

UNCONSCIONABILITY SHOULD NOT BE THE SOLE
ARBITER OF WHETHER TO ENFORCE MANDATORY
ARBITRATION PROVISIONS

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Discussions about whether companies should be able to force consumers to arbitrate their claims are often side-tracked by a debate about the desirability of class actions as a means of ensuring compliance with laws that the government has neither the resources nor the willingness to enforce. This is because arbitration simply cannot accommodate the procedures and complexities inherent in class actions and is instead designed to resolve individual claims. For example, under Federal Rule of Civil Procedure 23, which governs class actions filed in federal court, putative class members who are not direct participants in the case are required to receive notices about the proceedings and, under modern jurisprudence, a public hearing to decide whether a class should be certified.¹ None of these procedures would appear to be possible in arbitration since, by its very nature, arbitration is a confidential proceeding.

What is lost in this debate is something on which most observers agree: the consumer “contracts” where companies bury their mandatory arbitration provisions are classic contracts of adhesion. They are non-negotiable form contracts where one party has vastly superior bargaining power over the other. Typically, the provisions are very broad in scope, requiring consumers to arbitrate “all disputes arising from the sale, condition or performance” of the product or service sold.² Consumers do not bargain over their terms. Nor do most consumers read these contracts and those who do are unlikely to focus on the dispute resolution provisions. Indeed, these “contracts” are not what most people would consider

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¹ Fed. R. Civ. P. 23.

² *Norcia v. Samsung Telecomms. America, LLC*, 845 F.3d 1279, 1284 (9th Cir. 2017).

contracts at all, an agreement contemporaneous with the sale whereby the seller provides a product or service in return for the consumer's consent to arbitration. Many of the mandatory arbitration provisions in use are provided to consumers as part of a shrink-wrap agreement or owner's manual sent to consumers after they purchase the product or service at issue. The odds of a consumer reading a mandatory arbitration provision after she has made her buying decision are extremely low. The chances of that same consumer taking some action to negotiate or opt out of such a provision by returning the product is, if possible, even more remote.

The question is whether we should care that mandatory arbitration provisions are contracts of adhesion. I believe we should, at least in situations where the consumer's claim exceeds a certain monetary threshold, namely the amount of money that would be enough to attract a reasonably priced lawyer to handle the consumer's claim on an individual basis. It is in those situations that a consumer's unwitting agreement to an "adhesive" mandatory arbitration provision has the greatest adverse impact on her due process rights. The law does not favor the implied waiver of due process rights, and that is exactly what happens when a consumer is forced to arbitrate a claim that she otherwise could have prosecuted in court with the assistance of a lawyer.

I. MANDATORY ARBITRATION CLAUSES IN CONSUMER CONTRACTS ARE CONTRACTS OF ADHESION

As one state supreme court has stated, contracts of adhesion are "a fact of modern life."³ But so is texting while driving, and we do not condone that practice. Currently, state laws do not generally prohibit contracts of adhesion. A contract of adhesion is only unenforceable if it is either procedurally or substantively unconscionable. A company that effectively hides a mandatory arbitration provision by burying it in small print or in a place a reasonable consumer would not know to look is being procedurally unfair and risks that the provision will not be enforced. An agreement is substantively unfair when it is so one-sided as to be oppressive or impossible for a reasonable person to understand. For example, a provision that requires a consumer to arbitrate in a forum that is either geographically impractical or inordinately expensive given the stakes of the claim at issue may be voided by a court. Similarly, an

³ Kinkel v. Cingular Wireless LLC, 223 Ill. 2d 1, 26 (2006).

agreement to arbitrate that can only be understood by a lawyer is vulnerable to challenge.

Companies that depend on sales to consumers but want to avoid becoming embroiled in class actions generally understand these rules and utilize arbitration clauses that pass muster both procedurally and substantively. Those that do not – and there are still plenty of companies that overreach or bury the clauses in the fine print for reasons that are difficult to understand – deserve to be sued over the enforceability of those clauses. But should that be the end of our discussion? Should the outer bounds of mandatory arbitration agreements be defined solely by reference to law of the state law of unconscionability?

Unconscionability is a contract principle.⁴ A contract requires assent by each party to the contract and to each of the contract's terms. As discussed above, we know that consumers do not read and therefore, at best, only impliedly assent to mandatory arbitration provisions used by many sellers of consumer products and services. The law normally does not allow the implied waiver of a legal right unless the person has engaged in a course of conduct that is at odds with the intent to exercise that right. Given the broad scope of many arbitration provisions, it is difficult to imagine that a consumer who purchased a product intended to consent to waive her right to litigate any and all claims associated with that product.

For example, a consumer who buys a smart watch but does not bother to read the mandatory arbitration agreement contained in her bill of sale or warranty may have impliedly waived her right to litigate a claim that the watch does not function properly. But what if the watch explodes and burns her arm? Or what if the manufacturer fraudulently induced her to buy the watch in the first place through factual misrepresentations? Did she really intend to waive her right to bring a personal injury or consumer fraud lawsuit in court? I doubt it. Odds are she did not even contemplate the smart watch exploding or the company defrauding her and assumed that the government would not have allowed the company to fraudulently market or sell the product if it was not safe. If the consequence of the smart watch exploding is that the consumer suffered third degree burns up and down her arm, it is likely that a lawyer would take her case and be able to litigate it in court on a contingent fee. If the watch just stopped functioning because of the

⁴ *Unconscionability*, Black's Law Dictionary (5th ed. 1979). (Defining unconscionability as a "basic test . . . of contract.")

explosion but did not injure the consumer, the consumer should be entitled to a new watch or a refund of her money, but is probably not going to recover any additional damages even if she pursued a claim in court. If the consumer was told the watch was waterproof up to 100 meters but it leaked, the consumer would be entitled to the same relief. These latter two types of claims can be handled well in an arbitration setting without depriving the consumer of a right she might otherwise have exercised or a remedy she might have obtained in court.

What if the smart watch explodes and causes first or second-degree burns that are painful but temporary? On the one hand, the consumer probably never contemplated the watch exploding and therefore only impliedly agreed to waive her right to bring such a claim. On the other hand, her claim probably is not worth enough money to be litigated anywhere but in small claims court without the assistance of a lawyer.⁵ Small claims courts are characterized by lower filing fees, limited discovery, simplified pleading and motion procedures, relatively quick resolution tracks, and no class actions.⁶ Sound familiar? It should; these are the same characteristics as consumer arbitrations. Since there is practically no difference between the procedural rules used in the two fora, forcing a consumer to bring her claim in arbitration – even though she only “agreed” to do so via a contract of adhesion – does not raise serious due process concerns. In contrast, requiring a consumer to arbitrate her serious personal injury claim rather than let her paid lawyer prosecute that claim in non-small claims court could seriously impact her due process rights.

II. IMPOSING MONETARY LIMITS ON MANDATORY ARBITRATION PROVISIONS IN CONTRACTS OF ADHESION

A simple means exists in most states to channel consumer claims either to arbitration or to court where there is a mandatory arbitration provision that a court finds to be a contract of adhesion: minimum jurisdictional limits. In Illinois, for example, claims worth \$10,000 or less are handled in small claims court.⁷ Given the court costs, litigation expenses and legal fees associated with prosecuting a claim in court, a consumer in Illinois with a \$10,000 claim

⁵ In Illinois, for example, small claims courts handle disputes with \$10,000 or less at issue. IL R S CT Rule 281.

⁶ See e.g., IL R S CT Rules 282-289 (Illinois small claims procedures).

⁷ IL R S CT Rule 281.

is going to have a very difficult time finding a lawyer to prosecute that claim for her in court.⁸ Requiring a claim that would otherwise proceed in small claims court without the assistance of a lawyer to be resolved in arbitration would not adversely impact the consumer's due process rights. Obviously not all states have the same jurisdictional thresholds.⁹ But courts¹⁰ could take judicial notice of the minimum monetary thresholds in the consumer's state of residence to determine whether forcing her to arbitrate meaningfully impacts rights she might have exercised by hiring a lawyer to bring the claim in a forum other than the state's small claims system.

This proposal would not, of course, prohibit companies from arguing that their mandatory arbitration provisions are not contracts of adhesion and ought to be enforced as written. To strengthen that argument, companies could build into their arbitration provisions mechanisms to alert consumers to the due process consequences of their agreement to waive their due process right to bring certain claims in court and of the option to submit their claims, if eligible, to small claims proceedings.¹¹ Companies also could limit the scope of their arbitration provisions to claims seeking the return of monies paid for a product or service or for a replacement product or service, or the warrantability of either, and

⁸ If the case were filed in the Circuit Court of Cook County, Illinois, for example, the consumer would be required to pay a filing and jury fee of approximately \$300.00. If we assume her lawyer would need to spend 25 hours on the case to bring it to trial at an effective rate of \$200/hr. and incur litigation costs estimated at 10% of fees, it would not be profitable for the lawyer to take the case under a standard 33% contingency arrangement.

⁹ According to one source, small claims court thresholds range between \$2,500 and \$25,000, see <https://www.nolo.com/legal-encyclopedia/small-claims-suits-how-much-30031.html>.

¹⁰ It is now beyond dispute that the decision whether to enforce a mandatory arbitration provision under the Federal Arbitration Act is made by courts, not arbitrators.

¹¹ See e.g., American Arbitration Association, *Consumer Due Process Protocol Statement of Principles, Principle 11* (April 17, 1998), [https://www.adr.org/sites/default/files/document_repository/Consumer%20Due%20Process%20Protocol%20\(1\).pdf](https://www.adr.org/sites/default/files/document_repository/Consumer%20Due%20Process%20Protocol%20(1).pdf). ("Consumers should be given: . . . clear and adequate notice of the arbitration provision and its consequences . . . ; reasonable access to information regarding the arbitration process, including basic distinctions between arbitration and court proceedings, related costs . . . ; notice of the option to make use of applicable small claims court procedures as an alternative to arbitration . . . , etc.").

permit consumers to bring personal injury claims in court. Finally, companies could provide in their consumer contracts that claims worth less than a specified monetary threshold would be subject to arbitration and that only claims that exceed that threshold could be pursued in court.

III. POTENTIAL OBJECTIONS TO MONETARY LIMIT PROPOSAL

I can imagine concerns about the proposal I have outlined from both consumer advocates and from companies that use mandatory arbitration agreements. Consumers might complain that it will be expensive to litigate a case if they must hire a lawyer to challenge the enforceability of the arbitration agreement to a claim worth more than \$10,000. That is true, but is already the case where a company has included a mandatory arbitration provision in its consumer “contracts.” Moreover, that concern could be ameliorated by allowing courts to order companies to pay the attorney’s fees of consumers who successfully prove an arbitration agreement is unenforceable. Objectors might also point out that arbitrators usually severely limit discovery, making it more difficult for consumers who do not have the same access to information as companies to win their claims in arbitration. While this is generally accurate, most arbitrators are former judges or litigators who understand this uneven playing field and have fairly broad discretion under the rules governing arbitration to order a defendant to provide specific discovery.¹²

Consumer class action lawyers undoubtedly would object to this proposal on the ground that it would inhibit their ability to consolidate low dollar, consumer claims. Given the ubiquitous nature of mandatory arbitration provisions in consumer contracts, this concern seems overblown. Given most consumer product companies utilize these provisions and most courts are quick to enforce them, class action lawyers already face restrictions on the types of claims they can bring on a class basis. More importantly, the empirical evidence gathered by the Consumer Financial Protection

¹² See e.g., American Arbitration Association, *Consumer Due Process Protocol Statement of Principles, Principle 13* (April 17, 1998), [https://www.adr.org/sites/default/files/document_repository/Consumer%20Due%20Process%20Protocol%20\(1\).pdf](https://www.adr.org/sites/default/files/document_repository/Consumer%20Due%20Process%20Protocol%20(1).pdf). (“No party should ever be denied the right to a fundamentally-fair process due to an inability to obtain information material to a dispute.”).

Bureau shows that consumers who are willing to pursue their claims on an individual basis prevail more frequently and recover more money in arbitration than as a member of a class action in court.¹³ While it is true that many consumers would not pursue their claims in any forum but for the existence of a class action that allows their claim to be adjudicated without their involvement, the primary purpose of class action rules is not to give consumers a vehicle to file lawsuits they would not otherwise file but rather to help courts effectively manage a large number of related lawsuits while ensuring that individual litigant's due process rights are respected.¹⁴

Companies selling their products or services to consumers might complain that, under my proposal, they would not enjoy the "benefit of their bargain" with consumers. As discussed above, contracts of adhesion are by no means the result of real bargaining with consumers, who are basically presented with a take-it-or-leave-it proposition. Companies also might argue that this proposal could lead to consumer lawyers or class action lawyers exaggerating the size of consumers' claims to ensure disputes end up in court. While this is certainly possible, courts are accustomed to resolving disputes over monetary thresholds and presumably would see through such chicanery. Finally, companies might argue that leaving the enforceability of a mandatory arbitration provision to the vagaries of individual state jurisdictional thresholds would lead to lack of predictability. A \$10,001.00 claim in one state would be litigated in court while that same claim in another court would be subject to mandatory arbitration. This concern is valid but, again, overstated. The vast majority of consumer claims are worth less than the monetary maximum of any small claims court. If the real concern of companies is that they will be inundated with class actions where the average claim exceeds a state's minimum

¹³ See Arbitration Agreements, 81 Fed. Reg. 32830 (May 24, 2016) (noting that a study by the Bureau of Consumer Financial Protection found that 87% of class actions result in no compensation for consumers and that the average class member recovery is \$32.35 as opposed to \$5,400 in arbitration).

¹⁴ Class actions can serve other, albeit subsidiary, purposes such as encouraging the enforcement of consumer protection laws by private attorneys general. However, as discussed above, this article is not going to wade into that controversial thicket.

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threshold for non-small claims, they can always specify in their arbitration provisions a higher monetary threshold than the state provides for small claims and take their chances as to whether it will be enforced. My proposal would cut down on the number of class actions but not eliminate the more serious ones where a substantial amount of money is at stake in each consumer's claim. To me at least, this would reflect a better balancing of companies' interest in directing consumers into arbitration with the due process rights of consumers who have suffered serious losses or injuries and never intended to waive their right to assert those claims in a court of law.