Counterintuitive Approaches to Consumer and Labor Contract Arbitration Clauses in the United States and Japan

Michael L. WOLF*

I. Introduction

While the United States is often thought of as a very litigious nation, Japan maintains the opposite reputation.[1] As such, one might expect United States law to be particularly vigilant in upholding the rights of consumers and employees to access the courts to settle contractual disputes. Conversely, casual observers might assume that a nation relatively averse to litigation such as Japan would not object to legal restraints on access to the courts, and actively push potential litigants towards private arbitration. However, in each case, current law in the United States and Japan delivers the opposite results. The right to demand a fair and impartial trial in a court of law is limited for consumers or employees in the United States when companies routinely bury binding arbitration clauses in their consumer and employment agreements. Japanese law, however, explicitly gives consumers and employees the ultimate right to bring such disputes before a court of law.

Arbitration provisions as part of negotiated agreements between commercial entities can be of great value, in terms of convenience and cost savings. However, arbitration clauses included in boilerplate language in consumer and employment contracts that directly result in an individual's reduced access to a court are detrimental to justice in democratic nations. While the U.S. Supreme Court has been chipping away at the rights of consumers and employees to access the courts in recent years, Japan has taken the opposite approach, and strengthened the rights of such parties with decidedly weaker bargaining power. The United States should change its federal law to ensure that citizens retain the right to access public courts in civil disputes. To do so, this paper will look at the way federal law regarding arbitration provisions has evolved in the U.S., an example of New York's attempts to strengthen the rights of individuals to court access, and how Japan's 2003 arbitration law may serve as a model for federal statutory reform in the United States.

* Professor, Ritsumeikan University, Graduate School of Law.

1) It may be debatable as to whether the lower prevalence of lawsuits in Japan is attributable to any one or more of a combination of cultural, political, or economic reasons. Nevertheless, Japan has fewer litigation cases on a per capita basis than most common-law countries. *See* J. Mark Ramseyer & Minoru Nakazato, *The Rational Litigant: Settlement Amounts and Verdict Rates in Japan* in *Comparative Law: Law and the Process of Law in Japan* 362, 364 (Kenneth L. Port, Gerald Paul McAlinn & Salil Mehra, 3d ed., Carolina Academic Press 2015).

II. Arbitration Law in the United States

A. A Constitutional Right to a Trial, but Arbitration Agreements are Everywhere

The right to a jury trial is enshrined as one of the fundamental rights of American law. The United States Constitution provides that "[i]n Suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury, shall be otherwise re-examined in any court of the United States, than according to the rules of the common law."[2] Of course, not only can the right to a jury be waived,[3] but parties can agree to settle civil disputes privately, without the intervention of any court.[4]

Individuals are given great liberty under the rules of contract law. Post-dispute arbitration agreements may be formed when parties find themselves in a disagreement they cannot amicably resolve, and subsequently agree to settle the issue through binding arbitration. While relatively uncommon, this manner of arbitration is not controversial, as each party willingly and knowingly agrees to the arbitration to settle a known dispute between them. Conversely, commonly used pre-dispute arbitration agreements are often broadly-written additions to contracts that require unknown future disputes to be settled by arbitration.[5] While perhaps not problematic when executed between two parties of relatively equal bargaining power, the fairness of including contractual requirements to waive one's right to a trial is debatable when a party of disproportionate bargaining power allows for no deviation from its form contracts.

The use of standardized form contracts permits the imposition of terms shrouded in legalese within an agreement onto a signatory who may not understand, or even know of, such terms. Two major factors allow this to happen. The first is that the party offering the form usually has had sufficient time and legal resources to prepare it, while the other party is usually unfamiliar with the terms, and perhaps not even expected to read them. The second is that the parties are often not of equal bargaining power, or in the case of form agreements, no bargaining whatsoever can occur. A party in a stronger bargaining position can set the terms of an agreement before the parties even come to the table.[6]

The notion that individuals signing form contracts on paper or clicking "I agree" buttons online somehow creates true bargaining and consent does not reflect reality. Contracts were traditionally the formal codification of real agreements reached through the free bargaining and negotiation of two relatively equal parties. In the modern marketplace, mass-

2) U.S. Const. amend. VII.
3) Fed R. Civ. P. 38(d).
4) 9 U.S.C. §§ 1-16.
5) Stephen J. Ware & Ariana R. Levinson, *Principles of Arbitration Law* 3 (West Academic Publishing 2017).
6) E. Allen Farnsworth, *Contracts* 311-12 (2d ed., Little, Brown and Company 1990).

produced agreements prepared by the seller or service provider are presented to customers for acceptance without comment or question. While some terms, such as quantity and price, may be negotiable, the standard terms are presented as a "take it or leave it" proposition, with little other choice if the business transaction is to be completed.[7] Of course, one can argue that consumers are not forced into binding arbitration, because they are not required to buy any particular product, and can just walk away from a potential deal. However, when a consumer is purchasing a necessity, or all producers of certain items have virtually identical provisions in their contracts, the illusion of choice quickly evaporates.

It is easy to see why businesses generally prefer to avoid having contract disputes heard in courts before juries. A bulletin issued by the U.S. Department of Justice examined the results of state court contract cases from 2005, which showed that almost two-thirds of all cases were decided by bench trials, with the remainder heard by juries. Differences were stark, depending on the type of case. For example, in cases involving a "buyer plaintiff" (cases where the purchaser of goods or services sued for a return of money), just 44% went to juries. In employment discrimination cases, 91% were jury trials.[8] As one might expect, the percentage of plaintiff winners was generally higher with jury trials, but not in all cases. For example, buyer plaintiffs prevailed over 57% of the time with juries, but fared better with bench trials at a win rate of almost 69%. The expected disparity can be clearly seen, however, in employment discrimination cases, where plaintiffs prevailed in 65% of jury trials, but in only 36% of bench trials.[9] The median final award amounts for all contract jury trial winners was $75,000 and only $25,000 at bench trials. For prevailing buyer plaintiffs, the median was $38,000 from juries and $12,000 from the bench. The median award for employment discrimination case winners was $178,000 from jury trials and $99,000 from bench trials.[10]

Clearly, taking juries out of the equation reduces the size of awards. Even if bench trials do not necessarily increase their chances of prevailing overall compared with jury trials, companies generally prefer to keep the discovery process to a minimum, eliminate the potential costs of appeals, and be able to keep any less-than-favorable facts and determinations private. As a result, the insertion of form language requiring all disputes to be settled by mandatory arbitration has been on the rise by companies in their form contracts. Actions from banking to car rentals to television and internet service, and even health care can result in an average consumer being required to agree to arbitration provisions.[11]

---

7) *Id*. at 310-11.

8) Donald J. Farole, *Contract Bench and Jury Trials in State Courts*, Bureau of Justice Statistics Bulletin, NCJ 225634 1-2 (September 2009).

9) *Id*. at 4.

10) *Id*. at 5.

11) Jessica Silver-Greenberg, *Consumer Bureau Loses Fight to Allow More Class-Action Suits*, N.Y. Times (Oct. 24, 2017), https: //www. nytimes. com/2017/10/24/business/senate-vote-wall-street-regulation. html (accessed Feb. 2, 2019).

B. Federal Statutory Law

Federal law has enabled the corporate push for more and more aggressive arbitration provisions in consumer and employment agreements. In 1925, Congress tried to make voluntary arbitration agreements easier to enforce against a reluctant judiciary, with the enactment of the Federal Arbitration Act (the "FAA"). Section 2 of the FAA provides that written provisions in contracts involving commerce that require disputes to be settled by arbitration "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."[12] "Commerce" is defined broadly, and includes "commerce among the several States or with foreign nations".[13] Exceptions to the FAA are rather limited, and apply only to certain classes of workers,[14] rather than certain subject matters. One might imagine that this sort of language would apply primarily to contracts between sophisticated merchants, rather than employee or consumer agreements. While the intent of the statute was to push back at judicial skepticism of arbitral agreements and a reluctance of the courts to cede jurisdiction to private arbiters, the scope and effect of the law has expanded into almost every manner of commercial transaction in modern society with the help of successive Supreme Court rulings. The push towards strict enforcement of arbitration agreements was given much momentum in the 1967 case of *Prima Paint v. Flood & Conklin.*[15]

C. Federal Case Law

1. Consumer Contracts

Prima Paint involved a consulting agreement between the two companies, followed a few weeks later by a sale and purchase contract, where Prima Paint ("Prima") agreed to acquire the paint business of Flood & Conklin ("F&C"). F&C agreed that for six years it would provide expert advice related to the business to Prima. No provisions were made for the event of F&C's bankruptcy, but the agreement did include an arbitration clause requiring that any claim "arising out of or relating to" the agreement "shall be settled by arbitration in the City of New York" per American Arbitration Association rules.[16]

Prima failed to make the first payment due under the contract on time, but seventeen days later it paid the amount due into escrow. Prima contended that F&C fraudulently misrepresented its solvency and ability to perform its contractual obligations, as Prima learned that F&C intended to file for bankruptcy at the time the contracts were executed. F&C served notice of its intent to arbitrate, which was met with Prima's suit in federal court.

---

12) 9 U.S.C. § 2.

13) 9 U.S.C. § 1.

14) The FAA specifically exempts "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce." 9 U.S.C. § 1.

15) Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395 (1967).

16) *Id*. at 397-398.

Prima sought rescission of the agreement for fraudulent inducement.[17]

The key issue was whether a fraud in the inducement claim was a matter for determination by the court or arbitrators. The Supreme Court entertained the notion that if Prima's fraud in the inducement claim concerned the arbitration clause itself, the matter could proceed to trial. Since that was not the case, the Court held that "a federal court may consider only issues relating to the making and performance of the agreement to arbitrate."[18] As such, these two sophisticated businesses were required to have their dispute heard by arbitrators. Given the nature of the parties and the fact that this was a federal case involving a federal statute, the holding might not seem controversial. This was, however, the start of a slow and steady encroachment of the FAA into other, less obvious areas of control, such as an application to the state courts.

Until 1984, the Supreme Court had not applied the FAA to a state court case.[19] That changed when it affirmed in *Southland v. Keating*[20] that the FAA would override state law held contrary to the purposes of the FAA. Several franchisees of 7-Eleven stores sued Southland, which was the owner and franchisor of the stores, alleging fraud, oral misrepresentation, breach of contract, breach of fiduciary duty, and violation of certain California Franchise Investment Law disclosure requirements.[21] Subsequently, Keating filed a class action suit against Southland on behalf of hundreds of California franchisees. Southland sought arbitration of all claims, while the franchisees sought class certification.

The Supreme Court held that the FAA would govern in either state or federal court. In enacting the FAA, Congress contemplated judicial hostility toward arbitration, and the failure of state laws to require arbitration agreement enforcement. "To confine the scope of the Act to arbitrations sought to be enforced in federal courts would frustrate what we believe Congress intended to be a broad enactment..."[22] Thus, the Court upheld enforcement of the arbitration agreement itself, but remanded for further proceedings the question of whether the FAA precludes class action arbitration. The issue of whether the FAA would permit not just a waiver of the right to a trial, but waivers of class actions as well would be considered in 2011.

The Supreme Court would hold that the FAA permits arbitration agreements to preclude class action arbitration, notwithstanding any state law to the contrary, in *AT&T Mobility v. Concepcion.*[23] The Concepcions signed up for AT&T's cell phone service, which was advertised to include free phones. While the phones were provided at no cost, the Concep-

17) *Id*. at 398.
18) *Id*. at 404.
19) Stephen J. Ware & Ariana R. Levinson, *Principles of Arbitration Law* 17 (West Academic Publishing 2017).
20) Southland Corp. v. Keating, 465 U.S. 1 (1984).
21) *Id*. at 3-4.
22) *Id*. at 14.
23) AT&T Mobility LLC v. Concepcion, 563 U.S. 333 (2011).

cions were charged $30.22 for sales tax, calculated on the retail value of the phones. Their claim in California federal court, later merged with a class action, alleged in part false advertising for charging customers for the purportedly free phones. AT&T moved to compel arbitration.[24)]

AT&T's motion to compel arbitration was brought under the terms of the service agreement. The agreement included a provision requiring that all disputes be settled by arbitration, and that claims were required to be brought in the customer's individual capacity, rather than as a class member.[25)] The Concepcions claimed that the arbitration requirement was unconscionable under California law, due to the contract's prohibition of class actions. The lower courts agreed with the Concepcions, which relied on California Supreme Court precedent.[26)] In effect, California had prohibited contractual waivers of a consumer's right to a class action lawsuit.

The Supreme Court would not permit the conflict between California law and the broad language of the FAA to stand. "When state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA."[27)] The Court affirmed that "[r]equiring the availability of classwide arbitration interferes with fundamental attributes of arbitration and thus creates a scheme inconsistent with the FAA."[28)] The majority noted that class arbitration was not envisioned by Congress when it enacted the FAA, and "it is at the very least odd to think that an arbitrator would be entrusted with ensuring that third parties' due process rights are satisfied."[29)] The Court did not, however, mention that in 1925, Congress also did not envision that people would be required to sign away their rights to trials in order to get cell phone service, or that arbitration provisions would be included in voluminous online agreements that are seldom-read, but where a signature is obtained with a simple mouse click.

Additionally, the Court noted that a class arbitration "greatly increases the risks to defendants" as the "absence of multilayered review makes it more likely that errors will go uncorrected."[30)] Of course, the Court did not emphasize that in this particular case, the defendant at

24) *Id*. at 337.

25) *Id.* at 336 (internal citations omitted). The Court pointed out that the terms of the mandatory arbitration were described favorably by the District Court, including allowing for a simple online filing process, a short window for AT&T to make a settlement offer, AT&T shouldering the costs of a subsequent arbitration, assigning the arbitration location to the customer's billing area, permitting small claims court filings instead of arbitration, and denying AT&T requesting attorney fees. The Court did not state, however, whether its opinion would have changed in the event the terms were instead determined to be rather onerous for the consumer. The terms could have presumably been made radically different at any time, as AT&T's agreement allowed it to make unilateral changes thereto, and it did so to the arbitration provision "on several occasions". *Id*. at 336-337.

26) Discover Bank v. Superior Court, 113 P.3d 1100 (2005).

27) AT&T Mobility LLC v. Concepcion, 563, U.S. 333, 341 (2011).

28) *Id*. at 344.

29) *Id*. at 349-50.

30) *Id*. at 350.

risk was a multibillion-dollar corporation that made arbitration mandatory in the first place in its services agreement. The Court was also seemingly undisturbed that this very arbitration process, be it individual or class action, could have uncorrected errors made against the interests of one or more plaintiffs, even without class action status. It would seem that the opportunity for error by one arbiter acting alone is precisely why the Constitution established civil jury trials, under a court system to be established with multiple levels of appeal.

The expansion of the FAA's applicability continued in a pair of 2012 Supreme Court cases, holding in one case that when a federal law is silent as to whether claims under the law can be arbitrated, the FAA requires enforcement of the arbitration agreement.[31] The FAA is thus a default rule that requires specific exemption on a statute-by-statute basis. The other case determined that the FAA prevails over state court findings that arbitration clauses are unconscionable for specific types of claims (in this case, claims of personal injury or wrongful death against nursing homes) as violations of public policy.[32] After all, the intent of the FAA was to promote arbitration, not to make sure that potential wronged or injured parties had access to a judge and a jury.

Expediency and efficiency are hallmarks of arbitration proceedings. If the Supreme Court believed that one of the purposes of the FAA was to promote such efficiency, then it would stand to reason if a case demonstrated that individual arbitration costs were prohibitive, a class action waiver could be illogical. After all, if a class action could streamline multiple independent claims, it would stand to benefit all sides of the dispute. This, however, was not the case. In *American Express v. Italian Colors Restaurant*, a group of merchants who accepted American Express cards brought a class action suit against American Express. The merchants alleged that American Express violated federal antitrust laws, by using its monopoly power to charge higher fees than other credit cards. American Express moved to compel arbitration under the FAA, as the merchants' agreements included a clause requiring arbitration for all disputes, with a specific waiver of class action rights.[33] In overturning the lower federal court's ruling, the Supreme Court relied on its earlier decision in *AT&T Mobility*, reiterating that they "specifically rejected the argument that class arbitration was necessary to prosecute claims that might otherwise slip through the legal system."[34]

Essentially, an agreement to arbitrate prevails, even when basic justice would suffer on its face, as "the FAA's command to enforce arbitration agreements trumps any interest in ensuring the prosecution of low-value claims." Instead, the FAA favors "the absence of litigation when that is the consequence of a class-action waiver, since its 'principal purpose' is the enforcement of arbitration agreements according to their terms."[35] The Court

31) CompuCredit Corp. v. Greenwood, 565 U.S. 95, 104 (2012).
32) Marmet Health Care Ctr., Inc. v. Brown, 565 U.S. 530, 534 (2012).
33) Am. Express Co. v. Italian Colors Rest., 570 U.S. 228, 231 (2013).
34) *Id*. at 238 (internal quotations and citations omitted).
35) *Id*. at 238 n. 5 (internal quotations and citations omitted).

seems to support the notion that if the FAA is used to deny wronged groups of any practical means of relief, it is immaterial so long as the FAA's purpose remains undisturbed.[36]

The Court's support of limiting virtually any exception to the breadth of the FAA would continue in *DIRECTV v. Imburgia*.[37] Imburgia sued DIRECTV in California state court, alleging damages for early termination fees that violated California state law. DIRECTV's services agreement with customers required all claims to be settled only by binding arbitration, with an explicit class action waiver. What made this waiver uncertain, even in light of previous Supreme Court decisions on the matter, was language that provided if "the law of your state" invalidates the class arbitration waiver, the entire arbitration was unenforceable.[38] Imburgia argued that California state law, as per *Discover Bank v. Superior Court*, 113 P.3d 1100 (2005), would have rendered the waiver of class arbitration rights unenforceable. In rejecting this reasoning, the Court explained that California's state law regarding a prohibition of arbitration class waivers was invalidated by the 2011 *AT&T Mobility* decision. Even though the "state law" in force at the time of the DIRECTV service agreement's execution was the *Discover Bank* rule, it was not the current law of the state because the federal Supreme Court's *AT&T Mobility* decision trumped then-existing state law. This line of reasoning is logical, given that one cannot apply overturned case law any more than relying on revoked statutes. However, the application to this case would appear to put the nail in the coffin of any state law attempting to carve out certain exceptions to the broad authority of the FAA, if it "does not give due regard to the federal policy favoring arbitration."[39]

2. Employment Contracts

Not even employment agreements would be exempt from the FAA's reach in helping those with superior bargaining power strip individuals of their rights to court access. A Circuit City employee bound by an arbitration clause in an employment agreement filed an employment discrimination lawsuit in state court, arguing that the FAA's exclusion from coverage of "any other class of workers engaged in foreign or interstate commerce"[40] meant that most employment contracts were beyond the FAA's reach.[41] The Supreme Court

36) A scathing dissent noted that "if the arbitration clause is enforceable, Amex has insulated itself from antitrust liability—even if it has in fact violated the law. The monopolist gets to use its monopoly power to insist on a contract effectively depriving its victims of all legal recourse. And here is the nutshell version of today's opinion, admirably flaunted rather than camouflaged: Too darn bad." *Id*. at 240 (Kagan, J., dissenting). The dissent did not see the FAA as intended to provide parties with superior bargaining positions carte blanche in its contracts. "Put otherwise: What the FAA prefers to litigation is arbitration, not *de facto* immunity." *Id*. at 244 (Kagan, J., dissenting).

37) DIRECTV, Inc. v. Imburgia, 136 S. Ct. 463 (2015).

38) *Id*. at 466 (citations omitted).

39) *Id*. at 471 (internal quotations and citations omitted).

40) 9 U.S.C. § 1.

41) Circuit City Stores v. Adams, 532 U.S. 105, 109-10 (2001).

did not agree, ultimately holding that the FAA exemption is limited to employment contracts for transportation workers only.[42] The Court also emphasized that they "have been clear in rejecting the supposition that the advantages of the arbitration process somehow disappear when transferred to the employment context."[43] The ability of employees to escape the reach of arbitration clauses affecting the workplace would only worsen from there.

The rights of employees were further restricted in 2018, when the Supreme Court consolidated three cases with similar details in *Epic Systems v. Lewis*. Employees signed employment agreements which stipulated that any disagreements with the employers would be subject to arbitration.[44] Employees argued that they should be able to raise claims in class actions, notwithstanding agreements with their employers to the contrary, as rights protected under the National Labor Relations Act ("NLRA") conflicted with the FAA. The Court did not mince any words in rejecting the employees' claims, holding that while the NLRA protects employee rights to collective bargaining and union organization, it does not regulate how legal disputes are settled once they go from the workplace to a court or arbitrator: "This Court has never read a right to class actions into the NLRA… Far from conflicting, the Arbitration Act and the NLRA have long enjoyed separate spheres of influence and neither permits this Court to declare the parties' agreements unlawful."[45]

Employees further tried to argue that the saving clause of the FAA, as applied to the NLRA, would carve out an exception for labor contracts, as arbitration agreements are binding under the FAA, "save upon such grounds as exist at law or in equity for the revocation of any contract."[46] However, the Court noted that "the saving clause does not save defenses that target arbitration either by name or by more subtle methods, such as by interfering with fundamental attributes of arbitration."[47] The saving clause would not apply, because the employees did not claim the arbitration agreements were obtained by unconscionable action such as fraud or duress. By challenging just the requirement of individualized arbitrations to the exclusion of class actions, "the employees' argument seeks to interfere with one of arbitration's fundamental attributes."[48] The Court allows that "unconscionable" extraction of arbitration agreements might be treated differently, but does not see the use of grossly unequal bargaining positions to extract the waiver of a constitutional right as such. The effect of this ruling is that the ability of employees to actually enforce their rights is eroded, to the benefit of employers.[49]

---

42) *Id*. at 119.
43) *Id*. at 123 (reference omitted).
44) Epic Sys. Corp. v. Lewis, 138 S. Ct. 1612 (2018).
45) *Id*. at 1619.
46) 9 U.S.C. § 2.
47) Epic Sys. Corp. v. Lewis, 138 S. Ct. 1612, 1622 (2018) (internal quotations and citations omitted).
48) *Id*. at 1622.
49) The dissent believed that class action waivers were not just simple policy decisions, but rather at the core of employee rights under the NLRA. "Employees' rights to band together to meet their employers'↗

The majority opinion points out that any exceptions to the FAA can and will be specifically carved out by the legislative branch. "Congress has… shown that it knows how to override the Arbitration Act when it wishes… The fact that we have nothing like that here is further evidence that [the NLRA] does nothing to address the question of class and collective actions."[50] The Court is thus alerting Congress that unless the FAA itself is amended or revoked, any and all future legislation must clearly and explicitly exempt itself from the FAA if there is any intent whatsoever to preserve the rights of court access to those affected by such legislation. The rights of individuals to a trial by jury are thus possibly subordinated to the whims of form contract drafters by default, and require proactive exemption in every piece of new legislation possibly affecting these rights.

Given the mass-produced nature of modern consumer contracts and the inflexibility of employment agreements for most, this is not the most reasonable or just approach to mandatory arbitration clauses. If arbitration is the wonderful panacea that truly benefits all parties in a dispute, then the parties can and should willingly agree to it at the time a dispute arises, as a result of a mutual and equal understanding. While the federal government has yet to accept this notion, New York took a step in the right direction by passing its own laws to protect consumers and some employees, even though the scope of the protections is limited by the Supreme Court's decisions.

D. State Law Subordinated – the New York Example

As discussed above, the FAA has been interpreted to supersede a great deal of law that attempts to protect consumers or employees at the state level. Nevertheless, the states do have some authority to exempt their consumers from binding arbitration. While the FAA broadly regulates commerce, the term "commerce" as defined in Section 1 of the statute means "commerce among the several States or with foreign nations".[51] The states would thus, at a minimum, maintain authority to regulate matters not involving interstate commerce.

New York's General Business Law § 399-c[52] prohibits mandatory arbitration clauses in contracts for consumer goods. In the event one is included, the clause "shall be null and void."[53] A "consumer" is defined simply as a natural person residing in the state, and

↘ superior strength would be worth precious little if employers could condition employment on workers signing away those rights." *Id*. at 1641 (Ginsburg, J., dissenting).

50) Epic Sys. Corp. v. Lewis, 138 S. Ct. 1612, 1626 (2018). Some laws do indeed contain explicit exemption to the FAA, such as 15 U. S. C. § 1226(a)(2) which provides: "Notwithstanding any other provision of law, whenever a motor vehicle franchise contract provides for the use of arbitration to resolve a controversy arising out of or relating to such contract, arbitration may be used to settle such controversy only if after such controversy arises all parties to such controversy consent in writing to use arbitration to settle such controversy." Apparently, Congress does know how to override the default rules of the FAA in response to certain constituencies and their lobbyists, at least.

51) 9 U.S.C. § 1.

52) N.Y. Gen. Bus. Law § 399-c (Consol. 1984).

53) N.Y. Gen. Bus. Law § 399-c(2)(b) (Consol. 1984).

"consumer goods" as "goods, wares, paid merchandise or services purchased or paid for by a consumer, the intended use or benefit of which is intended for the personal, family or household purposes of such consumer".[54] While somewhat limited in its scope, the law is a major step in the right direction for consumer protection. With the application of this statute, it appeared that New York consumers could no longer be forced to give up their rights to trials and juries by simply purchasing goods and services as part of their daily lives. However, the good intentions of this law had to contend with the Supreme Court's expanding interpretation of the FAA, which came at the expense of state laws such as this.

The balance between the state law and the FAA was put to the test in *Schiffer v. Slomin's*.[55] Plaintiffs initiated a small claims action against Slomin's for $5,000 in damages relating to a home alarm and security system. Plaintiffs claimed fraud, breach of contract, and breach of warranty, alleging that the Slomin's salesperson changed the original contract to charge another plaintiff's credit card for services. Slomin's claimed that the FAA preempted the application of General Business Law § 399-c to the arbitration clause in the contract for the security system and home monitoring. Preemption in New York, however, required a review of the threshold consideration "that the contract or transaction 'involve' interstate commerce".[56] Slomin's claimed that it purchases, sells and installs security systems in many states, has multistate offices, advertises out of state, does business online, and monitors security systems in multiple states through phone lines, radio and internet. The court nevertheless held that this contract did not "affect interstate commerce" and was not subject to the FAA.

The court interpreted the implications of interstate commerce from the viewpoint of the consumer, rather than the company drafting the arbitration provision. It held that a consumer contract "which will be performed solely at the residence of the homeowner/consumer… [for] goods which will be installed and utilized in a security system for his or her personal and property protection at the residence, is not a transaction within the flow of interstate commerce." The contract did not give notice that the security monitoring would be provided by Slomin's out of state. The court distinguished the facts of *AT&T Mobility*, which involved interstate commerce due to the underlying interstate phone services and use of satellites. As to Schiffer and Slomin's, there was an "insufficient nexus with interstate commerce to establish Federal Arbitration Act coverage over the contract" and General Business Law § 399-c governed the Slomin's contract.[57]

This apparent victory for the consumer under applicable state law was only temporary, however, as it was modified on appeal. The appellate court did not take the same narrow

54) N.Y. Gen. Bus. Law § 399-c(1)(a) and (b) (Consol. 1984).

55) Schiffer v. Slomin's, Inc., 970 N.Y.S.2d 856 (NY Nassau Dist. Ct., 2013), *aff'd in part and modified in part*, Schiffer v. Slomin's, Inc., 11 N.Y.S.3d 799, 802 (N.Y. App. Term, 2d Dept. 2015).

56) *Id*. at 861 (internal citations omitted).

57) *Id*. at 864 (internal citations omitted).

view as to what constitutes "interstate commerce". Instead, much more weight was given to the nature of the company itself, rather than to the specific services it provided to a particular customer. The court held that because Slomin's showed it was a multi-state company, and its services and components are provided from several states, Slomin's "thereby established a sufficient nexus with interstate commerce to require preemption of the FAA over contradictory New York law" and that an order compelling arbitration should have been granted.[58] Thus, even in states with robust consumer protection laws, the judiciary is hamstrung and unable to stop the FAA from allowing companies to usurp the individual's right to a trial by jury.[59] While disappointing for supporters of the right to judicial access, the appellate court's decision is in line with the likely result the Supreme Court would have reached had this case been appealed to that level.

Despite the persistent threat of the FAA looming overhead, New York also enacted a law to protect employees by prohibiting mandatory arbitration for sexual harassment claims arising on or after July 11, 2018. While the reach of the statute is limited by federal law, the law prohibits any contractual provisions requiring "that the parties submit to mandatory arbitration to resolve any allegation or claim of an unlawful discriminatory practice of sexual harassment."[60] Perhaps overly cognizant of the FAA, the drafters provided that the new law would prevail, "[e]xcept where inconsistent with federal law".[61] How this works out in practice remains to be seen.

New York has provided models of consumer and employment protection in its domestic arbitration law that perhaps could be used as a model to amend the FAA. While this may not be forthcoming in the near future from Congress, a regulatory body did try to improve the position of certain consumers by protecting their access to class action suits. It was a very short-lived proposition.

E. A Federal Prohibition of Class Action Waivers in Consumer Financial Contracts and a Quick Reversal

Despite the reluctance of the Supreme Court to protect the rights of consumer access to

58) Schiffer v. Slomin's, Inc., 11 N.Y.S.3d 799, 802 (N.Y. App. Term, 2d Dept. 2015).

59) The frustration with waivers of access to courts and juries is not limited to the litigants trying to overturn the provisions in form contracts. Judge Rakoff lamented that "while appellate courts still pay lip service to the 'precious right' of trial by jury, and sometimes add that it is a right that cannot readily be waived, in actuality federal district courts are now obliged to enforce what everyone recognizes is a totally coerced waiver of both the right to a jury and the right of access to the courts - provided only that the consumer is notified in some passing way that in purchasing the product or service she is thereby 'agreeing' to the accompanying voluminous set of 'terms and conditions.'" Meyer v. Kalanick, 291 F. Supp. 3d 526, 529 (S.D.N.Y. 2018) (internal citations omitted). However, the Supreme Court continues to hold that the FAA preempts state laws that single out and disfavorably treat arbitration agreements. *See* Kindred Nursing Ctrs. Ltd. P'ship v. Clark, 137 S. Ct. 1421 (2017).

60) NY CLS CPLR § 7515(a)(2).

61) NY CLS CPLR § 7515(b)(i).

the courts, the legislative and executive branches tried to push back. In the aftermath of the 2008 financial crisis, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act, passed by Congress in 2010.[62] One of the benefits, from the viewpoint of consumer rights advocates, was the creation of the Consumer Financial Protection Bureau (the "CFPB"), with a goal of "watching out for American consumers in the market for consumer financial products and services."[63]

In 2015, the CFPB issued an Arbitration Study Report to Congress.[64] It noted the increasing prevalence of arbitration clauses in consumer financial services contracts. For example, from 2013-2014, 53% of outstanding credit card loans, 44.4% of checking accounts, and 99.9% of mobile phone contracts were subject to arbitration clauses.[65] Class action waivers were also found to go hand and hand along with almost all arbitration clauses.[66]

In an attempt to push back against the increasing use of forced waivers of consumer class actions, the CFPB issued its Arbitration Agreements rule in July, 2017.[67] Regulations would have prohibited class action waivers in arbitration agreements included in bank and credit card agreements.[68] It was set to go into effect for agreements entered into after March 19, 2018. Providers of applicable consumer financial products or services would have had to, with limited exceptions, include in any pre-dispute arbitration agreement the following provision: "We agree that neither we nor anyone else will rely on this agreement to stop you from being part of a class action case in court. You may file a class action in court or you may be a member of a class action filed by someone else."[69] While this rule was much more narrow in scope than the New York consumer arbitration law, it would have at least, to a limited extent, restored court access to financial institution customers otherwise bound under the terms of form services agreements containing arbitration clauses.

The good intentions of the CFPB were undone before they even had a chance to go into effect. Utilizing the Congressional Review Act,[70] on November 1, 2017, President Trump signed a Congressional joint resolution disapproving of the Arbitration Agreements

62) Pub. L. No. 111-203 (July 21, 2010).

63) https://www.consumerfinance.gov/about-us/the-bureau/creatingthebureau/ (accessed Feb. 3, 2019).

64) Issued pursuant to Dodd–Frank Wall Street Reform and Consumer Protection Act § 1028(a). The Report is available online at https://files.consumerfinance.gov/f/201503_cfpb_arbitration-study-report-to-congress-2015.pdf (accessed Feb. 3, 2019).

65) *Id.* at § 2.3, Table 1. The prevalence of arbitration clauses in credit card agreements is much lower than it would have been, but for private settlements of an antitrust lawsuit in 2009 and 2010 by credit card issuers, whereby they agreed to remove arbitration clauses from their consumer credit card contracts for a set period of time. If those issuers were included in the study, the number of outstanding credit card loans subject to arbitration would be about 94%. *Id.* at § 1.4.1.

66) *Id.* at § 1.4.1.

67) 82 Fed. Reg. 33210 (July 19, 2017).

68) *See* 82 Fed. Reg. 33428 (July 19, 2017).

69) 12 CFR 1040.4(a)(2)(i) (repealed).

70) 5 U.S.C. §§ 801-808.

rule, rendering it to have no force or effect. On November 22, 2017, the CFPB officially removed the Arbitration Agreements rule.[71] After all the time and effort spent studying the effects of and problems with binding arbitration clauses, Congress decided to bury this modest regulation before it could even be tried and tested.

For a more equitable set of rules, perhaps the United States should look to a nation with low litigation rates, but that protects the rights of its citizens to access the courts. Even as a nation without any rights to civil juries, Japan may provide a model arbitration law for the United States to follow.

III. Arbitration Law in Japan

A. Reluctant Litigants

Whether calculated by total numbers or on a per capita basis, fewer lawsuits are filed in Japan than in the United States. The number of civil cases brought to trial, when compared with the U.S., is demonstrative of Japan's relative reluctance to litigate. In 2016, 1,471,000 new civil and administrative cases were brought to Japanese courts.[72] In the United States, 15,300,000 civil cases were filed in state courts,[73] with an additional 291,851 cases filed in U.S. federal district courts.[74]

Perhaps because of this lower likelihood of litigation (or arguably, as a result thereof), Japan has far fewer lawyers than the United States. As of January 1, 2019, the Japanese Bar Association reported 41,143 lawyers[75] for a country with a total population of approximately 126,451,398. The American Bar Association reported 1,338,678 active lawyers in the United States in 2018[76] for a total population of approximately 326,625,791 people.[77] While the reasons for the discrepancy are debatable, the end result is that Japan not only has fewer licensed attorneys on a per capita basis, but a far lower incidence of lawsuits. One might think that this aversion to litigation might make the country even more recep-

71) 82 Fed. Reg. 55500 (November 22, 2017).

72) Statistics Bureau, Ministry of Internal Affairs and Communications, *Japan Statistical Yearbook 2019*, Table 28-9, http://www.stat.go.jp/english/data/nenkan/68nenkan/1431-28.html (accessed Feb. 3, 2019).

73) This figure includes the District of Columbia, Puerto Rico, and Guam. Court Statistics Project, *Number of Incoming Cases, by Case Category and Tier, 2016*, http://www.courtstatistics.org/~/media/Microsites/Files/CSP/National-Overview-2016/EWSC-2016-Overview-Page-5-Table.ashx (accessed Feb. 3, 2019).

74) United States Courts, Statistics and Reports, *U.S. District Courts - Judicial Business 2016*, https://www.uscourts.gov/statistics-reports/us-district-courts-judicial-business-2016 (accessed Feb. 3, 2019).

75) Japan Federation of Bar Associations, *Bengoshi-kai betsu kaiin-sū* [Membership by Bar Association] (Jan. 1, 2019), https://www.nichibenren.or.jp/library/ja/jfba_info/membership/data/190101.pdf (accessed Feb. 3, 2019).

76) American Bar Association, *ABA National Lawyer Population Survey* (2018), https://www.americanbar.org/content/dam/aba/administrative/market_research/Total_National_Lawyer_Population_1878-2018.pdf (accessed Feb. 3, 2019).

77) Population estimates are as of July 2017. Central Intelligence Agency, *The World Factbook*, https://www.cia.gov/library/publications/the-world-factbook/rankorder/2119rank.html (accessed Feb. 3, 2019).

tive than the United States to the notion of binding arbitration clauses in commercial and employment contracts. However, Japan's arbitration law has taken a decidedly different turn.

B. Statutory Law

Unlike the United States, the Japanese Constitution makes no provision for the right to trial by jury in civil matters. It does, however, provide that "[n]o person shall be denied the right of access to the courts."[78] This did not, however, prohibit parties from voluntarily agreeing to arbitrate their private claims.

Japan revised its old arbitration statute from its 1890 civil code and replaced it with the Arbitration Act (the "Act") enacted in 2003, and effective as of March 1, 2004,[79] using the UNCITRAL Model Law as a base for the statute, though making a number of changes unique to its system.[80] The main body of the Act defines arbitration procedures and the scope of the law, including procedures for commencing and terminating arbitrations, and the enforcement of arbitration awards. Contracting parties may agree to arbitration instead of litigation. While recognizing the freedom to contract, Japanese law also recognizes that sometimes when parties with unequal bargaining power form a contract, the law may provide certain protections to the weaker party, such as in consumer contracts.[81] Protections for consumers and employees are incorporated into the Act's Supplementary Provisions, which is a significant divergence from the FAA.

Drafters of the Act received public feedback that consumers and employees should not be denied the right to be heard in court. While the feedback was unexpected, the Act incorporated those concerns in Articles 3 and 4 of the Act's Supplementary Provisions.[82] Proponents of limitations on arbitration argued that consumers and employees generally possess less information and are in weaker bargaining positions than their counterparts, and that many consumers and employees are not even aware of what arbitration agreements mean when executing these kinds of contracts.[83] The implementation of these concerns

78) Nihonkoku Kenpō [Kenpō] [Constitution], art. 32 (Japan), unofficial English translation, https://japan.kantei.go.jp/constitution_and_government_of_japan/constitution_e.html (accessed Feb. 4, 2019).

79) Chūsaihō [Arbitration Act], Law No. 138 of 2003, unofficial English translation by the Arbitration Law Follow-up Research Group, https://japan.kantei.go.jp/policy/sihou/arbitrationlaw.pdf (accessed Feb. 3, 2019).

80) Masaaki Kondo, Takeshi Goto, Kotatsu Uchibori, Hiroshi Maeda & Tomomi Kataoka, *Arbitration Law of Japan* (i) (Shojihomu Co., Ltd. 2004).

81) Carl F. Goodman, *The Rule of Law in Japan: A Comparative Analysis* 311 (2d ed., Wolters Kluwer 2008).

82) Tatsuya Nakamura, *Salient Features of the New Japanese Arbitration Law Based Upon the UNCITRAL Model Law on International Commercial Arbitration* in Japan Commercial Arbitration Association Newsletter No. 17, p.5 (April 2004).

83) Hiroyuki Tezuka & Yutaro Kawabata, *Japan* in *Arbitration World* 531 (Karyl Nairn & Patrick Heneghan, eds., 4th ed., Thomson Reuters (Professional) UK Limited 2012).

gave consumers and employees very specific rights under the Act that are in stark contrast to the absence of such rights under the FAA.

Article 3 of the Act's Supplementary Provisions explicitly creates a separate set of rules for consumer arbitration agreements between consumers and businesses.[84] As to any contract between an individual (except where the individual is a party to a contract as a business or for a business purpose) and a corporation or association, or an individual who becomes a party to a contract as a business or for business purposes, the "consumer may cancel an arbitration agreement."[85]

A business wishing to initiate an arbitration proceeding based on its consumer contract must, once an arbitral tribunal is set up, request an oral hearing. Notice of the hearing must be given to the consumer. Using as simple language as possible, the arbitral tribunal will provide not only the place and time of the hearing, but explain that: an arbitral award has the same binding effect as a trial; lawsuits filed where an arbitration agreement is in effect will be dismissed; the consumer has the right to cancel the consumer arbitration agreement; and the consumer's failure to appear at the hearing is deemed to be a cancellation of the consumer arbitration agreement.[86]

Should the consumer appear at the oral hearing as scheduled, the tribunal must again explain that: an arbitral award is binding; lawsuits filed after arbitration is agreed will be dismissed; and the consumer has the right to cancel the arbitration agreement. The consumer may agree to the arbitration agreement if he or she desires, or reject it.[87]

As relatively few consumers in Japan are familiar with arbitration, or what the consequences of agreeing to it would mean, the Act is intended to protect court access after a consumer dispute arises. Even if consumers knew full and well what rights they were giving up by agreeing to an arbitration provision, it is unreasonable to expect that consumers could negotiate changes to the arbitration provisions of a contract, given the unequal bargaining power of the parties. Instead, the Act was drafted to allow consent to the arbitration process, but did not outright prohibit trial waivers. The consumer now has the right to make an informed choice.[88]

The notice and hearing requirements are meant to reduce the burdens of consumers who have no intention of arbitrating disagreements. Rather, the burden is placed on the businesses,[89] which likely have superior bargaining power and added the arbitration provisi-

84) Definitions of consumers and businesses are provided in the Consumer Contract Act. *See* shōhisha keiyakuhō [Consumer Contract Act], Act No. 61 of 2000, art. 2, unofficial English translation, http://www.japaneselawtranslation.go.jp/law/detail/?vm=04&re=02&id=3231&lvm=01 (accessed Feb. 3, 2019).

85) Chūsaihō [Arbitration Act], Law No. 138 of 2003, Supplementary Provision art. 3 para. 2.

86) *Id*. at Supplementary Provision art. 3 paras. 3, 5, and 7.

87) *Id*. at Supplementary Provision art. 3 para. 6.

88) Kondo et al., *supra* n. 80, at 299-300.

89) *Id.* at 302.

ons in the first place. An arbitral award made in violation of the requirements of the Act would result in either setting aside the award, or a refusal to recognize and enforce it.[90]

The Act has another major exception to arbitration provisions, this time as applied to employment agreements. It states simply that arbitration provisions affecting individual labor-related disputes[91] that may arise in the future are null and void,[92] but excludes collective bargaining agreements from these provisions. Like consumers in regard to consumer contracts, few workers in Japan understand the meaning or impact of arbitration clauses in employment agreements, and may not appreciate the serious consequences of waiving their rights to a trial.[93]

The Act includes no provisions that guarantee the right to a jury trial, because Japan's justice system does not utilize jury trials for civil matters. The Act as it stands removes the ability of parties with unequal bargaining positions in consumer and employment situations to deny individuals the right to access the court system. In that regard, it should serve as a model for the United States to follow and improve upon.

IV. Conclusion

The approaches of the United States of America and Japan regarding binding arbitration clauses in consumer and employment contracts seem counterintuitive. On the one hand, the United States is known as a country with an abundance of lawyers and lawsuits, yet has established a statute and growing body of case law that makes it more and more difficult for average consumers and employees to access the courts. On the other hand, Japan is known as a country that shies away from litigation, yet has enacted a law to protect access to its courts for those who may be the most susceptible to having that access taken away, due to unequal contractual bargaining positions.

The United States Constitution enshrined trial by jury as a fundamental right of American law. The Supreme Court's interpretation of the Federal Arbitration Act has slowly but surely ensured that this right can be casually waived, as long as carefully drafted language is tucked away in the administrative provisions of a consumer contract or employment agreement. Waivers of this constitutional right will be upheld even when the signatory is

---

90) *Id.* at 301.

91) Such disputes are defined as "individual disputes between individual workers and business operators with respect to working conditions and other matters concerning labor relationships (including disputes between individual job applicants and business operators with respect to matters concerning the recruitment and employment of workers" in Kobetsu rōdō kankei funsō no kaiketsu no sokushin ni kansuru hōritsu [Act on Promoting the Resolution of Individual Labor-Related Disputes], Act No. 112 of 2001, art. 1, unofficial English translation, http://www.japaneselawtranslation.go.jp/law/detail/?ft=5&re=02&dn=1&gn=99&sy=2001&ht=A&no=112&x=0&y=0&ia=03&ky=&page=1

92) Chūsaihō [Arbitration Act], Law No. 138 of 2003, Supplementary Provision art. 4.

93) Kondo et al., *supra* n. 80, at 305-306.

not expected to read the provision, or even understand the effects thereof. In most situations, consumers or employees are given no opportunity to bargain over such waivers, as they are presented as "take it or leave it" propositions.

Most arbitration agreements in the U.S. are quite the bargain for businesses. They get consumers and employees to waive two constitutional rights for the price of one clause: the rights to juries *and* trials. As a bonus, individuals will likely also be required to relinquish rights to join a class action, either in court or in arbitration. The proposition that mandatory arbitration and class action waivers in consumer contracts are somehow "equal" because they apply to each party is ultimately a weak reach. If a cat requires a mouse to "mutually agree" to refrain from bothering a watchdog with their squabbles, has the cat given up anything when it fears the watchdog, and would never have approached it in the first place? The supposedly mutual waivers would have a disproportionate effect in almost every case.

The New York legislative approach towards arbitration provisions provides a good starting point for amending the FAA. It would at least restore court access to consumers and a limited class of employees. But the Japanese model would be much stronger overall, so long as it was tailored for the U.S. to also specifically preserve the right to not just trials, but jury trials. If modern litigation in the United States is considered too expensive and time-consuming for most litigants, perhaps justice would be better served by focusing on efforts to reform and streamline the rules of civil procedure, rather than outsourcing the judiciary to private hands under little to no supervision.

It is ironic that the U.S. Supreme Court has created so much precedent about arbitration provisions at the expense of consumers and employees, while at the same time these very holdings will increase the number of binding arbitral decisions that will generally not be subject to review and have no precedential value for future jurists. Hopefully, the examples of New York and Japanese law can inspire the United States federal government to give form contract waivers of consumer and employee rights to trials a big wave goodbye.