy, Tony, thanks for being on today.

Tony, let's just set the stage here if you don't mind and tell the audience if they're not familiar with it, what is mass arbitration? What was I talking about when I introduced today's episode?

Tony Kaye:

Mass arbitration is an interesting development that plaintiff's lawyers came up with in an effort to turn the efforts of the finance industry or the consumer financial services industry to steer people towards arbitration on its head. It's also actually used in the employment context but here we're going to talk more about how it's used in financial services. And mass arbitration, a plaintiff's lawyer or firm will use a claim aggregator and social media to identify a large number of potential claimants with disputes and then file arbitration demands on behalf of everybody that they sweep up in that process. And that can be 10,000 people or more.

The immediate problem is that there are filing fees with most of the institutional arbitration providers like AAA and JAMS, and those fees can be really substantial, compounding that is the fact that a lot of arbitration, in order to address due process concerns, shift the burden of filing fees to the company. So, you can have immediately millions of dollars in filing fees if you've

shifted the cost over. And then plaintiff's lawyers can leverage that. So, they can say, look, we're going to file 500 of these now but we're going to file another 9,500 in two weeks unless you settle with us. And so, the defendant in that case is basically sitting with the decision about whether to pay an enormous amount of filing fees or to settle to avoid that. And bear in mind that those filing fees, they're not damages, they're just administrative costs for resolving the dispute.

Chris Willis:

Tony, last time I checked, in order to represent a client, there had to be an attorney client relationship formed between the lawyer and the client and that would require some interaction between the two, one would think at a minimum, is that happening on this mass scale in the circumstances as you've described them? Are there actually 10,000 attorney client relationships going on?

Tony Kaye:

Yeah, no, I mean, it depends on who you ask. If you ask the plaintiff's lawyers, they'll generally tell you that yes, of course, they've spoken with every one of their clients or they've communicated with them by email. But in reality, we have found that the lawyers really have not spoken to many at all of the group of consumers that they're filing on behalf of. They've just amassed information in a database and then used that to generate demands and file them. So, there has been contact because obviously, the consumer had to post some information someplace about their potential claim, but there isn't an attorney-client relationship in the traditional matter where conflicts have been vetted and there's been a communication, an agreement to pay fees and all of those sorts of things.

Chris Willis:

Has there been any response to this phenomenon from the major arbitration administrators? I mean, it seems like something that they might have said something about, have they taken any action or said anything about it?

Tony Kaye:

Yeah, they have taken some action about it. The American Arbitration Association in particular has modified its fee schedule. It used to be that a consumer would pay $250 under AAA's rules, which was akin to the fee for filing a lawsuit. Let's keep it fair. And oftentimes, the defendant or the financial services company would've agreed in its arbitration agreement to pay so that there'd be no cost to the consumer and that would protect the due process rights of the consumer and make it easier to enforce the arbitration agreement in court.

Now, what AAA has done is said that, look, with the first 500 or so claims, the consumer's going to pay, I can't remember the exact number but let's say the consumer pays $100 and AAA's going to pay 200. And then as the number of arbitrations demands goes up and they're all related, then the fees for both parties go down. But it's still a substantial amount. I mean, in the end, if it's over a thousand, the defendant's going to be paying $100 per case and the consumer's going to be paying 50. And if the arbitration agreement has said that the defendant is agreeing to pay those fees, then they'll still pay those fees under that scale.

Chris Willis:

It sounds like we're still left with a problem here from the standpoint of the financial services industry, which I guess of course, is why we're having today's episode, what are some of the strategies that consumer financial services providers can adopt, to try to minimize either the risk or the impact of this mass arbitration phenomenon?

Tony Kaye:

There are a number of things you can do, one, easy fix if you're willing to deal with small claims court is to give, in the arbitration agreement, both parties the right to select small claims court, assuming that you're in a jurisdiction or you're in jurisdictions where the amount in controversy requirements can be met or the amount is below the threshold for a small claims court dispute. The business can opt to go to small claims court and it's going to be way more complicated for the lawyer to represent 10,000 folks in small claims court. They'll actually have to meet with their clients, show up to court, do the things that you would expect if somebody in a regular court setting, with slightly less procedural hurdles. Another thing that the defendant can do is to reconsider in its arbitration agreement, whether or not it wants to pay the filing fees for the consumer.

That's been a solid method of making sure that your agreement complies with due process protocols but if you agree to pay too much, it's creating too much of an incentive for a plaintiff's lawyer to choose your company in that arbitration agreement as the basis for filing a mass arbitration. One more option is to not use an organization like AAA or JAMS to resolve your dispute. If you do what's called ad hoc arbitration, you're picking your own arbitrator from a list. And there are various ways that you can do this and some of it's court assisted. But there are no filing fees. So, you would be paying fees to the arbitrator for the hearing but you're not going to have an upfront filing fee cost because ad hoc arbitration doesn't have any rules like that.

An option that I like a lot is mandatory mediation. I've seen this in consumer agreements for purchasing real estate, where every agreement requires mediation, a foreign arbitration can be filed. And the advantage to that is it requires, again, the lawyer representing these claimants to show up individually on behalf of each claimant and try to negotiate a resolution to the dispute. And that's a strong disincentive to file a mass arbitration because there's expenses with that, the parties usually share mediation fees, the plaintiff will be responsible for at least a good portion of them unless they win.

Chris Willis:

That sounds like a lot of interesting ideas, some of which may involve judgment calls about what risk the company wants to take in terms of arbitration and private litigation. But let me use this as an opportunity to bring you Jeremy into the conversation now, because I know that you've given a great deal of thought to the mass arbitration situation and trying to put effective countermeasures in place, with respect to that, give us some background about your work in that area.

Jeremy Rosenblum:

Thanks, Chris. You mentioned earlier that I've been working in the consumer financial services space for decades and that's true. And of course, consumer arbitration is a critical weapon of defense for companies in this space. So, I've been working on arbitration agreements for many years as well. The goal there has always been to make sure you have an enforceable arbitration

agreement, primarily to help defend against potential class action liability. And we have gone through multiple variants of arbitration agreements, cases developed, we try to make sure that our arbitration agreements remain enforceable, even in courts that are generally hostile to arbitration.

What has not happened to date is that most arbitration agreements have not addressed the risk of mass arbitration. For every 10,000 companies that have an arbitration agreement, maybe one or less has an arbitration agreement that's been updated to address mass arbitration. In effect, companies have been burying their head in the sand and not making the modifications necessary to address the risk of mass arbitration.

Over the past year or so, I've put a lot of time into what a good arbitration agreement would do to minimize the leverage that claimants have when they bring or thread in mass arbitrations. I should say that a good arbitration agreement only works if the consumer has signed onto it and updated arbitration agreements will not be able to help with respect to existing exposure under less advanced arbitration agreements. But if you're in an open-end line of credit program and able to modify an existing arbitration agreement or starting a new loan program or just continuing with an existing program, in my view, it's really essential to address mass arbitration in an updated agreement. The principle objective here is to reduce the leverage that the claimants have in a mass arbitration context. In my view, the best way of doing that were a critical feature of an arbitration agreement designed to address mass arbitration is to depart from existing arbitrations and allow or indeed mandate group arbitration of common issues of law, in fact, in specified circumstances.

First thing you have to do is figure out what kind of mass arbitration context is a concern. Would you be horrified by 500 individual arbitrations brought against you or into your tolerance for higher and maybe it's only 1,000 or 10,000 arbitrations that would be troubling, but you want to define what a mass arbitration is and then provide for addressing those claims in some group format. You could throw all of the threaded arbitrations into a single arbitration and then you have something that looks a little bit like in opt-in class action as opposed to the risk that you're trying to address of in-opt out class action. Problem with that is if you've got 10,000 claims against you, you may not want the exposure that would result from having all those 10,000 claims addressed at the same time. So, you have to figure out how to break this mass arbitration into potentially multiple groups and address it that way.

And then instead of having to potentially bear the cost of 10,000 individual arbitrations, which are prohibited and totally unacceptable, you're defending a much smaller number of group arbitrations with presumably lower fees. Now, Tony has said that you can switch the norm of who bears arbitration filing fees or you can proceed without an arbitration administrator entirely. And these are good ideas that ought to be incorporated into an arbitration agreement addressing mass arbitration. The trick there is to make sure that you don't throw the baby out with the bath water and create an unenforceable arbitration agreement and end up in a situation where a class action can be brought against you without the ability to force that punitive class action into individual arbitration.

Chris Willis:

Right.

Jeremy Rosenblum:

So that needs to be addressed in the arbitration agreement as well. The goal basically is to minimize fee exposure, claimant leverage and to do that through mechanisms that include the group arbitration, that include fee shifting, that include the potential elimination of an arbitration administrator and the accompanying costs entirely.

Chris Willis:

That sounds really interesting. And of course, this whole conversation is a little bit nostalgic because I remember when consumer arbitration first came to the fore in the financial services industry because it was, I think, in Alabama, in the mid 1990s. And I know you've been involved with it since then and seeing the different iterations that arbitration agreements have gone through to deal with these various issues along the years. But Jeremy, can I ask you to just give a little bit more context about what would it look like to have a group arbitration as you're mentioning right now? Would it require basically a group of claimants with related or identical claims to file a single arbitration demand such that there'd only be one filing fee? Is that basically how it would work?

Jeremy Rosenblum:

It would be group arbitrations, presuppose that there's a common issue of law or fact, that should not be a difficult hurdle to surmount, if somebody brings 10,000 arbitrations against you, it's highly unlikely that they would purport to say that these are all unique cases and each of them have to be individually arbitrated. So, when you're in a mass arbitration context, you automatically have common issues of law in fact. And yes, you would whack the universe of claimants into one or more groups and provide that whatever issues of law in fact exist would be decided in those group arbitrations. I should say that two things that have taken up a lot of my time is, first, to make sure that our special group arbitration provisions for mass arbitration don't somehow impair the ability to enforce an arbitration agreement outside the mass arbitration context.

And secondly, to make sure that within the mass arbitration context, that whatever you come up with is essentially fair, that it's fair to the company and fair to the group of claimants who may in fact have legitimate claims against the company and deserve a forum to assert those claims. They're not getting that forum necessarily in the existing world, where the sure volume of individual arbitrations may put off a hearing for years and years as all sorts of procedural wrangling is going on, or as other claimants get their day before the arbitrator. So, in my mind, it really is possible to create an arbitration agreement that is fair both to the company and to the claimant and more effective than existing arbitration agreements. But in doing so, to eliminate this outrageous leverage that the plaintiffs have under current arbitration agreement.

Chris Willis:

And you're speaking, of course, to the leverage of just the imposing of the filing fee. The leverage has nothing to do with the merits of the claim, that's what's so offensive about it from the standpoint of interfering with really the just outcome of a controversy, if you ask me. I assume you agree with that, right, Jeremy?

Jeremy Rosenblum:

Absolutely. I mean, you talk about thousands of dollars of filing fees and arbitration fees that will necessarily issue from each individual arbitration. You multiply that by the numbers, 500, 1,000 or 10,000, you very quickly reach the result completely untenable to the company defending these claims.

Chris Willis:

It sounds like there's some really good ideas, both from you and from Tony about how companies can try to handle this situation. And it also sounds to me from your comments, Jeremy, that this is an area where a lot of companies have not taken the opportunity to protect themselves on this, only a small percentage of them have done so. And so, I really am hoping that this episode of our podcast can be a wake-up call to those in the industry who are still relying on their old arbitration agreement and haven't given thought to this issue because if you haven't, then you're right into the same situation that both you and Tony have been describing during today's episode. I wanted to thank both of you for being on the podcast today. Thank you for sharing your ideas and of course, obviously, we're going to continue working on this because it's something that affects so much of the financial services industry.

And of course, I want to thank our audience for tuning into today's episode as well. Don't forget to visit our blog, consumerfinancialserviceslawmonitor.com and hit that subscribe button so that you can get all of our daily updates on what's going on in the consumer financial services industry. And while you're at it, head on over to troutman.com and visit us there and add yourself to our Consumer Financial Services email list so that you can get notice of our alerts and our industry only webinars. And of course, stay tuned for a great new episode of this podcast every Thursday afternoon. Thank you all for listening.