A Horse of a Different Color:

Binding Arbitration and the FTC’s Interpretation of the
Magnuson-Moss Warranty Act’s “Informal Dispute Settlement Procedures”

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I. INTRODUCTION

Since the 1980s, the Supreme Court has increasingly expanded the coverage of the Federal Arbitration Act (FAA), including allowing binding arbitration of claims arising under federal statutes.1 Acknowledging this growing acceptance and respect for arbitration, the Fifth and Eleventh Circuits have found that claims under the Magnuson-Moss Warranty Act (MMWA) may be submitted to pre-dispute binding arbitration despite a Federal Trade Commission (FTC) Rule prohibiting such pre-dispute binding arbitration clauses in written warranties. But on September 19, 2011, the Ninth Circuit held in Kolev v. Euromotors West/The Auto Gallery that the Federal Trade Commission’s (FTC) Rule 703, which prohibits pre-dispute binding arbitration of warranty claims, was not preempted by the FAA, and therefore, warranty claims under the MMWA must be allowed to proceed to court for a trial.2 The decision created a circuit split that the Supreme Court may choose to resolve in the next term, as it presents an opportunity to further solidify the law surrounding the arbitration of statutory claims—particularly, clarifying the proper deference to give an agency interpretation that may run contrary to the strong federal policy favoring arbitration.3 If the Court upholds the Ninth Circuit’s ruling, the ruling will mark a dramatic shift in the way that the Supreme Court has interpreted the FAA and would seem to weaken the “strong federal policy favoring arbitration.” Alternatively, if the Court overturns the Ninth Circuit, the ruling will strengthen the already strong policy favoring arbitration as the ruling will create a precedent for rejecting agency rules and regulations that prohibit or hamper arbitration.

Though the Ninth Circuit’s finding has a credible basis in administrative law doctrine and conducts an appropriate Chevron analysis,4 the current Supreme Court most likely will not uphold the ruling. The Ninth Circuit’s analysis is predicated on an FTC interpretation of the term “informal dispute settlement procedure.” The Court is unlikely to accept this interpretation for two reasons. First, the FTC’s interpretation of “informal dispute settlement procedures” is far broader than the language of the statute supports, as it includes arbitration under its aegis. Under the MMWA, informal dispute settlement procedures are supposed to be precursors to litigation,5 but the Court has repeatedly held that arbitration is a substitute for litigation.6 Thus, the FTC overreached by including binding arbitration within the term “informal dispute settlement procedure”; the Court will not accept the agency changing the Court’s definition of arbitration.

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2 658 F.3d 1024, 1025 (9th Cir. 2011).
4 See infra, Part IIC.
Second, the Court will find the FTC regulation unreasonable due to the FTC’s overreach and the FTC’s hostility toward arbitration. As such, the Supreme Court likely will overturn the Ninth Circuit’s decision and resolve the split in favor of the Fifth and Eleventh Circuits.

II. THE LAW

The decisions of the Fifth, Ninth and Eleventh Circuits require interpretation of two federal laws and a judicial doctrine. This section explores the relevant provisions of the FAA and the MMWA as well as the Chevron Doctrine. The question these cases raise is whether an agency interpretation barring pre-dispute binding arbitration is entitled to deference given the strong federal policy favoring arbitration that the FAA created.

A. The Federal Arbitration Act

In 1924, Congress enacted the FAA with the purpose of “revers[ing] centuries of judicial hostility to arbitration agreements by plac[ing] arbitration agreements upon the same footing as other contracts.”\(^7\) Arbitration is an alternative dispute resolution method in which disputing parties submit their issues to a neutral third party for a binding decision.\(^9\) By submitting claims to arbitration, parties do not forgo their substantive rights but merely have them heard in an arbitral forum instead of a judicial one.\(^10\) Thus, arbitration replaces filing a lawsuit.

Section 2 of the FAA requires courts to enforce agreements to arbitrate disputes unless there are “grounds as exist at law or in equity for the revocation of any contract.”\(^11\) Because of the breadth of § 2, the Supreme Court has held that Congress has “[declared] a liberal federal policy favoring arbitration agreements.”\(^12\)

This “liberal federal policy” has resulted in the Court interpreting the FAA as preempting state statutes and judicial doctrines that do not comply with § 2 and allowing arbitration of

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\(^7\) Final Action Concerning Review of Interpretations of Magnuson-Moss Warranty Act; Rule Governing Disclosure of Written Consumer Product Warranty Terms and Conditions; Rule Governing Pre-Sale Availability of Written Warranty Terms; Rule Governing Informal Dispute Settlement Procedures; and Guides For the Advertising of Warranties and Guarantees [hereinafter FTC Explanation of Final Rule], 64 Fed. Reg. 19700-01, 19708 (April 22, 1999).


\(^9\) BLACK'S LAW DICTIONARY (9TH ED. 2009).

\(^10\) Mitsubishi Motors, 473 U.S. at 628.


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

\(^12\) Id. Moses, 460 U.S. at 24.
claims that arise from federal statutory causes of action.\textsuperscript{13} Several times, the Court has had the opportunity to except a statutory right to a cause of action from the FAA’s coverage. But each time the Court considered the question, “it has upheld binding arbitration if the statute creating the right did not \textit{explicitly} preclude arbitration.”\textsuperscript{14} The Court explains its holding and the policy underlying it in \textit{Mitsubishi Motors} on a freedom of contract of basis. “Having made the bargain to arbitrate,” the Court said, “the party should be held to it unless \textit{Congress itself has evinced an intention to preclude a waiver of judicial remedies} for the statutory rights at issue.”\textsuperscript{15} As a result, an agreement to arbitrate binds parties unless Congress has expressed clearly that arbitration of the statutory right is precluded.\textsuperscript{16}

Though the Supreme Court has not yet found that Congress has clearly expressed that arbitration of a statutory right is prohibited,\textsuperscript{17} in \textit{McMahon} the Court devised a three-factor test to determine Congress’s intent as to the arbitrability of causes of action:\textsuperscript{18}

(1) the text of the statute;
(2) its legislative history; and
(3) whether “an inherent conflict between arbitration and the underlying purposes [of the statute]” exists.\textsuperscript{19}

In applying the \textit{McMahon} test, “questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration,”\textsuperscript{20} and the burden of showing Congress’s intent was to preclude arbitration is on the party that opposes enforcing the arbitration agreement.\textsuperscript{21}

\textbf{B. The MMWA}

In 1975, Congress passed the MMWA as a response to an increasing number of consumer complaints regarding the inadequacy of warranties on consumer goods.\textsuperscript{22} The purpose of the MMWA is “to improve the adequacy of information available to consumers, prevent

\textsuperscript{13} \textit{Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.}, 473 U.S. 614 (1985) (holding that courts must enforce arbitration agreements according to their terms and that causes of action founded on statutory rights are not excepted from being enforced).
\textsuperscript{14} \textit{Davis v. S. Energy Homes, Inc.}, 305 F.3d 1268, 1272-74 (11th Cir. 2002). \textit{See also Gilmer v. Interstate/Johnson Lane Corp.}, 500 U.S. 20, 35 (1991) (holding that courts should enforce binding arbitration agreements regarding claims arising under the ADEA).
\textsuperscript{15} \textit{Mitsubishi Motors}, 473 U.S. at 628 (emphasis added).
\textsuperscript{16} \textit{Id.} \textit{See also Gilmer}, 500 U.S. at 26 (“questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration.”) (quoting \textit{Moses H. Cone Mem'l Hosp.}, 460 U.S. at 24).
\textsuperscript{17} \textit{See Rodriguez de Quijas v. Shearson/American Express, Inc.}, 490 U.S. 477 (1989) (holding that courts should enforce pre-dispute agreements to arbitrate claims under the Securities Act of 1933); \textit{McMahon}, 482 U.S. (holding that courts should enforce pre-dispute agreements to arbitrate Securities Exchange Act of 1934 claims and Racketeer Influenced and Corrupt Organizations Act claims); \textit{Mitsubishi Motors}, 473 U.S. at 628-40 (holding that courts should enforce arbitration of Sherman Antitrust Act claims in international transactions); \textit{Gilmer}, 500 U.S. at 35 (holding that claims brought under the Age Discrimination in Employment Act are subject to binding arbitration).
\textsuperscript{18} \textit{McMahon}, 482 U.S. at 226-27.
\textsuperscript{19} \textit{Id.} at 227.
\textsuperscript{20} \textit{Gilmer}, 500 U.S. at 26 (quoting \textit{Moses H. Cone Mem'l Hosp.}, 460 U.S. at 24).
\textsuperscript{21} \textit{McMahon}, 482 U.S. at 227.
\textsuperscript{22} \textit{See H.R.Rep. No. 93-1107 (1974).}
deception, and improve competition in the marketing of consumer products … .” In addition to establishing standards governing the content of warranties, § 2310(d) of the MMWA provides a statutory private right of action to consumers who are “damaged by the failure of a supplier, warrantor, or service contractor to comply with any obligation under this chapter, or under a written warranty, implied warranty, or service contract . . . .” Before a consumer brings such a suit, however, the consumer must give the warrantor a reasonable opportunity to “cure” its failure to comply with the warranty issued to the consumer. If the warrantor does not “cure” the defect, then a consumer may bring suit under the MMWA in either federal or state court. And if the consumer prevails in the suit, they may recover “reasonably-incurred costs and expenses,” which importantly includes attorneys’ fees.

The MMWA also includes an alternative dispute resolution provision that encourages settlements by means other than civil lawsuits. Section 2310(a) allows a warrantor to include a provision in consumer contracts that requires the consumer to submit his/her warranty claim to an informal dispute settlement procedure before bringing a suit. Importantly, the MMWA does not define what an “informal dispute settlement procedure” is. Instead, the MMWA instructs the FTC to “prescribe rules setting forth minimum requirements for any informal dispute settlement procedure which is incorporated into the terms of a written warranty.” Of note, the MMWA only provides that if a § 2310(a) informal dispute settlement procedure is included in the warranty, then the dispute settlement procedure must comply with FTC requirements.

In accordance with the statute, the FTC promulgated Rule 703, setting the minimum requirements and some limitations for warrantors that include informal dispute settlement procedures in their warranties. Instead of using the term “informal dispute settlement procedure,” the FTC defined a “mechanism” as “an informal dispute settlement procedure which is incorporated into the terms of a written warranty to which any provision of Title I of the [MMWA] applies … .” Section 703.5(j) of the Code of Federal Regulations states that “[d]ecisions of the [informal dispute settlement mechanism] shall not be legally binding on any

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24 Id. § 2310(d)(1).
25 Id. § 2310(e).
26 Id.
27 Id. § 2310(d)(2).
28 Id. § 2310(a).
29 Id. § 2310(a)(3) (“resort to such procedure before pursuing any legal remedy under this section respecting such warranty, the consumer may not commence a civil action ... under subsection (d) of this section unless he initially resorts to such procedure....”); see also H.R.Rep. No. 93-1107 (1974) (“Congress declares it to be its policy to encourage warrantors to establish procedures whereby consumer disputes are fairly and expeditiously settled through informal dispute settlement mechanisms.”).
30 The MMWA is the only federal statute to use the exact term “informal dispute settlement procedure.” The Civil Rights Act of 1991 also includes an ADR provision, but it specifically calls out arbitration in its text. (“Where appropriate and to the extent authorized by law, the use of alternative means of dispute resolution, including ... arbitration, is encouraged to resolve disputes arising under the [1991] Acts or provisions of Federal law amended by this title.” Pub.L. No. 102-166, § 118, 105 Stat. 1071 (codified at Notes to 42 U.S.C. § 1981).
33 16 C.F.R. § 703.1(e)(2002).
If a consumer “is dissatisfied with [a Mechanism's] decision or warrantor's intended actions, or eventual performance,” the Rule states, then “legal remedies, including use of small claims court, may be pursued.”

The rule and accompanying discussion in the Federal Register explain how the FTC has interpreted the term “informal dispute resolution procedure” in order to cover binding arbitration. At the time of the rule’s original adoption in 1975, the FTC explained that the agency was prohibiting pre-dispute binding arbitration clauses from being included in warranties for two reasons. First, the FTC cited Congressional intent that the informal dispute settlement procedures not be legally binding, which arbitration is. Second, the FTC said that it did not believe “that any guidelines which it set out could ensure sufficient protection for consumers.”

The FTC was uncomfortable “develop[ing] guidelines for a system in which consumers would commit themselves, at the time of product purchase, to resolve any difficulties in a binding, but nonjudicial proceeding.” In 1999, when the FTC reevaluated the rule, it declined to allow warrantors to include binding arbitration terms in their warranties. The FTC reiterated the two points from above and once again promulgated a rule in which “reference within the written warranty to any binding, non-judicial remedy is prohibited.” The FTC cited Congress’s intent for informal dispute settlement procedures to be precursors to litigation and thus nonbinding. Therefore, according to the FTC, the inclusion of a pre-dispute binding arbitration clause would be directly counter to that intent.

C. Judicial Deference to Agency Interpretations: The Chevron Doctrine

Because the MMWA does not speak definitively to the issue of arbitrability and the FTC has issued a rule interpreting and implementing the statute that bars arbitration, we must now turn to administrative law to determine if the FAA preempts the MMWA under the McMahon test. In Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., the Supreme Court set out a two part test for determining whether administrative agencies’ interpretations are entitled to deference. The first step asks whether Congress has “directly spoken to the precise question at issue” in a way that renders its intention “clear” and “unambiguously expressed.” The courts must use

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34 16 C.F.R. § 703.5(j).
35 Id. at § 703.5(g).
36 40 Fed. Reg. 60168, 60211 (Dec. 31, 1975) (adding 16 C.F.R. § 703) (“[T]here is nothing in the Rule which precludes the use of any other remedies by the parties following a Mechanism decision.... However, reference within the written warranty to any binding, non-judicial remedy is prohibited by the Rule and the Act.”).
37 Id. Whether this description of arbitration is correct under current Supreme Court jurisprudence will be discussed in Part IV, infra.
38 Id. at § 700.8 (“A warrantor shall not indicate in any written warranty or service contract either directly or indirectly that the decision of the warrantor, service contractor, or any designated third party is final or binding in any dispute concerning the warranty or service contract.”)
39 FTC Explanation of Final Rule, supra note 7.
41 Id. at 842–44.
“traditional tools of statutory construction”\textsuperscript{42} to determine Congress’s intent. If the statute is clear and unambiguous, then the analysis is complete and Congress’s intent must be enforced.\textsuperscript{43} If, however, the “statute is silent or ambiguous with respect to the specific issue,” then courts proceed to the second step of the \textit{Chevron} analysis.

The second step asks whether an agency’s interpretation “is based on a permissible construction of the statute.”\textsuperscript{44} If Congress’s intent is not clear under the statute and if “Congress delegated authority to the agency generally to make rules carrying the force of law, and the agency interpretation claiming deference was promulgated in the exercise of that authority,”\textsuperscript{45} then the agency’s “reasonable construction” is entitled to deference.\textsuperscript{46}

Congress’s intent, then, becomes the controlling factor in determining whether the FAA preempts the MMWA. If Congress had a clear intention in creating informal dispute settlement mechanisms, then that intent will control. But if Congress was ambiguous in creating the informal dispute settlement mechanisms, then the FTC’s interpretation of the statute will be given deference so long as it was a “reasonable construction” of the statute. Both of these possibilities will be explored in Section IV of this essay as it is likely the Supreme Court could decide the case on either basis.

III. The Split

In 2002, the Fifth and Eleventh Circuits issued decisions that the FAA preempts the MMWA on the basis that the MMWA “does not evince a congressional intent to prevent the use of binding arbitration.”\textsuperscript{47} But in September 2011, the Ninth Circuit found that the FTC regulation described above was entitled to deference under \textit{Chevron}. The Ninth Circuit held that the FAA did not preempt the MMWA because the FTC’s interpretation of the term “informal dispute settlement mechanism” was a reasonable construction of the MMWA and that the FTC was properly enforcing Congressional intent.\textsuperscript{48} This section explores each of the three circuit court cases and their application of the laws described in Part II.

\textit{A. The Eleventh and Fifth Circuit Decisions}

\textit{1. Fifth Circuit: Walton v. Rose Mobile Homes LLC}

The Fifth Circuit took up the issue of FAA preemption of the MMWA in Walton v. Rose Mobile Homes, LLC. The Waltons purchased a Southern Energy Homes mobile home from Rose Mobile Homes, a retail seller, in early 1999.\textsuperscript{49} Southern Energy, the manufacturer, issued a

\textsuperscript{42} \textit{Id.} at 843 n. 9.
\textsuperscript{43} \textit{Id.} (“The judiciary is the final authority on issues of statutory construction and must reject administrative constructions which are contrary to clear congressional intent.... If a court, employing traditional tools of statutory construction, ascertains that Congress had an intention on the precise question at issue, that intention is the law and must be given effect.”).
\textsuperscript{44} \textit{Id.} at 843.
\textsuperscript{45} \textit{Mead}, 533 U.S. at 218.
\textsuperscript{46} \textit{Chevron}, 467 U.S. at 844.
\textsuperscript{47} \textit{Walton v. Rose Mobile Homes LLC}, 298 F.3d 470, 476 (5th Cir. 2002); \textit{Davis v. S. Energy Homes, Inc.}, 305 F.3d 1268, 1278 (11th Cir. 2002).
\textsuperscript{48} \textit{Kolev}, 658 F.3d at 1032.
\textsuperscript{49} \textit{Walton}, 298 F.3d at 471.
one-year manufacturer’s warranty against defects in materials and workmanship that included an arbitration provision requiring warranty claims to be submitted to binding arbitration.\textsuperscript{50} The Waltons’ mobile home had many defects, and though the Waltons gave Southern Energy and Rose opportunities to cure those defects, the Waltons were not satisfied with the repairs and revoked their acceptance of the mobile home. The Waltons brought several causes of action against Southern Energy and Rose in federal court, and both Southern Energy and Rose filed motions to compel arbitration. Neither the magistrate judge nor trial court compelled arbitration of the Walton’s MMWA claim, and Rose and Southern appealed to the Fifth Circuit.\textsuperscript{51}

The Fifth Circuit began by summarizing the FAA and the MMWA. The court noted that there is a presumption in favor of enforcing all arbitration agreements, even those requiring the arbitration of statutory claims.\textsuperscript{52} This presumption is one that can only be rebutted by a showing of Congressional intent to “preclude a waiver of judicial remedies for the statutory rights at issue.”\textsuperscript{53} The court then explained the three factors of the \textit{McMahon} test, which is used to determine Congress’s intent as to arbitrability of claims. The three factors are (1) the statute's text, (2) its legislative history, and (3) whether there is “an inherent conflict between arbitration and the statute's underlying purposes.”\textsuperscript{54} Next the court discussed the MMWA, explaining that the statute’s purpose was to protect consumers, to create federal standards for written warranties, and to create a statutory cause of action for consumers. The court also explored the MMWA’s provision that allowed warrantors to create informal dispute settlement procedures in accordance with the FTC’s standards set for such procedures. As discussed above, when the FTC promulgated its rule regarding informal dispute settlement procedures, it barred the use of binding arbitration provisions in written warranties.

In setting out its organization for the analysis of the FAA, the MMWA and the related FTC regulation, the court followed the \textit{Chevron} framework, first asking if Congress had spoken directly to the issue.\textsuperscript{55} The court conceded that binding arbitration is not mentioned in the text or legislative history of the statute. But the Fifth Circuit held that this silence did not mean that Congress was unclear with regard to the issue. Relying on the “liberal federal policy favoring arbitration” to show that Congress had expressed a clear intention in favor of arbitrating claims, the Court applied the \textit{McMahon} test to determine if “Congress expressed any contrary intent” in the MMWA.\textsuperscript{56}

The first factor in the \textit{McMahon} test is the text of the statute. The court noted that the MMWA does not address the availability of arbitration, and it does not delegate authority to the FTC to permit or ban arbitration of claims under the MMWA. The court went on to explain that though the MMWA does allow warrantors to create “informal dispute settlement mechanisms” and the FTC to create regulations governing the procedures, the MMWA does not define what those procedures are.\textsuperscript{57} The court did emphasize that the one thing the MMWA makes clear is that the procedures are “to be used \textit{before} filing a claim in court.”\textsuperscript{58} The court explained that this

\textsuperscript{50} \textit{Id.} Note that the written warranty was \textit{not} in compliance with the FTC’s Rule 703.

\textsuperscript{51} \textit{Walton,} 298 F.3d at 472.

\textsuperscript{52} \textit{Id.} at 473 (citing \textit{McMahon,} 482 U.S. at 226).

\textsuperscript{53} \textit{Id.}

\textsuperscript{54} \textit{Walton,} 298 F.3d at 474 (quoting \textit{McMahon,} 482 U.S. at 226).

\textsuperscript{55} \textit{Walton,} 298 F.3d at 475 (\textit{citing} \textit{Chevron,} 467 U.S. at 843).

\textsuperscript{56} \textit{Walton,} 298 F.3d at 475.

\textsuperscript{57} \textit{Id.}

\textsuperscript{58} \textit{Id.}
does not indicate that Congress intended to bar binding arbitration, however, because “binding arbitration generally is understood to be a substitute for filing a lawsuit, not a prerequisite.”

Next the court held that the creation of “informal dispute settlement procedures” in the MMWA does not preclude arbitration of MMWA claims. The court looked to Gilmer for this contention, explaining that despite the ADEA allowing the EEOC to pursue “informal methods of conciliation, conference, and persuasion,” compulsory arbitration of the claims was still permitted. The court reasoned from Gilmer that “the availability of informal methods of settling a dispute plainly does not itself preclude the availability of arbitration.” The court also quickly dismissed the MMWA’s creation of a judicial forum for MMWA claims as a basis for showing Congressional intent to prohibit arbitration.

Finally, the court discussed the terminology of the MMWA, noting that “binding arbitration is not normally considered to be an ‘informal dispute settlement procedure.’” As such, the court held that binding arbitration “seems to fall outside the bounds of the MMWA and of the FTC’s power to prescribe regulations.” For all the reasons set out above, the court held that the text of the MMWA evinced no intent to prohibit arbitration of claims under MMWA.

Next the court looked at the second factor from the McMahon test, the statute’s legislative history. The court noted that while the legislative history does not either specifically discuss arbitrability or define “informal dispute settlement procedure,” the legislative history “does indicate that such procedures were meant to be non-binding.” This information about Congress’s intent with regard to “informal dispute settlement procedures” did not persuade the court that Congress meant to ban binding arbitration of MMWA claims, however. The court found “no evidence” that Congress considered arbitration an informal dispute settlement procedure. Additionally, the court held that “the fact that any informal dispute settlement procedure must be non-binding, does not imply that Congress meant to preclude binding arbitration” because binding arbitration “is of a different nature.” The court went on to compare the legislative history of the MMWA to the legislative history in McMahon itself. Finding that there was more legislative history to support barring arbitration in McMahon than in the MMWA, the court held that the MMWA’s legislative history does not show that Congress intended to preclude arbitration of MMWA claims.

Lastly, the court looked to the MMWA’s stated purposes of “improving the adequacy of information available to consumers, prevent[ing] deception, and improv[ing] competition in the marketing of consumer products.” Given the Supreme Court’s holding in Allied–Bruce Terminix Cos. v. Dobson that arbitration is not inherently unfair to consumers, the court held that there was no “inherent conflict between arbitration and these purposes.” The court also

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59 Id.
60 Walton, 298 F.3d at 476 (citing 500 U.S. at 29 (internal citations omitted))
61 Walton, 298 F.3d at 476.
62 Id.
63 Id.
64 Id.
65 Id.
66 Walton, 298 F.3d at 476.
67 Id.
68 Id. at 477.
69 Id. (citing 15 U.S.C. § 2302(a)).
70 Walton, 298 F.3d at 478 See Allied–Bruce Terminix Cos. v. Dobson, 513 U.S. 265, 280 (1995) (“Congress, when enacting the [FAA], had the needs of consumers ... in mind.”).
dismissed the purpose espoused in the MMWA’s legislative history of rectifying the inequality in bargaining power between consumers and warrantors, explaining that differences in bargaining power does not support a blanket ban on arbitration of claims.

Since the court found that the text, legislative history, and purposes of the MMWA evince no contrary intent to the arbitrability of claims, the court found that Congress was clear in allowing arbitration of MMWA claims. Therefore, the Fifth Circuit did not reach the second prong of the *Chevron* analysis and held that the MMWA did not preclude binding arbitration clauses in written warranties or the arbitration of MMWA claims.

Chief Judge King dissented on the basis that the FTC’s interpretation of the statute was reasonable and that it was improper to look to a less specific, older statute to determine Congress’s intent in passing a more specific, more recent statute. Judge King found that “the text of the MMWA contains a conspicuous and significant ambiguity” surrounding the use of arbitration: it could prohibit the use of binding arbitration or it could not, which would result in a presumption of arbitrability applying. Judge King rejected the majority’s holding that because Congress did not specifically bar binding arbitration clauses that it intended to allow them. Because Judge King believed the FTC interpretation to be reasonable and entitled to deference, she would have held that binding arbitration clauses were prohibited in written warranties.


The Eleventh Circuit took up the issue in *Davis v. S. Energy Homes, Inc.*. The Davises bought a home constructed by Southern Energy Homes, Inc., in October 1999. The home’s written warranty contained a binding arbitration clause. Soon after purchasing the home, the Davises had several problems with the home and notified Southern Energy of the defects, but Southern Energy did not correct the defects to the Davises’ satisfaction. The Davises filed a claim in state court, which Southern Energy removed to Federal Court and moved to compel arbitration. The trial court denied Southern’s motion to compel arbitration, and Southern appealed to the Eleventh Circuit.

The court began its analysis of the issue with a brief summary of the applicable law. The court noted that the MMWA was passed as a consumer protection measure and that Congress wanted to encourage settlements of warranty issues. To achieve the goal of warranty issues being settled, Congress allows warrantors to include a provision requiring the use of informal dispute settlement procedures. Congress did not define what an informal dispute settlement mechanism was, however, and it delegated to the FTC the authority to make rules setting out requirements for those mechanisms. The court also noted that the MMWA requires consumers to

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72 *Walton*, 298 F.3d at 478.
73 *Id.*
74 *Id.*
75 *Id.* at 480.
76 *Id.*
77 *Walton*, 298 F.3d at 480.
78 *Davis*, 305 F.3d at 1270.
79 *Id.* at 1272.
“resort to such procedure before pursuing any legal remedy” so long as the informal dispute settlement mechanism conforms with the FTC’s requirements.

Next the court summarized the FAA, noting that “the Supreme Court has interpreted § 2 of the FAA as a Congressional declaration of a liberal federal policy favoring arbitration agreements.” The court then explained that there is no “statutory rights” exception to the rule that courts should enforce arbitration agreements according to their terms. The court noted that it might be possible for Congress to have intended for arbitration of statutory claims to be precluded, and applied the Supreme Court’s McMahon test.

The first factor in the McMahon test is the text of the statute at issue. The court noted that the MMWA does not expressly prohibit arbitration and does not reference either binding arbitration or the FAA anywhere. The court rejected the Davises’ contention that the MMWA strictly reserves a judicial forum for MMWA claims when it created a private right of action for consumers. The court properly rejected that argument, explaining that a statute's provision for a private right of action alone is inadequate to show that Congress intended to prohibit arbitration.

It went on to cite the Fifth Circuit’s decision in Walton that “binding arbitration generally is understood to be a substitute for filing a lawsuit, not a prerequisite.”

The court next rejected the Davises’ argument that §2310(a)’s requirement that informal dispute settlement mechanisms be a prerequisite to litigation meant that “Congress intended to allow only non-binding alternative dispute resolution procedures. The court rejected the Davises’ argument on the basis that “a statute's provision for one out-of-court settlement mechanism does not necessarily preclude the enforcement of all alternative mechanisms.”

The court then moved to the second McMahon factor, the statute’s legislative history, and found no evidence to support binding arbitration being considered an informal dispute settlement procedure. The court noted that the MMWA’s legislative history, like the text, does not specifically mention binding arbitration or the FAA, just internal dispute settlement procedures. The Davises pointed to the MMWA’s House Report as evidence that Congress did not intend to allow arbitration of MMWA claims. The House Report stated that “[a]n adverse decision in any informal dispute settlement proceeding would not be a bar to a civil action on the warranty involved in the proceeding.” The court did not find this legislative history persuasive, saying that the MMWA’s legislative history is “ambiguous at most.” As a counterpoint to the House report, the court referred to a Senate report on an early draft of the MMWA that does mention arbitration specifically. The Senate Report said that “it is Congress' intent that warrantors of consumer products cooperate with government and private agencies to establish informal dispute

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81 Davis, 305 F.3d at 1273 (citing Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24, (1983)).
82 Davis, 305 F.3d at 1273.
83 Id. at 1274 (citing Gilmer, 500 U.S. at 29.).
84 Davis, 305 F.3d at 1274 (citing Walton, 298 F.3d at 475.).
85 Davis, 305 F.3d at 1275.
86 Id. (citing Cunningham v. Fleetwood Homes of Ga., Inc., 253 F.3d 611, 620 (11th Cir. 2001)).
87 Davis, 305 F.3d at 1276.
88 Id. at 1275 (citing H.R.Rep. No. 93-1107 (1974)).
89 Davis, 305 F.3d at 1276.
settlement mechanisms that take care of consumer grievances without the aid of litigation or formal arbitration."\(^{90}\)

The court then went on to compare the legislative history of the MMWA to the legislative history of the Securities Exchange Act of 1934, the statute at issue in \textit{McMahon}.\(^{91}\) The court noted that the legislative history of the Securities Exchange Act of 1934 seemed to actually take the position that arbitration is not an adequate forum for statutory claims.\(^{92}\) Because the legislative history of the MMWA is “considerably less clear than the legislative history of the Securities Exchange Act of 1934,” the court held that there was no “clear congressional intent to prohibit binding arbitration of MMWA claims."\(^{93}\)

Next the court analyzed the purposes of the MMWA and concluded that arbitrating MMWA claims would not frustrate any of the three stated purposes of the Act. The stated purposes are “to improve the adequacy of information available to consumers, prevent deception, and improve competition in the marketing of consumer products.”\(^{94}\) The court looked to the Supreme Court’s repeated holding that arbitration is not antithetical to consumer protection and that statutory claims can be arbitrated when the purpose of a statute is protecting and informing consumers.\(^{95}\) Because “consumers can adequately vindicate their rights arising under the MMWA and written warranties in an arbitral forum,” the court found that the purposes of the MMWA do not express a clear intent to bar binding arbitration of warranty claims.\(^{96}\)

The court also briefly touched on the MMWA’s undeclared purpose of rectifying the unequal bargaining power between warrantors and consumers. The court also rejected this purpose as preventing the inclusion of binding arbitration agreements in warranties because “unequal bargaining power alone, however, is not a sufficient reason to never enforce an arbitration agreement of a statutory claim.” Because unequal bargaining power requires a case-by-case analysis, this purpose does “does not create such a conflict with the FAA so as to prohibit binding arbitration of MMWA claims."\(^{97}\)

Having determined that statutory claims under the MMWA can be arbitrated under the \textit{McMahon} test, the court then turned to the question of whether the FTC regulations barring the inclusion of binding arbitration clauses in written warranties was entitled to deference. The court reiterated that Congress did not directly address binding arbitration anywhere in the text or legislative history of the MMWA.\(^{98}\) Because of this silence and the inclusion of a delegation to the FTC to define what “informal dispute settlement procedures” are, the court found that Congress was unclear and went on to determine if the FTC’s interpretation of the MMWA was reasonable.\(^{99}\)

To determine whether the FTC’s Rule 703 is reasonable, the court looked to the FTC’s rationale for interpreting the statute so that it bars the inclusion of binding arbitration clauses in

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\(^{90}\) Id. (citing S.Rep. No. 91-876, at 22-23 (1970) (emphasis added)).

\(^{91}\) \textit{Davis}, 305 F.3d at 1276.

\(^{92}\) Id. (citing \textit{McMahon}, 482 U.S. at 238 (NEED A QUOTE??)).

\(^{93}\) Id.


\(^{95}\) \textit{Davis}, 305 F.3d at 1276.

\(^{96}\) Id.

\(^{97}\) Id. at 1277.

\(^{98}\) Id. at 1278.

\(^{99}\) Id.
written warranties.\textsuperscript{100} First the court explained that “the FTC reasoned that a decision regarding the warranty dispute may not be binding because ‘section 110(d) of the Act gives state and federal courts jurisdiction over suits for breach of warranty and service contracts.’ ”\textsuperscript{101} As it did when discussing the text of the MMWA in its analysis for the first \textit{McMahon} factor, the court rejected this interpretation of the MMWA prohibiting arbitration as unreasonable.\textsuperscript{102} Specifically, the court said that “the FTC’s motive behind the legislative regulation is contradictory to Supreme Court rationale, and we conclude that its interpretation is unreasonable.\textsuperscript{103}

The court then went on to cite the FTC’s skepticism of arbitral forums being able to offer consumers sufficient protection as an invalid reason for barring binding arbitration clauses in written warranties.\textsuperscript{104} Looking to the Supreme Court’s holding that “arbitration is favorable to the individual,”\textsuperscript{105} the court found that the FTC’s hostility toward arbitration was unreasonable in the face of recent Supreme Court jurisprudence and therefore “based on an impermissible construction of the statute.”\textsuperscript{106}

\textbf{B. Ninth Circuit: Kolev v. Euromotors West/The Auto Gallery}

Diana Kolev purchased a used car that developed “serious mechanical problems” while it was under warranty and the dealership she purchased the car from refused to honor those warranty claims.\textsuperscript{107} She brought suit under the MMWA.\textsuperscript{108} The district court granted the defendant’s motion to compel arbitration.\textsuperscript{109} After the arbitration, Kolev appealed the decision to the Ninth Circuit who reviewed the motion \textit{de novo}.

Like the Fifth Circuit, the court began its analysis of the relevant law by setting out the \textit{Chevron} test for deference to agency interpretations of statutes.\textsuperscript{110} The court “agree[d] with the Fifth Circuit that ‘[t]he text of the MMWA does not specifically address binding arbitration.’ ”\textsuperscript{111} Unlike the Fifth Circuit, the Ninth Circuit did not inquire further into Congress’s intent by applying the \textit{McMahon} test and instead moved directly into asking whether the FTC’s construction of the statute was reasonable.

The court noted that Congress expressly delegated rulemaking authority to the FTC to “prescribe rules setting forth minimum requirements for any informal dispute settlement procedure which is incorporated into the terms of a written warranty.”\textsuperscript{112}

The court gave three reasons for the reasonableness of the FTC’s rule. First, the court noted that based on the MMWA’s legislative history, the FTC was trying to effectuate

\begin{itemize}
\item[\textsuperscript{100}] \textit{Id.}
\item[\textsuperscript{101}] \textit{Davis, 305 F.3d at 1278 (quoting 16 C.F.R. § 700.8 (2002)).}
\item[\textsuperscript{102}] \textit{Davis, 305 F.3d at 1279.}
\item[\textsuperscript{103}] \textit{Id.}
\item[\textsuperscript{104}] \textit{Id. at 1278–79. See supra Part II.B.}
\item[\textsuperscript{105}] \textit{Davis, 305 F.3d at 1279 (quoting Allied-Bruce Terminix Cos., 513 U.S. at 279, 115 S.Ct. at 842-43 (noting that “arbitration's advantages often would seem helpful to individuals, say, complaining about a product, who need a less expensive alternative to litigation.”)).}
\item[\textsuperscript{106}] \textit{Davis, 305 F.3d at 1280.}
\item[\textsuperscript{107}] \textit{Kolev, 658 F.3d at 1025.}
\item[\textsuperscript{108}] \textit{Id.}
\item[\textsuperscript{109}] \textit{Id.}
\item[\textsuperscript{110}] \textit{Id.}
\item[\textsuperscript{111}] \textit{Id. at 1026 (citing Walton, 298 F.3d at 475).}
\item[\textsuperscript{112}] \textit{Kolev, 658 F.3d at 1026 (citing 15 U.S.C. § 2310(a)(2)).}
\end{itemize}
Congress's intent. The court pointed to the FTC’s reliance on a House Subcommittee Staff Report (now unavailable) in making its determination that “Congressional intent was that decisions of Section 110 Mechanisms not be legally binding.”\footnote{Kolev, 658 F.3d at 1027 (citing 40 Fed.Reg. at 60210).} Second, the court believed that FTC’s interpretation “advances the statute's purpose of protecting consumers from being forced into involuntary agreements that they cannot negotiate.” The court found that because the FTC did not believe that any guidelines it set regarding binding arbitration would sufficiently protect consumers and an underlying purpose of the MMWA was consumer protection that the interpretation was reasonable.\footnote{Kolev, 658 F.3d at 1028} Third, the court accorded the FTC’s regulation with particular deference as it is a “longstanding, consistent interpretation of the statute.”\footnote{Id. at 1029.} The court supported its reasoning by citing that the regulation has stood for 35 years and was affirmed 25 years after it was first promulgated.\footnote{Id. at 1030.}

Then the court went on to “reject the argument that the FTC's construction is unreasonable in light of the Supreme Court's repeated holdings that Congress established a “liberal federal policy favoring arbitration agreements”\footnote{Id. at 1026 (quoting Walton, 298 F.3d at 483 (King, C.J., dissenting)).}

First, the court challenged the Fifth and Eleventh Circuits’ interpretation of Congress’s intent, noting that “it is unprecedented to locate Congress's intent with respect to one statute by looking to ‘a prior, less specific statute.’ ”\footnote{Id. at 1028 (quoting Walton, 298 F.3d at 490 (King, C.J., dissenting)).} The court also noted that the FAA only created a rebuttable presumption in favor of arbitration. As such, the court said that the Fifth Circuit erred in holding that the liberal federal policy favoring arbitration meant that Congress expressed a clear intent as to whether pre-dispute mandatory binding arbitration provisions are enforceable under the MMWA.\footnote{Kolev, 658 F.3d at 1030–31.}

Second, the court believed that the FTC’s interpretation of the MMWA was reasonable even though the regulation was reaffirmed 12 years after McMahon set forth a rebuttable presumption in favor of enforcing arbitration agreements.\footnote{Id. at 1030.} The court agreed that “the “FTC's longstanding interpretation of the statute … and that the MMWA evinces a ‘contrary congressional command’ sufficient to override the FAA's presumption in favor of arbitration.”\footnote{Id. (quoting McMahon, 482 U.S. at 226).} The court went on to note that what is more important than its agreement with the FTC is that the court is bound by the FTC’s decision under Chevron.\footnote{Kolev, 658 F.3d at 1030.}

Finally, the court held that the MMWA is “different in four critical respects from every other federal statute that the Supreme Court has found does not rebut the FAA's pro-arbitration presumption... .”\footnote{Id. (citing 15 U.S.C. § 2310(a)(2)).} The court noted first that the other four statutes did not have authorized agency interpretations.\footnote{Kolev, 658 F.3d at 1030.} Second, the court explained that the MMWA is the only statute in which Congress discussed informal, non-judicial remedies “in a way that would bar binding procedures such as mandatory arbitration.”\footnote{Id. (citing 15 U.S.C. § 2310(a)(2)).} Third, the MMWA is also the only statute in which
Congress explicitly preserved consumers’ rights to bring claims in court after the use of informal dispute settlement mechanisms.\(^{126}\) Lastly, the MMWA alone had a primary purpose of protecting consumers “by prohibiting vendors from imposing binding, non-judicial remedies.” The court noted that this purpose is in direct contrast to the Supreme Court’s own statement of the principal purpose of the FAA, “to ensure the enforcement of arbitration agreements according to their terms so as to facilitate streamlined proceedings.”\(^{127}\)

Of note, Judge Reinhardt may have a bias against pre-dispute arbitration clauses.\(^{128}\) In 1998, he authored \textit{Duffield v. Robertson Stephens & Co.}, a decision in which the Ninth Circuit held that Congress intended to prohibit binding arbitration of claims under the Civil Rights Act of 1991.\(^{129}\) Five years later in an \textit{en banc} decision, the Ninth Circuit explicitly overruled \textit{Duffield} as it was wrongly decided.\(^{130}\)

Judge Smith dissented from the opinion on the basis that the majority improperly relies on the supposition that informal dispute settlement procedures include arbitration and that Congress intended for the MMWA to prohibit arbitration.\(^{131}\) Reversing those assumptions, as they were in the Fifth and Eleventh Circuits, Judge Smith would hold that the FTC’s rule is not entitled to deference.\(^{132}\) Because prohibiting arbitration of MMWA claims would be “incompatible with the clear federal policy favoring arbitration under the Arbitration Act,” arbitration of MMWA claims must be permitted.\(^{133}\)

IV. HOW THE SUPREME COURT WOULD HOLD

The Supreme Court will almost certainly overturn the Ninth Circuit’s decision and hold that claims under the MMWA can be arbitrated and that the FTC’s Rule 703 is not a reasonable interpretation of the FAA. The Court could overturn the Ninth Circuit using several rationales. The court could simply look to the text of the MMWA and determine that Congress’s clearly did not intent for arbitration to be included within the term “informal dispute settlement procedures.” The Court could adopt the Fifth Circuit’s approach and find that given the strong federal policy favoring arbitration and Congress’s lack of a clear intent to bar arbitration, claims under MMWA can be arbitrated.\(^{134}\) Alternatively, the Court might adopt the Eleventh Circuit’s reasoning, finding that while Congress did not speak to the issue of binding arbitration, the FTC’s construction of the statute is unreasonable.\(^{135}\)

Though the simplest of the ways the Court might handle the issue presented, the Court might very well choose to simply find that the MMWA’s text was clear and that arbitration is not an “informal dispute settlement procedure” and thus is not subject to the FTC’s regulation. Not only is it a simple holding, it is a credible construction of the law. First, though the Court has


\(^{127}\) \textit{Kolev}, 658 F.3d at 1031 (\textit{quoting Concepcion}, 131 S.Ct. at 1748).

\(^{128}\) See \textit{Duffield v. Robertson Stephens & Co.}, 144 F.3d 1182, 1199 (9th Cir. 1998).

\(^{129}\) \textit{Id. See supra}, note 30 for the relevant text of the statute.

\(^{130}\) \textit{E.E.O.C. v. Luce, Forward, Hamilton & Scripps}, 345 F.3d 742, 745 (9th Cir. 2003).

\(^{131}\) \textit{Kolev}, 658 F.3d at 1032–34.

\(^{132}\) \textit{Id. at 1038}.

\(^{133}\) \textit{Id.}

\(^{134}\) See \textit{Walton}, 298 F.3d at 470; \textit{supra}, Part IIA.

\(^{135}\) See \textit{Davis}, 305 F.3d 1268; \textit{supra}, Part IIB.
previously lauded arbitration for its relative informality,\(^\text{136}\) the term “informal dispute settlement procedures” does not immediately call arbitration to mind. It is far more likely to make one think of mediation or some other nonbinding procedure. Second, the Court will focus on the MMWA’s provision that “the consumer may not commence a civil action (other than a class action) under subsection (d) of this section unless he initially resorts to such procedure.”\(^\text{137}\) But as the Fifth Circuit correctly noted in *Walton*, “binding arbitration generally is understood to be a substitute for filing a lawsuit, not a prerequisite.”\(^\text{138}\) Therefore, including arbitration within the category of “informal dispute settlement procedures” is clearly inconsistent with the Court and Congress’s understanding of what arbitration is.\(^\text{139}\)

Finally, if the Court looks to the MMWA’s legislative history, they will have further ammunition with which to discredit the notion that arbitration should be considered an “informal dispute settlement mechanism.” The House Report stated that “an adverse decision in any informal dispute settlement proceeding would not be a bar to a civil action on the warranty involved in the proceeding.”\(^\text{140}\) Because binding arbitration has such limited review under the FAA, Congress cannot have contemplated including it within the definition of an “informal dispute settlement procedure. In fact, the legislative history explicitly allows binding arbitration. In discussing the reasons for limiting class actions under the MMWA, twelve members of Congress expressed their belief that “[Warranty disputes] matters can be more promptly and effectively resolved through such techniques as more efficient small claims courts, neighborhood courts, binding consumer arbitration, voluntary settlement mechanisms, and improved enforcement agencies.”\(^\text{141}\)

In sum, the Court has a strong basis for simply holding that arbitration is not an “informal dispute settlement mechanism” and not engaging in the *McMahon* analysis that the Fifth and Eleventh Circuit’s reasoning requires. By holding that Congress was clear in not including arbitration within the definition of an “informal dispute settlement mechanism,” the FTC’s Rule prohibiting arbitration will be void and MMWA claims can be arbitrated.\(^\text{142}\)

The Court could still choose to adopt either the Fifth or the Eleventh’s reasoning as well. In brief summary, the Fifth Circuit used the *McMahon* test to see if Congress intended to

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\(^{136}\) *See Concepcion*, 131 S. Ct. at 1749 (citing 14 Penn Plaza LLC v. Pyett, 129 S.Ct. 1456, 1460, (2009)) (“The informality of arbitral proceedings is itself desirable, reducing the cost and increasing the speed of dispute resolution.”).


\(^{138}\) *Walton*, 298 F.3d at 475 (citing *Mitsubishi Motors* 473 U.S. at 628 (“By 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.”)).

\(^{139}\) Though *Mitsubishi Motors* was decided 10 years after the MMWA was passed, this would hardly be the first time the Court imputed its later interpretation onto a statute passed before that interpretation came into effect. *See Gilmer*, 500 U.S. at 35, for an example of the Court imputing a later understanding of arbitrability onto a statute passed half a decade earlier.

\(^{140}\) *HOUSE REP. NO. 93-1107* (1974) at 41.

\(^{141}\) *Id.* (emphasis added). *See also* S.Rep. No. 91-876, at 22-23 (1970) (a Senate report of an early draft of the MMWA stating “it is Congress' intent that warrantors of consumer products cooperate with government and private agencies to establish informal dispute settlement mechanisms that take care of consumer grievances without the aid of litigation or formal arbitration.”) (emphasis added).

\(^{142}\) *Chevron*, 467 U.S. at 842-43 (“If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.”).
preclude arbitration in the MMWA.143 Because the court found no intent to preclude arbitration, it held that the presumption of arbitrability of statutory claims was not rebutted.144 While the Fifth Circuit’s reasoning might be alluring, the criticisms that Judge King levied are not immaterial. Her contention that “the majority bases its conclusion that Congress has “directly spoken to the precise question” of how to interpret § 2310 of the MMWA on a general policy expressed in a prior, less specific statute” is accurate.145 She contends that the logic is circular and that “it is inappropriate to apply the presumption in ascertaining whether the statute in question contains such a command.”146 Judge King goes on to criticize the majority for ignoring a statutory ambiguity on the basis of what “arbitration” normally means.147 Given these weaknesses in the Fifth Circuit’s legal reasoning, the Court is not likely to adopt this reasoning.

On the other hand, the Eleventh Circuit’s reasoning is most in line with the Court’s jurisprudence, both on the FAA and in conducting a classic Chevron analysis. The Eleventh Circuit treated the issue as a classic Chevron problem.148 The court looked to the FAA and the text and legislative history of the MMWA to determine that Congress did not speak clearly to the issue of binding arbitration.149 As such it then considered whether the FTC’s construction was reasonable. After analyzing the text of the MMWA, its legislative history and the FTC’s reasoning for its interpretation, the court held that the FTC’s interpretation was not based on a permissible construction of the MMWA.150 This reasoning is the least controversial as it takes every opportunity to prohibit arbitration of consumer claims, which is growing more controversial as arbitration becomes more widespread.151

The Court should either find that the MMWA clearly adopt the Eleventh Circuit’s reasoning or simply hold that the MMWA is clear and allows arbitration on its face. If it chooses the latter it should not adopt the Fifth Circuit’s reasoning but simply stick to the text of the statute. While the way that the Court will get to its holding may not be clear, it is clear that the Court will overturn the Ninth Circuit.

143 Walton, 298 U.S. at 473.
144 Id. at 474.
145 Id. at 483.
146 Id. at 484.
147 Id. This criticism can also be levied at the Court choosing to simply hold that the MMWA is clear and unambiguous on its face.
148 Davis, 305 F.3d at 1277–78.
149 Id. at 1274–77.
150 Id. at 1278–79.