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**David Seligman Testimony**

**City of Chicago City Council**

**Committee on Finance**

**June 15, 2016**

Chairman Burke and Members of the Committee on Finance:

Thank you for this opportunity to speak to you about forced arbitration on behalf of the National Consumer Law Center and its low-income clients. I'm a contributing author at the National Consumer Law Center, where I specialize in forced arbitration. I drafted NCLC's "Model State Consumer and Employee Justice Enforcement Act," model legislation for state and local governments to mitigate the harms of forced arbitration. I'm also a staff attorney at Towards Justice in Denver, CO, where I litigate cases on behalf of low-wage workers.

I appreciate your willingness to take on this issue—an issue that fundamentally undermines the fairness and transparency of our marketplace but that has gone unscrutinized for far too long. The federal government and a number of states are now examining forced arbitration. But as far as I am aware, you are the first municipality to examine the harms of forced arbitration not only for consumers and workers but also for the public fisc.

Before I talk to you about how the proliferation of forced arbitration clauses harms Chicago, allow me to take a few moments to describe the issue. "Forced arbitration" clauses are fine-print terms included in take-it-or-leave-it contracts that force the individual to waive her right to sue the company in court. These clauses are prevalent in a number of types of contracts including, among others, cellphone contracts, credit agreements, auto loans, for-profit college enrollment forms, nursing home contracts, and employment contracts in non-union workplaces.

These clauses purport to provide employees and consumers with a private forum to resolve their claims against the company instead of the public, judicial forum that is generally available for such claims. The shift from public to private dispute resolution has many consequences for our marketplace and our civil justice system, but most importantly for our purposes here, arbitration is secret. Many arbitration clauses include confidentiality terms, but even when they do not, arbitration (unlike public judicial proceedings) is not subject to the First Amendment's presumption of openness that normally applies to civil proceedings. Unlike disputes in court, arbitration proceedings do not have a public docket. The claims, discovery, and even the arbitrator's decision are all secret.

Advocates have fought back against arbitration, however, not only because of its secrecy but also because of the harms it causes consumers and employees. For most individuals, arbitration doesn't mean an alternative dispute resolution forum, it means no dispute resolution forum at all. Most forced arbitration clauses require the employee or consumer to pursue her claims individually, without the benefit of class or collective action procedures that many consumers and employees rely on to assert their rights because individual damages are too small or suing individually too intimidating or costly. Moreover, some clauses require the consumer or employee to pay exorbitant arbitration fees or even to arbitrate in a far-off forum. And, finally, some businesses are now adept at manipulating the procedures of the arbitration provider to prolong the duration of the arbitration. When an employee or consumer is prevented from bringing claims in arbitration, she never has an opportunity to seek redress, and her claims are never aired openly for the public.

But even when consumers and employees do pursue their claims in arbitration, they often find that the deck is stacked against them. Arbitrators are often subject to "repeat player" bias in favor of the business and against the employee or consumer—the business, after all, is the entity appearing in front of the arbitrator most frequently and is the one paying the arbitrator's fees. What is more, under federal law, the right to appeal an arbitrator's decision is extremely limited. A consumer or employee cannot obtain relief on an appeal from an arbitrator's decision even when the arbitrator is clearly wrong on the facts or the law.

Now, why are we here before the Committee on Finance? As you know probably too well at this point, Chicago spends massive amounts of money on private service providers and contractors. You do your best to make sure that state negotiations with these entities are as transparent and public as possible. The public, after all, has a right to know how the state spends its money. But why don't the entities that you do business with have the same obligation to conduct themselves publicly and transparently? By forcing their consumers and employees into arbitration, these businesses obscure important information that you and your constituents have a right to know.

As one example of the harms forced arbitration causes to the broader marketplace because of its secrecy, consider a recent scandal involving sexual harassment problems at the clothing manufacturer and retail store American Apparel. For decades, American Apparel's chief executive officer had been the subject of sexual harassment claims and accusations on the part of employees, but he remained in control of the company until 2014. An article in The New York Times noted that forced arbitration clauses in employment contracts had helped to insulate his practices from public scrutiny and thus injured shareholders and customers. "If American Apparel hadn't been able to use arbitration and confidentiality clauses to keep investors and the public in the dark over those accusations, [the CEO] would most likely have been shown the exit some years earlier." As The Times further explained, "A board can use [arbitration clauses] to hide a pattern of bad conduct. Either employees will be deterred from bringing claims or, if they do, the claims will be buried in the silence of arbitration." In the same way that American Apparel's shareholders were harmed by the secrecy of arbitration, Chicago would be harmed by a large government contractor's use of arbitration as a way to resolve disputes whose pattern and frequency could say something important about the company and the quality of its goods and services.

As another example, consider the number of contracts that you have with telecommunications providers. Most of those providers insert arbitration agreements into their contracts with consumers. This means that if those consumers have disputes with the company about the quality of their service or excessive, unfair, and illegal fees, those disputes are much less likely to come to the public's attention. You could be buying a poor service or paying more than you'd otherwise need to pay, but you wouldn't have access to disputes filed by consumers who might have similar complaints.

There is something that you can do about this problem. Under federal law, you're not allowed to regulate arbitration agreements. But you aren't helpless either. As a market participant, you can rely on your proprietary powers to stop doing business with companies that use or enforce forced arbitration agreements in form contracts with consumers or employees.

This step would be important and bold. But it wouldn't be unprecedented. In 2014, President Obama issued an Executive Order that prevents large federal contractors from compelling arbitration of civil rights disputes brought by their employees. The President recognized that opaque dispute resolution not only harms those employees but harms the federal government in its procurement capacity as well. You should follow his lead.

Your action here is important notwithstanding some impressive movement at the federal level with regard to the harms of forced arbitration. Most notably, the Consumer Financial Protection Bureau has just proposed a rule that would prohibit many consumer finance companies from enforcing class action waivers in their agreements with consumers. Additionally, a panel of the Seventh Circuit Court of Appeals, which sits in Chicago, recently decided—in a split with the Fifth Circuit out of Houston—that class waivers in employment contracts violate employees' right to engage in concerted conduct under federal labor law. These are important steps, but they don't resolve the problem: the judicial decision out of the Seventh Circuit will continue to be tested, and the CFPB action will cover only consumer finance agreements and only on a prospective basis. Neither the CFPB rule nor the Seventh Circuit's approach, if adopted more broadly, would do anything about ***individual*** arbitration, just the use of arbitration clauses to prevent consumers and employees from bringing class actions. In sum, these developments are a call to action. They recognize the harmful effects of forced arbitration, but they do not address all of those effects now, and they do not resolve these issues for large market players like Chicago.

I'm happy to take your questions on my testimony, federal preemption, or any recent developments regarding arbitration law.