

## Corporate Hostility to Arbitration

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*In the last thirty years, corporations have aggressively and successfully pushed the Supreme Court to invalidate virtually all state regulation of mandatory arbitration clauses on the ground that the Federal Arbitration Act (FAA) preempts any state law that expresses “hostility” to arbitration. Under current doctrine, the FAA preempts any state law that treats arbitration clauses less favorably than other contracts, or that is premised on the idea that arbitration is inferior to litigation for resolving disputes.*

*Yet, at the same time corporations decry state-law hostility to arbitration, they frequently express their own hostility to arbitration in the way they draft their arbitration provisions. By carving out specific claims from arbitration, adopting procedural rules that approximate litigation, or imposing restraints that make it difficult for their consumers and employees to bring disputes in arbitration, corporations have shown that they believe arbitration to be inferior to litigation in multiple ways.*

*Although scholars have widely debated the Supreme Court’s arbitration jurisprudence, “corporate hostility” to arbitration has gone largely unnoticed. This article examines the various methods by which corporations express hostility to arbitration and argues that this hostility carries significant implications for FAA preemption doctrine. Currently, contract drafters can exempt claims from arbitration because they believe that arbitration is inferior to litigation. But when states seek to regulate arbitration for those same reasons, they are barred from doing so by the FAA. Thus, corporations can exempt claims from arbitration to maximize their self-interest, but states cannot exempt claims from arbitration to protect the public interest.*

*This dichotomy is anti-democratic and results in bad policy. This article proposes that corporate hostility to arbitration demonstrates that not all hostility to arbitration is improper and that states should have greater freedom to regulate arbitration clauses without violating the FAA.*

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## I. INTRODUCTION

Much of the debate surrounding the fairness of mandatory arbitration clauses centers around the question of how widely the Federal Arbitration Act (FAA) preempts state law. That is because many efforts to regulate the arbitration process, or to police the perceived abuses of arbitration, come from state legislatures or from judges who strike down arbitration clauses when they violate state law or public policy.<sup>1</sup>

Yet, most attempts by states to protect their citizens from being forced to submit all disputes with employers or businesses to binding arbitration run headlong into the FAA. According to the U.S. Supreme Court, Congress enacted the FAA in order “to reverse the longstanding judicial hostility to arbitration agreements” that existed in English common law and to place arbitration clauses on “the same footing” as other contracts.<sup>2</sup> As a result, the Act preempts any state law principle, “whether of legislative or

<sup>1</sup> See, e.g., E. Gary Spitko, *Federal Arbitration Act Preemption of State Public-Policy Based Employment Arbitration Doctrine: An Autopsy and an Argument for Federal Agency Oversight*, 20 HARV. NEGOT. L. REV. 1, 3 (2015) (stating that since the mid-1980s, “state legislatures and courts have forcefully sought in a vast array of contexts to regulate and, indeed, to invalidate arbitration agreements that the legislatures or the courts have perceived as threatening the interests of the state, its businesses, its consumers, or its workers”).

<sup>2</sup> *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 24 (1991).

judicial origin”—that directly regulates arbitration clauses, that declares a particular type of dispute non-arbitrable, or that makes arbitration clauses enforceable only if they meet certain minimum fairness standards—on the ground that it singles out arbitration clauses for differential treatment and thus is hostile to arbitration.<sup>3</sup>

Wielding this doctrine, corporations and other proponents of mandatory arbitration have aggressively pushed the courts, and the U.S. Supreme Court in particular, to strike down as preempted any state law that regulates arbitration or that seeks to police the most abusive uses of mandatory arbitration.<sup>4</sup> In recent years, arbitration proponents and corporate entities have convinced the Court to expand the reach of FAA preemption, asserting a *Lochnerian*<sup>5</sup> view that the FAA entrenches a rigid principle of freedom of contract and that it immunizes arbitration clauses from virtually any effort to make arbitration fairer, or to invalidate arbitration when it becomes unfair.<sup>6</sup> Corporate organizations including the U.S. Chamber of Commerce have taken the position that arbitration clauses

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<sup>3</sup> *Perry v. Thomas*, 482 U.S. 483, 492 n.9 (1987). This view that the FAA was intended have such a profound effect has been widely criticized. *See infra* notes 20–22 and accompanying text.

<sup>4</sup> For example, some state legislatures have outlawed mandatory arbitration of personal injury claims, employment-related claims, or insurance claims. Sarah Rudolph Cole, *Uniform Arbitration: “One Size Fits All” Does Not Fit*, 16 OHIO ST. J. ON DISP. RESOL. 759, 785–87 (2001). Similarly, some state courts have adopted rules prohibiting mandatory arbitration of certain claims. *See, e.g., Marmet Health Care Ctr., Inc. v. Brown*, 565 U.S. 530 (2012) (discussing and striking-down ruling of the West Virginia Supreme Court establishing that wrongful death and personal injury claims against nursing homes could not be subject to mandatory arbitration); *Broughton v. Cigna Healthplans of Cal.*, 988 P.2d 67 (1999) (holding that claims for injunctive relief could not be subject to mandatory arbitration).

<sup>5</sup> The high point in the Supreme Court’s elevation of contractual freedom to override laws that promote the health and welfare of citizens is exemplified the famous case of *Lochner v. New York*, 198 U.S. 45, 45 (1905), in which the Court struck down a state regulation limiting the working hours of bakers as violating Due Process protections for freedom of contract. *See* Matthew J. Kolodoski & Candace M. Groth, *The Future of Collective Employment Arbitration Part II: Apocalyptic Warnings, Lochnerizing, and the Right to Contract.*, 24 TEX. J. ON CL & CR. 1, 3 (2018) (speculating about whether the Supreme Court has essentially imposed a *Lochnerian* freedom of contract regime in its arbitration jurisprudence).

<sup>6</sup> *See, e.g.,* Thomas J. Stipanowich, *The Third Arbitration Trilogy: Stolt-Nielsen, Rent-A-Center, Concepcion, and the Future of American Arbitration*, 22 AM. REV. INT’L ARB. 323, 325–26 (2011) (stating that repeated Supreme Court decisions from the last two decades has “vastly expand[ed] the power of companies to impose and control arbitration procedures while tying the hands of state legislatures and courts”). Corporate organizations and organizations that litigate on behalf of corporate interests have advanced this position to the U.S. Supreme Court. *See, e.g.,* Brief for Pac. Legal Found. as Amicus Curiae Supporting Petitioner at 11, *Sonic-Calabasas A, Inc. v. Moreno*, 573 U.S. 904 (2014) (No. 13-856) (arguing the FAA enshrines a policy “in favor of contractual freedom” and asserting that “[t]he freedom to make and enforce contracts reflects a fundamental element of free choice that must be protected” by the FAA).

must be enforced according to their terms. In their view, this means that any state principle that would place limits on how a corporation (or any party) can draft its arbitration clause reflects the same “judicial hostility” to arbitration that the FAA was designed to abolish.<sup>7</sup>

Companies have good reason to aggressively expand FAA preemption. Arbitration clauses are largely drafted by corporations. Mandatory arbitration provisions are often included in non-negotiable, take-it-or-leave-it adhesion contracts in a variety of settings, including employment agreements, consumer contracts, lending and financial services, and car purchases.<sup>8</sup> Consumers and employees have little choice but to accept these terms and often sign agreements without even being aware that they include mandatory arbitration provisions. This allows corporations to stack the arbitration clause in their favor by imposing terms that make it difficult for individuals to vindicate their rights in arbitration, such as bans on aggregate litigation or class actions, secrecy provisions, or shortened statutes of limitations—provisions that both scholars and arbitration opponents claim unfairly advantage corporate parties and harm consumers and employees.<sup>9</sup> The only potential backstop is state legislation

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<sup>7</sup> The Litigation Center of the U.S. Chamber of Commerce has been involved with or has filed an amicus curiae brief supporting a broad reading of the FAA in virtually every arbitration case (and particularly in cases involving FAA preemption) to come before the U.S. Supreme Court in the last ten years, in addition to filing amicus briefs urging the Supreme Court to grant certiorari and reverse state court and lower court decisions refusing to enforce arbitration clauses, and filing amicus briefs in state supreme courts and intermediate appellate courts. It advertises that “The Litigation Center fights for business at every level of the U.S. judicial system, on virtually every issue affecting business, including class actions and arbitration . . .” *U.S. Chamber Litigation Center*, U.S. CHAMBER COM., <https://www.uschamber.com/us-chamber-litigation-center> (last visited July 17, 2019). A search for “arbitration” on the U.S. Chamber Litigation Center’s webpage reveals the wide range of business organizations seeking to expand the scope of the FAA and of FAA preemption. *See id.* (placing “arbitration” in the search function).

<sup>8</sup> *See, e.g.*, Myriam Gilles, *Killing Them with Kindness: Examining “Consumer-Friendly” Arbitration Clauses After AT&T Mobility v. Concepcion*, 88 NOTRE DAME L. REV. 825, 851–53 n.103 (2012) (listing more than 35 major companies that include mandatory arbitration provisions in their standard-form contracts); Imre Stephen Szalai, *The Prevalence of Consumer Arbitration Agreements by America’s Top Companies*, 52 U.C. DAVIS L. REV. ONLINE 233, 236 (2019) (finding that 81 of the top Fortune 100 companies use arbitration clauses in their consumer contracts); Jeff Sovern, *“Whimsy Little Contracts” with Unexpected Consequences: An Empirical Study of Consumer Understanding of Arbitration Agreements*, 75 MD. L. REV. 1, 11–13 (2015) (documenting the increasing use of mandatory arbitration provisions in consumer and employment contracts and noting that companies like PayPal and Verizon require their customers to submit disputes to mandatory binding arbitration). A study by the Consumer Financial Protection Bureau (CFPB) found that arbitration clauses are nearly universal in consumer financial services contracts. CONSUMER FIN. PROT. BUREAU, *ARBITRATION STUDY PRELIMINARY RESULTS: SECTION 1028(A) STUDY RESULTS TO DATE 54* (2013), [https://files.consumerfinance.gov/f/201312\\_cf\\_pb\\_arbitration-study-preliminary-results.pdf](https://files.consumerfinance.gov/f/201312_cf_pb_arbitration-study-preliminary-results.pdf).

<sup>9</sup> *See, e.g.*, David S. Schwartz, *Claim-Suppressing Arbitration: The New Rules*, 87

and public policy doctrine that tries to make arbitration fairer, as the federal government has shown little appetite, outside of a few narrow areas, to address mandatory arbitration.<sup>10</sup> If that backstop is preempted by the FAA, then companies can write their arbitration clauses however they wish, with virtually no oversight whatsoever.

Yet, at the same time that corporations are aggressively challenging efforts to protect consumers and employees as embodying “judicial hostility” to arbitration, they are simultaneously displaying what this article refers to as “corporate hostility” to arbitration. By corporate hostility, I refer to situations where corporations carve-out certain claims, procedures or remedies from their arbitration clauses because they believe that those types of claims are better handled through the courts than through private dispute resolution.<sup>11</sup> When corporations use carve-outs, they signal that litigation is superior to arbitration for certain claims—at the same that they argue in court that state legislatures and judges cannot decide that litigation is superior to arbitration for those same claims.

For example, many parties draft arbitration clauses to exclude claims for injunctive relief because those parties believe that arbitrators are inferior to courts when it comes to enforcing and monitoring an injunction.<sup>12</sup> But when courts have held that injunctive claims cannot be arbitrated because of an arbitrator’s inferior ability to design and manage injunctions, corporations and other pro-arbitration groups have asserted—

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IND. L.J. 239 (2012) (arguing that companies use arbitration clauses to prevent consumers and employees from bringing claims against them); Jean R. Sternlight, *Disarming Employees: How American Employers Are Using Mandatory Arbitration to Deprive Workers of Legal Protection*, 80 BROOK. L. REV. 1309, 1312 (2015). Recent statistics in the employment arena indicate that companies fare better in arbitration than in court. See Alexander J.S. Colvin, *Mandatory Arbitration and Inequality of Justice in Employment*, 35 BERKELEY J. EMP. & LAB. L. 71 (2014) (finding employees fare worse in arbitration than in litigation); David Horton & Andrea Cann Chandrasekher, *After the Revolution: An Empirical Study of Consumer Arbitration*, 104 GEO. L.J. 57, 68 (2015) (analyzing consumer arbitrations from the American Arbitration Association from 2009–2013 and concluding that corporate repeat players win at higher rates in arbitration than others and that consumers prevail less often than shown in previous studies).

<sup>10</sup> Indeed, if anything, Congress seems more interested in expanding mandatory arbitration than in regulating it. In 2017, the Consumer Financial Protection Bureau issued a final rule prohibiting the use of class action bans in arbitration clauses used by financial services companies and other entities covered by the CFPB. Arbitration Agreements, 82 Fed. Reg. 33,210 (July 19, 2017) (to be codified at 12 C.F.R. § 1040). Congress responded by repealing the rule pursuant to the Congressional Review Act, thus permitting financial services companies to continue inserting class action bans into their arbitration clauses. See Jessica Silver-Greenberg, *Consumer Bureau Loses Fight to Allow More Class Action Suits*, N.Y. TIMES (Oct. 24, 2017), <https://www.nytimes.com/2017/10/24/business/senate-vote-wall-street-regulation.html>.

<sup>11</sup> See *infra* Part III (describing different types of carve-outs used in arbitration clauses).

<sup>12</sup> See *infra* notes 75–79 and accompanying text.

often successfully—that such a rule is preempted.<sup>13</sup> In short, corporations are doing the very same things by contract that they are saying state lawmakers and judges are forbidden to do through the democratic process.

While there has been much scholarly consideration of judicial hostility to arbitration,<sup>14</sup> there has been little study of corporate hostility to arbitration.<sup>15</sup> This article seeks to identify and draw out the dissonance between the two and to consider how it should affect the scope of FAA preemption. It argues that corporate behavior in utilizing carve-outs shows that some hostility to arbitration is normal and expected. It is understandable for a contracting party to choose not to require arbitration of claims that it thinks arbitration is ill-suited to resolve. Every decision a company makes about what claims to submit to arbitration, or about the rules of arbitration, reflects a value judgment about the benefit of arbitration versus litigation or the benefit of one kind of arbitration versus another.

If corporations can express hostility to arbitration to further their private interest, state governments should be able to express hostility to arbitration to protect the public interest. This article proposes that the fact that a state regulation may indicate some hostility to arbitration should not automatically trigger preemption. Rather, just as the FAA permits corporate hostility to arbitration, it should permit state hostility to arbitration, unless the state law lacks any rational basis or is motivated by improper purposes.

To be sure, one might argue that there is a fundamental difference between parties contractually agreeing to restrict arbitration and the state imposing limits on arbitration. The FAA reflects a view that arbitration “is a creature of contract” and allows contracting parties, through the process of arm’s-length bargaining and negotiation, to decide which claims to arbitrate and which to litigate, and to tailor the arbitration process to their own needs.<sup>16</sup> But this reasoning has little resonance in the current world of non-negotiable, take-it-or-leave-it agreements. Instead, it merely allows a self-interested party to set the terms of arbitration to favor its own interests, while preventing democratically-elected and democratically-accountable lawmakers and judges from acting in the interest of their citizens who may

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<sup>13</sup> See *infra* notes 143–147 and accompanying text.

<sup>14</sup> See *id.*

<sup>15</sup> There has been some study of corporate use of arbitration carve-outs, most notably by Chris Drahozal, Steven Ware, and Erin O’Connor. See *infra* Part III.A. But there has been no analysis of how corporate practice with respect to carve-outs should be applied to FAA preemption doctrine.

<sup>16</sup> See *AT&T, Inc. v. Concepcion*, 563 U.S. 333, 344 (2011) (stating that the FAA protects the contracting parties’ discretion to adopt “efficient, streamlined procedures tailored to the type of dispute”).

become the victims of unfair and one-sided arbitration provisions.

This article offers a framework for adjusting FAA preemption doctrine to resolve this dichotomy. Many state efforts to regulate or limit arbitration do not reflect a hostility to arbitration in its entirety, but simply to certain aspects of arbitration—such as those that unduly restrict parties’ rights or unfairly favor one side over the other. Just as corporate contract drafters understand that not all arbitration looks the same and that arbitration may be better suited for some claims than others, preemption doctrine should similarly reflect that not all hostility to arbitration is unwarranted and in fact reflects sound policy judgment. Thus, when states pass legislation affecting arbitration, or when state courts adopt common-law rules affecting arbitration, reviewing courts should presume that the legislature or the court has sound reasons for being hostile to arbitration in those circumstances, rather than presuming that the laws are invalid. This approach is both faithful to the FAA and promotes democratic accountability by allowing legislatures to carve-out exceptions to arbitration to protect their citizens just as corporations carve out exceptions to protect their own private interests.

Part II of this article describes the current state of FAA preemption doctrine and how corporate organizations have fought to expand the FAA’s preemptive scope. Part III addresses corporate hostility to arbitration and identifies the ways that parties drafting arbitration clauses carve-out certain claims or remedies from their clauses either because they believe the claims are better suited for litigation or because they want to prevent plaintiffs from bringing claims in arbitration. Part IV examines how the current doctrine of allowing corporate hostility but disallowing legislative hostility undermines democratic accountability and is unwarranted. Part V addresses how corporate hostility to arbitration should affect FAA preemption and offers two proposals for how it could justify narrowing the FAA’s preemptive scope.

## II. THE SCOPE OF FAA PREEMPTION

Driving the doctrine of FAA preemption is the notion that the FAA was enacted to overcome perceived “judicial hostility” to arbitration.<sup>17</sup> The FAA was drafted in the early twentieth century by an American Bar Association Committee and was ultimately enacted by Congress in 1925.<sup>18</sup> According to the Act’s drafters, federal judges at that time were hostile to the idea that arbitration was an adequate substitute for courts and were

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<sup>17</sup> *Allied-Bruce Terminix Cos. v. Bruce*, 513 U.S. 265, 272–73 (1995).

<sup>18</sup> See generally IMRE SZALAI, *OUTSOURCING JUSTICE* 15–95 (2013) (detailing the history of the FAA’s drafting and enactment).

routinely refusing to enforce arbitration clauses.<sup>19</sup> Their refusal derived from two doctrines that the drafters concluded reflected a hostility toward arbitration vis-à-vis courts. The first was the “ouster” doctrine, under which federal courts refused to enforce any provision that would “oust” them of jurisdiction and transfer it to private arbitrators.<sup>20</sup> The second was the “dual agency doctrine,” which “maintained that an arbitrator was merely a dual agent of the parties and, as such, either party could revoke his authority at any time.”<sup>21</sup> As a result, arbitration clauses were essentially “revocable at will” by either party to the agreement.<sup>22</sup> According to the Act’s drafters, judges were refusing to grant specific performance when a party breached an arbitration agreement, simply because the breach involved arbitration.<sup>23</sup> In doing so, they were treating arbitration clauses less favorably than other contracts on the ground that arbitration could not be a substitute for the court’s jurisdiction: hence, “judicial hostility” to arbitration.

The U.S. Supreme Court has interpreted this history to mean that the FAA was enacted to overcome “longstanding judicial hostility” to arbitration agreements that existed dating back to English common law, and to place arbitration agreements on “the same footing” with other

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<sup>19</sup> See Cole, *supra* note 3, at 762–63 (describing how, prior to the FAA’s enactment, many American courts refused to enforce arbitration clauses).

<sup>20</sup> See David S. Schwartz, *Enforcing Small Print to Protect Big Business: Employee and Consumer Rights Claims in an Age of Compelled Arbitration*, 1997 WIS. L. REV. 33, 74 (1997); *Arbitration of Interstate Commercial Disputes: Joint Hearing on S. 1005 and H.R. 646 Before the S. Comm. on the Judiciary and the H. Comm. on the Judiciary*, 68th Cong. 13–15 (1924) (discussing the need for an arbitration statute in order to overcome problems created by the ouster doctrine). The ouster doctrine was criticized for being overly formalistic, reflecting an irrational judicial hostility to arbitration, and unduly interfering with the freedom of contract. See, e.g., *Kulukundis Shipping Co. S/A, v. Amtorg Trading Corp.*, 126 F.2d 978, 982–84 (2d Cir. 1942); *Ezell v. Rocky Mtn. Bean & Elevator Co.*, 232 P. 680 (Colo. 1925); *Park Constr. Co. v. Indep. Sch. Dist. No. 32, Carver Cty.*, 296 N.W. 475, 477 (Minn. 1941) (“Arbitration simply removes a controversy from the arena of litigation. It is no more an ouster of judicial jurisdiction than is compromise and settlement or that peculiar offspring of legal ingenuity known as the covenant not to sue. Each disposes of issues without litigation. One no more than the other ousts the courts of jurisdiction.”). See also Kenneth R. Davis, *When Ignorance of the Law Is No Excuse: Judicial Review of Arbitration Awards*, 45 BUFF. L. REV. 49, 61–63 (1997) (describing some criticisms of the ouster doctrine).

<sup>21</sup> Schwartz, *supra* note 20, at 74. See also Jean R. Sternlight, *Panacea or Corporate Tool?: Debunking the Supreme Court’s Preference for Binding Arbitration*, 74 WASH. U. L.Q. 637, 645 (1996).

<sup>22</sup> See, e.g., Margaret L. Moses, *Statutory Misconstruction: How the Supreme Court Created a Federal Arbitration Law Never Enacted by Congress*, 34 FLA. ST. U. L. REV. 99, 101 (2006); Schwartz, *supra* note 20, at 74.

<sup>23</sup> Moses, *supra* note 22, at 101 (noting that prior to the enactment of the FAA, “a party to an arbitration agreement could at any time prior to the award simply refuse to arbitrate and courts would not enforce the agreement”).



contracts.<sup>24</sup> The Act states that agreements to arbitrate “shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.”<sup>25</sup> In other words, arbitration clauses should be enforced in the same way as any other contract, and they also should be subject to the same defenses—such as duress, unconscionability, or lack of consideration—that apply equally to all contracts.

The principle that any rule treating arbitration clauses less favorably than other contracts embodies a hostility to arbitration has become the driving force in determining the FAA’s power to preempt state law. The Supreme Court has held that Section 2 of the FAA, which makes arbitration clauses enforceable, is substantive law that preempts and overrides conflicting state law.<sup>26</sup>

The particular preemption paradigm in which the FAA operates is known as “implied conflict preemption” or “implied obstacle preemption.”<sup>27</sup> Under this framework, the FAA preempts any “state-law rules that stand as an obstacle to the accomplishment of the FAA’s objectives.”<sup>28</sup> Importantly, state laws need not expressly target arbitration, as the FAA also preempts laws that are implicitly hostile to arbitration. This means that the FAA preempts both rules that forbid arbitration outright, as well as rules or contract principles “that derive their meaning from the fact that an agreement to arbitrate is at issue.”<sup>29</sup> In addition, rules that are generally applicable to all contracts but that target arbitration through “more subtle methods” by interfering with arbitration’s fundamental attributes also are preempted.<sup>30</sup> Interestingly, although the original motivation for the FAA was to overcome judicial refusal to order specific performance of arbitration agreements, courts have applied the FAA to preempt state statutes and regulations in addition to judicially-

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<sup>24</sup> *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 24 (1991).

<sup>25</sup> 9 U.S.C. § 2 (2018).

<sup>26</sup> *Southland Corp. v. Keating*, 465 U.S. 1, 16 (1984).

<sup>27</sup> See *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 343 (2011) (holding that the FAA overrides “state-law rules that stand as an obstacle to the accomplishment of the FAA’s objectives”). In addition to conflict preemption, there are two other preemption doctrines. The doctrine of “express preemption” applies when a federal statute contains an express preemption provision, which is then applied in conformance with the statutory language. *Pac. Gas & Elec. Co. v. St. Energy Res. Conservation & Dev. Comm’n*, 461 U.S. 190, 203 (1983) (“Congress may preempt state authority by saying so in express terms.”). In addition, field preemption occurs where Congress intended to entirely displace any state regulation in a particular area. *Id.* at 204.

<sup>28</sup> *Concepcion*, 563 U.S. at 343.

<sup>29</sup> *Id.* at 339.

<sup>30</sup> *Epic Sys. Corp. v. Lewis*, 138 S. Ct. 1612, 1622 (2018).

created rules.<sup>31</sup>

As a result, both the Supreme Court and lower courts have applied preemption principles to invalidate numerous state laws on the ground that they subject arbitration clauses to less favorable treatment than other contracts and thus conflict with the FAA. For example, courts have found that the FAA preempts rules barring certain types of claims from arbitration,<sup>32</sup> laws that make arbitration agreements unenforceable when they deprive individuals of the ability to vindicate their rights,<sup>33</sup> laws designed to help consumers understand that a contract contains an arbitration clause,<sup>34</sup> laws that do not target arbitration specifically but that only apply to certain categories of contracts,<sup>35</sup> procedural rules relating to who decides a dispute about the enforceability of an arbitration clause or the level of appellate review an arbitration award can receive,<sup>36</sup> and public policy doctrines that attempt to combat abusive practices in arbitration.<sup>37</sup>

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<sup>31</sup> See, e.g., *Perry v. Thomas*, 482 U.S. 483, 492 n.9 (1987) (indicating that “state law, whether of legislative or judicial origin” will be preempted if it singles out arbitration for disfavored treatment and holding that the FAA preempted a provision of the California Labor Code requiring a judicial forum for the resolution of wage disputes). See also *Preston v. Ferrer*, 552 U.S. 346, 356 (2008) (holding that the FAA preempts a state law granting a state commissioner exclusive jurisdiction to decide whether the parties agreed to arbitrate).

<sup>32</sup> See, e.g., *Marmet Health Care Ctr., Inc. v. Brown*, 565 U.S. 530, 532 (2012) (finding that the FAA preempted a West Virginia rule prohibiting mandatory arbitration of wrongful death and personal injury claims against nursing homes).

<sup>33</sup> *Concepcion*, 563 U.S. at 351 (holding that “States cannot require a procedure that is inconsistent with the FAA, even if it is desirable for unrelated reasons” and concluding that even if a class action ban precludes individuals from vindicating their rights states cannot preclude companies from including a class action ban in an arbitration clause).

<sup>34</sup> See *Doctor’s Assoc., Inc. v. Casarotto*, 517 U.S. 681, 688 (1996).

<sup>35</sup> See *Ting v. AT&T*, 319 F.3d 1126, 1147–48 (9th Cir. 2003) (finding that the FAA preempted portions of California’s Consumer Legal Remedies Act because the act was limited to consumers and therefore did not apply to all contracts).

<sup>36</sup> See *Hall Street Assocs., L.L.C. v. Mattel*, 552 U.S. 576, 581–83 (2008) (holding that the FAA precludes rules that expand the grounds for judicial review of an arbitration award beyond the grounds provided in the FAA itself); *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 449 (2006) (finding that FAA requires certain challenges to contracts containing an arbitration clause to be decided by the arbitrator, notwithstanding state-law rules to the contrary).

<sup>37</sup> See *Concepcion*, 563 U.S. at 351. Corporate organizations have pushed strongly for the Supreme Court to hold that the FAA preempts state public policy doctrines meant to promote fairness, when they are applied to arbitration clauses. See, e.g., Brief for Pac. Legal Found. as Amicus Curiae Supporting Petitioner at 12–13, *Sonic-Calabasas A, Inc. v. Moreno*, 573 U.S. 904 (2014) (No. 13-856). Clarence Thomas has expressed some sympathy to the view that the FAA preempts public policy defenses. See *Concepcion*, 563 U.S. at 352–57 (Thomas, J., concurring) (suggesting that the FAA only permits challenges to the formation of an arbitration clause rather than its enforceability, and that the Act would preempt state rules that make arbitration clauses unenforceable on public policy grounds). For one attempt to catalog the wide variety of state laws that courts have found preempted by the FAA, see David S. Schwartz, *State Judges as Guardians of Federalism: Resisting the Federal Arbitration Act’s Encroachment on State Law*, 16 WASH. U. J.L. & POL’Y 129, 154–

The only type of law that will not be preempted, per the FAA's savings clause, is a law that is generally applicable to all contracts, namely one that "exist[s] at law or in equity for the revocation of any contract."<sup>38</sup> For example, a decision finding that an arbitration clause is unconscionable generally will not be preempted because the doctrine of unconscionability applies to all contracts.<sup>39</sup> But even then, a generally applicable rule like unconscionability may be preempted if applying it would interfere with "fundamental attributes of arbitration."<sup>40</sup> For example, the Supreme Court found that a state law declaring that certain arbitration clauses containing class-action waivers were unconscionable and requiring that class claims be resolvable in arbitration was preempted because class-wide proceedings would conflict with arbitration's fundamental attributes of a streamlined, and procedurally flexible process.<sup>41</sup> Additionally, a state rule may be preempted if it is applied disproportionately to arbitration agreements in a way that disfavors arbitration or affects fundamental attributes of arbitration, because the disparate application may reflect back-door hostility to arbitration relative to other contracts.<sup>42</sup>

Although these laws are preempted under the broad mantle that they express hostility to arbitration, the general label of hostility can be broken down into two categories. One category encompasses laws that reflect a view that arbitration, or arbitration in a particular form, is inferior to litigation.<sup>43</sup> For example, a rule requiring that all dispute resolution

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59 (2004) (identifying forty-nine different state statutes that were found preempted by judicial decisions from January 2002 to April 2004).

<sup>38</sup> 9 U.S.C. § 2 (2018). Thus, state law applies if it was enacted "to govern issues concerning the validity, revocability, and enforceability of contracts generally." *Perry v. Thomas*, 482 U.S. 483, 493 n.9 (1987).

<sup>39</sup> See generally Richard Frankel, *Concepcion and Mis-Concepcion: Why Unconscionability Survives the Supreme Court's Arbitration Jurisprudence*, 2014 J. DISP. RESOL. 225 (2014) (describing the state of the unconscionability defense after *Concepcion* and explaining that generally applicable contract rules ordinarily are not preempted, unless they interfere with fundamental attributes of arbitration); see also *Lamps Plus, Inc. v. Varela*, 139 S. Ct. 1407, 1418 (2019) (explaining that neutral, non-discriminatory rules that apply to all contracts, such as unconscionability, ordinarily are not preempted, but that they can be preempted if they conflict with fundamental attributes of arbitration).

<sup>40</sup> *Concepcion*, 563 U.S. at 344.

<sup>41</sup> *Id.* at 344–45.

<sup>42</sup> *Id.* at 342 (indicating that a rule requiring judicially-monitored discovery could be preempted because even though it is facially neutral, "the rule would have a disproportionate impact on arbitration agreements" and could interfere with arbitration's fundamental attributes).

<sup>43</sup> See, e.g., *Andermann v. Sprint Spectrum, L.P.*, 785 F.3d 1157, 1159–60 (7th Cir. 2015) (describing the FAA as establishing that "judges should not allow any preference they might have for judicial resolution of a legal dispute to override the parties' dispute-resolution preferences as embodied in an arbitration clause"); *Armijo v. Prudential Ins. Co. of Am.*, 72 F.3d 793, 801 (10th Cir. 1995) (Jenkins, J., concurring) ("I believe part of the reason for the historical hostility towards arbitration agreements was the conventional

proceedings, including arbitration, must follow the Federal Rules of Evidence indicates a dissatisfaction with streamlined procedures and expresses a preference to make arbitration more like litigation. The rule may be generally applicable, but it evinces a suspicion of arbitration vis-à-vis litigation. A second category encompasses laws that express no view on the relative merits of arbitration versus litigation, but that treat arbitration provisions differently from other contractual provisions. One example is a law that requires arbitration clauses to appear on the front page of a contract in bold print.<sup>44</sup> Both categories may be seen as expressing hostility to arbitration, but for different reasons.

The courts' willingness to apply the FAA to override a wide variety of state laws that affect arbitration clauses is significant. The growing use of mandatory arbitration clauses, particularly by large corporations that impose mandatory arbitration as part of their non-negotiable standard-form contracts with their customers and employees, is enormously controversial. Critics of binding mandatory arbitration claim that it is inferior to litigation because the arbitration system stacks the deck in favor of corporations at the expense of consumers and employees. Arbitration opponents assert that many corporations draft arbitration clauses with terms that are designed to make it difficult or even impossible for individual claimants to succeed, such as by barring aggregate litigation or class actions, shortening statutes of limitations, requiring the parties to keep the arbitration proceedings secret, and by limiting the ability of parties to seek discovery or obtain necessary evidence to support their claims.<sup>45</sup> They also argue that

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wisdom that the litigation process was superior to alternative forms of dispute resolution, such as arbitration."); *Murphy Oil USA, Inc.*, 361 NLRB 774, 815 n.33 (NLRB 2014) (Johnson, Board Member, dissenting) ("[T]he FAA precludes any court, or this Agency, from regarding arbitration as inferior to litigation generally."), *overruled on other grounds by Epic Sys. Corp. v. Lewis*, 138 S. Ct. 1612 (2018).

<sup>44</sup> It is somewhat unclear whether such a law would be preempted, though it likely would. The Supreme Court previously invalidated just such a law in *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996). More recently, however, the Court opined in dicta that state rules making arbitration agreements or specific provisions in those agreements more prominently displayed might not be preempted. *See Concepcion*, 563 U.S. at 347 n.6.

<sup>45</sup> *See, e.g., F. PAUL BLAND ET AL., CONSUMER ARBITRATION AGREEMENTS 4–14* (NCLC 7th ed. 2014) (canvassing the various criticisms of binding mandatory arbitration). The impact of class action bans is hard to understate. By one measure, in the financial services sector alone, the use of class action bans has enriched corporations by more than half a billion dollars per year. The CFPB, in a comprehensive study of arbitration provisions in consumer financial services contracts, found that consumers who initiated individual arbitrations in the years 2010–2011 received total relief of \$172,433, and \$189,107 total debt forbearance. By contrast, during the period of 2008–2012, the study found that class actions involving financial services products provided total relief of \$540 million per year to an average of 70 million consumers a year. And that number does not account for the additional value of any injunctive relief those class actions provided. *See CONSUMER FIN. PROT. BUREAU, ARBITRATION STUDY: REPORT TO CONGRESS, PURSUANT TO*

arbitration creates a “repeat player bias” whereby arbitrators are inclined to support the repeat player—most often the corporation—out of fear that they will not be chosen by the company for future cases if they rule against it, though evidence regarding the bias so far appears inconclusive.<sup>46</sup> Detractors point out that arbitrators act in secret, that arbitrators are not bound to apply the law in the way that judges are, and that the FAA provides for extremely limited judicial review of an arbitrator’s decision.<sup>47</sup> Some recent studies suggest that consumers and employees fare less well in arbitration than they do in litigation.<sup>48</sup>

By contrast, supporters assert that arbitration offers a faster, cheaper and more efficient alternative to litigation.<sup>49</sup> They note that arbitration offers greater predictability to businesses, and helps reduce the passing of litigation costs onto consumers through higher prices.<sup>50</sup> Supporters argue that arbitration may increase access to justice for many individuals who may find that they cannot seek redress in court because litigation has

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DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT § 1028(a), §§ 1.4.3–1.4.7 (Mar. 2015), [https://files.consumerfinance.gov/f/201503\\_cfpb\\_arbitration-study-report-to-congress-2015.pdf](https://files.consumerfinance.gov/f/201503_cfpb_arbitration-study-report-to-congress-2015.pdf) [hereinafter “CFPB ARBITRATION STUDY”].

<sup>46</sup> See e.g., Lisa B. Bingham, *On Repeat Players, Adhesive Contracts, and the Use of Statistics in Judicial Review of Employment Arbitration Awards*, 29 MCGEORGE L. REV. 223 (1998); BLAND ET AL., *supra* note 45, § 1.3.3 (“There is some empirical evidence and a good deal of commentary suggesting that arbitrators do, in fact, have a tendency to favor ‘repeat player’ clients.”). *But see* SEARLE CIV. JUST. INST., CONSUMER ARBITRATION BEFORE THE AMERICAN ARBITRATION ASSOCIATION PRELIMINARY REPORT 13–16 (Mar. 2009), [https://www.adr.org/sites/default/files/document\\_repository/Searle%20Civil%20Justice%20Institute%20Report%20on%20Consumer%20Arbitration.pdf](https://www.adr.org/sites/default/files/document_repository/Searle%20Civil%20Justice%20Institute%20Report%20on%20Consumer%20Arbitration.pdf) (finding no statistically significant repeat-player effect in its analysis of American Arbitration Association data and ascribing any repeat-player effect to better case screening by repeat-players than to arbitrator bias).

<sup>47</sup> Section 10 of the FAA provides the grounds for vacating an arbitrator’s award. Those grounds are mostly limited to whether the award resulted from corruption or fraud, or if the arbitrators grossly exceeded their powers. 9 U.S.C. § 10 (2018). The Supreme Court has interpreted the grounds for vacating an award extremely narrowly. See, e.g., *Major League Baseball Players Ass’n v. Garvey*, 532 U.S. 504, 509 (2002).

<sup>48</sup> See *supra* note 9 and accompanying text.

<sup>49</sup> See, e.g., Alan S. Kaplinsky, *The Use of Pre-Dispute Arbitration Agreements in Consumer Contracts*, 17TH ANN. CONSUMER FIN. SERVICES INST. 221–22 (2012) (describing one study of arbitration participants showing that a majority thought that arbitration was faster, cheaper and simpler than going to court); Dwight Golann, *Developments in Consumer Financial Services Litigation*, 43 BUS. LAW. 1081, 1091 (1988) (“The primary advantage for consumers in binding arbitration is that it offers at least the possibility of a faster and cheaper decisionmaking mechanism for their complaints.”).

<sup>50</sup> See, e.g., *The “Arbitration Fairness Act of 2007”: Hearing on H.R. 3010 Before the H. Comm. on the Judiciary*, 110th Cong. 12–13 (2007) (testimony of Peter B. Rutledge) (arguing that eliminating mandatory arbitration would “increase the costs of dispute resolution, and a portion of these costs would be passed onto employees (in the form of lower wages), consumers (in the form of higher prices) and investors (in the form of lower share prices)”).

become too expensive and time consuming.<sup>51</sup>

Ordinarily, if some legal principle, rule, or regime is considered flawed or unfair in particular ways, state legislatures, state agencies, and courts can correct those flaws through legislation, regulation, and common-law rule making. For example, if state legislators believe that arbitration provides insufficient discovery and thus prevents consumers from proving their claims, or that arbitration is too costly and so consumers cannot afford it, an ordinary response would be to enact laws allowing for greater discovery in arbitration or limiting arbitration costs. But under current doctrine, that is precisely what the FAA bars courts from doing, because such laws arguably reflect a belief that arbitration is an inferior alternative to litigation absent such protections.

As FAA preemption broadens, corporate parties have greater freedom to design their arbitration clauses however they want without being subject to any state regulation designed to counteract their most self-interested impulses. Businesses and organizations acting on behalf of business have aggressively pushed courts to give the FAA an ever-broader preemptive effect so as to displace a greater body of state laws that attempt to regulate arbitration. Thanks in large part to the litigation strategies of business interests, the Supreme Court's view of what counts as hostility to arbitration has expanded in recent years, particularly in the area of class actions.<sup>52</sup>

Thus, states have very limited power to regulate arbitration. Even consumer groups and other advocacy groups that have drafted model state laws related to arbitration have recognized how powerfully the FAA (as currently interpreted) limits state power to engage in legislative reform.<sup>53</sup> For example, the National Consumer Law Center's Model Act is just as notable for what it does not do as for what it does do. It does not invalidate mandatory arbitration as to any specific type of claim, does not require the imposition of any specific contract terms to make arbitration clauses fairer, nor indicate that arbitration is inferior to litigation for resolving particular

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<sup>51</sup> See, e.g., Samuel Estreicher, *Saturns for Rickshaws: The Stakes in the Debate over Predispute Employment Arbitration Agreements*, 16 OHIO ST. J. ON DISP. RESOL. 559, 563–64 (2001) (claiming that mandatory arbitration actually expands opportunities by giving plaintiffs the ability to bring cases that they could not bring in court); see also *Circuit City, Inc. v. Adams*, 532 U.S. 105, 123 (2000) (“Arbitration agreements allow parties to avoid the costs of litigation, a benefit that may be of particular importance in employment litigation, which often involves smaller sums of money than disputes concerning commercial contracts.”).

<sup>52</sup> See Stipanowich, *supra* note 6, at 325–26.

<sup>53</sup> The National Consumer Law Center (NCLC) has drafted a “Model State Consumer & Employee Justice Enforcement Act” that addresses mandatory arbitration. DAVID SELIGMANN, NAT’L CONSUMER L. CTR., THE MODEL STATE CONSUMER & EMPLOYEE JUSTICE ENFORCEMENT ACT (2015).

types of claims. That is likely because such provisions would create a significant risk of being preempted.<sup>54</sup> Rather it focuses on contracts of companies that do business with the state, claims involving public injunctions, defining and applying general unconscionability principles to arbitration clauses, and requiring clear notice of the presence of an arbitration clause in standard form contracts.<sup>55</sup>

The principle of hostility to arbitration as a touchstone of preemption has expanded so widely that it has become unmoored from its original conception. The original form of hostility that the FAA drafters were responding to was judicial refusal to enforce arbitration clauses for any reason. The drafters did not say that arbitration was always superior (or at least equivalent) to litigation, or that arbitration could never operate in an unfair or flawed manner. There is a big gap between saying that legislatures and courts cannot prohibit arbitration altogether and saying that legislatures and courts cannot regulate arbitration to make it fair and balanced for both parties. But current FAA preemption doctrine equates the two.

Yet, hostility to arbitration is not expressed only by state legislatures and courts. Corporations also express hostility to arbitration in multiple ways. This article examines how corporate parties express hostility to arbitration by carving out certain claims, remedies and procedures from their arbitration provisions. Comparing this “corporate hostility” to arbitration to the various kinds of state-government hostility to arbitration that the FAA treats as preempted is instructive in evaluating how far FAA preemption doctrine should reach. This corporate hostility to arbitration is described in the next section.

### III. CORPORATE HOSTILITY TO ARBITRATION

At the same time that corporations argue that state laws regulating arbitration are hostile to arbitration and therefore preempted, they also express their own corporate hostility to arbitration in the way that they draft their arbitration clauses. They do so by deciding which disputes will be arbitrated, under which conditions, and utilizing which procedures. Most commonly, a company’s hostility to arbitration is represented in the form of a carve out. A carve out is where a party includes an arbitration clause in its contract but “carves out” certain claims from arbitration—such as claims for injunctive relief, claims for collection of unpaid debts, or claims to protect trade secrets—and reserves disputes regarding those claims for

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<sup>54</sup> See *id.* at 12–15 (describing the scope and limits of FAA preemption as background for understanding what areas the model act covers).

<sup>55</sup> See *id.*

litigation.<sup>56</sup> In addition, a company may establish specific procedures for arbitration that bring it closer to litigation, say by providing for expanded discovery or requiring the arbitration proceeding to comply with the rules of evidence. I refer to this conduct as “corporate hostility” because most arbitration clauses are drafted by companies, either in standard-form adhesion contracts with consumers and employees, or in their contracts with other companies.<sup>57</sup>

At the outset, it is worth clarifying that there is nothing inherently wrong about expressing hostility to arbitration. The decision to carve out a particular dispute from an arbitration clause simply reflects a judgment by the drafting party that litigation is a superior mechanism to arbitration for resolving that particular dispute. Similarly, adding specific procedural requirements that approximate court procedures may reflect a judgment that judicial-type processes may be preferable to the traditional streamlined arbitration process in certain circumstances. At its broadest level, every decision a company makes about whether to use an arbitration clause, or about the terms of the arbitration clause, reflects a value judgment about the relative merits of arbitration vis-à-vis litigation or the company’s comfort level with arbitral-type proceedings. A corporation’s decision to use an arbitration clause at all may indicate that it feels that, on the whole, arbitration is a superior form of dispute resolution for the corporation as compared to litigation. And vice versa, a decision not to use an arbitration clause may reflect a preference for litigation over arbitration.<sup>58</sup> A company that uses an arbitration clause in its contracts with consumers but not in its contracts with other corporations (a frequent practice)<sup>59</sup> may indicate that the company thinks that arbitration is inferior to litigation for disputes that are likely to arise with other corporations but that arbitration is superior for the types of disputes likely to arise with consumers. In short, companies may have various reasons for preferring one form of dispute resolution to another. That is normal and expected.

This understanding that parties to an agreement will always express some hostility to either arbitration or litigation is implicit in courts’ analysis of the FAA. The Supreme Court has repeatedly stated that it is a

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<sup>56</sup> See *infra* Part III.A.

<sup>57</sup> See *supra* note 8 and accompanying text (documenting the wide range of large companies that utilize contracts requiring parties to submit disputes to binding arbitration).

<sup>58</sup> See, e.g., Theodore Eisenberg & Geoffrey Miller, *The Flight from Arbitration: An Empirical Study of Ex Ante Arbitration Clauses in the Contracts of Publicly Held Companies*, 56 DEPAUL L. REV. 335, 336 (2007) (suggesting that corporations’ decisions not to use an arbitration clause indicates that those actors “prefer litigation to arbitration, encounter obstacles to negotiating mutually satisfactory contract terms that include arbitration clauses, or some combination of these factors”).

<sup>59</sup> See *infra* notes 161–162 and accompanying text.



fundamental principle of the FAA that “arbitration is a matter of contract,”<sup>60</sup> and that one of the main benefits of arbitration is that it “afford[s] parties discretion in designing arbitration processes” that are “tailored to the type of dispute.”<sup>61</sup> When choosing specific “arbitration processes” or specific claims that will be subject to arbitration, the contract drafter is making a value judgment that the terms it imposes are preferable to the terms it rejects, and that the selected terms best serve its interest. Courts have defined hostility, within the meaning of the FAA, as a preference for litigation over arbitration.<sup>62</sup> Under that definition, it is impossible to have choice without also having hostility. In short, the essence of private, contracted-for dispute resolution is a preference for one form of dispute resolution and therefore, by definition, a hostility to the other.

Similarly, when the federal government has regulated arbitration (since it does not have to worry about preemption), it normally has done so by carving out specific types of claims from the FAA’s reach. For example, Congress has restricted the use of mandatory arbitration agreements for whistleblower retaliation claims under the Sarbanes-Oxley Act (SOX),<sup>63</sup> in home mortgage loans,<sup>64</sup> in consumer credit contracts to active duty military personnel or their dependents,<sup>65</sup> in contracts between franchised auto dealers and auto manufacturers,<sup>66</sup> and in contracts between poultry farmers and purchasers.<sup>67</sup> Additionally, the FAA itself expresses hostility to arbitration by carving out contracts of employment for workers engaged in interstate commerce as exempt from the Act.<sup>68</sup>

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<sup>60</sup> *Rent-a-Center, W., Inc. v. Jackson*, 561 U.S. 63, 67 (2010).

<sup>61</sup> *AT&T Mobility, LLC v. Concepcion*, 563 U.S. 333, 344 (2011).

<sup>62</sup> *See supra* note 43 and accompanying text.

<sup>63</sup> 18 U.S.C. § 1514A(e)(2) (2018).

<sup>64</sup> 15 U.S.C. § 1639c(e)(1) (2018).

<sup>65</sup> 10 U.S.C. § 987(e)-(f) (2018).

<sup>66</sup> 15 U.S.C. § 1226 (2018).

<sup>67</sup> 7 U.S.C. § 197c (2018); *see also* *Cole*, *supra* note 3, at 780 (stating that when Congress has regulated arbitration, it “has taken a piecemeal approach, proposing amendments to exempt certain kinds of disputes from the FAA” rather than changing the arbitration process itself).

<sup>68</sup> 9 U.S.C. § 1 (2018) (stating that the FAA does not apply to “contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce.”). Many scholars believe that this provision was intended to exempt all employment contracts from the Act. *See, e.g.*, SZALAI, *supra* note 18, at 191–92 (examining the history surrounding the adoption of the FAA and concluding that the drafters intended to exempt all workplace disputes from the Act); Matthew W. Finkin, “Workers’ Contracts” *Under the United States Arbitration Act: An Essay in Historical Clarification*, 17 BERKLEY J. EMP. & LAB. L. 282 (1996) (same). The Supreme Court, however, held that section 1 only exempts contracts with workers who work directly in interstate commerce, such as interstate transportation workers. *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, 109 (2001). Nonetheless, the Supreme Court also recently clarified that the provision

If hostility to arbitration means, as courts have held, a view that arbitration is inferior to litigation, then corporations express a significant amount of hostility to arbitration. This section looks at two forms of corporate hostility to arbitration. One type is where corporations use carve-outs or other provisions to indicate that they see litigation as superior to arbitration for certain disputes. The second type is where companies use arbitration clauses to express hostility toward both arbitration and litigation—i.e., where the goal of the arbitration clause is not to move a dispute from court to arbitration, but to prevent the dispute from being addressed in any forum. This section suggests that both forms of corporate hostility are intended to promote the corporation's private self-interest, often at the expense of the potential opposing party in any dispute. Finally, it places these corporate practices within the context of the landscape of current litigation involving carve-outs.

*A. Contracts that Reflect a View that Arbitration Is Inferior to Litigation for Resolving Certain Disputes*

First, many companies express hostility to arbitration by carving out various types of claims from their arbitration clauses. These carve-outs indicate that companies believe arbitration to be inferior to litigation for resolving some types of disputes. Professors Christopher Drahozal and Erin O'Connor studied arbitration clauses from various contractual settings to see what kinds of claims were commonly carved out.<sup>69</sup> They found that arbitration clauses commonly carved out (a) claims for injunctive relief; (b) claims to protect confidential information, such as trade secrets; (c) claims that could affect the rights of third parties, such as in rem adjudications; and (d) claims for money owed, such as debt collections.<sup>70</sup> The majority of arbitration provisions they examined had some form of carve-out. In some sectors, nearly all the arbitration clauses had a carve-out.<sup>71</sup> They also found that where there is a large disparity in bargaining power between the parties, "carve-outs will appear at very high rates."<sup>72</sup> This fact suggests that the greater leverage the drafting party has, the more likely the party is

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covers both employees and independent contractors who work in interstate commerce. *New Prime, Inc. v. Oliveira*, 139 S. Ct. 532, 542–43 (2019).

<sup>69</sup> Christopher R. Drahozal & Erin O'Hara O'Connor, *Unbundling Procedure: Carve-Outs from Arbitration Clauses*, 66 FLA. L. REV. 1945, 1951 (2014) [hereinafter "Drahozal & O'Connor"].

<sup>70</sup> *Id.* at 1967–68.

<sup>71</sup> *Id.* at 1967 ("Carve-outs are present in essentially all franchise contract arbitration clauses, nearly two-thirds of domestic and cross-border technology contract arbitration clauses, and about one-half of domestic joint venture agreement arbitration clauses and CEO employment contract arbitration clauses.").

<sup>72</sup> *Id.* at 1968.

to include a carve-out. In turn, this suggests that companies include carve-outs in their arbitration clauses because they perceive carve-outs as advantageous or in their self-interest.

These carve-outs likely indicate a preference for litigation over arbitration for specific types of claims. For example, the fact that companies often exempt claims for injunctive relief reflects that courts may be better suited than arbitrators for issuing, enforcing, and monitoring injunctions. Courts have clearly defined structures for granting emergency relief, such as temporary restraining orders, that offer greater reliability than arbitration.<sup>73</sup> Courts can award emergency relief almost immediately. In arbitration, such relief must await appointment of an arbitrator, and that appointment can be delayed by the party opposing emergency relief.<sup>74</sup>

Similarly, companies carve out injunctive claims because they believe that “courts can more efficiently and effectively resolve disputes involving requests for injunctive relief.”<sup>75</sup> Courts have greater institutional powers, including contempt power, to ensure enforcement of an injunction.<sup>76</sup> Courts also may have a greater ability than arbitrators—whose authority comes from the parties to the dispute—to enforce injunctive relief that may affect the rights of third parties.<sup>77</sup> Further, arbitrators may lack the authority to provide oversight and monitoring of an ongoing injunctive decree, and may also lack the ability to modify, dissolve, or amend an existing injunction.<sup>78</sup> Unlike courts, which retain continuing jurisdiction over final injunctive relief, an arbitrator’s authority often ends at the conclusion of the proceeding, and thus the only way to affect an ongoing injunction would be to initiate a new arbitration proceeding.<sup>79</sup> Given how cumbersome these procedures are, parties may sensibly conclude that arbitration is an inferior venue to court for addressing claims for injunctive relief.

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<sup>73</sup> See Christopher R. Drahozal & Stephen J. Ware, *Why Do Businesses Use (Or Not Use) Arbitration Clauses?*, 25 OHIO ST. J. ON DISP. RESOL. 433, 456 (2010) (“[C]ourts also are better suited than arbitrators to grant emergency relief, such as a temporary restraining order (TRO).”); see also *id.* at 436 (stating that emergency relief is something “arbitration is ill-suited to provide”).

<sup>74</sup> *Id.* at 457.

<sup>75</sup> Drahozal & O’Connor, *supra* note 69, at 1993.

<sup>76</sup> *Id.* at 1971 (“Arbitrators have the authority to order injunctive relief, but without the contempt power of the courts, an arbitrator’s award may prove ineffective.”).

<sup>77</sup> See, e.g., *Broughton v. Cigna Healthplans*, 988 P.2d 67, 77 (Cal. 1999) (discussing how third parties may not be able to benefit from an injunction ordered by an arbitrator); see also Drahozal & O’Connor, *supra* note 69, at 1967–68 (noting that carve-outs are often used for claims that could affect the rights of third-parties to the dispute).

<sup>78</sup> See, e.g., *Broughton*, 988 P.2d at 77 (describing arbitrators’ limitations with respect to injunctive relief).

<sup>79</sup> See *id.*

Claims for the protection of trade secrets and confidential information, protection of intellectual property, or the enforcement of non-compete clauses are often carved out from arbitration.<sup>80</sup> In part, this is because the primary remedy in those disputes is injunctive relief, “a remedy that courts are more effective at providing.”<sup>81</sup> Even as to the underlying merits of intellectual property disputes, such carve-outs can indicate that the company views the right to litigate in court rather than arbitrate as a “legitimate commercial need,” and that courts provide an “extra margin of safety” with respect to intellectual property claims that arbitrators do not.<sup>82</sup>

Claims for money owed, such as debt collection or failure to pay on a loan, also are commonly carved out of arbitration clauses.<sup>83</sup> Parties drafting arbitration clauses may perceive debt collection and loan cases as ones where the law is generally clear and well-defined.<sup>84</sup> In such cases, parties may be suspicious of arbitration because they fear that arbitrators are less likely to follow the law and more likely to split the difference between the parties.<sup>85</sup> When the law is clear, arbitrator expertise is less necessary, and arbitration may be less efficient and more expensive, because parties must take the additional step of confirming the arbitration award in court before the award is final and binding.<sup>86</sup> In fact, studies of business-to-business loan and credit contracts show that loan contracts are unlikely to include arbitration provisions at all, because the disputes are likely to be clear and courts have substantial experience with them.<sup>87</sup>

Companies also tend to carve out claims where the company is more likely to be the plaintiff and the consumer or employee is more likely to be the defendant, while still requiring arbitration for claims where the company is likely to be the defendant. In debt collection claims, companies tend to be plaintiffs and the consumers tend to be defendants.<sup>88</sup>

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<sup>80</sup> See, e.g., *Tompkins v. 23andMe, Inc.*, 840 F.3d 1016, 1021 (9th Cir. 2016) (contract required arbitration of all disputes “[e]xcept for disputes relating to intellectual property rights, obligations, or any infringement claims”).

<sup>81</sup> *Drahozal & O’Connor*, *supra* note 69, at 1967.

<sup>82</sup> *Tompkins*, 840 F.3d at 1031.

<sup>83</sup> *Drahozal & O’Connor*, *supra* note 69, at 1968; see also *Cain v. Midland Funding, LLC*, 156 A.3d 307 (Md. 2017) (arbitration clause allowed lender to bring collection action against credit card debtor in small claims court).

<sup>84</sup> *Drahozal & Ware*, *supra* note 73, at 456, 460–61.

<sup>85</sup> See *id.*

<sup>86</sup> *Drahozal & O’Connor*, *supra* note 69, at 1968; *Drahozal & Ware*, *supra* note 73, at 456.

<sup>87</sup> *Drahozal & Ware*, *supra* note 73, at 460–61 (citing Keith N. Hylton, *Agreements to Waive or to Arbitrate Legal Claims: An Economic Analysis*, 8 SUP. CT. ECON. REV. 209, 231 (2000) (“Most loan contracts are relatively clear, and courts have a great deal of experience with them.”)).

<sup>88</sup> See Stephen J. Ware, *Paying the Price of Process: Judicial Regulation of Consumer Arbitration Agreements*, 2001 J. DISP. RESOL. 89, 97 (2001) (explaining that debt collection

Moreover, many debt collection claims result in default judgments, and companies prefer courts because they can more quickly and easily obtain and enforce those judgments against debtors.<sup>89</sup> Similarly, many arbitration clauses in consumer contracts will carve out claims for self-help repossession of homes, automobiles, or other purchases, or for enforcement of non-compete clauses.<sup>90</sup> Some clauses are even more explicit and simply give the drafting party the right to pursue any claim in court while requiring the consumer or employee to submit any disputes to arbitration.<sup>91</sup>

Such clauses evince a corporate hostility to arbitration as a plaintiff but a preference for arbitration as a defendant. That may mean that companies employing such carve-outs perceive arbitration as systematically favoring defendants and as being an inferior alternative to litigation for plaintiffs. Such a view is not surprising, as there are various ways in which arbitration may favor defendants. For example, arbitration does not provide for nearly as much discovery as litigation (unless the parties agree to import litigation-like discovery procedures into arbitration), which makes it harder for the plaintiff to build his or her case.<sup>92</sup>

Companies also are likely to carve out disputes that carry a risk of high damages awards, or “bet the company” cases.<sup>93</sup> And they do so because they feel that arbitration is ill-suited to address large-dollar claims, in part because of the risk of a high-dollar award combined with arbitration’s extreme limitations on appellate review.<sup>94</sup> When it comes to cases that have potentially large stakes from the company’s perspective,

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and repossession actions comprise nearly all the claims that a lender will affirmatively assert against a borrower).

<sup>89</sup> See *id.* at 97–98.

<sup>90</sup> See *id.* at 97 (“For example, some consumer credit agreements require arbitration of all claims except for: (1) collection actions; and (2) actions to preserve, repossess or foreclose on collateral.”). See also Brief of Appellee Option One Mortg. Corp. at 33–35, *Salley v. Option One Mortg. Corp.*, 925 A.2d 115 (2007) (No. 50 EAP 2005), 2006 WL 2923022 (listing numerous examples of arbitration clauses that carved out foreclosure and repossession claims).

<sup>91</sup> See BLAND ET AL., *supra* note 45, §§ 5.3.1, 6.7.3 (giving examples of cases involving non-mutual arbitration clauses); *White v. ACell, Inc.*, 779 F. App’x 359, 361–62 (6th Cir. 2019) (allowing the employer, but not the employee, to bring certain claims for injunctive relief in court).

<sup>92</sup> See Schwartz, *supra* note 20, at 61 (“The unavailability of discovery skews the system in favor of the corporate defendant. The plaintiff has the burden of production of evidence, much of which the defendant may well possess . . . . The combination of these factors make[s] arbitration a highly attractive alternative to litigation for corporate defendants in many circumstances.”).

<sup>93</sup> See Drahozal & O’Connor, *supra* note 69, at 1992; Drahozal & Ware, *supra* note 73, at 436.

<sup>94</sup> See, e.g., *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 350–51 (2011) (“Arbitration is poorly suited to the high stakes of class litigation . . . . We find it hard to believe that defendants would bet the company with no effective means of review . . . .”).

companies often want “the full panoply of procedural protection afforded by court and full appeal rights” and thus prefer litigation.<sup>95</sup> Companies may worry about a large award that could have a potentially devastating effect on its bottom line.<sup>96</sup> At the same time, however, companies routinely use arbitration clauses that prohibit consumers from bringing class actions, and instead require individualized arbitrations.<sup>97</sup> In defending arbitration in general and class action bans in particular, companies and other supporters of arbitration tout that arbitration is faster and cheaper than litigation, in no small part because of the limited ability to appeal an arbitration award, as appeals add both substantial cost, time, and uncertainty to a case.<sup>98</sup>

While this might not seem noteworthy at first blush, such carve-outs express significant hostility to arbitration. In essence, these carve-outs indicate that the more important a company considers a case to be, the more that arbitration is inferior to the courts for deciding it. Stating that arbitration is acceptable only for cases that do not matter—and not for cases that do matter—conflicts with the view that arbitration is just as good as litigation for resolving disputes.

In addition to situations where drafting parties carve out specific substantive claims from the arbitration provision, they also may use carve-outs to avoid the procedural aspects of arbitration that they find inferior to litigation. Procedural carve-outs include situations where companies require arbitration for most disputes but import litigation-type procedures

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<sup>95</sup> Drahozal & Ware, *supra* note 73, at 454.

<sup>96</sup> *Id.* at 455 (quoting Christopher R. Drahozal & Quentin R. Wittrock, *Is There a Flight from Arbitration?*, 37 HOFSTRA L. REV. 71, 79–80 (2008)). There is a level of hypocrisy about this that feels troubling. This carve-out prioritizes only cases that are large-stakes or important to the company, not ones that are important to the individual plaintiff. A case that involves small dollars for the company’s perspective may be immensely valuable to the consumer. Also, that does not even consider the dignitary interests the consumer has in having his or her case decided fairly and accurately. While companies can preserve appellate rights for judgments that may hurt them, however, the consumer or employee does not get the opportunity to carve out claims where an adverse judgment would be devastating to that individual. This includes cases like bankruptcy that have a dramatic effect on an individual’s future. See BLAND ET AL., *supra* note 45, § 4.3.3 (identifying the debate around what types of claims asserted in bankruptcy can be subject to mandatory arbitration).

<sup>97</sup> The CFPB found that in the financial services sector eighty-five percent of contracts with arbitration agreements, which accounted for ninety-nine percent of overall market share, contained class action bans. CFPB ARBITRATION STUDY, *supra* note 45, at 10. Another study found that all the business-to-consumer arbitration clauses it studied contained a class action ban. Theodore Eisenberg, Geoffrey P. Miller & Emily Sherwin, *Arbitration’s Summer Soldiers: An Empirical Study of Arbitration Clauses in Consumer and Nonconsumer Contracts*, 41 U. MICH. J.L. REFORM 871, 884 (2008).

<sup>98</sup> See, e.g., David K. Taylor, *Binding Arbitration: Limited Appeal Rights – Finality Is the Rule*, CONSTRUCTION AND PROCUREMENT L. NEWS (June 1, 2016), <https://www.bradley.com/insights/publications/2016/06/binding-arbitration-limited-appeal-rights-finality-is-the-rule> (explaining that parties in the construction industry like limited appeal rights because it provides for finality).

into the arbitration process. By doing so, the drafting party signals that it finds the procedural informality and flexibility of arbitration to be inferior to litigation and prefers to make arbitration look more like judicial dispute resolution.

For example, just as companies may carve out particular types of disputes that carry a risk of high damages awards, they may also use a procedural carve-out for high-stakes claims by providing for expanded appeal rights in cases where an award meets or exceeds a particular dollar threshold.<sup>99</sup> Additionally, companies use procedural carve-outs by engrafting litigation-like procedures for certain claims (like high-dollar claims), including procedures for expanded discovery and stricter rules of evidence. In the business-to-business context, it is becoming more common for companies to opt for expanded discovery rather than limited discovery. Studies of contemporary arbitration provisions indicate that “proceedings under standard arbitration rules are likely to include prehearing motion practice and extensive discovery” and that “[a]rbitration hearings are now often preceded by extensive discovery, including depositions.”<sup>100</sup> Parties may also dictate that the Federal Rules of Evidence will apply to any arbitration proceedings.<sup>101</sup>

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<sup>99</sup> See, e.g., *Sanchez v. Valencia Holdings Co., LLC*, 353 P.3d 741 (Cal. 2015) (addressing this type of arbitration clause). In addition, while courts traditionally review arbitration awards under a highly deferential standards, see 9 U.S.C. § 10 (2018) (listing the limited grounds for judicial review of an arbitration award), some companies had provided that courts must review arbitration awards de novo and without the benefit of traditional deference. Carroll E. Neesmann, *Contracting for Judicial Review: Party-Chosen Arbitral Review Standards Can Inspire Confidence in the Process, and Is Good for Arbitration*, DISP. RESOL. MAG. 18–19 (1998). The Supreme Court subsequently held, however, that the FAA prohibits parties from contracting for expanded judicial review or from changing the level of deference afforded to an arbitrator’s decision. *Hall St. Assocs., L.L.C. v. Mattel, Inc.*, 552 U.S. 576 (2008).

<sup>100</sup> Thomas J. Stipanowich, *Arbitration: The “New Litigation”*, 2010 U. ILL. L. REV. 1, 6, 12 (2010). See also Lawrence W. Newman, *Agreements to Arbitrate and the Predictability of Procedures*, 113 PA. ST. L. REV. 1323, 1323 (2009) (noting that business arbitration “has become more similar to litigation—particularly US-style litigation in United States courts—in large part because of increased procedural activity, including discovery”); *Comedy Club, Inc. v. Improv W. Assocs.*, 553 F.3d 1277, 1281 (9th Cir. 2009) (citing arbitration clause that stated: “In any such arbitration, the parties shall be entitled to discovery in the same manner as if the dispute was being litigated in Los Angeles Superior Court.”).

<sup>101</sup> The American Health Lawyers Association (AHLA) Dispute Resolution Service, for example, provides sample language for companies that wish to require arbitrators to follow the Federal Rules of Evidence. See *Guide to Arbitration Clauses*, AHLA DISPUTE RESOLUTION SERVICE 7, <https://www.healthlawyers.org/dr/Documents/Guide%20to%20Arbitration%20Clauses.pdf> (last visited July 12, 2019) (“Sample language: The arbitrator will admit into evidence only documents and testimony that would be admissible under the Federal Rules of Evidence.”). See also John M. Townsend, *Drafting Arbitration Clauses: Avoiding the 7 Deadly Sins*, DISP. RESOL. J. 4 (Feb.–Apr. 2003) (describing arbitration clause that stated: “The arbitration will be conducted in accordance with the Federal Rules

These procedural carve-outs also reveal strong hostility to arbitration and reflect the belief that arbitration leads to less accurate and trustworthy decisions than litigation. From the company's perspective, a primary benefit of arbitration is reducing costs. But it does so at the expense of accuracy. "Narrow discovery rights and evidence rules tend to enable the parties to conserve dispute resolution costs at the expense of accuracy, while broader discovery rights and evidence rules increase the cost of dispute resolution but can increase accuracy."<sup>102</sup> Companies may choose to accept that cost reduction and ensuing loss of accuracy when the case is not important to them, but their priorities switch when the case is important. Consumers and employees, however, do not get to make this choice, as they lack the ability to bargain over the terms of the arbitration agreement that companies impose on them, and thus are often stuck with arbitration regardless of how important the case is to them.<sup>103</sup>

Procedural carve-outs are not limited to high-dollar claims. Companies sometimes use carve-outs for small-dollar claims too. As with debt-collection claims, companies may be more likely to carve out small-dollar claims when the company is more likely to be the plaintiff than the defendant. In the consumer financial services context, a common carve-out is one that permits either party to bring claims of \$1,500 or less in small-claims court rather than in arbitration.<sup>104</sup> The CFPB found in its study that most of the arbitration clauses it reviewed contained a small-claims carve-out.<sup>105</sup> In several product markets, small-claims carve-outs were included in eighty to ninety-three percent of arbitration clauses.<sup>106</sup> Interestingly, the CFPB found that corporations were much more likely to bring claims against consumers in small-claims court than consumers were to bring

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of Civil Procedure applicable in the United States District Court for the Southern District of New York, and the arbitrators shall follow the Federal Rules of Evidence.”).

<sup>102</sup> Drahozal & O'Connor, *supra* note 69, at 1963.

<sup>103</sup> Another explanation is that companies only would want to absorb the extra costs of discovery and evidentiary rules when the case has sufficient financial stakes to make those costs worthwhile. But even if that is true, it does not change the fact that companies find that importing litigation procedures helps promote accuracy, and that litigation procedures are superior to arbitration procedures for producing a correct outcome.

<sup>104</sup> See Arbitration Agreements, 81 Fed. Reg. 32,835 n.71 (May 24, 2016) (codified at 12 C.F.R. 1040) (“[M]ost arbitration agreements in consumer financial contracts contain a ‘small claims court carve-out’ that provides the parties with a contractual right to pursue a claim in small claims court.”) (quoting CFPB ARBITRATION STUDY, *supra* note 45, at 33–34)).

<sup>105</sup> CFPB ARBITRATION STUDY, *supra* note 45, at § 1.4.6 (“Most arbitration clauses that we reviewed contained small claims court carve-outs”).

<sup>106</sup> More specifically, 93% of payday loan arbitration clauses, 85% of mobile wireless arbitration clauses, 83% of private student loan arbitration clauses, 59% of checking account arbitration clauses, and 66.7% of credit card arbitration clauses contained small claims court carve-outs. *Id.* § 2.5.2.



claims in small-claims court against companies.<sup>107</sup> In the jurisdictions the agency examined, consumers brought 870 small-claims actions in 2012, while corporations brought 41,000 small-claims actions, almost all of which were debt collection actions.<sup>108</sup>

The areas that Drahozal and O'Connor studied, with the exception of cell-phone service contracts, fell outside the consumer context, a context where standard-form, non-negotiable arbitration clauses are common.<sup>109</sup> But carve-outs are also common in the consumer and employment contexts. Business-to-consumer arbitration clauses might carve out claims related to debt collection,<sup>110</sup> mortgage foreclosure and repossession,<sup>111</sup> claims that are small enough to proceed in small-claims court,<sup>112</sup> and claims for injunctive relief.<sup>113</sup> In addition, in the consumer and employment contexts, corporations express a more troubling hostility to arbitration—by inserting terms that are designed to prevent consumers and employees from vindicating their rights in any forum, including arbitration. These provisions are discussed below.

#### B. Claim-Suppressing Arbitration Provisions

Some arbitration clauses that appear to be expressing a preference for arbitration over litigation are in fact expressing a hostility to any form of dispute resolution at all. The goal of these provisions is not to shift dispute resolution from court to arbitration but to prevent plaintiffs from vindicating their rights in any forum. This occurs where companies choose arbitration because they can design their arbitration clauses in such a way to make it virtually impossible for an injured consumer or employee to bring a claim in arbitration. If aggrieved parties are required to arbitrate, but the arbitration provision makes it infeasible for aggrieved individual to bring a claim, then corporate defendants are essentially unaccountable for their misconduct. Professor David Schwartz describes these types of provisions as “claim-suppressing” arbitration provisions.<sup>114</sup>

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<sup>107</sup> See *id.* § 1.4.6 (revealing credit card issuers were “significantly more likely” to sue consumers than the other way around).

<sup>108</sup> *Id.*

<sup>109</sup> See, e.g., Szalai, *supra* note 8, at 236. (stating that “the use of arbitration clauses in non-negotiable, adhesionary contracts is widespread in American society” and that meaningful consent and choice “is often lacking in consumer arbitration agreements”).

<sup>110</sup> See Ware, *supra* note 88, at 97.

<sup>111</sup> See *supra* notes 88–89, and accompanying text.

<sup>112</sup> See Ware, *supra* note 90, and accompanying text.

<sup>113</sup> See, e.g., *White v. ACell, Inc.*, 779 F. App'x 359, 361-62 (6th Cir. 2019) (describing employment arbitration agreement that allowed the employer to bring certain claims for injunctive relief in court).

<sup>114</sup> See David Schwartz, *Claim-Suppressing Arbitration: The New Rules*, 87 IND. L.J. 239, 240 (2012) (describing the current arbitration system as follows: “It is claim-

The most high-profile example is an arbitration clause that prohibits parties from proceeding in a class action or other joint proceeding and instead requires individual arbitrations. Class action bans are extremely prevalent in consumer contracts.<sup>115</sup> While the company may appear to be signaling that it finds individual arbitration preferable to class litigation, often the class action bans are used because companies know that injured consumers will not bring individual claims in arbitration.<sup>116</sup> For the types of high-volume, small-dollar injuries that companies often inflict on consumers, individual claims are not feasible, and a class action is the only way to ensure that those injuries can be redressed.<sup>117</sup> Thus, courts have referred to arbitration clauses that ban class actions as “get out of jail free” cards for companies.<sup>118</sup> These clauses do not reflect a preference for the arbitral forum. Rather, they reflect an attempt to keep disputes out of any forum at all.

Claim-suppressing carve-outs are not limited to class action bans. Companies have used arbitration clauses to prohibit individuals from bringing claims for public injunctions in any forum (either court or arbitration), and then have argued that the FAA preempts state-law rules requiring that such claims be available in some forum.<sup>119</sup> Companies also

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suppressing arbitration. It is designed and intended to suppress claims, both in size and number.”).

<sup>115</sup> See *supra* note 97 and accompanying text.

<sup>116</sup> The Consumer Financial Protection Bureau’s study of arbitration clauses found that although tens of millions of consumers are subject to arbitration clauses with financial services companies, on average only 411 individual arbitrations were filed per year, and most of those involved higher-dollar claims that were feasible on an individual basis. See CFPB ARBITRATION STUDY, *supra* note 45, at § 1.4.3; see also Judith Resnik, *Diffusing Disputes: The Public in the Private of Arbitration, the Private in Courts, and the Erasure of Rights*, 124 YALE L.J. 2804, 2804 (2015) (“The result has been the mass production of arbitration clauses without a mass of arbitrations. Although hundreds of millions of consumers and employees are obliged to use arbitration as their remedy, almost none do so—rendering arbitration not a vindication but an unconstitutional evisceration of statutory and common law rights.”).

<sup>117</sup> See *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 617 (1997) (“The policy at the very core of the class action mechanism is to overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights. A class action solves this problem by aggregating the relatively paltry potential recoveries into something worth someone’s (usually an attorney’s) labor.”).

<sup>118</sup> *Szetela v. Discover Bank*, 118 Cal. Rptr. 2d 862, 868 (Cal. Ct. App. 2002); see also Richard Cordray, *Prepared Remarks of CFPB Director Richard Cordray at the Arbitration Field Hearing*, CONSUMER FIN. PROT. BUREAU (Oct. 7, 2015), <http://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-cfpb-director-richard-cordray-at-the-arbitration-field-hearing-20151007> (describing class-action bans as giving companies a “free pass”).

<sup>119</sup> See, e.g., Alison Frankel, *The 9th Circuit Just Blew up Mandatory Arbitration in Consumer Cases*, REUTERS (July 1, 2019), <https://www.reuters.com/article/us-otc-injunction/the-9th-circuit-just-blew-up-mandatory-arbitration-in-consumer-cases-idUSKCN1TW300> (describing arguments from the U.S. Chamber of Commerce and other

use more subtle methods to suppress claims. Provisions that may appear to reflect an attempt to make dispute resolution faster or cheaper in reality may be attempting to suppress or limit claims altogether. Such provisions include distant forums,<sup>120</sup> shortened statute of limitations from a matter of years to a matter of weeks,<sup>121</sup> loser-pays rules (where the losing party pays attorneys' fees and costs to the prevailing party),<sup>122</sup> and limitations on awarding statutory or punitive damages.<sup>123</sup> Those types of provisions either make it too difficult or risky for a consumer to bring a claim in arbitration, or they reduce the potential arbitration award to such a degree that the benefit of bringing a claim in arbitration is not worth the cost. To be sure, courts have found unconscionable some of the most abusive examples of these provisions (at least outside the class-action context where the Supreme Court has indicated that class action bans can be enforced no matter how claim-suppressing they might be),<sup>124</sup>

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corporate groups that a California rule prohibiting arbitration clauses that ban plaintiffs from bringing public injunction actions in either court or arbitration is inconsistent with the FAA).

<sup>120</sup> See, e.g., *Willis v. Nationwide Debt Settlement Grp.*, 878 F. Supp. 2d 1208, 1221 (D. Or. 2012) (provision requiring Oregon residents to travel to San Joaquin County, California, is unconscionable).

<sup>121</sup> See, e.g., *Zaborowski v. MHN Gov. Servs., Inc.*, 936 F. Supp. 2d 1145, 1153 (N.D. Cal. 2013) (arbitration clause set six-month statute of limitations); *Samaniego v. Empire Today LLC*, 140 Cal. Rptr. 3d 492, 499 (Cal. Ct. App. 2012) (arbitration clause set six-month statute of limitations); *Potiyevskiy v. TM Transp., Inc.*, No. 1-13-1864, 2013 IL App (1st) 131864-U, at \*6, \*8 (Ill. Ct. App. Nov. 25, 2013) (arbitration clause set ten-day statute of limitations); *Gandee v. LDL Freedom Enters., Inc.*, 293 P.3d 1197, 1197 (Wash. 2013) (arbitration clause reduced statute of limitations from several years to thirty days); *Hill v. Garda CL Nw., Inc.*, 308 P.3d 635, 638 (Wash. 2013) (arbitration clause reduced statute of limitations to fourteen days).

<sup>122</sup> See e.g., *Newton v. Am. Debt Servs., Inc.*, 549 F. App'x 692, 694 (9th Cir. 2013) (arbitration clause contained "loser pays" provision); *Zaborowski*, 936 F. Supp. 2d at 1154 (arbitration "losers pays" provision); *Winston v. Academi Training Ctr., Inc.*, No. 1:12-CV-767, 2013 WL 989999, at \*2 (E.D. Va. Mar. 13, 2013) (refusing to enforce arbitration provision that required plaintiffs to pay all fees and costs even though the False Claims Act allows prevailing plaintiffs to collect attorney's fees); *Ajamian v. CantorCO2e, L.P.*, 137 Cal. Rptr. 3d 773, 799–800 (Cal. Dist. Ct. App. 2012) (arbitration provision required employee to pay employer's attorneys' fees if employer prevailed, but did not require employer to pay employee's fees if employee prevailed); *Gandee v. LDL Freedom Enters., Inc.*, 293 P.3d 1197, 1200–01 (Wash. 2013) (striking down "loser pays" rule as unconscionable as applied to the plaintiff).

<sup>123</sup> See, e.g., *Newton*, 549 F. App'x at 694 (arbitration clause precludes certain statutorily authorized damages); *Zaborowski*, 936 F. Supp. 2d at 1155 (arbitration provision barred punitive damages); *Ajamian*, 137 Cal. Rptr. 3d at 798–99 (arbitration provision precluded arbitrators from awarding special or punitive damages, but permitted the corporate party to recover liquidated damages on top of other damages); *Franks v. Bowers*, 116 So. 3d 1240, 1240 (Fla. 2013) (arbitration clause precluded damages awardable under the state's Medical Malpractice Act); *Brown v. MHN Gov. Servs., Inc.*, 306 P.3d 948, 955 (Wash. 2013) (same).

<sup>124</sup> See Frankel, *supra* note 39, at 242–49 (cataloging and discussing cases).

notwithstanding defendants' arguments that the FAA preempts state unconscionability doctrine. But these examples highlight that many companies use these provisions not because they like the arbitration process, but because these provisions can help them avoid being subjected to any dispute resolution process at all.

Corporations' use of anti-severability provisions in conjunction with claim-suppressing provisions like class action bans reveal another layer of corporate hostility to arbitration. While some arbitration provisions include severability clauses—clauses that state that if one portion of the arbitration clause is declared unenforceable, the rest of the clause will remain valid and binding<sup>125</sup>—it also is common for companies to use an anti-severability clause. These clauses state that if a particular aspect of the arbitration provision is invalidated, the entire arbitration clause shall be eliminated, and parties will be free to bring any disputes in court.

Anti-severability clauses are quite revealing and indicate that, as a general matter, companies find arbitration inferior to litigation. When a company drafts an arbitration clause and inserts it into its contracts, the company is not saying that arbitration is preferable to litigation without qualification. It is saying that it finds arbitration superior under the specific conditions and limitations that it has written into its arbitration provision. An anti-severability clause shows that if a court were to declare one or more of those conditions invalid or unenforceable, the drafting party no longer considers arbitration to be superior to litigation and would prefer to use the court system.

Anti-severability provisions are common and often are used in conjunction with a class action ban.<sup>126</sup> For example, in the recent Supreme Court case of *DIRECTV v. Imburgia*,<sup>127</sup> DIRECTV's arbitration clause stated that if the class action ban were to be found unenforceable, then the entire arbitration clause would become unenforceable.<sup>128</sup> Through this

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<sup>125</sup> See, e.g., Citi 2017 Employment Arbitration Policy at 67, para. 28 (on file with author) (“If any part or provision of this Policy is held to be invalid, illegal or unenforceable, such holding won’t affect the legality, validity or enforceability of the remaining parts and each provision of this Policy will be valid, legal and enforceable to the fullest extent permitted by law.”).

<sup>126</sup> CFPB ARBITRATION STUDY, *supra* note 45, at § 1.4.1 (finding that many of the arbitration clauses used in consumer financial services contracts included an anti-severability provision in conjunction with a class action ban); Eisenberg, Miller & Sherwin, *supra* note 97, at 884–85 (finding that 60% of class action waivers in consumer arbitration clauses that the author studied contained an anti-severability provision).

<sup>127</sup> *DIRECTV, Inc. v. Imburgia*, 136 S. Ct. 463 (2015).

<sup>128</sup> *Id.* at 469–71 (describing and interpreting an anti-severability clause used by DIRECTV which stated, in relevant part, “[i]f . . . the law of your state would find this agreement to dispense with class arbitration procedures unenforceable, then this [arbitration provision] is unenforceable”); see also JP Morgan Chase NA Arbitration Agreement (2019)

provision, DIRECTV expressed a hostility to any mandatory arbitration—individualized or joint—unless the arbitration clause contained a class action ban. The reason that anti-severability clauses are so common is that many corporations are fearful of, and hostile to, class arbitration. In fact, corporations have been quite clear that while they dislike class actions, they dislike class arbitration even more. Companies find that class litigation, with its procedural formalities and appellate rights, is far superior to class arbitration for protecting their rights. The United States Chamber of Commerce has described class arbitration as follows: “Class arbitration is a worst-of-all-worlds Frankenstein’s monster: It combines the enormous stakes, formality and expense of litigation that are inimical to bilateral arbitration with exceedingly limited judicial review of the arbitrators’ decisions.”<sup>129</sup> Stating that class actions, if allowed, must proceed in court rather than arbitration is consistent with the corporate preference for carving out “bet the company” cases.

Moreover, this type of anti-severability clause, while ostensibly indicating a hostility only to class arbitration, actually evinces hostility to all mandatory arbitration, both joint and individual. The anti-severability provision does not say that if the class action ban is declared unenforceable, then all class proceedings can proceed in court while individual cases will be sent to arbitration. It eliminates mandatory arbitration for all claims. Indeed, corporate organizations have been quite frank in stating that if they could not impose a class action ban as a condition of arbitration, they would walk away from arbitration entirely, including arbitration of individual claims.<sup>130</sup> The breadth of their statements, and of the anti-severability provisions that companies like DIRECTV use, suggests that companies never wanted their disputes to be resolved in arbitration. Rather, companies use arbitration to eliminate any dispute resolution at all.

### C. Current Litigation Regarding Carve-Outs

Although carve-outs are sometimes discussed in litigation, courts have not addressed carve-outs in terms of determining what is an appropriate or

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(on file with author) (“If these terms prohibiting class, representative, or consolidation procedures are held to be legally unenforceable for any reason with respect to a Claim, then the Claim must be handled through litigation in court instead of by arbitration.”).

<sup>129</sup> Brief of Chamber of Commerce of the United States of America as Amicus Curiae Supporting Plaintiff-Appellants at 9, *Marriott Ownership Resorts, Inc. v. Sterman*, No. 15-10627 (11th Cir. Apr. 1, 2015).

<sup>130</sup> See, e.g., Richard Frankel, “What We Lose in Sales We Make Up in Volume”: *The Faulty Logic of the Financial Services Industry’s Response to the Consumer Financial Protection Bureau’s Proposed Rule Prohibiting Class Action Bans in Arbitration Clauses*, 48 ST. MARY’S L.J. 283, 296 (2016) (documenting how businesses have said they would abandon arbitration if they could not ban class actions).

inappropriate level of hostility to arbitration for purposes of FAA preemption. When courts have addressed carve-outs, they generally have indicated that it is entirely acceptable for private parties to express hostility to arbitration, or to express the view that arbitration is inferior to litigation, by using carve-outs.

Carve-outs are sometimes discussed in determining whether a particular dispute falls within the carve-out and is not subject to arbitration,<sup>131</sup> or in determining whether an arbitration clause should be given a broad or a narrow interpretation.<sup>132</sup> Some parties also have argued that arbitration clauses with extremely broad carve-outs that give one party the right to bring any claim in court lack consideration because they do not place any obligation on that party. Courts have differed about whether an arbitration clause becomes unenforceable in that circumstance.<sup>133</sup>

Carve-outs also can be relevant to challenges to an arbitration clause's enforceability. Some parties have argued, and courts have gone in different directions, that "non-mutual" arbitration clauses are unconscionably one-sided if they allow the drafting party to bring most of the claims it would want to pursue in court while binding the other side to arbitration for the claims that party is most likely to pursue.<sup>134</sup> But even in this context, courts acknowledge that it is perfectly legitimate for a party to express hostility to arbitration. In fact, courts are less likely to find a non-mutual arbitration clause unconscionable if a party provides a business justification for the carve-out.<sup>135</sup> Ironically, in this context, expressing hostility to

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<sup>131</sup> See, e.g., *FT & T Consulting Inc. v. Cargowise EDI Inc.*, No. 09 C 1141, 2009 WL 1904415, at \*5 (N.D. Ill. June 30, 2009) (finding claims not arbitrable when the arbitration clause specifically excluded disputes relating to performance obligations); *Rebolledo v. Tilly's, Inc.*, 175 Cal. Rptr. 3d 612, 616 (Cal. Ct. App. 2014) (arbitration clause that excluded claims falling within jurisdiction of State Labor Commissioner excluded all statutory wage claims that could be brought in an administrative proceeding before Labor Commissioner, regardless of whether claim was actually brought).

<sup>132</sup> See, e.g., *Local 827, Int'l Bhd. of Elec. Workers, AFL-CIO v. Verizon N.J., Inc.*, 458 F.3d 305, 311 (3d Cir. 2006) (interpreting arbitration clause in collective bargaining agreement narrowly when the clause referred to five specific types of disputes to be arbitrated); *Simon v. Pfizer, Inc.*, 398 F.3d 765, 775–76 (6th Cir. 2005) (stating that if arbitration clause is limited to specific statutory claims it should not be interpreted to extend broadly to other statutory claims).

<sup>133</sup> See *BLAND ET AL.*, *supra* note 45, § 5.3.1 (discussing this issue and citing cases).

<sup>134</sup> See *BLAND ET AL.*, *supra* note 45, § 6.7.3 (discussing the issue of whether non-mutual arbitration clauses are unconscionable and citing cases).

<sup>135</sup> See, e.g., *Tompkins v. 23andMe, Inc.*, 840 F.3d 1016, 1030–31 (9th Cir. 2016) (finding that carve-out for intellectual property claims was not unconscionable because the defendant had a "legitimate business need" for the "extra margin of safety" that litigation provides); *Delmore v. Ricoh Ams. Corp.*, 667 F. Supp. 2d 1129, 1138 (N.D. Cal. 2009) (finding that arbitration agreement that carved-out claims for injunctive relief for breaches of confidentiality was not unconscionable because courts are superior to arbitrators in addressing claims for injunctive relief); *Torrance v. Aames Funding Corp.*, 242 F. Supp. 2d

arbitration, or explaining why some disputes are better addressed in litigation, makes the arbitration clause stronger and more impervious to challenges to its enforceability.

In other cases, courts have recognized that arbitration is inferior to litigation for certain claims,<sup>136</sup> and, paradoxically, have used that to justify FAA preemption of a rule allowing such claim to proceed in arbitration. Most notably, in *AT&T Mobility v. Concepcion*, the Supreme Court relied on corporate arguments about why arbitration is inferior to litigation for class proceedings to justify the use of class action bans and also to prohibit states from adopting laws that would place arbitration and litigation on equal footing with respect to class proceedings.<sup>137</sup> In other words, with respect to class proceedings, the Court required states to adopt a hostility to arbitration and forbade them from treating the two equally. Specifically, in finding that the FAA preempted a California judicial rule finding it unconscionable to use class action bans in arbitration clauses when applied to small-dollar claims, the Court applied some of the same reasoning that companies have used when writing carve-outs. The Court determined that arbitration was so “poorly suited to the higher stakes of class litigation” in significant part because class actions involve greater risks to defendants, which would be unlikely to agree to bet the company, especially given the limited appellate review of arbitrator decisions.<sup>138</sup>

There, the Court concluded that arbitration is inferior to litigation for class proceedings, and that such hostility to arbitration apparently is acceptable and does not violate the FAA. Ordinarily that would mean that such claims can be brought in court, much in the way that carve-outs

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862, 872 (D. Or. 2002) (finding that foreclosure claims “are heavily regulated by statute, allowing for streamlined procedures and effective protections for both sides,” and thus it is not “unreasonable, much less oppressive, to forego arbitration of such claims”); *Salley v. Option One Mortg. Corp.*, 925 A.2d 115, 128 (Pa. 2007) (finding that a carve-out for foreclosure remedies was not unconscionable because “there are sound pragmatic and policy reasons why foreclosure proceedings should be pursued in a court of law”).

<sup>136</sup> See *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26 (1991) (recognizing that agreements to arbitrate federal statutory claims are enforceable even if they do not appear to be “appropriate for arbitration”); *Sakkab v. Luxottica Retail N. Am., Inc.*, 803 F.3d 425, 437 (9th Cir. 2015) (“By their nature, some types of claims are better suited to arbitration than others.”).

<sup>137</sup> 563 U.S. 333, 348–51 (2011).

<sup>138</sup> *Id.* at 350–51; accord *Stolt-Nielsen S.A. v. AnimalFeeds Int’l Corp.*, 559 U.S. 662, 686–87 (2010) (expressing similar concerns about how class procedures may cause “fundamental changes” to the nature of arbitration). Buoyed by the Supreme Court’s decision in *Concepcion*, corporate parties have tried to extend that reasoning to bar consumers from bringing claims for public injunctive relief, either in court or in arbitration, on the ground that claims for public injunctions are incompatible with arbitration. See, e.g., Brief for the Chamber of Commerce of the United States of America, et al. as Amici Curiae Supporting Defendants-Appellants, *McArdle v. AT&T Mobility LLC*, 772 F. App’x 575 (9th Cir. 2019) (No. 17-17246).

preserve claims for court. The Court, however, concluded that California could not require class claims to be brought in court, but must enforce an arbitration clause banning any type of class proceeding whatsoever. Although *Concepcion* seems to be an unabashedly pro-business, pro-arbitration decision, it is interesting that *Concepcion* also implicitly recognizes that it is acceptable for a public body such as a court to express some hostility to arbitration.

While courts have addressed carve-outs in these contexts, they have not addressed carve-outs in considering whether they signal some level of hostility to arbitration. Nor have they considered whether the hostility evidenced by carve-outs should have any bearing on the scope and reach of FAA preemption. That question is discussed in the next section.

#### IV. THE IMPLICATIONS OF CORPORATE HOSTILITY TO ARBITRATION

The idea that entities believe that arbitration might be preferable to litigation for some disputes but not for others is hardly surprising. No one reasonably contends that the question of arbitration versus litigation is all or nothing, in the sense that arbitration is either always superior to litigation or that it is always inferior to litigation.<sup>139</sup> It naturally will be the case that arbitration might be better suited for some disputes than others.<sup>140</sup>

Yet, scholars have not examined the parallels between corporate hostility to arbitration that is permitted by contract, and the judicial and legislative hostility to arbitration that is preempted by the FAA. Nor have they examined whether a private party's value judgments about when arbitration is inferior to litigation should affect whether the FAA permits state legislatures and courts to enact laws or apply common-law doctrines that reflect similar judgments about the value of arbitration vis-à-vis litigation. This section explores those questions. First, it draws parallels between the reasoning companies use for carving out specific claims, and the reasoning that states use when adopting various regulations of arbitration that are preempted by the FAA. It draws out the dissonance that results in prohibiting states from expressing hostility to arbitration while

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<sup>139</sup> The exception might be if arbitration were truly viewed as a veiled attempt at claim suppression rather than as a mechanism for actual dispute resolution. If arbitration is a venue where all claims go to die, as some might reasonably argue, then one might be able to say that arbitration is always inferior to litigation. See, e.g., *Arbitration in America: Hearing Before the S. Comm of the Judiciary*, 116th Cong. 16 (Apr. 2, 2019) (testimony of Myriam Gilles) ("The one and only objective of forced, pre-dispute, class-banning arbitration clauses is to suppress and bury claims.").

<sup>140</sup> See, e.g., Drahozal & O'Connor, *supra* note 69, at 1992 ("Given that contractual relationships tend to involve multiple but differing performance risks, it is not surprising that parties might prefer to use courts to address some of those risks but arbitration to address others.").



celebrating the right of corporations to do so. Second, this section suggests that this dissonance is troubling given that companies use carve-outs to maximize their self-interest at the expense of their potential adversaries. Third, it suggests that allowing corporations with significant bargaining power to use carve-outs to promote their private interest while prohibiting states from regulating arbitration to promote the public interest is anti-democratic and that this distinction should be revisited.

*A. Corporate Hostility to Arbitration Parallels State Legislative and Judicial Hostility to Arbitration*

There are strong parallels between corporate hostility to arbitration as expressed in carve-outs, and state judicial and legislative hostility to arbitration that is prohibited by the doctrine of FAA preemption. That makes sense, because both corporate carve-outs and state regulation of arbitration reflect similar value judgments about the relative strengths of arbitration versus litigation.

The dichotomy between the two arises because while corporations necessarily make a value judgment as to the relative merits of arbitration versus litigation when they draft their arbitration provisions, state legislatures and state courts are prohibited from making those same value judgments in seeking to protect the state's citizens. When a corporation carves out particular disputes or disputes with particular parties from an arbitration clause on the theory that arbitration is ill-suited to address them, that is celebrated as an exercise of contractual freedom.<sup>141</sup> But if a legislature were to decide that a certain type of dispute was ill suited for arbitration and therefore must proceed in court, that legislation would be preempted by the FAA under its current interpretation.<sup>142</sup>

This dichotomy deserves closer scrutiny, as there are numerous examples where corporate hostility to arbitration as reflected in carve-outs is virtually no different than state legislative or judicial rules that corporations have argued are preempted as hostile to arbitration. Corporations like to keep claims for injunctive relief in court because they view courts as better suited to provide injunctive relief.<sup>143</sup> But when the California Supreme Court decided that claims for public injunctive relief should not be resolved in arbitration because of those very same limitations,<sup>144</sup> the Ninth Circuit held that California's rule was preempted because it reflected an assumption that arbitrators were inferior to judges in

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<sup>141</sup> See *supra* note 6 and accompanying text.

<sup>142</sup> See *supra* Part II.

<sup>143</sup> See *supra* notes 75–79 and accompanying text.

<sup>144</sup> See *Cruz v. PacifiCare Health Sys., Inc.*, 66 P.3d 1157 (Cal. 2003); *Broughton v. Cigna Healthplans of Cal.*, 988 P.2d 67 (Cal. 1999).

awarding injunctive relief.<sup>145</sup> And the argument that the FAA preempted California's rule was made by business interests, including the U.S. Chamber of Commerce and the American Bankers Association, both of which appeared as *amicus curiae* to argue in support of preemption.<sup>146</sup> Furthermore, corporations have taken their argument one step further, arguing that a California law requiring that public injunction claims be allowable in some forum, either court or arbitration, is preempted by the FAA, even though such a law treats litigation and arbitration equally.<sup>147</sup>

Similarly, just as many contracts carve out repossession actions from arbitration, because of the need for emergency relief and the necessity of various judicial procedures, some states prohibit repossession claims from being resolved in arbitration.<sup>148</sup> Those laws are almost certainly preempted by the FAA, which forbids declaring a particular type of action non-arbitrable.<sup>149</sup>

The same is true for procedural carve-outs. While companies may prefer to avoid arbitration for cases they consider to be high stakes,<sup>150</sup> or they may prefer to import litigation-like procedures such as expanded discovery and appeal rights,<sup>151</sup> legislatures and courts cannot adopt similar

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<sup>145</sup> See *Ferguson v. Corinthian Colls., Inc.*, 733 F.3d 928, 930 (9th Cir. 2013); *Kilgore v. KeyBank, Nat'l Ass'n*, 718 F.3d 1052, 1060–61 (9th Cir. 2013) (en banc).

<sup>146</sup> See Brief of the Chamber of Commerce of the United States of America as *Amicus Curiae* Supporting Defendants-Appellants on Rehearing En Banc, *Kilgore v. KeyBank, Nat'l Ass'n*, 718 F.3d 1052 (9th Cir. 2013) (No. 09-16703) (en banc); *Kilgore*, 718 F.3d at 1055 (listing *amicus curiae* brief filed by the American Bankers Association, among others).

<sup>147</sup> See *Blair v. Rent-a-Center, Inc.*, 928 F.3d 819, 827–31 (9th Cir. 2019); see also Frankel, *supra* note 119 (describing arguments from the U.S. Chamber of Commerce and other corporate groups that a California rule prohibiting arbitration clauses that ban plaintiffs from bringing public injunction actions in either court or arbitration is inconsistent with the FAA).

<sup>148</sup> See, e.g., PA. R. CIV. P. 1301 and explanatory comment (exempting foreclosure claims from the state's compulsory judicial arbitration process on the ground that foreclosure proceedings are not "not appropriate" for arbitration); MICH. COMP. LAWS ANN. § 600.5035 (forbidding arbitration of fee disputes in land such as quiet title actions), repealed by 2011 Mich. Legis. Serv. 902 (eff. July 1, 2013). Until recently, a state law prohibiting arbitration of foreclosure actions would have been preempted. The Dodd-Frank Act of 2010, however, amended the FAA to prohibit inserting mandatory arbitration provisions into mortgage contracts. 15 U.S.C. § 1639c(e)(1) (2018). Presumably, a company could still require a consumer to arbitrate a foreclosure action as long as the arbitration provision was part of a different contract and not part of the mortgage loan. Additionally, one district court has held that this provision of the Dodd-Frank Act does not apply to arbitration clauses in mortgage loans that were executed prior to Dodd-Frank's enactment. See *Weller v. HSBC Mortgage Servs., Inc.*, 971 F. Supp. 2d 1072, 1077–79 (D. Colo. 2013).

<sup>149</sup> *AT&T Mobility, Inc. v. Concepcion*, 563 U.S. 333, 341 (2011) ("When state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA.")

<sup>150</sup> See *supra* notes 93–96 and accompanying text.

<sup>151</sup> See *supra* notes 100–102 and accompanying text.

rules. The FAA would surely preempt a law stating that all claims over a certain threshold dollar amount must be brought in court.<sup>152</sup> Likewise, the FAA would preempt a rule that did not forbid arbitration of high-stakes claims, but simply required that such claims provide for expanded discovery or appellate review.<sup>153</sup>

If a state tried to carve out claims that are “high stakes” for the plaintiff but not necessarily for the corporate defendant, such laws likely would be preempted. For example, as the #MeToo movement sheds greater light on sexual harassment in the workplace, the ability to litigate sexual harassment claims or bring them to public light has taken on great importance. There is increased recognition that requiring arbitration of such claims can keep them in secret and allow serial harassers to continue their illegal conduct.<sup>154</sup> Yet, when New York’s state legislature recently tried to forbid mandatory arbitration of sexual harassment claims, that law was struck down as preempted.<sup>155</sup>

As explained above, parties carve out claims, such as debt collection claims, where they think the law is clear and where they worry that arbitrators are less likely than judges to follow the law.<sup>156</sup> But a law that makes debt-collection claims non-arbitrable, or any other law that tries to distinguish between claims that arbitrators are better suited to handle from ones they are less well-suited to handle, would be preempted. Parties exhibit a hostility to arbitration as a plaintiff by carving out claims in ways that ensure that they can litigate claims in court where they will be the plaintiff but that any claim where they will be a defendant will be subject to

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<sup>152</sup> See *Sakkab v. Luxottica Retail N. Am., Inc.*, 803 F.3d 425, 437–38 (9th Cir. 2015) (suggesting that parties can choose to litigate high-stakes claims but not that states could require parties to litigate high-stakes claims).

<sup>153</sup> *Concepcion*, 563 U.S. at 341–42 (stating that a law requiring judicially monitored discovery in arbitration would be preempted). The one place where there may be parity between corporate hostility and public hostility is in the area of appellate review. That is because the Supreme Court has indicated that both contracting parties and legislators or judges are prohibited from providing for expanded appellate review of an arbitrator’s decision. See *supra* note 99.

<sup>154</sup> See, e.g., Hope Reese, *Gretchen Carlson on How Forced Arbitration Allows Companies to Protect Harassers*, VOX (May 21, 2018), <https://www.vox.com/conversations/2018/4/30/17292482/gretchen-carlson-me-too-sexual-harassment-supreme-court> (describing how Gretchen Carlson and other victims of sexual harassment have argued that requiring arbitration of sexual harassment claims keeps allegations secret and allows harassment to continue, and describing how advocates have urged Congress to enact legislation to restrict mandatory arbitration of sexual harassment claims).

<sup>155</sup> See *Latif v. Morgan Stanley & Co., LLC*, No. 18cv11528 (DLC), 2019 WL 2610985 (S.D.N.Y. June 26, 2019) (finding that FAA preempted New York statute forbidding mandatory arbitration of sexual harassment claims).

<sup>156</sup> See *supra* notes 83–87 and accompanying text.

mandatory arbitration.<sup>157</sup> One way to address this hostility would be to enact a law giving the plaintiff the option of proceeding in court or in arbitration. That too, would be preempted.

State laws that attempt to mirror the anti-severability provisions of many corporate arbitration clauses also face preemption challenges. Courts have occasionally addressed anti-severability principles in the context of addressing unconscionability challenges to arbitration clauses. Specifically, when a provision in an arbitration clause is struck down as unconscionable, the court must decide whether to sever the unconscionable provision and enforce the remainder of the arbitration clause, or whether to strike down the entire arbitration clause. Some courts have applied an anti-severability principle in certain circumstances, holding that if an arbitration clause is permeated with unfairness, the entire provision should be struck down because the enforceable portions cannot be separated from the unenforceable ones.<sup>158</sup> Corporations have pushed forward the argument that the courts' application of anti-severability principles is preempted, because courts purportedly refuse to sever unconscionable arbitration provisions more often than they refuse to sever unconscionable provisions from other contracts.<sup>159</sup> While corporations have written anti-severability provisions into their arbitration clauses, they have simultaneously tried to invalidate judicial anti-severability rules as preempted by the FAA. In short, state governments seek to carve out claims or procedures from arbitration for many of the same reasons that corporations carve out claims. Yet, corporations are permitted to implement these carve outs while states are not.

#### B. *Corporate Carve-outs Maximize Self-Interest*

This dichotomy between prohibiting states from expressing hostility to arbitration while allowing corporations to do so is troubling given that corporations likely use carve-outs because they want to maximize their self-interest. It stands to reason that when parties express hostility to arbitration through the use of carve-outs, they do so because they believe that such hostility is advantageous to them. While no single carve-out is universally used, carve-outs reveal a flaw in the Supreme Court's

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<sup>157</sup> See *supra* notes 88–91 and accompanying text.

<sup>158</sup> See, e.g., *Samaniego v. Empire Today, LLC*, 140 Cal. Rptr. 3d 492, 501 (Cal. Ct. App. 2012).

<sup>159</sup> See, e.g., Brief for Chamber of Commerce of the United States of America as Amicus Curiae Supporting Petitioners, *MHN Gov't Servs., Inc. v. Zaborowski*, 136 S. Ct. 1539 (2016) (No. 14-1458) (arguing that the FAA preempts California's state-law rule about when an unenforceable portion of an arbitration clause can or cannot be severed from the rest of the agreement); *Petition for Writ of Certiorari at 28–34, Winston & Strawn, LLC v. Ramos*, No. 18-1437 (U.S. May 14, 2019) (same).

articulation of how the FAA preempts any rule that reflects hostility to arbitration. As previously explained, the Court has assumed that any state law must assume that arbitration is just as good or better than litigation for both parties involved in order to comply with the FAA.

But a company's decision to use an arbitration clause (or to designate certain claims for arbitration and carve out others for litigation) signifies its belief that arbitration is a superior alternative for the company and also an inferior alternative for the company's potential adversary. Indeed, companies' selective use of carve-outs—and particularly companies' use of carve-outs to distinguish between claims where the company will be a plaintiff and those where it will be a defendant—shows that companies use arbitration when they think it gives them an advantage over their adversary, and that they use litigation when they think litigation is more advantageous. Arbitration clauses are about dispute resolution, and dispute resolution is inherently adversarial. Thus, a party's choice about its dispute resolution system likely reflects its attempt to maximize its advantage relative to its potential opposing parties.<sup>160</sup> In other words, even a decision to use arbitration in the first place, with or without carve-outs, may be based on an assumption that arbitration is an inferior alternative for some party to the agreement. Accordingly, hostility to arbitration may be embedded in virtually any decision a company makes about arbitration, because every decision reflects a value judgment about the relative merits of arbitration versus litigation.

There are several reasons to think that carve-outs, particularly those appearing in non-negotiable adhesion contracts between companies and their customers or employees, are designed to advantage corporate defendants at the expense of individual plaintiffs. First, the claim-suppressing arbitration clauses described earlier are used to protect defendants from accountability by making it difficult or impossible for individuals to vindicate their rights. Second, the differential use of arbitration when companies are likely to be plaintiffs rather than defendants shows that companies may see arbitration as systematically favoring defendants.

Third, the way corporations carve out particular contractual relationships from arbitration, as opposed to particular types of disputes, reinforces that many companies do not see arbitration as a superior forum

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<sup>160</sup> That is not necessarily true in all circumstances, as a company might choose arbitration because it thinks that it will benefit from potential cost savings regardless of how it fares in particular disputes, or because it thinks it will get speedier resolution even if it loses more disputes that it would otherwise lose. *Cf.* Hylton, *supra* note 87, at 213 (hypothesizing that parties will use arbitration when the costs of litigation outweigh its benefits).

for addressing disputes, but instead as a way of suppressing those disputes. One study examined arbitration clauses used by publicly traded consumer finance and telecommunication companies and compared their contracts with other companies to the contracts they used with consumers.<sup>161</sup> They found that companies used arbitration clauses in consumer contracts at a much higher rate than they did in their business-to-business contracts.<sup>162</sup> Notably, the arbitration clauses in the consumer contracts all had class action bans, while almost none of the business-to-business contracts contained a class action ban.<sup>163</sup>

As to this latter reason, one possible explanation is that the types of disputes likely to arise in the business-to-business context are better suited to litigation, while the business-to-consumer disputes are better suited (in the corporate party's view) to arbitration.<sup>164</sup> But that seems unlikely, for several reasons. First, many consumer disputes involve disputes over credit and loans, and illegal and deceptive practices that relate to those loans. Lending and credit is one of the subject matters that is most often carved out of arbitration clauses and reserved for litigation in the business-to-business context.<sup>165</sup> It stands to reason that if litigation offers advantages over arbitration for debt collection in the business-to-business context, it should also offer advantages in the business-to-consumer context. Second, several corporate organizations have expressed that they prefer to operate under a single dispute resolution system rather than under two different dispute resolution systems. It is allegedly more costly and more complicated for a company to face some disputes in litigation and others in arbitration.<sup>166</sup> But if that is true, then companies should not prefer to arbitrate with some parties and litigate with others. They should prefer to entirely litigate or entirely arbitrate. The fact that companies differentiate between parties suggests that where they use arbitration clauses, they are doing so because they think it will stop disputes from being resolved, thus avoiding arbitration altogether, and not because they would rather arbitrate consumer claims and litigate business-to-business claims.

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<sup>161</sup> Eisenberg, Miller & Sherwin, *supra* note 97, at 880–81.

<sup>162</sup> Eisenberg, Miller & Sherwin, *supra* note 97, at 876 (finding that over 75% of consumer contracts required arbitration while less than 10% of business-to-business contracts required arbitration).

<sup>163</sup> Eisenberg, Miller & Sherwin, *supra* note 97, at 884 (finding that every arbitration clause in a consumer contract contained a class action ban).

<sup>164</sup> See Drahozal & Ware, *supra* note 73, at 457–67.

<sup>165</sup> See *supra* notes 83–90 and accompanying text.

<sup>166</sup> Frankel, *supra* note 130, at 297 (explaining how some business organizations and commentators “have suggested it is too expensive for companies to deal with two different dispute resolution systems—judicial and arbitration”).

Additionally, it is notable that carve-outs appear more often where there is greater disparity in bargaining power between the parties and less opportunity for negotiation.<sup>167</sup> Unsurprisingly, these “carve-outs often seem to benefit one party to the agreement.”<sup>168</sup> This also suggests that carve-outs are not used only in situations where both parties can freely negotiate and jointly decide that litigation is preferable to arbitration. Rather, it appears more likely that carve-outs are forced on the weaker party by the stronger party in order to maximize the stronger party’s advantage in any dispute. In other words, carve-outs are simply a reminder that the drafting party chooses arbitration where it thinks that arbitration will benefit the corporation, and chooses litigation where it thinks that arbitration is inferior to litigation for protecting its private interest.

### C. *Subverting Democratic Accountability*

This paper has attempted to show that parties (and, in particular, corporate parties) are expressing the same hostility to arbitration through contract that the Supreme Court has held that states are precluded from expressing through legislation and judicial decision-making. This dichotomy is troubling. It is not self-evident that the former should be permitted while the latter is prohibited. After all, if one purpose of the FAA is to eradicate hostility to arbitration, then the FAA should not distinguish between corporate hostility to arbitration and legislative or judicial hostility to arbitration. If corporations are allowed to indulge certain assumptions about the limitations and flaws of arbitration when they design their arbitration clauses, then it would seem equally appropriate for state governments to adopt those same assumptions when seeking to regulate arbitration.

Although existing arbitration doctrine provides an explanation for this disparate treatment, that explanation lacks force in a world of boilerplate, non-negotiable adhesion contracts. Current doctrine describes arbitration as being a matter of private choice. The Court has said that “arbitration under the [FAA] is a matter of consent, not coercion,”<sup>169</sup> that the FAA embodies the “fundamental principle that arbitration is a matter of contract,”<sup>170</sup> and that courts must enforce arbitration clauses “according to their terms.”<sup>171</sup> If the fundamental difference between arbitration and

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<sup>167</sup> Drahozal & O’Connor, *supra* note 69, at 1968 (finding that “[i]f that party has substantial bargaining power in the drafting of the contract, carve-outs will appear at very high rates”).

<sup>168</sup> *Id.*

<sup>169</sup> *Volt Info. Scis., Inc. v. Bd. of Trs. of the Leland Stanford Junior Univ.*, 489 U.S. 468, 479 (1989).

<sup>170</sup> *Rent-A-Center, W., Inc. v. Jackson*, 561 U.S. 63, 67 (2010).

<sup>171</sup> *Volt*, 489 U.S. at 478; *AT&T Mobility, Inc. v. Concepcion*, 563 U.S. 333, 347 n.6

litigation is choice—that in arbitration the parties can choose how they design their dispute resolution process, whereas in court they cannot—then contractual hostility is acceptable even if legislative hostility is not.<sup>172</sup>

Accordingly, current doctrine allows corporations to express as much or as little hostility to arbitration as they wish, by giving corporations wide latitude to design arbitration clauses in any way, subject only to the limitation that they cannot violate general principles that apply to all contracts.<sup>173</sup> And this gives corporate parties significant power to write their arbitration provision in the most self-interested manner possible, while arguing that any attempt by the state to rein in their behavior is preempted. Current doctrine gives corporate parties a powerful weapon to say that their arbitration clauses must be enforced at all costs, even if they are one-sided, because the FAA requires arbitration clauses to be enforced “according to their terms.”<sup>174</sup> Parties can choose to adopt limitations on their arbitration clauses based on hostility to arbitration, but those limitations cannot be forced upon them by state law. Parties can contract for expanded discovery in arbitration, but they cannot be required to allow for expanded discovery;<sup>175</sup> parties can agree to place their arbitration clause in bold type at the top of the contract, but they cannot be forced to do so; parties can agree to allow class actions in court or in litigation, but they cannot be forced by a state to allow class actions.<sup>176</sup>

This logic rests on the assumption that voluntary, bargained-for hostility to arbitration is acceptable because it reflects the will of the parties and is based on choice. By contrast, state regulation of arbitration that arises out of a suspicion that arbitration may be unfair or less favorable than litigation in certain circumstances is coercive and limits the parties’ freedom to design their arbitration clauses as they see fit.

That distinction may resonate in a world of bargained-for, arm’s-

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(2011); *see also* 9 U.S.C. § 4 (2018) (authorizing federal courts to order arbitration “in accordance with the terms of the agreement”).

<sup>172</sup> *See, e.g.*, *Chorley Enters. Inc. v. Dickey’s Barbecue Rests., Inc.*, 807 F.3d 553, 570–71 (4th Cir. 2015) (“FAA preemption prevents states from carving out wholesale exceptions to arbitration. It does not prevent private parties from agreeing to litigate, rather than arbitrate, specific claims.”) (internal citation omitted).

<sup>173</sup> *See* 9 U.S.C. § 2 (making arbitration clauses enforceable “save upon such grounds as exist at law or in equity for the revocation of any contract”).

<sup>174</sup> *Volt*, 489 U.S. at 478; *Concepcion*, 563 U.S. at 347 n.6; *see also* 9 U.S.C. § 4 (authorizing federal courts to order arbitration “in accordance with the terms of the agreement”).

<sup>175</sup> *Concepcion*, 563 U.S. at 351 (stating that parties can voluntarily agree to judicially enforceable discovery but that such a rule cannot be imposed on them).

<sup>176</sup> *See id.* at 351 (stating that parties could agree to allow class arbitrations, but they cannot be required by the state to do so, because “[a]rbitration is a matter of contract, and the FAA requires courts to honor parties’ expectations”).



length contracts between two parties with similar bargaining power and similar knowledge of the benefits and drawbacks of arbitration. Perhaps that world exists for some business-to-business contracts where the parties have the power to negotiate over the specific terms of an arbitration clause. But that world is a fantasy in the realm of boilerplate adhesion contracts that dominate consumer and employment relationships. Virtually all consumer contracts are non-negotiable contracts entered into between individual consumers and large corporations.<sup>177</sup> The Supreme Court has frankly acknowledged that “the times in which consumer contracts were anything other than adhesive are long past.”<sup>178</sup> The notion that arbitration clauses are voluntarily agreed to and reflect deliberate choice by the parties is illusory.<sup>179</sup> Instead, they arise in transactions where the consumer lacks bargaining power, and where there is a vast informational asymmetry between the consumer and the corporation about the significance and the effect of the arbitration clause.<sup>180</sup>

From the consumer’s perspective, the arbitration clause imposed by a corporation as part of a non-negotiable adhesion contract is just as involuntary as a rule imposed by a court or a legislature. There is little difference between a corporation unilaterally dictating that certain claims cannot be arbitrated because they are better suited for courts (such as class actions, debt collection, and injunctive relief) and a legislature dictating that those claims cannot be arbitrated because they are better suited for courts. For the consumer, the corporation is as powerful as the state.<sup>181</sup>

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<sup>177</sup> See *supra* note 8 and accompanying text.

<sup>178</sup> *Concepcion*, 563 U.S. at 346–47.

<sup>179</sup> See MARGARET JANE RADIN, *BOILERPLATE: THE FINE PRINT, VANISHING RIGHTS, AND THE RULE OF LAW* 86–90 (2013) (questioning whether that the rise of modern boilerplate adhesion contracts is consistent with traditional notions of contractual consent); Brian Bix, *Contracts*, in *THE ETHICS OF CONSENT* 251 (Franklin G. Miller & Alan Wertheimer eds., 2010) (concluding that the notion of consent, as “expressed by the ideal of ‘freedom of contract,’” is effectively “absent in the vast majority of contracts we enter into these days,” though also concluding that this lack of meaningful assent is not problematic).

<sup>180</sup> Indeed, some studies have shown that consumers are often not aware that the contracts they sign contain an arbitration clause, or if they are, they do not understand what it means or its significance. See *generally* *Sovern*, *supra* note 8.

<sup>181</sup> Courts have also, and perhaps unwittingly, reinforced this narrative that arbitration clauses simply represent the corporate defendant’s interest rather than the mutual agreement of the parties. When applying the FAA or interpreting arbitration clauses, courts have focused on what the corporate defendant’s expectations are and have ignored what the consumer would have wanted, tacitly acknowledging that the consumer has no bargaining power and the consumer’s interest is therefore irrelevant. In *Concepcion*, when describing why AT&T Mobility carved out class proceedings from its arbitration clause, the Supreme Court noted that “class arbitration increases risks to defendants” and concluded, “[w]e find it hard to believe that defendants would bet the company with no effective means of review.” *Concepcion*, 563 U.S. at 350–51. Noticeably absent is any discussion of what the consumer-plaintiffs would have wanted, or why they would have agreed to a class action

Neither situation is voluntary, and both are equally coercive.

In fact, in the adhesion world of consumer contracts, it is more troubling to give corporations the authority to determine when arbitration is flawed or inferior to court than it is to give authority to state legislatures and courts—yet that is exactly what the FAA does. Corporations act to maximize their own self-interest. Legislatures and courts are democratically accountable and are supposed to act to protect the public at large.<sup>182</sup> That means that corporations have full license to express hostility to arbitration when doing so works to their advantage. And it appears that is exactly how corporations use carve-outs: to maximize their own advantage, suppress claims by injured consumers and employees, and insulate themselves from accountability.

It would make more sense to give legislatures and courts acting in the interests of their citizenry an equal power to adopt carve-outs from arbitration or to regulate arbitration in order to promote fairness. Giving states this power would not necessarily cause undue harm to companies that currently use arbitration clauses. It is important to recognize that legislatures do not just speak for consumers, but for all constituents, including corporate constituents.<sup>183</sup> Thus, corporations would still have plenty of voice through the legislative process, especially given the money that they can bring to bear on campaigning and lobbying efforts. Whereas current doctrine gives the corporation unilateral power to express hostility to arbitration, a doctrine that gives the legislature equivalent power to express hostility through regulation would likely achieve fairer results. If corporations can avoid the problematic aspects of arbitration by contract, then legislatures also should be able to protect their constituents against the problematic aspects of arbitration by statute and regulation.

Thus, current doctrine seems to get everything backwards. The corporation, the party acting in its own self-interest, can express any

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ban that deprives them of any meaningful opportunity to vindicate their rights. Courts have done this in other arbitration contexts as well, such as whether a corporation's agents can enforce an arbitration clause even though they did not sign it. In one case, the Texas Supreme Court held, "When contracting parties agree to arbitrate all disputes 'under or with respect to' a contract (as they did here), they generally intend to include disputes about their agents' actions . . ." *In re Vesta Ins. Group, Inc.*, 192 S.W.3d 759, 762 (Tex. 2006). Although the court stated that the parties intend to include disputes involving "their" agents, typically only corporate parties have agents. Individuals and consumers often do not.

<sup>182</sup> See RADIN, *supra* note 179, at 94 ("The laws of the state are supposedly established in the public interest and not in the private interest of a particular firm. Boilerplate schemes by their nature are in the interest of a firm and its market strategy and profits.")

<sup>183</sup> See, e.g., Dee Pridgen, *Wrecking Ball Disguised as Law Reform: ALEC's Model on Private Enforcement of Consumer Protection Statutes*, 39 N.Y.U. REV. L. & SOC. CHANGE 279, 280 (2015) (describing the efforts of "influential business-funded think tanks" to lobby state legislatures to pass laws limiting the ability of consumers to protect their rights).

amount of hostility it wants in its arbitration clause, and there is virtually nothing a consumer or employee can do about it. The legislature, which is democratically accountable and supposed to represent its citizens as a whole, is powerless to address any aspect of arbitration that it deems problematic or less fair than litigation.<sup>184</sup>

While not all carve-outs are one-sided, many carve-outs are. Moreover, the fact that carve-outs are used more often where one party lacks bargaining power reinforces that carve-outs are imposed by the stronger party and are not voluntarily negotiated.<sup>185</sup> Giving legislatures similar authority to the parties that draft arbitration clauses can rectify this imbalance and will help ensure that when arbitration is used, it is used fairly. Just as companies can decide that they do not want the burdens and expense of class arbitration, states should be able to decide that class actions must be allowed in court if they are going to be prohibited in arbitration. Just as companies can contract for extra discovery if they are concerned about arbitrators making inaccurate decisions, legislatures also should be able to ensure that consumers have an ability to conduct sufficient discovery to build a case in arbitration. When a legislature regulates some aspect of arbitration to try and make it fairer for all parties involved, that purported hostility should not be treated any differently than the hostility exhibited by corporate drafters of arbitration clauses.

Of course, not all corporate hostility to arbitration necessarily is one-sided. A provision allowing repossession actions to proceed in court or for injunctive claims to proceed in court may help both parties, as both may benefit from additional judicial process or from a judge's greater ability to award injunctive relief. But whether corporate hostility systematically favors one side or the other obscures the larger point. If a corporation can decide that it wants to reserve certain claims for courts because it thinks courts are superior to arbitrators for those claims, then there is no reason why legislatures should not be able to draw the same conclusion and determine that certain types of claims should be decided by a court rather than an arbitrator.

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<sup>184</sup> This is a problem afflicting adhesive contracts generally. See, e.g., RADIN, *supra* note 179, at 23 (asserting that through adhesion contracts, corporations “delete rights that are granted through democratic processes”); see also David Horton, *Mass Arbitration and Democratic Legitimacy*, 85 U. COLO. L. REV. 459, 502 (2014) (arguing that “adhesive arbitration clauses push the boundaries of ex ante consent, eliminate ex post judicial oversight, and ultimately displace democratically-created rights”). That problem is exacerbated in the arbitration context. Whereas state governments can regulate the use of adhesion contracts, their power to regulate arbitration is much more limited thanks to the FAA.

<sup>185</sup> See *supra* note 72 and accompanying text.

Although current doctrine allows corporate hostility to arbitration while simultaneously prohibiting equivalent legislative or judicial hostility, that doctrine lacks salience in the world of adhesive, take-it-or-leave-it consumer and employment contracts. Instead, this distinction elevates absolute freedom of contract over genuine concern about arbitration fairness. In doing so, current doctrine merely perpetuates existing disparities by allowing the corporate party to carve out claims or design arbitration procedures that maximize its advantage while prohibiting government actors from taking steps to level the playing field for the individual on the other side of the contract. How current doctrine surrounding FAA preemption could be adapted to better account for corporate hostility to arbitration is discussed in the next section.

#### V. ACCOUNTING FOR CORPORATE HOSTILITY IN FAA PREEMPTION DOCTRINE

The fact that corporations frequently express some hostility to arbitration in the way they draft their arbitration clauses suggests that states should have greater latitude to express hostility to arbitration without running into FAA preemption. This section shows how corporate hostility to arbitration could justify re-conceptualizing FAA preemption doctrine in two possible ways. First, the fact that parties believe that litigation is sometimes preferable to arbitration indicates that not all hostility to arbitration is improper or reflects an irrational bias against arbitration. Accordingly, not all judicial or legislative hostility to arbitration should be deemed to conflict with the FAA's goals. Rather, if the hostility seems justifiable, because of the differences between litigation and arbitration, and because of the ways that arbitration can be designed to strategically favor one party over the other, then it is perfectly appropriate for the state to regulate arbitration in the name of fairness.<sup>186</sup>

Second, and more radically, the way that arbitration doctrine distinguishes between contracted-for limitations on arbitration and governmentally imposed limitations on arbitration suggests that FAA preemption should not apply to adhesion contracts at all. The fact that parties can contract for whatever limitations on arbitration they wish, but that the state cannot impose the same limitations, indicates that the most fundamental aspect of arbitration is choice, rather than any particular procedural device.<sup>187</sup> But adhesion contracts, by definition, are contracts

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<sup>186</sup> See Hiro N. Aragaki, *Arbitration's Suspect Status*, 159 U. PA. L. REV. 1233 (2011).

<sup>187</sup> See Stipanowich, *supra* note 99, at 51 ("Choice is what sets arbitration apart from litigation."); see also Hiro N. Aragaki, *The Federal Arbitration Act as Procedural Reform*, 89 N.Y.U. L. REV. 1939, 1946 (2014) (describing the prevailing view among arbitration scholars that the goal of the FAA was to preserve private autonomy and choice); Frankel,

where one party has no meaningful choice. If the FAA is about protecting the parties' ability to mutually choose the procedures they prefer, then it has no role to play in the world of adhesion contracts at all. In turn, arbitration clauses in adhesion contracts should be subject to government regulation in the same way as any other contract.

*A. Allowing Some Legislative and Judicial Hostility to Arbitration*

The fact that parties express hostility to arbitration by carving out particular claims or by importing judicialized procedures into arbitration, and the fact that Congress and agencies have acted similarly at the federal level, reveals that not all hostility to arbitration is improper. Parties have legitimate reasons for thinking that arbitration is inferior to litigation, and scholars have recognized as much.<sup>188</sup>

Hostility to arbitration therefore is both inevitable and legitimate. While current FAA doctrine pretends otherwise, there is no good reason to continue to perpetuate such a fiction. If it is acceptable for corporations to express hostility to arbitration in their adhesion contracts with consumers and employees, then it should be acceptable for governmental actors to express hostility by regulating arbitration, either by carving out certain claims from arbitration, or by regulating the arbitration process to make it fairer or to address its deficiencies.

This begs the question of how to distinguish legitimate hostility to arbitration from illegitimate hostility to arbitration. While it may seem difficult at first, there are various ways to approach this. Initially, a law that affects arbitration should not automatically trigger "rigorous"<sup>189</sup> scrutiny or inherent suspicion of that law. It may turn out to be the case that most hostility to arbitration, and hence most regulation of arbitration, is legitimate. Recall that the framers of the FAA were seeking to reverse a broad and sweeping hostility to arbitration in which courts would refuse to specifically enforce an arbitration clause simply because it was an arbitration clause—in other words, wholesale prejudice against arbitration writ large, without reference to whether arbitration was better or worse than litigation under any specific circumstances.<sup>190</sup> There is a big difference between stating that arbitration clauses are always unenforceable and stating, for example, that arbitration clauses are unenforceable for claims

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*supra* note 39, at 250–52.

<sup>188</sup> See *supra* Part III; Drahozal & O'Connor, *supra* note 69, at 1969 (stating that parties may choose carve-outs when "they trust courts to better protect their interests than arbitrators").

<sup>189</sup> *Securities Indus. Ass'n v. Connolly*, 883 F.2d 1114, 1119–20 (1st Cir. 1989) (stating that the FAA enshrines "a principle of rigorous equality" between arbitration clauses and other contracts).

<sup>190</sup> See *supra* notes 19–23 and accompanying text.

involving high stakes, or stating that arbitration clauses can be enforced, but that the arbitration system must allow for sufficient discovery to enable the plaintiff to build his or her case. These limitations are not fully hostile to arbitration, but instead rest on assumptions that arbitration, in particular situations, may be less likely than a court to result in an accurate and satisfactory outcome.

One way to approach this is by looking to the carve-outs used by private parties. If private arbitration clauses carve out a particular claim or procedure, then that should give rise to a rebuttable presumption that a state regulation equivalent to the carve-out is not preempted. For example, if private parties carve out injunctive claims because they think that courts are superior at managing injunctive claims, then states should be able to adopt a regulation forbidding mandatory arbitration of injunctive claims. If they did so, that regulation would be presumptively legitimate, though that presumption could be rebutted by evidence that the state had an illegitimate or pretextual reason for adopting the regulation. This would also hold true for other types of frequently carved-out claims, such as small claims, debt collection claims, anti-severability principles, and so on.

A related framework is one that would look at the state government's motivation or purpose in assessing whether a particular rule expressing hostility to arbitration is preempted or not. Professor Hiro Aragaki has suggested applying an anti-discrimination framework that asks if legislation regulating arbitration is motivated by invidious discrimination or whether it has a legitimate justification, in the same way that anti-discrimination law analyzes allegedly illegal behavior.<sup>191</sup> Similarly, Professor David Horton argues that the FAA should only preempt state rules that "unjustifiably disfavor arbitration," i.e., ones that rest on an inherent suspicion of arbitration rather than ones that attempt to recognize a specific and concrete drawback or deficiency of arbitration.<sup>192</sup> These models are commendable, and deserve fuller consideration. Looking at the FAA through the lens of contractual hostility to arbitration reinforces the view of these scholars that some hostility to arbitration is acceptable and bolsters the argument that states should be free to express justified hostility to arbitration without being subject to federal preemption.

In determining whether a legislature has a legitimate reason for regulating arbitration, courts could also borrow from Commerce Clause or Equal Protection analysis. In particular, state legislatures could make findings when adopting laws regulating arbitration, and courts could examine those findings as part of the preemption inquiry. Just as courts

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<sup>191</sup> Aragaki, *supra* note 186, at 1263–71.

<sup>192</sup> David Horton, *Federal Arbitration Act Preemption, Purposivism, and State Public Policy*, 101 GEO. L.J. 1217, 1255, 1265–72 (2013).

can consider congressional findings in determining whether a federal law affects interstate commerce, courts could also look to legislative findings that explain the reasons for regulating arbitration in considering whether the law reflects an unjustified hostility to arbitration.<sup>193</sup> And unlike current law, which establishes a presumption that any regulation of arbitration is inappropriately hostile and is preempted unless shown otherwise, accepting the proposition that hostility to arbitration is natural and inevitable should lead courts to give some deference (subject to rebuttal) to legislative findings indicating that the state has a legitimate reason for imposing some limit on the scope or process of arbitration.<sup>194</sup> Similarly, courts could import an Equal Protection framework and presume that the state has a rational basis for regulating arbitration unless evidence shows otherwise.<sup>195</sup>

As explained above, allowing regulation where there is justified hostility to arbitration is more even-handed and better levels the playing field between corporations and consumers. Instead of allowing only self-interested hostility that is used to maximize one party's advantage relative to the other, allowing regulation by democratically accountable bodies can advance everyone's interests.

This view also is consistent with the Court's statements that Congress enacted the FAA to place arbitration clauses "upon equal footing" with other contracts. If one thinks of "equal footing" in a process-oriented way rather than in a substantive way, then allowing regulation of arbitration clauses treats them the same as other contracts. Contract law generally is state law. Thus, contracts are subject to regulation by state governments.<sup>196</sup>

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<sup>193</sup> See *United States v. Morrison*, 529 U.S. 598, 612 (2000) ("While Congress normally is not required to make formal findings as to the substantial burdens that an activity has on interstate commerce, the existence of such findings may enable us to evaluate the legislative judgment that the activity in question substantially affects interstate commerce, even though no such substantial effect is visible to the naked eye.") (internal citations and quotations omitted).

<sup>194</sup> In fact, that is how courts used to analyze federal statutes under the Commerce Clause, before the Supreme Court changed the law in *United States v. Lopez*, 514 U.S. 549, 557 n.2 (1995). See, e.g., *Presault v. I.C.C.*, 494 U.S. 1, 17 (1990) ("We evaluate this claim under the traditional rationality standard of review: we must defer to a congressional finding that a regulated activity affects interstate commerce if there is any rational basis for such a finding[.]") (internal citation omitted); *United States v. Stillwell*, 900 F.2d 1104, 1111 (7th Cir. 1990) ("If we find that Congress has any rational basis for finding that a regulated activity affects interstate commerce, our investigation is at an end.").

<sup>195</sup> See *FCC v. Beach Comm'ns, Inc.*, 508 U.S. 307, 313 (1993) ("In areas of social and economic policy, a statutory classification that neither proceeds along suspect lines nor infringes fundamental constitutional rights must be upheld against equal protection challenge if there is any reasonably conceivable state of facts that could provide a rational basis for the classification.").

<sup>196</sup> See *Nebbia v. New York*, 291 U.S. 502, 523 (1941) ("[N]either property rights nor contract rights are absolute . . . . Equally fundamental with the private right is that of the public to regulate it in the common interest.").

Currently, while legislators can regulate most contracts in almost any way they wish, one type of contractual provision they cannot regulate is an arbitration clause.<sup>197</sup> States often regulate contracts where they perceive a risk of unfairness. States might regulate contracts in one substantive area, such as franchise contracts.<sup>198</sup> Or they might regulate where they perceive market failures, such as where there are disparities in bargaining power between contracting parties.<sup>199</sup> Allowing states to regulate arbitration where they perceive justifiable hostility, say to address specific shortcomings, or to carve out specific subject matters from arbitration where arbitration may be inferior to litigation, is perfectly consistent with how states regulate other contracts. Making arbitration clauses impervious to all regulation other than general common-law rules applicable to all contracts is not.

### B. *Adhesion and Preemption*

A more radical viewpoint is that the dissonance between permissible corporate hostility to arbitration expressed through contract and impermissible hostility expressed in state regulation indicates that the FAA should not limit or prohibit states from regulating arbitration clauses in non-negotiable adhesion contracts at all. In other words, the FAA should not preempt any regulation of adhesive arbitration clauses.

As the Supreme Court recognized in *Concepcion*, parties can contract for limitations, conditions, or restrictions on arbitration that state legislatures cannot impose.<sup>200</sup> That distinction is important in thinking about the FAA's purposes and objectives, because the FAA only preempts rules that stand as an obstacle to the performance of the statute's purposes. The FAA's purpose cannot be to enshrine any particular procedure or characteristic of arbitration, because as the Court indicated, parties can contract for almost any procedure they want, subject to a few limitations.<sup>201</sup> Rather, as several scholars have identified, this distinction suggests that the fundamental characteristic of arbitration that the FAA was concerned with

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<sup>197</sup> *Securities Indus. Ass'n v. Connolly*, 883 F.2d 1114, 1120 (1st Cir. 1989) (“[N]o state may simply subject arbitration to individuated regulation in the same manner as it might subject some other unprotected contractual device (say, a prescriptive period or exculpatory clause contained within a private contract).”).

<sup>198</sup> *See, e.g., R.I. GEN. LAWS* § 6-50-4 (2014) (regulating a franchisor's ability to terminate a franchisee).

<sup>199</sup> Minimum wage laws, child labor laws, or other laws regulate contractual employment relationships are examples of state laws that limit the rights of contracting parties for the purpose of protecting fairness.

<sup>200</sup> *AT&T, Inc. v. Concepcion*, 563 U.S. 333, 351 (2011).

<sup>201</sup> *See id.*



was choice.<sup>202</sup> And as I have argued elsewhere, that choice means meaningful, freely negotiated choice exercised by both parties to the transaction.<sup>203</sup>

The adhesion contracts and arbitration clauses that are present in consumer transactions, however, are defined by the absence of choice. The only party with any control over the contract terms is the corporate party that drafts and imposes the arbitration clause. This adhesion regime is arguably at odds with the FAA's purpose of preserving meaningful choice. Several scholars have addressed how the FAA was intended for commercial transactions between sophisticated parties with roughly equal bargaining power rather than for take-it-or-leave-it business-to-consumer transactions.<sup>204</sup> Moreover, the Act's legislative history indicates that Congress never envisioned that the Act would apply to take-it-or-leave-it adhesion contracts like the ones used in employment settings.<sup>205</sup>

If the FAA was intended to protect the enforcement of arbitration clauses that were the product of meaningful choice, then the Act has no bearing on adhesion contracts marked by the absence of choice. Regulation of arbitration clauses in adhesion contracts therefore does not run afoul of the FAA and should not be preempted. Society may now accept that "the times in which consumer contracts were anything other than adhesive are long past[.]"<sup>206</sup> but that does not mean that it must accept that such contracts are beyond the reach of reasonable regulation designed to rectify the one-sided nature of adhesion contracts. Treating arbitration clauses equally with other contracts should recognize that adhesive arbitration clauses, like other adhesive contracts, are characterized by a

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<sup>202</sup> See *supra* note 187 and accompanying text.

<sup>203</sup> Frankel, *supra* note 39, at 251.

<sup>204</sup> See, e.g., David S. Schwartz, *Enforcing Small Print to Protect Big Business: Employee and Consumer Rights Claims in an Age of Compelled Arbitration*, 1997 WIS. L. REV. 33, 75–81 (arguing that the framers intended the FAA to be limited to commercial disputes between business entities); Sternlight, *supra* note 21, at 647 ("Most commentators have concluded that the FAA was envisioned as applying to consensual transactions between two merchants of roughly equal bargaining power, and not necessarily to transactions between a large merchant and a much weaker and less knowledgeable consumer.").

<sup>205</sup> See Sternlight, *supra* note 21, at 647; see also *Epic Sys. Corp. v. Lewis*, 138 S. Ct. 1612, 1642–43 (2018) (Ginsburg, J., dissenting) ("The legislative hearings and debate leading up to the FAA's passage evidence Congress' aim to enable merchants of roughly equal bargaining power to enter into binding agreements to arbitrate commercial disputes.") (emphasis in original); *DIRECTV, Inc. v. Imburgia*, 136 S. Ct. 463, 477–78 (2015) (Ginsburg, J., dissenting) (asserting that the FAA was intended to address arbitration of commercial disputes and that "Congress in 1925 could not have anticipated that the Court would apply the FAA to render consumer adhesion contracts invulnerable to attack by parties who never meaningfully agreed to arbitration in the first place").

<sup>206</sup> *Concepcion*, 563 U.S. at 346.

disparity in bargaining power. And just as it is appropriate to regulate other contracts to correct any unfairness resulting from that disparity, it is perfectly appropriate for states to correct against unfairness that manifests in an adhesive arbitration clause. Because adhesion contracts are outside the purview of what the FAA was trying to protect, states should be permitted to regulate arbitration clauses appearing in adhesion contracts without being subject to FAA preemption. This in turn could promote free choice. If courts interpret the FAA to give states greater authority to regulate adhesive arbitration agreements than they previously had, that may encourage parties that wish to use arbitration agreements to give contracting parties greater negotiating power over the arbitration provision's terms.<sup>207</sup>

## VI. CONCLUSION

Aided by corporate and business interests that have a strong interest in enforcing mandatory arbitration clauses, the Supreme Court in the last thirty years has greatly expanded the scope of FAA preemption on the ground that the Act preempts any state law expressing hostility to arbitration. At the same time that corporations seek to invalidate any law that regulates arbitration as representing inappropriate hostility to arbitration, however, they frequently express their own hostility to arbitration by using carve-outs and other drafting techniques. While corporations have the power to express hostility to arbitration when this approach serves their own interests, they have strategically prevented democratically accountable state-government institutions from expressing that same hostility to arbitration in the interest of protecting their citizens. Current preemption doctrine does not account for this dichotomy. It should, and FAA preemption principles should recognize that state laws expressing hostility to arbitration should not necessarily be preempted, as many of those laws express the same hostility to arbitration that corporations express in their arbitration clauses.

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<sup>207</sup> Frankel, *supra* note 39, at 253.