Consumers Want to be in Europe; Corporations Want to be in the U.S.: How to Reform Mandatory Consumer Arbitration Agreements to be Fair to Both Parties

Kelly Parfitt
# TABLE OF CONTENTS

I. Introduction .......................................................................................................................... 3

II. Background .......................................................................................................................... 5

   A. Consumer arbitration development in the United States. ........................................... 5
   B. The European system focuses on consumer protection. ............................................. 8

III. Analysis ............................................................................................................................. 14

   A. These agreements are unfair to consumers. .............................................................. 14
      1. These agreements are nonconsensual and consumers are usually unaware of them
         ........................................................................................................................................... 15
      2. Mandatory arbitration agreements are written in the drafter’s favor, not the
         consumers’ ................................................................................................................ 15
      3. Arbitration providers and arbitrators are not required to give the same rights to a
         consumer as they would have in a courtroom with a judge.............................................. 16
   B. The costs of arbitration outweigh any benefits ......................................................... 20
      1. Fees charged by the leading arbitration providers are not less expensive .......... 20
      2. Challenging the agreement as cost-prohibitive is difficult without knowing the
         costs before it begins......................................................................................................... 22
      3. Forcing arbitration instead of litigation is only less expensive for businesses...... 25
   C. Current pending legislation banning mandatory arbitration would only
      exacerbate the problem ................................................................................................. 26
      1. Banning these agreements causes more problems than it would solve. ............... 26
      2. The business world cannot afford to litigate every dispute, but the system needs to
         be reformed to be similar to the European model....................................................... 27
IV. Conclusion
Consumers Want to be in Europe; Corporations Want to be in the U.S.: How to Reform Mandatory Consumer Arbitration Agreements to be Fair to Both Parties

Kelly Parfitt

I. Introduction

Arbitration is supposed to involve similarly situated disputants in terms of bargaining power, wealth, background, and expectations. Arbitration agreements between businesses or merchants were usually negotiated as part of the contract or accepted as an industry standard. These agreements did not need much government or judicial regulation. The Federal Arbitration Act (FAA) was adopted in 1925 and required courts to enforce pre-dispute arbitration agreements in contracts between businesses. Pre-dispute arbitration agreements were rarely enforced against consumers.

In the 1980’s, the attitude toward these agreements changed abruptly. The new Supreme Court held in a series of decisions that arbitration between businesses and consumers was “favored” and rejected public policy claims that certain categories of cases were non-arbitrable. This led many companies to require their customers to arbitrate instead of filing a claim in court.

Now, a consumer cannot get a credit card, bank account or mortgage, insurance, health care, or purchase products without agreeing to give up their right to a trial. Instead
they are forced to arbitrate any disputes. More importantly, most people are unaware they gave up their rights as these agreements are usually written in small print in a contract, envelope stuffer, warranty, application form or receipt. A normal contract that included an arbitration agreement would have to be signed by both parties to be enforceable. Section Two of the Federal Arbitration Act only requires that the arbitration agreement be written but does not require it to be signed to be enforceable. These agreements “essentially provide for more limited discovery, less formal rules of evidence, and virtually no opportunity to reverse or vacate an erroneous decision.” One critic has said that they are “the single biggest threat to consumer rights in recent years.”

This article is an analysis of how mandatory consumer arbitration agreements are treated in the U.S. and Europe, and how the American system needs to be reformed. The first part of this article discusses the progression of consumer arbitration and how the use of these mandatory consumer arbitration agreements became widespread throughout American businesses. The second part of this article analyzes how the many disadvantages of these agreements affect consumers and their rights. The third part of this article discusses current legislation pending in the U.S. Congress, and how banning these agreements will not solve the underlying problems. The last part of the paper will

9 Id.
10 Id. at 834-35.
12 Id. at 127.
14 See STERNLIGHT, ARBITRATION LAW, supra note 11, at 127.
discuss a regulatory solution to balance consumer rights and businesses interests in a stream-lined and less expensive process for consumer disputes. Mandatory pre-dispute agreements forced on consumers need to be reformed because they are unfair to consumers, take away their substantives rights, are too expensive and the results of the arbitrations are overwhelmingly slanted in the corporate direction. This new system will make arbitration a fair and cost-effective solution to both consumers and corporations, while offering a way to get back to court if necessary.

II. Background

A. Consumer arbitration development in the United States.

By using arbitration, we “close off access to proceedings, eliminat[e] judicial precedent, allow[] parties to write their own laws, [and] we compromise society’s role in setting the terms of justice”. 15 Companies in the U.S. are using mandatory consumer arbitration agreements in contracts of adhesion to force consumers to give up their right to a trial and instead try to get relief through arbitration. 16 It is virtually impossible to buy goods or even services in the U.S. without being subject to one of these agreements. 17 Arbitration was originally intended only for sophisticated merchants but the Federal Arbitration Act did not state that it applied only to businesses. 18 Later, the United States Supreme Court determined Congress had intended it to apply to everyone when they

18 Id. at 265.
stated that “Congress, when enacting [the FAA], had the needs of consumers, as well as
other[s], in mind.”19 This widening of arbitration to reach ordinary consumers is because
of the “United States Supreme Court rulings that have made arbitration agreements nearly
impossible to challenge as contracts.”20 The FAA virtually always applies because it
applies to all transactions involving interstate commerce.21 States may restrict or prohibit
these types of arbitration agreements, but very few cases are not preempted by the FAA.22
The prevailing opinion from the Supreme Court is that everyone wins by referring
disputes to arbitration.23 Consumer rights groups and legal scholars would dispute that
assertion.24

Critics have said that these are adhesion contracts, meaning a “standard form
contract prepared by one party, to be signed by the party in a weaker position . . . a
consumer, who has little choice about the terms.”25 The Seventh Circuit Court held the
fact that the terms were unilaterally imposed and not subject to negotiation did not affect
the validity of the arbitral agreements.26 The Court concluded that the Federal

19 Christopher R. Drahozal & Raymond J. Friel, Consumer Arbitration in the European Union and the
Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265, 280 (1995)).
21 Shelly Smith, Mandatory Arbitration Clauses in Consumer Contracts: Consumer Protection and the
Circumvention of the Judicial System, 50 DEPAUL L. REV. 1191, 1221 (2001) [hereinafter Smith, Consumer
Protection] (citing Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265, 278 (1995)).
22 See F. PAUL BLAND, JR., LESLIE A. BAILEY, MICHAEL J. QUIRK, RICHARD H. FRANKEL & JONATHAN
SHELDON, CONSUMER ARBITRATION AGREEMENTS: ENFORCEABILITY AND OTHER TOPICS 43 (5th ed. 2007)
[hereinafter BLAND, CONSUMER ARBITRATION].
23 See Harris, 183 F.3d at 173.
24 See Sarah E. Larson, An Examination of the Broad Scope of the Federal Arbitration Act and Binding
Mandatory Consumer Agreements: Not the Answer to Racial Bias in the United States Legal System, 24
HAMLINE J. PUB. L. & POL’Y 293, 317 (2003); Sternlight, Panacea, supra note 15, at 695;
Drahozal & Friel, Consumer Arbitration, supra note 19, at 374-75.
25 BLACK’S LAW DICTIONARY 139 (8th ed. 2007).
26 See CARBONNEAU, PRACTICE OF ARBITRATION, supra note 17, at 265-66; Hill v. Gateway, 105 F.3d 1147
(7th Cir. 1996), cert denied, 522 U.S. 808 (1997), (citing ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir.
1996)).
Arbitration Act did not require arbitration agreements to be prominently displayed in order to be enforceable, and the Supreme Court denied certiorari.\textsuperscript{27} However, state courts are more suspicious of these agreements and more likely to invalidate them.\textsuperscript{28} The New York Supreme Court has seen a judicial trend in state courts toward holding arbitration agreements in consumer transactions unconscionable.\textsuperscript{29} It also found that the rules and fees charged by arbitration providers become oppressive when “applied to unsophisticated borrowers of limited means in disputes over small claims.”\textsuperscript{30} However, they are preempted by the FAA and the Supreme Court and most arbitrations are upheld.\textsuperscript{31}

The National Consumer Disputes Advisory Committee of the American Arbitration Association (AAA) has developed a national Due Process Protocol for Mediation and Arbitration of Consumer Disputes.\textsuperscript{32} The AAA will not take on any case that “substantially and materially deviates from the minimum standards of the Protocol”.\textsuperscript{33} These standards have not been enough to protect consumers from a flawed system. Courts have stated that these agreements can be challenged on grounds of unconscionability, costs, or for the way the agreement is integrated into consumer transactions.\textsuperscript{34} However, it is difficult to get into court to challenge an agreement because arbitrators are supposed to decide if arbitration is the best way to resolve the

\textsuperscript{27} Id. (citing Hill, 522 U.S. 808).  
\textsuperscript{29} Id. (citing Hayes, 713 N.Y.S.2d at 268; Powertel, Inc. v. Bexley, 743 So. 2d 570, 574 (Fla. Dist. Ct. App. 1999)).  
\textsuperscript{30} Id. (citing Hayes, 713 N.Y.S.2d at 270 (quoting Patterson v. ITT Consumer Fin. Corp., 18 Cal. Rptr. 2d 563, 567 (Cal. Ct. App. 1993)).  
\textsuperscript{31} See id.  
\textsuperscript{32} Id.; see AAA Adapts Due Process Protocol for Consumer Dispute Resolution, 9 WORLD ARBITRATION & MEDIATION REPORT 203 (1998).  
\textsuperscript{33} Id.  
\textsuperscript{34} See id. at 283.
These agreements only increase the burden on an already over-congested judicial system. Consumers try to invalidate these clauses in court or appeal the awards, and because class actions are not allowed this means hundreds to thousands of cases going through the system. The system needs to be changed in order to provide cost-effective, neutral, and efficient dispute resolution.

B. The European system focuses on consumer protection.

Mandatory consumer arbitration agreements are heavily restricted in Europe. The Council of the European Union is the main decision-making body of the European Union and run by representatives of all the Member States, similar to the U.S. Congress. It issued the Unfair Terms in Consumer Contracts Directive in 1993. This provides that any provision in a consumer contract, with the exception of subject matter and price, can be challenged on the grounds that it has not been individually negotiated and is unfair. “Terms are regarded as unfair if, contrary to the requirement of good faith, [they] cause[] a significant imbalance in the parties’ rights and obligations arising under the contract, to the detriment of the consumer.” In an annex, the Directive set out a list of terms that may be “regarded as unfair if they cause a significant imbalance in

35 See id.
36 See Smith, Consumer Protection, supra note 21, at 1236.
37 Id.
40 Sternlight, US Out on a Limb, supra note 4, at 844 (citing Council Directive 93/13, Unfair Terms in Consumer Contracts, 1993 O.J. (L 95) 29, WL OJ 1993 L95/29) (Council Directives are like Community laws. Once they are issued, European Union member states are required to draft or revise existing legislation to conform to the Directive within a certain period of time.).
41 See Drahozal & Friel, Consumer Arbitration, supra note 19, at 357.
A contractual provision included on this list was “excluding or hindering the consumer’s right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration.” All terms in written contracts must be written with plain, intelligible language. If there is doubt about the meaning of a term, the most favorable interpretation to the consumer prevails.

When determining the enforceability of such contracts, the court will look at factors such as “the nature of the subject matter of the contract, the circumstances attending the conclusion of the contract and all the other terms of the contract”. If an imbalance is found, the court has to determine if it is contrary to the principles of good faith. This is assessed using three basic principles: 1) “strength of the bargaining positions of the parties”, 2) “any inducements made to the consumer to secure agreement to the term . . .” and 3) “the extent to which the seller or supplier had dealt fairly with the consumer.” A prima facie unfair term is any term that excludes or hinders the consumer’s right to take legal action. The Directive clearly gives the courts the power to invalidate any term in a contract it feels to be unfair to the consumer. The Directive can be invoked by individual consumers in a legal action, but it also grants powers to the Director General of the Office of Fair Trading to apply for an injunction to prevent the

43 See Sternlight, U.S. Out on a Limb, supra note 4, at 844.
45 See Overby, Institutional Analysis, supra note 42, at 1266-67 (citing 1993 O.J. (L95) 29, art. 5).
46 Id.
47 See Sternlight, U.S. Out on a Limb, supra note 4, at 845 (quoting 1993 O.J. (L95) 29, art. 4(1)).
48 Id. (citing art. 3(1)).
49 Id. (quoting Consumer Protection, 1994, S.I. 1994/3159, art. 4(3) & schedule 2 (U.K.)).
50 Id. at 364-65 (citing 1993 O.J. (L95), art. 3(3), and Annex 1(a) through (q)).
51 Id. at 365 (citing 1993 O.J. (L95) 29, art. 6(1)).
continued inclusion of unfair terms in general usage.\textsuperscript{52} This enforcement power extends to other qualifying bodies, and allows them to oversee the use of these agreements by businesses.\textsuperscript{53}

In 1998, the European Commission issued a Recommendation on the “Principles Applicable to the Bodies Responsible for Out-of-Court Settlement of Consumer Disputes” (\textquotedblleft 1998 Recommendation\textquotedblright).\textsuperscript{54} It is not binding law but has a strong practical effect on member states and is a strong indicator of how member states treat this issue.\textsuperscript{55} The European Commission is the European Union’s executive branch and is responsible for implementing the decisions of the Parliament and the Council.\textsuperscript{56} The Recommendation quotes Article 6 of the European Human Rights Convention, which says \textquoteleft access to the courts is a fundamental right that knows no exception.\textquoteright\textsuperscript{57} It provides that \textquoteleft out-of-court alternatives may not deprive consumers of the right to bring the matter before the courts unless they expressly agree to do so, in full awareness of the facts and only after the dispute has materialised.\textquoteright\textsuperscript{58} This is a very strong statement, clearly, they do not believe these agreements are inherently fair to consumers and it is a per se ban on them in the EU.\textsuperscript{59} The European Court of Justice recently ruled that national courts must consider the validity of the arbitration clause even if its validity was not pleaded in the

\textsuperscript{52} See Collins, \textit{Compulsory Arbitration Agreements, supra} note 38, at 340.
\textsuperscript{53} See id.
\textsuperscript{55} Id.
\textsuperscript{57} See Sternlight, \textit{U.S. Out on a Limb, supra} note 4 at 846.
\textsuperscript{58} Id. (quoting 1998 Recommendation).
\textsuperscript{59} Id.
 Consumers are free to choose arbitration after a dispute has been started, but the waiver of the right to a trial must be voluntary and informed. The European approach is to protect the weaker party while the American approach is to protect the freedom of the parties.

In the United Kingdom, consumers can choose arbitration after the dispute arises but are not forced into it. In English common law, the two principal reasons they do not like arbitration are the lack of unity and competition. Under traditional English common law, a contractual agreement that purported to oust the jurisdiction of the courts was void as being contrary to public opinion. The Consumer Arbitration Agreement Act of 1988 provided that “any such agreement entered into by a consumer before a dispute arose would not be binding on the consumer”. In the UK, all pre-dispute arbitration agreements are unenforceable when the potential claim is less than £5,000. For higher claims, the validity of the agreement is judged on a case-by-case basis to decide if it is unfair under the Directive. Under the UK’s Arbitration Act 1996, the loser pays for the costs of both parties. A court will not strike the arbitration clause unless the consumer can prove they failed to obtain government funding to pay costs widely available because of the arbitral procedure itself and that some form of funding

---

61 Id. at 337 (citing from Stretford v. Football Association Ltd, EWCA Civ. 238, [2007] Bus LR 1052).
62 See Draholz & Friel, supra note 19, at 386.
63 Id.
64 Id. at 367 (quoting G.H. Treitel, The Law of Contract 251 (9th ed. 1995)).
66 See Drahozal & Friel, supra note 19, at 386.
67 Id.
68 See Collins, Compulsory Arbitration Agreements, supra note 38, at 346 (citing Arbitration Act, 1996, c. 23, § 61(2) (Eng.)).
could have been available if the action proceeded in the courts.\textsuperscript{69} Funding depends on whether the matter is one of “widespread public interest”.\textsuperscript{70} This means arbitral proceedings are less likely to be funded because they do not provide real benefits to a large segment of society or establish new legal precedent.\textsuperscript{71}

Besides funding, there is a reason why the U.S. is one of the few countries to not only allow these agreements but to encourage their use.\textsuperscript{72} Europeans use civil law, which does not allow for punitive damages, restricts class actions lawsuits, and severely restricts the right to a jury trial.\textsuperscript{73} If American common law did the same, arbitration would be much more attractive to the consumer. American companies have used these agreements as their own version of tort reform, without the legislation, to fight the excessive amounts of frivolous lawsuits and huge jury awards that are common under the American common law system.\textsuperscript{74}

While this revolution in expanding the use of these agreements has been led by the Supreme Court, other judges have followed their lead for reasons of their own. Legal scholars have also theorized that the source of judicial campaign contributions have a direct correlation to how that jurist votes in arbitration cases.\textsuperscript{75} Additionally, many judges take high-paying jobs as arbitrators once they are off the bench, which makes it very likely they will rule favorably towards arbitration.\textsuperscript{76} In contrast, judges in many European countries are appointed by the government and are not influenced by campaign

\begin{footnotes}
\item[69] Id.  \\
\item[70] Id.  \\
\item[71] Id. (citing Funding Code (n 64) § 5.7.5).  \\
\item[72] See id.  \\
\item[73] See Sternlight, U.S. Out on a Limb, supra note 4, at 854; see Drahozal & Friel, supra note 19, at 390.  \\
\item[74] Id. at 854-55.  \\
\item[75] See Sternlight, U.S. Out on a Limb, supra note 4, at 856 (citing Stephen J. Ware, Money, Politics, and Judicial Decisions: A Case Study of Arbitration Law in Alabama, 15 J.L. & Pol., 645, 684 (1999)).  \\
\item[76] Id. (citing Reynolds Holding, Judges’ Action Cast Shadow on Court’s Integrity: Lure of High Paying Jobs as Arbitrators May Compromise Impartiality, S.F. CHRON., Oct. 9, 2001 at A13).
\end{footnotes}
contributions needed to win elections. The cultural differences add to the debate because Europe is more concerned with consumer rights and protection. On the other hand, the U.S. is more pro-business, which has led to the election and appointment of conservative judges with a very friendly business philosophy.

The European Union uses a system called the European Extra-Judicial Network (EEJ-Net) to manage cross-border disputes in Member states. The goal is to allow EU citizens fair, cheap and efficient access to justice in relation to their cross-border consumer dispute using appropriate ADR schemes and bodies in the relevant state. It is organized through clearing houses in the European Consumer Centres Network (ECC-Net) in each State that helps consumers formulate a complaint, monitors the system, and coordinates various national ADR schemes. According to the 2007 European Consumer Centre Network Annual Report, the ECC-Net handled 55,000 cases in 2006. The ECC-Net is financed through grants by the EU Commission and Member states. It is cost effective for consumers and businesses use it as a marketing tool to reassure consumers that they are covered in case of a dispute. Businesses sign up to one of the

77 Id. (citing Frank B. Cross, Institutions and Enforcement of the Bill of Rights, 85 CORNELL L. REV. 1529, 1538 (2000)).
78 Id.
82 See Consumer Voice, supra note 80, at 1.
84 Id. at 7.
85 See Consumer Voice, supra note 80, at 2.
ADR schemes allied to the EEJ-Net and anything the consumer purchases is covered.\textsuperscript{86} The ECC-Net provides an EU-wide network designed to promote consumer confidence by advising citizens on their rights and providing easy access to redress through the EEJ-Net.\textsuperscript{87} These Centres advise consumers on out-of-court settlement procedures and provide information on EU legislation and national legislation and case law.\textsuperscript{88}

The seven principles of the EEJ-Net are independence, transparency, respect of the adversarial principle, effectiveness, legality, liberty and representation.\textsuperscript{89} “Compliance with these principles is intended to guarantee consumers and traders that their cases will be treated with rigor, fairness and independence; with the expected advantage, of course, of a simpler and quicker settlement of their dispute.”\textsuperscript{90} Arbitration works in the EU partly because their court systems are different from the U.S., but the U.S. could use a similar approach to make arbitration more palatable to American consumers.

\section*{III. Analysis}

\textbf{A. These agreements are unfair to consumers.}

1. These agreements are nonconsensual and consumers are usually

\begin{itemize}
\item \textsuperscript{86} Id.
\item \textsuperscript{88} Id. at 2.
\item \textsuperscript{90} Id.
\end{itemize}
unaware of them.

The nonconsensual nature of pre-dispute mandatory arbitration agreements makes them unfair. Very few consumers read these agreements and even less understand them. “Some companies deliberately design their arbitration agreements in a manner . . . to decrease the likelihood that the consumer will focus on [it].” Also, consumers tend to ignore them or think they are unimportant because they will not be suing the company. They lose their constitutional right to a trial, along with extended discovery and an extensive appeal process. These ‘take it or leave it’ contracts leave consumers without any bargaining rights and no alternatives because every company uses them.

2. Mandatory arbitration agreements are written in the drafter’s favor, not the consumers’.

As in choice of law provisions, the arbitration agreement will most likely include the arbitrator or arbitration provider, the location where the arbitration will take place, and other rules of the arbitration. The consumer has no choice and cannot bargain for these things. The agreements impose high costs on consumers to reduce the chance of them filing for arbitration, including “selecting an arbitrator or provider with high fees, locating the arbitration in a distant forum, and limiting available discovery” so consumers

---

91 See STERNLIGHT, ARBITRATION LAW, supra note 11, at 143.
93 Id. at 143; see, e.g. Ting v. AT&T, 182 F. Supp. 2d 902, 911-13 (N.D. Cal. 2002), aff’d in part, rev’d in part, 319 F.3d 1126 (9th Cir.), cert denied, 540 U.S. 811 (2003) (showing AT&T spent substantial resources determining how best to implement their arbitration agreement so it would not be opposed by consumers).
94 Id.
95 Id. at 144.
96 See Smith, Consumer Protection, supra note 21, at 1192.
97 Id.
98 Id. at 1192.
must “gather evidence through more expensive means.”  Furthermore, they prohibit class actions, which results in quashing many claims that are not financially viable on their own.  While consumers are only allowed to use arbitration, the companies reserve the right to sue the consumer in court.  Lastly, some companies use these agreements to limit consumers’ access to substantive relief.  This includes shortening statute of limitations; barring recovery of punitive damages, compensatory damages, or attorney fees; or barring recovery of injunctive relief.  While courts have removed or invalidated some of these agreements, it is difficult and expensive to challenge them.  The courts have not consistently decided that these costs will be considered when determining the financial feasibility of arbitration for the consumer.  These agreements make it unlikely to be able to get representation when the expected recovery will be small.  Companies draft these agreements in order to avoid expensive awards, punitive damages, empathetic juries, bad publicity and bad precedent.

3. Arbitration providers and arbitrators are not required to give the same rights to a consumer as they would have in a courtroom with a judge.

99 See STERNLIGHT, ARBITRATION LAW, supra note 11, at 145-46.
100 Id. at 146; see Jean R. Sternlight & Elizabeth J. Jensen, Using Arbitration to Eliminate Consumer Class Actions: Efficient Business Practice or Unconscionable Abuse?, 67 LAW & CONTEMP. PROBS. 75 (2004); Jean R. Sternlight, Arbitration Meets the Class Action, Will the Class Action Survive?, 42 WM. & MARY L. REV. 1 (2000).
101 See STERNLIGHT, ARBITRATION LAW, supra note 11, at 146.
102 Id.
103 Id.
104 Id. at 147.
106 See STERNLIGHT, ARBITRATION LAW, supra note 11, at 147; Budnitz, High Cost, supra note 105, at 148.
Arbitration is “designed to abbreviate judicial proceedings to reduce the cost of litigation and to make adjudication workable.” But it does not provide the same rights as if you were in a court. Arbitral awards are reviewed by courts on a minimal basis, with the courts deferring to the arbitrator’s authority in most cases. Under the FAA, a court is required to confirm an award ‘unless the award is vacated, modified, or corrected under Section 10 or 11 of the FAA.’ Section 10 provides for vacating awards for corruption, fraud, evident partiality, procedural misconduct or excess arbitral authority. Arbitration is private and there are rarely transcripts or even a written award, so it is difficult to get it overturned for any reason.

Companies sign agreements with arbitration providers so that particular provider will be named in all of their mandatory arbitration agreements. According to critics, this gives providers a financial incentive to make sure the companies are pleased with the results of their arbitration. Otherwise, they could switch providers. Also, the companies have the advantage of the “repeat player” bias. When companies are “repeat players” in arbitration, they gain experience in the process and how the system works that consumers are unable to duplicate. Most of the empirical evidence regarding this phenomenon is from litigation, so it is unclear whether it also applies to

---

109 Id. at 261-62 (citing Green Tree Fin. Corp. v Bazzle, 539 U.S. 444, 453 (2003)).
111 Id.
112 See id.
113 See STERNLIGHT, ARBITRATION LAW, supra note 11, at 145.
114 Id.
115 Id.; see Marc Galanter, Why the “Haves” Come out Ahead: Speculation on the Limits of Legal Change, 9 LAW & SOC’Y REV. 95 (1974) (Repeat player concept first introduced by Marc Galanter).
116 Id. at 145.
arbitration. Nevertheless, consumers who are unused to any type of legal situation are always at a disadvantage with companies who engage in litigation or arbitration often.

Public Justice attorney Paul Bland testified at a hearing in front of the House Judiciary Committee on these agreements.

He stated that private arbitration companies are under great pressure to devise systems that favor the corporate repeat players … arbitrators who rule against corporations and in favor of individuals are often blackballed … some arbitration companies have undertaken advertising campaigns aimed at prospective corporate clients which make a number of inappropriate promises of favorable treatment.

For example, the National Arbitration Forum’s website disclosures show the decisions from one arbitrator for a quarter. This arbitrator handled eighty cases brought by banks against individuals, and ruled for the banks in all of the cases. In seventy-eight of the cases, the bank was awarded the entire amount it had claimed and in two slightly less. Case studies show that arbitration is highly slanted towards businesses.

California is the only state that requires arbitration providers to publicly disclose the outcomes of arbitrations.

Available evidence indicates that the corporate clients of arbitration companies enjoy a truly staggering success rate – between 94 percent and 99 percent – and that individual arbitrators sometimes dispose of dozens of cases in a single day, ruling 100 percent for corporate claimants. Such a

---

118 Id.
120 Id.
122 Id.
123 Id.
124 Id.
record reinforces the impression that arbitrators are essentially rubber-stamping corporate claims.\(^{126}\)

After a court case in Alabama forced First USA Bank to turn over its arbitration records, it found that in 20,000 cases using NAF, First USA won an astonishing 99.6 percent of the time.\(^{127}\) Arbitrators can decide dozens of cases a day.\(^{128}\) Joseph Nardelli, California’s busiest arbitrator, signed sixty-eight decisions on January 12, 2007 and awarded over a million dollars to the corporate plaintiffs.\(^{129}\) Arbitrators do not need a law degree and are not required to follow legal precedent.\(^{130}\) They may be unable to decide complex legal issues without the appropriate legal background.\(^{131}\)

Arbitrators are rarely subject to appeal.\(^{132}\) The Supreme Court stated in *Major League Baseball Association v. Garvey* that “courts are not authorized to review the arbitrator's misinterpretation of the parties' agreement.”\(^{133}\) Even if an “arbitrator is even arguably construing or applying the contract and acting within the scope of his authority,” the fact that “a court is convinced he committed serious error does not suffice to overturn his decision.”\(^{134}\) Arbitrators are not legally accountable for any errors they may make.\(^{135}\) They are not subject to oversight, most decisions are confidential and they are not

\(^{126}\) Id.

\(^{127}\) Id. (citing Michael A. Bownes v. First USA Bank NA, et al, Circuit Court of Montgomery, AL, Civil Action No. 99-2479-PR).

\(^{128}\) Id. at 16.

\(^{129}\) Id.


\(^{131}\) Id. at 686 (citing Cole v. Burns Int’l Servs., 105 F.3d 1465, 1477 (D.C. Cir. 1997)).

\(^{132}\) Id.

\(^{133}\) Major League Baseball Assoc. v. Garvey, 532 U.S. 504, 509 (2001)).


required to have a written decision.\textsuperscript{136} In this way, corporations are avoiding setting negative precedent and evading corporation accountability.\textsuperscript{137}

**B. The costs of arbitration outweigh any benefits.**

1. Fees charged by the leading arbitration providers are not less expensive than court fees.

Arbitration is supposed to be cost-effective for both sides. Filing fees for litigation are relatively small, but arbitration fees can be much larger.\textsuperscript{138} There are two main groups that provide arbitration services.\textsuperscript{139} The American Arbitration Association (AAA) is the largest and most used provider.\textsuperscript{140} If a consumer’s claim is for less than $10,000, they must pay half of the arbitrator’s compensation but it cannot exceed $125.\textsuperscript{141} If the claim is between $75,000 and $150,000, the consumer must pay a $2,250 administrative fee and a $4,000 fee for a claim between $150,000 and $300,000.\textsuperscript{142} Individual arbitrators charge different rates, and the AAA does not provide the rate until the arbitrator is appointed.\textsuperscript{143} Therefore, the consumer will not know the amount of the fee until after they file the claim. Larger claims are more expensive in arbitration than if

\textsuperscript{136} Id.
\textsuperscript{137} Id. at 3.
\textsuperscript{138} HANDBOOK ON AMERICAN ARBITRATION ASSOCIATION HANDBOOK ON COMMERCIAL ARBITRATION 84 (Thomas E. Carbonneau & Jeannette A. Jaeggi eds., 2006).
\textsuperscript{139} See id.
\textsuperscript{140} See Caroline E. Meyer, Hidden in Fine Print: ‘You Can’t Sue Us’: Arbitration Clauses Block Consumers From Taking Companies to Court, WASH. POST, May 22, 1999 at A1.
\textsuperscript{142} Id. at 136-37 (citing AAA Commercial Rules).
\textsuperscript{143} Id. at 137.
the consumer filed in court.\textsuperscript{144} Also, if the agreement bars an award with multiple, consequential, punitive or exemplary damages, that raises the cost of individual claims relative to possible awards.\textsuperscript{145} In comparison, the cost of filing a complaint in a federal district court is about $150.\textsuperscript{146} The consumer would not have to pay for the judge’s salary or expenses.\textsuperscript{147} Nor would they be expected to pay up front for any costs. If they lost, there would be a payment plan for any costs awarded to the other side. In arbitration, the consumer must pay thousands of dollars in fees before it will begin.\textsuperscript{148}

Another arbitration provider is the National Arbitration Forum (NAF). Under this provider, a consumer must pay minimum fees depending on the amount of damages alleged.\textsuperscript{149} Those fees include a filing fee, participation fee, commencement fee, administrative fee, and participatory hearing fees if the business selects a hearing.\textsuperscript{150} Then consumers must pay “additional fees for each request for an amendment, subpoena, discovery order, continuance, stay, or any other type of dispositive or nondispositive order.”\textsuperscript{151} These fees are difficult if not impossible to determine beforehand because they are dependent on factors not known before a complaint is filed.\textsuperscript{152} These fees can act to prevent a consumer from filing a claim, and in the long run will affect the goal of the legal system – to compensate consumers from injuries suffered at the hands of businesses


\textsuperscript{145}Id.


\textsuperscript{147}Id.

\textsuperscript{148}Id.

\textsuperscript{149}See id.


\textsuperscript{152}Id. at 139.
and to deter and remedy egregious commercial conduct.\textsuperscript{153} Most providers do have special programs set up to waive these fees, but there are strict standards to follow and very few are granted.\textsuperscript{154}

2. Challenging the agreement as cost-prohibitive is difficult without knowing the costs before it begins.

Some courts have ruled the arbitration agreement is unenforceable if it would be too cost-prohibitive.\textsuperscript{155} The fundamental case dealing with this issue is \textit{Green Tree Financial Corporation v. Randolph}.\textsuperscript{156} In this case, a mobile home was purchased on credit and the consumer claimed the creditors violated two federal statutes.\textsuperscript{157} The arbitration agreement required binding arbitration but did not designate an arbitration provider.\textsuperscript{158} The Eleventh Circuit held the agreement was “unenforceable because it fails to provide the minimum guarantees required to ensure that Randolph’s ability to vindicate her statutory rights will not be undone by steep filing fees, steep arbitrators’ fees, or other high costs of arbitration”.\textsuperscript{159} The Supreme Court reversed and held that the record did not show enough information on high costs to prove she would be barred from vindicating her statutory rights.\textsuperscript{160} In 2000, the Supreme Court ruled that a consumer seeking to invalidate an arbitration agreement on the grounds of the arbitration being prohibitively expensive bears the burden of showing the likelihood of incurring such

\begin{itemize}
\item \textsuperscript{153} \textit{Id.} at 140.
\item \textsuperscript{154} \textit{See id.} at 144.
\item \textsuperscript{155} \textit{Id.}
\item \textsuperscript{156} \textit{Id.} (citing Green Tree Financial Corp. v. Randolph, 531 U.S. 79 (2000)).
\item \textsuperscript{157} \textit{Id.} at 157 (citing \textit{Green Tree}, 531 U.S. at 79).
\item \textsuperscript{158} \textit{Id.} (citing \textit{Green Tree}, 531 U.S. at 83).
\item \textsuperscript{159} \textit{Id.} (quoting Randolph v. Green Tree Fin. Corp., 178 F.3d 1149, 1158 (11th Cir. 1999)).
\item \textsuperscript{160} \textit{Id.} at 158 (citing \textit{Green Tree}, 531 U.S. at 90).
\end{itemize}
costs. But they did not provide any guidelines for determining what constituted prohibitively expensive. In Popovich v. McDonald’s Corp, the Court found the Plaintiff had carried his burden under Green Tree Financial Corporation v. Randolph in demonstrating that arbitration would be cost-prohibitive and that the arbitration agreement was unenforceable. The cost of the arbitration would “likely be $48,000 and could be as high as $126,000.”

To challenge an arbitration based on prohibitive cost, a consumer must somehow estimate costs that are impossible to determine in advance. Arbitration agreements may stipulate a certain provider or rules to be used, but they usually do not provide information about costs. Courts have rejected a consumer’s challenge because they could not prove the provider would actually conduct the arbitration or charge the specified fees because using their rules was the only thing required in the agreement. The consumer would have to estimate the costs for an arbitrator not yet appointed and attempt to guess at what hearings or orders they will need.

Arbitration providers frequently change their rules, adding to the uncertainty. If the agreement does not specify a version of the provider’s rules, a court or arbitrator must decide. Winning a case based on costs requires substantial expertise and skilled lawyers. Most consumers cannot afford attorneys like those in Ting v. AT&T. They

161 Id. at 92.
162 See Budnitz, High Costs, supra note 139, at 143 (citing Popovich v. McDonald’s Corp., 189 F. Supp. 2d 772 (N.D. Ill. 2002)).
163 Id.
164 Id. at 151.
165 Id.
166 Id. at 152 (citing In re First Merit Bank, 52 S.W.3d 749, 757 (Tex. 2001)).
167 Id. at 152.
168 Id. at 153.
169 Id.
170 Id. at 154.
had the resources needed to mount a sophisticated attack that included extensive
discovery and commissioning their own survey on costs.\textsuperscript{172}

Courts are split over how to prove that costs are so high as to be prohibitive to a
consumer.\textsuperscript{173} They focus on three factors: “the financial condition of the claimant, the
absolute cost of the arbitration, and the relative cost of arbitration when compared to
court proceedings”.\textsuperscript{174} Those consumers who can least afford to suffer from a businesses
conduct are those who likely to be barred by the costs of arbitration.\textsuperscript{175}

Courts need a legal theory to justify concluding that high costs invalidate an
arbitration agreement. They have used two legal theories to strike down arbitration
agreements or their terms based on cost.\textsuperscript{176} First, “courts have asked whether the costs of
arbitration impermissibly preclude the consumer from vindicating their statutory
rights”.\textsuperscript{177} Second, “courts have asked whether the costs make the agreement or [parts of
it] unconscionable”.\textsuperscript{178}

In \textit{Mitsubishi Motors Corp. v Soler Chrysler-Plymouth}, the Supreme Court found
that one party can force another to pursue a statutory claim in arbitration “so long as the
litigant effectively may vindicate the statutory cause of action in the arbitral forum”.\textsuperscript{179}
The Court made it clear the converse also applies: a party can successfully challenge an
arbitration agreement on the basis that she cannot effectively vindicate her statutory

\begin{footnotes}
\item[\textsuperscript{171}] \textit{Id.} at 154 (citing Ting v. AT&T, 182 F. Supp. 2d 902, 906 (N.D. Cal. 2002), \textit{rev’d in part, aff’d in part}, 
319 F.3d 1126 (9th Cir. 2003)).
\item[\textsuperscript{172}] \textit{Id.}
\item[\textsuperscript{173}] \textit{Id.}
\item[\textsuperscript{174}] \textit{Id.}
\item[\textsuperscript{175}] \textit{Id.} at 156.
\item[\textsuperscript{176}] \textit{Id.} at 157.
\item[\textsuperscript{177}] \textit{Id.}
\item[\textsuperscript{178}] \textit{Id.}
\item[\textsuperscript{179}] \textit{Id.} (quoting Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, 473 U.S. 614, 637 (1985)).
\end{footnotes}
rights” based on excessive cost.\textsuperscript{180} The person who challenges the arbitration based on cost has the burden of proof.\textsuperscript{181}

3. Forcing arbitration instead of litigation is only less expensive for businesses.

The anti-business attitude of today’s consumers, frivolous lawsuits, and irrational jury awards make litigation very expensive for companies. There are seven ways arbitration causes costs to decrease. First, arbitration does not allow a jury so an expensive damages award is less likely.\textsuperscript{182} Second, the mandatory confidentiality of an arbitration award and lack of a published case “lessens the risk of adverse publicity”.\textsuperscript{183} Businesses like the fact that no one but the parties involved know the amount of the award, both to prevent bad publicity and so other potential parties do not file after seeing a big award.\textsuperscript{184} Third, arbitration uses a “nationally uniform set of standards” that allows businesses to avoid the costs of “adapting to different procedural rules in different states”.\textsuperscript{185} It also saves on hiring local counsel.\textsuperscript{186} Fourth, there is very little appellate review available after an arbitration award is given.\textsuperscript{187} Fifth, these arbitration agreements can eliminate the right to a class action lawsuit.\textsuperscript{188} Class action lawsuits always involve a

\textsuperscript{180} Id.
\textsuperscript{181} Id. at 138 (citing Green Tree Financial Corp. v. Randolph, 531 U.S. 79, 92 (2000)).
\textsuperscript{183} Id.; see Alan S. Kaplinsky & Mark J. Levin, Alternative to Litigation Attracting Consumer Financial Services Companies, in Arbitration of Consumer Financial Services Disputes, CONSUMER FINANCIAL SERVICES LAW REPORT (June 27, 1997).
\textsuperscript{184} Id.
\textsuperscript{185} Id.
\textsuperscript{186} Id.
\textsuperscript{187} Id. at 90.
very large damages award. Sixth, arbitration deters claims because the filing fees and arbitrator fees that must be paid by the consumer can be much higher than litigation.\textsuperscript{189} Seventh, arbitration sometimes allows only limited discovery for the consumer, which lowers the time and money businesses must spend and makes it more difficult for the consumer to prove their claim.\textsuperscript{190} Arbitration favors businesses overwhelmingly and consumers need to have more ways to ensure their rights are allowed.

C. Current pending legislation banning mandatory arbitration would only exacerbate the problem.

1. Banning these agreements causes more problems than it would solve.

Banning these agreements would increase litigation and overload courts.\textsuperscript{191} When parties claim the arbitration agreement was void because the claim was brought pursuant to a covered statute, domestic courts would have to sort it out before they got to arbitration.\textsuperscript{192} Consumers would be more likely to choose litigation over arbitration because they are familiar with the system. Our court system is overwhelmed with disputes and it can take years and thousands of dollars in legal fees to get a judgment, only to have it appealed and the process starts over. If the system were more fair and balanced, arbitration could be the consumer’s choice.

For the past few years, multiple bills have tried to ban these mandatory consumer arbitration agreements.\textsuperscript{193} Now that the Democrats are in control and the country is

\textsuperscript{189} Id.; see American Arbitration Association, Commercial Arbitration Rule R4(a)(ii) & Administrative Fees (1999).

\textsuperscript{190} Id.; see ALAN S. KAPLINSKY & JEAN R. STERNLIGHT, ARBITRATION OF CONSUMER FINANCIAL SERVICES DISPUTES 763, 790 (Practicing Law Institute 1999).

\textsuperscript{191} See Smith, Consumer Protection, supra note 21, at 1236.

\textsuperscript{192} Id.

\textsuperscript{193} See Arbitration Trap, supra note 125, at 63.
decidedly anti-big business and for any regulation that will hold businesses accountable, the new legislation may pass. The Consumer Fairness Act of 2009 will “treat arbitration agreements which are unilaterally imposed on consumers as an unfair and deceptive trade practice and prohibit their use in consumer transactions”. The fact that they were introduced in the very first session of the House after the election is very telling. This issue has been very important to many individuals and groups for years, even though the public is mostly unaware of it.

2. The business world cannot afford to litigate every dispute, but the system need to be reformed to be similar to the European model.

There are many problems associated with mandatory consumer arbitration agreements. They take away too many rights and are too costly to consumers. But the larger problem remains, which is that corporations are fighting against the increasing amount of frivolous lawsuits, the high amounts awarded by sympathetic juries and an incredibly overcrowded court system. Forcing consumers into an arbitration system that is more efficient but is costly and unfair to consumers is not the answer. The system needs to be reformed to include more regulation, oversight and fairness. Europe’s system is very successful and is voluntarily used by both sides. The U.S. needs to use their system as a model, and use some of their ideas to create a better way to resolve disputes between businesses and consumers. Trying to fix these cost issues would involve standard national policies and more regulation of arbitration providers. It would be

similar to the National Association of Securities Dealers, whose subsidiary set up a Regulation Office of Dispute Resolution to handle disputes.\(^{195}\)

The Europeans use the EEJ-Net and clearing houses to handle cross-border disputes between consumers and businesses.\(^{196}\) Consumers choose arbitration voluntarily after a dispute has begun because of the lack of punitive damages and restricts on class actions lawsuits and jury trials in Europe.\(^{197}\) Because Americans do not have those same limitations, it will be harder to persuade them to use arbitration.

In order to implement a new system, Congress needs to establish a Consumer Disputes Arbitration Board. This oversight board will be the final determination on a case-by-case basis for whether it is unfair to hold a consumer to the arbitration agreement. It will include stringent but clear guidelines on which cases may come before them. It will be run by a panel of four judges who are experienced in arbitration and litigation. The panel will also be responsible for writing a national code of conduct for arbitrations and arbitrators.

Each state will have their own mini boards, whose responsibilities would include approving arbitration providers and publishing their results online to ensure a transparent process. Arbitrations will be randomly chosen to be monitored by an oversight committee of these mini boards. This board would also check for conflicts of interest and ensure each arbitration is given enough time and attention by its arbitrator. It will also provide a number of pro bono lawyers to explain the process and their rights to consumers, and provide recommendations for representation.

\(^{196}\) See Consumer Voice, supra note 80, at 1.
\(^{197}\) See Sternlight, U.S. Out on a Limb, supra note 4, at 854; see Drahozal & Friel, supra note 41, at 390.
An arbitrator working for any arbitration provider must sign the national code and be held accountable for their actions by a panel who reviews their behavior, their cases and any complaints filed against them. There will be a strict vetting process to make sure there are no improper relationships or ties between an arbitrator and the defendant corporation before they are allowed to take a case. Arbitrators must be neutral, competent, and independent.\textsuperscript{198} At minimum, an arbitrator should be barred from handling a case where they would be prohibited from sitting as a judge or a juror.\textsuperscript{199} Also, there should be a nationwide training course for any arbitrators without a law degree. These arbitrators will be limited in the cases they handle and any cases involving complex legal issues must be handled by an arbitrator with a law degree.

In the past few years, businesses have proven they are unable to govern themselves properly and the market will not do it either. Today consumer confidence is extremely low and anti-business sentiment is very high. This system would provide reassurance to the consumers and could even be used as a marketing tool to sophisticated consumers. Large and small businesses can sign up with an approved arbitration provider in their state so consumers know they will have a fair alternative to court. This system would also enhance the enforceability of the arbitration agreement and award, and hopefully lead to fewer appeals. This will lower dispute costs for businesses and lessen uncertainty so consumers can be adequately represented.

\textbf{IV. Conclusion}

\textsuperscript{198} See Stempel, \textit{Shearson/American Express, supra} note 1, at 409.
\textsuperscript{199} \textit{Id.}
The use of these types of agreements goes against the very foundations of law and justice in this country. “Our existing system of justice serves a public purpose. By closing off access to proceedings, eliminating judicial precedent, and allowing parties to write their own laws, we compromise society’s role in setting the terms of justice.”

Article Seven of the United States Bill of Rights guarantees the right of a trial by jury. Waiving a constitutional right must at least be clear, if not knowing and voluntary.

Businesses should not be able to force consumers to give that up with an agreement hidden in a warranty or contract. The fact that the Supreme Court seems to think efficiency and supposed cost savings are worth giving up these rights so the courts are less crowded is surprising. The system needs to be changed to benefit both parties so they can settle disputes amicably, efficiently, and in a cost-effective manner that is fair.

“It is highly problematic to permit the most powerful actors in a society to craft a dispute resolution system that is best for them but not necessarily their opponents or the public at large”.

Arbitration tends to favor the repeat player. Furthermore, corporations themselves fight binding arbitration when it applies to them. For example, franchised car dealers have an exemption from the FAA because they complained the dealers

---


201 See BLAND, CONSUMER ARBITRATION AGREEMENTS, supra note 22, at 105 (citing Fuentes v. Shevin, 407 U.S. 67, 95 (1972)).


204 Id.
exploited them because of their superior bargaining position. A recent study found only eleven percent of contracts between companies included binding arbitration, suggesting that corporations do not view arbitration as an efficient substitute for litigation as they claim. Proponents of these agreements claim their studies show consumers benefit from their use. Because arbitration is private and confidential, there is very little information available to do a study. It is also difficult to do a cost comparison between arbitration and litigation. A study often cited by industry supporters considers the consumer to have prevailed if they win any amount, regardless of its relation to the amount they should have received. Also, the data set was only the 226 cases filed by consumers and does not include the more than 100,000 cases filed by corporations against consumers during that same time period. Another study widely used by proponents of these agreements was conducted for the U.S. Chamber of Commerce’s Institute for Legal Reform. It only used parties who voluntarily chose arbitration, so it has no bearing on the discussion. Arbitration providers should be required to publish the data on these arbitrations so an independent group can do a real study to determine the actual results.

---

207 Id.
208 Id.
209 Id.
211 Id.
213 Id.
Corporations have created their own solution to the problems inherent in today’s court system. However, their version of tort reform primarily benefits them and prevents consumers from exercising their rights. An arbitrator is not the right person to adjudicate complicated federal statutory claims. Consumers are entitled to a trial in court, with a jury and the extensive discovery needed to prove their claims. Arbitration is a great idea in theory, but with more oversight, regulation and clear rules the new system will be fair, efficient and cost-effective for both consumers and corporations.