

March 20, 2000

Secretary
Federal Trade Commission
Room H-159
600 Pennsylvania Avenue, N.W.
Washington, D.C. 20580

Re: Alternative Dispute Resolution for Consumer Transactions in the Borderless
Online Marketplace

Trial Lawyers for Public Justice ("TLPJ") respectfully submits the following public comments in response to the Federal Trade Commission ("the FTC") and the Department of Commerce's ("the Department") Initial Notice Requesting Public Comment and Announcing Public Workshop (the "Initial Notice").

TLPJ also respectfully requests that TLPJ Staff Attorney F. Paul Bland, Jr. be permitted to participate as a panelist in the public workshop to be held in Spring 2000.

TLPJ's comments urge the FTC and the Department not to support or endorse or encourage the use of mandatory binding pre-dispute arbitration for international on-line transactions. Our experience and extensive research into the use of mandatory binding pre-dispute arbitration in the United States reveals that it is subject to serious and widespread abuse. A great many American consumers have lost important constitutional rights to mandatory binding pre-dispute arbitration without realizing that this had occurred, and many mandatory binding pre-dispute arbitration systems are severely unfair to consumers. We respectfully suggest that if the FTC and the Department undertake to encourage the use of Alternative Dispute Resolution ("ADR") for on-line transactions, that they only encourage the use of ADR that is voluntary (not mandatory), non-binding, and post-dispute in nature.

INTEREST OF TLPJ

Trial Lawyers for Public Justice is a national public interest law firm that specializes in precedent-setting and socially significant civil litigation and is dedicated to pursuing justice for the victims of corporate and governmental abuses. Litigating throughout the federal and state courts, TLPJ prosecutes cases designed to advance consumers' and victims' rights, environmental protection and safety, civil rights and civil liberties, occupational health and employees' rights, the preservation and improvement of the civil justice system, and the protection of the poor and the powerless.

Over the past two years, TLPJ has been contacted by numerous consumer attorneys around the nation facing mandatory arbitration schemes that threatened to deprive their clients of their day in court. We have also spoken directly with a large number of consumers themselves. In each case, the consumers wished to pursue their claims through the civil justice system, and to

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have their cases heard by a jury of their peers, but the corporate defendant sought to force these claims into arbitration. As a result of our investigations and research, TLPJ has become convinced that, in many cases, mandatory arbitration is seriously abused.

TLPJ has represented a number of clients resisting arbitration abuse, has filed *amicus* briefs in several cases around the nation on this issue, and has provided assistance, legal research and advice to more than 50 consumer attorneys fighting arbitration abuse in more than 20 states. We have also have written several articles on this topic, and spoken about it at conferences and continuing legal education seminars in Chicago, Denver, Hartford, Houston, Kansas City, San Francisco and Washington, D.C.

TLPJ has not been extensively involved in issues of international law or electronic commerce, and does not purport to offer great expertise with respect to some of the technology issues posed by some of the questions set forth in the Notice. Our litigation and advocacy to date have been exclusively based within the United States, and we are not in a position to comment upon ADR systems that may exist or operate elsewhere in the world. Nonetheless, our extensive research into mandatory predispute binding arbitration in the United States may inform some of the FTC and Department's conclusions as to the sort of ADR that should be encouraged for global online transactions. By studying what can happen "when ADR turns bad," the FTC and the Department can avoid encouraging systems susceptible to great abuse.

COMMENTS ON MANDATORY BINDING PRE-DISPUTE ARBITRATION IN THE UNITED STATES TODAY

The second set of questions posed by the Department and the FTC asks:

2) Under what circumstances is ADR used to resolve disputes about consumer transactions today? How does ADR work in such cases? How are decision makers or mediators selected under ADR program? What lessons can be taken from such a mechanism?

In TLPJ's experience, there are a wide variety of ADR programs in operation throughout the United States today. Many of these programs operate fairly and successfully, to the general satisfaction of their participants, particularly (a) many non-binding mediation programs; (b) post-dispute voluntary arbitration programs; and (c) binding predispute mandatory arbitration programs agreed to by two or more equally sophisticated commercial entities who are equally likely to be repeat players in the arbitral forum. TLPJ has no objection to any of these sorts of ADR, and has largely heard favorable reports about such efforts.

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However, many American consumers, employees and victims have had a very different experience with predispute binding arbitration. In a relatively recent but very rapidly growing phenomenon, large corporations are imposing binding arbitration upon largely unaware individuals in a number of different commercial settings. Mandatory arbitration clauses are showing up in credit card agreements, automobile and computer sales contracts, HMO and health insurance contracts, employment contracts, home sales contracts, and many others.

In far too many cases, these arbitration clauses are extremely unfair. When the FTC and the Department hear comments in response to the Initial Notice that sing the praises of mandatory pre-dispute binding arbitration, it is very unlikely that any of this praise will come from individual consumers, employees or victims, or from anyone who represents such individuals or advocates their interests.

I. MANDATORY ARBITRATION IS OFTEN IMPOSED UPON AMERICANS WHO DO NOT REALIZE OR UNDERSTAND THAT THEY ARE LOSING CONSTITUTIONAL RIGHTS.

Literally millions of Americans have unknowingly received mandatory arbitration clauses in a manner that ensures that the clauses would not be read or understood by all but a very few of their recipients. We have seen dozens of arbitration clauses, including clauses used by some of the largest and richest corporations in the United States, that are (a) cast in dense and cryptic legalese that is incomprehensible to lay persons (and even many lawyers); (b) set forth in minuscule print, often on the back side of a document; and (c) buried in the center of a mailing that contained a variety of other pieces, most of which were solicitations and advertisements unlikely to be read by most recipients. Even when consumers are asked to sign or initial below or at the arbitration clause, it is often in the context of a transaction where the consumer is asked to quickly flip through a large body of “standard” documents or contract provisions, which rarely includes an explanation of the arbitration clause.

In light of these sorts of common practices, it should not be surprising that most people first learn that a company says that they have lost the right to sue it in court – and that they have “waived” their constitutional right to trial by jury – only after a dispute rises. In most cases, an individual’s first awareness of an arbitration clause comes as a bitter surprise. We have spoken to literally hundreds of persons on this topic in the last few years, including consumer and civil rights attorney’s, consumers, employees, journalists and arbitrators. Again and again in those conversations, we have heard from people – often very angry, very dissatisfied people – who had never known that they had been sent an arbitration clause, and who believed that they had never agreed to such a clause.

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Some courts in the U.S. have taken a dim view of “surprise” arbitration clauses, and have held that individuals may not be found to have waived their constitutional rights to a day in court and to trial by jury unless they knowingly, voluntarily and intelligently agreed to arbitrate all disputes. In several other cases, however, courts have effectively held that consumers will be legally bound by any language contained in any fine print that was sent to them in any manner, regardless of whether that language takes away their constitutional rights to a day in court and to trial by jury. A number of courts have treated consent as a purely formal and constructive requirement, unconnected to the actual state of an individual’s knowledge or awareness.

Remarkably, a number of corporate defendants have filed lengthy briefs in cases across the nation sharply opposing the notion that one should not be forced into arbitration unless one agreed to arbitrate knowingly, voluntarily and intelligently. This has produced the odd spectacle of some of America’s wealthiest corporations, represented by some of its largest and best-known law firms, arguing that constitutional rights may be taken from citizens *unknowingly*, *involuntarily* and *unintelligently*. Some of these same companies have also railed (sometimes with success) against those courts that have insisted that waivers of the right to a jury trial be “unambiguous” and “unequivocal.”

Another common problem in the current American legal landscape is arbitration clauses that are sent out to consumers only after they have agreed to a transaction. Some such clauses are included in the packaging with computers that are delivered to consumer’s homes, others are sent to home buyers weeks after the closing on their properties, and still others are included in a “second” contract of a two contract agreement where a consumer buys an item and then also finances his or her purchase with the seller via a financing agreement that contains an arbitration clause. While consumers and their attorneys are challenging these sort of late arriving arbitration clauses in many settings, several early U.S. court decisions on the subject suggest that some courts are quite willing to treat consent as a merely formal requirement in this context as well.

The issue of consent should be at the forefront of the FTC and Department’s deliberations about the possibility of encouraging ADR in on-line transactions, because at the same time that corporate defendants are rushing to take disputes to arbitration service providers, very few consumers are seeking out these services. *See* Caroline E. Mayer, “Win Some, Lose Rarely? Arbitration Forum’s Rulings Called One-Sided,” *The Washington Post*, March 1, 2000 (“Since First USA implemented its arbitration clause in early 1998, it has filed 51,622 claims against consumers with the forum. . . . Meanwhile, only four consumers have filed cases against First USA with the forum.”) Similarly, at a March 14, 2000 discussion in Hartford, Connecticut before several sections of the Connecticut Bar Association, American Arbitration Association (“AAA”) representative Karen Jalkut stated that AAA had handled more than 140,000 arbitrations in 1999, but that fewer than 300 of them had been initiated by consumers.

These statistics refute one of the more common defenses offered by supporters of mandatory arbitration. At the March 1, 2000 United States Senate Judiciary Committee hearing, several Senators asked witnesses testifying against mandatory predispute binding arbitration some version of this question: "If mandatory arbitration is not allowed, won't consumers lose the valuable right to take the corporation to arbitration?" This was also a central theme of the witness speaking on behalf of several banking trade groups. The statistics cited above, however, demonstrate that relatively few consumers consider this option to be very valuable. Thus, for example, only four First USA consumers found mandatory arbitration to be valuable, compared to the more than 51,000 times that the company found it to be valuable.

The disinterest of many consumers in submitting their claims to arbitration is particularly striking in light of the energetic propaganda sent out by some companies to individuals. When a Red Lobster restaurant decided to impose a forced arbitration program upon its employees, for example, it showed them a slick videotape telling the employees what a boon arbitration would be to them. The video features in part a man identified as Bruce Chapin, an arbitrator with the American Arbitration Association, answering questions from employees (or actors pretending to be employees, it is not clear). Two of the exchanges go as follows:

Q. Won't I be giving up some rights by going in front of an arbitrator instead of the court with a jury?

A. I don't believe so. The goal is the same: that's a full fair hearing. The only thing that changes is the way we go about achieving the goal. In arbitration we can move to that goal quicker and sooner and in a more informal and private setting. To try to move to that goal in the court setting often becomes time consuming and expensive, and I can assure you that the court system will assure you that the arbitration system will be a full and fair hearing for you.

Q. But doesn't the constitution guarantee every American a right to trial by jury?

A. Certainly any one who is ever charged with a crime should insist upon a jury trial. But in a civil setting, a dispute in the workplace, for instance, this is not a matter that would be best tried in front of a jury. The amount of time that would be spent, the amount of money to be expended to get before a jury with that kind of dispute does not make it cost effective. . . .

These statements express a value judgment that constitutional provisions like the Seventh Amendment (protecting the right to trial by jury in *civil* trials), and corresponding state civil jury trial provisions, are bad policy and should be ignored. AAA's representative addresses the subject as if we had a Bill of Suggestions rather than a Bill of Rights. Despite such urgings, however, the

actual data shows that corporations are far more interested in pursuing arbitration than their consumers are.

II. MANDATORY PREDISPUTE BINDING ARBITRATION IS OFTEN EXTREMELY UNFAIR TO AMERICAN CONSUMERS.

The mandatory arbitration clauses imposed upon Americans without their consent are also far too often seriously unfair. These clauses are often drafted in such a way that renders them completely one-sided, setting up a playing field where the consumer stands little chance of winning regardless of the strength of his or her case.

Without attempting to chronicle every abuse of mandatory arbitration that we have encountered, these comments will discuss some of the most serious and prevalent problems.

C Arbitration Clauses Often Impose Unreasonably Large Fees. In paying taxes, American citizens cover the costs of operating the court system, so they are only required to pay a nominal filing fee to initiate a lawsuit. People forced into arbitration frequently pay far greater fees to file their case, and to have the decision maker hear their case and hear various motions that go with the case, than the fees consumers must pay to file a case in court. We have seen a number of arbitration clauses that require individual consumers to pay fees that exceed the amount of money they would stand to gain if they won their cases. A number of consumers and consumer attorneys have told us that they (or their clients) would abandon their cases if forced into arbitration, because they could not afford the fees likely to be charged by the arbitrators. This problem is exacerbated by the widespread practice of hidden or uncertain fees, where an arbitration service provider loudly touts a small “filing fee” (such as the National Arbitration Forum (“NAF”)’s initial filing fee of \$49), but then adds on a variety of subsequent fees for handling disputes over discovery, motions and the like. We are familiar with a recent employment case where a person was required to pay arbitration fees of more than \$60,000 to pursue civil rights claims. While it is true that a number of courts have refused to enforce arbitration clauses that imposed excessive fees upon consumers, some other courts have treated the issue very lightly and enforced arbitration clauses in the face of evidence that the large fees would end the claimants’ chances of proceeding.

C Arbitration Clauses that Require Consumers to Travel Long Distances to Resolve their Disputes. A number of arbitration clauses that we have seen require that any consumer having a dispute with a company go to a single location to resolve that dispute. In light of the size of the United States, requiring all consumers in the country to go to any one place – whether it is San Jose, Minnesota or Maine – is certain to deter millions of persons from raising their claims.

- C **One-way arbitration clauses.** Many arbitration clauses drafted by large companies and imposed upon individuals provide that if the individual wishes to pursue a claim, he or she must take the complaint to binding arbitration, but if the companies wish to pursue a claim, they retain the option of going to either arbitration or to court. These clauses are emblematic of a one-sided transaction where the party with the predominant economic power forces its will upon the weaker party. One court has characterized these types of clauses as the sort of contract that a rabbit might make with a fox. *Arnold v. United Companies Lending Co.*, 511 S.E.2d 854 (W. Va. 1998). While a number of courts have refused to enforce such contracts, some other courts have embraced and approved of these clauses.
- C **“Loser Pays” Provisions.** Many arbitration clauses require an individual who loses his or her case to pay the corporate defendants’ attorneys’ fees and expenses. In fact, one of the most prominent arbitration service providers in the United States, the NAF, generally follows a “Loser Pays” approach. Given that most individual consumer claims are relatively modest in size, the prospect of potentially paying enormous fees to a corporate defendant’s high priced law firm (fees that could easily exceed \$200 or \$300 per hour for a partner in a reputable firm in a large city) is all too often enough to deter a consumer from going forward with even the strongest claim.
- C **Arbitration Clauses that Shorten the Limitations Period for an Individual to Bring a Claim.** Many arbitration clauses purport to re-write the substantive law under statutes or the common law by shortening the limitations period for various causes of action. One HMO arbitration clause that we have seen provides that any HMO member wishing to raise a dispute in arbitration must do so within 60 days of discovering that they have a claim, a provision that would ensure that most members of the HMO would never get a fair hearing on any legal claims they might have. While a number of courts have struck down provisions of this sort, it is far from clear at this time that every jurisdiction would refuse to enforce such a rule.
- C **Clauses that Limit the Remedies An Arbitrator May Provide.** A number of arbitration clauses prohibit punitive damages, limit the ability of the arbitrator to grant injunctions, deny attorneys fees to prevailing plaintiffs, or otherwise ensure that the remedies available to a consumer are weaker than those available in court, regardless of the merits of their case. Again, a number of courts have refused to enforce clauses of this sort, but this judicial reaction has not deterred this type of abuse.
- C **Clauses that Prevent Consumers from Pursuing their Claims on a Class Action Basis.** A number of corporate defendants and their defense attorneys have implemented

or advocated for mandatory arbitration clauses because they see these clauses as a means of blocking the possibility of class action liability. This is crucial in many cases, because frequently individual consumer claims are so small that consumers will have no realistic remedy unless it is possible for them to proceed on a class action basis. As a result, mandatory arbitration provisions that prohibit class-wide adjudication or constructively require individualized adjudication are often effectively exculpatory clauses – they insulate a company from liability no matter what it does to its consumers, so long as the consumers are individually harmed in increments too small for them to locate counsel to pursue their individual claims. Some courts have begun to seriously question the enforceability of arbitration clauses that bar class actions in such circumstances,¹ but most courts have been insensitive to or uninterested in the issue.

- C **Some Arbitrator Service Providers Advertise Themselves to Businesses in Ways that Suggest that the Arbitrators Are Likely to Be Biased in Favor of the Corporations and Against their Consumers.** We have seen documents, for example, where the for-profit NAF has marketed its arbitration services as providing a defense for financial services companies against lawsuits from their consumers. For example, NAF boasts in its solicitations that it prohibits class actions, that it limits recoveries to the amount initially claimed, that it doesn't decide cases on "equity" and that it limits discovery. If a court were to solicit business from a party that might come before it with strong hints that the solicited party would get a good deal in her or his courtroom, there is no doubt that this would be improper behavior. The same standard should apply to NAF.
- C **The Lists of Arbitrators Used By Some Arbitration Service Providers in Many States Are Tilted Towards Corporate Defense Lawyers.** TLPJ knows of no broad empirical data relating to the background of arbitrators as a group across the United States. A number of consumer attorneys have reported to us that the list of arbitrators used by major arbitration service providers such as AAA in their states is overwhelmingly comprised of defense attorneys. Several consumer attorneys have told us that they sought to become AAA arbitrators, only to be told that the AAA lists in their state are filled, but then they later learned that more corporate defense lawyers have subsequently been added to the list. While we have also heard of a few states where consumer attorneys report that the AAA lists are more balanced, the broad tendency appears to be a heavy preponderance of defense attorneys.

¹ See *In re Knepp*, 229 B.R. 821 (N.D. Ala. 1999); *Johnson v. Telecash, Inc.*, 1999 U.S. Dist. LEXIS 20632 (D. Del. 1999); *Ramirez v. Circuit City Stores, Inc.*, 90 Cal. Rptr. 2d 916 (1999); and *Powertel v. Bexley*, 743 So. 2d 570 (Fla. App. 1999).

- C **Some Arbitration Service Providers Maintain Inappropriately Close Relationships with Corporate Clients.** Documents and evidence on file at the Federal Communications Commission (“FCC”) suggest that telecommunications giant MCI has a very close relationship with the mandatory arbitration services provider (J.A.M.S./ Endispute, or “JAMS”) specified in its Tariff with the FCC. Allegations included in these pleadings indicate, for example, that (a) MCI paid hundreds of thousands of dollars to JAMS entirely separate from fees to arbitrate specific disputes; (b) MCI provided valuable free long distance services to JAMS; (c) that while one part of a large corporation held a majority of the shares of JAMS, another part of this corporation held more than \$23 million of MCI stock at the same time that JAMS was arbitrating disputes involving MCI; and (d) JAMS was providing information, reports and analyses about other MCI arbitrations to MCI that it was not provided to consumers arbitrating disputes against MCI. TLPJ is also aware of several lawsuits in federal court in Texas and state court in Alabama raising serious questions about the close relationship of First USA Bank and the National Arbitration Forum.
- C **Some Arbitrators Nearly Always Rule for Corporate Defendants.** The Washington Post has reported that “The data, disclosed last month by First USA in a class-action lawsuit challenging mandatory arbitration, show that not only has the company sought arbitration far more often than consumers, it has also won in 99.6 percent of the cases that went all the way to an arbitrator.” See Caroline E. Mayer, “Win Some, Lose Rarely? Arbitration Forum’s Rulings Called One-Sided,” *The Washington Post*, March 1, 2000. The story notes that First USA had won 19,618 cases that went to an arbitrator, and that consumers had won only 87.
- C **Arbitrators often favor large corporate “repeat player” clients.** Arbitrators often face powerful economic incentives that can affect their neutrality. Many arbitrators compete for the same business. If an arbitrator rules against a corporate client too often, the company can easily take its business to another arbitrator. See J. Sternlight, *Panacea or Corporate Tool?: Debunking the Supreme Court’s Preference for Binding Arbitration*, 74 Wash. U.L.Q. 637, 684-85 (1996); D. Schwartz, *Enforcing Small Print to Protect Big Business: Employee and Consumer Rights Claims in an Age of Compelled Arbitration*, 1997 Wisc. L. Rev. 33, 60-61 (1997); L. Bingham, *Employment Arbitration: The Repeat Player Effect*, 1 Empl. Rts. & Empl. Policy Journal 1 (1997) (employees recover a lower proportion of their claims in repeat player cases than in non-repeat player cases); James L. Guill, Edward A. Slavin, Jr., *Rush to Unfairness: The Downside of ADR*, 28 Judges’ Journal No. 3, at 8, 11 (1989) (“[A]n arbitrator’s decision might be influenced by the desire for future employment by the parties. . . . Some arbitrators openly solicit work. They write letters to parties noting their availability, sometimes enclosing samples of their awards. They occasionally call on parties at their offices for the same purpose”)

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(citations omitted). *See also id.* at 12 (“Consider the parties’ frequency of need for an arbitrator, the arbitrator’s necessary qualifications for being selected, and the payment plan, the odds are against the individual plaintiff versus the manufacturers, health providers, and corporate landlords who will likely be parties to dispute resolution time and again.”) Judges and juries are less prone to these temptations.

CONCLUSION

Our experience demonstrates that mandatory binding predispute arbitration systems in the United States are often seriously abused. Consumers often find themselves locked into systems that they did not knowingly, voluntarily or intelligently choose, and the systems are all too often one-sided, anti-consumer and unfair.

One of the questions posed by the Initial Notice is:

15) What should be the role of governments, if any, in connection with the use and/or development of alternative dispute resolution programs for online consumer transactions?

When considering whether and how to promote the use of ADR for international on-line transactions, the FTC and the Department should vigorously work to avoid expanding the scope and prevalence of these abuses. As a general rule, we support that ADR that is non-binding, truly voluntary, and solely post-dispute. If consumers have a meaningful choice as to whether they will participate in an ADR system, then the persons providing ADR services will have an incentive to design much fairer ADR systems, and consumers will be given an opportunity to correct abuse.

Respectfully,

F. Paul Bland, Jr.
Staff Attorney