

## 13 Tips for Consumer Arbitration Clauses That Work

### From the Experts

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The U.S. Supreme Court has made clear that state law prohibiting the enforcement of a class action waiver in an arbitration clause is preempted by the Federal Arbitration Act (FAA), even if the practical effect is that a claim will not be pursued (see *AT&T Mobility LLC v. Concepcion* and *American Express Co. v. Italian Colors Restaurant*). But that doesn't mean that plaintiffs' counsel and courts hostile to arbitration won't keep looking for ways to avoid enforcing an arbitration clause in a consumer agreement.

Here are some drafting tips to maximize the chance that your agreement will be enforced:

#### **1. The Consumer Actually Has to Agree**

An agreement to arbitrate can be made in any of the ways that any other contract can, and, under the FAA, courts must be evenhanded in applying those general rules. But courts are skeptical when an arbitration clause is buried in text, is not immediately available, is not visible until after the underlying transaction is complete or in some other way is a surprise. While the mere posting of terms on a website (known as a "browsewrap") is often enforceable, sometimes it's not.

Avoid a fight by (1) highlighting at the beginning that the contract



includes an arbitration clause foreclosing class actions and jury trials, and (2) requiring the customer to take an affirmative act (such as clicking "I agree") to signal agreement.

#### **2. Clarify What the Arbitrator Will Decide**

While a court must always decide whether an agreement to arbitrate was made in the first place, that agreement can also include a provision that, if expressed unmistakably, delegates to the arbitrator the power to determine the validity and scope of the arbitration clause itself. Several courts have held that this may be done solely by reference to the rules

of arbitration administrators that so provide, but the safer course is to do so explicitly in the agreement itself. For example, the arbitration shall cover "any and all claims or disputes arising out of or relating to the customer agreement, including the breach, application, validity, interpretation or scope thereof."

#### **3. Provide That the Arbitrator Shall Have No Power to Conduct Class, Mass, Private Attorney General or Consolidated Proceedings Without Your Client's Consent**

That way, if a rogue arbitrator attempts to allow a class action (or similar variant), his or her action

may be set aside in court. Adding a belt to the suspenders, provide that if the prohibition on class action were to be stricken, the entire arbitration clause is invalid.

#### **4. Select Your Arbitration Administrator Carefully**

Many companies chose the now-defunct National Arbitration Forum because of its low fees, but when the forum was sued by the Minnesota Attorney General for alleged improprieties and elected to exit the consumer arbitration business, many companies had to litigate whether a substitute could be appointed<sup>3/4</sup>not always successfully.

#### **5. Provide for a Substitute Arbitrator**

A mutually designated arbitration administrator may not be available when the dispute arises, so make sure your agreement authorizes the court to appoint a substitute. Alternatively, give the claimant a choice of administrators, such as the American Arbitration Association (AAA), JAMS or the International Institute for Conflict Prevention and Resolution (CPR).

#### **6. Pay Attention to Your Administrator's Rules**

Administrator rules are important. For example, the AAA and JAMS require consumer arbitration clauses to permit consumer claims in small claims court; JAMS makes the company responsible for any consumer's fee expense over \$250. Make sure that your clause doesn't contradict the procedures, policies or practices of the designated administrator, but do provide that, should there be a conflict, your agreement will control—with the understanding that you may then have to use a different administrator.

#### **7. Pay Attention to the Fees**

There is certainly an argument that arbitration inherently requires an arbitrator's fee that would be greater than fees charged by publicly funded courts, and that such expense is no basis to invalidate an arbitration clause. However, the Supreme Court has left open the possibility that excessive arbitral fees may do so. Review the fees of your intended administrator(s), and, if in doubt, provide that any fees greater than the filing fees of the customer's home trial court will be paid by the company.

#### **8. Specify Who Has the Right to Arbitrate**

Plaintiffs' counsel will often seek to make an end-run around an arbitration clause by suing peripheral players such as subcontractors or employees. To avoid this problem, explicitly provide that the agreement to arbitrate covers claims against those third parties, which should be specified by name or role.

#### **9. Name the Venue**

Most companies want to arbitrate in their own backyard. But some courts have held that, for smaller claims, requiring the consumer to arbitrate far from home is unconscionable. (JAMS requires a consumer hometown option.) So specify your preferred venue, but authorize the arbitrator to select another one if that one is unreasonably burdensome to the customer.

#### **10. Make the Obligation to Arbitrate Mutual**

California has held that the obligation to arbitrate must display a "modicum of bilaterality." There is a strong argument that, like other California principles hostile to arbitration, this rule is forbidden by the FAA, since the common law does not require that all contractual obligations apply equally

to all parties. But until that issue is settled, make any carve-outs apply by subject matter rather than party, although be aware that some courts reject even this approach.

#### **11. Specify That the FAA Applies**

Provide expressly that the FAA applies, but do not specify the application of any state's law—unless you further provide that any state law does not apply if it is preempted by the FAA.

#### **12. Consider a Severability Clause**

Authorize the court to sever any unenforceable provision of the arbitration clause (other than the prohibition of a class and like proceedings).

#### **13. Don't Overreach**

Too many consumer agreements have clauses that so strongly favor the company that no court or arbitrator will be willing to enforce them. Such clauses are actually counterproductive, because they increase the likelihood that a court will want to refuse to enforce the arbitration clause. Ask yourself whether an intelligent and reasonable consumer, knowing all material facts, would agree to what you've drafted. If not, rewrite.

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