EXHIBIT 1
DATE 3-9-05
SB 165

RILEY

MEMORANDUM

TO: Tony Colletti; Jabo Covert; Lauren Hosie

FROM: Greg Madson

DATE: August 28, 2004

RE: Montana Deferred Deposit Loan Act
Amendments Related to Arbitration

Current Law Conflicts with FAA

The Montana Deferred Deposit Loan Act, at MCA 31-1-723(20), currently prohibits "including any of the following provisions in the loan agreement required by 31-1-721: ...

(c) a waiver of the right to a jury trial, if applicable, in any action brought by or against a consumer;

(d) a mandatory arbitration clause; ...."

Both of these provisions conflict with the Federal Arbitration Act (FAA), and both should be stricken from the Montana Deferred Deposit Loan Act.

FAA's Preemption of State Arbitration Prohibitions

A long line of decisions by the United States Supreme Court holds that the FAA preempts state laws which single out and invalidate arbitration agreements. See, for example, *Doctor's Associates, Inc. v. Casarotto*, 116 S.Ct. 1652, 1656 (1996) and *Allied-Bruce Terminix Companies, Inc. v. Dobson*, 115 S.Ct. 834, 839 (1995). These cases hold that the FAA removes state power to require a judicial forum when parties choose arbitration.

Congress passed the FAA in the 1920s, seeking to put arbitration provisions on "the same footing" as a contract's other terms. *Scherk v. Alberto-Culver Co.*, 94 S.Ct. 2449, 2453 (1974), citing H.R.Rep.No.96, 68th Cong., 1st Sess., 1, 2 (1924); *see also* S.Rep.No.536, 68th Cong., 1st Sess. (1924). The FAA was intended to ensure "that private agreements to arbitrate are enforced according to their terms." *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University*, 109 S.Ct. 1248, 1256 (1996).

In 1984 and again in 1987, the United States Supreme Court ruled that "...the Act does displace state law to the contrary." *Southland Corp. v. Keating*, 104 S.Ct. 852, 859 (1984) and *Perry v. Thomas*, 107 S.Ct. 2520, 2525 (1987). So by the 1980s, the United States Supreme Court had clearly mandated that (1) the FAA preempts contrary state law and (2) states cannot mandate policy that invalidates arbitration agreements. *Southland Corp.*, 104 S.Ct. 852, 858 (1984).

In 1995, the United States Supreme Court reaffirmed its previous ruling. Once again, the court ruled that the FAA preempts contrary state law and state courts cannot apply state statutes

that invalidate arbitration agreements. *Allied-Bruce Terminix Companies, Inc.*, 115 S.Ct. 834, 838 (1995) reaffirming *Southland Corp.*, 104 S.Ct. 852, 852 (1984).

In *Doctor's Assoc.*, 116 S.Ct. 1652, 1657 (1996), the Court applied these same principals to invalidate a Montana law that had singled our arbitration agreements, much as the current Montana Deferred Deposit Loan Law singles out arbitration agreements. In an 8-1 ruling, the United States Supreme Court struck down a Montana law that singled out arbitration agreements for stricter scrutiny than other contracts. That law required that arbitration agreements be printed on the first page of an agreement in underlined capital letters. That law only created special notice requirements for arbitration agreements, while the current Montana Deferred Deposit Loan Law goes much farther by banning arbitration agreements altogether. Nonetheless, the Supreme Court held that that law violated the FAA.

In striking down that Montana law, the Court wrote:

> The "goals and policies" of the FAA, this Court's precedent indicates, are antithetical to threshold limitations placed specifically and solely on arbitration provisions. Section 2 "mandate[s] the enforcement of arbitration agreements," *Southland*, 465 U.S., at 10, 104 S.Ct., at 858, "save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. Section 27-5-114(4) of Montana's law places arbitration agreements in a class apart from "any contract," and singularly limits their validity. The State's prescription is thus inconsistent with, and is therefore preempted by, the federal law.

Doctor's Assoc., 116 S.Ct. 1652, 1657 (1996). Thus, federal law, as enunciated by the United States Supreme Court and Congress, unmistakably prohibits states from "singling out and restricting arbitration agreements." Arbitration agreements may only be invalidated for the same reasons that any other contract may be invalidated (fraud, unconscionability, duress, etc.).

FAA is to be Broadly Interpreted

The Supreme Court has repeatedly addressed the importance of broadly interpreting the FAA. In *Allied-Bruce Terminix Companies, Inc.* the Court stated, "...a broad interpretation of this language is consistent with the Act's basic purpose, to put arbitration provisions on the same 'footing' as a contract's other terms." *Allied-Bruce Terminix Companies, Inc.*, 115 S.Ct. at 840 (1995), *citing Scherk*, 94 S.Ct. 2449, 2453 (1974). Likewise, the Court has ruled that "State attempts at narrowing Congress's arbitration policy are 'not consistent with the Act's purpose.'" *Allied-Bruce Terminix Companies, Inc.*, 115 S.Ct. at 840 (1995). The Court noted that these attempts were "unnecessarily complicating the law and breeding litigation from a statute that seeks to avoid it." *id.*

Waiver of Jury Trial; Procedural Rights v. Substantive Rights

Note, however, that not all arbitration agreements are enforceable under the FAA. When parties agree to arbitrate they agree to have their disputes settled in a different forum and by a different set of rules. Courts have consistently upheld arbitration agreements in which the parties

agree to limit these procedural rights. But courts do not typically uphold arbitration agreements in which the parties agree to limit their substantive rights and remedies.

For example, "TILA [Truth in Lending Act] does not create a substantive right to a class action. While '[i]t is true that compelling arbitration ... will eliminate a plaintiff's ability to arbitrate his claims on behalf of a class ... this result is required because Congress has not created a statutory right to bring class actions under TILA. ... In agreeing to arbitrate, plaintiffs did not sign away their ability to pursue substantive rights under TILA, but only their ability to use the procedural device of the class action in a judicial forum." *Thompson v. Illinois Title Loans, Inc.*, 2000 WL 45493, *3 (N.D. Ill.) (citing *Lopez*, 1996 WL 210073, at *3; *Gilmer*, 500 U.S. at 26; and *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985)) (emphasis added).

Similarly, and importantly for this issue, courts have consistently held that the right to a jury trial in a civil case is a procedural right, not a substantive right, and may be waived by executing an arbitration agreement. In fact, courts around the country have consistently upheld jury trial waivers that are materially identical to the Waiver of Jury Trial and Arbitration Agreement that Check into Cash of Montana, LLC desires to use in its Montana stores. *See, for example, Aimee Jump v. Creditcorp of Indiana, Inc., et al.*, No. 3:01CV0806AS (N.D. Ind. March 19, 2002); *Kingston v. McKenzie Check Advance of Indiana, Inc.*, 2001 WL 238129 (S.D. Ind. Jan. 3, 2001); *Dienese, et al. v. McKenzie Check Advance of Wisconsin, LLC, et al.*, U.S.D.C. E.D. Wis. Case No. 98-C-50 (Dec. 11, 2001); *Ballard, et al. v. First American Cash Advance of Arkansas, LLC, et al.*, U.S.D.C. W.D. Ark. Case No. CIV-2001-130-4 (Feb. 6, 2002).