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# I AGREED TO WHAT?: PROTECTING CONSUMERS FROM UNFAIR PRACTICES IN BINDING CONSUMER ARBITRATION

Laura Magnotta\*

## I. INTRODUCTION

On July 1, 2011 Maryland House Bill 442 was enacted into law.<sup>1</sup> The Act, entitled Consumer Protection –Transparency in Consumer Arbitrations Act, is aimed at protecting consumers who become parties to binding consumer arbitration, particularly through adhesion.<sup>2</sup> The Act requires that specified arbitration organizations collect, publish and make available information relating to binding consumer arbitration.<sup>3</sup> Additionally, the Act lays out specific guidelines for how and when the information is to be published.<sup>4</sup> Failure to comply with the requirements of the Act can result in the arbitration agreement being deemed unconscionable or unenforceable, but may not be “the sole reason to refuse to enforce an award made in consumer arbitration.”<sup>5</sup> A prior attempt at similarly protecting consumers’ interest in binding arbitration was introduced in the Maryland House of Delegates in 2010, was passed out of the House, but died in the Senate coming up one vote shy of passage in the Senate Finance Committee.<sup>6</sup> This article will discuss specific aspects of the new law, place the law within the context of other attempts to protect consumers in binding arbitration, and discuss the practical implications of the law.

## II. CONSUMER PROTECTION – TRANSPARENCY IN CONSUMER ARBITRATIONS ACT

The Consumer Protection –Transparency in Consumer Arbitration Act applies “to an arbitration organization that performs an arbitration activity related to 50 or more consumer arbitrations during a five-year period.”<sup>7</sup> As defined by the Act, “arbitration activity” includes participation in any one or more aspects of arbitration including “initiation, conduct, sponsorship, or administration of, or the appointment of an arbitrator.”<sup>8</sup> Additionally, consumer arbitration is defined as “binding arbitration conducted in accordance with a consumer arbitration agreement.”<sup>9</sup>

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<sup>1</sup> See H.B. 442, 428th Leg., Reg. Sess. (Md. 2011) (enacted) (codified at MD. CODE ANN., COM. LAW §§ 14-3901-3905 (West 2011)). H.B. 442 was crossfiled with S.B. 309 (See S.B. 309, 428th Leg., Reg. Sess. (Md. 2011) (enacted) (codified at MD. CODE ANN., COM. LAW §§ 14-3901 to -3905 (West 2011))).

<sup>2</sup> See Consumer Protection—Transparency in Consumer Arbitration Act, MD. CODE ANN., COM. LAW §§ 14-3901-3905 (West 2011).

<sup>3</sup> See *id.*

<sup>4</sup> See *id.*

<sup>5</sup> See MD. CODE ANN., COM. LAW § 14-3905(b)(1)-(2) (West 2011).

<sup>6</sup> See H.B. 379, 427th Leg., Reg. Sess. (Md. 2010).

<sup>7</sup> MD. CODE ANN., COM. LAW § 14-3902 (West 2011).

<sup>8</sup> *Id.* § 14-3901(b).

<sup>9</sup> *Id.* § 14-3901(e)(1).

This does not include binding arbitration resulting from an agreement for property insurance, casualty insurance or surety insurance; arbitration according to “arbitration rules adopted by a securities self-regulatory organization and approved by the United States Securities and Exchange Commission”; or consumer arbitration involving an institution licensed by the Department of Health and Mental Hygiene if the agreement to arbitrate is not a mandated condition for admission into the institution.<sup>10</sup>

### **A. Required Information**

Arbitration organizations that are subject to the Act are required to “collect, publish, and make available to the public...information regarding each consumer arbitration for which it performed an arbitration activity during the preceding five-year period.”<sup>11</sup> The information required to be published includes: the name of the non-consumer party; whether the dispute involved goods, services, real property or credit; the type of claim or cause of action; which party prevailed; “the number of times during reporting period that the non-consumer party has been a party in a consumer arbitration for which the arbitration organization performed an arbitration activity”; the name of the attorney representing the consumer party; “the date the arbitration organization received the demand for the consumer arbitration, the date the arbitrator was appointed, and the date of disposition by the arbitrator or arbitration organization”; the type of disposition of the dispute; the amount of the claim, award or any other relief granted; the name of the arbitrator, their fee and the percentage of the arbitrator’s fee allocated to each party; and the address of where the consumer arbitration was conducted.<sup>12</sup>

### **B. Publication Method**

The required information is to “be reported beginning on the first day of the month following the month an arbitration organization becomes subject to this [Act]” and “shall be updated at least quarterly thereafter.”<sup>13</sup> More specifically, to be made sufficiently available to the public, the required information shall be published in a “computer-searchable format that is accessible at the Internet Web site of the arbitration organization and may be downloaded without a fee.”<sup>14</sup> The information shall also be made available in writing on request “at a fee that does not exceed the actual cost to the arbitration organization of copying the information.”<sup>15</sup>

### **C. Uses for Information/Failure to Comply**

The requirement for arbitration organizations to collect information regarding consumer arbitration can affect organizations in two main ways. First, the information provided by the arbitration organization as required by the Act “may be considered in determining whether a

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<sup>10</sup> See *id.* § 14-3901(e)(2)(i)-(iii).

<sup>11</sup> *Id.* § 14-3903(a).

<sup>12</sup> See *id.* § 14-3903(a)(1)-(11).

<sup>13</sup> *Id.* § 14-3903(b)(1).

<sup>14</sup> *Id.* § 14-3903(c).

<sup>15</sup> *Id.*

consumer arbitration agreement is unconscionable or otherwise unenforceable under the law.”<sup>16</sup> Second, while an arbitration organization’s failure to comply with the provisions of the Act “may not be the sole reason to refuse to enforce an award made in a consumer arbitration,” it “may be considered as a factor in determining whether a consumer arbitration agreement is unconscionable or otherwise unenforceable under the law.”<sup>17</sup>

An arbitration organization’s failure to comply with the Act allows “a consumer or the Attorney General [to] seek an injunction to prohibit an arbitration organization that has engaged in or is engaging in a violation of §14-3903...from continuing or engaging in the violation.”<sup>18</sup> If the court issues an injunction or the arbitration organization voluntarily complies with §14-3903 after the action is filed, the organization is liable to the person bringing the action for an injunction for the person’s reasonable attorney’s fees and costs.<sup>19</sup>

#### **D. Liability for Reporting**

To encourage reporting of required information, the Act includes a provision that shields arbitration organizations from liability for reporting the information.<sup>20</sup> Under the Act, “[a]n arbitration organization is not liable for collecting, publishing, or distributing the information required under [the Act].”<sup>21</sup> This provision precludes a party whose information was published as required by the Act from suing the publishing arbitration organization.

### **III. ANALYSIS**

The need to protect consumers in binding arbitration is not a new concept. Several cases and specific situations throughout the United States have highlighted the need for consumer protection in binding consumer arbitration particularly where the arbitration agreement is adhesionary. Issues arise as a result of how consumers, who are often forced into arbitrating their claims, are treated during the process. Without transparency in the consumer arbitration process, consumers are typically faced with a foreign process against an entity that has participated in the process numerous times and has the benefit of familiarity with the process, familiarity with the arbitrator(s) or arbitration organization, and institutional memory and resources.

The basis for issues arising out of binding consumer arbitration concerns the adhesionary nature of the arbitration agreements where consumers can either agree to the arbitration agreement or forego the transaction altogether. The fact that the contract is adhesionary does not make it *per se* unconscionable or unenforceable. The Supreme Court in *AT&T Mobility v. Concepcion* mentioned that adhesionary contracts remain enforceable because of the proliferation of their use.<sup>22</sup> The problems with these types of adhesionary arbitration agreements arise when

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<sup>16</sup> *Id.* § 14-3904.

<sup>17</sup> *Id.* § 14-3905(b).

<sup>18</sup> *Id.* § 14-3905(c)(1).

<sup>19</sup> *See id.* § 14-3905(c)(2).

<sup>20</sup> *See id.* § 14-3905(a).

<sup>21</sup> *Id.*

<sup>22</sup> *See AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1750 (2011) (“[T]he times in which consumer contracts were anything other than adhesive are long past.”).

either the consumer does not know that they have entered into an agreement to arbitrate their disputes, or, if they are aware of the agreement to arbitrate, they either 1) do not expect to need it, 2) do not fully understand the ramifications, or 3) value the benefits of the product or service over the costs of arbitration. This lack of knowledge on the part of the consumer allows non-consumers to navigate a system with which they are familiar in a way that is potentially harmful and unfair to the consumer.

This issue was more specifically addressed in *Engalla v. Permanente Medical Group, Inc.* In his concurring opinion, Justice Kennard noted the potential for unfairness in binding consumer arbitration where contracts are adhesionary.<sup>23</sup> This unfairness arises when businesses and/or arbitrators in binding consumer arbitration become repeat players in the arbitration system causing “arbitrators [to] consciously or unconsciously bias their decisions in favor of an organization or industry that hires them regularly as an arbitrator.”<sup>24</sup> While the majority of the court in *Engalla* did not find that Permanente Medical Group’s method of selecting arbitrations made the contract to arbitrate unconscionable, they did find that Permanente’s practices were contrary to those of reputable neutral, third party arbitration organizations.<sup>25</sup> Subsequently, the California Supreme Court affirmed the need for neutral arbitrators in *Armendariz v. Foundation Health Psychcare Services, Inc.*<sup>26</sup>

To prevent the possibility of non-consumer parties taking advantage of the binding consumer arbitration process at the cost of the consumer, it is essential that consumer arbitration is made fair through the use of neutral and impartial arbitrators. Arbitration institutions have taken affirmative steps towards ensuring fairness and transparency in consumer arbitration by implementing protocols and other regulations requiring arbitrator neutrality.<sup>27</sup> In 1997, the National Consumer Disputes Advisory Committee promulgated recommendations for ensuring fairness in consumer arbitration entitled *Due Process Protocol for the Mediation and Arbitration of Consumer Disputes*, which were later adopted by the American Arbitration Association.<sup>28</sup> Principle three of the protocol addresses “Independent and Impartial Neutrals and; Independent Administration.” The principle entitles all parties to arbitration procedures administered by an independent ADR institution and overseen by an independent and impartial

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<sup>23</sup> See *Engalla v. Permanente Med. Grp., Inc.*, 938 P.2d 903, 926-927, 15 Cal. 4th 951, 987-988 (Cal. 1997) (Kennard, J., concurring) (“Finally, it is worth noting that new possibilities for unfairness arise as arbitration ventures beyond the world of merchant-to-merchant disputes in which it was conceived into the world of consumer transactions....”).

<sup>24</sup> *Id.* at 927.

<sup>25</sup> See *id.* at 925 (majority opinion).

<sup>26</sup> See *Armendariz v. Found. Health Psychcare Servs., Inc.*, 6 P.3d 669, 682 (Cal. 2000) (citing *Cole v. Burns Int’l Sec. Servs.*, 105 F.3d 1465, 1482 (D.C. Cir. 1997)) (A mandatory employment arbitration agreement (similar to the mandatory consumer arbitration contract here) is lawful if it “(1) provides for neutral arbitrators, (2) provides for more than minimal discovery, (3) requires a written award, (4) provides for all of the types of relief that would otherwise be available in court, and (5) does not require employees to pay either unreasonable costs or any arbitrators’ fees or expenses as a condition of access to the arbitration forum. Thus, an employee who is made to use arbitration as a condition of employment effectively may vindicate his or her statutory cause of action in the arbitral forum.”).

<sup>27</sup> See generally AMERICAN ARBITRATION ASSOCIATION, CONSUMER DUE PROCESS PROTOCOL (1998) (a series of principles aimed at ensuring a fair process in consumer dispute resolution).

<sup>28</sup> See *id.*, Introduction: Genesis of the Advisory Committee.

neutral.<sup>29</sup> Additionally, the principle also requires equality between consumer and non-consumer in selecting a neutral and that the chosen neutral discloses “any circumstance likely to affect impartiality...”<sup>30</sup>

Specific instances of conflicts of interest between arbitration organizations and non-consumer parties to consumer arbitration influenced the Maryland legislature’s decision to enact a law aimed at protecting the consumer.<sup>31</sup> For example, in 2009, the Minnesota Attorney General sued the National Arbitration Forum (Forum) alleging that the Forum generated revenue by convincing creditors to include mandatory arbitration clauses and appoint the Forum as the arbitrator.<sup>32</sup> The Attorney General also alleged that the Forum, the country’s largest provider of debt collection arbitration, financially affiliated itself with Mann Bracken, one of the country’s largest debt collectors.<sup>33</sup> The Mann Bracken law firm, based in Maryland before its collapse in 2010, employed a debt-collection process that was inherently biased against consumers.<sup>34</sup> Mann Bracken took cases to the Forum which was “connected to Mann Bracken through a common ownership structure,” where the arbitrators would almost always find in Mann Bracken’s favor.<sup>35</sup> These actions, it was alleged, hid from consumers the fraudulent nature of these associations and the bias of their arbitrators.<sup>36</sup> The issue was settled with an agreement that the Forum cease to arbitrate credit card debt and other consumer collection disputes.<sup>37</sup>

The Maryland legislature was also influenced by a July 2010 Federal Trade Commission Report titled *Repairing a Broken System: Protecting Consumers in Debt Collection Litigation and Arbitration*.<sup>38</sup> To prevent bias and unfairness in binding arbitration, the Federal Trade Commission (FTC) recommended measures to increase transparency and fairness in the arbitration process. The measures included drafting contracts so consumers are aware of their choice to arbitrate, eliminating bias in the arbitration process and conducting arbitration so that consumers will be more likely to participate.<sup>39</sup> The FTC recommended that these measures be adopted by Congress to create a nationwide system requiring that debt collection arbitration decisions be reported and made public. Congress has yet to follow through and pass such legislation, leaving the states to protect their citizens. In addition to Maryland, California and the District of Columbia have enacted arbitration disclosure laws similar to those recommended by the FTC.<sup>40</sup>

In an attempt to protect consumers who are not participating in arbitration with an arbitration organization such as AAA and JAMS who have consumer protection safeguards in

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<sup>29</sup> See *id.*, Principle 3.

<sup>30</sup> See *id.*, Principle 3.5. Circumstances that might affect impartiality include: 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, including past ADR experiences.

<sup>31</sup> See S.B. 309 *Fiscal and Policy Note: Consumer Protection - Transparency in Consumer Arbitrations Act*, Dept. Legis. Servs., 428th Leg., Reg. Sess. (Md. 2011).

<sup>32</sup> See Complaint at 2, *Minnesota v. Nat’l Arb. Forum*, No. 27CV0918550 (Minn. Dist. Ct. 2009) (settled out of court) [hereinafter “Complaint”].

<sup>33</sup> See *id.*

<sup>34</sup> See Jamie Smith Hopkins & Andrea K. Walker, *After the Fall: Collapse of Mann Bracken, One of the Largest-Debt Collector Law Firms, Lifts the Veil of an ‘Oppressive’ Industry*, BALTIMORE SUN, Mar. 21, 2010, at 1C.

<sup>35</sup> See *id.*

<sup>36</sup> See Complaint, *supra* note 32.

<sup>37</sup> See *Firm Agrees to End Role in Arbitrating Card Debt*, N.Y. TIMES, July 19, 2009, at B8.

<sup>38</sup> See S.B. 309 *Fiscal and Policy Note*, *supra* note 31.

<sup>39</sup> See S.B. 309 *Fiscal and Policy Note*, *supra* note 31.

<sup>40</sup> See S.B. 309 *Fiscal and Policy Note*, *supra* note 31.

place, the Maryland General Assembly enacted the Consumer Protection –Transparency in Consumer Arbitrations Act in an attempt to ensure fairness in binding consumer arbitration in all consumer arbitrations taking place in Maryland. As introduced by Delegate Samuel Rosenberg in the Maryland House of Delegates, House Bill 442 was aimed at equipping consumers with the tools to determine whether or not the arbitrator(s) hearing their case are neutral and to allow consumers to make an informed decision when choosing arbitrators.<sup>41</sup> Proponents of the bill commented that, unlike in court, there is no way to discover information about arbitrators and their decisions because that information is kept secret.<sup>42</sup> The Act solves this problem by requiring that information about arbitrators and their decisions are published, thereby uncovering information about arbitration organizations and increasing transparency.

Opponents of the bill argued that the bill could have negative effects on the consumers it is intended to protect. First, by requiring publication of arbitration decisions, the arbitration process becomes more like a typical courtroom legal proceeding, which is what the parties had contracted to avoid.<sup>43</sup> Second, publication of awards could invite burdensome and complicated discovery requests in subsequent disputes that could significantly increase the cost and time for arbitration, which is adverse to the central purpose of choosing arbitration.<sup>44</sup> Specific industries also had concerns with the need for confidentiality in highly regulated industries such as healthcare.<sup>45</sup>

Practically speaking, the Act will allow consumers who become involved in consumer arbitration to examine information about arbitrators and their past decisions before choosing the arbitrator that will hear their case. Theoretically, this requirement should keep the arbitrators honest because arbitrators and arbitration organizations who want to maintain business and revenue will come to decisions in a fair and transparent way to make themselves more appealing to the parties for whom they wish to act as arbitrators. Moreover, the requirement opens the doors of the arbitration process to the consumers who are unfamiliar with how it works. Not only will this allow consumers to choose arbitrators who have a history of fair decision-making, it will also give them insight into how the process works.

The requirements may also benefit the state of Maryland by revealing details of arbitration organizations' decisions, thereby allowing the state to take action against arbitration organizations that are biased in favor of non-consumers. As in the case brought against the Forum by the Attorney General of Minnesota, Maryland may be able to take action against arbitration organizations who habitually decide in favor of repeat players in an attempt to bolster their business. This could prevent issues of bias and unfairness from ever reaching the consumer. The required disclosures may also give the Maryland General Assembly greater insight into the consumer arbitration industry, allowing them to enact further regulations if necessary.

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<sup>41</sup> See *Hearing on H.B. 442 Before the H. Comm. on Economic Matters*, 428th Leg. (Md. 2011) (oral statement of Delegate Samuel Rosenberg, Sponsor of H.B. 442, at 1:16:30, available at <http://mgahouse.maryland.gov/House/Viewer/?peid=790f93a2b9174df299e187ad54255d751d> (noting that the purpose of the bill was to prevent someone who ruled against consumers in an overwhelming number of cases from being the required arbitrator in mandatory consumer arbitration).

<sup>42</sup> See *id.* (oral statement of Paul Bland at 1:19:00).

<sup>43</sup> See *id.* (oral statement of Robin Schavitz, Representative of Health Facilities Association of Maryland, at 1:36:40).

<sup>44</sup> See *id.* (oral statement of Susan O'Brien, Vice President with Health Facilities Association of Maryland at 1:34:00).

<sup>45</sup> See *id.* (oral statement of Robin Schavitz, Representative of Health Facilities Association of Maryland at 1:35:50) (noting the secretive nature of healthcare decisions and recommending that the provisions of the Act not apply to long term care facilities).

The Act is also designed to insulate the reporting arbitration organizations from being sued by parties whose information is revealed pursuant to the Act. By relieving the arbitration organization from liability for disclosing information about the parties to arbitration, the Act protects arbitration organizations from the financial and reputational effects that revealing private information about the parties for whom they arbitrate may create.<sup>46</sup> This provision may work to encourage arbitration organizations to disclose the required information rather than risk not reporting to protect their reputations and prevent lawsuits for breaching confidentiality. However, issues may arise in implementing this provision where consumer arbitration contracts include a confidentiality clause that prohibits disclosure of the same information required by the Act. Where the Act and the language of the contract contradict one another, the courts will likely need to determine which prevails. Inviting the courts into the arbitration process defeats the purpose of choosing to enter into arbitration as opposed to bringing the issue before the court. Once the courts get involved in determining whether the requirements of the Act overcome the provisions of the contract, issues regarding the parties' freedom of contract arise. Section 2 of the Federal Arbitration Act (FAA) declares that a written agreement to arbitrate in any contract involving interstate commerce or a maritime transaction "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."<sup>47</sup> Additionally, section 4 of the FAA allows a party to such an arbitration agreement to "petition any United States district court . . . for an order directing that such arbitration proceed in the manner provided for in such agreement."<sup>48</sup> If the courts respect the parties' freedom of contract as called for in the FAA, all non-consumers will likely include non-disclosure or confidentiality provisions in their adhesionary arbitration contracts to ensure that their information is not disclosed under the Act. This would, in effect, destroy any protections the Act was enacted to create.

The act may also negatively affect arbitration organizations' willingness to participate in consumer arbitration. If the organizations find that reporting requirements are too burdensome or may uncover unsavory details about the organization, they may choose not to participate in consumer arbitration or purposely fail to disclose the required information and risk the penalties to protect their reputations. Similarly, arbitration organizations may fear implicating themselves or revealing too much to the public to such an extent that they leave the business altogether, reducing competition among arbitration organizations and increasing the price of arbitration. In addition, the new reporting requirements may also increase the cost of arbitration due to the increased requirements placed on the organization. While these risks may be a concern to the arbitration organizations, the benefits that the consumers will experience in the form of increased transparency, fairness and accountability in binding consumer arbitration outweigh the potential risks.

#### **IV. CONCLUSION**

With binding and often adhesionary consumer arbitration provisions becoming the norm in consumer agreements, consumers are often forced to participate in an adjudicatory process with which they are unfamiliar. As a result, the businesses against whom they are forced to

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<sup>46</sup> See MD. CODE ANN., COM. LAW, § 14-3905(a).

<sup>47</sup> See Federal Arbitration Act, 9 U.S.C. § 2 (1925).

<sup>48</sup> *Id.* § 4.

arbitrate are often more advantageously situated because, as repeat players in consumer arbitration, they are in the position to compel arbitration organizations to find in their favor in exchange for continued business and revenue. Consumers are left to fend for themselves in a system that is essentially set up for them to fail. As a result, consumer arbitration has the potential to become highly unfair to the consumer who has no choice but to participate or forego the business transaction altogether.

The Consumer Protection –Transparency in Consumer Arbitrations Act was enacted to prevent these fraudulent and often secretive relationships between the non-consumers and the arbitration organizations by requiring that the organizations disclose and publish information about how they decide consumer arbitration cases. This allows consumers to make informed decisions regarding the appointment of the arbitrator to their cause and ensures neutrality and fairness in the consumer arbitration process. While the regulations place a greater burden on the arbitration organization by requiring them to publish information in the specified manner, the benefits to the consumer and the protection of the reputation of the arbitration process as a whole can be seen to outweigh the costs to the arbitration organizations.