No. 1022063
IN THE SUPREME COURT OF ALABAMA

GARY LEEMAN AND KATHRYN LEEMAN,

Appellants,

v.

COOK'S PEST CONTROL, INC., a corporation; *et al*,

Appellees.

After an Order by the Circuit Court of Jefferson County, Civil Action No. CV-02-4976, Granting Appellee's Motion to Compel Arbitration and Stay Proceedings, The Honorable Joseph A. Boohaker

APPELLANTS' OPENING BRIEF

ORAL ARGUMENT REQUESTED

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STATEMENT REGARDING ORAL ARGUMENT

Appellants respectfully suggest that oral argument is appropriate and desirable in this case. The case poses important issues of public policy, and presents this Court with a well developed evidentiary record on the subject of arbitration costs in a consumer setting. While no one in this case disputes that the Federal Arbitration Act embodies a policy favoring the enforcement of valid arbitration agreements, this case raises the issue of whether generally applicable principles of Alabama contract law place an outer limit on the use of arbitration clauses in contracts of adhesion that are proven to impose enormous arbitration fees on persons bringing modest consumer claims.

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STATEMENT OF JURISDICTION

This Court has jurisdiction over this appeal under Ala. R. App. P. 4(d), "Appeals from Orders Granting or Denying Motions to Compel Arbitration." That rule provides that "an order granting or denying a motion to compel arbitration is appealable as a matter of right, and any appeal from such an order must be taken within 42 days. . . ."

The Circuit Court granted Appellee Cook's Pest Control's Motion to Compel Arbitration on July 23, 2003, and Appellants filed this appeal forty (40) days later on September 2, 2003. This appeal is thus timely and appropriate under Rule 4(d).

STATEMENT OF THE CASE

This case was originally filed in the Circuit Court of Jefferson County on August 19, 2002. In their Complaint, Gary and Kathryn Leeman ("the Leemans") alleged that defendants had failed to provide termite extermination services required by statute and the parties' contract, that defendants had negligently and recklessly failed to properly supervise inspectors and exterminators, and various other state and contract law violations related to termite inspection, prevention and eradication. Clerk's Record ("C") 1. The Complaint was filed against Cook's Pest Control, the extermination company, as well as three individuals: James Aycock, President of Cook's Pest Control; Harold R. Pinckard, a Certified Pest Operator, and Dennis Duggan, the Pest Control Representative from Cook's who signed the contract with the Leemans.

On September 19, 2002, Defendants ("Cook's") filed a Motion to Compel Arbitration and Stay Proceedings. C15. Cook's claimed that under the terms of the Leemans' contract, which they signed in May 2000, the Leemans claims could only be brought in arbitration before the American Arbitration Association ("AAA").

On Nov. 18, 2002, the Leemans filed a request for an extension of time in order to permit discovery regarding Cook's Motion to Compel. C46. Specifically, the Leemans asked to be able to gather evidence relating to the cost of prior arbitration proceedings against Cook's and other pest control companies. C43.

On June 4, 2003, Cook's filed a Supplemental Motion to Compel Arbitration. C59.[1]

On June 6, 2003, the Leemans filed their First Opposition to Defendants' Motion to Compel Arbitration. C79. In this Opposition, the Leemans argued that 1) the arbitration clause in the contract between Cook's and the Leemans was unconscionable and unenforceable because of its breadth, imposition of prohibitive costs, and lack of meaningful choice; and 2) the three individuals listed as defendants in the complaint were not parties to the contract and thus could not compel arbitration. C79. The Leemans' Opposition included extensive exhibits relating to the cost of arbitration. C86.

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[1] Cook's also filed a Supplement to its Motion to Compel Arbitration, on June 4, 2003. However, that document focused exclusively on whether the Termite Control Contract was a contract in interstate commerce, a question that is not at issue in this appeal.

On June 17, 2003, Cook's filed a Reply to Plaintiffs' Opposition, C534, arguing that its arbitration clause was not unconscionable under Alabama law and that the clause could be invoked by the individual defendants, as the Leemans' claims against these individuals were "intertwined" with those against the company.

On June 20, 2003, the Leemans filed a Supplemental Opposition to the Motion to Compel. C602.

On June 30, Cook's filed a Reply to Plaintiffs' Supplemental Opposition. C644.

On July 1, 2003, the Leemans filed a Second Supplemental Opposition to the Motion to Compel Arbitration. C649. The Leemans attached trial exhibits from *Leonard v. Terminix*, 854 So.2d 529 (Ala. 2002), to this Supplemental Opposition, and asked the court to take judicial notice of these documents. C650.

On July 23, 2003, the Circuit Court entered its order granting Cook's Motion to Compel Arbitration. C794. The court held that the non-signatory defendants may enforce the arbitration clause so long as the clause is valid, and that the clause is not unconscionable because the cost of arbitration is not high enough in relation to the potential

recovery in arbitration to make the cost truly prohibitive.

STATEMENT OF THE ISSUE

1. Where the party with greater economic power drafts an arbitration clause that is imposed upon a consumer without the possibility of negotiation, and all the other companies in that field require consumers to sign similar arbitration provisions, and the arbitration provision has an exceptionally broad scope, is the arbitration provision unconscionable when it requires consumers to pay undisclosed arbitration forum fees in the range of $12,000 to $16,000 to obtain any remedy for wrongs done to the consumers?

STATEMENT OF THE FACTS

On May 15, 2000, Gary Leeman, a public school principal, and his wife Kathryn, an elementary school teacher, entered into a Subterranean Termite Control Agreement Service Order and Retreatment Guarantee (the "Termite Control Contract") with Cook's Pest Control to cover termite inspections in their new home. C574. The Termite Control Contract was part of a packet of materials that the Leemans were given to sign at the closing on their home. C578.

No Cook's representative was present at the closing.

C564. Instead, the Contract had the pretyped signature of Dennis Duggan, identified as "Cook's Pest Control Representative." C38. The Contract contained an extremely broad arbitration provision stating that "any dispute, controversy or claim arising out of or relating to the agreement and guarantee or the breach thereof, or arising out of any prior or future dealings between Cook's and customer, shall be settled in arbitration . . . ." C17. The arbitration clause further stated that arbitration would proceed in accordance with the Commercial Rules of the American Arbitration Association ("AAA"). *Id.*

The Leemans believed that their contract with Cook's covered all termite inspection, annual reinspection and remediation. C576-77. With this understanding, they renewed the contract the following year. C583. However, in late 2001, just before Christmas, when Cook's arrived to do a retreatment of their property, the Leemans learned that their home was infested with termites. C585-86.

Because they believed that Cook's had not lived up to its agreement to protect their home from termite infestation, the Leemans brought the present suit in Circuit Court in Jefferson County on August 19, 2002. In their Complaint, the Leemans

alleged that their home had not been adequately inspected and treated against termite infestation, and that Cook's had misrepresented that it would adequately inspect and treat the property. C5-6. The Leemans' specific claims against Cook's in the Complaint included: fraud, breach of warranty, negligence, breach of contract, and unjust enrichment. C9-12. The Leemans asked for unspecified damages including compensatory, incidental, consequential and punitive damages, as well as equitable relief against Cook's. C12. Damages were unspecified because the Leemans could not quantify the amount of damage that had been done to their home, or the extent of other compensable damage. C563, 592.

Cook's, on behalf of all defendants, responded to the Leemans' Complaint by filing a Motion to Compel Arbitration and Stay Proceedings. C15. Cook's stated that because Kathryn Leeman had signed the Termite Control Contract, and because the Leemans received the benefit of the contract in the form of the termite retreatment on December 7, 2001, the Leemans were bound to the contract and the arbitration clause found therein. C30-31.

The Leemans opposed arbitration of their claims against Cook's. They argued that the clause was the product of

overwhelming bargaining power, and that it contained two major terms that were grossly favorable to Cook's: first, the breadth of the clause, which purported to cover all prior and future claims against the company, C80-81; and second, the excessive cost of arbitration under the AAA Commercial Rules. C81.

Facts Relating to Overwhelming Bargaining Power

The Leemans were presented with a contract as part of a stack of closing documents for their new home. No one pointed out the arbitration clause to the Leemans. There was no Cook's representative present to answer any questions they may have had about the contract or the arbitration clause. C564. No one explained to them the potential costs that they would have to incur if they brought future claims to arbitration under the AAA Commercial Rules. In fact, Cook's admits that it does not advise its employees how to answer questions about the arbitration clause. C421-422 ("[W]e are not the neighborhood advice givers . . . as far as how to interpret contracts. I think people can understand the terms themselves. And if they need more information about it, there are other sources to get that information than from us.").

Even if they had attempted to investigate the matter, the Leemans had no way to learn the full magnitude of costs of AAA arbitration. As this Statement of Facts will discuss in more detail below, the record contains extensive evidence of the costs imposed on consumers who brought other claims against Cook's to arbitration. In those other cases, AAA not only charged filing fees (money that goes to the AAA itself to administer cases and perform the types of functions handled by court clerks), but also charged very significant arbitrators' fees (money that goes to the for-profit AAA arbitrators themselves).[2] The hourly and/or daily rates of arbitrators are not posted on the AAA's website or otherwise made available to consumers such as the Leemans; indeed, the only way that a consumer can learn the magnitude of the costs that

[2] This fact is also widely recognized in the case law. *See, e.g., Phillips v. Associates Home Equity Services, Inc.*, 179 F. Supp.2d 840, 846 (N.D. Ill. 2001) ("Furthermore, the initial filing fee is far from the only cost involved in the arbitration. The AAA's Commercial Rules provide that the arbitrator's fees (which range from $750 to $5,000 per day, with an average of $1,800 per day in the Chicago area), travel expenses, rental of a hearing room, and other costs are borne equally by the parties...."); *Camacho v. Holiday Homes, Inc.*, 167 F. Supp.2d 892, 897 (W.D. Va. 2001) ("However, even if the initial $2,000 in administrative fees were waived or deferred, Mrs. Camacho has demonstrated that the additional costs of the arbitration process itself amount to an insurmountable financial burden to her.").

are likely to be imposed is to use the discovery process in litigation such as this to uncover what costs have been imposed upon other consumers in the past.

The record establishes that at the time the Leemans signed the Termite Control Contract, nearly every other pest control company in Alabama also required its consumers to agree to mandatory, binding, pre-dispute arbitration. The record includes standard form contracts, complete with arbitration provisions, from Orkin Exterminating Company, Vulcan Termite, Inc., Terminix Int'l, American Pest Control, and Alapestco. C703-735.[3] Cook's acknowledged in its interrogatory answers in this case that "Cook's is not aware of any particular competitor that does not include a provision for arbitration in its customer agreements, . . ." C476. Cook's further stated that "Cook's is aware that many pest control operators in the State of Alabama do require its [sic] customers to agree to submit disputes to arbitration, . . ."

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[3] This Court already has notice of the fact that still other pest control companies also impose arbitration clauses upon their customers. This Court recently heard cases against Sears Termite & Pest Control and Security Pest Control that revolved around the arbitration clauses in those companies' standard contracts. *See Sears Termite & Pest Control, Inc. v. Robinson*, 2003 WL 21205646 (Ala. May 23, 2003); *Bowen v. Security Pest Control, Inc.*, 2003 WL 22272915 (Ala. Oct. 3, 2003).

Id.

The record establishes that the Leemans had no input into negotiating the terms of the Termite Control Contract, which was a standard form contract drafted by Cook's. Cook's General Counsel, Donald Sides, said in the company's Rule 30(b)(6) deposition testimony below that Cook's arbitration clauses "were part of the standard contract" used by Cook's, rather than being individually negotiated agreements. C342. In its answers to the Leemans' interrogatories, Cook's answered the question "Can a customer negotiate removal of the arbitration clause?" with the statement, "No, not as a general rule." C476. In answer to the next question, "Would this Defendant transact business with a customer who refused to sign the arbitration clause?" Cook's stated simply, "No." *Id.*[4]

The Factual Record on Costs of

[4] This statement echoes a similar statement made by one of Cook's attorneys during the oral argument before this Court in *Cook's Pest Control v. Rebar*, Ala. Sup. Ct. No. 1010897, *opinion published at* 852 So.2d 730. During that argument, Cook's attorney stated at one point in regards to the Cook's standard contract that "[T]he consumer is not in a bargaining position to alter the terms and conditions. They make the payment, they accept what is offered to them. And if they don't like it, they go down the street." The relevant portion of this Transcript is attached as an Appendix.

Arbitration under Cook's Arbitration Clause

1. The AAA's Commercial Rules Govern this Dispute.

The undisputed record in this case establishes that the AAA's Commercial Rules apply to this dispute, not the less expensive AAA Consumer Rules. First, the arbitration clause itself specifies that disputes will be resolved under the AAA Commercial Rules. C38. Furthermore, as noted above, the Leemans have sought equitable and injunctive relief for their claims, a category of relief to which they are entitled under Alabama law should they prevail upon their claims.[5] In addition, the Leemans were not able to specify a dollar figure for their damages claims. Accordingly, the record establishes that these claims fall within the AAA's Commercial Rules.

In an e-mail to the Leemans' counsel that was put into evidence in this case, a AAA representative named Margaret Wilson of the AAA stated that any consumer bringing a claim in arbitration for unspecified damages or injunctive relief is automatically placed under the Commercial Arbitration Rules.

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[5] Equitable relief is often appropriate in termite cases where facts establish that termite service providers have never applied the minimum chemical treatments required by law in Alabama. *See* Ala. Admin. Code 80-10-9-.18. Hence, specific performance injunctions are often warranted, and such remedies may require ongoing court supervision.

C329.[6]

The Commercial Rules state that the consumer must pay a nonrefundable filing fee of $3250 and a nonrefundable administrative fee. C329.[7] The administrative fee, called a "Case Service Fee," was $750 in 2001, when the Leemans originally filed this claim; it has now gone up to $1250. Compare C166 with American Arbitration Association, Commercial Arbitration Rules and Mediation Procedures, available at http://www.adr.org/index2.1.jsp?JSPssid=15747 (last visited Nov. 6, 2003).

Furthermore, Ms. Wilson explained, "The consumer must also deposit one-half of the arbitrator's compensation. This deposit is used to pay the arbitrator. This deposit is

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[6] This fact is also recognized in the case law. *See, e.g., Luna v. Household Fin. Corp.*, 236 F. Supp.2d 1161, 1182, n. 7 (W.D. Wash. 2002) ("Because Plaintiffs seek equitable relief, the AAA consumer dispute provisions likely would not apply."). The reason that claims for any kind of injunctive relief must always be handled under AAA's Commercial Rules is that proceedings under AAA's Consumer Rules are sharply limited. Under the Consumer Rules, consumer claimants are not permitted to take any discovery whatsoever, to participate in a live hearing, or to file any briefs with the arbitrator. Under these circumstances, it is hardly surprising that persons with claims similar to the Leemans' are required to bring those claims under the Commercial Rules.

[7] As noted below, consumers bringing similar claims under the Commercial Rules in the *Porter* and *Wunderlich* cases were required to pay precisely these initial fees.

refunded if not used." C329.[8]

2. Evidence of Arbitration Costs Imposed Upon Consumers in Other Cases Against Cook's and Similar Pest Control Companies.

The record contains undisputed evidence of the arbitration fees that were imposed upon consumers in five different cases brought against pest control companies under AAA's Commercial Rules. In each case, the consumers advanced claims that were nearly identical to the Leemans'. C326. In two of these cases, the defendant was Cook's Pest Control, the same defendant as in this case. Only one of these five cases, *Porter v. Cook's Pest Control*, actually went all the way through the AAA process to an arbitrator award, C475; the others all settled after proceeding in arbitration for some time.[9] As a result, the costs reflected in four of the five cases understate the arbitration costs that one would expect

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[8] Arbitrator compensation accrues for all time spent by the arbitrator, including conducting discovery and other pretrial hearings, research, and the like. Arbitrators do not just bill for time spent in a hearing on the merits, as is commonly believed.

[9] The record evidence cited is Cook's answer to Interrogatory number nine, dated February 2003. After the record below was filed, the *Wunderlich v. Cook's* matter was resolved through AAA arbitration in May 2003. A modest recovery was obtained by Ms. Wunderlich in that case.

in a case that proceeds all the way through to an award.

In the *Porter* case, the plaintiffs were obligated to pay $12,950 in arbitration costs to the AAA in order to have their claims heard. C225-28. The Porter's arbitration costs broke down as follows:

- Initial Administration Fee: $3250
- Case Service Fee: $ 750
- Mediator Compensation (Plaintiff's share of 2 days hearing, 4 hours study at $1200/day) $1500
- Arbitrator Compensation (Plaintiff's share of 10 hours study and 4 days hearing at $850/day) $2450
- Arbitrator Compensation (Plaintiff's share of 5 days hearing, 5 days study at $850/day) $5000

Id. In the *Porter* case, the arbitrator ultimately entered an award for the consumers in the amount of $16,000, plus just over $4800 in reimbursement for their share of the arbitrator's fees and costs. C230-231. Under the arbitrator's order, the consumers had to pay out more than $8,000 in arbitration fees that were not to be reimbursed in order to recover $16,000.

In *Wunderlich v. Cook's Pest Control*, the only other case

ever brought against Cook's in arbitration, the consumer plaintiff's arbitration costs (half the total cost of arbitration) amounted to $13,750. C111-114. The Wunderlich's arbitration costs broke down as follows:

- Initial Administration Fee: $3200
- Case Service Fee: $ 750
- Mediator Compensation (Plaintiff's share of 2 days hearing, 4 hours study at $175/hour) $1750
- Arbitrator Compensation (Plaintiff's share of ½ day study and 1 day hearing at $1200/day) $900
- Arbitrator Compensation (Plaintiff's share of 12 hours study and 2 days hearing at $1200/day) $2100
- Arbitrator Compensation (Plaintiff's share of 2 days hearing, 12 hours study at $1200/day) $5000

The three other cases taken to arbitration by consumers against pest control companies other than Cook's are *Plummer v. Sears Termite & Pest Control, Inc.*, *Barnard v. Orkin Exterminating Co., Inc.*, and *Travers v. Terminix Int'l*. Although, as noted above, all three cases settled before an arbitration award was entered,

C168, the initial arbitration fees were similar. In *Plummer*, the plaintiffs paid $7425 in costs, including $4000 in initial costs and $3425 in additional arbitrator costs. C257. The *Plummer* case settled on the third day of the arbitration hearing. C168. In *Barnard*, Plaintiffs paid $11,500 altogether, including $4000 in initial costs, $7000 to cover four days of the arbitrator's study and hearing time, and $500 for the arbitrator's anticipated travel and hotel costs. C290, 292. The *Barnard* case settled prior to the commencement of a hearing. C168. And in *Travers*, plaintiffs paid $6425 in arbitration forum fees: $4000 in initial costs and an additional $2425 for two days of the arbitrator's study and hearing time. C320-21. The *Travers* case settled prior to commencement of a hearing. C168.[10]

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[10] That the costs under AAA's Commercial Rules are often so high should not come as a surprise – there is extensive public documentation of the fact that the AAA's Commercial Rules frequently impose extremely hefty costs upon individuals with modest claims. One recent report collected invoices from a number of AAA arbitrations that involved similar costs. *See* Public Citizen Congress Watch, *The Cost of Arbitration* (April 2002) at 6-7, available at http://www.citizen.org/documents/ACF110A.PDF (last visited Nov. 5, 2003)(in *Betzler v. Ryland Corp.*, a case involving alleged construction defects in a home, AAA invoices document that the homeowners were required to advance $7,563.75), at 8-15 (in *Paul v. Allred*, a case involving legal malpractice claims, the claimant dropped her case upon

In short, the initial Administrative and Case Service Fees in all five cases were $4,000. The average of additional costs (mostly arbitrators' fees) for the five cases was $6,560, and only two of these five cases ever went to the point of an evidentiary hearing.

The evidence also shows that if these five cases had been brought in the judicial system instead of arbitration, forum costs – that is, fees paid to a decisionmaking system in order to use that system – would be on average 51 times lower. C109. The *Porter* case, which was brought in a Circuit Court in Alabama before that court ordered parties to arbitrate, cost $211 to file. The *Wunderlich* case cost $229. The *Plummer*, *Barnard*, and *Travers* cases cost $221, 218, and $225.50, respectively. C109.

The record also shows that in *Morris v. Cook's Pest Control*, a consumer case against a pest control company with similar claims to those raised here, the court fees were about $300 altogether – $211 in initial filing fees,

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receiving AAA's latest invoice for $37,500, after she had already spent $17,762 on fees to AAA); at 16-18 (in *Malkanis v. #1 Custom Homes*, AAA billed homeowners $13,068.67 to litigate a claim that resulted in an award of $18,818.93).

and $88 in additional costs. C126.[11] Hence, the cost of trying a similar case (*Morris*) to a civil jury to a conclusion was $300, whereas the cost of bringing a similar case (*Porter*) in arbitration to a conclusion was nearly $13,000.

3. The Impossibility of Finding Counsel to Advance These Fees.

The record contains sworn testimony from a number of Alabama attorneys that they would not take on consumer cases against companies incorporating the AAA Commercial Rules into their contracts, because the high forum costs make these cases financially infeasible, and from several Alabama consumers who attempted to find attorneys to represent them in arbitration, but were unable to do so. C680-96. One attorney testified that "consumers may not be able to find anyone to help them with their claim and may well be discouraged from pursuing meritorious claims on their own because of the high filing fees in

[11] This fact is also consistent with the holdings of a number of courts. *See, e.g., Morrison v. Circuit City Stores, Inc.*, 317 F.3d 646 (6th Cir. 2003) ("Courts charge plaintiffs initial filing fees, but they do not charge extra for in-person hearings, discovery requests, routine motions, or written decisions, costs that are all common in the world of private arbitrators.").

arbitration and difficulty in obtaining counsel which regularly handles civil litigation." C689.

As noted above, there have been five cases against pest control companies raising allegations similar to those at issue here, that have proceeded to arbitration. The record establishes that all five of those cases were brought by the same counsel who represented the Leemans in the trial court here. The record contains unrebutted testimony that these counsel brought those cases not because it was economically justifiable to do so, but because it was the only way to establish an evidentiary record demonstrating the magnitude of the forum costs that consumers are required to bear in these types of cases. C652 ("Plaintiffs have built a record here, and their counsel have spent tens of thousands of dollars to build the record to show plainly and irrefutably that arbitration costs for typical single plaintiff cases are grossly unfair.").

STANDARD OF REVIEW

This Court's review of an order granting a motion to compel arbitration is *de novo*. *BankAmerica Housing Services v. Lee*, 833 So.2d 609, 617 (Ala. 2002).

"Therefore, this Court must determine 'whether the trial judge erred on a factual or legal issue to the substantial prejudice of the party seeking review.' *Ex parte Roberson*, 749 So.2d 441, 446 (Ala.1999)." *Id.; see also Stevens v. Phillips*, 852 So.2d 123, 128 (Ala. 2002).

SUMMARY OF THE ARGUMENT

The record in this case establishes beyond serious contention that (a) Cook's arbitration clause is excessively broad, in the manner that this Court has found grossly favorable to the drafter in several previous cases; and (b) the Leemans had no meaningful choice with respect to Cook's arbitration clause because every other major pest control company in Alabama has the same sort of arbitration clause and because Cook's refuses to negotiate over the provision. The only issue that Cook's seriously disputes in this case is whether the Leemans have met their evidentiary burden of proving that Cook's arbitration clause imposes unconscionable costs upon its customers. They have.

In *Green Tree Financial Corp. v. Randolph*, 513 U.S. 79, 90 (2000), the U.S. Supreme Court recognized that if

an arbitration clause imposes such heavy costs that a party would not be able to vindicate their rights, then the clause could not be enforced. The problem for the consumer plaintiff in *Randolph* was that she introduced no hard evidence to *prove* that the costs of arbitration were likely to be high. In the years that have followed, this Court has also rejected a number of challenges to arbitration clauses that were based on the cost of arbitrating, on the grounds that there was not enough evidence to prove that arbitration would be expensive in those cases.

This case is entirely different from those failed challenges; it is cut from a different cloth. In this case, the consumer plaintiffs have introduced admissible evidence that proved three propositions that were not proven in *Randolph* or in any previous case to come before this Court.

First, the plaintiffs conclusively proved which set of rules would govern any arbitration of their claims: the AAA's Commercial Rules. As this brief will establish, half a dozen federal and state courts have held that these rules impose such enormous forum costs

that it is unconscionable for a corporation to require consumers to submit their claims to that system.

Second, the Leemans conclusively proved here how large the arbitration fees are going to be in a case of this sort, by introducing the very best evidence available on the subject. The plaintiffs established that in the only two consumer cases that have ever proceeded in arbitration against Cook's, the cost of arbitration was at least $12,000 and as much as $16,000. In five cases brought against Alabama pest control companies, the initial filing and administrative fees were $4,000 (in all five cases) and the other fees (mostly arbitrators' fees) averaged $6,560. In the only termite case where the case was tried to conclusion before the AAA, *Porter v. Cook's Pest Control*, the cost was nearly $13,000. These are shockingly high forum costs to impose on consumers bringing relatively modest claims. (In the only case to produce an award from the arbitrator, the award amounted to only $16,000.) The plaintiffs further proved that in similar cases that have been brought in Alabama against other pest control companies with essentially identical arbitration clauses,

the arbitration fees were comparably large prior to those cases settling. This is not a case involving "speculation" about arbitration costs, and it is not a case involving generalities about arbitration in general. Instead, this Court has before it the irrefutable proof as to what arbitration under Cook's system has actually cost consumers with the same type of claims as the Leemans.

Finally, the record contains unrefuted proof that Alabama consumers can find no attorneys who are willing to advance such forum costs or pursue such claims under the AAA's Commercial Rules. The record establishes that the only reason that the five cases alluded to above proceeded in arbitration against pest control companies is that the counsel in those cases were willing to undergo those costs as the only way of establishing a evidentiary record on the subject of those costs.

In short, Cook's arbitration clause does not offer consumers such as the Leemans an alternative forum to the civil justice system, it offers them no forum at all. Cook's arbitration clause is, in reality, effectively an exculpatory provision, and a remedy-stripping clause.

This Court has held that corporations may not impose upon their consumers contracts that state, in effect, that "you may never bring claims against us for punitive damages, even where those claims are provided for by state law." *See Ex parte Thicklin*, 824 So.2d 723, 733 (Ala. 2002). In this case, this Court should clarify that, by the same logic, a corporation may not impose upon its consumers contracts that effectively state "we will establish a system that is rigged to ensure that you may never bring any claims against us for any type of damages for wrongs that we may do to you, even where those claims are justified under state law."

The trial court disagreed for at least two clearly wrong reasons. First, the trial court disregarded the empirical evidence of the actual costs of arbitrating a case such as this, preferring to hazard a guess based upon a misunderstanding of how the AAA's Commercial Rules work. Second, the trial court concluded, in essence, that arbitration fees are never excessively high (even when they render a case prohibitive to any economically rational actor) if it is technically possible for a consumer to pay those fees.

As to the costs to be expected if the Leemans were to take this case to arbitration, the Circuit Court made an erroneous finding of fact about the magnitude of the arbitration costs in this case. The record in this case establishes that the AAA's Commercial Rules require claimants to pay two principal categories of fees: filing fee designed to cover AAA's administrative costs, and fees payable to the arbitrator himself. The record reflects that the arbitrator's fees tend to be far larger than the filing fees. Mistaking the visible tip for the entire iceberg, the trial court made a finding of fact that assumed that the entire cost of arbitration is found in the filing fee, and asserted that it was unimaginable that arbitration fees for a case such as the Leemans' could amount to sums such as $16,000. Given that this assertion is based upon a plainly wrong premise, and that the empirical experience of every case against a pest control company to actually proceed to arbitration in Alabama flatly contradicts the trial court's unsupported guess on the matter, this Court should hold that the Circuit Court's finding of fact on this point was erroneous.

As to the trial court's legal conclusion that a consumer's technical, conceivable ability to advance such costs is determinative, this Court has already rejected that notion in the context of arbitration clauses that require consumers to proceed on an individual, as opposed to a class action, basis. In *Leonard v. Terminix*, 854 So.2d 529 (Ala. 2002), this Court held that an arbitration clause that requires individuals to pay costs that are excessive relative to their expected recovery is unconscionable, without respect to whether all of those consumers are impoverished. The fact that the Leemans are a school principal and an elementary school teacher does not deprive them of any rights under Alabama law.

ARGUMENT

I. This Court Should Apply Alabama Law to Determine Whether Cook's Arbitration Clause is Unconscionable

A. This Court Must Determine Whether Cook's Arbitration Clause is Unconscionable

This Court, and not the arbitrator, should decide whether this arbitration agreement is unconscionable. *See Anderson v. Ashby*, 2003 WL 21125998 at *5 (Ala. May 16, 2003). As this Court pointed out in *Anderson*, the Federal Arbitration Act ("FAA") requires this Court to

"'faithfully apply general principles of Alabama contract law when considering a challenge to the validity of an arbitration agreement.'" *Id.*, *quoting Green Tree Fin. Corp. v. Wampler*, 749 So.2d 409, 416 (Ala. 1999). The only time this validity analysis should be done by the arbitrator is where a party is challenging the entire contract as invalid, rather than the arbitration clause itself. *Id., citing Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 398 (1967); *see also Ex parte Dan Tucker Auto Sales, Inc.*, 718 So.2d 33, 43 (Ala. 1998) ("While *Prima Paint* . . . relegates challenges to the validity of the contract as a whole to the arbitrator, a challenge to the arbitration clause only is properly determined by the court.") (Lyons, J. concurring) (citation omitted).

In this case, as in *Anderson*, the issue is the unconscionability of an arbitration clause, and therefore the court properly has jurisdiction over this question. *Anderson* at *6 ("Because Mrs. Ashby contends that the arbitration agreement included in the note and security agreement was itself unconscionable, the trial court did not err in holding that it had the authority to resolve

that issue."); *see also American Gen. Fin., Inc. v. Branch*, 793 So.2d 738 (Ala. 2000) ("[T]he threshold 'issue of unconscionability of an *arbitration clause* is a question for the court and not the arbitrator.'") (citations omitted, emphasis in original).

If this Court were to reverse field and hold that arbitrators were to decide questions of unconscionability, it would have to overturn a number of its own recent decisions on the unconscionability of arbitration agreements. *See, e.g.*, *Anderson* (arbitration clause held unconscionable on the basis of unusually broad language, lack of mutuality, limitation of damages and lack of meaningful choice); *Branch* (same); *Leonard v. Terminix*, 854 So.2d 529 (Ala. 2002) (arbitration clause held unconscionable based on class action ban and resulting prohibitive costs of arbitration for individual consumers); *Harold Allen's Mobile Home Factory Outlet, Inc. v. Butler*, 825 So.2d 779 (Ala. 2002) (arbitration clause held unconscionable based on the vendor's unilateral right to appoint the arbitrator).

As further evidence that courts are to decide unconscionability challenges, there are literally dozens

of courts that have held that particular arbitration clauses had been drafted in a manner that rendered them unconscionable in particular cases.[12]

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[12] *Ting v. AT&T*, 319 F.3d 1126 (9th Cir. 2003), *cert. denied*, 2003 WL 1988529 (Oct. 6, 2003); *Alexander v. Anthony Int'l*, 341 F.3d 256 (3d Cir. 2003); *Circuit City Stores, Inc. v. Adams*, 279 F.3d 889 (9th Cir. 2002), *cert. denied*, 535 U.S. 1112 (2002); *Ticknor v. Choice Hotels Int'l, Inc.*, 265 F.3d 931 (9th Cir. 2001); *Shankle v. B-G Maint. Mgmt. of Colo., Inc.*, 163 F.3d 1230 (10th Cir. 1999); *Faber v. Menard, Inc.*, 267 F.Supp.2d 961 (N.D. Iowa 2003); *Plaskett v. Bechtel Int'l*, 243 F.Supp.2d 334 (D.V.I. 2003); *Luna v. Household Fin. Corp.*, 236 F.Supp.2d 1161 (W.D. Wash. 2002); *Comb v. Paypal, Inc.*, 218 F.Supp.2d 1165 N.D. Cal. 2002); *Cooper v. MRM Inv. Co.*, 199 F. Supp.2d 771 (M.D. Tenn. 2002); *Brennan v. Bally Total Fitness*, 198 F. Supp.3d 377(S.D.N.Y. 2002); *Geiger v. Ryan's Family Steak Houses, Inc.*, 134 F.Supp.2d 985 (S.D. Ind. 2001); *Prevot v. Phillips Petroleum Co.*, 133 F. Supp. 2d 937 (S.D. Tex. 2001); *Lozada v. Dale Baker Oldsmobile, Inc.*, 91 F. Supp. 2d 1087 (W.D. Mich. 2000); *In re Knepp*, 229 B.R. 821 (Bankr. N.D. Ala. 1999); *Nicholson v. Labor Ready, Inc.*, 1997 U.S. Dist. LEXIS 23494 (N.D. Cal. May 23, 1997); *Armendariz v. Found. Health Psychcare Services, Inc.*, 24 Cal. 4th 83, 99 Cal. Rptr. 2d 745, 6 P.3d 669 (2000); *Graham v. Scissor-Tail, Inc.*, 28 Cal. 3d 807, 171 Cal. Rptr. 604, 623 P.2d 165 (1981); *Worldwide Ins. Group v. Klopp*, 603 A.2d 788 (Del. Supr. 1992); *Powertel, Inc. v. Bexley*, 743 So. 2d 570 (Fla. Dist. Ct. App. 1999); *Ballard v. Southwest Detroit Hosp.*, 119 Mich. App. 814, 327 N.W.2d 370 (1982); *East Ford, Inc. v. Taylor*, 826 So.2d 709 (Miss. 2002); *Iwen v. U.S. W. Direct*, 293 Mont. 512, 977 P.2d 989 (1999); *Teleserve Sys., Inc. v. MCI Telecommunications Corp.*, 230 A.D.2d 585, 659 N.Y.S.2d 659 (1997); *Williams v. Aetna Fin. Co.*, 83 Ohio St. 3d 464, 700 N.E.2d 859 (1998), *cert. denied*, 526 U.S. 1051 (1999); *O'Donoghue v. Smythe, Cramer Co.*, 2002 WL 1454074 (Ohio Ct. App. July 3, 2002); *Myers v. Terminix Int'l Co.*, 91 Ohio Misc. 2d 41, 697 N.E.2d 227 (Ct. Com. Pl. 1998); *Zak v. Prudential Prop. & Cas. Ins. Co.*, 713 A.2d 681 (Pa. Super. Ct. 1998); *In re Turner Bros. Trucking Co.*, 8 S.W.3d 370

B. Alabama State Contract Law Governs the Question of Whether this Arbitration Clause Is Unconscionable.

As discussed above, this Court has recognized that the FAA directs it to apply state contract law when addressing questions of the validity of an arbitration clause. The FAA incorporates a savings clause that provides that arbitration clauses will not be enforced if there are grounds under state contract law for invalidating the clause. 9 U.S.C. § 2. The U.S. Supreme Court has recognized that the defense of unconscionability is available to a party challenging an arbitration agreement. *Doctor's Assocs., Inc. v. Casarotto,* 517 U.S. 681, 687 (1996) ("[G]enerally applicable contract defenses, such as fraud, duress or unconscionability, may be applied to invalidate arbitration agreements without contravening [the F.A.A.]."). In other words, state contract law applies to arbitration clauses. This principle is incorporated into the federal substantive law of arbitration. *Perry v.*

(Tex. App. 1999); *Sosa v. Paulos*, 924 P.2d 357 (Utah 1996); *Toppings v. Meritech Mort.*, 569 S.E.2d 149 (W.Va. 2002); *Arnold v. United Companies Lending Corp.*, 204 W. Va. 229, 511 S.E.2d 854 (1998); and *Mendez v. Palm Harbor Homes, Inc.*, 45 P.3d 594 (Wash. Ct. App. 2002).

Thomas (1987) 482 U.S. 483, 492-93 ("An agreement to arbitrate is . . . enforceable, *as a matter of federal law*, 'save upon such grounds as exist at law or in equity for the revocation of *any* contract.' . . . Thus state law, whether of legislative or judicial origin, is applicable *if* that law arose to cover issues concerning the validity, revocability, and enforceability of contracts generally.") (emphasis in original, citations omitted).

In Alabama, the state law of unconscionability is most clearly set out in *American General Finance, Inc. v. Branch*, 793 So.2d 738 (Ala. 2000). There, this Court recognized an earlier four-part test to determine whether a contract is unconscionable under Alabama law: "'(1) whether there is an absence of meaningful choice on one party's part; (2) whether the contractual terms are unreasonably unfavorable to one party; (3) whether there was unequal bargaining power between the parties; and (4) whether the contract contained oppressive, one-sided, or patently unfair terms.'" *Branch*, 793 So.2d at 748, quoting *Layne v. Gardner*, 612 So.2d 404 (Ala. 1992). This Court then collapsed the test into two more

comprehensive prongs: whether the clause contains grossly favorable terms, and whether there is an overwhelming disparity of bargaining power. *Id. ; see also Anderson*, 2003 WL 21125998 at *8-9. Cook's arbitration clause clearly satisfies both prongs of this test, and is unconscionable.

II Cook's Arbitration Clause Is Unconscionable In This Case Because It Was Imposed Through Cook's Overwhelming Bargaining Power.

A. The Leemans Had No Meaningful Choice to Avoid Arbitration.

In both *American General Finance v. Branch* and *Anderson v. Ashby*, this Court focused in on the question of whether the consumer had "meaningful choice" in contracting with a service provider with an arbitration clause in its contract. "A primary indicium of unconscionability in the modern consumer-transaction context," stated this Court in *Branch*, "is whether the consumer has the ability 'to obtain the product made the basis of [the] action' without signing an arbitration clause." *Branch*, 793 So.2d at 750.

This Court made clear in *Anderson* that in order to show a lack of meaningful choice, a consumer does not have to show that she "actually shopped around for an

arbitration-free [contract]." *Anderson* at *9. Instead, it is sufficient for the consumer to show that at the time the contract was signed, it was the practice of companies in same geographical area providing the same service to include arbitration provisions in their contracts. *Id.* at *10; *see also Branch*, 793 So.2d at 750-51 (basing the finding of overwhelming bargaining power on a record showing that every company listed in the City of Tuscaloosa phone book offering similar services to American General Finance, with the exception of one, also included an arbitration clause in its contract).

Finally, in *Leonard v. Terminix*, this Court found based on the record that "Terminix's competitors in Alabama also used arbitration provisions in their contracts at the time the Leonards bought their home." *Leonard*, 854 So.2d at 538.

The fact that this evidence is in the Leemans' record serves to distinguish this case from those in which this Court has refused to find a lack of meaningful choice because plaintiffs have presented no support for such a finding. *See, e.g., Vann v. First Community*

Credit Corp., 834 So.2d 751, 754 (Ala. 2002) (holding that the Vanns "have not put forth substantial evidence demonstrating that . . . First Community had overwhelming bargaining power.); *Green Tree Fin. Corp. v. Lewis*, 813 So.2d 820, 825 (Ala. 2001) ("The Lewises have made no showing that they lacked a meaningful choice in obtaining financing; the plaintiff in *Branch* did make such a showing."). As this Court noted in *Anderson*, both *Vann* and *Lewis* "turn[] on the utter failure of the plaintiffs to submit evidence of the scarcity of lenders that did not require arbitration agreements in the particular market in which the plaintiffs were seeking loans." *Anderson*, 2003 WL 21125998 at *11. The Leemans' case has no such failing; plaintiffs here have presented reams of evidence to this effect. Moreover, Cook's admits that it is unaware of any company which would issue termite bonds without an arbitration clause.

Another factor that this Court has considered in determining whether the non-drafter had meaningful choice when signing a contract is whether that party had any right to negotiate the terms of the contract. In *Anderson v. Ashby*, this Court found that "the Ashbys had

no input into negotiating the terms of or drafting the arbitration agreement. This evidence establishes that the Ashbys had no meaningful choice in accepting the arbitration agreement and that American General Finance had overwhelming bargaining power in obtaining the arbitration agreement." *Anderson*, 2003 WL 21125998 at *11; *see also Leonard*, 854 So.2d at 538 (including in discussion of unconscionability the fact that "[t]he Leonards have shown that the Terminix contract is a contract of adhesion that has never been modified for any Alabama customer; they have also shown that they were not given any opportunity to accept or reject the arbitration provision.").

The upshot of these answers is that Cook's presents its consumers with a standard form contract on a take-it-or-leave-it basis. There is no way that the Leemans, or any Cook's customer, could have gotten out of this arbitration clause and still received any services from Cook's. Furthermore, the record also shows that the Leemans had no choice but to agree to arbitrate their pest control claims, as every conceivable local company providing these services included an arbitration clause

similar to Cook's clause. Taken together, these facts alone support the conclusion that Cook's had overwhelming bargaining power in this transaction. *See Anderson*, 2003 WL 21125998 at *11 (holding that evidence that other lenders also used arbitration clauses combined with evidence that the borrowers here had no power to negotiate out of the arbitration clause "is sufficient to meet the second prong of the *Branch* unconscionability test.").

B. The Leemans Were Surprised, Given Cook's Failure to Disclose Information and the Impossibility of Determining the Costs of Arbitration.

Though this Court has not required a showing beyond lack of meaningful choice to meet the *Branch* test, it has indicated that more general principles, such as "the prevention of oppression and unfair surprise," are germane to the unconscionability analysis. *Stevens v. Phillips*, 852 So.2d 123, 134 (Ala. 2002), quoting Alabama Code § 7-2-302, comment 1.

The Alabama courts have not established a specific definition of the words "unfair surprise" in this section of the Alabama code. However, the Arizona Supreme Court, interpreting the same "oppression and unfair surprise"

language in its own state law, has indicated that "unfair surprise" includes "fine print clauses, mistakes or *ignorance of important facts* or other things that mean bargaining did not proceed as it should." *Maxwell v. Fidelity Fin. Servs., Inc.*, 907 P.2d 51, 57-58 (Ariz. 1995); citing DAN B. DOBBS, 2 LAW OF REMEDIES 703, 706 (2nd ed. 1993) (emphasis added); *see also Hutcherson v. Sears Roebuck & Co.*, 793 N.E.2d 886, 891 (Ill. App. 2003) (same).

At the time they agreed to arbitrate their claims, the Leemans did not – and could not – learn of the magnitude of the costs that would be imposed on them if they ever brought claims to arbitration. As such, Cook's contract, and the circumstances surrounding the signing of that contract, certainly meet the general definition of "unfair surprise" set forth in the Alabama Code.

The element of surprise is enhanced by the fact that the AAA is not a transparent body whose fees, like those of courts, are easy to discern. While a schedule of filing fees can be obtained (with effort), the most significant element of the fees under the Commercial Rules – the arbitrator's fees – is not publicly

available. For example, *see Ting v. AT&T*, 182 F.Supp.2d 902, 916-17 (N.D. Cal. 2002), *aff'd with respect to unconscionability*, 319 F.3d 1126 (9th Cir. 2003), *cert. denied*, 2003 WL 1988529 (Oct. 6, 2003):

> Different AAA arbitrators charge different hourly rates. To estimate the cost of an arbitration to be conducted under the AAA's Commercial Rules, a claimant must learn the hourly rate of the arbitrator who will hear the case. To determine . . . [this rate], a claimant must first initiate an arbitration with the AAA. . . . This makes it difficult for a class member before filing to meaningfully estimate the cost to have the case arbitrated under the Commercial Rules. Neither the AAA website or rules, nor the AT&T website, provides a class member with any information about likely arbitrator's fees.

See also Camacho, 167 F.Supp.2d at 897 n.4 ("It is impossible to establish the exact amount Camacho would have to pay because the arbitrator sets the amount after the arbitration has been initiated."). It is wrong to suggest that the Leemans could have readily determined the magnitude of these arbitration fees in advance of the dispute. The principal variable is the arbitrator's fees, and the rate that AAA arbitrators charge (much less the ultimate amount of fees that will be charged) cannot be determined until after one initiates the arbitration. However, in this record, there is evidence developed by

extraordinary and unprecedented effort to establish the cost of AAA arbitration of termite cases.

C. Cook's Contract Is Not Rendered Conscionable Merely Because the Leemans Are Educated People.

Throughout this case, Cook's has attempted to argue that the fact that the Leemans are educated means that they cannot have signed an unconscionable arbitration clause. Cook's premise is apparently that no contract entered into by a school teacher could ever be unconscionable under Alabama law. As Cook's would have it, an arbitration clause in a contract of adhesion that required individual consumers to spend $1 million to vindicate a valid claim worth $41,000, or that would require consumers to travel enormous distances (perhaps to the deserts of New Zealand) to vindicate those claims, would still necessarily be enforceable if the consumers had college degrees and could read. Simply put, Cook's argument is preposterous. The law in Alabama (like other states) is *not* that "nothing done to a school teacher is ever unconscionable."

However, a finding that the consumer is uneducated or unsophisticated is not necessary to the unconscionability analysis in Alabama. In *Layne v.*

Gardner, 612 So.2d 404 (Ala. 1992), where this Court first articulated the four-part unconscionability test later summarized and turned into a two-part test in *Branch*, this Court also mentioned the possibility that courts could look to whether one party was "unsophisticated and/or uneducated" in making a determination of unconscionability. *Layne*, 612 So.2d at 408. However, this specific question was never part of the four-part unconscionability test, and in fact it has dropped out completely in later renditions of that test. *See, e.g., Mason v. Acceptance Loan Co., Inc.*, 850 So.2d 289, 301 n.7 (Ala. 2002) (describing the four-part test, without mention of any "unsophisticated and/or uneducated" factor, as the "established – and still applicable" test for unconscionability in this state); *Gayfer Montgomery Fair Co. v. Austin*, 2003 WL 21480639 at *6,n.4 (Ala. July 27, 2003) (stating that the 2-part test of unconscionability used in *Branch* was created by "consolidating the four components of the test described in *Layne v. Gardner*," but not including any mention of the "unsophisticated and/or uneducated" factor).

As this Court made clear in *Leonard v. Terminix* and

Anderson v. Ashby, it is not essential that a consumer be uneducated for a contract to be found unconscionable. In *Leonard*, as discussed above, this Court specifically did not rest its unconscionability holding on the Leonards' personal financial circumstances, arguing instead that disproportionately expensive arbitral forum costs will deter all consumers, rich and poor, from bringing claims in arbitration. *Leonard*, 854 So.2d at 537.

And in *Anderson*, the most recent case where this Court discussed the plaintiffs' education and sophistication level, this discussion was only in response to Justice Stuart's request in her special writing for evidence that the Ashbys actually shopped around for an arbitration-free loan. *Anderson*, 2003 WL 2125998 at *10. Though this Court specifically stated that such a finding was *not* required in order to find that the Ashbys had no meaningful choice, *id.*, it nonetheless went on to discuss the fact that the Ashbys could not read the contract containing the arbitration agreement, were not told about the arbitration agreement, and therefore had no compelling reason to think they needed to look around for another lender. *Id.* at *11.

The context of this Court's discussion of the education/sophistication issue in *Anderson*, however, focused upon the meaningful choice issue. *Id.* ("[T]he facts of this case do not logically present an issue whether the Ashbys should have 'actually shopped around' for a lender that would not require that they execute an arbitration agreement."). Nor is it a dispositive issue in this case, where the Leemans have clearly shown that they could not have gone to another pest control company in the area and expect to find a contract without an arbitration clause, even had they tried to do so.[13]

III. The Arbitration Clause At Issue In This Case Contains Terms That are Grossly Favorable to Cook's.

This Court made clear in *Branch* that any provision in an arbitration clause that, as a practical matter, benefits only the stronger bargaining party, will satisfy the first prong of the Alabama unconscionability test. *Branch*, 793 So.2d at 749. Cook's arbitration clause

[13] The record reflects that the Leemans could not have obtained a bond without an arbitration clause if they had searched, and therefore that the search would have been futile. "The law is reasonable, and does not require the doing of useless or impossible things." *City of Mobile v. Jackson*, 474 So.2d 644, 650 (Ala. 1985).

contains two provisions that clearly benefit Cook's at the expense of consumers. The first provision requires arbitration for an extremely broad set of claims. The second designates the AAA Commercial Rules, which impose forum costs that are so prohibitive as to deter consumers from bringing claims against Cook's in arbitration.

A. Cook's Arbitration Clause is So Broad as to Cover all Real and Potential Consumer Claims.

The arbitration clause in the Leemans' contract applies to "any dispute, controversy or claim arising out of or relating to the agreement and guarantee or the breach thereof, or arising out of any prior or future dealings between Cook's and customer, shall be settled in arbitration . . . ." C17. Moreover, Cook's has argued in this case that the clause applies not only to signatories to the contract, but to nonsignatories as well. C547-49.

This extremely broad arbitration clause is strikingly similar to the clause found unconscionable in both *Branch* and *Anderson*. In both cases the defendant, American General Finance, had included in its contracts an arbitration clause applying to "'every dispute[] or controversy[] relating to' every actual or potential

transaction – whether past, present, or future – and to every person, whether signatory or nonsignatory to any document, involved in such a transaction between the parties." *Branch* at 748. This Court found that because "[t]he first indicium of unconscionability is the breadth of the clause," and that American General Finance's "unusually broad" arbitration clause was clearly unconscionable in that it "applie[d] to every cause of action that could conceivably arise in favor of Branch, and to every individual against whom a claim could conceivably be brought." *Id.; see also Anderson* at *9.

As in *Branch* and *Anderson*, the arbitration clause at issue here is so broad that it covers every conceivable claim that the Leemans ever had or ever could have, at any future date, against Cook's. In combination with the prohibitive costs imposed by Cook's chosen arbitration forum and the Leemans' lack of bargaining power or ability to negotiate a more fair contract, the sheer scope of the clause renders it unconscionable.[14]

[14] Although the Leemans argued that Cook's Arbitration clause was unconscionably overbroad, C80-81, the Circuit Court below did not address this issue.

B. The Law Is Clear that Arbitration Clauses That Impose Prohibitive Costs on Consumers are Grossly Favorable to the Drafting Party.

1. The United States Supreme Court has Declared that Arbitral Costs Must Not be So High As to Deny Claimants a Forum to Vindicate Their Rights.

The U.S. Supreme Court has stated repeatedly that arbitration must allow a party to "effectively vindicate" its rights. *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 637 (1985); *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 28 (1991) (quoting *Mitsubishi*). That Court has also recognized that arbitration will not meet this standard if the parties' arbitration clause imposes excessive costs, thus preventing a party from even entering the arbitral forum. *Green Tree Financial Corp. v. Randolph*, 513 U.S. 79, 90 (2000).

In *Randolph*, the Supreme Court addressed the question of whether an arbitration clause that was silent as to the allocation of forum costs would undermine a plaintiff's ability to enforce her rights under the federal Truth In Lending Act. *Id.* at 91. The Court began by emphasizing that "[i]t may well be that the existence of large arbitration costs could preclude a litigant such

as Randolph from effectively vindicating her federal statutory rights in the arbitral forum," but found that Randolph had not satisfied her burden of showing the likelihood of incurring such prohibitive costs because "the record contains hardly any information on the matter." *Id.*

2. Alabama Law Is Consistent with the U.S. Supreme Court's Prohibition on Prohibitively Costly Arbitration Clauses.

Notwithstanding the suggestions of Cook's, this Court has never held that an arbitration clause may impose such high costs upon consumers that the consumers are left with no effective remedy. Instead, this Court has held that arbitration clauses may not strip consumers of their legal rights under Alabama law. In the context of contractual bans on consumers' rights to bring class actions, this Court has held that arbitration clauses that have the predictable economic effect of stripping consumers of their legal rights cannot be enforced. Finally, while it is true that this Court has rejected a number of challenges to arbitration clauses based upon claims that they would impose excessive costs, it has always done so on the grounds that there was not adequate

evidence to support those claims, grounds that are certainly not relevant here.

First, the U.S. Supreme Court's statement in *Randolph* that arbitration clauses may not impose prohibitive costs is consistent with this Court's repeated statements that contracts of adhesion may not eliminate substantive rights. *See, e.g., Ex parte Thicklin*, 824 So.2d 723, 733 (Ala. 2002) ("[I]t violates public policy for a party to contract away its liability for punitive damages, regardless whether the provision doing so was intended to operate in an arbitral or judicial forum. Thus, enforcement of this portion of the arbitration agreement violates public policy, and its enforcement would be unconscionable."). This body of Alabama law is applicable to all contracts, *see, e.g., Reece v. Finch*, 562 So.2d 195, 199 (Ala. 1990) ("[E]xculpatory agreements are not valid as to extreme forms of negligence or any conduct that constitutes an intentional tort."), and therefore is not preempted by the FAA.

Second, this Court has applied this principle not only to arbitration clauses that expressly stripped

consumers of their rights, but also to clauses that effectively did so. In *Leonard v. Terminix*, this Court held that a pest control company's arbitration clause was unconscionable because that clause effectively banned class actions, with the result of keeping consumers with small claims out of arbitration altogether. *Leonard*, 854 So.2d at 539. This Court determined that if the Leonards were forced to arbitrate their claims on an individual basis, they would be placed in a position where their claims would actually be worth less than their filing fees, and that such a situation was clearly unconscionable:

> This arbitration agreement is unconscionable because it is a contract of adhesion that restricts the Leonards to a forum where the expense of pursuing their claim far exceeds the amount in controversy. The arbitration agreement achieves this result by foreclosing the Leonards from an attempt to seek practical redress through a class action and restricting them to a disproportionately expensive individual arbitration.

Id.

There have been a number of cases where this Court has not held high costs to be unconscionable, but the reason has almost uniformly been that claimants did not present enough evidence of those costs to this Court.

Those cases are thus clearly distinguishable from the instant case, where the Leemans have presented an extensive and comprehensive record to show that their forum costs will be excessively high.

In *Ex Parte Thicklin*, for instance, the consumer plaintiff argued that the arbitration clause included in her contract with a mobile home seller and manufacturer, which required arbitration under the AAA Commercial Rules, was unconscionable. *Ex Parte Thicklin*, 824 So.2d at 734. Thicklin pointed to the filing fee under the AAA Commercial Rules, but introduced no evidence relating to any arbitrators' fees, or evidence to compare the costs of the combined arbitration fees to the value of the lawsuit.

This Court, citing *Randolph*, held that Thicklin had not met her burden of showing that her anticipated arbitration costs were more than speculative. *Id.* at 735. In fact, this Court noted that Thicklin had not presented "any evidence, such as her income, her family's expenses, or the estimated costs of the arbitration procedure, that would support an argument that the use of the Commercial Rules renders the arbitration clause

unconscionable from a financial standpoint." *Id.* Here, in contrast, the Leemans have produced extensive evidence on the estimated costs of the arbitration procedure, which as we discussed above would deter anyone, regardless of income, from entering this arbitral forum for this type of claim.

In another case involving the AAA Commercial Rules, this Court similarly found that the consumer plaintiff had not presented adequate proof of prohibitive costs to warrant a finding of unconscionability. In *Stevens v. Phillips*, 852 So.2d 123 (Ala. 2002), this Court upheld a lower court opinion that an arbitration clause providing that claims would be arbitrated under the AAA's Commercial Rules was not unconscionable. There, the defendants had already paid the cost of the filing fee and the plaintiffs had not produced proof of any other prohibitive costs. *Id.* at 134-35. Without any evidence of such costs, the lower court had summarily stated in its opinion that "'Plaintiff's other costs in prosecuting her claims should be no different in arbitration, if not less, than in civil litigation in the Circuit Court of Lee County, Alabama.'" *Id.* Because the plaintiff on

appeal never disputed or even addressed this statement, this Court took the statement as true and upheld the clause. *Id.* at 135.

The case at bar could hardly be more different. Here, Cook's has not offered to pay any of the Leemans' costs in arbitration, and the Leemans have presented exhaustive evidence to show that the filing fee is only one fee among many forum costs that they would face in arbitration under the Commercial Rules. Finally, the Leemans have specifically shown that these arbitral forum costs would indeed be much greater than costs in civil litigation of the same claims – in fact, arbitration costs would be almost *51 times greater* than those court costs. C126, 168.

C. The Record Here Demonstrates that Cook's Arbitration Clause Is Prohibitively Expensive.

As discussed above in the Statement of Facts, the Leemans have assembled a comprehensive factual record to support their argument that the costs that will be imposed on them if they are forced into arbitration will be prohibitive, and thus unconscionable.

In this case, the Leemans have brought claims typical of claims by consumers against pest control

companies. These same type of claims were at the heart of the only two cases ever brought in arbitration by a consumer against Cook's itself: *Porter v. Cook's Pest Control* and *Wunderlich v. Cook's Pest Control*. C326.

As the Statement of Facts demonstrates, the Leemans' claims – like the claims of the plaintiffs in the *Porter* and *Wunderlich* cases that proceeded through arbitration – would automatically be arbitrated under the AAA Commercial Rules. C329.

The record demonstrates that the AAA Commercial Rules require the consumer to pay an initial fee of $3250 as well as a case management fee, which under the rules in effect when the record was filed was $750, C148, but which has since been increased to $1250. *See* American Arbitration Association, Commercial Arbitration Rules and Mediation Procedures, *available at* http://www.adr.org/index2.1.jsp?JSPssid=15747 (last visited Nov. 6, 2003). Therefore the Leemans, to even get in the door of arbitration, will certainly have to pay at least $4000, and perhaps as much as $4500, to the AAA. Under the AAA's Commercial Rules, consumers must also pay half the anticipated arbitrator fee at the

beginning of arbitration, simply in order to access the arbitral forum. C329. As Margaret Wilson of the AAA explained in her memo, this up-front arbitrator fee is based on the hourly rate of the arbitrator in any given case. *Id.* In *Porter*, this fee was $1500; in *Wunderlich*, $1750. In *Travers v. Terminix Int'l, Inc.*, the other case in which complete AAA invoices are available, this fee was $1600. The Leemans could therefore expect to have to pay at *least* $1500 in up-front arbitrator fees in order to access the arbitral forum.

The record further demonstrates that were the Leemans to actually litigate a case against Cook's to completion in arbitration, complete with witness testimony and argument, their forum costs would run much higher. The Porter case took 4 days to resolve in arbitration. The arbitrator's fees in that case, including study time and hearing time, came to $8,950. These costs were not paid to the witnesses or to any lawyers; these were forum costs paid to the AAA throughout the course of the arbitration. If the Porters had not been able to pay each AAA bill as it came in, their case could have been suspended or terminated,

according to the AAA Rules. C146. Altogether, the Porters paid $12,950 in forum fees. C168.

The potential recovery in these cases may be quite low in some cases. As discussed above, the *Porter* case was the only one of these five cases against pest control companies that went all the way through the arbitration process to an award at the time the record evidence was assembled below. The arbitrator in that case ruled for the Porters and awarded them $16,000. He then granted them about $4800 more, which he claimed was to reimburse them for their share of the arbitrator fees. C230-31. In fact, this reimbursement covered only a small portion of their fees, which had amounted to $12,950.

The upshot of these facts is that for the Leemans to arbitrate their claims, they would certainly have to pay, at the bare minimum, either $5500 (using the old Case Filing Fee of $750) or $6000 (using the new Fee), in up-front forum fees. If Cook resisted and the Leemans were obliged to put on their substantive case in arbitration, they would certainly pay thousands of dollars more for the arbitrator's study and hearing time. All of this would be required for a case where the ultimate award

could easily be less than $20,000. In contrast, filing these cases in court would result in forum fees between $211 - $299, depending on which Alabama Circuit Court consumers happened to use and whether a jury is required. C109.

The prohibitive nature of these fees is proven with the sworn testimony of a number of Alabama lawyers, discussed in the Statement of Facts, that they would not (meaning that they could not afford to) bring cases such as this under the AAA's Commercial Rules.

The conclusion that these fees are prohibitive is hardly a new or radical one. Half a dozen courts across the country faced with similar factual records to that in this case have found the AAA's fees to be prohibitively high, even in cases where the fees imposed on the parties were expected to be far less than the over $12,000-$16,000 that would likely be demanded of the Leemans here.

In *Ting v. AT&T*, 182 F.Supp.2d 902 (N.D. Cal. 2002), *aff'd with respect to unconscionability*, 319 F.3d 1126 (2003), *cert. denied*, 2003 WL 1988529 (Oct. 6, 2003), for example, the district court examined an exhaustive

evidentiary record on the average arbitration costs under the AAA's Commercial Rules. It found that the average daily rate for an arbitrator is nearly $2000, and that the AAA, though it offers the possibility of fee waivers, typically does not waive fees but instead defers them until the time of the hearing. *Id.* at 917.[15] The court held that these high costs, plus the additional case costs and service fees, would clearly "deter many potential litigants from proceeding" with arbitration. *Id.* at 934.

The *Ting* court's conclusions with respect to AAA's Commercial Rules are entirely consistent with the decisions of a host of other courts. *See also Camacho v. Holiday Homes, Inc.*, 167 F.Supp.2d 892 (W.D.Va. 2001) (arbitration clause precluded consumer from effectively vindicating her statutory rights because the fees under AAA's Commercial Rules were financially prohibitive); *Popovich v. McDonald's Corp.*, 2002 WL 47965 (N.D.Ill. Jan. 14, 2002) (refusing to enforce an arbitration clause on the grounds that under the AAA's Commercial Rules,

[15] In *Wunderlich v. Cook's Pest Control, Inc.*, the AAA arbitrator flatly refused to defer any payment of costs until after arbitration, and actually suspended the hearing pending both parties' payment of these costs. C497-98.

"the costs of arbitration are likely to be staggering," and finding that the costs of arbitrating the consumer claims at issue in that case were likely to amount to $48,000 to $126,000); *Phillips v. Associates Home Equity Services*, 179 F.Supp.2d 840 (N.D.Ill. 2001) (arbitration clause not enforced in Truth in Lending Act suit because the costs of arbitration under AAA's Commercial Rules are prohibitive, noting that the filing fees alone would amount to $4,000); *Mendez v. Palm Harbor Homes, Inc.*, 45 P.3d 594, 605 (Wash. Ct. App. 2002) (arbitration clause requiring consumer bringing claims involving a defective home was unconscionable because the costs under the AAA's Commercial Rules were unconscionable; "Avoiding the public court system in a way that effectively denies citizens access to resolving everyday societal disputes is unconscionable"); *Arnold v. Goldstar Fin. Sys., Inc.*, 2002 WL 1941546 * 10 (N.D.Ill. Aug. 22, 2002) (consumer cannot be required to arbitrate claims because of prohibitive costs under AAA's Commercial Rules); *Giordano v. Pep Boys – Manny, Moe & Jack, Inc.*, 2001 WL 484360 (E.D.Pa. Mar. 29, 2001) (fees under AAA rules would deter plaintiff's vindication of claims in arbitration).

It is important to note that the Leemans' challenge is not an attack on arbitration generally. In fact, a great many major corporations have moved to draft arbitration clauses contained in adhesive contracts that require the corporation to pay or at least advance nearly all of the costs of arbitration.[16] The issue in this case is not whether Cook's can require its customers to arbitrate their cases, but if it can require *them* to pay costs that are likely to be in the range of $12,000 to $16,000 to litigate claims likely to be modest in size.

D. The Circuit Court's Decision Relating to the Costs of Arbitration Is Based On Two Major Mistakes of Fact and Law.

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[16] *See, e.g.*, National Consumer Law Center, *Consumer Arbitration Agreements: Enforceability and Other Topics* (2d ed. 2002) (CD Rom accompanying book) (contains copies of such arbitration clauses; a few illustrative examples are clauses from Advance America, Cash Advance Centers of Louisiana, Inc. ("If you demand arbitration, upon your written request to us, we will advance the arbitration organization's filing or hearing fees."); Associates Financial Services Co. of Texas ("If you start arbitration, you agree to pay the initial filing fee required by the American Arbitration Association up to a maximum of $125. We agree to pay for the filing fee and any deposit required by the American Arbitration Association in excess of $125."); MBNA America Bank, N.A. ("At your written request, we will advance any arbitration-filing fee, administrative and hearing fees, which you are required to pay to pursue a claim in arbitration.")).

Despite a wealth of evidence as to what arbitration fees actually have been in the real world in cases essentially identical to this one, the Circuit Court mis-analyzed the AAA Commercial Rules to come to the conclusion that the costs would necessarily be far lower. The court indicated that "in order for the arbitration fees to be in this range [from $12,000 - $16,000], the fee schedule of the . . . [AAA Commercial Rules] specify a range of between $5,000,000 and $10,000,000 in the amount of the claim to require an initial fee of $10,000 and a case service fee of $4,000." C798-99.

It is evident from this passage that the Circuit Court was operating under the assumption that the only fees associated with arbitration under the AAA were the filing fees set forth in AAA's schedules. (There are no public schedules setting forth any information whatsoever about arbitrators' fees under the AAA Commercial Rules.) C150-166.

The Circuit Court's incorrect conclusion derives from its incorrect premise. As the evidence from cases such as *Porter* and *Wunderlich* demonstrates, forum fees include not only initial fees and case service fees, but

also anticipated and actual arbitrator fees for both study time and hearing time. These fees, which are in the thousands of dollars, combine with the initial $4000 to bring forum costs into the tens of thousands of dollars, regardless of the amount of the potential recovery. This Court should hold that the Circuit Court's guess as to the likely arbitration fees is clearly erroneous and contrary to all of the evidence in this case.

The Circuit Court also concluded that the costs of arbitration were not unconscionable in this case, because there was no evidence that the Leemans were so impoverished that they unable to pay these sums. In so holding, the Circuit Court invented an extremely high hurdle that is contrary to Alabama law. Simply put, it is unconscionable to require any consumer to pay up front arbitration forum fees amounting to $12,000 to $16,000 to bring typical, comparatively modest claims for property damage to a home.

In *Leonard*, this Court compared the costs to proceed under the arbitration clause to the claimant's likely recovery. The Court did not require a showing that the

claimant's income was too low to afford the arbitration. In *Leonard*, the consumer plaintiffs disclaimed any reliance on an economic hardship argument, since they could not claim poverty status. *Leonard*, 854 So.2d at 537 n.4. This Court deliberately did not base its decision on a financial hardship standard, instead holding: "That the expenses of arbitration would exceed the amount in controversy is not a problem personal or peculiar to any particular consumer but is, rather, a phenomenon inherent in the transaction itself." *Id.* at 537. Such is the case here: forum fees of up to $16,000 in cases where the amount in controversy may be less than $20,000 are disproportionate, regardless of the economic situation of the consumer faced with those fees.

As the Statement of Facts reflects, this case also presents a situation where an arbitration clause has been drafted in such a way as to be prohibitive -- it requires individuals to pay costs that are disproportionate to their likely recovery. The Leemans' evidence shows that such costs will deter consumers from bringing their claims in arbitration. Indeed, it demonstrates that no counsel can be found in Alabama to handle such cases

under the AAA's Commercial Rules. As such, Cook's arbitration clause, imposing as it does enormously high forum costs that would surely deter any rational consumer from even attempting to arbitrate against Cook's, meets the Circuit Court's own definition of an unconscionable clause. As that court held, arbitration clauses are unenforceable "if they work to *deny the claimant a forum* in which to litigate or arbitrate their claim." C802 (emphasis added).

CONCLUSION

Cook's arbitration clause is the product of overwhelming economic bargaining power and contains terms that are grossly favorable to Cook's. This Court should hold that Cook's arbitration clause is unconscionable under generally applicable principles of Alabama contract law, and reverse the Circuit Court's order compelling the Leemans to arbitrate their claims.

Date: November __, 2003

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing has been served upon all counsel of record VIA FACSIMILE and by placing a copy of same in the U.S. Mail, postage prepaid and properly addressed, on this the ___ day of November, 2003, as follows:

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