UNVEILING FAIRNESS FOR THE CONSUMER: THE LAW, ECONOMICS AND JUSTICE OF EXPANDED ARBITRATION

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Abstract: In recent years, the US Supreme Court has rather controversially extended the ambit of the Federal Arbitration Act to extend arbitration's reach into, *inter alia*, consumer matters, with the consequence that consumers are often (and unbeknownst to them) denied remedies which would otherwise be available. Such denied remedies include: recourse to class action proceedings, effective denial of punitive damages, access to discovery and the ability to resolve the matter in a convenient forum.

The court's extension of arbitration's ambit is controversial. Attempts to overturn this extension have been made in Congress, but to no avail. In contrast to American law, European consumer law looks at pre-dispute agreements to arbitrate directed at consumers with extreme suspicion, and does so on the grounds of fairness. In contrast, some argue that pre-dispute agreements in consumer (and employment) matters are consumer welfare enhancing: they decrease the costs of doing business, and the savings are in turn passed on to the consumer. This Article examines these latter claims from both an economic and normative perspective.

The economic analysis of these arguments shows that their assumptions do not hold. Rather than being productive of consumer surplus, the use of arbitration is likely to have the opposite effect. The industries from which the recent Supreme Court cases originated not only fail to exhibit the industrial structure assumed by the proponents

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of expanded arbitration, but are also industries which exhibit features that facilitate consumer welfare reducing collusion.

The normative analysis addresses the fairness concerns. It is explicitly based upon John Rawls' notion of "justice as fairness," which can provide a lens to evaluate social institutions. This Rawlsian analysis considers the use of extended arbitration in consumer matters in the light of the earlier economic results. It suggests that the asymmetries present in the contractual allocation of rights serve as prima facie evidence that such arbitration–induced exclusions are prima facie unjust and unfair. However, as asymmetry is only a prima facie test, a generalized criticism of the arbitration exclusions (of the sort found in Congress and underlying the European regime) is overbroad.

INTRODUCTION

The litigation process is described as having two social functions: dispute resolution and rule formation. "See you in court" or "Tell it to the judge" are typical, but somewhat vernacular, means of expressing the former function of litigation.[1] Litigation also has the benefit of producing rules which can be used by other parties to shape their conduct in the future, and these rules can guide or determine how subsequent judges make their decisions in future cases. However, to a very significant extent, this latter function of litigation is a secondary concern to the parties of the dispute; they do not care about being the next Palsgraf[2] or Carlill.[3] Rather, the litigants want their dispute resolved, and preferably in their favor.

As parties to disputes are generally only interested in the result as it pertains to them, they tend to consider aspects other than rule making for an appropriate dispute resolution system. At minimum, parties will want independent decision makers who respect what are to be viewed as the fundamental rights of the participants. Among these rights are matters such as due process, fairness, and perceived legitimacy. These criteria are usually satisfied in most public dispute resolution systems.

Arbitration, in addition to potentially possessing the above criteria, is often credited with a host of other values conducive to efficient dispute resolution including: speed, privacy, expertise of the

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[1] *See, e.g.*, William M. Landes & Richard A. Posner, *Adjudication as a Private Good,* 8 J. LEGAL STUD. 235, 236 (1979).

[2] Palsgraf v. Long Island R. Co., 248 N.Y. 339, 162 N.E. 99 (N.Y. 1928).

[3] Carlill v. Carbolic Smoke Ball Co., [1892] 1 Q.B. 256 (C.A.).

chosen arbitrator, a less formal (hence potentially less adversarial) forum, and the ability to select governing law and procedure. These advantages are interrelated. For instance, an arbitrator with expertise in a particular industry will not require background evidence to be put before her, thus reducing the litigation costs to the parties. When grounded by an appropriate enabling statute (for example, the Federal Arbitration Act[4] ("FAA")) an arbitrator's decision can have the force of a judicial decision, and can be enforced internationally.

Recent years have witnessed an effort to expand arbitration's domain to account for the perceived advantages of arbitration. In the United States and Canada there has been a movement to use pre-dispute arbitration clauses in consumer matters. Recent court decisions in the U.S. have, quite controversially, removed many of the fetters that have prevented this expansion.[5] These fetters remain in Canada.[6] In stark contrast, EU law disfavors the use of pre-dispute

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[4] Federal Arbitration Act, 9 U.S.C. §§ 1–16, 201–208, 301–307.

[5] These recent decisions have been criticized by members of Congress. Senator Al Franken is among the most vocal critics of these decisions. *See, e.g.,* Senator Al Franken, *Senator Reintroduces Legislation to Restore Consumers, Workers and Small Businesses' Right to Seek Justice through Courts,* AL FRANKEN U.S. SENATOR FOR MINNESOTA, (May 7, 2013), http://www.franken.senate.gov/?p=hot_topic&id=2392. This criticism has resulted in the repeated introduction of Acts to legislatively repeal the Supreme Court's decisions. *See infra* text accompanying notes 49–52. This has been echoed in the press. *See infra* notes 47–48. Academics have also not been shy with their own criticism. *See, e.g.,* S. I. Strong, *Constitutional Conundrums in Arbitration,* 15 CARDOZO J. OF CONFLICT RESOL. 41 (2013) [hereinafter Strong, *Constitutional Conundrums*] (reviewing PETER B. RUTLEDGE, ARBITRATION AND THE CONSTITUTION (2013)). *See also id.* at 55 n.71 (in particular Alan Scott Rau, *Arbitral Power and the Limits of Contract: The New Trilogy*, 22 AM. REV. INT'L. 435 (2011); Judith Resnik, *Comment, Fairness in Numbers: A Comment on AT&T v. Concepcion, Wal-Mart v. Dukes, and Turner v. Rogers*, 125 HARV. L. REV. 78 (2011); Jean R. Sternlight, *Tsunami: AT&T Mobility LLC v. Concepcion Impedes Access to Justice,* 90 OR. L. REV. 703 (2012); Gary B. Born & Claudio Salas, *The United States Supreme Court and Class Arbitration: A Tragedy of Errors*, 2012 J. DISP. RESOL. 21 (2012); Thomas J. Stipanowich, *Punitive Damages and the Consumerization of Arbitration*, 92 NW. U. L. REV. 1 (1997); S. I. Strong, *Resolving Mass Legal Disputes Through Class Arbitration: The United States and Canada Compared*, 37 N. C. J. INT'L L. & COM. REG. 921 (2012) [hereinafter Strong, *Resolving Mass Legal Disputes Through Class Arbitration*].

[6] In Canada some fetters still remain, though arbitration is generally permitted as a means of resolving consumer disputes. *See* Dell Computer Corp. v. Union Des Consommateurs, [2007] 2 S.C.R. 801 (Can.); Seidel v. TELUS Commc'ns Inc., [2011] 1 S.C.R. 531 (Can.). *See also* Shelly McGill, *Consumer Arbitration and Class Actions: The Impact of* Dell Computer Corp. v. Union Des Consommateurs,

arbitration clauses. Directive 93/13[7] makes it clear that, under EU law, there is a presumption that pre-dispute arbitration clauses in consumer contracts are unfair to the consumer and thus invalid.[8]

Similar views have been expressed in the U.S. in the aftermath of recent Supreme Court decisions that have further extended the use of arbitration into the domain of consumer law.[9] All of the discussion resonates with the tune of "unfairness" or "injustice." Yet, this tune is often sung at a very unsophisticated level—with the terms "fairness" and "justice" thrown out at a very intuitive level.

In this Article, I propose to use a developed account of fairness and its relationship to justice to examine the expansion of arbitration into the domain of consumer law. The theory used is John Rawls' well known theory of "justice as fairness,"[10] which provides for a means of determining whether a particular arrangement is just or fair. Rawls' insight is by way of a thought experiment. Designers of a particular social institution are put behind a metaphorical "veil of ignorance," which deprives them of any particular knowledge of morally irrelevant characteristics which they can use to design the social system to their advantage. To the extent that an actual social system reflects one which would be hypothetically designed behind the veil, the actual system can be regarded as "fair" or just.

This analytic lens provides a useful insight into the fairness, and hence justice, of contractual arrangements recently considered by the Supreme Court. I argue that the Rawlsian approach demonstrates that asymmetries in the creation or exclusion of rights and obligations by means of such arbitration agreements are strong indicia of unfairness. However, they are merely prima facia indicia, capable of being rebutted when the benefits of the exclusions are subjected to further scrutiny. As such, sweeping condemnation of such clauses may be too far-reaching.

The examination of these benefits is primarily an economic

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45 CAN. BUS. L. J. 334 (2007); Jonnette Watson Hamilton, *Pre-Dispute Consumer Arbitration Clauses: Denying Access to Justice?,* 51 MCGILL L. J. 693 (2006); Strong, *Constitutional Conundrums, supra* note 5; Strong, *Resolving Mass Legal Disputes Through Class Arbitration, supra* note 5.

[7] Council Directive 93/13/EEC, of 5 April 1993 on Unfair Terms in Consumer Contracts, 1993 O.J. (L 95) 29 [hereinafter Council Directive 93/13/ECC].

[8] *See, e.g.*, CHARTERED INST. OF ARBITRATORS, PRACTICE GUIDELINE 17: GUIDELINES FOR ARBITRATORS DEALING WITH CASES INVOLVING CONSUMERS AND PARTIES WITH SIGNIFICANT DIFFERENCES OF RESOURCES § 1.2 (n.d), *available at* http://www.ciarb.org/information-and-resources/Practice%20Guideline%2017.pdf.

[9] *See infra* text accompanying notes 15–45.

[10] JOHN RAWLS, A THEORY OF JUSTICE (rev. ed. 1999).

task, the results of which suggest that the industries involved in recent Supreme Court consumer arbitration matters have a structure that facilitates collusion and cartel formation. As cartels not only fix prices, but also collude on terms of service, I suggest that a consequence of the use of such exclusions is not to benefit consumers. Rather, the use of arbitration may have the very opposite effect, namely the facilitation of appropriation of consumer surplus. If my suggestion is correct, this has significant import not just for our Rawlsian normative argument, but also it may well undermine the economic assumptions used to justify these exclusions in the first place.

This Article is structured as follows: Part I examines the use of arbitration as a dispute resolution method in international commercial disputes. The widespread use of arbitration in this context points to some of its intuitive advantages as a means of resolving these sorts of disputes. It thus provides an example of paradigmatically "fair" arbitration. Such a paradigm serves as a point of contrast to what follows it.

Part II evaluates the American regime of expanded consumer arbitration. This Part argues that the expansion of arbitration, which could possibly benefit consumers by reducing prices (as some proponents of consumer arbitration argue), has had the actual result of shifting costs onto unsuspecting (and perhaps unsophisticated) consumers.

Part III considers the purported advantages of expanded arbitration. The economic assumptions of these advantages are discussed in Part IV. These assumptions raise concerns of fairness and justice, which are considered in Part V. To address these issues, I use Rawls' perspective, which develops a sophisticated accounting of fairness as a basis for determining the extent to which a particular social institution can be regarded as just. This analysis shows difficulties with some of the exclusions considered by the Supreme Court. However, this analysis does not unequivocally condemn all such exclusions, thus suggesting not just that there may be room for some of these exceptions in normatively "fair" arbitration agreements, but also that legislative efforts to limit the use of exceptions may therefore be overbroad.

I. PARADIGMATICALLY "FAIR" ARBITRATION

Before discussing the FAA and its recent judicial expansion into consumer and employment matters, a few words must be said regarding the type of arbitration that is intuitively viewed as a paradigm of a fair arbitration: namely the use of dispute resolution in the context of a transaction between two parties who possess roughly equal bargaining power.[11] The transaction in question may have an international dimension, which provides an additional reason for the parties to select a private, non-state, means of resolving their dispute.

This international dimension of the contracts governing the transaction introduces not just a need for precision regarding the applicable law which governs the contract and the law governing the arbitration, which can be different; but also may influence a desire for a neutral adjudicator (that is, not of the same nationality as either party). Such a dimension assists in eliminating the feeling that one party may have a "home field advantage," were that party's courts or citizens are permitted to determine the outcome. The use of arbitration may facilitate the parties' confidence in the arbitrator's ability to come to an appropriate decision because of the arbitrator's possession of a specialized background (*e.g.,* specialized knowledge of the practices of a particular industry). Further, arbitration may have the advantage of confidentiality: the parties may prefer that their business affairs and/or the details of their relationships not become widely known within or beyond the industry. The less adversarial nature of the arbitration process may facilitate or not hinder future cooperation between the parties, should they envisage a relationship beyond the contract in dispute.

If the transaction occurs in the context of a specialized market, it may make sense to appoint an adjudicator with expertise in that market. This typically reduces not only the costs of presenting the required information before a possibly inexpert adjudicator, but also the possibility of error resulting from a misapprehension of evidence.[12] Likewise, in the case of, for example, an extensive construction project, the parties—prior to the dispute occurring—may have little idea of the subject matter of any particular dispute which may occur in the future. Again, from a cost reduction perspective, it makes significant

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[11] For similar discussions of the merits of arbitration, *see, e.g.,* GARY B. BORN, INTERNATIONAL ARBITRATION: CASES AND MATERIALS 19–25 (2011) (hereafter, "BORN, CASES AND MATERIALS"); GARY B. BORN, INTERNATIONAL ARBITRATION: LAW AND PRACTICE 3–6, 9–17 (2012) (hereafter, "BORN, LAW AND PRACTICE"); Edna Sussman, *The Arbitration Fairness Act: Unintended Consequences Threaten U. S. Businesses*, 18 AM. REV. INT'L ARB. 455, 461–62 (2009).

[12] These error costs could be significant where the *lex arbitri* precludes setting aside (or appeal) of an arbitral award on the grounds of misapprehension of fact. *See, e.g.,* Arbitration Act, 1996, §§ 67–73 (U.K.); *Id.* § 69 (error on a point of law *may* be a ground. However, it should be noted that the institutional arbitration rules require parties to specifically waive their § 69 rights. *See* LCIA Arbitration Rules, Art. 26.9 (1998); Int'l Comm. Arb., Rules of Arbitration, Art. 28 (2012).

sense to be able to appoint the adjudicator once the nature of the dispute is known. Presenting the relevant material to an adjudicator with an engineering background may be appropriate if a quality issue is the subject of dispute, but an adjudicator with a different background may be more appropriate to resolve other sorts of issues. A lawyer or an industry expert may be a more appropriate choice where other controversies (for example, interpretation of "within a reasonable time") are involved.

Arbitration through an arbitration institution, for instance the International Chamber of Commerce or the London Court of International Arbitration has the further advantage of credence, as these institutions have developed an international reputation for knowledgeable competent arbitrators. They operate under an attractive *lex arbitri.* Their reputation insures not only that the appropriate judicial oversight of the process will be used in the unlikely event that things go wrong during the arbitration, but also the ability for international enforceability of the award.

Arbitration pursued through trading or industry associations may share the best features of institutional and ad hoc arbitration: the membership of both parties in the organization is recognition of that institution's credibility. The specialized nature of the organization and its choice of members of arbitration panels ensure that these arbitrators have the desired technical and industry background to accurately and efficiently resolve the disputes.[13] Further, given the commercial context of bulk commodities trading, a trading house may be both a purchaser and seller of commodities under the same standard form contract. These parties therefore arbitrate disputes under the contract in both capacities; hence there is simply no incentive for the terms of the arbitration agreement or the institutional rules to favor one side over the other. In contrast, there is every incentive to ensure equality between the parties' contractual rights and obligations in such circumstances.

Note that central to this paradigm is the idea that the agreement to arbitrate is voluntary concluded with awareness on the part of the parties of the benefits gained through arbitration and what rights

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[13] *See, e.g.,* the arbitration and contract-issuing practices of The Federation of Oils, Seeds and Fats Associations (FOSFA), the London-based body which develops standard form contracts (and arbitrates disputes which arise under them) for the sale of oilseeds, oils and fats. *See,* FOSFA INTERNATIONAL, http://www.fosfa.org. Approximately 85% of the world trade in these commodities is conducted under these contracts. *Id.*

and remedies may be waived in the arbitration process.[14] The voluntary acceptance of the arbitration agreement by parties with equal bargaining power is significant evidence that, in agreeing to arbitration as part of the bargain, any consequences of arbitration (for instance, prohibitions on the pursuit of remedies of a certain type, waivers of certain rights, limitations as to the set of potential arbitrators) are otherwise compensated for by other aspects of the bargain construed in its entirety.

II. THE FAA AND THE EXPANSION OF CONSUMER ARBITRATION

Although the original purpose of the FAA was to establish a statutory basis to overcome judicial hostility towards commercial arbitration,[15] the Supreme Court has subsequently interpreted the Act to widen its scope and regard it as a cornerstone of a "liberal federal policy favoring arbitration."[16] This widened scope has facilitated, if not encouraged, the spread of arbitration from a method of resolving disputes among commercial entities to a means of resolving business-consumer disputes.[17] Consumer contracts requiring arbitration now concern cellular phones,[18] nursing homes,[19] retailers' contracts with charge card providers,[20] dealings with pay-day loan providers,[21] and

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[14] For instance, in a Bermuda form contract, punitive damages are excluded from the available remedies. These contracts are reinsurance contracts, governed by New York law with punitive damages excluded, arbitrated (typically in London) under the Arbitration Act, 1996 (U.K.). *See, e.g.,* C. v. D., [2007] EWHC 1541 (Comm); [2007] 2 All E.R. (Comm.) 557, [2007] 2 Lloyd's Rep. 367, [2007] 1 C.L.C. 1038. The LCIA and ICC arbitration rules limit discovery. *See* BORN, LAW AND PRACTICE, *supra* note 11 at 178–189. They further require the parties to waive the right to set aside an award on the ground of arbitrator's error on a point of law. *See supra* note 12.

[15] *See* A.T. & T. Mobility LLC v. Concepcion, 131 S. Ct. 1740, 1745 (2011); BORN, CASES AND MATERIALS, *supra* note 11, at 19–25.

[16] Moses H. Cone Memorial Hospital v. Mercury Construction Corporation, 460 U.S. 1, 24, 103 S. Ct. 927, 941 (1983).

[17] *See* Jean R Sternlight, *Creeping Mandatory Arbitration: Is it Just?,* 57 STAN. L. REV. 1631, 1635–1642 (2004).

[18] *E.g., Concepcion*.

[19] *E.g.,* Marmet Health Care Center Inc. v. Clayton Brown, 132 S. Ct. 1201 (2012) *vacated sub nom.* Brown v. Genesis Healthcare Corp., 724 S.E.2d 250 (W. Va. 2011) *remanded to sub nom.* Brown v. Gensis Healthcare Corp., 729 S.E.2d 217 (W. Va 2012).

[20] *E.g.,* American Express Co. v. Italian Colors Restaurant, 133 S. Ct. 2304 (2013).

even fast-food restaurant contests.[22] One study, published in 2002 showed that approximately 33% of "important" consumer transactions were governed by contracts which mandated arbitration.[23] Arbitration agreements have also crept into employment matters.[24] Given this recent explosion of judicial support for the expanded use of arbitration, the prevalence of contractually mandated arbitration is bound to increase. Mandatory arbitration will likely continue to rapidly extend to other areas involving crucial aspects of peoples' lives.

The result of expanded arbitration is that these arbitration clauses have required consumers and employees to: forego claims of punitive damages,[25] forego the ability to take part in class actions[26] (even when participating in class actions would be the only economically feasible means of pursuing the action),[27] forego discovery,[28] have the choice of the arbiter imposed on the consumer or employee,[29] and to arbitrate the matter in a location far removed from the consumer's place of residence.[30]

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[21] *E.g.,* Buckeye Check Cashing Inc. v. Cardegna, 546 U.S. 440 (2006).

[22] *E.g.,* Popovich v McDonald's Corp., 189 F. Supp. 2d 722 (N.D. Ill. 2002).

[23] Linda J. Demaine & Deborah R. Hensler, "*Volunteering" to Arbitrate Through Predispute Arbitration Clauses: The Average Consumer's Experience,* 67 LAW & CONTEMP. PROBS. 55, 58 (2005) ("Important purchases" were defined as "as purchases that are expensive, ongoing, or have a potentially large impact on [the consumer's] life").

[24] *See, e.g.,* Rent-A-Center, West, Inc. v. Jackson, 561 U.S. 63 (2010); Hooters of America, Inc. v. Phillips, 173 F. 3d 933 (4th Cir. 1999). Note though that in the latter case the employee prevailed. This was due to the one-sided nature of the employer's arbitration procedure and not because this dispute was not amenable to arbitration.

[25] *See, e.g.,* Marmet Health Care Center Inc. v. Clayton Brown, 132 S. Ct. 1201 (2012); Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52 (1995); Stipanowich, *supra* note 5.

[26] *See, e.g.,* A.T. & T. Mobility LLC v. Concepcion, 131 S. Ct. 1740 (2011); American Express Co. v. Italian Colors Restaurant, 133 S. Ct. 2304 (2013).

[27] *E.g., Italian Colors*.

[28] *See, e.g. Hooters of America, Inc.*, 173 F. 3d at 938; Hooters of America Inc. v. Phillips, 39 F. Supp. 2d 582, 614, 618 (D. S.C. 1998) (regarding the asymmetries in discovery).

[29] *See, e.g., Hooters of America, Inc.*, 173 F. 3d at 938.

[30] *See, e.g.,* Newton v. American Debt Svces. No. 12–15549, 2013 WL 6501391 (9th Cir. Dec. 12, 2013). This was an almost foregone conclusion resulting from Carnival Cruise Lines v. Shute, 499 U.S. 585 (1991) and Scherk v. Alberto Culver Co., 417 U.S. 506 (1971). *See* Jean R. Sternlight, *Panacea or Corporate Tool?: Debunking the Supreme Court's Preference for Binding Arbitration*, WASH. U. L. Q. 637, 688 (1996). *See also,* Nagrampa v. Mailcorps, Inc., 496 F. 3d 1257 (9th Cir. 2006).

According to recent US Supreme Court case law, the justification for this is that arbitration is a contractual matter,[31] and as such, arbitration agreements are to be enforced according to their terms. In a 2011 pronouncement, *A.T.&T. Mobility LLC v. Concepcion*, the majority of the US Supreme Court reasoned:

> The "principal purpose" of the FAA is to "ensur[e] that private arbitration agreements are enforced according to their terms." . . . . This purpose is readily apparent from the FAA's text. Section 2 makes arbitration agreements "valid, irrevocable, and enforceable" as written (subject, of course, to the saving clause); §3 requires courts to stay litigation of arbitral claims pending arbitration of those claims "in accordance with the terms of the agreement:" and §4 requires courts to compel arbitration "in accordance with the terms of the agreement" upon the motion of either party to the agreement (assuming that the "making of the arbitration agreement or the failure . . . to perform the same" is not at issue). In light of these provisions, we have held that parties may agree to limit the issues subject to arbitration, . . . to arbitrate according to specific rules, . . . and to limit *with whom* a party will arbitrate its disputes, ...[32]

The majority opined that this expanded role of arbitration is justified on the grounds of party autonomy and efficiency:

> The point of affording parties discretion in designing arbitration processes is to allow for efficient, streamlined procedures tailored to the type of dispute. It can be specified, for example, that the decision maker be a specialist in the relevant field, or that proceedings be kept confidential to protect trade secrets. And the informality of arbitral proceedings is itself desirable, reducing the cost and increasing the speed of dispute resolution. . . .[33]

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[31] Rent-A-Center, West, Inc. v. Jackson, 561 U.S. 63, 130 S. Ct. 2772, 2776 (2010) ("The FAA reflects the fundamental principle that arbitration is a matter of contract. . . . The FAA thereby places arbitration agreements on an equal footing with other contracts . . . and requires courts to enforce them according to their terms." citing Buckeye Check Cashing Inc. v. Cardegna, 546 U.S. 440, 443 (2006); Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ., 489 U.S. 468, 478, (1989)).

[32] A.T. & T. Mobility LLC v. Concepcion, 131 S. Ct. 1740, 1748–49 (2011).

[33] *Id.* at 1749.

Consequently, the majority interpreted that the FAA mandates a wide scope for parties to resolve any disputes through arbitration.

To the extent that state law precludes the arbitration of certain types of claims, state law is displaced by the FAA.[34] Although §2 of the FAA provides that arbitration agreements are unenforceable on the same legal or equitable grounds as any other contract,[35] courts interpret the savings clause to mean that any ground for "revoking" an arbitration clause must apply to *all* contracts generally, and not merely to agreements to arbitrate.[36] In other words, neither state legislatures nor state courts can carve out arbitration-specific exceptions to the FAA's pro-arbitration policy.

Consequently, courts uphold arbitration agreements which eliminate consumer's recourse to class action.[37] In February 2012, holding a state statute which purportedly invalidated pre-dispute agreements to arbitrate—here an agreement to arbitrate wrongful death cases against nursing home—was contrary to the FAA, referring to its past rulings, the US Supreme Court remarked:

> West Virginia's prohibition against predispute agreements to arbitrate personal-injury or wrongful-death claims against nursing homes is a categorical rule prohibiting arbitration of a particular type of claim, and that rule is contrary to the terms and coverage of the FAA. . . . . See also, *e.g., Preston* v. *Ferrer*, 552 U. S. 346, 356 (2008) (FAA preempts state law granting state commissioner exclusive jurisdiction to decide issue the parties agreed to arbitrate); *Mastrobuono* v. *Shearson Lehman Hutton, Inc.*, 514 U. S. 52, 56 (1995) (FAA preempts state law requiring judicial resolution of claims involving punitive damages); *Perry* v.

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[34] *Id.* at 1747. *See also* Doctor's Associates v. Casarotto, 517 U.S. 681 (1995).

[35] *See* Federal Arbitration Act, 9 U.S.C. § 2, which provides:
A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

[36] *Concepcion,* 131 S. Ct. at 1747 provides:
We said that a court may not "rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable, for this would enable the court to effect what . . . the state legislature cannot.
(citations omitted).

[37] *Id.*

Thomas, 482 U. S. 483, 491 (1987) (FAA pre-empts state-law requirement that litigants be provided a judicial forum for wage disputes); *Southland Corp.* v. *Keating*, 465 U. S. 1, 10 (1984) (FAA pre-empts state financial investment statute's prohibition of arbitration of claims brought under that statute).[38]

Accordingly, the Court remanded the matter back to the State Supreme Court to determine if the arbitration clauses in question were "unenforceable under state common law principles that are not specific to arbitration and pre-empted by the FAA."[39] Next, in June 2013, the Supreme Court upheld the enforceability of arbitration clauses which precluded class arbitration even when the costs of the required individual arbitration would exceed the possible recovery.[40]

As a result of this bias towards enforceability of arbitration agreements, American consumer contracts frequently contain clauses which limit consumers' substantive remedies and procedural safeguards.[41] Typically limits on remedies and procedure imposed by arbitration clauses include: (1) the exclusion of class relief;[42] (2) a limit to exposure to certain types of damages (*e.g.*, punitive damages);[43] (3) limit discovery;[44] and (4) limit the sorts of disputes which can be arbitrated, hence reserving—or "carving out"—for the company the right to litigate other matters.[45] These latter cases are often found in credit agreements, requiring arbitration of all matters other than those relating to debt collection. The resulting popularity with larger entities thus rests in the entity's ability to use arbitration clauses to limit or exclude the larger entity's exposure to certain types of damages and/or class action claims.[46] In addition, by making arbitration uneconomical or inconvenient, the party requiring arbitration can effec-

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[38] Marmet Health Care Center Inc. v. Clayton Brown, 132 S. Ct. 1201, 1203–4 (2012).

[39] *Id.* at 1205.

[40] American Express Co. v. Italian Colors Restaurant, 133 S. Ct. 2304 (2013).

[41] *See* Demaine & Hensler, *supra* note 23 and accompanying text.

[42] *Italian Colors* and *Concepcion*.

[43] *Marmet Health Care Center*. *See also, infra* text accompanying note 71.

[44] Hooters of America, Inc. v. Phillips, 173 F. 3d 933 (4th Cir. 1999).

[45] *See, e.g.,* Lackey v. Green Tree Financial Corp., 498 S.E.2d 898 (S.C. Ct. App. 1998); Green Tree Financial Corp. v. Randolph, 531 U.S. 79 (2000).

[46] *See,* Jean A. Sternlight & Elizabeth J. Jensen, *Using Arbitration to Eliminate Consumer Class Actions: Efficient Business Practice or Unconscionable Abuse?,* 67 LAW & CONTEMP. PROBS. 75, 75 n.2 (2004) (who canvass some of practitioner literature which advise companies to use arbitration clauses to this end).

tively insulate itself from exposure to damages it might otherwise be compelled to pay.

These limitations, foisted through arbitration clauses, are almost exclusively imposed on the economically weaker party. As such they are typically viewed as solely beneficial to the stronger party, which imposed the limitations, and by being written into "take it or leave it" contracts of adhesion, the "fairness" or "justice" in use and enforcement of arbitration agreements in this way is a concern. It is particularly concerning given the effects of the arbitration clause. The concern is not only an academic concern,[47] but has also been a subject of comment in the popular press.[48] It also appears to be part of the motivation behind Congressional attempts to reverse the favorable approach to the use of arbitration to preempt state consumer legislation.

The most recent Congressional attempt at reform, the Arbitration Fairness Act of 2013,[49] identifies the problem in the parties' disparate economic strength. Section 2 of that Act would read:

The Congress finds the following:

> . . .
>
> (3) Most consumers and employees have little or no meaningful choice whether to submit their claims to arbitration. Often, consumers and employees are not even aware that they have given up their rights.
>
> (4) Mandatory arbitration undermines the development of public law because there is inadequate transparency and inadequate judicial review of arbitrators' decisions.
>
> (5) Arbitration can be an acceptable alternative when consent to the arbitration is truly voluntary, and occurs after the dispute arises.

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47 *See, e.g.,* Franken, *supra* note 5.

48 *See, e.g.*, Erwin Chemerinsky, Op-Ed., *Justice for Big Business*, N.Y. TIMES, July 1, 2013, http://www.nytimes.com/2013/07/02/opinion/justice-for-big-business.html?_r=1&; Alison Frankel, *What hope remains for consumers, employees after SCOTUS Amex ruling?*, REUTERS, June 20, 2013, http://blogs.reuters.com/alison-frankel/2013/06/20/what-hope-remains-for-consumers-employees-after-scotus-amex-ruling-2/.

49 S. 878, 103th Cong. (2013); H.R. 1844, 113th Cong. (2013). This Act is identical to the Arbitration Fairness Act 2011, S. 987 112th Congress; H.R. 1873, 112th Cong. (2011).

The 2007[50] and 2009[51] Acts are somewhat more emphatic, noting that abuses arising from the asymmetries of bargaining power and information are found in many situations where such agreements are used. These asymmetries act to the detriment of consumers and employees. Accordingly these Acts find:

> (3) Most consumers and employees have little or no meaningful option whether to submit their claims to arbitration. Few people realize, or understand the importance of the deliberately fine print that strips them of rights; and because entire industries are adopting these clauses, people increasingly have no choice but to accept them. They must often give up their rights as a condition of having a job, getting necessary medical care, buying a car, opening a bank account, getting a credit card, and the like. Often times, they are not even aware that they have given up their rights.
>
> (4) Private arbitration companies are sometimes under great pressure to devise systems that favor the corporate repeat players who decide whether those companies will receive their lucrative business.
>
> (5) Mandatory arbitration undermines the development of public law for civil rights and consumer rights, because there is no meaningful judicial review of arbitrators' decisions. With the knowledge that their rulings will not be seriously examined by a court applying current law, arbitrators enjoy near complete freedom to ignore the law and even their own rules.
>
> (6) Mandatory arbitration is a poor system for protecting civil rights and consumer rights because it is not transparent. . . .
>
> (7) Many corporations add to their arbitration clauses unfair provisions that deliberately tilt the systems against individuals, including provisions that strip individuals of substantive statutory rights, ban class actions, and force people to arbitrate their claims hundreds of miles from their homes. While some courts have been protective of individuals, too

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[50] S. 1782, 100th Cong. (2007); H.R. 3010, 110th Cong. (2007).

[51] Arbitration Fairness Act of 2009, S. 931, 111th Cong. (2009); H.R. 1020, 111th Cong. (2009).

> many courts have upheld even egregiously unfair mandatory arbitration clauses in deference to a supposed Federal policy favoring arbitration over the constitutional rights of individuals.[52]

The concerns expressed in the Arbitration Fairness Acts are not unique to members of Congress.

EU law takes a similar view to contracts of adhesion. Article 3 of Council Directive 93/13/EEC deems contractual provisions which are significantly detrimental to the consumer and imposed in such circumstances to be unfair. It provides:

> 1. A contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer.
>
> 2. A term shall always be regarded as not individually negotiated where it has been drafted in advance and the consumer has therefore not been able to influence the substance of the term, particularly in the context of a pre-formulated standard contract.
>
> The fact that certain aspects of a term or one specific term have been individually negotiated shall not exclude the application of this Article to the rest of a contract if an overall assessment of the contract indicates that it is nevertheless a pre-formulated standard contract.[53]

Pursuant to Article 6 of that Directive, such unfair terms are void and severable from the remainder of the contract[54] and Member States are permitted to adopt the "most stringent provisions compatible with the Treaty in the area covered by this Directive, to ensure a

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[52] Arbitration Fairness Act 2009, S. 931, 111th Cong. § 2 (2009). This is taken verbatim from the Arbitration Fairness Act 2007, S. 1782, 110th Cong. § 2.

[53] Council Directive 93/13/EEC, *supra* note 7. This has been transposed into U.K. law by the Unfair Terms in Consumer Contracts Regulations, 1999, S.I. 1999 No. 2083, § 5(1) (U.K.).

[54] *See* Council Directive 93/13/EEC, *supra* note 7., Art. 6(1) provides:
Member States shall lay down that unfair terms used in a contract concluded with a consumer by a seller or supplier shall, as provided for under their national law, not be binding on the consumer and that the contract shall continue to bind the parties upon those terms if it is capable of continuing in existence without the unfair terms.

maximum degree of protection for the consumer."[55] Pre-dispute consumer agreements are voidable under the laws of the United Kingdom,[56] and, in addition, these laws provide:

> 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 not covered by legal provisions, unduly restricting the evidence available to him or imposing on him a burden of proof which, according to the applicable law, should lie with another party to the contract[57]

are deemed to be unfair, and hence voidable, provisions in a consumer contract.

In light of these Congressional assertions regarding unfairness of such terms imposed through arbitration, and the fact that other jurisdictions appear to agree with this sentiment, an assessment of the "fairness of" or "justice in using" such clauses is merited. This assessment must be conducted from two angles. First, from the perspective of those advocating the use of these exclusions, to identify their purported advantages. Second, from a normative perspective informed by a well-developed theory of fairness. This is the purpose of the final Parts of this Article.

III. The Purported Advantages of Arbitration Exclusions

There are strong arguments which suggest that these types of exclusions can have a consumer welfare enhancing effect by reducing the costs consumers pay for their goods or services. In his 2001 article, Ware,[58] selected what he considers to be four instances where the exclusion of consumers' substantive and procedural rights through arbitration agreements has the effect of reducing the prices that consumers pay for goods or services, thus enhancing consumer welfare. The exclusions which Ware identifies are: (1) disallowance of class

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[55] *Id.*, Art. 8.

[56] Consumer Arbitration Agreements Act, 1988, c. 21, § 1 (Eng., Wales, and N. Ir.), §§ 6–9 (Scot.). *See also,* the Unfair Terms in Consumer Contracts Regulations, 1999, S.I. 1999 No. 2083, § 5(5) (U.K.).

[57] The Unfair Terms in Consumer Contracts Regulations, 1999, S.I. 1999 No. 2083, sch 2, §1(q) (U.K.).

[58] *See, e.g.*, Stephen J. Ware, *Paying the Price of Progress: Judicial Regulation of Consumer Arbitration Agreements,* 2001 J. DISP. RESOL. 89 (2001).

actions; (2) disallowance of "subsidized" arbitration fees (*i.e.,* consumers pay their share of the costs of arbitration); (3) limitation on discovery; and (4) permitting "carve-outs" (*i.e.*, the practice that the consumer is required to arbitrate all matters in dispute, but the business can "carve-out" matters from arbitration and litigate these).[59] Typically "carve-outs" reserve the right to litigate collections issues in finance contracts.[60] An often encountered carve-out is the limit (either explicitly or as a consequence of the choice of a "professional" arbitrator) of certain forms of damages, particularly punitive damages.[61] The justification for, and analysis of, this exclusion reduces to those surrounding exclusions for class actions. These arguments merit further analysis.

The analysis contains three stages. First, the arguments themselves must be examined to measure their force. Second, the assumptions on which the arguments rest require investigation, which will permit the display of any limits that these arguments have. Finally, even if these arguments are forceful and based on realistic assumptions which permit them to be taken to have more general effect, a further line of inquiry must still be pursued. These arguments are ultimately premised on the idea that cost savings are the paramount, if not sole, goal to be pursued by this approach to consumer arbitration. In this Part, I will examine whether this is or is not the case. The remainder of this Part addresses the first of these two points.

A. Elimination of Class Actions and Punitive Damages

By eliminating consumers' access to class actions, companies can effectively insulate themselves from a significant amount of damages. The transaction and opportunity costs involved in prosecuting low value claims significantly outweigh the value of such claims. This is enhanced in the American "user-pays" cost system where no costs are awarded irrespective of the party's success. In addition, an opportunity cost involved in litigation may, and often does, exceed the expected value of the result. Thus pursuit of the litigation becomes an irrational pastime, and thus not pursued by any economically rational individual.

Justice Breyer's dissent in *Concepcion* points out this consequence:

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[59] *Id.* at 93–99.
[60] *Id*. at 97–98.
[61] *See infra* discussion and text accompanying notes 69–71.

> Regardless, the majority highlights the disadvantages of class arbitrations, as it sees them. See ante, . . . (referring to the "greatly increase[d] risks to defendants"; the "chance of a devastating loss" pressuring defendants "into settling questionable claims"). But class proceedings have countervailing advantages. In general agreements that forbid the consolidation of claims can lead small dollar claimants to abandon their claims rather than to litigate. I suspect that it is true even here, for as the Court of Appeals recognized, AT&T can avoid the $7,500 payout (the payout that supposedly makes *Concepcions'* arbitration worthwhile) simply by paying the claim's face value, such that "the maximum gain to a customer for the hassle of arbitrating a $30.22 dispute is still just $30.22." *Laster v. AT&T Mobility LLC*, 584 F. 3d 849, 855, 856 (CA9 2009).
>
> What rational lawyer would have signed on to represent the Concepcions in litigation for the possibility of fees stemming from a $30.22 claim? See, e.g., *Carnegie v. Household Int'l, Inc*., 376 F. 3d 656, 661 (CA7 2004) ("The realistic alternative to a class action is not 17 million individual suits, but zero individual suits, as only a lunatic or a fanatic sues for $30").[62]

This strategy can be extended by increasing the costs of pursuing a remedy. Imposing an arbitration process which requires consumers to incur costs, whether in the form of filing or other fees for services[63] or cost shifting (*i.e.*, "loser pays") will deter a significant number of claims. By reducing their exposure, the argument runs, companies reduce their costs in numerous ways. These involve such savings as lower insurance and legal costs, financial resources can be invested rather than being held in reserve to possibly defend and satisfy claims, and the like. These cost savings will via markets forces be passed onto consumers. Or, so it is argued.

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[62] A.T. & T. Mobility LLC v. Concepcion, 131 S. Ct. 1740, 1760–61 (2011) (Breyer, J., dissenting).

[63] Subpoenas and hearings to compel discovery are examples of such services which add costs. *See,* Brown v. Genesis Healthcare Corp., 724 S.E.2d 250, 294 (W. Va. 2011). *See also,* Morten Hviid & Greg Shaffer, *Hassle Costs: The Achilles' Heel of Price-Matching Guarantees*, 8 J. ECON. & MAN. STRAT. 489 (1999) (who explore the notion of "hassle costs," and their effect on deterring otherwise beneficial behavior).

This argument is frequently buttressed with the claim that class actions benefit class counsel rather than members of the class, thus resulting in little consumer benefit. Ware supports this position, arguing that businesses can incur liability as a result of class actions. Yet consumers do not see the benefits of such actions, rather class counsel appropriates these benefits in the form of enhanced fees.[64]

Three points must be made regarding this latter claim. Since 2005, the Class Action Fairness Act (CAFA)[65] has remedied some of the perceived excesses of the previous class action system, particularly in regard to control of counsels' conduct of the matter and their remuneration. Specifically, the CAFA attempts to control the excesses of coupon settlements.[66] Likewise the CAFA enhances judicial review of settlements to ensure that class members' interests are taken into account during the settlement process.

Second, to a great extent, the issues surrounding class counsels' conduct in litigation (and their subsequent remuneration) involves an agency problem. By definition, class members have a small stake in the outcome of the litigation, giving rise to limited incentive to monitor class counsel. Class counsel's incentive is to obtain an acceptable settlement with the least effort, and then move on to more lucrative endeavors. However, such agency issues are pervasive in the attorney-client relationship. Counsel paid by the hour has an incentive to expend a significant amount of time on matters which may be of peripheral relevance to the particular client's concern. Likewise, in a flat-fee arrangement, the incentive for a lawyer is to produce a minimally acceptable result in as little time as possible. Given the pervasive nature of these sorts of issues in the attorney-client relationship, it is somewhat disingenuous to single out class actions as a matter of specific concern.[67]

Third, and certainly not of least significance, is the point

[64] Ware, *supra* note 58, at 93. *See also e.g.,* John C. Coffee, Jr., *Class Wars: The Dilemma of the Mass Tort Class Action*, 95 COLUM. L. REV. 1343 (1995).

[65] Class Action Fairness Act of 2005, 28 U.S.C. §§ 1332(d), 1453, 1711–1715.

[66] Coupon settlements are those which all or part of the "payment" to class members takes the form of the "coupons" for future discounts. The value of the settlement (and hence counsel's remuneration) is based on the total value of the coupons issued, not the value of coupons redeemed. Such settlements are now controlled by § 1712 of the CAFA. *See* 28. U.S.C. § 1712.

[67] Some of these arguments are canvassed in greater detail in Bruce Wardhaugh, *Bogeymen, Lunatics and Fanatics: Collective Actions and the Private Enforcement of European Competition Law,* 34 LEGAL STUD. 1 (2014) [hereafter Wardhaugh, *Bogeymen*].

made by the dissents in both *Concepcion* and *Italian Colors*,[68] that by imposing such arbitration clauses, the entity in the stronger economic position will "make pursuit of the . . . claim a fool's errand,"[69] by ensuring that the pursuit of any claim is uneconomical. The result of this is for the stronger party to "depriv[e] its victims of all legal recourse."[70] While depriving a harmed individual of any remedy may reduce the costs of the party which inflicted the harm, as we examine below such cost-savings may not necessarily be passed on, nor may this imposition of risk be viewed as "fair" or "just" when exposed to a normative analysis which considers more than just cost-savings.

The argument that the use of arbitration agreements to limit the types of damages available to consumers results in costs savings which are in turn passed onto consumers reduces to the argument above. The arbitration agreements need not specifically exclude such claims to have this effect. Rather, the fact that the dispute is placed into the hands of a professional arbitrator takes it away from a potential "runaway jury." Not only was this the reason why arbitration was incorporated into the contract by the nursing homes in *Brown* but also that the State Supreme Court saw through this motivation in their judgment. They reasoned:

> Still, we have recognized that the constitutionally-enshrined and fundamental rights to assert one's claims for justice before a jury in the public court system may be the subject of a legally enforceable waiver. However, ''Courts indulge every reasonable presumption against waiver of a fundamental constitutional right and will not presume acquiescence in the loss of such fundamental right.''
>
> In essence, our [state] Constitution recognizes that factual disputes should be decided by juries of lay citizens rather than paid, professional fact-finders (arbitrators) who may be more interested in their fees than the disputes at hand.[71]

This suggests that an arbitrator's award is less likely to compensate for non-economic losses than a jury's verdict. If this assumption is correct, such elimination of remedies thereby deprives a

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[68] American Express Co. v. Italian Colors Restaurant, 133 S. Ct. 2304, 2313–2317 (2013) (Kagan J., dissenting). *See* A.T. & T. Mobility LLC v. Concepcion, 131 S. Ct. 1740, 1759–60 (2011) (Breyer, J., dissenting).

[69] *Italian Colors*, 133 S. Ct. at 2313.

[70] *Id.*

[71] Brown v. Genesis Healthcare Corp., 724 S.E.2d 250, 271 (W. Va. 2011).

claimant of her rights to recover for non-economic damages. However, if this analysis of the assumption that a professional arbitrator is less likely to award certain categories of damages is correct, then the merits of the use of arbitrators to achieve these purposes reduce to the earlier discussed case of the use of arbitration to eliminate class actions.

B. Elimination of Discovery

Limitations on discovery clearly reduce costs to the companies involved. However, in spite of this potential benefit, courts have been somewhat reluctant to uncritically enforce arbitration agreements which unduly restrict consumers' discovery. Due to the asymmetry in availability of information, restrictions on discovery can make it difficult and sometimes impossible for a consumer to pursue a valid claim.[72] In *Kinney v United Health Care Services*,[73] (cited by Ware)[74] the California Court of Appeals remarked:

> The unconscionable nature of the unilateral arbitral obligation is heightened by certain other terms of United's arbitration policy. Given that United is presumably in possession of the vast majority of evidence that would be relevant to employment-related claims against it, the limitations on discovery, although equally applicable to both parties, work to curtail the employee's ability to substantiate any claim against United. Further, to the extent the arbitration clause forecloses any finding that the employment relationship was other than at will, an employee is precluded from demonstrating that United could only terminate for good cause so as to support a recovery of contract damages that might otherwise be available. Similarly, the arbitration policy caps the employee's recovery of compensatory and punitive damages for employment discrimination.[75]

Such reluctance is increased where limitations on discovery

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[72] *See* the references in Ware, *supra* note 58, at 97 n.49–51; Paul Haagen, *New Wineskins for New Wine: The Need to Encourage Fairness in Mandatory Arbitration,* 40 ARIZ. L. REV. 1039, 1051 (1998); Jean R. Sternlight, *Rethinking the Constitutionality of the Supreme Court's Preference for Binding Arbitration: A Fresh Assessment of Jury Trial, Separation of Powers, and Due Process Clauses,* 72 TUL. L. REV. 1, 89–90 (1997).

[73] Kinney v. United Healthcare Services, 70 Cal. App. 4th 1322 (1999).

[74] Ware, *supra* note 58, at 97.

[75] *Kinney*, 70 Cal. App. 4th at 1332.

form one aspect of a number of procedural barriers which may act to prevent a consumer from vindicating her claim.[76] *Kinney* is not an outlier example of this.[77]

Prior to 2012, courts were likely to find arbitration agreements which, through asymmetric discovery provisions, did not provide one party[78] sufficient opportunity for discovery as unconscionable and thus unenforceable. However, post- *Concepcion*, courts have begun favoring enforcement of arbitration agreements notwithstanding discovery concerns. A recent judgment of the District Court for the Northern District of California, *Lucas v. Hertz Corp.*, noted:

> Prior to the Supreme Court's ruling in *Concepcion*, numerous courts, at both the state and federal level, found arbitration agreements substantively unconscionable where the rules of the arbitral forum allowed for only minimal discovery or where the affect of the discovery rules operated solely to one side's benefit.
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> . . .
>
> *Concepcion*, however, suggests that limitations on arbitral discovery no longer support a finding of substantive unconscionability.
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> . . .
>
> Although there is a difference between a failure to provide for ''judicially monitored discovery'' and a failure to affirmatively allow for any discovery devices to be used, the court believes the above reasoning applies with equal force here. And although they do not cite *Concepcion*, many post-*Concepcion* federal district court decisions taking up this issue suggest the same.[79]

The justification for limiting discovery is to cap the costs of

[76] *See supra* note 63 and text accompanying.

[77] *Hooters v. Phillips* is another well-known matter. *See, e.g.,* Hooters of America Inc. v. Phillips, 39 F. Supp. 2d 582, 614, 618 (D. S.C. 1998); Hooters of America, Inc. v. Phillips, 173 F. 3d 933, 938 (4th Cir. 1999) (for the one-sided nature of discovery and disclosure of witnesses which the employer attempted to impose in that case).

[78] Who is almost inevitably the consumer or the employee.

[79] Lucas v. Hertz Corp., 875 F. Supp. 2d 991, 1007–08 (N.D. Cal. 2012) (citations omitted).

arbitration. Every requirement imposed upon a party to obtain and provide information during arbitration increases the party's costs. While limiting discovery is a frequent and uncontroversial practice in larger commercial arbitrations,[80] its primary uses in that context are to *expedite* the dispute resolution process and ensure a greater protection of confidentiality than would be found in the litigation process, while simultaneously potentially reducing the processes' costs. This latter point is magnified under a US-style costs regime in which legal fees and related expenses are non-recoverable irrespective of the outcome of the litigation.

However, in these larger, non-consumer arbitrations, the asymmetries of information or resources found in consumer arbitrations are unlikely to be present. In these sorts of disputes both parties are likely to have sufficient awareness of the commercial context of the contract, copies of records relating to the transaction in question, and sufficient resources to make any other sorts of investigations which may be necessary. This symmetry rarely exists in simple consumer arbitration. This difference in resources and information possessed by the parties in these two sorts of matters illustrates the difficulty with restrictions on discovery. The problem is to strike the appropriate balance between a restriction of discovery to enhance economies of time and costs, and a restriction of discovery which has the effect of eliminating one party from effectively vindicating their rights. While the economies in theory[81] will be passed on to consumers, restrictions on the use of discovery to deny access to needed information *frustrates* the dispute resolution process to the detriment of the consumer.

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[80] *See, e.g.,* American Arbitration Association, International Dispute Resolution Procedures, Art. 19; International Chamber of Commerce, Rules of Arbitration, Art. 20; LCIA, Arbitration Rules, Art. 20, 22; UNCITRAL, Arbitration Rules, Art. 24. For a discussion of discovery in international commercial arbitration, *see* BORN, CASES AND MATERIALS, *supra* note 11, at 778–791 (and the cases cited therein); BORN, LAW AND PRACTICE, *supra* note 11, at 182–193; Giacomo Rojas Elgueta, *Understanding Discovery in International Commercial Arbitration Through Behavioral Law and Economics: A Journey Inside the Minds of Parties and Arbitrators*, 16 HARV. NEGOT. L. REV. 165 (2011).

[81] Writing pre-*Concepcion*, Ware, *supra* note 58, at 97, remarked:

It is not clear whether these precedents will be extended to consumer arbitration or whether they require as much discovery as litigation has. If they require litigation-like discovery, they would raise the cost of arbitration to businesses and therefore raise prices to consumers. Litigation-like discovery would both increase the amount of time and money the business must spend on the discovery process and make it easier for consumers to prove their claims." (Ware's footnotes omitted). The assumptions on which this position is based will be explored below.

C. The Use of "Carve-outs"

"Carve-outs" are situations where one party (inevitably the company) reserves the right to litigate some disputes, but the other party (typically, the consumer) is required to arbitrate all matters.[82] Such asymmetric contractual allocations of remedies are alleged to be unfair (hence unconscionable) precisely in virtue of this asymmetry. However, the asymmetry itself ought not to be viewed as the problem. Rather the source of the problem rests in the reasons why certain types of disputes have been carved out from the arbitration agreement.

Typically such "carve-outs" reserve the right for the company to litigate in order to realize upon a security or claim a debt. As recent American experience with "robo-signing" in mortgage foreclosures attests, debt collection is a highly automated process. Most collections actions are undefended, proceeding as default judgments. The same would likely happen if the collection process were to proceed through arbitration. The difficulty therefore is not with obtaining a judgment, but collecting it from a judgment proof defendant.[83] Obtaining an award—whether at arbitration or as a result of litigation—is the easy part: the difficulty is enforcing the award through a garnishment of a bank account or wages, or through foreclosure or seizure and sale.

Accordingly, the collections process requires a judgment, the additional step of obtaining some kind of garnisheeing order, and enforcement of the latter order. If this process were pursued through arbitration, an additional legal step is required. This is usually of the form of an application (to a court) to convert the arbitrator's award to a court order.

Were "carve-outs" for collections processes eliminated, companies would be required to incur the expense of this additional legal step. Additionally, the costs of this step may serve as an impediment to collecting smaller debts owed to the company, the losses from which would be passed on to consumers in the form of higher prices and interest rates in financing agreements.

D. Elimination of "Subsidized" Arbitration

There is an argument that consumer arbitration, where the

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[82] Lackey v. Green Tree Financial Corp., 498 S.E.2d 898 (S.C. Ct. App. 1998) is commonly taken as a classic example of such a use of carve-outs.

[83] Ware, *supra* note 58, at 98.

consumer pays less than half of the costs of the arbitration, is subsidized. The argument continues that this in turn elevates the price of the goods or services purchased by consumers. This argument is ultimately premised upon the principles that to the extent that a purchaser of a good or service does not pay the full price for any good or service, that purchaser is subsidized; and the principle that the subsidy will necessarily be recouped by the seller in the form of higher prices.[84] However, Pre-*Concepcion* and *Italian Colors* employment[85] and consumer contracts[86] cases point to the proposition that significant dispute resolution costs act as a disincentive and sometimes barrier to the consumer/employee from availing herself of the arbitration procedure. These costs can arise where the consumer or employee is required to pay a non-trivial amount to engage in the arbitration process.

In *Green Tree Financial Corp. v. Randolph*, the Supreme Court appeared sympathetic to the argument that large arbitration costs impose barriers to the vindication of rights through that process. The court noted, "It may well be that the existence of large arbitration costs could preclude a litigant such as Randolph from effectively vindicating her federal statutory rights in the arbitral forum."[87] In *Green Tree*, however, the concern was that the arbitration record was silent on the matter of cost barriers.[88] However, the post-*Italian Colors*

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[84] *See, e.g., id.* at 95:

It has long been customary in arbitration for the claimant to pay the filing fee charged by the arbitration organization and for the parties to pay equal shares of the arbitrator's fee. Recent employment arbitration cases, however, have refused to enforce agreements requiring the employee-claimant to pay fees according to this custom. These cases effectively require the business to subsidize the arbitration claim against it. (footnotes omitted)

[85] Shankle v. B-G Maintenance Mgmt. of Colorado, Inc., 163 F.3d 1230 (10th Cir. 1999); Paladino v. Avnet Computer Technologies, Inc., 134 F.3d 1054, 1062 (11th Cir. 1998); and Armendariz v. Foundation Health Psychcare Servs., Inc*.,* 99 Cal. Rptr. 2d 745 (Cal. 2000) are cited by Ware, *supra* note 58, at 95 n.38 as illustrative cases of this proposition.

[86] A classic case is Green Tree Financial Corp. v. Randolph, 531 U.S. 79 (2000). *See also* Lackey v. Green Tree Financial Corp., 498 S.E.2d 898 (S.C. Ct. App. 1998).

[87] *Green Tree Financial Corp.*, 531 U.S. at 90.

[88] *Id.* at 90–91:

But the record does not show that Randolph will bear such costs if she goes to arbitration. Indeed, it contains hardly any information on the matter. . . . The record reveals only the arbitration agreement's silence on the subject, and that fact alone is plainly insufficient to render it unenforceable. The ''risk'' that Randolph will be saddled with prohibitive costs is too speculative to justify the invalidation of an arlandscape is somewhat different.

This concern was expressed in the aftermath of *Italian Colors*.[89] *In Italian* Colors the claim could only be economically pursued as a class action or through the common action of prospective claimants in the production of and payment for a market study. The arbitration agreement's waiver of class action and requirement of confidentiality precluded either course of action. Nevertheless, the Court held that this was consistent with federal policy under the FAA, as the agreement did not eliminate the *right to pursue* a remedy[90] such a waiver merely made it more difficult for a prospective claimant to *prove the claim*.[91] While the Court appeared careful not to explicitly overturn its decision in *Green Tree*, the *Italian Colors* decision raises doubt as to how long *Green Tree* will in fact survive.[92]

IV. The Underlying Economic Assumptions

Restrictions in arbitration agreements are supported by economic arguments based on the assumptions that (1) entry and exit to markets are based on a rate of return equalization principle and (2) that in a competitive market savings will be passed on to consumers.[93] The return equalization principle holds that investment will flow to markets in such a way as to equalize the return on investment (relative to risk). Hence if there were a prospect of a super-normal return in a given sector, that prospect would attract further entry to the sector. This entry and the further competition entailed by such entry, would result in prices, and thus returns, in that sector of the market dropping to normal. Over time, the return on investment would no longer be super-normal.

The assumption that in a competitive market cost savings will be passed on to consumers, is a corollary of the first assumption. It holds that in the event these savings are not passed on to the consum-

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bitration agreement.

[89] *See* Franken, *supra* note 5, and text accompanying notes 47–48.

[90] American Express Co. v. Italian Colors Restaurant, 133 S. Ct. 2304, 2310 (2013).

[91] *Id.* at 2311.

[92] *Id.* at 2310–11:

> That would certainly cover a provision in an arbitration agreement forbidding the assertion of certain statutory rights. And it would *perhaps* cover filing and administrative fees attached to arbitration that are so high as to make access to the forum impracticable.

(emphasis in original).

[93] *See* Ware, *supra* note 58, at 91–92.

er, they represent a super-competitive return. This super-competitive return will ultimately, and depending on the speed of market entry, may rapidly be eliminated by the entry of others into the sector. Such entry—or even its threat—will be sufficient to drive down prices, thereby passing savings on to the consumer.

While these economic arguments provide a priori grounds for the belief that exclusion of such remedies via arbitration can lower the prices consumers pay, two significant normative and economic objections can be raised. The former objection questions the realism of the economic assumptions underlying the argument, particularly in light of the characteristics of the industries which have adopted such exclusions.

This objection has two prongs: the first prong is related to the structure of the market in which these waivers are found, to explore whether or not market entry and exit is as easy as assumed (and thus the extent to which the return equalization principle is applicable). The second prong is related to the commercial context in which those contracts containing the exclusions in question are found. The context in which these contractual waivers are found is in a market dominated by contracts of adhesion. The party in the weaker economic position simply cannot bargain its way into a less disadvantageous contractual position. In effect since there is no means of that party "paying more" to have the exclusion removed from the contract, the weaker party has no alternative but to accept the contract as proffered. This has significance not just for the economic assumptions on which the argument is premised, but also for our normative concern. In the remainder of this Part, we address these two points.

The normative objection can be succinctly expressed as a concern: is the value of low prices at the exclusion of almost all else (and particular, the exclusion of those remedies which concern us) to be taken as the sole goal which is to be pursued by these strategies? The evaluation of this concern raises normative questions of "justice" and "fairness," which our analysis, based upon Rawls' insights, will attempt to address. This is the focus of Part V.

A. Economic Assumptions: Are they Accurate?

An examination of the assumptions used in the arguments that such exclusions reduce prices for consumers exacerbate our grounds for concern. The assumptions rest upon the premise that if these exclusions lead to supernormal return, other firms will enter the market, increasing the supply of the goods or services, thereby causing a drop in prices. Even the threat of entry is sufficient to temper attempts at obtaining super-competitive returns. The locus classicus of such thinking can be found in the works of Baumol, Panzar and Willig.[94] Their view of a "contestable market" suggests that in markets with free entry and exit there will be a competitive constraint, in that this threat of entry tempers loss of consumer welfare, even in the case where the incumbent is a monopoly or an oligopolistic concentration.[95] Baumerol et al.'s writings on contestable markets have had a non-trivial effect on the development of antitrust policy in the US[96] and EU[97] since the mid-1980s.

Yet, the conditions required for a contestable market are quite strong. As one reviewer notes, a contestable market exhibits the following:

> . . . under certain structural conditions on technology and certain technical requirements on demands, frictionless entry and exit together with equal access to technology lead to a type of competitive equilibrium with desirable welfare consequences, even though there may be only one active firm in equilibrium. A market with the foregoing characteristics of frictionless reversible entry and equal access to technology is called a "perfectly contestable market" . . . . The market for air travel between two cities serves as a canonical example.[98]

The conditions for such a market are: (1) easy (*i.e.,* low/no cost) entry to the market, in particular, "The entrant can immediately duplicate and entirely replace any existing firm, even a complete monopolist."[99] Ease of entry into a market requires not just the capital to

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[94] WILLIAM J. BAUMOL, JOHN C. PANZAR & ROBERT D. WILLIG,, CONTESTABLE MARKETS: THE THEORY OF INDUSTRY STRUCTURE (1982); however, some chapters of this work appeared earlier in article form.

[95] *Id.* at 5–7.

[96] *See, e.g.,* HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE 33-36(4th ed. 2011).

[97] *See, e.g.,* Cases T-374/94, T-375/94, T-384/94 & T-388/94, Eur. Night Services Ltd. (ENS) et al. v. Comm'n, 1998 E.C.R. II-3141, ¶ 137 (stressing that the examination of conditions of competition is based on already present existing competition between undertakings and on potential competition); *Cf.*, Commission Notice, 1997 O.J. C 372/033 ¶ 24 (noting the third source of competitive restraint, potential competition is not considered when defining markets).

[98] William A. Brock, *Contestable Markets and the Theory of Industry Structure: A Review Article*, 91 J. POL. ECON. 1055, 1055 (1983); *See also* BAUMOL, PANZAR & WILLIS, *supra* note 94, at 5.

[99] William G. Shepherd, *"Contestability" vs. Competition*, 74 AM. ECON. REV.

enter into the market, but also the ability to overcome any regulatory barriers which impede entry. Condition (2) holds that exit from the market must also be easy (*i.e.*, costless).[100] While sale or leasing of assets can reduce the friction of exit, sunk costs involved with intangibles (goodwill, advertising, non-transferable licenses, etc.) move the actual market further away from the paradigm of the contestable market. Hence the market is characterized by "costlessly reversible entry."[101] A corollary of the former two points is condition (3) that there is equal access to the technology and infrastructure required by the market to produce and/or deliver the goods.[102] And condition (4) holds that a new entrant can establish itself on the market instantaneously, "The entrant can establish itself before an existing firm makes any price response."[103] In effect, such a contestable market can be described as one where it is possible to "hit and run," *i.e.,* enter and leave the market rapidly and without expense.

Baumol et al. use the example of air travel as an illustration:

> Consider two towns between which the demand for travel is only sufficient to support one flight a day. This is a natural monopoly market. And yet, because airline equipment (virtually "capital on wings") is so freely mobile, entry into the market can be fully reversible. In principle, faced with a profitable opportunity in such a market, an entrant need merely fly his airplane into the airport, undercut the incumbent's price, and fly the route profitably. Then should the incumbent respond with a sufficient price reduction, the entrepreneur need only fly his airplane away to take advantage of some other lucrative option—even if he only returns his rented aircraft or resells it in the well-functioning secondary aircraft market. Thus it is highly plausible that air travel provides real examples of contestable markets.[104]

This may overstate their case.[105] As Sheppard notes, the as-

572, 573 (1984).

[100] *Id.*

[101] *Id.* at 576.

[102] In the canonical example of air travel, this would include equality of access to slot pairs.

[103] Sheppard, *supra* note 99, at 573.

[104] BAUMOL, PANZAR & WILLIS, *supra* note 94, at 7.

[105] *See*, *e.g*., Sheppard, *supra* note 99, at 581 (noting that airlines and long distance telephone services do not reflect ultra-free entry; rather, airline shifts have been far from instantaneous, and entrants into long-distance telephone service gained a mere five percent of the market in the course of four years); *See, e.g., Id.*

sumptions on which Baumol et al. build their case are very demanding.[106] Further, even in the example of air travel, one wonders how fast a potential entrant can establish itself in a new market, whether this speed exceeds the incumbent's ability to drop prices, how low the sunk costs in establishing a new route are, and whether the secondary aircraft market is sufficiently efficient to allow costless exit from aircraft ownership or lease.[107]

The commercial parties in *Concepcion*, *Brown,* and *Italian Colors* operate in markets which are structurally different from contestable markets, as we show below. I further note that the further from the structure of a contestable market a particular market is, the more susceptible that particular market is to collusion (cartelization).

Developing on the work of Steigler,[108] industrial organization economists[109] have identified numerous features in a market's structure which are conducive to collusive conduct by players in the market. Prominent among these features which allow for ease in collusion are:

- Inelastic demand of the product;
- A concentrated sellers' market;
- Barriers to entry;
- Lack of concentration in the buyers' market; and,
- Homogeneous goods.[110]

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at 575 (noting that ". . . Baumol et al.'s optimism about efficiency appears to exceed even Chicago school levels").

[106] *Id.* at 573: "These conditions are pure, and the deductive results hold only when they hold. Under any departures from the pure conditions, Baumol et al.'s deductive analysis becomes speculative. One can revert then to the extensive literature on entry barriers for guidance in estimating the outcomes."

[107] *See also* MASSIMO MOTTA, COMPETITION POLICY: THEORY AND PRACTICE 73-75 (1st ed. 2004) (describing problems with the Baumol, Panzar and Willig's assumptions).

[108] George J. Steigler, *A Theory of Oligopoly*, 72 J. POL. ECON. 44 (1964).

[109] *See, e.g.,* ROBERT C. MARSHALL & LESLIE M. MARX, THE ECONOMICS OF COLLUSION: CARTELS AND BIDDING RINGS 211–37 (2012); *See* William E. Kovacic, Robert C. Marshall, Leslie M. Marx & Halbert L. White, *Plus Factors and Agreement in Antitrust*, 110 MICH L. REV. 393 (2011); *See* Margaret C. Levenstein & Valerie Y. Suslow, *What Determines Cartel Success?*, 44 J. ECON. LIT. 43 (2006).

[110] *See* Cento Veljanovski, *The Economics of Cartels*, FINNISH COMPETITION

This is not an exhaustive list.[111] It, however, does show that the industries in which these recent US cases originated are not only different from paradigmatic contestable markets, but are markets which are more susceptible to collusion.[112] In *Concepcion* the market related to cellular telephones and services (a homogenous commodity), in *Brown* it was care home services, and in *Italian Colors* the market involved charge cards. There are significant entry barriers to the cellular phone market: these include regulatory approval and infrastructure access (the ability to use transmission towers and have access to other networks for call-termination). The advertising expenditure required to promote a viable alternative network is a significant sunk cost, and thus represents a formidable exit barrier.

Care homes require some regulatory approval, sunk costs in the development of specialized facilities, and the existence of long-term care contracts provides a formidable exit barrier. The geographic markets tend to be concentrated. Credit and charge card markets are two-sided platforms which require significant cost (and a non-trivial amount of time) to develop. The greater the developmental cost necessary to enter (and compete on) the market, the further away that market is from a contestable market (due to the exit friction of sunk costs). Likewise, the greater the time it takes for a product (such as a charge card) to be accepted in the market, the less instantaneous the challenger's entry can be, thus permitting the incumbent a greater opportunity to respond. This market structure can thus lead to collusive behavior in the market. [113] Such collusion will often take the form of standardization in terms of service.

B. The Commercial Context and Contracts of Adhesion

The consumer contracts that are the source of the present discussion are in effect contracts of adhesion, with no room for the consumer to bargain and pay for additional remedies. In the *Concepcions*' case there would have been no opportunity for them to offer or be presented a second contract which permitted class action suits in

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LAW YEAR BOOK 4-6 (2006) (Veljanovski does not add homogeneity of product as a characteristic; however, a significant number of major domestic and international cartels involve homogenous goods).

[111] *See id.* (noting that absence of non-price competition, high risk of bankruptcy, static or declining demand, multi-market contacts, a market in intermediate products and a history of collusion are others); *See* sources cited *supra* note 109.

[112] See *supra* note 109.

[113] *See also,* MOTTA, *supra* note 107, at 142–49 (discussing the market structure and product characteristics facilitating collusive behavior).

exchange for a premium on their monthly cellular phone charge, nor was the Brown family able to pay a supplement to the care fees to ensure that jury awards would be available were Clarence Brown mistreated. The "negotiating process" (if one could call it that) which went into the formulation of these contracts was vastly different from a situation where there is some "give and take" in what one wants and is willing to pay. Indeed, the process of buying, say, a computer has greater scope for the "purchase" of additional remedies: one is almost always presented with the option of buying an extended warranty. Hence in cases such as this, some additional protection or remedies are available, albeit for a price.

Theories suggesting the equalization of a rate of return or contestability of the particular market might imply the entry of a maverick into the market to provide the product but without the exclusions normally demanded by the incumbents. Yet, high entry and exit barriers prevent the emergence of such contenders. Indeed, the absence of alternatives to the contracts proffered to the consumers in each of these cases is significant. The unavailability of alternatives casts doubt on the contestable nature of the markets and the applicability of the equalization of return principle within those particular markets. And the highly concentrated nature of the market may be suggestive of some sort of coordinated activity, if not outright collusion.

The use of arbitration-facilitated exclusions in employment contracts adds an additional level of concern. These contracts are most certainly contracts of adhesion, presented to someone who is in weaker bargaining position than the entity which presents the contract. Outside of the occasional superstar, very few employees have sufficient bargaining power to have much influence on the terms and conditions of their employment. Even when such power exists, it is unlikely to extend to the means by which disputes are resolved, due to industry practice. Last year's MVP, who is this year's free agent, is unlikely to be able to bargain their way out of the league's employment dispute resolution provision. In the context in which the contracts in question occurred, the employee was very much a replaceable, homogenous good for the employer. Had he or she balked at agreeing to the terms proffered, another employee would have been hired in their stead.[114] And it would be somewhat disingenuous to

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[114] *See also* Cole v. Burns Security Services, 105 F. 3d 1465, 1469 (D.C. Cir. 1997) (noting that the contract of employment included the following term: "YOU MAY WISH TO CONSULT AN ATTORNEY PRIOR TO SIGNING THIS AGREEMENT. IF SO, TAKE A COPY OF THIS FORM WITH YOU. HOWEVER, YOU WILL NOT BE OFFERED EMPLOYMENT UNTIL THIS

suggest that another employer would have gladly come along and offered these employees contracts without the exclusions for some consideration in the form of a slightly reduced wage. The commercial context in the cases of both consumer and employment contracts raises the normative challenges of "justice" and "fairness," which we explore in the following section.

V. A RAWLSIAN DIGRESSION: ARE THESE EXCLUSIONS FAIR?

Given that in the case of exclusions of remedies through the use of arbitration agreements no supplementary remedies are available (even at a price) it is worth inquiring whether this situation could be regarded as just or fair. This is particularly so given the push within Congress for reforms to the Federal Arbitration Act on fairness grounds. While discussions of justice have been an ongoing theme in the western intellectual tradition since at least the time of Plato, Rawls' late twentieth century analysis of the idea of justice[115] within a liberal society, and its explicit link to a sophisticated analysis of fairness is an appropriate point from which to begin our analysis.

The central conception which motivates Rawls' theory is an understanding of the need to develop a procedure or conditions by which parties can come to a hypothetical agreement on developing what would be viewed by those parties as fair or just institutions. Those coming to such an agreement, Rawls suggests, would be highly risk averse[116] and this risk aversion would shape their attitudes to their choice of institutions. Key to Rawls' analysis of fairness and the shaping of fair institutions is the insight that such institutions be designed by those who are unable to take advantage of any morally irrelevant characteristics which they could use for their advantage in the design of such institutions.[117] Rawls' insight is to place the bargaining parties into a situation where no irrelevant information can have an influence on what option a party would choose, hence that party could not bargain from a position of self-interest. This is the meaning behind the maxim "justice as fairness," which drives the bulk of Rawls' argument.

Institutional choice would be made behind a hypothetical

FORM IS SIGNED AND RETURNED BY YOU.") Cole was required to agree to the contract after his original employer was taken over by Burns. *Id.*

[115] RAWLS, *supra* note 10.

[116] *Id.* at 132–53.

[117] *Id.* at 11, 118–23.

"veil of ignorance."[118] This veil of ignorance is a thought experiment developed by Rawls[119] to allow one to determine what choices would be made by people who were unable to bargain from a position of self-interest using morally irrelevant information. Rawls describes the concept thus:

> It is understood as a purely hypothetical situation characterized so as to lead to a certain conception of justice. Among the essential features of this situation is that no one knows his place in society, his class position or social status, nor does anyone know his fortune in the distribution of natural assets and abilities, his intelligence, strength and the like. I shall even assume that the parties do not know their conceptions of the good or their special psychological propensities. The principles of justice are chosen behind a veil of ignorance. This ensures that no one is advantaged or disadvantaged in the choice of principles by the outcome of natural chance or the contingency of social circumstances. Since all are similarly situated and no one is able to design principles to favor his particular condition, the principles of justice are the result of a fair agreement or bargain. . . . The original position is, one might say, the appropriate initial status quo, and thus the fundamental agreements reached in it are fair. This explains the propriety of the name "justice as fairness:" it conveys the idea that the principles of justice are agreed to in an initial situation that is fair.[120]

The hypothetical choices made in this thought experiment will be shaped by the information that can be provided to the participants. Initially, little information is provided, and the participants will formulate the most basic social and legal principles. Institutional design will come later, as the veil is metaphorically "lifted" and the participants gain more general knowledge about the society for which the institutions are developed. However, this knowledge is still suffi-

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[118] This approach has been suggested by Sternlight and Jensen. *See* Sternlight & Jensen, *supra* note 46, at 96, n.128; *see also* Bruce Wardhaugh, *A Normative Approach to the Criminalization of Cartel Activity*, 32 LEGAL STUD. 369 (2012) (discussing Rawls' use of this thought experiment to argue that the market would be the means of distributive justice chosen in a just society and the sort of conduct one would expect in such a market).

[119] RAWLS, *supra* note 10.

[120] *Id.* at 11; *See also id.* at 118–23 (elaborating and justifying restrictions found "under the veil of ignorance").

ciently non-specific so that it cannot be used for self-interested purposes.

Those selecting under the veil of ignorance are also deprived of any knowledge of probabilities of possible outcomes. This ensures that any principles chosen or social institutions designed by them are done in ignorance of any morally irrelevant factors which can be used for the advantage of those so selecting or designing. Additionally, those under the veil are risk adverse, and unwilling to gamble. Hence choices will be made under a maximin principle of choice under uncertainty which suggests a ranking of possible outcomes and a choice of the least bad outcome (*i.e.*, maximize the minimum).[121]

The participants would initially choose fundamental principles, and then as the veil was lifted, design social institutions. The choice of fundamental principles and design of institutions is guided by this risk aversion. Rawls notes:

> [In the original position] the person choosing has a conception of the good such that he cares very little, if anything, for what he might gain above the minimum stipend that he can, in fact, be sure of by following the maximin rule. It is not worthwhile for him to take a chance for the sake of a further advantage, especially when it may turn out that he loses much that is important to him.[122]

From this position, Rawls argues that those under the veil agree upon two principles of justice. To avoid conflicts between competing applications of the principles they would be ranked in lexical order with priority given to the first principle.

These principles of justice, in their final version,[123] are:

> First Principle
>
> Each person is to have an equal right to the most extensive total system of equal basic liberties compatible with a similar system of liberties for all.
>
> Second Principle

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[121] *See also* MELVIN DRESHER, GAMES OF STRATEGY: THEORY AND APPLICATIONS 21-35 (1961) (presenting a classic, albeit formal, discussion of this rule).

[122] RAWLS, *supra* note 10, at 134.

[123] *Id.* at 53 (initially presenting a preliminary version, which contains some ambiguities resolved in subsequent discussion).

> Social and economic liberties are to be arranged so that they are both:
>
> to the greatest benefit of the least advantaged, consistent with the just savings principle, and
>
> attached to offices and positions open to all under conditions of fair equality of opportunity.[124]

Given their foundational nature, these principles of justice will shape the participants' formulation of all other social institutions. Hence the promotion of liberty, when consistent with equal liberties for others, will be a fundamental precept by which legal and social institutions are designed. Likewise, the underlying maximin rule which prompted the choice of the two principles of justice will also prompt similar risk aversion—and hence considerations of fairness—when more specific social and legal institutions (such as legal codes and dispute resolution means) are designed.

In designing such institutions, this metaphorical "veil of ignorance" precludes a participant in the bargaining (*i.e.,* design) process from knowing their role in the application of the institution, the likelihood that particular events would occur, and the costs of these events. Further, the application of the "veil of ignorance" excludes knowledge of probabilities and amounts from the bargaining parties' knowledge,[125] thereby precluding parties designing social institutions from using expected value calculation in their design.

Those designing a legal system under a "veil of ignorance" would initially arrive at the two principles of justice identified above.[126] The principles serve to establish the foundation of any liberal society, upon which the most general economic and legal institutions would be established. The principle of liberty would point towards both a market-based means of distributive justice,[127] and a democratic constitution.[128] Once these fundamental legal and economic principles are established, or agreed upon, those under the veil would be provided with more information which they would be able to use in developing more specific legal fields designed to respond to the more particular social circumstances facing those under the veil.

It would be at this point where our hypothetical social archi-

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[124] *Id.* at 266.
[125] *Id.* at 148–53, 160.
[126] *See supra* text accompanying notes 122–123.
[127] RAWLS, *supra* note 10, at 239–43.
[128] *Id.* at 173–75, 195–200.

tects would design the legal regimes regulating our interaction. These would include contract regimes to govern our voluntary exchanges and tort and criminal regimes to govern involuntary interactions. In addition to these substantive principles, those under the veil would also design the procedural systems which would be used to give effect to the substantive regimes. While the information made available to those hypothetically designing such a system would be more complete during the process of design, the designers would never be provided with information that they could use to their own advantage. This would ensure that the substantive regimes and procedural rules are not in any way biased. For instance, since those designing the legal rules surrounding accident compensation would not know if they would be tortfeasors or victims, there would be every incentive not to design the tort system (and the procedural means by which it is enforced) to favor either victims or tortfeasors.

Once these legal regimes of general application are developed and as the legal architects obtain further information about the society whose legal system they are developing, the architects will be in a position to enlarge the regime by adding legal rules and systems to complement those developed earlier. For instance, a "basic" intellectual property regime which provides copyright protection for printed media can be supplemented by providing protection for digital media, once the architects recognize that the society for which they are designing a legal system is sufficiently technologically advanced to require such security.

Likewise, supplementary provisions can also be added to procedural regimes via a developed and recognized alternative dispute resolution ("ADR") system outside of, but complementary to, the courts. In family matters, for example, systems of pre-trial mediation may be added to take the "edge" off an adversarial system (if the architects indeed opted for an adversarial system). Similarly, arbitration panels could be established to facilitate dispute resolution, by offering arbitrators whose expertise reduces the chance of decision error which may result from a non-specialist judge deciding the matter; or by offering speedier resolution to a matter than would be perhaps obtained by waiting one's turn in an overcrowded docket.[129]

What is fundamental about these supplementary provisions—whether substantive or procedural—is that they build on and are additions to the preexisting legal regimes that they enhance. As such, the

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[129] *See, e.g.,* Stephen J. Ware, *Is Adjudication a Public Good? "Overcrowded Courts" and the Private Sector Alternative of Arbitration,* 14 CARDOZO J. OF CONFLICT RESOL. 899 (2013).

regime on which the supplement rests serves as the baseline for the "fairness" or justice of the supplementary provisions which augment it. As an example, as the principles of justice serve as a baseline for the moral legitimacy of the constitution which underpins the legal system, it would be improbable that Rawlsian social architects would design a society's constitution the provisions of which would fall below the standards of the two principles of justice. It is submitted that the Rawlsian legal architects designing ADR provisions to supplement existing procedural institutions (and their rules) would use what exists as a baseline for the fairness. This baseline serves as a yardstick to measure the fairness of what is developed as a supplement. Accordingly, as a baseline, these legal standards should serve as a minimum by which any supplementary institutions constructed "on to of them," are to be evaluated.

This Rawlsian lens can permit us to focus our analysis of the fairness or justice of arbitration systems and exceptions. There are two focal points to the discussion. The first is in regards to the fairness of arbitration procedures. The second focus concerns the exceptions imposed by these arbitration agreements, to determine the extent that such exceptions may be viewed as unjust or unfair, in the sophisticated sense shown by this analysis, and not in the intuitive, instinctive sense which informs much of the rhetoric surrounding the controversy. In effect, the Rawlsian lens asks us to examine these points from the perspective of a disinterested party. As noted above, this disinterest takes the form of ignorance, in the literal sense, *i.e.,* a lack of knowledge of that party's present or future position, to ensure that party's inability to use such information to its advantage in subsequent design of any social or legal institution.

By applying this lens to arbitration generally, as an adjunct to the public system and as long as the arbitration regime was freely chosen by all parties, a system of arbitration in skeletal form would appear to be unproblematic. Like the court system it supplements, a neutral party is charged with resolving the dispute between parties. As a supplement to this system, it will not fall below the baseline of fairness of the court system. Further, the first principle of liberty,[130] guaranteeing the greatest set of liberties co-extensive with an equal set for others, compels granting individuals the opportunity to select such a system of dispute resolution.

It is when the metaphorical skeleton of arbitration—particularly in the consumer context—gets "fleshed out" that difficulties arise. If we apply this thought experiment to the four exclusions

[130] *See* RAWLS, *supra* note 10.

at issue, I suggest our results would be mixed if not inconclusive. Limitations on discovery are a procedural matter. Looked at through the Rawlsian lens, there is no easy, *a priori* answer to the fairness issue. Although the arbitration system's use of discovery analogous to the regime mandated by the more general litigation would ensure a baseline of fairness, truncated discovery can also be fair. Illustrative of this are the limitations to discovery imposed by the rules of the major international, commercial arbitration institutions.[131] The significance of the limits imposed in such arbitrations is that they are symmetric, imposing identical limitations on each side to the dispute. Under the uncertainty imposed by the "veil of ignorance" of not knowing "which side" of a dispute a designer of the system will be on, it would be highly unlikely that—in the absence of countervailing considerations—the Rawlsian legal architect would design a system of dispute resolution which incorporates such asymmetries. Indeed, it is submitted that if the Rawlsian analysis of fairness advocated in this paper is accepted, then asymmetries in the arbitration regime should serve as a prima facie screen of unfairness.

However, asymmetries are only prima facie screens. Countervailing considerations may well exist which could justify asymmetry. "Carve-outs" for collections may be one such example. If the parties—under a "veil of ignorance"—were aware that (1) the vast majority of majority of collections actions proceed in default[132] and (2) commencing collections by arbitration required the addition of an extra legal step,[133] which adds expense to the procedure, the parties may very well agree to this asymmetry. Given that consumers would benefit from not bearing the burden of costs arising from these redundant legal steps, the asymmetry of the "carve-outs" may well be regarded as failures, when examined under this lens.

The exclusion of certain categories of damages (*e.g.,* punitive damages) and class remedies is problematic. Where such remedies are unavailable in the underlying legal system, there is no concern that their exclusion by way of arbitration reduces the level of justice offered by that supplementary ADR regime. It is significant to note that in Europe, punitive damages are extremely limited[134] and class

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[131] *See* sources cited *supra* note 80

[132] *See supra* text accompanying notes 80–81.

[133] *Id.*

[134] Indeed, in the Franch legal regime, the maxim "*tout le dommage, mais rein que le dommage,*" ("all the damage, but nothing more than the damage") applies as the maxim to measure and limit compensation.

actions are ill-developed.[135] To facilitate redress of consumer and competition claims, the European Commission and Parliament have, over the past few years, been drafting proposals to expand and harmonize collective redress regimes within the differing European legal systems.[136] The most recent (June 2013)[137] proposal involves an opt-in (versus the US-style opt-out) system, designed specifically to prevent the importation of perceived American-style abuses into Europe.[138] As class claims and punitive damages are not well-developed features of the European legal landscape, fears of the use of arbitration in consumer matters to deprive consumers of this remedy would be misplaced.[139] Indeed the European response to the use of arbitration in consumer matters shows little other than fears of asymmetric bargaining strength in contracts of adhesion.[140] However, in a jurisdiction (such as the US), in which such remedies and procedural devices are available, to require a party to forego them (*via* a contract of adhesion) appears to fall below the minimum standard of justice which appears through the Rawlsian lens, unless other compensatory benefits are passed on in exchange.

But while the elimination of such remedies and procedural

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[135] S*ee, e.g.,* JURGEN G. BACKHAUS, ALBERTO CASSONE & GIOVANNI B. RAMELIO, THE LAW AND ECONOMICS OF CLASS ACTIONS IN EUROPE: LESSONS FROM AMERICA (2012); *see, e.g.,* Wardhaugh, *Bogeymen*, *supra* note 67, at 16–22.

[136] *See, e.g., id*., at 13–18.

[137] Commission Recommendation of XXX on Common Principles for Injunctive and Compensatory Collective Redress Mechanisms in the Member States Concerning Violations of Rights Granted Under Union Law, Strasbourg XXX, 2013 C 3539/3, *available at* http://ec.europa.eu/justice/civil/files/c_2013_3539_en.pdf; Commission Communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions "Towards a European Horizontal Framework for Collective Redress" Brussels, XXX, 2013 COM 401/2, *available at* http://ec.europa.eu/justice/civil/files/com_2013_401_en.pdf.

[138] *See also* Press Release, European Comm'n, Commission Recommends Member States to Have Collective Redress Mechanisms in Place to Ensure Effective Access to Justice (June 11, 2013), *available at* http://europa.eu/rapid/press-release_IP-13-524_en.htm (quoting Vice-President Viviane Reding "Member States have very different legal traditions in collective redress and the Commission wants to respect these. Our initiative aims to bring more coherence when EU law is at stake. . .This Recommendation is a balanced approach to improve access to justice for citizens while avoiding a US-style system of class actions and the risk of frivolous claims and abusive litigation").

[139] It makes no sense to suggest that arbitration can be used to deny a remedy to which a party has no legal entitlement.

[140] *See supra* text accompanying note 53.

devices will reduce the costs to consumers—assuming that the savings will be passed on to consumers—it is far from clear that savings from the excluded remedies would be welcomed by consumers were they given a choice. Even if this assumption is correct, as consumers, we may wish to pay more (as a sort of insurance policy) in order to have the benefits of collective remedies and recourse to classes of damages which might be otherwise excluded. However, if the assumption is false and the market structure of the industries in which these exclusions are found is indeed anti-competitive, a different result follows. The so-called "savings" from the excluded remedies are thus retained by the firms as a form of appropriated consumer surplus. If these exclusions are used to facilitate such anti-competitive conduct, then it is further submitted, they would fail the test of fairness.

CONCLUSION

The foregoing Rawlsian analysis casts doubts on whether the practice of using arbitration agreements to exclude certain remedies and means of pursuing remedies is just. The underlying insight of the theory is to show, via a thorough experiment, that a fair or just institution would be the sort of institution that is designed by those who have no knowledge of how that institution would affect them. The architects of the relevant social institution are placed under a metaphorical "veil of ignorance" which precludes them from being aware of any morally irrelevant information which they could use to their own advantage in the institution's design. Being risk adverse, particularly with their liberty interests, these hypothetical social and legal architects would design fair social and legal systems.

Given that those designing the institution would be rendered ignorant of how this institution could possibly affect them, this Rawlsian analysis suggested that the existence of symmetry of the rights and obligations of parties within an institutional framework was indicative of such fairness. Deprived of morally irrelevant knowledge, the Rawlsian who drafts a consumer arbitration contract would be unaware (once the "veil of ignorance" is lifted) which side of the bargain they would be facing. Accordingly, the agreement would not be drafted to advance the interests of one side over the other.

A "real world" example of such contracts might be found in those commodities contracts (and the arbitration institutions which resolve disputes arising from transactions governed by them) used by trading houses whose business is dealing in these goods.[141] Given their near universal use in the trade, and that the parties using them use them as both buyers and sellers, these contracts exhibit no asymmetries which advantage one side over the other. Indeed, as the parties to the contracts would be buyers about half the time, and sellers the other half, it would make no commercial sense for asymmetric contracts to be used.

However, as I have argued, under this Rawlsian lens, asymmetry is only a prima facie indicium of unfairness. Asymmetries in contractual rights and obligations may give rise to a presumption of fairness, but this presumption is nevertheless rebuttable. My discussion of asymmetrical collections "carve-outs" showed that they may in fact be fair. If such "carve-outs" promote cost savings which are then passed onto consumers, these savings may represent an appropriate quid pro quo for the lost opportunity to arbitrate collections matter. Indeed, given that such collections actions usually proceed in default, the cost of this lost opportunity is likely negligible.

On the other hand, investigation of other asymmetries points in a different direction. As seen above, the elimination of class actions and punitive damages via arbitration agreements appear not just to be uncompensated for by other benefits flowing from the agreement, but part of a general practice in industries whose structure is susceptible to collusion. If this is the case, such industrial structure casts into doubt the veracity of many of those assumptions underlying the arguments used to support the expansion of arbitration agreements to eliminate consumers' access to such remedies. But what is significant is that this paper shows that not all exceptions can be treated as unequivocally unfair or unjust: some may be beneficial to consumers. Accordingly, efforts to condemn them generally—as done in Europe and has been proposed from time-to-time in the US—are likely overbroad. "Putting on" and then "pulling aside" a Rawlsian "veil of ignorance" serves as an appropriate, albeit metaphorical, means of demonstrating these points.

[141] *See supra* text accompanying notes 13–14.