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#### Recommended Citation

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Judicial Attitudes Toward Arbitration and  
the Resurgence of Unconscionability

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*Buffalo Law Review*  
Vol. 52, p. 185, 2004

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## Judicial Attitudes Toward Arbitration and the Resurgence of Unconscionability

SUSAN RANDALL†

### INTRODUCTION

The common law traditionally rejected arbitration as a deprivation of the jurisdiction of the courts and therefore contrary to public policy. The enactment of the Federal Arbitration Act in 1925<sup>1</sup> signaled the United States' acceptance of arbitration as a permitted method of dispute resolution. The purpose of the Federal Arbitration Act is "to reverse the longstanding judicial hostility to arbitration agreements . . . and to place [them] on the same footing as other contracts."<sup>2</sup> Since the United States Supreme Court's decision in *Southland Corp. v. Keating* in 1983, the Federal Arbitration Act has been read as embodying a "national policy favoring arbitration."<sup>3</sup> The Federal Arbitration Act preempts all state laws which undermine arbitration.<sup>4</sup>

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† Professor of Law, University of Alabama School of Law. The author thanks the University of Alabama Law School Foundation for generous research support and Carol Rice Andrews, Al Brophy, and Ken Randall for helpful discussions and comments.

1. Act of Feb. 12, 1925, ch. 213 §§ 1-15, 43 Stat. 883-85 (codified as amended at 9 U.S.C. §§ 1-14 (1970)).

2. *Green Tree Fin. Corp.-Ala. v. Randolph*, 531 U.S. 79, 89 (2000) (quoting *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 24 (1991)).

3. *Southland Corp. v. Keating*, 465 U.S. 1, 10 (1983) (O'Connor & Rehnquist, JJ., dissenting).

4. The states have generally followed the federal government's example in permitting and even favoring arbitration, most notably through almost universal enactment of the 1955 Uniform Arbitration Act. The Uniform Arbitration Act has been adopted by thirty-five states. Fourteen states have adopted substantially similar legislation, for a total of forty-nine states. UNIF. ARBITRATION ACT, §§ 1-25 prefatory note (2000) (Nat'l Conference of Comm'rs on Unif. State Laws). Alabama is the only state which has not adopted the Uniform Arbitration Act or any variant. In August 2000, the National Conference of Commissioners on Uniform State Laws approved, nearly unanimously, a modernized Uniform Arbitration Act. REVISED UNIF. ARBITRATION ACT §§ 1-25 (amended 2000).

However, the Federal Arbitration Act preserves a role for state law in arbitration through Section 2, which provides that a written agreement to arbitrate in a contract involving interstate commerce “shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.”<sup>5</sup> The United States Supreme Court has interpreted Section 2 to mean that state law controls the issue of contract revocation. Courts may revoke arbitration agreements, leaving the parties free to litigate their claims, on generally applicable state law grounds such as fraud, duress, and unconscionability.<sup>6</sup>

This Article suggests that federal and state judges retain some measure of the long-standing judicial hostility toward arbitration, and that they have expanded the doctrine of unconscionability beyond its typical uses to revoke arbitration agreements and permit litigation of claims by parties subject to arbitration agreements. The article attempts in three ways to demonstrate that judges use an arbitration-specific version of the unconscionability doctrine to avoid the Federal Arbitration Act. First, judges currently find arbitration agreements unconscionable at twice the rate of nonarbitration agreements. Twenty years ago, judges found arbitration and nonarbitration agreements unconscionable at approximately the same rate.

This increased receptivity to claims of unconscionability in the context of arbitration agreements suggests judicial hostility to arbitration. Second, judges find unconscionable specific features of arbitration agreements, such as forum selection clauses and confidentiality requirements, which are routinely enforced as unobjectionable in nonarbitration agreements. Other features of arbitration agreements often found unconscionable in the arbitration context but not generally considered unconscionable are punitive damages limitations and cost-splitting provisions. This differential application of the doctrine of unconscionability in comparable arbitration and nonarbitration contexts further evidences judicial hostility to arbitration. Third, the statements of a few outspoken judges provide direct evidence that at least some judges dislike arbitration and lend support to the broader conclusions drawn from the

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5. 9 U.S.C. § 2 (1970).

6. *See, e.g.,* *Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 686-87 (1996).

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increased numbers of cases involving the unconscionability doctrine and comparative case analysis.

Section I briefly describes the doctrine of unconscionability and examines United States Supreme Court precedent dealing with contract defenses, particularly unconscionability, under the Federal Arbitration Act. Section II analyzes the number of unconscionability claims in 1982-1983 and 2002-2003 in both arbitration and nonarbitration agreements and the rates of unconscionability findings. In 2002-2003, most of the claims of unconscionability involved arbitration agreements, and courts were much more likely to hold arbitration agreements unconscionable than nonarbitration agreements. Twenty years earlier, very few claims of unconscionability involved arbitration agreements and courts were no more likely to find arbitration agreements unconscionable than nonarbitration agreements. Section III examines case law dealing with unconscionability in the arbitration context and compares it to case law in nonarbitration contexts. Contract features which are unobjectionable in nonarbitration agreements ground a finding of unconscionability in arbitration agreements. Section IV describes various judicial statements which explicitly illustrate judicial animosity towards arbitration.

There may be many possible reasons for judicial expansions of unconscionability at the expense of arbitration, including self-interested protection of the judicial function. However, the negative judicial reactions to arbitration and the significant expansion of unconscionability to avoid arbitration by many judges nationwide suggests that arbitration does in fact create serious problems for potential claimants.<sup>7</sup> It may be

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7. The extensive secondary literature addresses these problems in detail. See, e.g., Richard M. Alderman, *Pre-Dispute Mandatory Arbitration in Consumer Contracts: A Call for Reform*, 38 HOUS. L. REV. 1237 (2001); Reginald Alleyne, *Statutory Discrimination Claims: Right "Waived" and Lost in the Arbitration Forum*, 13 HOFSTRA LAB. L.J. 381 (1996); Mark E. Budnitz, *Arbitration of Disputes Between Consumers and Financial Institutions: A Serious Threat to Consumer Protection*, 10 OHIO ST. J. ON DISP. RESOL. 267 (1995); Richard B. Cappalli, *Arbitration of Consumer Claims: The Sad Case of Two-Time Victim Terry Johnson or Where Have You Gone Learned Hand?*, 10 B.U. PUB. INT. L.J. 366 (2001); Christopher R. Drahozal, *"Unfair" Arbitration Clauses*, 2001 U. ILL. L. REV. 695 (2001); Sen. Russell D. Feingold, *Mandatory Arbitration: What Process is Due?*, 39 HARV. J. ON LEGIS. 281, 289 (2002) (stating that Congress did not originally intend "the FAA to enable stronger

reasonable for courts to continue to expand unconscionability to address these problems, despite preemption concerns under the Federal Arbitration Act; the malleability of the doctrine of unconscionability is acknowledged as one of its chief virtues. The Supreme Court has foreclosed more direct state law solutions to the problems posed by arbitration with its recent extensions of the Federal Arbitration Act. Since 1983, with the Supreme Court's decision in *Southland Corp. v. Keating*,<sup>8</sup> the Federal Arbitration Act has been held to apply in state as well as federal court. Four Supreme Court justices have criticized this aspect of *Southland*, based on their reading of the Federal Arbitration Act's legislative history: Justice O'Connor and then-Justice Rehnquist in a dissent to *Southland*, and Justices Scalia and Thomas in a dissent to *Allied-Bruce Terminix*,<sup>9</sup> which reaffirmed *Southland* in

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parties to force weaker parties into binding arbitration"); Margaret M. Harding, *The Redefinition of Arbitration by Those with Superior Bargaining Power*, 1999 UTAH L. REV. 857 (1999); Larry J. Pittman, *The Federal Arbitration Act: The Supreme Court's Erroneous Statutory Interpretation, Stare Decisis, and a Proposal for Change*, 53 ALA. L. REV. 789, 829 (2002) (noting that drafters and supporters of FAA envisioned that "the FAA should apply only to arbitration agreements between merchants who have freely entered into such agreements, and that the FAA does not apply to adhesion arbitration agreements between powerful sellers and weak buyers"); David S. Schwartz, *Enforcing Small Print to Protect Big Business: Employee and Consumer Rights Claims in an Age of Compelled Arbitration*, 1997 WISC. L. REV. 33 (1997); Jean R. Sternlight, *As Mandatory Binding Arbitration Meets the Class Action, Will the Class Action Survive?*, 42 WM. & MARY L. REV. 1 (2000); Jean R. Sternlight, *Mandatory Binding Arbitration and the Demise of the Seventh Amendment Right to a Jury Trial*, 16 OHIO ST. J. ON DISP. RESOL. 669 (2001); Jean R. Sternlight, *Panacea or Corporate Tool? Debunking the Supreme Court's Preference for Binding Arbitration*, 74 WASH. U. L.Q. 637, 647 (1996) ("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."); Jean R. Sternlight, *Rethinking the Constitutionality of the Supreme Court's Preference for Binding Arbitration: A Fresh Assessment of Jury Trial, Separation of Powers, and Due Process Concerns*, 72 TUL. L. REV. 1 (1997); Katherine Van Wezel Stone, *Rustic Justice: Community and Coercion Under the Federal Arbitration Act*, 77 N.C. L. REV. 931 (1999).

8. 465 U.S. 1, 16 (1983) (O'Connor & Rehnquist, JJ., dissenting).

9. *Southland Corp. v. Keating*, 465 U.S. 1, 21 (1983) (O'Connor & Rehnquist, JJ., dissenting), *reaff'd by Allied-Bruce Terminix Co., Inc. v. Dobson*, 513 U.S. 265, 285 (1995) (Scalia & Thomas, JJ., dissenting). Justice O'Connor stated in her concurrence in *Allied-Bruce*, "I continue to believe that Congress never intended the Federal Arbitration Act to apply in state courts, and that this Court has strayed far afield in giving the Act so broad a compass," 513 U.S. at

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1995. Twenty state attorneys general argued unsuccessfully to overturn *Southland* based on legislative history and public policy and to return control over arbitration to the individual states.<sup>10</sup> The Supreme Court has also extended the Federal Arbitration Act to statutory claims, overruling earlier precedent.<sup>11</sup> Finally, the Federal Arbitration Act applies to the full extent of the commerce power, precluding efforts by some state supreme courts to limit its application.<sup>12</sup> Judicial, political, and academic opposition to arbitration in some of its forms<sup>13</sup> suggests that some controls are needed. Absent Supreme Court reconsideration of its extensions of the Federal Arbitration Act, application of unconscionability doctrine may be one of the judiciary's only remaining tools for protection of individuals and small businesses. Section V provides some suggestions for restrained use of the doctrine to avoid potential preemption issues.

## I. UNCONSCIONABILITY AND THE FEDERAL ARBITRATION ACT

Unconscionability has roots in law and equity. The Uniform Commercial Code ("UCC") provision on

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283, but stopped short of overruling based on special considerations of stare decisis in statutory interpretation. *Id.* at 283-84.

10. *Id.* at 284 (Scalia, J., dissent).

11. See *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 485 (1989), rev'g *Wilko v. Swan*, 346 U.S. 427 (1953) (ruling that Securities Act of 1933 prohibits waiver of a judicial remedy through predispute agreement to arbitrate). See also *Green Tree Fin. Corp.-Ala. v. Randolph*, 531 U.S. 79 (2000) (Truth in Lending Act); *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26-27 (1991) (Age Discrimination in Employment Act); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985) (federal antitrust laws).

12. See *Citizens Bank v. Alafabco*, 123 S.Ct. 2037 (2003); *Allied-Bruce Terminix Co. v. Dobson*, 513 U.S. 265, 268 (1995) (interpreting the language in the Federal Arbitration Act § 2, "involving commerce" to be read broadly). *Allied-Bruce* distinguished *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 200-01 (1956), which held that evidence failed to show that an employment contract made in New York between New York residents but performable in Vermont evidenced a transaction involving interstate or foreign commerce as required by Federal Arbitration Act § 2. The Alabama Supreme Court in particular had attempted to limit the reach of arbitration clauses through narrow interpretation of the language "involving commerce" in the Federal Arbitration Act. See *Sisters of the Visitation v. Cochran Plastering Co.*, 775 So.2d 759 (Ala. 2000). *Citizens Bank* has ended that effort.

13. Particularly as applied to consumers, employees, and small businesses in their dealings with more powerful corporate entities.

unconscionability, Section 2-302, has been central to the development of the modern law of unconscionability. However, even prior to the adoption of Section 2-302, courts occasionally refused to enforce unconscionable contracts.<sup>14</sup> An often-quoted decision states that an unconscionable agreement is one “such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other.”<sup>15</sup> The term “unconscionability” is not defined specifically in either the case law or in the UCC. Section 2-302 states simply that a court may refuse to enforce an unconscionable contract or clause, or may limit an unconscionable clause to avoid an unconscionable result.<sup>16</sup> The Official Comment to the section elaborates on the concept by setting out a “basic test” for unconscionability:

[W]hether, in the light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract. . . . The principle is one of the prevention of oppression and unfair surprise.<sup>17</sup>

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14. Perhaps the most significant cases dealing with the doctrine of unconscionability were decided before the UCC was enacted. *See Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445 (D.C. Cir. 1965) (refusing to enforce agreement under which seller retained security interest in various chattels bought on deferred payment plans and sought replevin on all chattels following late payment on one; the UCC had been adopted but was not yet in effect); *Campbell Soup Co. v. Wentz*, 172 F.2d 80 (3d Cir. 1948) (denying specific performance of adhesion contract requiring farmer to sell crop at \$23-30/ton, based on market price at time of delivery, when market price rose to \$90/ton); *Henningsen v. Bloomfield Motors, Inc.*, 161 A.2d 69 (1960) (noting a disclaimer of warranty for personal injuries resulting from failure of steering mechanism unconscionable; citing UCC § 2-302 although it was not in effect in jurisdiction).

15. *Earl of Chesterfield v. Janssen*, 28 Eng. Rep. 82, 100 (Ch. 1750). One of the earliest quotations of this definition appears in *Hume v. United States*, 132 U.S. 406, 411 (1889) (agreeing to pay \$1200 per ton for materials worth \$35 per ton is unconscionable and unenforceable).

16. U.C.C. § 2-302 (1989) reads:

If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

17. U.C.C. § 2-302 cmt. official (1989).



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Courts generally recognize two types of unconscionability, procedural and substantive,<sup>18</sup> and may require the presence of both in order to find a particular agreement unconscionable.<sup>19</sup> Procedural unconscionability refers to the making of an agreement, and substantive unconscionability refers to its terms. In assessing procedural unconscionability, courts consider the experience, intelligence, and education of the parties, their relative bargaining power, the presence or absence of meaningful choice on the part of the weaker party, the conspicuousness and clarity of the contract terms, and other factors. Indicia of substantive unconscionability include harsh, one-sided or oppressive terms; for example, a grossly excessive price may be found unconscionable.<sup>20</sup> Over time, courts have applied the doctrine to transactions outside of Article 2 of the UCC<sup>21</sup> and a common law doctrine of unconscionability has developed. Section 2-302 and related issues have generated a huge volume of commentary,<sup>22</sup> while the case law has been sparse.<sup>23</sup> Section 2 of the Federal Arbitration Act permits assertion of generally applicable contract defenses, including unconscionability, against arbitration agreements.<sup>24</sup> However, any special

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18. See *supra* note 17 and accompanying text. The comment to UCC § 2-302 suggests this division, with “prevention of oppression” referring to substantive unconscionability and “prevention of . . . unfair surprise” referring to procedural unconscionability.

19. The UCC does not require both. Most cases involve elements of both substantive and procedural unconscionability.

20. See, e.g., *Hume*, 132 U.S. at 414.

21. Including, for example, prenuptial and divorce agreements.

22. See, e.g., Evelyn L. Brown, *The Uncertainty of U.C.C. Section 2-302: Why Unconscionability Has Become a Relic*, 105 COM. L.J. 287 (2000); Richard Craswell, *Property Rules and Liability Rules in Unconscionability and Related Doctrines*, 60 U. CHI. L. REV. 1 (1993); Robert A. Hillman, *Debunking Some Myths About Unconscionability: A New Framework for U.C.C. Section 2-302*, 67 CORNELL L. REV. 1 (1981); Arthur Allen Leff, *Unconscionability and the Code—The Emperor’s New Clause*, 115 U. PA. L. REV. 485 (1967); Eric A. Posner, *Contract Law in the Welfare State: A Defense of the Unconscionability Doctrine, Usury Laws, and Related Limitations on the Freedom to Contract*, 24 J. LEGAL STUD. 283 (1995); John A. Spanogle, *Analyzing Unconscionability Problems*, 117 U. PA. L. REV. 931 (1969); Carol B. Swanson, *Unconscionable Quandary: UCC Article 2 and the Unconscionability Doctrine*, 31 N.M. L. REV. 359 (2001).

23. See *infra* note 32 and accompanying text.

24. Section 2 provides that a written agreement to arbitrate in a contract involving interstate commerce “shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any

rules regarding the enforceability of arbitration agreements are unlawful, as contrary to the language of the Federal Arbitration Act and Congressional intent. Because the doctrine of unconscionability is purposefully open-ended and its parameters undefined,<sup>25</sup> it is particularly susceptible to expansions superficially within the scope of Section 2. The nature of unconscionability allows simple circumvention of the Federal Arbitration Act, permitting parties to an arbitration agreement to litigate their claims through judicial application of arbitration-specific principles of unconscionability.

The leading case dealing with unconscionability in the context of arbitration agreements is *Doctor's Associates, Inc. v. Casarotto*.<sup>26</sup> In the initial decision,<sup>27</sup> the Montana Supreme Court invalidated an arbitration agreement which violated a Montana statute requiring a first-page, special type-face notice of the presence of an arbitration agreement in a contract.<sup>28</sup> The United States Supreme Court ruled that the Federal Arbitration Act preempted the Montana statute. Courts may apply contract defenses to invalidate arbitration agreements under Section 2 of the Federal Arbitration Act. If, however, courts apply the common law doctrine of unconscionability differently in the context of arbitration than in other contexts, preemption issues under the Federal Arbitration Act arise. In the Supreme Court's words:

[S]tate law, whether of legislative or judicial origin, is applicable *if* that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally. A state-law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with this requirement of § 2. . . . A court may not, then, in assessing the

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contract." 9 U.S.C. § 2 (2000). *See, e.g.,* *Wilmot v. McNabb*, 269 F. Supp. 2d 1203 (N.D. Cal. 2003).

25. Commentators have long noted the undefined character of the doctrine. *See supra* note 22.

26. 517 U.S. 681 (1996). *Doctor's Associates* built on the earlier decisions of *Southland*, *Perry*, and *Allied-Bruce Terminix*.

27. *See Casarotto v. Lombardi*, 886 P.2d 931 (1994), *rev'd*, 517 U.S. 681 (1996).

28. MONT. CODE ANN. § 27-5-114(4), which provided: "Notice that a contract is subject to arbitration pursuant to this chapter shall be typed in underlined capital letters on the first page of the contract; and unless such notice is displayed thereon, the contract may not be subject to arbitration."

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rights of litigants to enforce an arbitration agreement, construe that agreement in a manner different from that in which it otherwise construes nonarbitration agreements under state law. Nor may a court rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable, for this would enable the court to effect what we hold today the state legislature cannot.<sup>29</sup>

Counsel for Casarotto offered an alternative view of the Montana court's decision at oral argument. Counsel argued that the Montana court could have invalidated the arbitration agreement under general principles of informed consent, holding independent of the statute that unexpected provisions in adhesion contracts were enforceable only if conspicuous. Since the Montana Supreme Court did not rely on such a general principle, the United States Supreme Court rejected this argument.<sup>30</sup>

If the Montana Supreme Court had in fact relied on general principles of Montana contract law, holding the arbitration agreement unconscionable because it was inconspicuous, did not provide adequate notice of its contents, and ran counter to the reasonable expectations of average consumers, what would have been the result in the United States Supreme Court? Case law makes it clear that a court may not apply unconscionability doctrine differently for arbitration agreements than for other agreements. Assuming, however, that Montana common law identified as general indicia of unconscionability the features of the arbitration agreement in *Doctor's Associates*, Montana courts could have invalidated the agreement under Section 2. The Federal Arbitration Act would not have preempted the general law of unconscionability in Montana as applied to an arbitration agreement in the same way it would apply to any contract.<sup>31</sup> Even if Montana courts had only articulated general principles of unconscionability, presumably they could have invalidated the agreement.

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29. *Perry v. Thomas*, 482 U.S. 483, 492 n.9 (1987) (emphasis in original).

30. *See* 517 U.S. 687-88 n.3.

31. For a different answer to this question, see Stephen J. Ware, *Arbitration and Unconscionability after Doctor's Associates, Inc. v. Casarotto*, 31 WAKE FOREST L. REV. 1001, 1016 (1996). Professor Ware reasons that because the FAA does not distinguish between common law and statutory law, "Justice Trieweiler could not have avoided FAA preemption by labeling the reasoning he used in *Doctor's Associates* 'unconscionability,' instead of '*Montana Code* section 27-5-114(4).'"

Unconscionability is an open-ended, undefined concept subject to judicial definition case-by-case. Judges in Montana and elsewhere have the power to hold, as a matter of common law, that a particular agreement is one-sided, oppressive, and unfair (in a word, unconscionable) and thus the power to circumvent the Federal Arbitration Act. What they may not say, under the Federal Arbitration Act, is that the agreement is one-sided, oppressive, and unfair simply because it is an arbitration agreement. But that limitation is minimal and easily skirted. As the next sections attempt to demonstrate, judges are in fact circumventing the Federal Arbitration Act and permitting litigation by parties to arbitration agreements through expansive, arbitration-specific uses of unconscionability.

## II. THE RESURGENCE IN UNCONSCIONABILITY

Litigants rarely invoked unconscionability prior to the increase in the use of arbitration agreements. The conventional wisdom was that unconscionability claims fail.<sup>32</sup> However, as the use of arbitration agreements has increased, claims of unconscionability have also increased and those claims have been surprisingly successful. A systematic examination<sup>33</sup> shows that in 2002-2003, litigants raised issues of unconscionability in 235 cases, and courts found contracts or clauses<sup>34</sup> to be unconscionable in 100 of those cases, or 42.5%. Of those 235 cases, 161, or 68.5%, involved arbitration agreements. Significantly, courts were much more likely to find arbitration agreements, as opposed to other sorts of contracts, unconscionable. Courts found 50.3% of the arbitration agreements unconscionable, as opposed to 25.6% of other types of contracts. Although federal and state courts in California decided a significant

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32. See Joseph M. Perillo, *Avoidance and Reformation*, in 7 CORBIN ON CONTRACTS § 29.4 (“Most claims of unconscionability fail.”).

33. Computer searches yielded the cases. I included only cases in which one of the parties asserted that an agreement was unconscionable and in which the court actually addressed and decided the issue. I excluded criminal cases which dealt primarily with various types of plea and proffer agreements. I also excluded agreements related to family and marital issues: prenuptial, divorce, custody, and child support agreements, and the like.

34. In most of the cases, courts invalidated the entire agreement, permitting litigation of the claim. In a few of the cases, courts severed an unconscionable provision and enforced the remainder of the arbitration agreement. This latter category is included in the count of judicial findings of unconscionability.

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number of these cases, a total of seventeen state courts<sup>35</sup> and fifteen federal courts<sup>36</sup> found provisions in arbitration agreements unconscionable.

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35. Alabama, *see, e.g.*, *Anderson v. Ashby*, No. 1011740, 2003 WL 21125998 (Ala. May 16, 2003); *Harold Allen's Mobile Home Factory Outlet, Inc. v. Butler*, 825 So.2d 779 (Ala. 2002); *Ex Parte Thicklin*, 824 So.2d 723 (Ala. 2002); California, *Wilson v. Bally Total Fitness Corp., Inc.*, No. D039355m 2003 WL 21398324 (Cal. Ct. App. June 18, 2003); Florida, *Romano ex rel. Romano v. Manor Care, Inc.*, 861 So.2d 59 (Fla. Dist. Ct. App. 2003); Idaho, *Murphy v. Mid-West Nat'l Life Ins. Co. of Tenn.*, 78 P.3d 766 (Idaho 2003); Kentucky, *Wilder v. Absorption Corp.*, 107 S.W.3d 181 (Ky. 2003); Louisiana, *Posadas v. Pool Depot, Inc.*, 2002-1819 (La. App. 1 Cir. 6/27/03), 858 So.2d 611, writ denied, 2003-2125 (La. 11/7/03), 857 So.2d 502; *Simpson v. Grimes*, 2002-0869 (La. App. 3 Cir. 5/21/03), 849 So.2d 740, writ denied, 2003-2497 (La. 12/19/03), 861 So.2d 567; Massachusetts, *Buhrer v. BDO Seidman, LLP*, 16 Mass. L. Rptr. 551 (Ma. Super. 2003); Mississippi, *E. Ford, Inc. v. Taylor*, No. 2000-IA-01527-SCT (Miss. 2002), 826 So.2d 709, *aff'd*, 537 U.S. 1194 (2003); Missouri, *Swain v. Auto Servs., Inc.* No. ED82788, 2003 WL 22890022 (Mo. Ct. App. Dec. 9, 2003); New Mexico, *Padilla v. State Farm Mut. Auto. Ins. Co.*, 2003-NMSC-011, 68 P.3d 901 (N.M. 2003) Nevada, *Burch v. 2nd Jud. Dist. Ct. of State ex rel., County of Washoe*, 49 P.3d 647 (Nev. 2002); Ohio, *O'Donoghue v. Symthe, Cramer Co.*, No. 80453, 2002 WL 1454074 (Ohio Ct. App. July 3, 2003); Pennsylvania, *Lytle v. Citi Fin. Servs., Inc.*, 810 A.2d 643 (Pa. Super. Ct. 2002); *Carll v. Terminix Int'l Co.*, 793 A.2d. 921 (Pa. Super. Ct. 2002); Tennessee, *Howell v. NHC Healthcare-Fort Sanders, Inc.*, 109 S.W.3d 731 (Tenn. Ct. App. 2003); Texas, *In re Palm Harbor Homes, Inc.*, No. 01-02-00370-CV, 2003 WL 23096490 (Tx. App. 2003); Washington, *Mendez v. Palm Harbor Homes, Inc.*, 45 P.3d 594 (Wash. App. Ct. 2002); and West Virginia, *Toppings v. Meritech Mortgage Servs. Inc.*, 569 S.E.2d 149 (W.Va. 2002); State *ex rel Dunlap v. Berger*, 567 S.E.2d 265 (W.Va. 2002), *aff'd*, 537 U.S. 1087 (2002).

36. The Third Circuit, applying Virgin Islands law, *Alexander v. Anthony Int'l, L.P.*, 341 F.3d 256 (3rd Cir. 2003); the Fourth Circuit, applying Maryland law, *Murray v. United Food & Commercial Workers Int'l Union*, 289 F.3d 297 (4th Cir. 2002); the Ninth Circuit, applying California law, *see, e.g., Circuit City Stores, Inc. v. Mantor*, 335 F.3d 1101 (9th Cir. 2003), *aff'd*, No. 03-605, 2004 WL 110852 (2004); *Ingle v. Circuit City Stores, Inc.*, 328 F.3d 1165 (9th Cir. 2003), No. 03-604, 2004 WL 110851 (2004); *Ting v. AT&T*, 319 F.3d 1126 (9th Cir. 2003), *aff'd*, 124 S.Ct. 53 (2003); Hawai'i law, *Kyocera Corp. v. Prudential-Bache Trade Services, Inc.*, 341 F.3d 987 (9th Cir. 2003), *aff'd*, 124 S.Ct. 980 (2004); and Montana law, *Domingo v. Ameriquet Mortgage Co.*, 70 Fed. Appx. 919 (9th Cir. 2003); and district courts in Arkansas, *Casteel v. Clear Channel Broad., Inc.*, 254 F.Supp. 2d 1081 (W.D. Ark. 2003) California, *Comb v. Paypal, Inc.* 218 F.Supp. 2d 1165 (N.D. Cal. 2002); *Acorn v. Household Int'l, Inc.* 211 F.Supp. 2d 1160 (N.D. Cal. 2002); Illinois, *Plattner v. Edge Solutions, Inc.*, No. 03C2646, 2003 WL 22859532 (N.D. Ill. Dec. 2, 2003); Iowa, *Faber v. Menard, Inc.*, 267 F.Supp. 2d 961 (N.D. Iowa 2003); Michigan, *DeOrnellas v. Aspen Square Mgmt., Inc.*, No. 03-10147, 2003 WL 22966021 (E.D. Mich. Dec. 4, 2003); Minnesota, *Gooden v. Vill. Green Mgmt. Co.*, No. Civ. 02-835 (JRT/SRN), 2002 WL 31557689 (D. Minn. Nov. 15, 2002); New York, *Brennan v. Bally Total Fitness*, 198 F.Supp. 2d 377 (S.D.N.Y. 2002); Ohio, *Garrett v. Hooters-Toledo*, No. 3:03CV7053 2003 WL 22989049 (N.D. Ohio Nov 24, 2003); *Hagedorn v.*

For purposes of comparison, twenty years ago<sup>37</sup> there were fifty-four cases in which the court was called upon to decide a question of unconscionability. In nine of those, or 16.7%, the court found the contract unconscionable. Eight of the fifty-four decisions, or 14.8%, involved arbitration agreements; one of the eight arbitration agreements was found to be unconscionable. The rate of unconscionability findings by type of contract, arbitration or nonarbitration, showed little variation. Courts held 12.5% of the arbitration agreements, as compared to 15.2% of other types of contracts, unconscionable. Thus, twenty years ago, courts were slightly less likely to find arbitration agreements unconscionable than nonarbitration agreements; in 2002-2003, courts found arbitration agreements unconscionable twice as frequently as other types of contracts.

These increases raise preemption issues under the Federal Arbitration Act. Courts may not use unconscionability differently in arbitration than in nonarbitration contexts. Judicial application of arbitration-specific contract defenses to arbitration agreements violates the Federal Arbitration Act. According to the Supreme Court, "state law, whether of legislative or judicial origin, is applicable [to arbitration agreements] *if* that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally."<sup>38</sup> Various factors may account in some part for the increases in findings of unconscionability, including increases in numbers of cases generally and an escalating aggressiveness in the drafting of arbitration agreements. However, increased judicial willingness to find unconscionability in arbitration agreements suggests a latent judicial hostility to arbitration and use of unconscionability contrary to the Federal Arbitration Act's mandate: an arbitration agreement "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the

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Veritas Software Corp., 250 F.Supp. 2d 857 (S.D. Ohio 2002); Oregon, *Torrance v. Aames Funding Corp.*, 242 F.Supp. 2d 862 (D. Or. 2002); Tennessee, *Walker v. Ryan's Family Steak Houses, Inc.*, 289 F.Supp. 2d 916 (M.D. Tenn. 2003); Cooper v. MRM Inv. Co., 199 F.Supp. 2d 771 (M.D. Tenn. 2002); Washington, *Luna v. Household Fin. Corp. III*, 236 F.Supp. 2d 1166 (W.D. Wash. 2002); and the Virgin Islands, *Plaskett v. Bechtel Int'l, Inc.*, 243 F.Supp. 2d 334 (D.V.I. 2003); *Lloyd v. Hovensa, LLC*, 243 F.Supp. 2d 346 (D.V.I. 2003).

37. 1982 and 1983.

38. *Perry v. Thomas*, 482 U.S. 483, 492 n.9 (1987).

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revocation of *any contract*.”<sup>39</sup> As the next section demonstrates, courts uphold the same contract provisions in nonarbitration contracts that they find unconscionable in arbitration agreements. The next section turns to an examination of various grounds on which courts have found arbitration agreements unconscionable,<sup>40</sup> and assesses

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39. Federal Arbitration Act, 9 U.S.C. § 2 (2000) (emphasis added).

40. When a court finds an arbitration agreement unconscionable, it of course refuses to enforce it. Where only a portion of that agreement is unconscionable, the court has a choice to sever the offending provision or find the entire agreement unenforceable. Where there are multiple unconscionable provisions, courts generally declare the entire agreement unenforceable. A growing number of courts recognize that severance of an unconscionable provision presents potential opportunities for abuse. *See, e.g.*, *Clary v. Stanley Works*, No. 03-1168-JTM, 2003 WL 21728865 (D. Kan. July 24, 2003); *Bailey v. Ameriquist Mortgage Co.*, No. CIV. 01-545(JRTFLN) 2002 WL 100391 (D. Minn. Jan. 23, 2002). A court’s severance of an offending provision may encourage parties with superior bargaining power to include questionable or unlawful provisions in their arbitration agreements, with the purpose of deterring potential claims. For example, defendants have often attempted to circumvent rules invalidating arbitration agreements which impose prohibitive costs on a claimant by offering to pay all costs. Many courts reject such attempts with the aim of protecting claimants generally. *See, e.g.*, *Spinetti v. Serv. Corp. Int’l*, 324 F.3d 212, 217-218 n.2 (3d Cir. 2003); *Morrison v. Circuit City Stores*, 317 F.3d 646, 673 n.15 (6th Cir. 2003); *Cooper v. MRM Inv. Co.*, 199 F.Supp. 2d 771, 781-82 (M.D. Tenn. 2002); *In re Managed Care Litig.*, 132 F.Supp. 2d 989, 1001 (S.D. Fla. 2000); *O’Hare v. Mun. Resource Consultants*, 132 Cal. Rptr. 2d 116, 126 (Cal. Ct. App. 2003) (“No existing rule of contract law permits a party to resuscitate a legally defective contract merely by offering to change it.”); *West Virginia ex rel. Dunlap v. Berger*, 567 S.E.2d 265 (W. Va. 2002); *Flyer Printing Co. v. Hill*, 805 So. 2d 829, 833 (Fla. Dist. Ct. App. 2001). Some courts have failed to recognize the potential problems with permitting an after-the-fact offer to pay and have permitted defendants to cure problematic arbitration agreements with such offers. *See* *Murphy v. AmSouth Bank*, 269 F.Supp. 2d 749, 752 (S.D. Miss. 2003) (“Plaintiffs’ objection that the potential costs of arbitration render, or may render enforcement of the agreement unconscionable is rendered moot by AmSouth’s stipulation that it will bear the cost of arbitration”); *Brown v. Dorsey & Whitney, LLP*, 267 F.Supp. 2d 61 (D.D.C. 2003) (if defendant agrees to waive presumably prohibitive cost provisions of arbitration agreement, agreement enforceable); *Large v. Consecro Fin. Serv. Corp.*, 292 F.3d 49, 56-57 (1st Cir. 2002) (holding plaintiffs’ challenge to the enforceability of the arbitration agreement based on provision requiring them to pay costs not viable because defendant’s offer to pay costs of arbitration mooted the issue); *Nelson v. Insigna/ESG, Inc.*, 215 F.Supp. 2d 143 (D.C. Cir. 2002) (stating that employer’s offer to pay arbitration fees cured any potential inability of employee to vindicate statutory claims as a result of financial situation); *Arellano v. Household Fin. Corp. III*, No. 01 C 2433, 2002 WL 221604 (N.D. Ill. Feb. 13, 2002) (demonstrating that court permitted mortgagor’s agreement to pay costs after-the-fact); *Ex parte Celtic Life Ins. Co.*, 834 So. 2d 766, 768 (Ala. 2002) (demonstrating that a party to a contract can waive a provision beneficial to

substantive Federal Arbitration Act preemption issues with respect to each.

### III. UNCONSCIONABILITY IN ARBITRATION AGREEMENTS

The analysis in Section II demonstrates that judges have used unconscionability with increasing frequency in recent years and are much more likely to hold arbitration agreements, as compared to nonarbitration agreements, unconscionable. An examination of the application of unconscionability to similar issues in arbitration and nonarbitration contexts supports the conclusion that judges are avoiding arbitration through arbitration-specific expansions of the doctrine of unconscionability.

#### A. *Excessive Costs Which Limit One Party's Access to Arbitration*

Various courts, including the United States Supreme Court, have held that excessive arbitration costs<sup>41</sup> which limit a party's access to an arbitral forum may render an

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itself; in this instance, provision in arbitration agreement prohibiting punitive damages held in other Alabama cases to render agreement unenforceable). Courts which permit such strategies encourage and perpetuate bad behavior. Fundamental fairness requires that courts reviewing the ability of plaintiffs to pay arbitration costs should not consider these offers where the arbitration agreement provides that the plaintiff is liable, or potentially liable, for arbitration fees and costs. Excessively burdensome cost-splitting or "loser pays" provisions in arbitration agreements deter all potential litigants from bringing claims in arbitration. Courts should refuse to require arbitration in such cases, regardless of whether a defendant agrees to pay a particular claimant's share of fees and costs. Judicially-sanctioned "curing" of such provisions encourages overreaching by the drafters with adverse consequences for weaker parties generally.

41. Such costs may include filing fees, fees for the use of a facility in which to hold the hearing, arbitrator's fees, which the parties to the arbitration often split, or costs imposed under "loser-pays" provisions, which require the losing party to pay various fees and costs in full. Many of the issues related to arbitration costs will become less pervasive as a result of procedures adopted by arbitration service providers which prevent excessive fees from precluding vindication of rights. *See, e.g.,* American Arbitration Association, *National Rules for the Resolution of Employment Disputes*, [http://www.adr.org/index2.1.jsp?JSPssid=15747&JSPsrc=upload\LIVESITE\Rules\\_Procedures\National\\_International\...\focusArea\employment\AAA121current.html](http://www.adr.org/index2.1.jsp?JSPssid=15747&JSPsrc=upload\LIVESITE\Rules_Procedures\National_International\...\focusArea\employment\AAA121current.html) (last visited Feb. 4, 2004); JAMS, *JAMS Employment Arbitration Rules & Procedures*, [http://www.jamsadr.com/employment\\_arbitration\\_Rules-2003.asp](http://www.jamsadr.com/employment_arbitration_Rules-2003.asp) (last visited Feb. 4, 2004).



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arbitration agreement invalid, affording the party access to court. These cases demonstrate hostility to arbitration, even at the Supreme Court level. In virtually all civil cases, a prospective litigant's inability to afford litigation is irrelevant; no accommodations are made to ensure that a mechanism is available to resolve the dispute. A comparison of the case law regarding prohibitive arbitration costs, which may afford court access, and prohibitive court costs, for which there is no relief, illustrates the point.

1. *Green Tree and Individualized Assessments of Access to Arbitration*. The United States Supreme Court has held that excessive arbitration costs that limit one party's access to an arbitral forum may render an arbitration agreement invalid. In *Green Tree Financial Corp. v. Randolph*,<sup>42</sup> Randolph argued that her agreement to arbitrate was unenforceable because it said nothing about the costs of arbitration, and thus failed to protect her from potentially prohibitive costs of pursuing her federal statutory claims.<sup>43</sup> The Court acknowledged that substantial arbitration costs could preclude a litigant from vindicating federal statutory rights<sup>44</sup> in the arbitral forum. However, Randolph had not presented evidence demonstrating that she would in fact bear such costs if she were required to arbitrate, and the Court declined to hold the agreement unenforceable.<sup>45</sup>

The Supreme Court did not determine "[h]ow detailed the showing of prohibitive expense must be before the party seeking arbitration must come forward with contrary

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42. 531 U.S. 79 (2000).

43. *See id.* at 90.

44. Randolph alleged violations of the Truth in Lending Act (TILA), 15 U.S.C. § 1601 *et seq.*, by failing to disclose as a finance charge the Vendor's Single Interest insurance requirement, and of the Equal Credit Opportunity Act, 15 U.S.C. §§ 1691-1691f, by requiring her to arbitrate her statutory causes of action. *See id.* at 83.

45. Justices Ginsburg, Stevens, Souter and Breyer dissented from that holding, and would have remanded to the Eleventh Circuit for further consideration of the financial accessibility of the arbitral forum. These justices also suggested that the majority's allocation of the burden of proof on this issue was incorrect. Given Green Tree's superior information about the cost to consumers of pursuing arbitration and the fairness of assigning the burden of proof to the party with special knowledge, the dissenters stated, "it is hardly clear that Randolph should bear the burden of demonstrating up front the arbitral forum's inaccessibility." *Id.* at 96.

evidence.”<sup>46</sup> The federal courts have generally adopted a case-by-case determination, focusing on the claimant’s ability to pay, the difference between costs of litigation and arbitration, and the likelihood that the cost of arbitration will deter the bringing of claims.<sup>47</sup> The burden of proof is on

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46. *Id.* at 92.

47. See *Spinetti v. Service Corp. Int’l*, 324 F.3d 212 (3d Cir. 2003); *Musnick v. King Motor Co. of Fort Lauderdale*, 325 F.3d 1255, 1259 (11th Cir. 2003) (stating that the “overwhelming consensus” among Circuits is that cost-splitting or “loser pays” provisions of arbitration agreements are not a denial of federal statutory rights; arbitration agreement is not unenforceable merely because the party seeking to vindicate federal statutory rights may have to pay some costs); *Thompson v. Irwin Home Equity Corp.*, 300 F.3d 88 (1st Cir. 2002); *Blair v. Scott Specialty Gases*, 283 F.3d 595, 610 (3d Cir. 2002) (demonstrating how the court followed the reasoning of *Green Tree* and required showing of prohibitive arbitration expenses by party opposing arbitration; mere existence of fee-splitting provision does not render arbitration agreement unenforceable); *Primerica Life Ins. Co. v. Brown*, 304 F.3d 469, 471 n.1 (5th Cir. 2002); *Bess v. Check Express*, 294 F.3d 1298, 1302 (11th Cir. 2002) (recognizing that the Eleventh Circuit’s prior adherence to the per se invalidation rule was no longer good law in light of the Supreme Court’s reversal of its decision in *Green Tree*); *LaPrade v. Kidder, Peabody & Co.*, 246 F.3d 702, 708 (D.C. Cir. 2001) (affirming arbitration award to be paid by employee after employee failed to demonstrate “that the assessment against her [ran] afoul” of public policy); *Bradford v. Rockwell Semiconductor Sys., Inc.*, 238 F.3d 549, 553-57 (4th Cir. 2001) (explaining the case-by-case inquiry into financial circumstances of party opposing arbitration required under *Green Tree*); *Burden v. Check into Cash of Kentucky, LLC*, 267 F.3d 483, 492 (6th Cir. 2001) (stating that a party resisting arbitration must demonstrate prohibitive expenses; case-by-case analysis required); *Gannon v. Circuit City Stores, Inc.*, 262 F.3d 677, 683 n.9 (8th Cir. 2001) (reading *Green Tree* to require case-by-case analysis with plaintiff bearing the burden of proof that arbitration expenses are likely to be prohibitive); *Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 170 F.3d 1, 15-16 (1st Cir. 1999) (refusing to invalidate arbitration agreement even where plaintiff may be charged “tens of thousands of dollars per case” because claimant’s argument too speculative; also observing that “arbitration is often far more affordable to plaintiffs and defendants alike” than litigation); *Williams v. Cigna Fin. Advisors, Inc.*, 197 F.3d 752, 764 (5th Cir. 1999) (adopting case-by-case analysis to determine whether claimant can effectively vindicate statutory rights; also holding that a fee-splitting provision did not invalidate the arbitration agreement because the plaintiff had not shown that the arbitration fees required were prohibitive to his ability to vindicate his statutory claims); *Koveleskie v. SBC Capital Mkts.*, 167 F.3d 361, 366 (7th Cir. 1999) (following *Rosenberg*); *Shankle v. B-G Maint. Mgmt. of Colo.*, 163 F.3d 1230, 1234-35 (10th Cir. 1999) (holding that an arbitration agreement was invalid because the plaintiff’s total estimated arbitration costs of between \$1,875-\$5,000 were prohibitively high); *In re Currency Conversion Fee Antitrust Litig.*, 265 F.Supp. 2d 385 (S.D.N.Y. 2003); *Raasch v. NCR Corp.*, 254 F.Supp. 2d 847 (S.D. Ohio 2003) (explaining that per se invalidation of an arbitration agreement based on fee-splitting provision contradicts Supreme Court’s holding in *Green Tree*, that

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the party resisting arbitration.<sup>48</sup> State courts have endorsed similar tests.<sup>49</sup> Others have refused generally to invalidate arbitration agreements on grounds of cost.<sup>50</sup>

The *Green Tree* approach evidences some remnants of judicial hostility toward arbitration on the part of the United States Supreme Court. If Randolph's complaint was that her financial situation prevented her from paying court costs, the Court's current precedents would certainly not afford her a remedy. The Supreme Court has recognized only an extremely narrow category of civil cases in which the state must provide access to its judicial processes without regard to a party's ability to pay court fees. In cases in which fundamental rights are involved, and where protection of those fundamental rights may occur only through the judicial process, the Supreme Court has held access to courts without payment of fees constitutionally required.<sup>51</sup> In other cases, there is no right of free access to

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party resisting arbitration bears burden of proving the likelihood of incurring prohibitive costs); *Lloyd v. Hovensa LLC.*, 243 F.Supp. 2d 346 (D.C.V.I. 2003) ("[F]ee-splitting provision in an agreement does not, in and of itself, deny a plaintiff an opportunity to vindicate his or her statutory rights . . . plaintiff must show that the costs of the arbitral forum are prohibitive."); *Nelson v. Insignia/Esg, Inc.*, 215 F.Supp. 2d 143, 157-58 (D.C. Cir. 2002); *Stewart v. Paul, Hastings, Janofsky & Walker, LLP*, 201 F.Supp. 2d 291, 293 (S.D.N.Y. 2002); *Goodman v. ESPE America, Inc.*, No. 00-CV-862, 2001 WL 64749, at \*3-5 (E.D.Pa. Jan. 19, 2001) (rejecting a per se rule that fee-splitting is unenforceable; also holding that the "loser pays" provision does not invalidate arbitration agreement in absence of particularized showing that provision would preclude plaintiff from seeking to vindicate rights); *Arakawa v. Japan Network Group*, 56 F.Supp. 2d 349 (S.D.N.Y. 1999) (finding that the agreement to arbitrate Title VII claims is not unenforceable as a matter of law simply because the plaintiff faces the possibility of being charged arbitration fees; also arguing that a fee splitting arrangement is contrary to the remedial and deterrent aims of Title VII only if the fees are so great and plaintiff's financial situation is such that fees would substantially deter plaintiff from seeking to enforce statutory rights).

48. See cases cited *supra* note 47.

49. See, e.g., *Sanderson Farms, Inc. v. Gatlin*, 848 So. 2d 828, 849 (Miss. 2003) (requiring analysis of claimant's financial circumstances and using a "shock the judicial conscience" test).

50. See, e.g., *Lovey v. Regence BlueShield of Idaho*, 72 P.3d 877, 885 (Idaho 2003) ("We have never previously held that the prohibitive cost of arbitration could be a basis for invalidating an agreement to arbitrate, and we decline to do so in this case.").

51. See, e.g., *Boddie v. Connecticut*, 401 U.S. 371 (1971) (deciding that indigent divorce claimants have right of access to court without payment of filing fees because marriage is fundamental and dissolution is possible only through the courts); see also *M.L.B. v. S.L.J.*, 519 U.S. 102 (1996) (holding there

the courts. For example, an indigent bankruptcy petitioner does not have a right to free access to bankruptcy court because the personal interest at stake is not fundamental and because there are other methods of protecting the interest, for example, through negotiated agreement with creditors.<sup>52</sup> Similarly, welfare recipients have no right to appeal an adverse welfare benefits decision without the payment of a filing fee.<sup>53</sup>

Thus, the Court provides virtually no redress for a potential litigant prevented from obtaining access to the court system as a result of financial circumstances. It will, however, invalidate an otherwise valid private agreement to arbitrate because a potential claimant cannot afford to arbitrate. The situations are not exactly analogous, of course. The Supreme Court's access to courts jurisprudence turns on constitutional issues and the ability of a government institution to pass some of its costs onto litigants; its arbitration holdings focus on protection of statutory rights and the legitimacy of private agreements which may interfere with Congressional objectives.<sup>54</sup> Nonetheless, the Court's willingness to inquire into a party's financial situation to evaluate access to an arbitral forum (with the possible result that the party may then utilize the courts), but not to the judicial system, suggests a bias against arbitration.

2. *Generalized Assessments of Access to Arbitration.* A modification of the case-by-case approach advanced in *Green Tree* focuses more broadly, permitting a party to demonstrate that potential arbitration costs are significant enough to deter the actions of similarly situated individuals who may seek to vindicate federal statutory rights through

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is a right of access to court in civil cases only where fundamental interest, such as termination of parental rights, is at stake, and resort to judicial process mandatory). Whereas the claims in *Boddie* and *M.L.B.* dealt with access to the court to vindicate divorce and parental rights, Randolph's complaint involved her purchase of a mobile home.

52. *United States v. Kras*, 409 U.S. 434, 443-46 (1973).

53. *Ortwein v. Schwab*, 410 U.S. 656, 659 (1973).

54. If Congress chose to do so, it could of course require, through the FAA or in particular statutes, that any party to an arbitration, defending its practices against an alleged violation of a federal statutory right, would bear the burden of arbitration costs.

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arbitration.<sup>55</sup> This approach differs from that described above by focusing on the chilling effects of cost-splitting provisions generally as opposed to its effect on the actual plaintiff in the case. If a cost-splitting provision would deter a substantial number of potential claimants, it undermines the broader social purposes of the statutes alleged to have been violated. The Sixth Circuit in *Morrison v. Circuit City* explained this approach by reference to *Gilmer*, which held that “[s]o long as the prospective litigant effectively may vindicate [his or her] statutory cause of action in the arbitral forum, the statute will continue to serve both its remedial and deterrent function.”<sup>56</sup> In other words, the approach accounts for both the remedial and deterrent roles of federal anti-discrimination statutes. To protect the statutory rights at issue, the court must consider similar potential claimants as well as the actual claimant, since the potentiality of significant claims deters discriminatory practices.<sup>57</sup>

This more generalized assessment of the effects of costs on the ability of individuals to enforce their statutory rights through arbitration raises the issues identified in the preceding section. Why does an inability to afford arbitration costs ensure access to the civil justice system, while an inability to afford court costs is irrelevant to that access?

3. *Per Se Rules*. A minority of courts have rejected the *Green Tree* approach and adopted a rule which carries greater evidence of hostility to arbitration. These courts,

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55. See, e.g., *Morrison v. Circuit City Stores, Inc.*, 317 F.3d 646, 676-78 (6th Cir. 2003); *West Virginia ex rel. Dunlap v. Berger*, 567 S.E.2d 265, 282 (W. Va. 2002) (“[W]e hold that provisions in a contract of adhesion that if applied would impose unreasonably burdensome costs upon or would have a substantial deterrent effect upon a person seeking to enforce and vindicate rights and protections or to obtain statutory or common-law relief and remedies that are afforded by or arise under state law that exists for the benefit and protection of the public are unconscionable.”).

56. *Morrison*, 317 at 658 (citing *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 28 (1991) (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth*, 473 U.S. 614, 637 (1985))).

57. Other courts have taken a similar approach, although less explicitly. For example, in *Shankle*, the court concluded that an arbitration agreement was unenforceable because the plaintiff could not afford the fee, “and it is unlikely that other similarly situated employees could either.” *Shankle v. B-G Maint. Mgmt. of Colo.*, 163 F.3d 1230, 1234-35 (10th Cir. 1999).

which include the Ninth Circuit,<sup>58</sup> district courts in Iowa<sup>59</sup> and Oregon,<sup>60</sup> and the California state courts,<sup>61</sup> have adopted a per se rule that fee-splitting arrangements render an arbitration agreement invalid.<sup>62</sup> The seminal case

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58. *See, e.g.*, *Ingle v. Circuit City Stores, Inc.*, 328 F.3d 1165, 1174, 1178 n.17 (9th Cir.2003) (finding the cost-splitting provision of the Circuit City arbitration agreement, providing that arbitrator had discretion to require unsuccessful employee to pay Circuit City's costs and to require successful employee to pay her share of the costs of arbitration, unconscionable and in opposition to Congress's intent in enacting civil rights statutes); *Ting v. AT&T*, 319 F.3d 1126, 1151 (9th Cir. 2003); *Ferguson v. Countrywide Credit Indus., Inc.*, 298 F.3d 778, 785 (9th Cir. 2002) (holding that the arbitration scheme at issue "imposes multiple fees which would bring the cost of arbitration for [the employee] into the thousands of dollars").

59. *See, e.g.*, *Faber v. Menard, Inc.*, 267 F.Supp. 2d 961, 986-87 (N.D. Iowa 2003) (refusing to sever cost provisions of arbitration agreement in employment agreement which included a "pay own costs" provision and required payment of half arbitrator's fees, since parties' resources and access to counsel are disparate and would deter pursuit of otherwise valid statutory claims; no inquiry into employee's particular financial circumstances).

60. *See, e.g.*, *Torrance v. Aames Funding Corp.*, 242 F.Supp. 2d 862, 875 (D. Or. 2002) ("Requiring payment of arbitrator's fees, as opposed to reasonable costs, is not permitted as a condition of arbitration."). Similarly, the court in *Lelouis* seems to be rejecting *Green Tree* in stating,

the issue here is not just whether the costs in this particular case would deter this particular plaintiff from arbitrating her claims. That could necessitate a fact-intensive inquiry into the plaintiff's assets and ability to pay, whether someone might lend her the money, etc. However, it is neither necessary, nor efficient, for the court to examine such matters for each arbitration agreement. The better approach is that taken by the California Supreme Court in *Armendariz*, which 'places the cost of arbitration on the party that imposes it.' This rule applies only when an employer demands that an employee sign an arbitration agreement; it does not apply to freely negotiated arbitration agreements.

*Lelouis v. W. Directory Co.*, 230 F.Supp. 2d 1214, 1224 (D.Or. 2001) (citations omitted) (quoting *Armendariz v. Found. Health Psychcare Servs., Inc.*, 6 P.3d 669, 682 n.8, 688 (Cal. 2000)).

61. The leading case on this issue is *Armendariz*, 6 P.3d at 687-88.

62. The Tenth Circuit has been cited as adopting the per se rule, but a careful reading of the case in question demonstrates that it has not actually done so. In *Shankle*, the Tenth Circuit asserted that an arbitration must provide an adequate forum for the resolution of federal statutory claims. *See Shankle*, 163 F.3d at 1233-34 (citing *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26 (1991)). The Court also cited *Cole*, the seminal case adopting the per se rule that fee splitting provisions render an arbitration agreement invalid. *Shankle*, 163 F.3d at 1233 (citing *Cole v. Int'l Sec. Servs.*, 105 F.3d 1465, 1468 (D.C. Cir. 1997)). A number of courts have cited *Shankle* as adopting the per se rule. *See, e.g.*, *Williams v. Cigna Fin. Advisors, Inc.*, 197 F.3d 752, 763 (5th Cir. 1999). The *Shankle* court, however, actually applied the case-by-case rule,

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adopting a per se rule that cost-splitting invalidates an arbitration agreement is *Cole v. Burns International Security Services*,<sup>63</sup> a D.C. Circuit Court opinion which predated the Supreme Court's decision in *Green Tree*. Although it has not yet directly addressed the question of *Green Tree*'s impact on *Cole*, the D.C. Circuit has retreated from its holding in *Cole*. In *LaPrade v. Kidder, Peabody & Co., Inc.*,<sup>64</sup> the D.C. Circuit Court held that, given the limited fees assessed against the plaintiff, she failed to prove a claim that the possibility of substantial fees prevented her from attempting to vindicate her statutory rights. Without overruling *Cole*, the court declined to follow *Cole*'s per se rule that fee shifting renders an arbitration agreement unenforceable. Following *LaPrade*, the Court refused to extend *Cole* to non-statutory state claims.<sup>65</sup> Other courts have declined to follow *Cole* based on their reading of *Green Tree*.<sup>66</sup> The Eleventh Circuit, which had adopted a per

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reviewing the plaintiff's financial situation and holding that he could not afford the fees, and adding "it is unlikely other similarly situated employees could either." 163 F.3d at 1234-35. This last statement along with the approving citation of *Cole* injects some ambiguity into the Tenth Circuit's position, but *Shankle* has been read by other federal courts as effectively adopting the majority case-by-case rule. See, e.g., *Musnick v. King Motor Co. of Fort Lauderdale*, 325 F.3d 1255, 1259 n.4 (11th Cir. 2003); *Morrison v. Circuit City Stores, Inc.*, 317 F.3d 646, 648 n.4 (6th Cir. 2003); *Bradford v. Rockwell Semiconductor Sys., Inc.*, 238 F.3d 549, 555 (4th Cir. 2001) ("Notably, although *Shankle* found that the fee-splitting provision rendered the arbitration agreement unenforceable, it framed its analysis in terms of the complaining party's actual inability to afford the arbitration costs and fees."); *Perez v. Hospitality Ventures-Denver LLC*, 245 F.Supp. 2d 1172, 1173 (D. Colo. 2003) (reading *Shankle* as requiring individualized assessments of particular claimant's ability to access the arbitral forum).

In *Ball v. SFX Broadcasting, Inc.*, 165 F.Supp. 2d 230, 239-40 (N.D.N.Y. 2001), the District Court read *Green Tree* as requiring that a party seeking to avoid arbitration must show only the "likelihood" of incurring prohibitive arbitration costs and distinguished this analysis from the analysis adopted by courts focusing on the financial situation of the particular plaintiff. The District Court, however stopped short of adopting a per se rule, holding that the plaintiff had demonstrated that she could not afford the fees which would be imposed on her in the arbitration.

63. 105 F.3d at 1468 (holding that fee-splitting provisions in arbitration agreements per se invalid because such cost obligations deter or prohibit employees from pursuing their statutory rights in an arbitral forum).

64. 246 F.3d 702, 704 (D.C. Cir. 2001) (explaining that *Cole* only prohibited the assessment of "arbitration-related costs that are analogous to a judge's salary or expenses in a traditional judicial forum.>").

65. See *Brown v. Wheat First Secs., Inc.*, 257 F.3d 821, 823 (D.C. Cir. 2001).

se rule,<sup>67</sup> retreated from those pre-*Green Tree* holdings in *Musnick v. King Motor Co. of Fort Lauderdale*,<sup>68</sup> based on its reading of *Green Tree*.

All of the decisions adopting a per se rule that cost-splitting provisions invalidate an arbitration agreement run counter to *Green Tree*. Under *Green Tree*, a party resisting arbitration shoulders the initial burden of demonstrating the likelihood of incurring prohibitively expensive arbitration costs.<sup>69</sup> The Supreme Court found an arbitration agreement that was silent about the costs of the arbitration enforceable, because the record did not contain any evidence that the individual plaintiff would bear expenses that would effectively prohibit arbitration of her statutory

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66. See, e.g., *Raasch v. NCR Corp.*, 254 F.Supp. 2d 847, 858 (S.D. Ohio 2003) (noting that the holdings in *Cole*, *Paladino*, and *Armendariz* are “questionable,” given the Supreme Court’s subsequent decision in *Green Tree*). See also *Sparks v. Stone St. Capital, Inc.*, No. 3-02-CV-724-R, 2002 WL 1575404 (N.D. Tex. July 15, 2002) (reading *Shankle*, supra note 47, which relied on *Cole*, as being overruled by *Green Tree*); *Cooper v. MRM Inv. Co.*, 199 F.Supp. 2d 771 (M.D. Tenn. 2002); *Klinedinst v. Tiger Drylac, U.S.A., Inc.*, No. 01CV040, 2001 WL 1561821 (D.N.H. Nov. 28, 2001) (finding the *Cole* rationale unpersuasive because it predates *Green Tree*); *Manuel v. Honda R & D Americas, Inc.*, 175 F.Supp. 2d 987 (S.D. Ohio 2001) (holding that a per se invalidation of an arbitration agreement, due to the presence of a fee-splitting provision, contradicts the Supreme Court’s holding in *Green Tree*); *Boyd v. Hayneville, AL*, 144 F.Supp. 2d 1272, 1280 (M.D. Ala. 2001) (arguing that given Supreme Court’s decision in *Green Tree*, “prudent course” is to follow circuit courts which have declined to adopt a per se rule against fee-splitting; arbitration-related expenses acceptable so long as they do not render arbitral forum inaccessible); *Rains v. Found. Health Sys. Life & Health*, 23 P.3d 1249 (Colo. Ct. App. 2001); and *Martindale v. Sandvik, Inc.*, 800 A.2d 872, 889 (N.J. 2002) (dissenting opinion).

67. See, e.g., *Bess v. Check Express*, 294 F.3d 1298 (11th Cir. 2002); *Paladino v. Avnet Computer Techs., Inc.*, 134 F.3d 1054, 1057-58 (11th Cir. 1998).

68. *Compare Musnick v. King Motor Co. of Fort Lauderdale*, 325 F.3d 1255, 1259 (11th Cir. 2003) (“After *Green Tree*, an arbitration agreement is not unenforceable merely because it may involve some ‘fee-shifting.’ The party seeking to avoid arbitration under such an agreement has the burden of establishing that enforcement of the agreement would ‘preclude’ him from ‘effectively vindicating [his] federal statutory right in the arbitral forum.’ ”), with *Bess v. Check Express*, 294 F.3d 1298, 1303 (11th Cir. 2002) (recognizing that under *Green Tree*, a Title VII plaintiff attempting to avoid his agreement to arbitrate his discrimination claim by arguing that prohibitive arbitration costs would undermine his statutory remedy must demonstrate that he is likely to bear such costs).

69. 531 U.S. at 92.



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claims.<sup>70</sup> Thus, the Supreme Court focused on the individual employee's ability or inability to demonstrate economic inaccessibility of the arbitral forum. This language indicates that the Supreme Court envisions a case-by-case analysis to determine whether imposition of costs, including through fee-splitting agreements, are enforceable.<sup>71</sup>

The federal court cases holding that cost-splitting provisions automatically invalidate an arbitration agreement<sup>72</sup> raise questions of the correct interpretation of the Federal Arbitration Act and its reconciliation with various federal statutes. These federal courts' willingness to invalidate a private arbitration agreement, simply because it requires a party claiming federal statutory rights to pay a share of arbitration costs, demonstrates a clear bias against arbitration. Other cases decided by these courts do not find an agreement substantively unconscionable merely because it requires some payment by the weaker party. Particularly against the backdrop of the Supreme Court's access to courts jurisprudence, these decisions demonstrate a differential application of the standards of substantive unconscionability to arbitration and nonarbitration agreements.

The California state court cases involve the additional issue of preemption by the Federal Arbitration Act. The seminal case, *Armendariz*, held that mandatory arbitration agreements requiring arbitration of California Fair Employment and Housing Act<sup>73</sup> claims oblige an employer to pay all costs unique to arbitration.<sup>74</sup> According to the court, "when an employer imposes mandatory arbitration as a condition of employment, the arbitration agreement or arbitration process cannot generally require the employee to bear any *type* of expense that the employee would not be required to bear if he or she were free to bring the action in court."<sup>75</sup> The *Armendariz* holding, which predated the United States Supreme Court's decision in *Green Tree*, and

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70. *See id.* at 90-91.

71. Justices Ginsburg, Stevens, Souter, and Breyer disagreed with the majority on these points, focusing on the accessibility of arbitration to employees generally, and seemingly advocating a per se rule which would place the burden of proof on the employer.

72. *See supra* notes 59-62 and accompanying text.

73. CAL. GOV'T CODE §§ 12900-12909 (1992).

74. These consist of fees above court fees and arbitrator's fees.

75. *Armendariz*, 6 P.3d at 687 (emphasis in original).

which relied heavily on the now questionable D.C. Circuit Court decision of *Cole v. Burns International Security Service*,<sup>76</sup> has nonetheless been followed<sup>77</sup> and extended by the California state and federal courts to other statutory<sup>78</sup> and nonstatutory claims.<sup>79</sup>

The California Supreme Court recognizes that its holdings raise preemption issues but recently concluded in *Little v. Auto Stiegler, Inc.*,<sup>80</sup> that the Federal Arbitration Act and the United States Supreme Court's interpretation of it in *Green Tree* do not preempt the California approach. The California Supreme Court avoided *Green Tree's* interpretation of the Federal Arbitration Act by characterizing as *dicta* its holdings that employers may not impose prohibitive arbitration costs on employees and that whether costs are prohibitive must be determined case-by-case with the employee bearing the burden of proof.<sup>81</sup> The *Little* Court concluded,

Armendariz's cost-shifting requirement is not preempted by the FAA. It is not a barrier to the enforcement of arbitration agreements, nor does it improperly disfavor arbitration in comparison to other contract clauses. Rather, it is derived from

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76. See *supra* text accompanying notes 64-66.

77. See, e.g., *Circuit City Stores, Inc. v. Adams*, 279 F.3d 889, 894 (9th Cir. 2002) (holding that a fee allocation provision requiring employee to share arbitration costs was in itself sufficient to invalidate arbitration agreement).

78. See *Ting v. AT&T*, 182 F.Supp. 2d 902, 926-27 (N.D. Cal. 2002) (holding arbitration agreement between telephone service provider and customers invalid as limitation of consumer rights under California Consumer Legal Remedies Act, Cal. Civ. Code §§ 1751, 1781(a), 1783); *Mercuro v. Superior Court*, 116 Cal. Rptr. 2d 671, 680 (Cal. Ct. App. 2002) (applying *Armendariz* holding to claims alleging violation of Cal. Lab. Code §§ 230.8 and 970).

79. See *Boghos v. Lloyd's of London*, 1 Cal. Rptr. 3d 447 (Cal. Ct. App. 2003) (extending *Armendariz* holding to invalidate insurance policy arbitration clause which required claimant for disability benefits to split arbitration costs); *Little v. Auto Stiegler Inc.*, 63 P.3d 979 (Cal. 2003) (extending *Armendariz* holding to nonstatutory claims involving fundamental public policy, specifically judicially-created claim known as "Tameny claim" under which an employer may not terminate an at-will employee for reasons that would be contrary to public policy). Not all California courts have agreed. See, e.g., *Swiderski v. Milberg, Weiss, Bershad, Hynes & Lerach, LLP*, 114 Cal. Rptr. 2d 513 (Cal. Ct. App. 2001) (declining to extend *Armendariz* to nonstatutory wrongful termination claim).

80. 63 P.3d 979 (2003).

81. *Id.*

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state contract law principles regarding the unavailability of certain public rights in the context of a contract of adhesion.<sup>82</sup>

The court's logic is flawed. Arbitration is simply an alternative method for resolving disputes and vindicating rights.<sup>83</sup> Agreeing to arbitrate rights clearly does not entail a waiver of those rights,<sup>84</sup> unless (perhaps), as *Green Tree* holds, costs render the arbitral forum inaccessible to a particular potential claimant. The per se approach of *Armendariz* and its progeny thus conflicts with the basic purpose of the Federal Arbitration Act, "to place arbitration agreements on the same footing as other contracts."<sup>85</sup> Under the rule of *Armendariz*, parties to an arbitration contract cannot, unlike parties to other types of contracts or parties to arbitration contracts in other jurisdictions, expect judicial enforcement of their contract. California courts treat arbitration agreements differently precisely because they are arbitration agreements, in direct contradiction of the Federal Arbitration Act. Despite the California Supreme Court's protestations to the contrary, the Federal Arbitration Act in fact preempts *Armendariz* and its progeny.

*B. Limitations of Damages Which May Be Awarded in Arbitration*

Case law is divided on the issue of whether prohibition or limitation of punitive damages in an arbitration agreement is enforceable. The United States Supreme Court has not specifically decided whether it is unconscionable to prohibit an arbitral award of punitive damages.<sup>86</sup> It has, however, indicated that the parties'

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82. *Id.* at 992.

83. *Green Tree* and other Supreme Court cases make this clear.

84. *Gilmer*, 500 U.S. at 26 ("[B]y agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum.") (quoting *Mitsubishi Motors Corp. v. Soler Chrysler- Plymouth, Inc.*, 473 U.S. 614, 628 (1985)).

85. *Id.* at 24.

86. See *PacificCare Health Sys., Inc. v. Book*, 538 U.S. 401 (2003) (explaining plaintiffs' argument that arbitration provisions, which prohibited punitive damages, impeded RICO claims for which treble damages were available, 18 U.S.C. § 1964(c); Supreme Court compelled arbitration, holding that arbitration agreement was ambiguous as to whether it contravened RICO, since treble

agreement as to punitive damages in an arbitration agreement is generally enforceable.<sup>87</sup> In accordance with that holding, the D.C.,<sup>88</sup> Seventh,<sup>89</sup> and Fifth Circuits,<sup>90</sup> as well as the federal district court in the Central District of California<sup>91</sup> and the Mississippi Supreme Court,<sup>92</sup> have ruled that agreements prohibiting or limiting the award of punitive damages in arbitration are enforceable. In contrast, state courts in Alabama,<sup>93</sup> California,<sup>94</sup>

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damages are considered “remedial” not punitive, and it was merely speculative to assume that arbitrator will interpret ambiguous provisions as contrary to RICO).

87. *See* *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 56-57 (1995).

88. *See* *Brown v. Dorsey & Whitney, LLP*, 267 F.Supp. 2d 61 (D.C. Cir. 2003) (holding prohibition of punitive damages not unconscionable).

89. *See* *Hawkins v. Aid Ass’n for Lutherans*, 338 F.3d 801 (7th Cir. 2003) (rejecting claim that prohibition on recovery of punitive damages in arbitration agreement rendered it unconscionable).

90. *See* *Inv. Partners, L.P. v. Glamour Shots Licensing, Inc.*, 298 F.3d 314, 318 n.1 (5th Cir. 2002) (“Provisions in arbitration agreements that prohibit punitive damages are generally enforceable.”).

91. *See* *Gatton v. T-Mobile USA, Inc.*, No. SAC 03-130 DOC. 2003 WL 21530185 (C.D. Cal. Apr. 18, 2003) (commenting on no support for the proposition that prohibition on punitive damages, standing alone, renders arbitration agreement unenforceable); *Lozano v. AT&T Wireless*, 216 F.Supp. 2d 1071 (C.D. Cal. 2002) (holding provision of arbitration clause waiving claims for punitives not substantively unconscionable; limit applied only to extent allowed by law).

92. *See* *Sanderson Farms, Inc. v. Gatlin*, 848 So. 2d 828, 854-55 (Miss. 2003) (holding mutual exclusion of recovery of punitive damages enforceable as according with “sound business sense” and not contradicting Mississippi public policy). An earlier decision of the Mississippi Supreme Court reached a contrary conclusion. *See* *East Ford, Inc. v. Taylor*, 826 So. 2d 709 (Miss. 2002) (holding limitation on punitive damages unconscionable).

93. *See, e.g.*, *Anderson v. Ashby*, No. 1011740, 2003 WL 21125998 (Ala. May 16, 2003) (limitation of punitive damages to 5 times economic loss for borrower unconscionable; no limit for lender) (See, J., dissenting); *Ex Parte Celtic Life Ins. Co.*, 834 So. 2d 766 (Ala. 2002) (holding arbitration clause prohibiting recovery of punitive damages unenforceable; insurance company waived clause and remainder of agreement enforced); *Ex parte Thicklin*, 824 So. 2d 723, 733-34 (Ala. 2002) (See, J., dissenting) (describing how it is against public policy for private parties to contract away liability for punitive damages; clause severed as per severance clause in arbitration agreement); *Cavalier Mfg., Inc. v. Jackson*, 823 So. 2d 1237 (Ala. 2001) (holding arbitration clause that forbids an arbitrator from awarding punitive damages is void as contrary to public policies of protecting citizens in legislatively prescribed actions from wrongful behavior and punishing wrongdoers; clause severed in accordance with severance provision in agreement).

94. *See, e.g.*, *Pardee Constr. Co. v. Superior Court*, 123 Cal. Rptr. 2d 288 (Cal. Ct. App. 2002) (holding limit on punitive damages unconscionable);

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Pennsylvania,<sup>95</sup> and West Virginia,<sup>96</sup> have ruled that limitation of punitive damages in arbitration agreements is unconscionable. The Ninth Circuit has reached a similar conclusion, but only with regard to limitation of punitive damages to which a party may be entitled by statute.<sup>97</sup>

For the most part, the state court decisions holding punitive damages limitations unconscionable will survive preemption challenges. These decisions will generally fall within Section 2 of the Federal Arbitration Act. Limits on punitive damages often involve some measure of procedural unconscionability, in that the drafter of the arbitration agreement has superior bargaining power and in some sense forces the terms upon a weaker party, such as a consumer or an employee. Since the threat of punitive damages serves the important public policies of deterring various sorts of antisocial behavior, prohibitions of punitive damages may also be substantively unconscionable.

In some instances, however, courts appear to use unconscionability principles differently in the context of arbitration than in other contexts, and in these cases preemption challenges should succeed under the rule of

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Adamany v. Superior Court, No. B156220, 2002 WL 1722412 (Cal. Ct. App. July 25, 2002) (holding limit on punitive damages unconscionable; court severed and enforced remainder of arbitration agreement).

95. *See, e.g.*, Carll v. Terminix Int'l Co., L.P., 793 A.2d 921, 923 (Pa. Super. Ct. 2002) (holding that arbitration agreement was unconscionable because it precluded arbitrator from awarding "special, incidental, consequential, exemplary or punitive damages").

96. *See, e.g.*, State *ex rel.* Dunlap v. Berger, 567 S.E.2d 265 (W. Va. 2002) (holding that arbitration agreement which prohibited punitive damages and use of class action was unenforceable as against West Virginia public policy; defendant may not shield itself through adhesive contracts from an important sanction provided by law for the public benefit).

97. *See* Ingle v. Circuit City Stores, Inc., 328 F.3d 1165 (9th Cir. 2003) (holding arbitration agreement unconscionable because, inter alia, it limited availability of punitive damages, proscribing available statutory remedies under 42 U.S.C. §§ 1981a and 2000e-5(g)(1)); *see also* Graham Oil Co. v. ARCO Prods. Co., 43 F.3d 1244 (9th Cir. 1994), *cert. denied*, 516 U.S. 907 (1995) (holding that clause prohibiting arbitrator from assessing punitive damages was invalid because it required plaintiff to surrender statutory remedies for alleged violations of the Petroleum Marketing Practices Act). Most circuit court decisions are to the contrary. *See* Anders v. Hometown Mortgage Servs., Inc., 346 F.3d 1024, 1030-31 (11th Cir. 2003); *see also* Hawkins v. Aid Ass'n for Lutherans, 338 F.3d 801, 807 (7th Cir. 2003); Bob Schultz Motors, Inc. v. Kawasaki Motors Corp., U.S.A., 334 F.3d 721, 726 (8th Cir. 2003); Larry's United Super, Inc. v. Werries, 253 F.3d 1083, 1086 (8th Cir. 2001).

*Doctor's Associates*.<sup>98</sup> For example, the Alabama Supreme Court in *Anderson v. Ashby*<sup>99</sup> found unconscionable an arbitration agreement's limitation of the consumer's punitive damages to five times economic loss. Under the Alabama Code, punitive damage awards may not exceed three times compensatory damages (or \$500,000, whichever is greater).<sup>100</sup> Alabama courts use a two-part test to assess unconscionability: a contract is unconscionable if (1) its terms are grossly favorable (2) to a party with overwhelming bargaining power.<sup>101</sup> Given the existence of punitive damages caps established by the Alabama legislature, and in particular the legislature's use of a multiplier, the contractual limit on punitive damages at issue in *Anderson* can hardly be termed "grossly" favorable to the drafter of the arbitration agreement, who would have enjoyed a comparable, or greater, advantage in a courtroom.<sup>102</sup> Similarly, the Alabama Supreme Court could not plausibly defend its ruling in *Anderson* on public policy grounds given the legislative cap.

The California decisions may be subject to similar criticisms. The California Civil Code limits punitive damages in certain circumstances. For example, punitive

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98. See *supra* note 26 and accompanying text.

99. No. 1011740, 2003 WL 21125998 (Ala. May 16, 2003) (See, J., concurring in the result in part, dissenting in part).

100. ALA. CODE § 6-11-21 (1975). There are statutory exceptions to this general rule for particular circumstances.

101. See, e.g., *Am. Gen. Fin., Inc. v. Branch*, 793 So.2d 738, 748 (Ala. 2000).

102. Other jurisdictions which have enacted similar tort reform measures regarding punitive damages would also face limitations on the use of the unconscionability doctrine. See ALASKA STAT. § 09.17.020 (Michie 2002) (3 times compensatory damages or \$500,000); see also COLO. REV. STAT. ANN. § 13-21-102 (West 1997) (no more than actual damages); FLA. STAT. ANN. § 768.73 (West 2003) (3 times compensatory damages or \$500,000, or in egregious circumstances, 4 times compensatory damages or \$2 million, with additional exception for specific intent to harm); IDAHO CODE § 6-1604 (Michie 2001) (3 times compensatory damages or \$250,000); KAN. STAT. ANN. § 60-3701 (1994) (annual gross income of defendant or \$5 million); MISS. CODE ANN. § 11-1-65 (2004) (sliding scale based on defendant's net worth; for example, no more than 4% of defendant's net worth for defendants with net worth of \$50 million or less); NEV. REV. STAT. 42.005 (1998) (3 times compensatory damages if compensatory damages are \$100,000 or more; \$300,000 if compensatory damages are less than \$100,000, with exceptions for specific circumstances); N.J. STAT. ANN. § 2A:15-5.14 (West 1987) (5 times compensatory damages or \$350,000); N.D. CENT. CODE § 32-03.2-11 (1991) (two times compensatory damages or \$250,000); VA. CODE ANN. § 8.01-38.1 (Michie 2001) (no more than \$350,000 against all defendants).

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damages may not be recovered against a health care provider.<sup>103</sup> In a case where a consumer is unfairly denied credit, punitive damages may not exceed \$10,000.<sup>104</sup> If the legislature may eliminate or limit punitive damages in certain situations, it may be difficult to sustain the argument that a private limitation of punitive damages is always harsh, oppressive, and grossly unfair.

In general, limitations of damages other than punitive damages in arbitration agreements have not been held to be unconscionable,<sup>105</sup> given the widespread acceptance of such contractual limitations.<sup>106</sup> In special circumstances, however, a limitation of damages may be unconscionable. For example, in *O'Donoghue v. Smythe, Cramer & Co.*,<sup>107</sup> the court ruled a home inspector's limitation of liability to \$265 in an arbitration agreement unconscionable since it precluded any meaningful remedy, given the costs of arbitration. Cases like *O'Donoghue* may also exemplify

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103. CAL. CIV. PROC. CODE § 425.13 (West 2004).

104. CAL. CIV. CODE § 1787.3 (West 1985).

105. See *Telecom Int'l Am., Ltd. v. AT & T Corp.*, 280 F.3d 175 (2d Cir. 2001) (holding that remedies for failure of goods are limited; exclusion of consequential damages permitted; no failure of essential purpose under UCC 2-719); see also *MRO Communications Inc. v. AT & T*, No. 98-16716, slip op. at 4 (9th Cir. Dec. 13, 1999) (limitation of damages clause); *Networktwo Communications Group, Inc. v. Spring Valley Mktg.*, No. 99-72913, 2003 WL 11197633 (E.D. Mich. Feb. 13, 2003); *Agri-Mark, Inc. v. Niro, Inc.*, 233 F.Supp. 2d 200 (D. Mass. 2002) (limitation of damages not unconscionable); *Best Vendors Co. v. Air Express, Inc.*, No. Civ. 00-2224, 2002 WL 31163039 (D. Minn. Sept. 23, 2002) (holding that provision prohibiting damages for termination was not unconscionable); *Sears Termite & Pest Control, Inc. v. Robinson*, No. 1020304, 2003 WL 21205646 (Ala. May 23, 2003) (limitation of consequential damages).

106. See RESTATEMENT (SECOND) OF CONTRACTS § 356 (1979); see also U.C.C., § 2-719. Section 2-719 provides: (1) Subject to the provisions of subsections (2) and (3) of this section and of the preceding section on liquidation and limitation of damages, (a) the agreement may provide for remedies in addition to or in substitution for those provided in this Article and may limit or alter the measure of damages recoverable under this Article, as by limiting the buyer's remedies to return of the goods and repayment of the price or to repair and replacement of non-conforming goods or parts; and (b) resort to a remedy as provided is optional unless the remedy is expressly agreed to be exclusive, in which case it is the sole remedy. (2) Where circumstances cause an exclusive or limited remedy to fail of its essential purpose, remedy may be had as provided in this Act. (3) Consequential damages may be limited or excluded unless the limitation or exclusion is unconscionable. Limitation of consequential damages for injury to the person in the case of consumer goods is prima facie unconscionable but limitation of damages where the loss is commercial is not.

107. No. 80453, 2002 WL 1454074 (Ohio Ct. App. July 3, 2002).

arbitration-specific uses of unconscionability. Limitations of remedy provisions may preclude a potential litigant from actually bringing an action in court, but that is not a sufficient ground for avoiding the limitation.

### C. *Forum Selection Clauses*

Forum selection clauses are presumptively valid under long-standing precedent.<sup>108</sup> Under the Supreme Court's test, a forum selection clause is enforceable unless:

- (1) [its] incorporation into the contract was the result of fraud, undue influence, or overweening bargaining power[;]
- (2) the selected forum is so "gravely difficult and inconvenient" that the complaining party will "for all practical purposes be deprived of its day in court[;]" or
- (3) [its] enforcement . . . would contravene a strong public policy of the forum in which the suit is brought, [declared by statute or judicial decision.]<sup>109</sup>

Most forum selection clauses pass this test.<sup>110</sup>

However, federal and state courts in California,<sup>111</sup> the federal circuit court in Hawaii,<sup>112</sup> the federal district courts

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108. *See, e.g.*, *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972).

109. *Id.* at 10.

110. *See Vimar Seguros y Reaseguros, S.A. v. M/V Sky Reefer*, 515 U.S. 528, 541, (1995) (enforcing arbitration forum selection clause in international bill of lading); *see also Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585, 595 (1991) (enforcing forum selection clause in consumer contract); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 518-20 (1974) (enforcing arbitration forum selection clause in securities fraud case); *Sec. Watch, Inc. v. Sentinel Sys., Inc.*, 176 F.3d 369 (6th Cir. 1999); *Outek Caribbean Distribs., Inc. v. Echo, Inc.*, 206 F.Supp. 2d 263 (D. P.R. 2002); *Dassero v. Edwards*, 190 F.Supp. 2d 544 (W.D.N.Y. 2002); *Gill v. Jim Walter Homes of La., Inc.*, 187 F.Supp. 2d 618 (W.D. La. 2002); *Benefit Ass'n Int'l., Inc. v. Mount Sinai Comprehensive Cancer Ctr.*, 816 So. 2d 164 (Fla. Dist. Ct. App. 2002) (finding no procedural unconscionability; no showing that arbitration in designated forum would be so gravely difficult and inconvenient that it would, for all practical purposes, deprive claimant of an effective forum); *Info Leasing Corp. v. Jaskot*, 784 N.E.2d 1192 (Ohio Ct. App. 2003).

111. *See Wilmot v. McNabb*, No. C-0203720-JF, 2003 WL 21512814 (N.D. Cal. July 2, 2003) (holding that forum selection clause which required weaker party to arbitrate in nondomiciliary forum was substantively unconscionable, but that it could be severed from arbitration agreement); *see also Comb v. PayPal, Inc.*, 218 F.Supp. 2d 1165, 1177 (N.D. Cal. 2002) (holding that although forum selection clauses are generally presumed prima facie valid, a forum selection clause unconscionable if "place or manner" in which arbitration is to occur is unreasonable taking into account "the respective circumstances of the parties"); *GMAC Commercial Fin. LLC v. Super. Ct.*, No. B166070, 2003 WL



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in Illinois<sup>113</sup> and Ohio,<sup>114</sup> and state courts in Kentucky,<sup>115</sup> Missouri,<sup>116</sup> and Montana<sup>117</sup> have ruled that forum selection clauses in arbitration agreements are unenforceable under

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21398319 (Cal. Ct. App. June 18, 2003) (stating that California courts will not enforce a forum selection clause where it will deprive plaintiff of benefits of a California statute that would otherwise govern) (Turner, J. dissenting, on basis that no evidence that forum selection clause adhesive or unconscionable or that selected forum would fail to apply law); *Stone v. Memberworks Inc.*, No. G030740, 2003 WL 21246771 (Cal. Ct. App. May 30, 2003) (holding that it was unconscionable to require California consumers to arbitrate in Connecticut); *Bolter v. Super. Ct.*, 104 Cal. Rptr. 2d 888 (Cal. Ct. App. 2001) (holding that an arbitration agreement requiring a weaker party to resolve disputes in a geographically distant state substantively unconscionable).

112. *See, e.g., Domingo v. Ameriquest Mortgage Co.*, No. 02-15232, 2003 WL 21675550, at \*1 (9th Cir. July 14, 2003) (holding that a forum selection clause requiring Hawaii employees to arbitrate claims against an employer in California “strongly supports a finding of unconscionability” since costs of travel and arbitration might exceed damages).

113. *See Plattner v. Edge Solutions Inc.*, No. 03 C 2646, 2003 WL 22859532, at \*5 (N.D. Ill. Dec. 2, 2003) (holding that a forum selection clause requiring an Illinois resident to arbitrate in Suffolk County, New York was unconscionable solely on substantive grounds).

114. *Hagedorn v. Veritas Software Corp.*, 250 F.Supp. 2d 857, 862 (S.D. Ohio 2002) (holding that a forum selection clause requiring a life-long Ohio resident to arbitrate in San Francisco was unconscionable). *But see Lindsey v. Sinclair Broad. Group, Inc.*, No. 19903, 2003 WL 22972357 (Ohio Ct. App. Dec. 19, 2003) (holding that a forum selection clause in an arbitration agreement was not unconscionable where plaintiff failed to demonstrate financial inability to travel to the designated forum).

115. *See Wilder v. Absorption Corp.*, 107 S.W.3d 181, 185 (Ky. 2003) (holding that enforcement of the arbitration clause requiring arbitration in Washington, defendant’s principal place of business, was so unjust and inconvenient as to deprive Kentucky claimants of opportunity for hearing). The dissenter noted that Wilder was a businessman who sought to do business with a corporation knowing that its corporate headquarters were in Washington, freely signed an employment contract knowing that it required any contractual disputes to be resolved in Washington, and negotiated other terms of the contract, choosing to leave this term intact. *Id.* at 188-89 (Cooper, J., dissenting).

116. *See Swain v. Auto Servs., Inc.*, No. ED 82788, 2003 WL 22890022, at \*3-4 (Mo. Ct. App. Dec. 3, 2003) (holding that an agreement to arbitrate was enforceable, because unconscionable forum selection clause was separable from the general agreement to arbitrate). *But see High Life Sales, Co. v. Brown-Forman Corp.*, 823 S.W.2d 493, 497 (Mo. 1992) (“By this opinion, we join the better-reasoned majority rule and will enforce [forum selection] clauses . . .”).

117. *See Keystone, Inc. v. Triad Sys. Corp.*, 971 P.2d 1240, 1245-46 (Mont. 1998) (holding a forum selection clause void as against public policy expressed in Montana statutes, where a seller and installer of a computer system moved to compel arbitration in California in accordance with a forum selection clause in an arbitration agreement).

Section 2 of the Federal Arbitration Act because they are unconscionable. These decisions are likely preempted under the Federal Arbitration Act since they generally appear to treat forum selection clauses in arbitration agreements differently than in nonarbitration agreements. For example, California courts have recently enforced forum selection clauses against a policyholder suing in California whose policy specified that any lawsuit would be heard in an Ontario, Canada court,<sup>118</sup> against a consumer protection organization suing on behalf of California consumers whose contracts specified New Jersey as the forum,<sup>119</sup> and against a California former employee whose stock options agreement specified that any disputes would be resolved in the courts of Hamburg, Germany.<sup>120</sup> The fact that the contracts were adhesive was irrelevant according to the decisions.<sup>121</sup> Because these same courts reach a different conclusion for arbitration agreements, finding those agreements unconscionable as a result of a forum selection clause, those decisions are preempted by the Federal Arbitration Act.<sup>122</sup>

The Montana case requires a different analysis. In *Keystone, Inc. v. Triad Systems Corp.*,<sup>123</sup> the Montana

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118. *Shepherd v. Dominion of Can. Gen. Ins. Co.*, No. D039718, 2003 WL 21388251, at \*10 (Cal. Ct. App. June 17, 2003).

119. *Net2Phone, Inc. v. Super. Ct.*, 135 Cal. Rptr. 2d 149, 153 (Cal. Ct. App. 2003) (“The fact that the forum selection clause may have been a ‘take it or leave it’ proposition, and not vigorously ‘bargained for’ as Consumer Cause contends, does not make the clause unenforceable.”).

120. *Intershop Communications v. Super. Ct.*, 127 Cal. Rptr. 2d 847 (Cal. Ct. App. 2002) (“A forum selection clause within an adhesion contract will be enforced ‘as long as the clause provided adequate notice to the [party] that he was agreeing to the jurisdiction cited in the contract.’”).

121. *See Shepherd*, 2003 WL 21388251 at \*7 (noting that voluntary forum selection clauses do not offend due process); *Net2Phone*, 135 Cal. Rptr. 2d at 152 (noting that entering a contract voluntarily makes a forum selection clause valid); *Intershop*, 127 Cal. Rptr. 2d at 855 (holding that adhesion contracts are, nonetheless, valid and existing contracts.).

122. As the United States Supreme Court stated in *Perry v. Thomas*: “A court may not, then, in assessing the rights of litigants to enforce an arbitration agreement, construe that agreement in a manner different from that in which it otherwise construes nonarbitration agreements under state law.” 482 U.S. 483, 493 n.9 (1996). *See also Doctor’s Assocs., Inc. v. Casarotto*, 517 U.S. 681, 687 n.3 (1996) (citing *Perry*, 482 U.S. at 493 n.9) (holding that a court may not “rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable, for this would enable the court to effect what . . . the state legislature cannot.”).

123. 971 P.2d 1240 (Mont. 1998)

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Supreme Court found a contract provision calling for arbitration of any disputes in California invalid as violating Montana Code §§ 28-2-708, which provides:

Every stipulation or condition in a contract by which any party thereto is restricted from enforcing his rights under the contract by the usual proceedings in the ordinary tribunals . . . is void. This section does not affect the validity of an agreement enforceable under Title 27, Chapter 5.<sup>124</sup>

Title 27, Chapter 5 of the Montana Code Annotated includes the Montana Uniform Arbitration Act. In pertinent part, it provides: “No agreement concerning venue involving a resident of this state is valid unless the agreement requires that arbitration occur within the state of Montana. This requirement may only be waived upon the advice of counsel as evidenced by counsel’s signature thereto.”<sup>125</sup>

The court found that § 28-2-708 protects Montana residents from having to litigate outside of Montana. Section 27-5-323 provides the same protection for Montana residents who have agreed to arbitrate, in the absence of waiver made upon the advice of counsel. The court accordingly held the forum selection clause in the arbitration agreement void because it violated Montana law. The Federal Arbitration Act did not preempt Montana’s statutory law, since sections 28-2-708 and 27-5-323, respectively, articulate the same rules for contracts generally and arbitration agreements. In short, Montana law does not distinguish between forum selection clauses which are part of contracts generally, and forum selection clauses found in agreements to arbitrate. The court relied on Section 2 of the Federal Arbitration Act, which permits judicial invalidation of an arbitration agreement “upon such grounds as exist at law or in equity for the revocation of any contract,”<sup>126</sup> and on the Supreme Court’s decision in *Doctor’s Associates*, which clarified the scope of Federal Arbitration Act preemption:

Courts may not . . . invalidate arbitration agreements under state laws applicable *only* to arbitration provisions. By enacting §§ 2, we have several times said, Congress precluded States from singling

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124. MONT. CODE ANN. § 28-2-708 (2003).

125. MONT. CODE ANN. § 27-5-323 (2003).

126. 9 U.S.C. § 2 (2000).

out arbitration provisions for suspect status, requiring instead that such provisions be placed ‘upon the same footing as other contracts.’<sup>127</sup>

The Montana court found further that its decision was consistent with the Federal Arbitration Act because the parties’ obligation to arbitrate was enforced; only the forum selection clause was invalidated, and such a clause would have been invalidated in the context of litigation as well.

#### D. Confidentiality

Many arbitration agreements provide that the arbitration proceedings and the award must be kept confidential. The majority of courts have held these provisions unconscionable.<sup>128</sup> Only a few courts have found

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127. 517 U.S. at 687-88 (citations omitted) (emphasis in original).

128. *Ting v. AT&T*, 319 F.3d 1126, 1151-52 (9th Cir. 2003) (holding that plaintiffs were unable to mitigate AT&T’s advantages inherent in being a repeat player as a result of confidentiality provision, and thus the provision was unconscionable), *cert. denied*, 124 S. Ct. 53 (2003); *Cole v. Burns Int’l. Sec. Servs.*, 105 F.3d 1465, 1476 (D.C. Cir. 1997) (finding confidentiality in arbitration awards unconscionable because secrecy favors companies, who as repeat participants have superior information about arbitrators and may prevent potential plaintiffs from establishing intentional misconduct or a pattern or practice of discrimination by particular companies; confidentiality also precludes deterrent effect of adverse findings); *Plaskett v. Bechtel Int’l, Inc.*, 243 F.Supp. 2d 334, 344-45 (D. Virgin Islands 2003) (holding that provisions requiring confidentiality or arbitration, preventing inclusion of the party’s name in arbitration award at the party’s unilateral option, and permitting closed hearings at the arbitrator’s discretion were unconscionable); *Lloyd v. Hovensa LLC.*, 243 F.Supp. 2d 346, 352 (D. Virgin Islands 2003) (finding that since the confidentiality provisions were collateral to the arbitration agreement, the provisions could be severed and the agreement enforced, even though the provisions were unconscionable to the extent they provided for confidentiality); *Torrance v. Aames Funding Corp.*, 242 F.Supp. 2d 862, 865 (D. Or. 2002) (finding confidentiality provisions unconscionable where the drafter was in a “vastly superior legal posture” and no rationale was given for the provisions); *Luna v. Household Fin. Corp. III*, 236 F.Supp. 2d 1166, 1180-81 (W.D. Wash. 2002) (holding that confidentiality provisions advantage repeat participants and are thus unconscionable); *Acorn v. Household Int’l, Inc.*, 211 F.Supp. 2d 1160, 1172 (N.D. Cal. 2002) (finding confidentiality provisions unconscionable because they affect outcomes of arbitrations and favor defendant/drafter); *cf. Kloss v. Edward D. Jones & Co.*, 54 P.3d 1, 8 (Mont. 2002) (providing guidance to future litigants by listing this question as relevant: “Are arbitration proceedings shrouded in secrecy so as to conceal illegal, oppressive or wrongful business practices?”), *cert denied*, 538 U.S. 956 (2003).

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otherwise.<sup>129</sup> Despite their facial neutrality, these provisions favor the drafter of arbitration agreements. The drafter is likely a repeat participant in arbitrations, and so has advantages in arbitrator selection and case presentation.<sup>130</sup> One-time participants in arbitration have no hope of countering these advantages if information about past arbitrations is kept secret. The one-sided advantages of confidentiality clauses thus create substantive unconscionability.

Confidentiality of arbitration proceedings and awards has no exact analogue for purposes of assessing whether judicial responses to the issue vary from other contexts. Perhaps the closest analogy is confidentiality of settlement agreements and negotiations. Confidentiality of settlement negotiations and agreements is supported by strong public policies and grounded in long tradition.<sup>131</sup> Both settlement

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129. See *Ortiz v. Winona Mem. Hosp.*, No. 1:02-CV-1975-JDT-TAB, 2003 WL 21696524, at \*3 (S.D. Ind. 2003) (finding confidentiality rules not unconscionable; if they were, however, they could be severed as collateral to main purpose of arbitration agreements); see also *Hutcherson v. Sears Roebuck & Co.*, 793 N.E.2d 886 (Ill. App. Ct. 2003).

130. See generally Alleyne, *supra* note 7, at 426 (arguing that employers track arbitrator records and will dominate selection process); Lisa B. Bingham, *Employment Arbitration: The Repeat Player Effect*, 1 EMPLOYEE RTS. & EMPL. POL'Y J. 189, 213 (1997); Julius G. Getman, *Labor Arbitration and Dispute Resolution*, 88 YALE L.J. 916, 936; Robert A. Gorman, *The Gilmer Decision and the Private Arbitration of Public Law Disputes*, 1995 U. ILL. L. REV. 635, 656; Lewis Maltby, *Paradise Lost—How the Gilmer Court Lost the Opportunity for Alternative Dispute Resolution to Improve Civil Rights*, 12 N.Y.L. SCH. J. HUM. RTS. 1, 4-5 (1994) (arguing that employees are disadvantaged vis-a-vis employers in determining whether a given arbitrator is truly neutral because employees lack financial resources to research an arbitrator's past decisions); Sternlight, *supra* note 7, at 685 (arguing that "one-shot players" such as employees and consumers are less able to make informed selections of arbitrators than "repeat-player" companies). Other possible advantages, not relevant here, include the ability to identify and settle meritorious cases and the potential incentives for arbitrators to satisfy repeat participants.

131. See *Goodyear Tire & Rubber Co. v. Chiles Power Supply, Inc.*, 332 F.3d 976, 980-81 (6th Cir. 2003); see also *Herrnreiter v. Chicago Hous. Auth.*, 281 F.3d 634, 636-37 (7th Cir. 2002) (holding that if parties request judicial interpretation and enforcement of confidential settlement agreement, then that agreement enters the record and becomes available to the public); *Jessup v. Luther*, 277 F.3d 926, 930 (7th Cir. 2002) (holding that settlement agreements contained in court files must be disclosed because "documents in judicial files are presumptively open to the public"); *Palmieri v. New York*, 779 F.2d 861, 865 (2d Cir. 1985) (citing *In re Franklin Nat'l Bank*, 92 F.R.D. 468, 472 (E.D.N.Y. 1981)) (stating that "[s]ecrecy of settlement terms . . . is a well-established American litigation practice").

and arbitration are a means of alternative dispute resolution; like arbitration, settlement may occur without judicial involvement. Both are supported by strong public policies favoring negotiated, nonjudicial resolution of disputes. Both are viewed as more efficient and more cost-effective than litigation. Both lessen the burdens on an overtaxed judiciary. Additionally, confidentiality in both arbitration and settlement presents problems for potential claimants. Institutions which enter confidential settlements, like institutions which resolve disputes through confidential arbitration, are able to minimize information available to potential claimants. Both potential litigants and potential participants in arbitration will consequently be impeded in their efforts to build a case, particularly if they attempt to prove intentional misconduct or a pattern and practice of misconduct.

There are, of course, differences between settlement and arbitration which may provide additional justifications for confidentiality in settlements, not applicable to arbitration. Settlement negotiations are intended to obviate the need for trial, while arbitration is intended from the outset as a replacement for trial. Admissibility of information from failed negotiations would create a significant disincentive to settlement efforts. However, the analogy between confidentiality of settlement and arbitration awards is close. The fact that judges find confidentiality requirements to be harsh, oppressive, and ultimately unenforceable in the context of arbitration agreements but perfectly acceptable in the context of settlement agreements once again suggests a bias against arbitration.

#### IV. ANECDOTAL EVIDENCE

The most notable example of modern judicial hostility to arbitration took place in connection with the case of *Doctor's Associates*.<sup>132</sup> In that case, the United States Supreme Court reversed and remanded the Montana Supreme Court's decision that an arbitration clause in a franchise agreement was unenforceable under Montana law. On remand, Justices Trieweler and Hunt of the

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132. See *Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 687 (1996) (requiring states to treat arbitration provisions as any other contract).

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Montana Supreme Court refused to sign the order staying the case pending arbitration. The justices stated, “[w]e cannot in good conscience be an instrument of a policy which is as legally unfounded, socially detrimental, and philosophically misguided as the U.S. Supreme Court’s decision in this and other cases which interpret and apply the Federal Arbitration Act.”<sup>133</sup> In his special concurrence to the Montana Supreme Court’s original opinion, Justice Trieweiler criticized “federal judges who consider forced arbitration as the panacea for their ‘heavy case loads’ and who consider the reluctance of state courts to buy into the arbitration program as a sign of intellectual inadequacy.”<sup>134</sup> He enumerated the rules and procedures developed over a century of Montana jurisprudence to ensure access to fair dispute resolution.<sup>135</sup> He recognized that “[t]he procedures we have established, and the laws we have enacted, are either inapplicable or unenforceable in the process we refer to as arbitration.”<sup>136</sup> In sum, Justice Trieweiler criticizes federal judiciary for arrogance, preoccupation with their own caseload, and disregard for the difficulties forced on unwilling participants to mandatory arbitration.<sup>137</sup> In a subsequent Montana Supreme Court decision, Justice Nelson opined that the case law dealing with arbitration compels the conclusion that large corporations have effectively privatized a segment of the civil justice system by including mandatory binding arbitration clauses in standard form contracts, noting the “horror stories of corporate abuse of ordinary citizens and small business people.”<sup>138</sup>

## V. APPROPRIATE JUDICIAL USES OF UNCONSCIONABILITY

The chief values of unconscionability are its flexibility and adaptability to a variety of situations. There are good and important reasons that it has remained largely undefined in the case law and in various statutes, left

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133. Richard C. Reuben, *Western Showdown: Two Montana Judges Buck the U.S. Supreme Court*, A.B.A. J., Oct. 1996, at 16.

134. *Casarotto v. Lombardi*, 886 P.2d 931, 939 (Mont. 1994).

135. *See id.* at 939-40.

136. *Id.* at 940.

137. *See id.*

138. *Kloss v. Edward D. Jones & Co.*, 54 P.3d 1, 14 (Mont. 2002) (Nelson, J., concurring), *cert denied*, 538 U.S. 956 (2003).

instead to be given content by the workings of judicial intelligence in response to specific cases as they arise. What must be avoided under Section 2 of the Federal Arbitration Act and the rule of *Doctor's Associates* are arbitration-specific applications of unconscionability doctrine. Since some of the failures described above in Section III of this article are fairly egregious, some of the suggestions made here are fairly obvious. First, judges should be careful to articulate the general principles which animate the doctrine of unconscionability, including one-sidedness, oppression, unfairness, and harshness, and to identify general features of unconscionable contracts, such as hidden terms, ambiguous terms, unequal bargaining power, and so on. In holding an arbitration agreement unconscionable, judges must demonstrate how the agreement exemplifies these general characteristics and features of unconscionable contracts. Second, conclusions that a particular arbitration agreement or provision is unconscionable should be assessed against other decisions in the jurisdiction. The holdings that forum selection clauses in arbitration agreements are unconscionable, for example, cannot stand in comparison to holdings in other contract cases which universally reach the opposite conclusion. Such decisions must simply be avoided as contrary to the Federal Arbitration Act's prescription in Section 2. Third, it may often be possible to hold an arbitration agreement unconscionable without creating an arbitration-specific rule which violates Section 2 of the Federal Arbitration Act. For example, many of the decisions discussed in Section III of this article dealing with forum selection clauses in arbitration agreements involved multiple findings of unconscionability. In other words, it was unnecessary to assert the preemptable arbitration-specific ground in order to reach the result. Several other unconscionable features of the arbitration agreement would have justified the holding, avoiding the creation of invalid bases for a finding of unconscionability.

#### CONCLUSION

There has been a resurgence in the use of the doctrine of unconscionability over the years as the use of arbitration has increased. Despite legislative pronouncements and the strong national policy favoring arbitration, evidence points



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to continuing judicial hostility to arbitration. The expansion of unconscionability doctrine, through which judges avoid enforcing arbitration agreements, is, in many instances, preempted by the Federal Arbitration Act. Unconscionability as it is used with regard to any contract may invalidate an arbitration agreement under Section 2 of the Federal Arbitration Act. However, where courts find agreements regarding costs, forum selection, punitive damages, and confidentiality unconscionable only in the context of arbitration, they exceed the permissible scope of Section 2 and are subject to preemption. Restrained judicial application of unconscionability doctrine will avoid preemption problems while permitting judges to invalidate arbitration agreements in appropriate cases.