

ARBITRATION OF CONSUMER DISPUTES

The AAA's Consumer Due Process Protocol

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I. Due Process Concerns

One of the most significant complaint regarding arbitration of consumer disputes is that arbitration lacks many of the crucial due process protections of the justice system.¹ The arbitration forum deprives consumers of an independent judge, a jury of one's peers, and a system with built-in due process safeguards.² Frequently, the arbitration process provides little or no opportunity to conduct discovery, making it difficult for victims to vindicate their rights against wrongdoers.³ Most arbitration awards include no reasoned explanation of the decision reached and arbitrator's decisions do not have precedential effect in later arbitration proceedings.⁴ Arbitrators who are not lawyers cannot be compelled to follow the standards of ethics established by the legal community.⁵ Arbitrators are not required to adhere to formal rules of evidence and may consider evidence that would be inadmissible in a court of law, such as hearsay evidence.⁶ Adding to these problems is the fact that arbitrator's decisions are generally exempt from meaningful review.⁷ Because arbitrators generally do not issue extensive written opinions, it is often impossible for a party to provide sufficient evidence of a defective arbitration proceeding or award.⁸

II. AAA Response—Consumer Due Process Protocol

The American Arbitration Association, "AAA," has addressed many of the due process concerns associated with consumer arbitration through its newly adopted *Consumer Due Process Protocol* (the Protocol) developed by the AAA's National Consumer Disputes Advisory Committee (the Advisory Committee).⁹ The purpose of the Advisory Committee is to advise the AAA in the development of standards and procedures for the equitable resolution of consumer disputes.¹⁰

A. Scope of the Protocol

The Protocol was developed to address a wide range of consumer transactions—from small claims to complex disputes—pertaining to the purchase or lease of goods or services for personal, family or household use.¹¹ These include, among other things, transactions involving: banking, credit cards, home loans and other financial services; health care services; brokerage services; home construction and improvements; insurance; communications; and the purchase and lease of motor vehicles and other personal property.¹²

B. Goals of the Advisory Committee

The Advisory Committee sought to develop principles that would establish clear benchmarks for conflict resolution, while recognizing that a process appropriate in one context may be inappropriate in another.¹³

Therefore, the Protocol embodies flexible standards that permit consideration of a consumer's specific circumstances.¹⁴ For example, some consumer arbitration agreements are the product of negotiation between sophisticated companies or corporations.¹⁵ However, many arbitration provisions found in consumer contracts often do not involve arm's length negotiation of terms, and frequently consist of boilerplate language presented on a "take it or leave it" basis by suppliers of goods or services.¹⁶ Therefore, there are legitimate concerns regarding the fairness of consumer Alternative Dispute Resolution (ADR).¹⁷ This is particularly true in the realm of binding arbitration, where the courts are displaced by private adjudication systems.¹⁸ In such cases, consumers are often unaware of their procedural rights and obligations until the realities of out-of-court arbitration are revealed to them after disputes have arisen.¹⁹ While the results may be entirely satisfactory, they may also fall short of consumers' reasonable expectations of fairness and have a significant impact on consumers' substantive rights and remedies.²⁰

The AAA recognizes that users of ADR programs are entitled to a process that is fundamentally fair.²¹ The Protocol provides consumers and businesses with standards governing consensual and court-connected ADR programs, including arbitration.²² The Protocol attempts to enhance the likelihood that consumers will have specific knowledge of ADR provisions at the time of contracting by describing a baseline of consumers' reasonable expectations for ADR in consumer transactions.²³

C. Enforcement of the Protocol

The AAA is able to enforce the due process standards set by the protocol by closing its doors to those businesses that refuse to adhere to the Protocol's standards.²⁴ Businesses that use the arbitration services of the AAA in consumer arbitration transactions are required to (1) notify the AAA of their intention to do so; and (2) provide the AAA with a copy of the clause at least thirty (30) days before the planned effective date of the clause.²⁵ If the AAA determines, in a case involving a claim under \$75,000, that a dispute resolu-

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tion clause on its face, substantially and materially deviates from the minimum due process standards of the Protocol, the AAA may decline to administer cases arising under the clause.²⁶

Additionally, where arbitration provisions in standardized consumer contracts fail to meet Consumers' reasonable expectations, there is authority for the principle that courts may properly refuse to enforce the arbitration agreement in whole or in part.²⁷ In *Cantella & Co. v. Goodwin*, the Texas Supreme Court considered the question of whether non-compliance with the arbitration rules and procedures established by a private, independent, self-regulating organization makes an arbitration agreement void.²⁸ The party seeking to avoid arbitration alleged that Cantella failed to comply with the Rules of Fair Practice, regarding arbitration provisions, established by the National Association of Securities Dealers (NASD). Therefore, it alleged, the agreement to arbitrate was void.²⁹ The court rejected the argument in this case, finding that the parties' agreement did not require that the NASD rules apply. The outcome, however, probably would have been different had the agreement expressly called for the NASD rules to apply.³⁰ Where parties' contracts containing arbitration provisions have violated the NASD rules and, at the same time, expressly called for the NASD rules to apply, courts have declared the arbitration agreements invalid.³¹ The court's discussion in *Cantella* supports the proposition that businesses who designate the AAA as their arbitration service provider in arbitration agreements must comply with the requirements of the AAA, including the standards set by the Protocol, or run the risk of the arbitration agreement being declared invalid upon review.³²

D. The Principles

PRINCIPLE 1. FUNDAMENTALLY-FAIR PROCESS

All parties are entitled to a fundamentally-fair ADR process. As embodiments of fundamental fairness, these Principles should be observed in structuring ADR Programs.

PRINCIPLE 2. ACCESS TO INFORMATION REGARDING ADR PROGRAM

Providers of goods or services should undertake reasonable measures to provide Consumers with full and accurate information regarding Consumer ADR Programs. At the time the Consumer contracts for goods or services, such measures should include (1) clear and adequate notice regarding the ADR provisions, including a statement indicating whether participation in the ADR Program is mandatory or optional, and (2) reasonable means by which Consumers may obtain additional information regarding the ADR Program. After a dispute arises, Consumers should have access to all information necessary for effective participation in ADR.

PRINCIPLE 3. INDEPENDENT AND IMPARTIAL NEUTRAL; INDEPENDENT ADMINISTRATION

1. Independent and Impartial Neutral. All parties are entitled to a Neutral who is independent and impartial.

2. Independent Administration. If participation in mediation or arbitration is mandatory, the procedure should be administered by an Independent ADR Insti-

tution. Administrative services should include the maintenance of a panel of prospective Neutrals, facilitation of Neutral selection, collection and distribution of Neutral's fees and expenses, oversight and implementation of ADR rules and procedures, and monitoring of Neutral qualifications, performance, and adherence to pertinent rules, procedures and ethical standards.

3. Standards for Neutrals. The Independent ADR Institution should make reasonable efforts to ensure that Neutrals understand and conform to pertinent ADR rules, procedures and ethical standards.

4. Selection of Neutrals. The Consumer and Provider should have an equal voice in the selection of Neutrals in connection with a specific dispute.

5. Disclosure and Disqualification. Beginning at the time of appointment, Neutrals should be required to disclose to the Independent ADR Institution any circumstance likely to affect impartiality, including any bias or financial or personal interest which might affect the result of the ADR proceeding, or any past or present relationship or experience with the parties or their representatives. The Independent ADR Institution should communicate any such information to the parties and other Neutrals, if any. Upon objection of a party to continued service of the Neutral, the Independent ADR Institution should determine whether the Neutral should be disqualified and should inform the parties of its decision. The disclosure obligation of the Neutral and procedure for disqualification should continue throughout the period of appointment.

PRINCIPLE 4. QUALITY AND COMPETENCE OF NEUTRALS

All parties are entitled to competent, qualified Neutrals. Independent ADR Institutions are responsible for establishing and maintaining standards for Neutrals in ADR Programs they administer.

PRINCIPLE 5. SMALL CLAIMS

Consumer ADR Agreements should make it clear that all parties retain the right to seek relief in a small claims court for disputes or claims within the scope of its jurisdiction.

PRINCIPLE 6. REASONABLE COST

1. Reasonable Cost. Providers of goods and services should develop ADR programs which entail reasonable cost to Consumers based on the circumstances of the dispute, including, among other things, the size and nature of the claim, the nature of goods or services provided, and the ability of the Consumer to pay. In some cases, this may require the Provider to subsidize the process.

2. Handling of Payment. In the interest of ensuring fair and independent Neutrals, the making of fee arrangements and the payment of fees should be administered on a rational, equitable and consistent basis by the Independent ADR Institution.

PRINCIPLE 7. REASONABLY CONVENIENT LOCATION

In the case of face-to-face proceedings, the proceedings should be conducted at a location which is reasonably convenient to both parties with due consideration of their ability to travel and other pertinent circumstances. If the parties are unable to agree on a location, the determination should be made by the Independent ADR Institution or by the Neutral.

PRINCIPLE 8. REASONABLE TIME LIMITS

ADR proceedings should occur within a reasonable time, without undue delay. The rules governing ADR should establish specific reasonable time periods for each step in the ADR process and, where necessary, set forth default procedures in the event a party fails to participate in the process after reasonable notice.

PRINCIPLE 9. RIGHT TO REPRESENTATION

All parties participating in processes in ADR Programs have the right, at their own expense, to be represented by a spokesperson of their own choosing. The ADR rules and procedures should so specify.

PRINCIPLE 10. MEDIATION

The use of mediation is strongly encouraged as an informal means of assisting parties in resolving their own disputes.

SPECIAL PROVISIONS RELATING TO BINDING ARBITRATION

PRINCIPLE 11. AGREEMENTS TO ARBITRATE

Consumers should be given:

(a) clear and adequate notice of the arbitration provision and its consequences, including a statement of its mandatory or optional character;

(b) reasonable access to information regarding the arbitration process, including basic distinctions between arbitration and court proceedings, related costs, and advice as to where they may obtain more complete information regarding arbitration procedures and arbitrator rosters;

(c) notice of the option to make use of applicable small claims court procedures as an alternative to binding arbitration in appropriate cases; and,

(d) a clear statement of the means by which the Consumer may exercise the option (if any) to submit disputes to arbitration or to court process.

PRINCIPLE 12. ARBITRATION HEARINGS

1. Fundamentally-Fair Hearing. All parties are entitled to a fundamentally-fair arbitration hearing. This requires adequate notice of hearings and an opportunity to be heard and to present relevant evidence to impartial decision-makers. In some cases, such as some small claims, the requirement of fundamental fairness may be met by hearings conducted by electronic or telephonic means or by a submission of documents. However, the Neutral should have discretionary authority to require a face-to-face hearing upon the request of a party.

2. Confidentiality in Arbitration. Consistent with general expectations of privacy in arbitration hearings, the arbitrator should make reasonable efforts to maintain the privacy of the hearing to the extent permitted by applicable law. The arbitrator should also carefully consider claims of privilege and confidentiality when addressing evidentiary issues.

PRINCIPLE 13. ACCESS TO INFORMATION

No party should ever be denied the right to a fundamentally-fair process due to an inability to obtain information material to a dispute. Consumer ADR agreements which provide for binding arbitration should establish procedures for arbitrator-supervised exchange of information prior to arbitration, bearing in mind the expedited nature of arbitration.

PRINCIPLE 14. ARBITRAL REMEDIES

The arbitrator should be empowered to grant what-

ever relief would be available in court under law or in equity.

PRINCIPLE 15. ARBITRATION AWARDS

1. Final and Binding Award; Limited Scope of Review. The arbitrator's award should be final and binding, but subject to review in accordance with applicable statutes governing arbitration awards.

2. Standards to Guide Arbitrator Decision-Making. In making the award, the arbitrator should apply any identified, pertinent contract terms, statutes and legal precedents.

3. Explanation of Award. At the timely request of either party, the arbitrator should provide a brief written explanation of the basis for the award. To facilitate such requests, the arbitrator should discuss the matter with the parties prior to the arbitration hearing.

III. Conclusion

The Principles in the Protocol identify minimum due process standards that embody the concept of fundamental fairness. Because they represent a fundamental standard of fairness, an attempt to waive any of these Principles in a pre-dispute agreement would naturally be subject to scrutiny for failing to conform with the reasonable expectations of the parties and other judicial standards governing the enforcement of ADR contracts. However, assuming they have sufficient knowledge and understanding of the rights they are waiving, consumers may waive compliance with these Principles after a dispute has arisen.

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In establishing the Consumer Due Process Protocol, it is the intent of the AAA to create Consumer ADR agreements that are the product of informed consent on the part of the consumer. The purpose of the Protocol is not only to set standards that govern the conduct of businesses that use ADR agreements, but also to educate consumers about the differences between ADR and the court process so that they can make informed decisions about whether or not to submit their claims to ADR. The AAA charges the provider of goods or services with the responsibility for making certain that consumers have access to the appropriate information regarding ADR. Nonetheless, the AAA takes an active role in providing consumers with the information necessary for the effective use of the ADR process by providing an 800 customer service telephone number, written materials, and a website where consumers can learn more about mediation and arbitration procedures.

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¹ F. Paul Bland, Jr., *Resisting Corporate Efforts to Impose Mandatory Arbitration on Consumers*, J. TEX. CONSUMER L., Spring 1999, at 95.

² See *id.*

³ See *id.*

⁴ See *id.*; *IDS Life Ins. Co. v. SunAmerica Life Ins. Co.*, 136 F.3d 537, 543 (7th Cir. 1998) (arbitrator's decisions are not intended to have precedential effect unless given that effect by contract or by later proceeding in court).

⁵ See Preamble: A Lawyer's Responsibilities (1998). However, the conduct of arbitrators and mediators of the American Arbitration Association is guided by the Association's Code of Ethics, prepared by a joint committee of the American Arbitration Association and the American Bar Association, and the Model Standards of Conduct for Mediators, developed by the American Arbitration Association, the American Bar Association and the Society of Professionals in Dispute Resolution. The arbitrators of the National Arbitration Forum conduct arbitrations under the Forum Code of Procedure, which is updated regularly to comply with changes in the law and to ensure fairness.

⁶ See F. Paul Bland, Jr., *Resisting Corporate Efforts to Impose Mandatory Arbitration on Consumers*, J. TEX. CONSUMER L., Spring 1999, at 95.

⁷ See *id.*

⁸ See F. Paul Bland, Jr., *Resisting Corporate Efforts to Impose Mandatory Arbitration on Consumers*, J. TEX. CONSUMER L., Spring 1999, at 100.

⁹ American Arbitration Association, *Consumer Due Process Protocol: Important Notice to Consumers and Businesses* (2001), available at <http://www.adr.org/>.

¹⁰ See American Arbitration Association, *Introduction: Genesis of the Advisory Committee* (2001), available at <http://www.adr.org/>.

¹¹ American Arbitration Association, *Consumer Due Process Protocol: Scope of the Consumer Due Process* (2001), available at <http://www.adr.org/>.

¹² See *id.*

¹³ See American Arbitration Association, *Introduction: Genesis of the Advisory Committee* (2001), available at <http://www.adr.org/>.

¹⁴ See *id.*

¹⁵ See *J.J. Gregory Gourmet Servs., Inc. v. Antone's Import Co.*, 927 S.W.2d 31, 32 (Tex. App.—Houston [1st Dist.] 1995, no writ) (dispute regarding arbitration award arose from arbitration provision in complex franchise agreement and issue of trademark infringement).

¹⁶ See *In re Turner Bros. Trucking Co., Inc.*, 8 S.W.3d 370, 372 (Tex. App.—Texarkana 1999, orig. proceeding) (“take it or leave it” arbitration agreement between employee and employer found to unconscionable and unenforceable where employee was found to be functionally illiterate and had no one to explain the meaning of the document to him).

¹⁷ See *id.* at 375.

¹⁸ See American Arbitration Association, *Introduction: Genesis of the Advisory Committee* (2001), available at <http://www.adr.org/>.

¹⁹ See *id.*

²⁰ See *id.*

²¹ American Arbitration Association, *Reporter's Comments to the Consumer Due Process Protocol* (2001), available at <http://www.adr.org/>.

²² See *id.*

²³ See *id.*

²⁴ See American Arbitration Association, *Consumer Due Process Protocol: Important Notice to Consumers and Businesses* (2001), available at <http://www.adr.org/>.

²⁵ See *id.*

²⁶ See *id.*

²⁷ See American Arbitration Association, *Reporter's Comments to the Consumer Due Process Protocol* (2001), available at <http://www.adr.org/> (citing Restatement (Second) of Contracts § 211 (1981); *Broemmer v. Abortion Services of Phoenix, Ltd.*, 173 Ariz. 148, 840 P.2d 1013 (1992) (standardized arbitration agreement was unenforceable where its terms fell beyond patient's reasonable expectations); *Graham v. Scissor-Tail, Inc.*, 623 P.2d 165 (Cal. 1981) (arbitration clauses in adhesion contracts are unenforceable if they are contrary to the reasonable expectations of parties or unconscionable). Cf. *Cole v. Burns International Security Services*, 105 F.3d 1465 (D.C. Cir. 1997) (setting forth minimum due process standards for judicial enforcement of arbitration agreement in the context of a statutory employment discrimination claim where the employee was required to enter into the agreement as a condition of employment).

²⁸ See *Cantella & Co. v. Goodwin*, 924 S.W.2d 943, 945 (Tex. 1996).

²⁹ See *id.* at 944-45.

³⁰ See *id.* at 945 (citing *Nielsen v. Piper, Jaffray & Hopwood, Inc.*, 66 F.3d 145 (7th Cir. 1995); *Mueske v. Piper, Jaffray & Hopwood, Inc.*, 859 P.2d 444 (Mont. 1993) (in both these cases the courts declared the respective arbitration agreements void because the contracts had specific language requiring that arbitration “shall be in accordance with the rules of the NASD)).

³¹ See *Cantella*, 924 S.W.2d at 945 (citing *Nielsen*, 66 F.3d at 146-47; *Mueske*, 859 P.2d at 450).

³² See *id.*