

NOTE

Show Me the Money?: Washington Adopts the Cost Prohibitive Defense to Arbitration Clauses in Consumer Contracts

*Merryn B. DeBenedetti**

When one has been threatened with a great injustice, one accepts a smaller as a favour.¹

I. INTRODUCTION

Arbitration has rapidly become a preferred method of resolving disputes. The American Arbitration Association (“AAA”) alone handled 230,255 cases in the last year, a figure representing over eleven percent of all the cases handled since 1926.² Since 1926, the AAA has administered over two million cases.³ Proponents of arbitration often tout its efficiency and its ability to conserve judicial

*J.D. Candidate 2004, Seattle University School of Law; B.A. Political Science, Western Washington University. The author dedicates this article to her father, Robert Gregory Lathram, Esq., whose pro bono case at the Kentucky Court of Appeals inspired this topic, and whose substantive comments, constructive criticism, and belief in the merits of our legal system helped the author formulate this article; to her mother, Catherine Paxton, for helping the author believe that she could achieve anything with hard work, common sense, and a sense of humor; and to her husband, Matthew, for his unconditional support and patience during the author's journey through law school. The author also would like to thank the Seattle University Law Review for their support, helpful suggestions, and leadership, and Chris Engle for his insight on the author's initial drafts.

1. JANE WELSH CARLYLE, LETTERS AND MEMORIALS, entry for Nov. 21, 1855 (1883), in THE MACMILLAN DICTIONARY OF QUOTATIONS 281 (John Daintith et al. eds., 1989).

2. Statistics regarding the volume of arbitrations conducted by the AAA are from the AAA website, at <http://www.adr.org> (last visited March 1, 2004). The AAA is the leading national arbitrator and provides the best baseline for examining the protocols and rules associated with arbitration in the United States.

3. *Id.*

resources.⁴ Nevertheless, arbitration may not provide some consumers these intended benefits when used by commercial entities in consumer contracts to prevent claims alleging the sale of defective goods and the use of improper financing practices.

In *Conseco Finance Servicing Corp. v. Wilder*,⁵ the attorney for the consumers contesting the arbitration clause at issue wrote: "The vigorous assertions of Appellant notwithstanding, the Federal Arbitration Act ("FAA")⁶ is not some all-encompassing panacea for litigation; to be blindly invoked and rotely applied simply because it has been incorporated into a consumer contract."⁷ Although the legislative history surrounding the FAA suggests that this assertion is entirely accurate, commercial entities regularly misuse arbitration clauses to preclude consumer disputes from reaching a judicial forum, as the following hypothetical scenario illustrates.

Bobby Turner is a twenty-nine-year-old entry-level carpenter for a construction company doing business in Eastern Washington. Although he shows talent in his chosen vocation, he does not earn very much money because he is an apprentice, and his employment is seasonal. Emily, his twenty-eight-year-old wife, draws social security disability because she suffers from chronic fatigue syndrome and hypertension. Emily's monthly social security disability check contributes \$600 to the family's income. The Turners have two children under the age of ten and receive an additional \$400 per month for the two children from social security disability.

The Turners currently rent a small, two-bedroom house just beyond the town's city limits. Although money is tight, especially with two children, Bobby and Emily want to own their own home. However, after looking at a couple of houses with a real estate agent, the Turners realize that they cannot afford a conventional home. On their way home from another disappointing meeting with the real estate agent, the Turners stop off at the local mobile home dealer after seeing a large plastic banner and balloons proclaiming "Special Financing for First Time Buyers." If nothing else, they believe that they might be able to buy a mobile home and put it behind the home of Emily's parents, who own a five-acre tract of land out in the county. The mobile home salesman, anxious to meet his monthly sales quota, initially shows them a double-wide model with a dealer price of \$65,000 before determining that the Turners can only afford a small

4. See *infra* note 48 and accompanying text.

5. 47 S.W.3d 335 (Ky. App. 2001).

6. Federal Arbitration Act, 9 U.S.C. §§ 1-307 (1999).

7. Brief of Appellee at 5, *Conseco*, 47 S.W.3d 335 (Ky. App. 2001).

three-bedroom, two-bath single-wide home with a price tag of \$35,000. When the Turners try to negotiate a better price, the salesman tells them that this price includes all appliances, as well as a master bedroom suite and a living room suite.

The Turners are excited. The appliances are new and shiny, and they get to pick from several styles of furniture in the dealer office, which doubles as a small showroom. While Emily is choosing her carpet from several samples, Bobby asks the salesman about installation of the mobile home and some problems he saw in the interior wood trim. The salesman assures Bobby that the dealer's installation crew is one of the best in the area and that any small "cosmetic" interior problems will be fixed after delivery to the Turner's satisfaction. The salesman tells the Turners that the mobile home comes with a one-year warranty from the manufacturer and the dealer. Having been reassured, the Turners sign a purchase agreement and a loan application. Disappearing for a half-hour, the salesman returns and tells the Turners that his finance manager will not send in the application unless they can make a \$5000 down payment or put up a tract of land as collateral to secure payment of the loan. The salesman asks the Turners to talk with Emily's parents about sub-dividing their tract and deeding them one acre of their own. He also tells them that a co-signor on the note or a small down payment of \$1000 would guarantee that the deal would go through.

The Turners agree to talk to Emily's parents and, after much discussion, call the salesman the next day and tell him that her parents will deed them a one-acre tract and will loan them \$1000 for a partial down payment. The Turners meet with the salesman and the finance manager approximately ten days later with a new deed and \$1000 to sign the documents for the purchase of their new home. Within the fifty pages of closing documents are approximately twenty-five places for the Turners to sign or initial. The salesman makes it easy for them to wade through the morass of paperwork, pointing out where they need to sign or initial and telling them that their new home is being manufactured right now and should be ready for delivery in approximately thirty days. An hour later, the Turners emerge with a copy of all of their paperwork. Upon arriving home, they promptly put it in a box that they will read later after going to her parent's house to look at their new tract of land.

Later, Bobby briefly reviews some of the paperwork and is reassured to discover that their mortgage company, a national corporation specializing in financing mobile homes, will conduct a telephone audit after delivery of the mobile home to ensure that they

have accepted delivery of their home. The Turners and Emily's parents spend the next four weekends doing their own site preparation. Shortly thereafter, the dealer's site installation crew arrives and installs the footers, followed three days later by their new mobile home. After the mobile home is installed, the Turners discover that most of the doors and windows are difficult to open and close and some windows will not open at all. During the telephone audit, Bobby mentions this to the mortgage representative, who assures him that these issues are covered by his warranty, and that he should immediately contact his dealer. After obtaining his recorded acceptance of the mobile home, the mortgage representative congratulates him on his purchase of a new home and reminds him that that his monthly mortgage payment must be made in a timely manner.

Over the next ten months, the Turners are unable to get the windows and doors repaired in addition to a leak that has developed in the wall in the master bedroom. The dealer tells them that the issues with the windows and doors are a manufacturer's problem and not an installation problem. When the manufacturer's local repair representative arrives, however, he informs the Turners that the home is not set up "right." Frustrated, the Turners begin taking turns calling the dealer, getting no response; calling the manufacturer, which tells them that it has made its repairs; and finally, calling the mortgage company, which tells them that it simply bought their contract and has no obligation to make any repairs. In addition, the mortgage company informs the Turners that they were late with their last monthly payment. In this call, Bobby tells this particular representative that he is not going to pay for a defective mobile home, and that he is going to see a lawyer. The representative tells Bobby that he had better read his contract again and hangs up.

Later, the Turners decide to visit a lawyer in town with all of their paperwork. After listening patiently to the Turners' story and reviewing their contract, the lawyer finally says that they cannot sue anyone, other than the manufacturer, because their contract contains an arbitration clause that they signed. Bobby Turner asks what that means, and the lawyer simply shakes her head and sighs.

Although this is only a hypothetical scenario, it is representative of the predatory manufacturing and financing tactics that some commercial entities employ and the use of arbitration clauses to avoid costly consumer claims that result from defective and rapacious manufacturing, sale, and financing practices. The Turners' situation is not unique. Manufacturers, dealers, and commercial financing

institutions often bury arbitration clauses in fine print as a method to preclude a consumer from pursuing his or her claim, even though the sold goods are defective or the financing methods and lack of disclosure are reprehensible. Courts continue to struggle with whether arbitration is a comparable forum to litigation to protect consumer rights, and some courts have attempted to delineate new exceptions to the presumption in favor of arbitration in order to address these sharp business practices.⁸

In commercial-consumer contracts, arbitration may well be incapable of protecting consumers to the extent that litigation can create consumer awareness regarding defective products and predatory lending practices, assist in regulating these business practices in our market economy, preserve consumer choice regarding whether to arbitrate or litigate statutory claims, and protect consumers from economic harm.

Some courts have adopted a new exception to invalidate agreements to arbitrate: a prohibitive cost defense. If the consumer can demonstrate that the arbitral forum is economically inaccessible, courts will permit that consumer to litigate, rather than arbitrate, his or her claims under the contract. Such exceptions, however, may prove to be more troublesome than beneficial to consumer interests.

* * *

In *Mendez v. Palm Harbor Homes*,⁹ the Washington Court of Appeals recently recognized that arbitration should not be rotely applied to every consumer contract, notwithstanding the existence of a clause in the contract whereby the parties agreed to arbitrate their disputes.¹⁰ The court adopted a legal and equitable cost prohibitive defense with respect to mandatory arbitration agreements.¹¹ Like the hypothetical scenario discussed above, *Mendez* involved a mobile home sale to a low-income consumer who was unable to afford the costs of arbitration to bring his claims.¹²

Although Washington courts presume arbitration agreements to be enforceable,¹³ the adoption of the cost prohibitive defense to

8. See *Mendez v. Palm Harbor Homes*, 111 Wash. App. 446, 45 P.3d 594 (2002); *Conseco*, 47 S.W.3d 335 (Ky. App. 2001); *In re FirstMerit Bank*, 52 S.W.3d 749 (Tex. 2001).

9. 111 Wash. App. 446, 45 P.3d 594 (2002).

10. *Id.* at 464, 45 P.3d at 604.

11. *Id.* at 450, 45 P.3d at 597.

12. *Id.*

13. *E.g., id.* at 458, 45 P.3d at 601 (citing WASH. REV. CODE § 7.04.010, which provides that arbitration agreements are enforceable "save upon such grounds as exist in law or equity for the revocation of any agreement").

mandatory arbitration agreements may allow consumers of limited means and in certain circumstances to find their way into a courtroom and litigate their disputes with businesses. The adoption of the cost prohibitive defense may provide some relief to consumers who wish to litigate, rather than arbitrate, their claims; however, it is not an adequate remedy for the problems associated with arbitration. Despite Washington courts' sympathy for low-income consumers, several inherent problems with the cost prohibitive defense defeat its purposes and undermine its usefulness in the consumer context.

First, the cost prohibitive defense places the burden on the consumer to prove that arbitration presents an insurmountable financial barrier to bringing his or her claims. Second, the cost prohibitive defense requires an evidentiary hearing to determine if arbitration is indeed cost prohibitive for a particular plaintiff. This evidentiary inquiry likely will further increase, rather than decrease, costs to consumers and produce inefficiency in the resolution of claims. Because arbitration is meant to counteract inefficiency, any method of avoiding arbitration that produces inefficiency undercuts the policies behind alternative dispute resolution. Third, the cost prohibitive defense fails to address inherent problems of adhesive contracts, such as the lack of informed consent and lack of consensual bargained-for exchange. Instead, the defense continues to protect commercial interests, rather than consumers, by providing only a narrow exception to the presumption in favor of arbitration. Finally, the cost prohibitive defense, as applied by the courts, offers no definitive standard by which potential litigants can measure their likelihood of success in surviving a motion to stay litigation and compel arbitration. This lack of guidance for future litigants also invites the use of this defense in varying contexts—where parties may well be on essentially equal bargaining terms—in order to avoid arbitration. For the foregoing reasons, any potential benefits gained by allowing plaintiffs to demonstrate prohibitive costs as a defense to mandatory arbitration agreements clearly come at a significant cost because successfully asserting this defense requires expense and time and ignores the issue of unconscionability in the contract itself entirely. By virtue of the FAA and with an unwillingness to invalidate adhesive arbitration clauses as unconscionable, courts have failed to protect consumer interests in commercial settings. The cost prohibitive defense, although attempting to protect citizens who are less fortunate from an economic standpoint, does not adequately correct that failure.

Many commentators have argued that mandatory arbitration clauses in consumer contracts unfairly preclude those consumers from pursuing their claims.¹⁴ The scope of this Note, however, focuses on whether the courts have adequately corrected the substantive failures of mandatory arbitration agreements when they permit consumers to prove prohibitive costs.

Following this Introduction, Part II of this Note explores the origin and history behind the adoption of the FAA and the legislative desire to place parties of equal bargaining power in a position to arbitrate. Part III examines the acceptance of this defense in other jurisdictions. Part IV considers the *Mendez* case and analyzes Washington's newly adopted approach to invalidate mandatory arbitration clauses in consumer contracts. Part V illustrates the appropriateness of this defense and addresses the benefits and burdens of applying it in the consumer context. Part VI concludes the Note, identifying the unjustified presumptions that undercut the value of arbitration as an alternative forum to resolve disputes in the consumer context and evaluating the cost prohibitive defense as an adequate response.

II. THE BACKGROUND OF THE FAA AND THE EMERGENCE OF THE COST PROHIBITIVE DEFENSE

Section A of this part examines the FAA, provides the justifications for its adoption, and considers the practical effects of binding arbitration agreements in the consumer context. Section B outlines Washington's arbitration statute. Section C discusses the Supreme Court's *Green Tree* decision, suggesting that the cost prohibitive defense may be available in some consumer cases.

A. Equal Bargaining Power and the Federal Arbitration Act

The FAA was initially enacted in 1925.¹⁵ Section 2 of the FAA, which addresses the validity, irrevocability, and enforcement of arbitration agreements, states:

14. See discussion *infra* section II.A.

15. 43 Stat. 883 (1925). The FAA was reenacted and recodified in 1947 as Title 9 of the United States Code. 9 U.S.C. §§ 1–15 (1947). See also Richard M. Alderman, *Pre-Dispute Mandatory Arbitration in Consumer Contracts: A Call for Reform*, 38 HOUS. L. REV. 1237, 1244 (2001) (noting that the provisions of the FAA are meant to counteract a longstanding judicial hostility toward arbitration agreements and, consequently, they suggest a liberal enforcement policy with regard to mandatory arbitration agreements); Rita M. Cain, *Commercial Disputes and Compulsory Arbitration*, 44 BUS. LAW 65 (1988) (discussing the enactment of the FAA and the purposes behind its adoption, including reversal of the common law rule that either party could

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.¹⁶

The stated purpose of section 2 of the FAA is a “congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary.”¹⁷ Notably, this purpose was only meant to place arbitration agreements on the same footing as other traditional contracts, not to eliminate fundamental access rights to the judicial forum.¹⁸

Traditional contract theory presumes that contracts result from a bargained-for exchange by parties on equal footing.¹⁹ Doctrines such

revoke a pre-dispute arbitration agreement because the purpose of pre-dispute arbitration was to oust the jurisdiction of the courts).

16. 9 U.S.C. § 2 (1999); *see also* Duplan Corp. v. W.B. Davis Hosiery Mills, Inc., 442 F. Supp. 86 (1977) (concluding that Congress intended 9 U.S.C. § 2 “only to place arbitration agreements affecting commerce or maritime affairs on the same footing as other contracts”). Common contract defenses resulting in revocation include: mistake, duress, incapacity, fraud, and unconscionability. Such defenses may be used to invalidate arbitration agreements without “contravening § 2 [of the FAA].” *Doctor’s Assocs., Inc. v. Casarotto*, 517 U.S. 681, 687 (1996). Notably, however, these defenses are generally recognized as narrow in scope and inconsistently applied in different jurisdictions, and consumers cannot place much reliance in these doctrines to escape mandatory arbitration clauses. Many cases alleging fraud and other contractual defects illustrate this point. *See Saneii v. Robards*, 187 F. Supp. 2d 710, 711 (W.D. Ky. 2001) (holding the buyers must arbitrate their claim that sellers fraudulently induced sale of house because the allegation of fraud is to the contract generally and not the arbitration clause itself); *Lawrence v. Comprehensive Business Servs. Co.*, 833 F.2d 1159, 1162 (5th Cir. 1987) (rejecting argument that arbitration is prohibited because illegality of contract is a ground which “[exists] at law or equity for the revocation of any contract”). *But cf.* *Hayes Children Leasing Co. v. NCR Corp.*, 37 Cal. App. 4th 775 (1995) (denying petition to compel arbitration where arbitration clause itself fraudulently induced).

17. *Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983); *see also* Alderman, *supra* note 15, at 1244; Cain, *supra* note 15, at 66; Jason Bradley Kay, Note, *The Post-Green Tree Evidentiary Standard for Invalidating Arbitration Clauses in Consumer Lending Contracts: How Much Justice Can You Afford?*, 6 N.C. BANKING INST. 545, 545 (2002) (arguing that the right to trial by jury, a liberty secured by the United States Constitution, has been qualified by the enactment of the FAA in 1925).

18. *See* discussion *supra* note 15.

19. *See, e.g.*, Alderman, *supra* note 15, at 1247–48; *see also* James J. White, *Autistic Contracts*, in *PERSPECTIVES ON CONTRACT LAW* 158 (Randy E. Barnett ed., 2001) (arguing that the benefits of adhesive, or “autistic” contracts, including the reduction in transactional costs, outweigh the costs imposed on “dissenting offerees”). However, if a single contract controls a large quantity of costs or services, the adhesive contract system is unlikely to be more efficient. *See id.* For a comprehensive review on the theory and application of the doctrine of

as unconscionability bolster this premise, because if a contract results from procedural or substantive unfair advantages held by one party, courts may void the contract. The FAA was designed in part to encourage courts to find arbitration agreements as enforceable as other contracts in order to overcome the longstanding judicial hostility to arbitration as an ouster of jurisdiction.²⁰ The FAA establishes that an arbitration agreement is binding if (1) the arbitration agreement exists, (2) the arbitration agreement is in writing, and (3) the parties consented to the agreement.²¹ The FAA has proven influential in courts' decisions to enforce arbitration clauses, and large commercial interests employ the FAA to stay litigation.²²

When the FAA was adopted in 1925, there were few transactions between commercial entities and consumers.²³ During the debate surrounding its adoption, one U.S. congressman raised his concern that arbitration clauses might be placed in adhesive contracts. He was reassured, however, by the FAA's supporters that it was not intended to cover such situations.²⁴ Senator Walsh from Montana, troubled by the FAA's potential application to adhesive consumer contracts,²⁵ argued:

The trouble about the matter is that a great many of these contracts that are entered into are really not voluntarily [sic] things at all. Take an insurance policy; there is a blank in it. You can take that or you can leave it. The agent has no power at all to decide it. Either you can make that contract or you can not make any contract. It is the same with a good many contracts of employment. A man says "These are our terms. All right, take it or leave it." Well, there is nothing for a man to do except to sign it; and then he surrenders his right to have his case tried by the court, and has to have it tried before a tribunal in which he has no confidence at all.²⁶

unconscionability, see generally RANDY E. BARNETT, *CONTRACTS CASES AND DOCTRINES* 1130–1161 (2d ed. 1999).

20. Alderman, *supra* note 15, at 1244.

21. *See id.* at 1246.

22. Shelly Smith, Comment, *Mandatory Arbitration Clauses in Consumer Contracts: Consumer Protection and the Circumvention of the Judicial System*, 50 DEPAUL L. REV. 1191, 1193–94 (2001).

23. Jean K. Sternlight, *Panacea or Corporate Tool?: Debunking the Supreme Court's Preference for Binding Arbitration*, 74 WASH. U. L. Q. 637, 647 (1996).

24. *Id.*

25. Senator Thomas J. Walsh, 1923, *quoted in* Linda Alle-Murphy, Comment, *Are Compulsory Arbitration Clauses in Consumer Contracts Enforceable? A Contractual Analysis*, 75 TEMP. L. REV. 125, 138 (2002).

26. *Id.* For further review of the Senate debates surrounding the adoption of the FAA, see *Sales and Contracts to Sell in Interstate and Foreign Commerce, and Federal Commercial*

In response, Senator Platt, Chairman of the ABA Committee on Commerce, Trade, and Commercial law, reassured Senator Walsh that the proposed FAA was not intended to cover insurance contracts, or any other kind of legislation, that would “force a man to sign that kind of contract.”²⁷ The legislative intent of the FAA clearly indicates that arbitration clauses in adhesive consumer contracts were not originally within the purview of the statute because this concern was specifically raised during floor debates and dismissed by the FAA’s proponents as inapplicable.

Seventy-six years later, in May 2001, Dudley Butler, an attorney from Mississippi, testified before the Senate Appropriations Subcommittee on Agriculture regarding adhesive agreements to arbitrate in the poultry industry.²⁸ He argued that while arbitration “is a valuable alternative resolution procedure,” arbitration clauses that waive any right to a jury trial and contain “cost laden” provisions take away the “litigation forum . . . by contract and the arbitration forum . . . by economics.”²⁹ He posits that “the use of mandatory arbitration clauses along with the waiver of any right to a jury trial is in fact counterproductive to the promotion of the arbitration process” because the arbitration process essentially functions as a “cost controlling liability reduction device,” rather than a “dispute resolution device.”³⁰ He proposed that Congress amend the FAA to mandate that the individual or entity can choose the forum at the time a claim is made.³¹

Arbitration clearly has become fraught with inefficiencies and inequity from the time when Congress enacted the FAA to today. Commentators like Mr. Butler condemn the use of mandatory arbitration clauses in certain kinds of contracts and argue that the FAA must be amended or, alternatively, courts should cease to give agreements to arbitrate such expansive deference.

In addition to the distinction that the 1925 Congress made between consumer-commercial transactions and arm’s length business transactions, the legislative history surrounding the adoption of the FAA also suggests its narrow jurisdictional application. The FAA was intended to govern disputes regarding arbitration in federal

Arbitration: Hearing Before a Subcomm. of the Comm. on the Judiciary, S. 4213 and S. 4214, 67th Cong. 9 (1923).

27. Alle-Murphy, *supra* note 25, at 138.

28. 2001 WL 534234 (F.D.C.H. May 17, 2001).

29. *Id.*

30. *Id.*

31. *Id.*

courts, not in state courts.³² This congressional intention is bolstered by the fact that proponents of the FAA were simultaneously working on similar state laws that would have been “superfluous” had the FAA been intended to govern state courts.³³

* * *

The Supreme Court introduced an expansive reading of the FAA for the first time in *Moses H. Cone Memorial Hospital v. Mercury Construction*.³⁴ The dispute in *Moses H. Cone* arose when a hospital entered into a contract with a contractor to build additions to the hospital building.³⁵ The contract provided that the parties could arbitrate disputes either decided by the architect or not decided within a specified time.³⁶ The contractor submitted claims to the architect for extended overhead and increased construction costs due to the hospital’s delay.³⁷ The hospital refused to pay the claims and filed an action seeking a declaratory judgment stating that, inter alia, the contractor had no right to arbitration.³⁸ The case eventually reached the United States Supreme Court.³⁹

Justice Brennan, writing for the Court, declared that “[t]he Arbitration Act establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration.”⁴⁰ Justice Brennan relied on *Prima Paint Corp. v. Flood & Conklin Manufacturing Corp.*⁴¹ Although *Prima Paint* extended only to the specific issue presented,⁴² Justice Brennan noted in *Moses H. Cone*

32. *Id.* at 649.

33. *Id.* at 649–50.

34. *Id.* at 660; *Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1 (1983); see also *Perry v. Thomas*, 482 U.S. 483, 489 (1987) (noting that section 2 of the FAA is a congressional declaration of a liberal federal policy favoring arbitration agreements, and Congress, by enacting section 2, has withdrawn from the states the power to require a judicial forum for resolution of claims which the parties agreed to resolve by arbitration). Although the FAA was not intended to supersede state law, states are prevented from requiring the judicial resolution of claims. This policy may raise a federalism issue outside the scope of this Note; nevertheless, states which choose to provide more protections for their consumers than arbitration currently allows should be able to do so.

35. 460 U.S. at 1.

36. *Id.*

37. *Id.*

38. *Id.*

39. *Id.*

40. *Id.* at 24–25.

41. *Id.* at 24; *Prima Paint Co. v. Flood & Conklin Mfg. Corp.*, 388 U.S. 395 (1967). *Prima Paint* involved a contract containing an arbitration clause where one party alleged that the contract had been fraudulently induced. *Id.* The issue before the Court was whether fraud in the contractual exchange was itself an arbitrable controversy. *Id.* at 402. The Court held that the language and policy behind the FAA rendered the fraud issue also arbitrable. *Id.* at 402–04.

42. *Prima Paint*, 388 U.S. at 402–04; *Moses H. Cone*, 460 U.S. at 24.

that “the courts of appeals have since consistently concluded that questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration.”⁴³ In this context, the Supreme Court’s subsequent decisions “can be seen as expressing a law and economics philosophy favoring the alienability of court access rights.”⁴⁴

The problem with the Court’s interpretation regarding arbitration agreements in consumer contracts, however, is that a stay of litigation may result in a complete stay of the dispute because consumers traditionally are less willing to arbitrate disputes than to litigate a claim in a jury trial.⁴⁵ This unwillingness of potential plaintiffs to arbitrate disputes allows commercial interests to effectively use arbitration to avoid consumer lawsuits.⁴⁶

Arbitration has its benefits. As one author has noted, its proponents regularly assert the following: arbitration provides efficiency and greater flexibility.⁴⁷ Moreover, parties with equal bargaining power may reduce transactional costs by agreeing in advance to arbitrate disputes.⁴⁸ To some extent, the traditional judicial forum has proven inadequate to resolve disputes,⁴⁹ and the FAA was Congress’s response, designed to relieve an overburdened judicial system.⁵⁰ Because the burden on the judicial system historically increases from year to year, Congress created the FAA to reduce the costs of dispute resolution, and to encourage parties to

43. *Moses H. Cone*, 460 U.S. at 24.

44. Sternlight, *supra* note 23, at 674.

45. Smith, *supra* note 22, at 1194.

46. *Id.* at 1195.

47. See, e.g., Alderman, *supra* note 15, at 1239.

48. Smith, *supra* note 22, at 1191; see also Larry J. Pittman, *The Federal Arbitration Act: The Supreme Court’s Erroneous Statutory Interpretation, Stare Decisis and a Proposal for Change*, 53 ALA. L. REV. 789, 826 (2002) (arguing that the supporters and drafters of the FAA “envisioned arbitration agreements between merchants, and not arbitration of issues arising from consumer contracts”). Moreover, the floor debates over the FAA suggest that the FAA was not intended to be applicable to adhesion contracts that powerful commercial interests force upon consumers. *Id.*

49. Alderman, *supra* note 15, at 1267–68. Professor Alderman contends that the “underlying premise of ADR rhetoric [is] simple: the legal system had become too expensive, too slow, and too inefficient to deal with the myriad of problems it was being asked to resolve.” *Id.* at 1238. Consequently, from a philosophical perspective, there is little fault with the concept of ADR. *Id.* at 1239. However, it is apparent that the realities of pre-dispute mandatory arbitration as employed in consumer transactions “differ sharply from the idealized process” that ADR was meant to achieve because consumers rarely choose pre-dispute arbitration, as it is usually imposed upon the consumer in an adhesion contract. *Id.* at 1240.

50. See Smith, *supra* note 22, at 1191. Arbitration was initially created so that parties with equal bargaining power could reduce the costs of litigation by agreeing to submit their disputes to arbitration. *Id.*

salvage contractual relationships.⁵¹ Prior to the enactment of the FAA, courts would allow two parties to submit a dispute to binding arbitration, but rarely enforced a pre-dispute arbitration agreement.⁵² The FAA was primarily envisioned, therefore, as applying to *consensual* transactions between parties with equal bargaining power, not necessarily applying to transactions between consumers and commercial entities.⁵³ Initial Supreme Court decisions consistently applied the principle that arbitration involved voluntary and consensual parties.⁵⁴

Such benefits notwithstanding, arbitration has not been an adequate remedy to the burdens and costs associated with litigation. While some consumers may prefer the asserted benefits of arbitration, including prompt and efficient resolutions of their claims,⁵⁵ arbitration lacks many protections and safeguards for consumer rights,⁵⁶ such as developing common law in an open forum by virtue of a jury trial. The prompt and inexpensive resolution of claims should never take precedence over consumer protections and safeguards that manifest in a lay jury because the justice system's primary concern should not focus solely on efficiency and expense.

Because arbitration emphasizes efficiency and lowered transactional costs, powerful commercial parties are often able to mislead less powerful consumers into agreements to arbitrate by burying arbitration clauses in complicated and lengthy documents.⁵⁷ Consumers are less likely to realize any inherent efficiency benefits resulting in lowered transactional costs when they waive their right to litigate a claim; they are giving up that right in favor of lower transactional costs that substantially benefit only the commercial entity.⁵⁸ In the most egregious cases, commercial interests insert

51. *See id.* at 1220; *see also* Pittman, *supra* note 48, at 828.

52. Sternlight, *supra* note 23, at 644.

53. *See id.* at 647.

54. *See id.*

55. Alderman, *supra* note 15, at 1239–40.

56. *See* Smith, *supra* note 22, at 1222 (“Mandatory arbitration effectively strips consumers of their rights to protect themselves from large corporations and jeopardizes the American judicial process of developing common law.”).

57. *Id.* at 1192.

58. *Id.* Although it may well be that mandatory arbitration clauses lower transactional costs, thereby helping the consumer because those savings are passed through to the consumer, the fact that mandatory arbitration agreements in consumer contracts often function as a bar to the consumer's claim may suggest that the commercial entity likely receives the most benefit because consumers are prevented from bringing their claims at all. Thus, it is not merely that the good or service may cost less because of the existence of the arbitration, but rather that the insertion of the arbitration clause in an adhesive consumer contract allows the commercial entity to sell goods or services without recourse for defects, illegal or improper financing, and other sharp business practices.

unilateral clauses in arbitration agreements whereby one party retains the right to choose between arbitrating and litigating certain disputes whereas the other party must arbitrate all claims.⁵⁹

Viewing the issue in this context, mandatory arbitration clauses are detrimental to consumer rights rather than an alternative and efficient forum to resolve disputes as intended by the FAA, both legislatively and as a matter of public policy.⁶⁰ Consequently, “[t]he notion that arbitration is ‘merely’ a different forum is a myth, just like the belief that the world was flat or that the sun revolved around the earth.”⁶¹ Because the FAA encourages a liberal enforcement policy regarding arbitration and because courts are reluctant to disturb contractual bargains, consumers retain no viable judicial alternatives or remedies other than to proceed to mandatory arbitration.⁶² The FAA’s liberal policy toward arbitration and the judiciary’s reluctance to invalidate adhesive arbitration clauses also fundamentally jeopardizes the judicial process of common law development because arbitration typically is not an open forum with published decisions and spectators.⁶³

These considerations suggest that arbitration clauses should never be blindly upheld, despite the potential benefits gained by efficiency and lowered transactional expense. Courts mistakenly embrace arbitration agreements as a philosophically comparable solution to litigation even though such agreements are often injurious to consumer rights. One author suggests that the four major policy arguments in support of a judicial preference for binding arbitration are substantially unjustified in light of the imposition of “unregulable arbitration on nonconsenting consumers and other little guys.”⁶⁴ Such pro-arbitration arguments include the notion that two parties should

59. Adam M. Nahmias, *The Enforceability of Contract Clauses Giving One Party the Unilateral Right to Choose Between Arbitration and Litigation*, 21 CONSTR. LAWYER 36 (2001).

60. See Alderman, *supra* note 15, at 1267; see also Andrew J. Sarapas, Comment, *Amending Maine’s Plain Language Law to Ensure Complete Disclosure to Consumers Signing Arbitration Contracts*, 50 ME. L. REV. 83, 117 (1998) (arguing that arbitrators, as business people or attorneys, are not only less likely to award punitive damages, but that commercial interests rely on arbitration agreements to avoid sympathetic juries composed of consumers).

61. Alderman, *supra* note 15, at 1264; see also Sternlight, *supra* note 23, at 641. Ms. Sternlight commented:

When Congress passed the FAA in 1925, it intended only to require federal courts to accept arbitration agreements that had been voluntarily entered into by two parties of relatively equal bargaining power in arms’ length transactions. Congress did not intend to enforce arbitration agreements that had been foisted on ignorant consumers, and it did not intend to prevent states from protecting weaker parties.

Id.

62. See Alderman, *supra* note 15, at 1264.

63. Smith, *supra* note 22, at 1222.

64. Sternlight, *supra* note 23, at 674–75.

retain the freedom to contract as they see fit.⁶⁵ Another argument is that the benefits of arbitration outweigh the harms of non-consensual transactions.⁶⁶ A third argument is that the market has an inherent ability to correct itself with regard to commercial entities that misuse arbitration and that the harm levied against a few individuals is small compared to the overwhelming benefits of arbitration.⁶⁷ Like other states, the Washington legislature and Washington courts have approached agreements to arbitrate with favor, even in adhesive consumer contracts.

B. Presumed Valid: Washington's Approach to Mandatory Arbitration Clauses

Washington State courts have become enamored by the "efficiency and economics" aspects of binding arbitration and continue to overlook the substantive unfairness in unilaterally forcing consumers to forego remedies in the judicial forum. Court enforcement of mandatory arbitration clauses in the consumer context furthers the ability of commercial interests to deal in sharp business practices without recourse in a jury setting. Juries would likely view rapacious business practices suspiciously and punish commercial entities accordingly. Like its federal counterpart, Washington State recognizes arbitration agreements as enforceable. According to Washington statute:

Two or more parties may agree in writing to submit to arbitration, in conformity with the provisions of this chapter, any controversy which may be the subject of an action existing

65. *See id.* at 675.

66. *See id.*

67. *See id.* at 674. In discrediting the theories regarding the policy justifications for binding arbitration, Ms. Sternlight suggests that freedom of contract cannot "... realistically be used to justify imposing binding arbitration through contracts of adhesion on unwitting consumers" because "[f]ew, if any, would be foolish enough to argue that most employees and consumers actually read and understand the form contracts that they sign which commit them to binding arbitration." *Id.* at 676. Moreover, Ms. Sternlight rightly asserts that the "fiscal savings to courts from diverting cases from trial may be outweighed by the costs of running an efficient ADR program, and savings in lawyer time are often modest and not necessarily passed on to litigants through lower legal fees." *Id.* at 679. Ms. Sternlight suggests three arguments that undermine the economically based assertion that arbitration is an adequate response to litigation: (1) procedure determines substantive outcome, (2) the party drafting an agreement maximizes that agreement's provisions to its own advantage, and (3) market competition will not prevent commercial entities from taking advantage of less powerful parties. *Id.* at 675-693. The crux of the argument against binding arbitration agreements in consumer contracts extends beyond whether a particular method of commercial exchange is "Pareto optimal." *See id.* at 677. Rather, the most important consideration is that consumers should not be forced to forego a judicial remedy based upon an unconscionably drafted agreement by parties on unequal footing despite particular economic or commercial advantages offered by arbitration. *See id.*

between them at the time of the agreement to submit, or they may include in a written agreement a provision to settle by arbitration any controversy thereafter arising between them out of or in relation to such agreement. Such agreement shall be valid, enforceable, and irrevocable save upon such grounds as exist in law or equity for the revocation of any agreement.⁶⁸

If a contract executed in Washington provides for the arbitration of disputes, a plaintiff cannot maintain an action without first submitting to arbitration.⁶⁹ Washington courts generally refuse to intervene in the arbitration process because public policy and the statutory scheme suggest a narrow approach to construing the exceptions to the arbitration statute.⁷⁰ To stay legal action, a court simply must find the arbitration clause valid as well as the dispute referable to arbitration under the agreement.⁷¹ Notably, the terms of the parties' agreement govern the power and method of the arbitrators and govern who will bear costs.⁷² Following in the footsteps of federal courts, Washington courts also initially recognized a strong public policy favoring arbitration and adopted a "narrow approach" to intervening in the arbitration process.⁷³

C. *The Emergence of the Cost Prohibitive Defense to Mandatory Arbitration: Green Tree Financial Corp. v. Randolph*

In *Green Tree Financial Corp. v. Randolph*,⁷⁴ the U.S. Supreme Court entered the fray over the validity of mandatory arbitration clauses in adhesive consumer contracts.⁷⁵ The Court addressed the possibility that a mandatory arbitration clause in an adhesive consumer contract may pose significant barriers to plaintiffs who desire to vindicate their statutory rights.⁷⁶ While not explicitly providing a particular standard, the *Green Tree* Court noted that proof

68. WASH. REV. CODE § 7.04.010 (2002).

69. See generally *Hughes v. Bravinder*, 9 Wash. 595, 38 P. 209 (1894); *Wager v. Odden*, 148 Wash. 188, 268 P. 151 (1928).

70. See *Perez v. Mid-Century Ins. Co.*, 85 Wash. App. 760, 934 P.2d 731 (1997).

71. See WASH. REV. CODE § 7.04.030; *Greenlee v. AAACON Auto. Transp., Inc.*, 6 Wash. App. 742, 743-44, 496 P.2d 359, 360 (1972).

72. See *Hegeberg v. New England Fish Co.*, 7 Wash. 2d 509, 520, 110 P.2d 182, 186 (1941); see also *Puget Sound Bridge & Dredging Co. v. Lake Wash. Shipyards*, 1 Wash. 2d 401, 410, 96 P.2d 257, 261 (1939) (holding that arbitration is subject to the contract and the parties may agree to any terms) (emphasis added).

73. *Perez*, 85 Wash. App. at 767, 934 P.2d at 734.

74. 531 U.S. 79 (2000).

75. *Id.*

76. *Id.* at 84.

of prohibitive costs might permit a plaintiff to litigate, rather than arbitrate, his or her claims.⁷⁷

The *Green Tree* case arose when plaintiff Randolph purchased a mobile home from Better Cents Home Builders Inc. in Alabama.⁷⁸ Randolph financed the home through Green Tree Financial Corporation.⁷⁹ Randolph later sued Green Tree, alleging Truth in Lending Act (“TILA”)⁸⁰ violations by failing to disclose as a finance charge the “Vendor’s Single Interest” insurance requirement.⁸¹ Randolph later amended her complaint to add a claim that Green Tree violated the Equal Credit Opportunity Act by requiring her to arbitrate her statutory causes of action.⁸² Green Tree filed a motion to compel arbitration, stay the action, or dismiss Randolph’s complaint.⁸³ The district court granted Green Tree’s motion to compel arbitration, denied the motion to stay the proceedings, and dismissed Randolph’s claim with prejudice.⁸⁴ On appeal, the Court of Appeals for the Eleventh Circuit determined that, relative to arbitration, the Green Tree arbitration agreement failed to provide “minimum guarantees” that Randolph could vindicate her statutory rights with respect to her

77. *Id.* at 90.

78. *Id.* at 82.

79. *Id.*

80. 15 U.S.C. § 1601 (1998). The Truth in Lending Act (“TILA”) addresses a congressional desire to promote disclosure to consumers regarding credit for consumer transactions. The Congressional findings and declaration of purpose of TILA state:

(a) Informed use of credit. The Congress finds that economic stabilization would be enhanced and the competition among the various financial institutions and other firms engaged in the extension of consumer credit would be strengthened by the informed use of credit. The informed use of credit results from an awareness of the cost thereof by consumers. It is the purpose of this subchapter to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit, and to protect the consumer against inaccurate and unfair credit billing and credit card practices.

(b) Terms of personal property leases. The Congress also finds that there has been a recent trend toward leasing automobiles and other durable goods for consumer use as an alternative to installment credit sales and that these leases have been offered without adequate cost disclosures. It is the purpose of this subchapter to assure a meaningful disclosure of the terms of leases of personal property for personal, family, or household purposes so as to enable the lessee to compare more readily the various lease terms available to him, limit balloon payments in consumer leasing, enable comparison of lease terms with credit terms where appropriate, and to assure meaningful and accurate disclosures of lease terms in advertisements.

Id. As this statutory scheme suggests, TILA was meant to protect consumers from commercial entities that take advantage of lease situations to charge exorbitant fees without disclosure to the consumer.

81. *Green Tree*, 531 U.S. at 83.

82. *Id.*; 15 U.S.C. § 1691 (1998).

83. *Green Tree*, 531 U.S. at 83.

84. *Id.*

allegation of TILA violations.⁸⁵ The court of appeals observed that the arbitration agreement was silent regarding payment obligations of filing fees, arbitrator's costs, and the other arbitration expenses.⁸⁶ This was the basis for the 11th Circuit's decision that the agreement to arbitrate "posed a risk" that Randolph would be unable to vindicate her statutory rights due to "steep" arbitration costs.⁸⁷ The U.S. Supreme Court granted certiorari and reversed.⁸⁸

With respect to the arbitration agreement, the Court noted that "[i]t may well be that the existence of large arbitration costs could preclude a litigant such as Randolph from effectively vindicating her federal statutory rights in the arbitral forum."⁸⁹ However, the Court declined to provide a judicial remedy for Randolph by voiding the arbitration agreement at issue.⁹⁰ The rationale behind that decision suggests that the Court was not persuaded that Randolph made any factual showing that the AAA would conduct the arbitration at issue and that, if it did, Randolph would be charged the filing fee or arbitrator's fee.⁹¹ Because the arbitration agreement at issue was silent on that matter, the Court found little basis to "invalidate the agreement" and undermine the "liberal federal policy favoring arbitration."⁹²

However, the Court's rationale in *Green Tree* opened the door for consumers to allege that arbitration in the consumer context is cost prohibitive—a defense that, as this Note discusses, has been adopted in some state courts. The lack of guidance provided for future plaintiffs in this regard instigated jurisdictional confusion over the evidentiary requirement to assert this new defense. As other commentators have noted, the *Green Tree* decision provided the possibility that an arbitration clause could be deemed unenforceable because of high costs.⁹³ However, the Supreme Court failed to provide

85. *Id.* at 84.

86. *Id.*

87. *Id.*

88. *Id.*

89. *Id.* at 90.

90. *Id.* at 91.

91. *See id.*

92. *Id.* (quoting *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983)).

93. Kay, *supra* note 17, at 546. The party asserting that arbitration is prohibitively expensive bears the burden of showing the likelihood of incurring significant costs. However, the Court declined to provide an evidentiary standard regarding what would be necessary to show prohibitive costs. *See id.*; *see also* Franklin D. Romines II, Note, *The Supreme Court Defines "Final Decisions" Relating to Arbitration Decisions and Ducks the More Important "Costs" Issue*, 2001 J. DISP. RESOL. 363, 373 (arguing that the Supreme Court's *Green Tree* decision did not provide lower courts with a "scintilla" of evidence as to what constitutes prohibitive costs in

guidance as to the evidentiary standard placed on the plaintiffs to prove high costs and receive the opportunity to vindicate their rights in the judicial forum.⁹⁴ Consequently, courts view the type, quality, and amount of evidence necessary to assert the cost prohibitive defense differently. Perhaps because the *Green Tree* case stemmed from a controversy regarding the purchase of a mobile home, subsequent defective or improperly financed mobile home cases best illuminate the success or failure of plaintiffs who assert prohibitive costs.

III. THE COST PROHIBITIVE DEFENSE INTERPRETED IN OTHER JURISDICTIONS

Different jurisdictions have interpreted the Supreme Court's *Green Tree* decision regarding prohibitive costs in various ways. One jurisdiction failed to recognize the pre-arbitration availability of the defense at all, withholding any decision relating to prohibitive costs until after the consumer proceeds through arbitration and proves prohibitive costs in practice.⁹⁵ Another jurisdiction recognized that arbitration may prove prohibitively costly, but refused to allow the defense unless the plaintiff proved that a certain arbitrator would conduct the arbitration and that certain costs would apply.⁹⁶ In contrast, the District Court for the Western District of Virginia held that a plaintiff proved prohibitive costs by producing specific evidence regarding her income and expenses.⁹⁷ Washington also allowed the prohibitive cost defense, although it did not require as comprehensive an evidentiary showing.⁹⁸ In the post-*Green Tree* setting, courts remain divided with respect to the validity of this defense and the proper evidentiary standard required to prove prohibitive costs.⁹⁹

the arbitral context and, consequently, the Court has "invited division among lower courts as to what constitutes inaccessibility."). These authors predicted correctly, as various jurisdictions have treated the availability to and burden on plaintiffs regarding this defense very differently as the cases discussed here demonstrate.

94. Romines, *supra* note 93, at 363.

95. *Conseco Fin. Serv. Corp. v. Wilder*, 47 S.W.3d 335, 343-44 (Ky. App. 2001).

96. *In re FirstMerit Bank*, 52 S.W.3d 749, 756 (Tex. 2001).

97. *Camacho v. Holiday Homes, Inc.*, 167 F. Supp. 2d 892, 895 (W.D. Va. 2001).

98. *Mendez v. Palm Harbor Homes, Inc.*, 111 Wash. App. 446, 450, 45 P.3d 594, 597 (2002).

99. Romines, *supra* note 93, at 373.

A. *Unconscionability in Practice Required: Conseco Finance Servicing Corp. v. Wilder*

Although the decision in *Green Tree* recognized the potential availability of the cost prohibitive defense, courts do not necessarily review arbitration clauses under the theory of merely potentially prohibitive costs. For example, in *Conseco Finance Servicing Corp. v. Wilder*,¹⁰⁰ the Wilders, Kentucky residents, agreed to purchase a mobile home from Southern Living Housing, Inc., a North Carolina corporation with offices in Kentucky.¹⁰¹ The Wilders paid \$15,000 toward the purchase price of \$60,000, and they agreed to pay the remaining \$45,000 balance in monthly installments.¹⁰² The contract signed by the Wilders was a three-page, preprinted, fill-in-the-blank form.¹⁰³ The arbitration clause at issue was in the middle of page three.¹⁰⁴ Like the hypothetical discussed in the Introduction to this Note, the Wilders discovered numerous manufacturing, set-up, and installation defects. They contacted the dealer and manufacturer requesting repairs under their mobile home warranties, but to no avail.¹⁰⁵ Eventually, the Wilders stopped their monthly payments, and Green Tree filed a “Complaint to Foreclose Security Interest” in the Bell Circuit Court, and a Writ of Possession was served on Mr. and Mrs. Wilder.¹⁰⁶ After realizing that they had several causes of action, both contractual and under the Kentucky Consumer Protection Act, the Wilders filed a counter lawsuit.¹⁰⁷ In response, Green Tree

100. 47 S.W.3d 335 (Ky. App. 2001).

101. *Id.* at 337.

102. *Id.*

103. *Id.* at 338.

104. *Id.* The arbitration clause provided:

All disputes, claims or controversies arising from or relating to this Contract or the parties thereto shall be resolved by binding arbitration by one arbitrator selected by you [seller/assignee] with my [buyers'] consent. . . . Notwithstanding anything hereunto the contrary, you retain an option to use judicial (filing a lawsuit) or non-judicial relief to enforce a security agreement relating to the Manufactured Home secured in a transaction underlying this arbitration agreement, to enforce the monetary obligation secured by the Manufactured Home or to foreclose on the Manufactured Home.

Id. at 338–39. This is a prime example of a unilateral arbitration agreement whereby one party, usually the commercial interest, retains the right to judicial and non-judicial relief, and requires the other party, usually the consumer, to arbitrate any claims. *See also* Nahmias, *supra* note 59, at 36 (discussing the prevalence of unilateral arbitration agreements).

105. Brief of Appellee, *supra* note 7, at 1.

106. *Id.* at 3.

107. *Id.* For the full text of the Kentucky Consumer Protection Act, *see* KY. REV. STAT. ANN. §§ 367.110–367.370 (1972).

moved to compel arbitration.¹⁰⁸ The Circuit judge entered an order denying Green Tree's motion, and Green Tree appealed.¹⁰⁹

In asserting the unconscionability of the arbitration clause at issue, the Wilders argued that the unilateral arbitration clause, which allowed Conseco to seek judicial redress of its likeliest claims while reserving the right to arbitrate the Wilders' claims, was oppressively one-sided and unconscionable.¹¹⁰ Moreover, the Wilders asserted that Conseco maximized profits by selling defective mobile homes to low and moderate-income consumers and subsequently refused to repair or replace the homes—even after being ordered to do so by the Kentucky State Fire Marshal.¹¹¹ In response, Conseco asked the court to release it, its manufacturers, and its dealers from having to honor their legal and equitable obligations in the judicial forum by upholding the mandatory arbitration clause against the Wilders.¹¹²

The Kentucky Court of Appeals disagreed with the Wilders' arguments.¹¹³ The court concluded that arbitration is meant to provide for expedited resolution of disputes and that the agreement permits Conseco to litigate rather than arbitrate certain claims—essentially claims asserting its security interest may be litigated expeditiously.¹¹⁴ The court rejected the Wilders' argument that the arbitration clause allowing Conseco the right to litigate claims while requiring the Wilders to submit their claims to arbitration was “unreasonable” or “oppressive.”¹¹⁵ In dicta, however, the court noted that “[s]hould it transpire, however, that the unspecified details of Conseco's arbitration procedure prevent or unfairly hinder the Wilders' from meaningfully presenting their case, the arbitration clause consigning them to that procedure would appear in a different

108. *Id.*

109. *Id.* at 4.

110. *Conseco*, 47 S.W.3d at 342.

111. Brief of Appellee, *supra* note 7, at 4.

112. *Id.* at 4–5.

113. *Conseco*, 47 S.W.3d at 344.

114. *See id.*

115. *Id.* *But cf.* *Luna v. Household Fin. Corp. II*, No. C02-1635L, 2002 U.S. Dist. LEXIS 21761, *31 (W.D. Wa. November 4, 2002) (holding that a one-sided arbitration provision whereby the consumer is forced to submit all claims to arbitration while the commercial interest retains the right to judicial remedies is “one-sided in Household's [commercial interest] favor and overly harsh to borrowers. As such, it weighs in favor of finding the Arbitration Rider substantively unconscionable.”). Household's argument on appeal failed to “address the unfairness of this [unilateral] provision when considered in the larger context of disputes between Household and borrowers. The Arbitration Rider preserves access to the courts . . . for the only context in which Household is likely to bring a claim against borrowers—foreclosure.” *Id.* This directly opposes the *Conseco* court's stance on a unilateral arbitration clause in a consumer contract.

light.”¹¹⁶ The court further stated that “[i]n that event, our ruling today would not preclude the Wilders’ from renewing their objection to the arbitration clause in circuit court on the ground that the clause had proved unconscionable in practice. On the record before us, however, there is no basis for such a conclusion.”¹¹⁷ Focusing on the fact that the Wilders failed to prove the arbitration clause unconscionable in practice, the court relied on a ripeness argument to conclude that the Wilders had to proceed through arbitration in order to prove prohibitive costs.

The Wilders’ brief to the Kentucky Court of Appeals reveals that they were not sophisticated business people.¹¹⁸ In fact, the Wilders’ only source of income was worker’s compensation benefits.¹¹⁹ Although the court suggested that the cost prohibitive defense might, in the future, be available for litigants who prove that arbitration is unconscionable in practice, the court left potential litigants with no meaningful standard to apply.¹²⁰ If the defense was not available to the Wilders, who presumably were of limited means since their only source of income was worker’s compensation benefits, the court provided no guidance as to how unsophisticated or how indigent a consumer would have to be in order to take advantage of the cost prohibitive defense.¹²¹ This may be significant because the court essentially barred the Wilders’ claims because the Wilders could not afford to proceed through arbitration and then return to court with the requisite proof that arbitration proved too expensive in practice.

The Kentucky Court of Appeals distinguished the amount of proof required to assert prohibitive costs from the issue of unconscionability at formation, and the court viewed the issue from the standpoint of unconscionability during performance. To be successful in avoiding the arbitration clause, the Wilders likely should have emphasized that performance of the agreement would be unconscionable. However, the court’s dicta required the Wilders to bring forth evidence of de facto unconscionability such as expended costs in arbitration in order to prevail.

116. *Conseco*, 47 S.W.3d at 344.

117. *Id.*

118. Brief of Appellee, *supra* note 7, at 16.

119. *Id.* at 3.

120. *Conseco*, 47 S.W.3d at 344.

121. *Id.*

B. *The Burden to Prove Prohibitive Costs: In re FirstMerit Bank*

In another defective mobile home case where a court failed to find prohibitive costs, *In re FirstMerit Bank*,¹²² the Texas Supreme Court also failed to provide any guidance regarding how and when it would apply the cost prohibitive defense to mandatory arbitration agreements.¹²³ Pete and Janie de los Santos purchased a mobile home for their daughter and son-in-law from Verde Homes.¹²⁴ The de los Santoses agreed to Verde's "Retail Installment Financing Agreement."¹²⁵ The agreement included an arbitration clause, which required the parties to arbitrate "all disputes, claims, or other matters in question arising out of or relating to this Loan, its interpretation, or validity, performance or the breach thereof."¹²⁶ Verde subsequently assigned the contract to FirstMerit Bank.¹²⁷ Similar to the arbitration clause at issue in *Conseco*, this arbitration clause permitted FirstMerit Bank to seek judicial relief to enforce its security interest, recover the de los Santoses' monetary loan obligation, and foreclose.¹²⁸ After delivery of the mobile home, the de los Santoses tried to revoke acceptance, claiming that the mobile home was defective and that Verde had failed to make certain repairs.¹²⁹ Verde refused to rescind the contract, and the de los Santoses stopped payments on the mobile home.¹³⁰

The de los Santoses then filed suit against Verde Homes claiming breach of contract, revocation of acceptance, breach of warranty, negligence, and fraud.¹³¹ The de los Santoses also claimed numerous violations of various acts including the Deceptive Trade Practices Act, the Fair Debt Collection Practices Act, the Equal Credit Opportunity Act, and the Fair Credit Reporting Act.¹³² The de los Santoses

122. 52 S.W.3d 749 (Tex. 2001).

123. *Id.*

124. *Id.* at 752.

125. *Id.*

126. *Id.*

127. *Id.*

128. *Id.* The arbitration clause at issue required binding arbitration for "all disputes, claims, or other matters in question arising out of or relating to this Loan, its interpretation, validity, performance or the breach thereof." *Id.* The arbitration clause permitted the bank to seek judicial relief to enforce its security interest, recover the buyers' monetary loan obligation, and foreclose, but stated that "the scope of arbitrability is broad and includes, without limitation, contractual, tort, statutory, and caselaw claims." *Id.*

129. *Id.* at 753.

130. *Id.*

131. *Id.*

132. *Id.* For the text of the Consumer Credit Protection Equal Credit Opportunity Act, see 15 U.S.C. §1691 (1998). For the text of the Fair Debt Collection Act, see *id.* § 1692(f).

requested an injunction to enforce their security interest.¹³³ In response, FirstMerit Bank moved to stay the litigation and to compel arbitration.¹³⁴ The trial court denied FirstMerit's motion to compel arbitration. FirstMerit petitioned the Court of Appeals for a writ of mandamus, which was denied.¹³⁵ FirstMerit then appealed to the Texas Supreme Court.¹³⁶

The de los Santos raised several defenses in the Texas Supreme Court including unconscionability, duress, fraudulent inducement, and revocation.¹³⁷ The court noted that Texas favors arbitration, and that the burden was on the de los Santos to prove that arbitration was unconscionable because it was cost prohibitive.¹³⁸ Citing *Green Tree*, the de los Santos argued that the United States Supreme Court had recognized that large arbitration fees could preclude a litigant from vindicating his or her statutory rights.¹³⁹ The Texas Supreme Court, however, noted that *Green Tree* neither indicated nor specified "how detailed a showing of prohibited expense must be," but that "some specific information of future costs was required."¹⁴⁰ Although the de los Santos had testified in sworn affidavits that the AAA charged a minimum \$2000 filing fee and a \$250 per day/per party hearing fee, the Texas Supreme Court concluded that it need not decide whether the costs would be excessive because the de los Santos had provided no evidence that AAA would conduct the arbitration or charge the fees.¹⁴¹ Because the record contained no specific evidence that the de los Santos would be charged excessive fees, the court concluded that the evidence was insufficient to show that plaintiffs would be denied access to arbitration due to costs.¹⁴²

In contrast to the Kentucky Court of Appeals, the Texas Supreme Court in *In re FirstMerit Bank* would likely have sided with

133. *In re FirstMerit Bank*, 52 S.W.3d at 753.

134. *Id.*

135. *Id.*

136. *Id.*

137. *Id.* at 756.

138. *Id.*

139. *Id.*

140. *Id.*

141. *Id.* Notably, it makes little difference whether AAA or some other arbitration organization would conduct the arbitration at issue because the AAA is the most widely used and standardized arbitration organization. If the AAA were to conduct the arbitration in the de los Santos' case, the AAA's fees represent the low-end regarding fees of the various arbitration organizations available. See [name of page of website], American Arbitration Association, at http://www.adr.org/index2.1.jsp?JSPssid=15769&JSPsrc=upload\LIVESITE/Rules_Procedures/Protocols\...\Resources\EduResources\consumer_protocol.html (last visited March 1, 2004).

142. *In re FirstMerit Bank*, 52 S.W.3d at 757.

the de los Santos had they shown that the particular arbitrator of their claims charged excessive fees.¹⁴³ However, the Texas Supreme Court adopted a completely different approach from other jurisdictions applying 'the cost prohibitive defense because it focused solely on whether the fees for arbitration were excessive rather than whether the costs borne by a plaintiff in relation to the income of that plaintiff proved prohibitively costly.¹⁴⁴ Therefore, the Texas Supreme Court looked at the arbitrator's fees, rather than a particular plaintiff's means.¹⁴⁵ While this may produce some consistency, because arbitrator's fees, at least in a particular area, may be similar, this approach does not take into account a particular plaintiff's economic means with regard to those fees.¹⁴⁶

C. Evidence Before Substance: *Camacho v. Holiday Homes*

In contrast to *Conseco* and *In re FirstMerit Bank*, other courts have found that consumer plaintiffs have successfully shown that arbitration is prohibitively costly. However, these courts have varied in the amount of documentation and evidence necessary to prove prohibitive costs.

In *Camacho v. Holiday Homes*,¹⁴⁷ Heidi Camacho purchased a newly manufactured home in March 2000 for herself and her three young children.¹⁴⁸ The contract was on a pre-printed form provided by Holiday Homes.¹⁴⁹ The contract contained an arbitration clause that made no mention of the costs of arbitration or which party would be responsible for those costs.¹⁵⁰ Camacho sued Holiday Homes in March 2001, alleging TILA violations, common law trespass, and

143. *See id.*

144. *See id.*

145. *See id.*

146. *See id.*

147. 167 F. Supp. 2d 892 (W.D. Va. 2001).

148. *Id.* at 893.

149. *Id.*

150. *Id.* The arbitration clause at issue provided:

Arbitration of Disputes and Waiver of Jury Trial: a. Dispute Resolution. Any controversy or claim between or among you and me or our assignees arising out of or relating to the Contract or any agreements or instruments relating to or delivered in connection with this Contract, including any claim based on or arising from an alleged tort, shall, if requested by either you or me, be determined by arbitration, reference, or trial by judge as provided below. . . . YOU AND I AGREE AND UNDERSTAND THAT WE ARE GIVING UP THE RIGHT TO TRIAL BY JURY, AND THERE SHALL BE NO JURY WHETHER THE CONTROVERSY OR CLAIM IS DECIDED BY ARBITRATION, BY JUDICIAL REFERENCE, OR BY TRIAL BY A JUDGE.

Id. at 893.

violations of the Virginia Uniform Commercial Code.¹⁵¹ Camacho filed her suit in forma pauperis, and the court exempted her from the \$150 filing fee.¹⁵² Holiday Homes moved to dismiss for lack of subject matter jurisdiction, or alternatively, to stay the proceedings and compel arbitration pursuant to the arbitration clause contained in the contract.¹⁵³ Camacho opposed Holiday's motion to compel arbitration, arguing that arbitration would prove unconscionable because of the excessive fees and would essentially preclude her from pursuing her claims.¹⁵⁴ Camacho's fees would include an initial filing fee for arbitration of \$1250 and a case fee of \$750 before the case could proceed to an evidentiary hearing.¹⁵⁵ Attorney's fees would not be reimbursed unless the initiating party prevailed before the arbitrator in the final disposition of the case.¹⁵⁶ Holiday argued that the arbitration rules permitted the initiating party to apply for a waiver, reduction, or deferral of arbitration fees, but the court found that, in practice, complete waiver of fees was rarely granted.¹⁵⁷ Moreover, the Commercial Arbitration Rules established that Camacho could not proceed until she pays the arbitrator's fees and expenses and that each party is responsible for those costs.¹⁵⁸ The arbitrator's fee and expenses typically range between \$100 and \$300 per hour, for a minimum of one full day, plus the arbitrator's additional preparation and research time.¹⁵⁹ Camacho argued that the total amount of arbitration to vindicate her claims would cost between \$1200 and \$8000.¹⁶⁰

Camacho presented substantial evidence, including lists of her monthly expenses and income, indicating that the costs of arbitrating her claims would preclude her from pursuing Holiday Homes.¹⁶¹ This evidence included a "declaration of her financial condition."¹⁶² Camacho's declaration stated that she provides sole support for herself and her three children and earns an average weekly income of \$300.¹⁶³ She rarely received the \$600 per year of child support to which she was

151. *Id.* at 894.

152. *Id.*

153. *Id.*

154. *Id.*

155. *Id.*

156. *Id.*

157. *Id.*

158. *Id.*

159. *Id.*

160. *Id.*

161. *Id.*

162. *Id.*

163. *Id.*

entitled, and she attended a local community college part-time to earn an associate degree in sociology.¹⁶⁴ Camacho also provided a comprehensive list of her monthly expenses.¹⁶⁵ These expenses included \$60 to \$75 for electricity, \$20 for the telephone, \$430 for food, and various expenses for her daughter's drug prescriptions and car payments.¹⁶⁶

After recognizing that Camacho was on a very limited income, the court focused on two issues.¹⁶⁷ First, the court had to determine whether the parties agreed to arbitrate their claims.¹⁶⁸ In this case, the court concluded that the parties agreed to arbitrate their claims, notwithstanding the fact that Camacho argued that the initial sentence in the arbitration clause providing that arbitration of any claim shall be determined by arbitration "if requested by you or me," essentially provided for elective arbitration.¹⁶⁹

Second, the court had to determine whether Camacho "adequately demonstrated" that arbitration was financially inaccessible to her.¹⁷⁰ The court compared Camacho's evidence of financial inaccessibility with the evidence produced in *Green Tree* and concluded that "in contrast to the plaintiff Randolph, Camacho has presented substantial evidence that the costs of arbitrating her claims would preclude her from vindicating her federal statutory rights."¹⁷¹ In addition to producing evidence of her own income, Camacho also produced detailed evidence that the arbitrator would cost between \$600 and \$4100 for twenty-four hours and \$1000 in travel fees and expenses.¹⁷² The court also recognized that Camacho was unable to pay the \$150 filing fee to initiate the claim the court considered.¹⁷³ Consequently, the court concluded, "In view of these facts, the court finds that Camacho's limited income affords no margin for expenses of the magnitude required to pay an arbitrator to consider her claim."¹⁷⁴ In contrast to the *Camacho* court's significant evidentiary findings with regard to the plaintiff's income and expenses, the Washington

164. *Id.*

165. *Id.* at 895.

166. *Id.*

167. *Id.*

168. *Id.*

169. *Id.* Camacho also argued that Holiday did not provide her with the opportunity to read the contract prior to signing it. The court held, however, that "[t]he failure to provide such an opportunity is of no consequence" because "[i]t is well settled that a party to a written contract is responsible for 'informing herself of its contents before executing it.'" *Id.* at 896.

170. *Id.*

171. *Id.*

172. *Id.* at 897.

173. *Id.*

174. *Id.*

Court of Appeals did not require as significant a finding regarding whether a plaintiff had shown that arbitration would prove prohibitively costly.¹⁷⁵

Courts in the preceding cases developed a continuum of evidence required to prove prohibitive costs and avoid mandatory arbitration in favor of the judicial forum. These cases illuminate the difficulty in identifying the type, quality, and amount of evidence required to prove prohibitive costs. The court in *Conseco v. Wilder* found no evidence that the Wilders could not afford arbitration unless the Wilders proceeded through arbitration, returned to court, and proved that it was too costly.¹⁷⁶ The *In re FirstMerit Bank* court found the evidence regarding prohibitive costs too speculative absent evidence of a specific commercial arbitrator.¹⁷⁷ In *Camacho*, the court found that the plaintiff had successfully shown prohibitive costs by providing her personal income and an arbitrator's average fees, although she clearly did not need to show that a specific arbitrator would conduct the arbitration at issue.¹⁷⁸ In contrast, a Washington court has adopted this defense without the evidentiary specificity of a plaintiff's economic means as demonstrated by the *Camacho* plaintiff, or the proof of a certain arbitrator that the court required in *In re FirstMerit Bank*.¹⁷⁹

IV. THE COST PROHIBITIVE DEFENSE IN WASHINGTON: *MENDEZ V. PALM HARBOR HOMES*

The Washington Court of Appeals addressed the validity of the cost prohibitive defense for the first time in *Mendez v. Palm Harbor Homes*.¹⁸⁰ In contrast to the Virginia District Court in *Camacho*, the Washington Court of Appeals required a less detailed showing that arbitration would prove prohibitively costly in order to invalidate an arbitration clause in the consumer context.

Significantly, the court noted at the outset of the case that the plaintiff, Wenceslao Mendez, did not complete high school, worked two jobs to earn less than \$20,000 annually, and supported a family of five.¹⁸¹ Mendez purchased a used mobile home for \$12,000 from Palm Harbor Homes at its dealership in Union Gap, Washington.¹⁸² Palm

175. *Mendez v. Palm Harbor Homes, Inc.*, 111 Wash. App. 446, 450, 45 P.3d 594 (2002).

176. 47 S.W.3d 335, 337 (Ky. App. 2001).

177. 52 S.W.3d 749, 756-57 (Tex. 2001).

178. 167 F. Supp. 2d at 894-95.

179. 111 Wash. App. at 465, 45 P.3d at 605.

180. *Id.*

181. *Id.* at 450, 45 P.3d at 597.

182. *Id.*

Harbor's preprinted sales contract contained the following arbitration clause:

Arbitration and Disputes: Disputes arising out of this Agreement are subject to compulsory and binding arbitration in accordance with the following provisions and conditions:

(a) *Enforcement.* Upon the election and written demand by either party showing the existence of a bona fide controversy and to the full extent permitted by law, arbitration shall be the exclusive procedure for resolving disputes and shall be binding upon the parties. Arbitration shall be commenced and enforced pursuant to [Revised Code of Washington] RCW 7.04 and procedure shall be governed by the civil rules for superior courts for the State of Washington and the evidentiary rules thereto. The parties agree arbitration shall be by a three person panel: one selected by each party and one selected by the two arbitrators. Arbitration shall be held in Yakima County, Washington.

(b) *Scope of Arbitration.* Arbitration shall extend to and the arbitrators shall have the power to decide all matters and issues of fact and/or law, including, but not limited to, the existence of the validity of the Agreement as contract including the issue of fraud and inducement or in its construction, performance or breach and enforceability, operation or duration. The arbitrators shall give full force and effect to all lawful terms of the Agreement whether expressed or implied in fact. The arbitrators shall further have power to decide the appropriate remedies, including damages, restitution, awarding of interest, costs and reasonable attorneys' fees, and costs of arbitration. Arbitration shall not be binding on or extend to any lender or other third party who has acquired rights arising out of any financing or consumer credit contracts and/or security agreements which may be a part or supplement the Agreement.¹⁸³

Mendez also signed a separate arbitration agreement, providing in relevant part:

The parties to the Retail Installment Contract or Cash Sale Contract agree that any and all controversies or claims arising out of, or in any way relating to, the Retail Installment Contract or Cash Sale Contract or the negotiation, purchase, financing,

183. *Id.* at 450–51, 45 P.3d at 597–98. Note that this arbitration clause precludes a court from adjudicating whether the clause or contract itself was fraudulently induced.

installation, ownership, occupancy, habitation, manufacture, warranties (express or implied), repair or sale/disposition of the home which is the subject of the Retail Installation Contract or Cash Sale Contract, whether those claims arise from or concern contract, warranty, statutory, property or common law, will be settled solely by means of final and binding arbitration before a three-panel judge of the American Arbitration Association (AAA) in accordance with the rules and procedures of the AAA. Judgment on the arbitration award may be entered in any court having jurisdiction.

....

The parties agree that any contests to the validity or enforceability of this Arbitration Provision... will be determined by arbitration in accordance with the terms of this Arbitration Provision.¹⁸⁴

Subsequent to the formation of the contract to purchase the mobile home, a dispute arose between the parties regarding payment and delivery.¹⁸⁵ Mendez filed a complaint for specific performance or damages against Palm Harbor, alleging violations of the Dealers and Manufacturers Act, RCW section 46.70, and the Consumer Protection Act, RCW section 19.86.¹⁸⁶ Palm Harbor relied on the arbitration agreement to move to stay the proceeding and compel arbitration under RCW section 7.04.¹⁸⁷ In response, Mendez relied on *Green Tree* and opposed the motion to stay the proceeding, arguing that taking his claim to arbitration would be prohibitively costly.¹⁸⁸ Mendez also provided information from AAA, demonstrating that the initial filing fee to submit his claim to arbitration would be \$2000, notwithstanding various other expenses associated with the arbitration.¹⁸⁹ Palm Harbor argued that no Washington authority has allowed an exception to RCW section 7.04 for people of limited financial means.¹⁹⁰

184. *Id.* at 451–52, 45 P.3d at 598. Notice that under *Hurdle v. Fairbanks Capital Corp.*, No. 02-2788, 2002 U.S. Dist. LEXIS 18357, at *20 n.3 (E.D. Pa. Sept. 17, 2002), a court may hold that this clause represents a relationship between a borrower and a lender, and not a consumer and lender. The AAA's Supplementary Procedures for Consumers likely would not apply unless this provision expressly so stated, which it does not. Thus, if the Washington court had stayed this litigation, Mr. Mendez likely would have been responsible for arbitration fees under the commercial rules, a much more costly endeavor.

185. *Mendez*, 111 Wash. App. at 452, 45 P.3d at 598.

186. *Id.*

187. *Id.*

188. *Id.* at 452, 45 P.3d at 598.

189. *Id.* at 452, 45 P.3d at 598–99.

190. *Id.* at 453, 45 P.3d at 599.

The trial court filed a memorandum opinion denying Palm Harbor's motion to compel arbitration.¹⁹¹ The trial court reasoned, "invok[ing] either of the arbitration clauses would deprive the Plaintiff of the opportunity for a hearing on his complaint."¹⁹² The trial court further noted that Palm Harbor had failed to disclose the potential financial burdens on Mendez regarding arbitration, stating, "the total absence of disclosure of the financial burdens on the plaintiff" would deny Mendez the informed choice regarding waiving his access to the judicial forum.¹⁹³ Palm Harbor appealed the trial court's decision.¹⁹⁴

On appeal, the court first addressed whether Mendez's claims were subject to arbitration under RCW section 7.04, 9 U.S.C. § 10 (the FAA), or both.¹⁹⁵ The court noted that the settled law in Washington is that Consumer Protection Act (CPA) and other statutory claims are subject to arbitration under the FAA.¹⁹⁶ However, no controlling authority suggested whether state statutory claims were generally arbitrable.¹⁹⁷ The court held that Mendez's statutory claims were generally arbitrable under RCW section 7.04.¹⁹⁸

The second question presented on appeal involved whether the adhesion contract signed by Mendez was unconscionable.¹⁹⁹ Palm Harbor conceded that the contract was adhesive.²⁰⁰ The court recognized that "adhesion contracts are not necessarily unconscionable" but that ambiguities are construed against the drafter.²⁰¹ Noting that the lack of cost information in an arbitration clause does not render the provision unenforceable, the court approached a solution in equity.²⁰² The court took note of the *Green Tree* decision, and stated that it "highlights the crux of Mr. Mendez's 'access to justice' argument: the cost of arbitration is so high relative to his financial condition and the small size of his primary claim (\$1500) that forcing AAA arbitration with three arbitrators effectively precludes him from pursuing his claims against Palm Harbor."²⁰³ Moreover, the court noted that the circumstances represented the

191. *Id.*

192. *Id.*

193. *Id.*

194. *Id.*

195. *Id.*

196. *Id.* at 454, 45 P.3d at 599.

197. *Id.*

198. *Id.* at 454-57, 45 P.3d at 599-601.

199. *Id.* at 458, 45 P.3d at 601.

200. *Id.* at 459, 45 P.3d at 602.

201. *Id.*

202. *Id.* at 460, 45 P.3d at 602.

203. *Id.* at 461, 45 P.3d at 603.

“antithesis” of access to justice because the \$2000 filing cost represented much less than the “thousands more” anticipated to litigate Mendez’s claims.²⁰⁴ Distinguishing the *Green Tree* plaintiff, the court found that Mendez successfully shifted the burden to the party seeking arbitration by showing the likelihood of incurring prohibitive arbitration costs.²⁰⁵

The Washington Court of Appeals stated: “Washington’s policy favoring arbitration is grounded on the proposition that arbitration allows litigants to avoid the formalities, expense, and delays inherent in the court system.”²⁰⁶ According to the court, however, the policy behind arbitration is defeated when an arbitration agreement triggers prohibitive costs.²⁰⁷ In finding prohibitive costs, the court relied on the trial court’s findings that (1) the arbitration would take a minimum of \$2000 to commence, (2) Mendez is poverty stricken without practical means to arbitrate, and (3) Mendez agreed to arbitrate under the “faulty premise” that arbitration would be less expensive and burdensome to him than the judicial process.²⁰⁸ Specifically, the court recognized the “disparate commercial sophistication and unequal financial footing between the parties.”²⁰⁹

In adopting this defense, the Washington Court of Appeals provided some, but not enough, guidance. The court determined that the level of review is abuse of discretion; that is, a trial court’s decision will not be reversed if it is on tenable grounds and for tenable reasons.²¹⁰ This deferential standard of review allows a trial court more latitude to determine whether a particular plaintiff successfully proves prohibitive costs.²¹¹ The defense “requires the trial judge to consider the particular facts bearing upon equitable unconscionability as well as legal unconscionability.”²¹² The court also would not require precise calculation of the average cost to arbitrate a claim in Washington because precise calculation is not possible without going through arbitration.²¹³

204. *Id.*

205. *Id.* at 462, 45 P.3d at 603.

206. *Id.* at 464, 45 P.3d at 604.

207. *Id.*

208. *Id.* at 466, 45 P.3d at 605.

209. *Id.*

210. *Id.*

211. *See id.* *But cf.* *Conseco Financial Serv. Corp. v. Wilder*, 47 S.W.3d 335, 345 (Ky. App. 2001) (disregarding the lower court’s findings that the arbitration clause at issue was oppressively one-sided and granting Conseco’s motion to stay litigation and compel arbitration).

212. *Mendez*, 111 Wash. App. at 467, 45 P.3d at 606.

213. *Id.*

In addressing Palm Harbor's arguments, the court noted that Mendez failed to provide evidence allowing the reviewing court to compare expected arbitration costs to expected litigation costs.²¹⁴ However, the court here relied on the fact that the filing fee for arbitration is approximately twenty times higher than the filing fee for a court action, which proved dispositive because Mendez would be unable to even get his claim before an arbitrator at that amount.²¹⁵ Palm Harbor also argued that Mendez could avoid AAA arbitration costs by hardship provisions contained in AAA rules.²¹⁶ Refusing to place Mendez at the mercy of the AAA, the court instead recognized that the AAA rarely grants waivers and that such waivers are generally unavailable until after the complaining party has "expended considerable funds in arbitration."²¹⁷

The court next addressed whether the initial costs of arbitration in Mendez's case were "prohibitive."²¹⁸ The court relied on the fact that Palm Harbor conceded that even a \$500 filing fee would likely be "prohibitive" to Mendez in determining that the trial court's finding as to Mendez's inability to pay is "unchallenged" and a "verity on appeal."²¹⁹

After the plaintiff established prohibitive costs, the court determined that the opposing party must then present contrary evidence to enforce arbitration.²²⁰ Because Palm Harbor did not dispute Mendez's claim of being unable to afford the filing fee, did not offer to defray the cost of arbitration pending the outcome, and did not take steps "to limit the plaintiffs' costs of arbitration in a meaningful fashion," Palm Harbor presented no offsetting evidence that would allow enforcement of the arbitration agreement.²²¹ Consequently, in light of Mendez's prohibitive costs to arbitration, and absent contrary evidence from Palm Harbor, Mendez was entitled

214. *Id.* at 468, 45 P.3d at 606.

215. *Id.*

216. *Id.* The Mendez court noted that although the court in *In re FirstMerit Bank*, 52 S.W.3d 749 (Tex. 2001), found the availability of a potential waiver persuasive, "other courts have found such potential waivers unpersuasive because the AAA rarely grants them and they are generally unavailable until after the complaining party has already expended considerable funds in arbitration." Mendez, 111 Wash. App. at 468, 45 P.3d at 606. Consequently, unlike the reasoning the Texas court employed in *In re FirstMerit Bank*, "Palm Harbor's argument on this point is merely speculative." *Id.*

217. Mendez, 111 Wash. App. at 468, 45 P.3d at 606; see also *Camacho v. Holiday Homes, Inc.*, 167 F. Supp. 2d 892, 897 (W.D. Va. 2001).

218. Mendez, 111 Wash. App. at 470, 45 P.3d at 607.

219. *Id.*

220. *Id.*

221. *Id.* (quoting *Ting v. AT&T*, 182 F. Supp. 2d 902, 934-35 (N.D. Cal. 2002)).

to pursue his remedies in a judicial forum.²²² The *Mendez* decision is fair because Mr. Mendez would not have been able to otherwise pursue his claims in arbitration due to his limited means. While the *Wilder* and *In re First Merit Bank* plaintiffs were unable to obtain a judicial remedy because they were not able to prove prohibitive costs, those plaintiffs were similarly economically situated to Mr. Mendez, which suggests that courts are applying the cost prohibitive defense differently in similar situations, violating horizontal equity.²²³

V. LIMITATIONS OF THE COST PROHIBITIVE DEFENSE AND PROPOSALS FOR PROTECTING CONSUMERS FROM COMMERCIAL ARBITRATION COSTS

As discussed previously in this Note, Congress enacted the FAA for a variety of reasons. First, the policy behind the Act was to provide an efficient and cost-reducing method of resolving disputes. The key prerequisite in this regard, however, was that the parties agreeing to arbitrate disputes were on essentially equal footing in terms of bargaining power. As the foregoing cases suggest, commercial interests inappropriately rely on the FAA and unilateral arbitration clauses to circumvent consumer rights. This use does not coincide with congressional intent.²²⁴ Second, arbitration had been viewed with some reluctance by the courts as an ouster of their jurisdiction to hear disputes. In response, Congress enacted the FAA in order to place agreements to arbitrate on the same favored footing as other contractual relationships. Perhaps because of the historical increase in litigation, courts have viewed arbitration agreements not with skepticism and scrutiny, but as a presumptive ouster of their jurisdiction.²²⁵

Problems arise regarding agreements to arbitrate disputes with the development of the adhesive contract whereby a consumer is presented with terms on a “take it or leave it” basis.²²⁶ Commercial entities soon realized that arbitration clauses were a valuable tool to use in consumer contracts to avoid potentially large jury verdicts. As

222. *Id.* at 471, 45 P.3d at 607–08.

223. The term “horizontal equity” typically is applied to taxation considerations and involves whether our tax system treats similarly situated taxpayers similarly. Michael J. Graetz and Deborah H. Schenk, *FEDERAL INCOME TAXATION, PRINCIPLES AND POLICIES* 26 (Rev. 4th ed. 2002). I use the term here only to demonstrate that in the recent cases where courts examine the cost prohibitive defense, similarly situated consumers are being treated differently.

224. See discussion *infra* note 16 and accompanying text.

225. See discussion *infra* note 15 and accompanying text.

226. See *White*, *supra* note 19, at 158. Arbitration agreements in consumer contracts do control a “large quantity. . . of services.” See *id.* As such, the argument that arbitration is more efficient in the consumer context is seriously flawed.

one author suggests, commercial entities use arbitration clauses as a tool to prevent consumers from pursuing claims.²²⁷ Thus, the use of arbitration clauses in consumer contracts minimizes the potential deterrent effect of large jury awards because commercial entities can make defective products with little recourse in the courts. Without the prospect of a jury, consumers are left little leverage to counteract defective manufacturing or deceptive commercial financing practices. This is not the only problem with adhesive arbitration agreements in consumer contracts. Although the cost prohibitive defense attempts to provide a meaningful remedy to those consumers of limited means, it has likely created even more problems and uncertainties. The following proposals may provide concrete remedies that the cost prohibitive defense fails to address.

A. Adhere to the FAA's Legislative History and Purpose

Congress never intended that arbitration should be used in merchant/consumer contracts.²²⁸ The legislative history on this point is clear: members of Congress were specifically concerned that arbitration clauses might be used to thwart consumers by means of adhesive contracts.²²⁹ For this reason, courts should be reluctant to favor arbitration clauses in consumer contracts and be more willing to conclude that these clauses are unconscionable, whether or not consumers prove that they do not have the money to pursue their claims in arbitration. The judiciary's primary function is not to make law; rather, the judiciary ought to interpret the law in light of congressional intent and purpose. Congress enacted the FAA as a method for parties with *equal* bargaining power to resolve disputes with greater ease and efficiency and preserve *commercial* relationships.²³⁰ Congress did not enact the FAA to permit commercial entities to prey on unwitting consumers by selling defective goods and precluding consumer claims by inserting arbitration clauses under which a consumer cannot possibly afford to adjudicate his or her claim.

227. Smith, *supra* note 22, at 1191.

228. See discussion *infra* section II.A.

229. See *id.*

230. See *id.*

B. Equalize the Burden Between Consumers and Commercial Entities

The cost prohibitive defense places the burden solely on the consumer to prove prohibitive arbitration costs.²³¹ Courts have treated the consumer's burden very differently depending on the jurisdiction. In *Conseco*, for example, the court apparently found that the Wilders' potential prohibitive costs unpersuasive because they produced no evidence that they could not afford the cost of arbitration.²³² Despite the fact that the Wilders' sole source of income was worker's compensation payments,²³³ the court concluded that this evidence was insufficient to prove prohibitive costs prior to proceeding through arbitration.²³⁴ The court suggested that if the arbitration clause at issue in *Conseco* proved too costly in practice, the Wilders then might be able to assert the defense.²³⁵ The burden on the Wilders was significant because the Wilders would be required to expend their limited financial resources to submit their claims to arbitration prior to obtaining any assistance from the courts in asserting their claims against *Conseco*.²³⁶

Similarly, in *In re FirstMerit Bank*, the court found that the de los Santos had not shown that arbitration would be prohibitively costly.²³⁷ Although the de los Santos had produced evidence of AAA fees, the court found that the de los Santos produced no specific evidence that they would be charged those fees.²³⁸ Again, this approach suggests that the de los Santos would be required to submit their claim to arbitration and proceed through that process prior to bringing a claim that the fees charged were excessively costly.²³⁹ Undoubtedly, the plaintiffs in these cases spent some money initially litigating the arbitration clause at issue. Because the respective courts deemed the arbitration clause valid, each plaintiff's only available option was to pursue his or her claim in arbitration.

In contrast, the *Camacho* court found that the plaintiff had met her burden of proving the prohibitive costs of arbitration by producing significant evidence of her personal budget.²⁴⁰ Unlike *In re FirstMerit Bank*, the *Camacho* court focused not on the fees likely to be charged a

231. See *Mendez*, 111 Wash. App. at 465, 45 P.3d at 605.

232. See *Conseco*, 47 S.W.3d 335, 344 (Ky. App. 2001).

233. Brief of Appellee, *supra* note 7, at 3.

234. See *id.*

235. *Id.*

236. See *id.*

237. 52 S.W.3d 749, 756–57 (Tex. 2001).

238. *Id.* at 756.

239. *Id.* at 756–57.

240. *Camacho v. Holiday Homes, Inc.*, 167 F. Supp. 2d 892, 895–97 (W.D. Va. 2001).

particular plaintiff by a designated arbitrator,²⁴¹ but rather on a particular plaintiff's income and expenses.²⁴² Consequently, the *Camacho* plaintiff was not required to expend substantial money to go through arbitration prior to bringing a claim that arbitration costs are excessive.²⁴³ Instead, the plaintiff produced documentation regarding her personal financial situation.²⁴⁴ Although requiring the plaintiff to do anything in the face of a unilateral and unconscionable contract seems suspect, the *Camacho* plaintiff at least had access to the information she was required to produce.

However, the *In re FirstMerit Bank* plaintiff would be unlikely to gain access to the total cost of arbitration because such information necessarily requires the plaintiff to submit to arbitration.²⁴⁵ The *Camacho* and *Mendez* approaches are better in this respect because those courts concluded that the evidence required to assert the defense was the type of evidence to which a plaintiff likely has access. Furthermore, the *Camacho* court provided at least some guidance for future litigants, stating that *Camacho* had produced "substantial evidence" that arbitrating her claims would preclude her from pursuing her statutory rights.²⁴⁶ Plaintiffs seeking to successfully

241. *In re FirstMerit Bank*, 52 S.W.3d at 756.

242. *Camacho*, 167 F. Supp. 2d at 895.

243. *See id.*

244. *See id.*

245. Costs to arbitrate a claim under the AAA vary according to the plaintiff's location, the number of days the arbitrator requires to hear the dispute, travel and preparation costs, and initial filing fees. Any estimate of a "typical" arbitration would depend upon the nature and complexity of the claim and the experience of the arbitrator. Also, although the AAA has established the Supplementary Procedures for Consumer-Related disputes, which restrict the amount a consumer must pay to arbitrate a dispute with a business, at least one court has held that the relationship between a consumer and a refinancing institution is one of "a borrower and a lender, and not of a consumer and a business [and therefore] the Supplementary Procedures do not apply in this instance." *Hurdle v. Fairbanks Capital Corp.*, No. 02-2788, 2002 U.S. Dist. LEXIS 18357, at *20 n.3 (E.D. Pa. Sept. 17, 2002) (holding that plaintiff proved prohibitive costs based upon her financial condition and absent proof of a particular arbitrator's fees). This is significant because the Commercial Procedures for AAA do not have similar consumer protections to minimize fees. *See* AAA's Supplementary Rules for Consumer Related Disputes, available at http://www.adr.org/index2.1.jsp?JSPssid=1547&JSPsrc=upload\LIVESITE\Rules\Procedures\National_International\...\focusArea\consumer\AAA236current.htm (last visited March 1, 2004). The *Hurdle* decision suggests that unless a commercial interest explicitly provides that the AAA's consumer Supplementary Procedures apply, arbitration between a consumer and a refinancing institution likely will be conducted under the AAA's commercial rules. *Hurdle*, 2002 LEXIS 18357, at *20 n.3. The commercial rules do not restrict the amount a consumer must pay.

246. *Camacho*, 167 F. Supp. 2d at 896.

assert this defense would be wise to produce documentation of both the arbitrator's potential fees, and their personal financial situation in order to prevail. At least in West Virginia, such documentation likely would constitute substantial evidence of the economic unavailability of arbitration.

C. Address the Inherent Unfairness in Unilateral Arbitration Agreements

Another significant issue with the cost prohibitive defense is that it fails to address the inherent unfairness in forcing arbitration on consumers in adhesive contracts. This problem becomes especially apparent when the commercial interest retains the right to use both judicial and non-judicial remedies, yet leaves the consumer with arbitration as his or her only remedy. The practical effect of these unilateral arbitration clauses is that the commercial entity retains the ability to seek judicial relief to repossess the goods and obtain a deficiency judgment against the consumer. At least in the context of the mobile home cases, a repossession and deficiency judgment likely means that the consumer not only loses his or her home, but also forfeits any down payment and monthly payments to the commercial entity. Rather than providing the cost prohibitive defense in some contexts, courts should invalidate these unilateral arbitration clauses as unconscionable. This would allow consumers to seek immediate judicial relief for claims and allow commercial interests to seek immediate judicial relief to protect their security interests. Even if the contract contained unfair provisions at formation because of the unilateral arbitration clause, invalidating unilateral or otherwise unconscionable arbitration clauses would at least provide equitable remedies to both parties.²⁴⁷

In these cases, arbitration cannot possibly be the best answer to the overburdened judicial system because the commercial interests, particularly in the consumer context, usually retain the unilateral right to use a judicial remedy against the consumer. Thus, the commercial entity clearly continues to burden the judicial forum by bringing its

247. As this article was scheduled for press, Marissa Dawn Lawson of The University of Texas Law School published an interesting article proposing that courts should hold "binding arbitration clauses prima facie unconscionable." Marissa Dawn Lawson, *Judicial Economy at What Cost: An Argument for Finding Binding Arbitration Clauses Prima Facie Unconscionable*, 23 REV. LITIG. 463, 465 (2004). I am not arguing here for prima facie unconscionability; rather, I propose that courts should truly consider the realities of the parties' relative bargaining power and how and why commercial entities use these clauses. In many consumer cases, particularly the ones that I have described, the cost prohibitive defense misses the point because the clauses examined here are likely unconscionable outright, especially considering their unilateral nature, regardless of whether the consumer affirmatively proves that arbitration costs are in fact prohibitive. This was certainly the case in *Conseco*.

claims against the consumer in court, and any efficiency gained by mandatory arbitration significantly decreases. The best solution would be to allow the consumer also to bring claims against the commercial interest in the judicial forum if the commercial interest itself chooses that remedy. This solution would place parties previously on unequal footing at contract formation on equal footing for remedial purposes.

One commentator suggests that courts should not construe a contract to prefer arbitration any more than they should interpret ambiguities in favor of banks or insurance companies:

If parties want pink elephants to proliferate, they may so contract, but the court should interpret ambiguous contracts either evenhandedly or *against* the interest of the drafting party. Congress [has] *never* authorized the Court to put its thumb on the scale to favor arbitration in the commercial or consumer context, and such bias also lacks support as a matter of policy.²⁴⁸

With the development of other equitable contractual remedies such as promissory estoppel, courts have recognized that the sanctity of contractual relationships must be tempered²⁴⁹ if public policy so requires. Courts should interpret agreements to arbitrate similarly. Courts should not adopt a defense to a binding arbitration agreement that is procedural in form and substantive in function in the consumer context; rather, courts should be more willing to apply traditional contract theories, such as unconscionability, to void contracts where one party had no reason to know of his or her obligations under the contract, and where the risk allocation in the contract is substantively unfair.

248. Sternlight, *supra* note 23, at 705 (emphasis added).

249. Grant Gilmore remarked that classical contract theory is being "reabsorbed" into tort by virtue of equitable developments such as promissory estoppel. GRANT GILMORE, *THE DEATH OF CONTRACT* 96 (Ronald K.L. Collins, ed., 1995). He posits that we are approaching a point where "there is really no viable distinction between liability in contract and liability in tort," and that the two areas are "gradually merging and becoming one." *Id.* At least in these cases, the courts' reluctance to invalidate arbitration agreements in consumer-merchant situations as unconscionable appears to fully embrace laissez-faire economics and thus illustrates that the sanctity of contract and contractual relationships still prevails in some measure. For an interesting discussion on this move from "sanctity" to "fairness," see generally K.M. Sharma, *From "Sanctity" to "Fairness": An Uneasy Transition in the Law of Contracts?*, 18 N.Y.L. SCH. J. INT'L & COMP. L. 95 (1999).

D. Require Commercial Entities to Use the AAA's Consumer Protocol in Consumer Contracts

In *Hurdle*, the court held that the AAA's Consumer Protocol did not apply to a contract between a borrower and a refinancing institution because that relationship constituted one of "borrower and lender," not one of consumer and merchant.²⁵⁰ This decision suggests that unless a commercial interest explicitly provides that the AAA's Consumer Protocol, which limits the monetary responsibility of a consumer in arbitration, applies to the contract, courts will construe the arbitration provision to require a commercial procedure.

Commercial procedures do not shift fees to the commercial interest and restrict the amount the consumer must pay to submit his or her claim to arbitration. For this reason, and to increase its bottom line, a commercial entity is unlikely to expressly include a provision in its arbitration clause that provides for disputes to be resolved under any Consumer Protocol unless forced to do so by a state legislature as a matter of public policy.

In order to avoid the issue of prohibitive costs altogether, state legislatures should require commercial entities to permit consumers to use the consumer protocols available under many professional arbitration associations. The practical effect of such legislation would be three-fold. First, it would provide an incentive to properly manufacture and finance goods for retail sale because the manufacturers, dealers, and financing institutions would be liable for the bulk of the costs if a consumer claim proceeds to arbitration and the consumer prevails. Second, it would minimize the potential unconscionability of unilateral arbitration agreements because the consumer would not be forced to forego a judicial remedy in favor of a more costly method to pursue his or her claims. Finally, such a rule would promote efficiency because it would retain the benefits of arbitration, without prohibitive costs: it would further those policies that arbitration was intended to address—judicial inefficiency and significant case loads—while at the same time preserving arbitration as a comparable forum to litigation.

Without legislation protecting a consumer from commercial arbitration rates, which can be extremely burdensome if not economically out of reach, the AAA's Consumer Protocol is nothing more than an illusory promise that arbitration is indeed less expensive than litigation, which the commercial entity can avoid simply by contract. Moreover, consumers are not likely well versed in

250. 2002 LEXIS 18357, at *20 n.3.

arbitration protocols and rules to know that a commercial arbitration will be significantly more expensive than consumer arbitration and to be able to bargain for the use of a Consumer Protocol. Because commercial entities will be more likely to have this knowledge, the legislature should allocate this risk to the commercial entity, not the consumer. Arbitration and litigation should be about choice, and the misuse of arbitration by some commercial entities has fundamentally taken away consumer choice. It is time for legislatures and courts to restore the ability for consumers to choose their forum and allow this fundamental check on our free-market economy to function unimpaired.

VI. CONCLUSION

The cost prohibitive defense relies on several assumptions that are plainly unjustified in light of how commercial entities use arbitration in the consumer context. The first assumption involves arbitration as a comparable forum to litigation. The crux of the issue is that the FAA was enacted as a philosophical alternative to litigation. However, the FAA and its subsequent application by courts to consumer contracts, assumes too much. It assumes that the allocation of risk for non-performance of a contract is evenly apportioned. It assumes that a contract is not adhesive or unconscionable. It assumes that an arbitration clause, which provides for an alternative forum to resolve disputes about the contract, is not adhesive or unconscionable. It assumes that an arbitration clause is procedural, not substantive. As a result, when both the contract and the arbitration clause are adhesive and unconscionable, as is often the case in today's consumer transactions, the practical effect is to reapportion the contractual risks to ensure that the consumer bears the entire burden in these transactions. This shift is particularly egregious in those unconscionable and adhesive arbitration clauses where the commercial entity blatantly retains all of its judicial remedies.

Similarly, the cost prohibitive defense also is procedural because it interposes an evidentiary hearing requirement on the consumer before reaching the substantive issues of adhesion and unconscionability in the arbitration clause itself.²⁵¹ However, any

251. See Sternlight, *supra* note 23, at 705. Ms. Sternlight suggests that arbitration clauses function procedurally, but provide substantive outcomes. The cost prohibitive defense has the exact same function because, in many cases, a failure by the consumer to demonstrate the precise costs of arbitration will allow a court to stay litigation for the consumer's claims and compel arbitration. This outcome is substantive because a consumer may be forced to proceed in arbitration—a remedy that many, like the hypothetical Turner family, would be unable to afford on even a modest income under common commercial arbitration protocols.

failure by the consumer to produce the type, amount, or quality of evidence regarding prohibitive costs produces a substantive result in that the consumer often is prevented financially from bringing his or her claim. The unfortunate result is that the consumer, who wants to remain in the judicial forum to assert traditional and modern remedies such as consumer protection act claims against a commercial entity for breach of the underlying contract, simply cannot argue that the substantive provisions of an arbitration clause are adhesive and unconscionable. Instead, the consumer must carefully and clearly respond to this new court-imposed procedural requirement of "show me the money" that he or she does not have.

This is not to say that arbitration does not have the capacity to adequately resolve the problems with the judicial system, particularly with regard to efficiency and expense. However, if the benefits of arbitration are to be realized, legislators must create, and courts must enforce, certain protections so that arbitration may not be continually misused against consumers. As I have suggested, such protections may well include invalidating unilateral arbitration clauses, requiring that the Consumer Protocol and its fee-shifting provisions apply to all commercial-consumer contracts, recognizing that the relationship between a consumer and a lender, dealer, or manufacturer is not a commercial relationship, and invalidating as unconscionable those arbitration provisions that may preclude a consumer from asserting statutory claims even if the consumer has not proven the particular costs of his or her arbitration. Consumer protection requires our legislatures and courts to do nothing less, and the cost prohibitive defense will not provide the broad-based reforms that these problems warrant.