



**University of  
Leicester**

# **Consumer Confidence in Online Cross-Border Business-to-Consumer Arbitration**

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by

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# **Abstract**

## **Consumer Confidence in Online Cross-Border Business-to-Consumer Arbitration**

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The present thesis argues that the current legal framework regulating online cross-border business-to-consumer arbitration reduces the consumer confidence in online arbitration. The analysis focuses on the law applying to online cross-border business-to-consumer arbitration in England and on the U.S. Federal level, as these are identified as main emerging legal systems in this field.

The main points in support of the above argument are as follows: First, the current rules do not oblige the business to notify the consumer about the existence of the arbitration clause in the B2C e-commerce contract. Second, the current choice of law rules applicable to online cross-border B2C arbitration do not ensure the consumer that he will enjoy the protection awarded to him under the law of his country of domicile. Third, the current jurisdiction rules applicable to online B2C arbitration do not give the consumer the right to litigate disputes related to online arbitration agreements and processes in the Courts of his country of domicile. Fourth, the current rules governing the online arbitral procedures do not promote the consumer perception of fairness.

Finally, this thesis concludes that consumer confidence is essential for the success of this form of electronic dispute resolution, and that it can be increased by the adoption of an international convention which resolves all the above mentioned problems.

*I dedicate this thesis to my parents*

*Ahmad and Fatima Alqudah*

*to*

*my wife Dua*

*and to*

*my sons Faris and Ahmad*

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# Chapter 1

## Introduction

Consumers can easily use the Internet to conclude transactions with businesses located in other countries without any need to travel and this is what is called cross-border Business-to-Consumer e-commerce (hereinafter B2C e-commerce).<sup>1</sup> In this thesis, the term consumer means “any natural person who is acting for purposes which are outside his trade, business or profession”.<sup>2</sup> The term business means that a company or an establishment that is acting for commercial or professional purposes. Cross-border means that the business and the consumer are located in different countries. The Internet is a medium of communication that consists of massive worldwide collection of computer networks, cooperating with each other to exchange data using a common software standard.<sup>3</sup> The common software standard is the Internet Protocol which is usually abbreviated as IP. However, the development of B2C e-commerce sector is threatened by the lack of consumer’s confidence in e-commerce.<sup>4</sup> The issue of redress in the case of B2C e-commerce disputes is one of the main factors that reduce the consumer confidence in e-

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<sup>1</sup>Karen Stewart and Joseph Matthews, “Online Arbitration of Cross-Border, Business to Consumer Disputes”, 56 U. Miami L. Rev. 1111, 1113.

<sup>2</sup>This definition for the term consumer is derived from the EU law on consumer protection. For example, see Article 2, Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts, OJL 095 , 21/04/1993 p. 0029 - 0034

<sup>3</sup>Charles Oppenheim, *The Legal and Regulatory Environment for Electronic Information*, (4<sup>th</sup> edn, Infonortics, England, 2001), p.5, 6, 7.

<sup>4</sup>A European Initiative in Electronic Commerce: Communication of 15 April 1997 to the European Parliament, the Council, the Economic and Social Committee of the Regions COM(1997) 157 Final, para, 35.

commerce.<sup>5</sup> For consumers to have confidence in transacting with businesses located in other countries via the Internet, consumers should be certain that in the case of B2C e-commerce dispute, they will have the access to an efficient, cost-effective and quick method of dispute resolution. Online arbitration is a traditional arbitration proceeding but conducted over the Internet.<sup>6</sup> In other words, online arbitration is a procedure in which a dispute is submitted, by agreement of the parties, to one or more arbitrators who will conduct the arbitral proceedings via the Internet and make a binding decision on the dispute.

Online arbitration is efficient because it leads to a final and binding settlement. It is cost-effective and quick because it is conducted over the Internet.<sup>7</sup> This means that online arbitration should contribute in raising the consumer confidence in e-commerce. However, currently online arbitration does not have an effective role in raising the consumer confidence in B2C e-commerce. This is deduced from the fact that it has been rarely used to resolve B2C e-commerce disputes.<sup>8</sup> The main reason behind the failure of cross-border online B2C arbitration services is the lack of consumer's confidence in the online arbitral process.<sup>9</sup> Cross-border online B2C

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<sup>5</sup>Consumers International, Office for Developed and Transition Economies, "Disputes in Cyberspace 2001: Update of Online Dispute Resolution for Consumers in Cross-Border Disputes", p. 6, available at:

<[http://www.consumersinternational.org/document\\_store/Doc517.pdf](http://www.consumersinternational.org/document_store/Doc517.pdf)>, accessed on 12/07/2005. There are several reasons that may reduce the consumer's confidence in e-commerce. For example, the issue of security, this belongs to the question whether the online payment system is secure enough. Another factor is that the consumer cannot examine the goods before he decides to buy.

<sup>6</sup>D.V. Zhivotova, "International Commercial Arbitration and Online Dispute Resolution", in L.N. Shestakov, William E. Butler (eds & trs), *Theory of International Law*, (2<sup>nd</sup> edn, Wildy, Simmonds & Hill Publishing, London, 2003), p.482.

<sup>7</sup>This is explained in section 2.1 of chapter two.

<sup>8</sup>Ethan Katsh and Janet Rifkin, *Online Dispute Resolution: Resolving Conflicts in Cyberspace*, (1<sup>st</sup> edn, Jossey-Bass, San Francisco, 2001), p.56. This issue is explained in section 1.2 of chapter two.

<sup>9</sup> This issue is explained in-depth in section 1.2 of chapter two.



arbitration means that the dispute submitted to arbitration via the Internet has resulted from B2C e-commerce transactions in which the business and the consumer located in different countries. This thesis argues that the current legal framework of online cross-border B2C arbitration reduces the consumer confidence in online arbitration. Therefore, an international convention that imposes a new model of online cross-border B2C arbitration should be adopted in order to raise consumer confidence in the online arbitral process.

## **1. Purpose of the Study**

The main objective of this study is to show that the current legal framework of online cross-border B2C arbitration reduces the consumer confidence in the online arbitral process. Raising the consumer confidence in online cross-border B2C arbitration requires adopting an international convention that imposes a new model of online B2C arbitration. Moreover, special attention is directed to the following substantive issues:

- a) To show that the current rules that regulate online B2C arbitration clauses does not oblige the business to introduce the arbitration clause into the B2C e-commerce contract in a transparent way. In other words, the current rules do not oblige the business to notify the consumer about the existence of the arbitration clause in the B2C e-commerce contract.
- b) To show that the choice of law rules applicable to online B2C arbitration do not ensure the consumer that he will enjoy the protection awarded to him under the law of his country of domicile.

- c) To show that the jurisdiction rules applicable to online B2C arbitration do not give the consumer the right to litigate disputes related to online arbitration agreements and processes in the Courts of his country of domicile.
- d) To show that the current rules governing the online arbitral procedures do not promote the consumer's perception of fairness.

## **2. Scope and Methodology of the Study**

### **2.1 Scope of the Study**

This study mainly focuses on the English law and the U.S. federal law. Several reasons have encouraged the present author to particularly focus on the English law and U.S. federal Law. First, both are English speaking countries. This has helped to obtain sufficient material to write the thesis. Second, e-commerce is a fast-growing sector in both countries. Third, both countries have deep histories of reliance on arbitration to resolve commercial disputes. Fourth, in both countries few dispute resolution centres have started offering online arbitration services.

Under the English Law, reference will be made to the English Arbitration Act 1996, The Unfair Terms in Consumer Contracts Regulations 1999, and the English choice of law and jurisdiction rules. Under the U.S. federal law, reference will be made to the Federal Arbitration Act 1925, the Uniform Commercial Code, the Restatement (Second) of Contracts (1981), and the Restatement Second of Conflict of Laws (1971). In matters related to the New York Convention 1958, reference will also be made to Courts decision from other jurisdictions. This is in order to effectively

clarify the issues subject to discussion. The present author will also refer to the arbitral practice. This shall include institutional arbitration rules and many arbitral awards.

## 2.2 Methodology of the Study

While this study focuses on English Law and U.S Federal Law, it is, however, not a comparative study in the traditional sense of the term.<sup>10</sup> These two jurisdictions are chosen for the reasons outlined above, to illustrate main aspects of online B2C arbitration. But this thesis does not intention to focus on the hermeneutics of comparative law,<sup>11</sup> or the depth of legal culture,<sup>12</sup> to conduct a comparison between the two. The focus of the study remains one of cross-border online B2C arbitration. Two aspects of research methodology are considered:

- a) Critical analysis of the theoretical aspect: this involves analyzing the theoretical side of the topic. This will be done by analyzing written literature that is taken from law books, journal articles, and various reports.<sup>13</sup>

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<sup>10</sup>H. C. Gutteridge, *Comparative Law: An Introduction to the Comparative Method of Legal Study & Research*, (2<sup>nd</sup> edn, CUP, London, 1949 reprinted 1971), p.72. Peter de Cruz, *Comparative Law in A Changing World*, (2<sup>nd</sup> edn, Cavendish Publishing Limited, London, 1999), p.1-30.

<sup>11</sup>For comparative law and hermeneutics, see Geoffrey Samuel, "Taking Method Seriously", Parts I and II in *Journal of Comparative Law* 2007(2) and 2008(1).

<sup>12</sup>For the significance of law and legal culture in comparative law, see amongst many others Pierre Legrand, "How to Compare Now", (1996) 16 *Legal Studies*. 232-242.

<sup>13</sup>J. Myron Jacobstein and Roy Mersky, *Fundamentals of Legal Research*, (5<sup>th</sup> edn, The Foundation Press Inc, New York, 1977), p.307-368.

- b) Critical analysis of the legal aspect: this involves the critical analysis of legislations, case law, and arbitral awards.<sup>14</sup>

### **3. Organization of the Study**

This study includes 8 chapters. Following this introduction, chapter 2 clarifies why the consumer's confidence in online arbitration should be raised. It also explains that consumers do not have confidence in online cross-border B2C arbitration because it is mainly governed by the laws that regulate arbitration between commercial parties. Therefore, raising the consumer's confidence in online arbitration requires adopting an international convention that imposes a new model of online B2C arbitration. The third chapter will explain that business is not under an obligation to specifically notify the consumer that the online B2C contract includes an arbitration clause. Therefore, a rule that obliges the business to notify and explain the arbitration clause to the consumer should be in place. The fourth chapter explains that adopting a new rule stipulating the knowing and intelligent standard of consent to an online arbitration clause will help to avoid two types of uncertainties. These two uncertainties may arise when trying to enforce an online B2C arbitration clause under the New York Convention 1958.

The fifth chapter explains that a choice of law clause imposed by the business deprives the consumer of the protection that is awarded to him under the law of his country of domicile. Therefore, in order to instil the consumer confidence in online

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<sup>14</sup>Marie Fox and Christine Bell, *Learning Legal Skills*, (3<sup>rd</sup> edn, Blackstone Press Limited, London, 1999), p.258-288.

arbitration, a rule that stipulates the application of the law of the consumer's country of domicile to the subject matter of the dispute should be in place.

The sixth chapter explains that a choice of an arbitral seat that is foreign to the consumer means that the consumer cannot refer disputes over the online arbitral process to the Courts of his country of domicile. Therefore, a rule that stipulates the consumer's country of domicile as the arbitral seat should be in place.

The seventh chapter explains that the current rules that regulate the online arbitral procedures do not promote the consumer perception of fairness. Therefore, a new model of online B2C arbitration that aims to raise the consumer's confidence in online arbitration should promote consumer's perception of fairness of the online arbitral procedures.

The study is ended by a conclusion and recommendation for policy makers and this is presented in chapter 8.

## **Chapter 2**

# **Analysis of Consumer Confidence in Online Cross-Border B2C Arbitration**

This chapter introduces an analysis of consumer confidence in online cross-border business-to-consumer arbitration (hereinafter online B2C arbitration). The first part of this chapter clarifies why the consumer's confidence in online arbitration should be raised. The first section of this part explains that online arbitration is cost-effective and quick. The second section explains that online arbitration has not been successful as an e-commerce activity. The third section explains that raising the consumer's confidence in online arbitration will increase the growth of B2C e-commerce. The second part of this chapter explains that consumers do not have confidence in online B2C arbitration because it is governed by the laws that regulate arbitration between commercial parties. The third part of this chapter explains that raising the consumer's confidence in online arbitration requires adopting an international convention that imposes a new model of online B2C arbitration. The first section explains that there should be transparency in the method of introducing the arbitration clause into the online B2C contract. The second section explains that the consumer should enjoy the protection awarded to him under the law of his domicile. The third section explains that the consumer should have the right to litigate matters related to the online arbitration agreements and processes in the Courts of his country of domicile. The fourth section explains that perceived fairness of the online arbitral procedures is necessary for raising consumer confidence in

online arbitration. The fifth section explains that this new model of online B2C arbitration should be regulated by an international convention.

## **1. Reasons for Raising the Consumer's Confidence in Online Arbitration**

Three factors justify the need for raising consumer confidence in online B2C arbitration. These factors are, first, online arbitration is cost-effective and quick. Second, online arbitration has not been successful as an e-commerce activity. Third, raising the consumer's confidence in online arbitration will increase the growth of B2C e-commerce.

### **1.1 Online Arbitration is Cost-Effective and Quick**

Online arbitration is cost-effective and quick. Online arbitration is an Online Dispute Resolution (hereinafter ODR) method. Hörnle defined ODR as:

“... information technology and telecommunication via the Internet - (together referred to as ‘online technology’) applied to alternative dispute resolution. The term alternative dispute resolution (ADR) in this context refers to dispute resolution other than litigation in the courts, including other adjudicative techniques such as arbitration. Or in other words, ODR applies IT and distance communication to the traditional ADR processes such as conciliation, mediation and arbitration (including the various mutants thereof).”<sup>1</sup>

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<sup>1</sup>Julia Hörnle, “Online Dispute Resolution-the Emperor’s New Clothes”, (2003) 17(1) Int’l. Rev. L. Computers & Tech. 27, 28, (hereinafter New Clothes). Tyler and Raines explained that the term ODR is used interchangeably with terms “on-line ADR,” “eADR,” “iADR,” “virtual ADR,”. Melissa Conley Tyler and Susan S. Raines, “The Human Face of On-line Dispute Resolution”, (2006) 23(3) C. R. Q. 333, 334.

Online arbitration is a traditional arbitration proceeding but conducted over the Internet.<sup>2</sup> In other words, online arbitration<sup>3</sup> is a procedure in which a dispute is submitted, by agreement of the parties, to one or more arbitrators who will conduct the arbitral proceedings via the Internet and make a binding decision on the dispute.<sup>4</sup> The quickness and the cost-effectiveness of online arbitration are attributable to two factors which are the parties' autonomy and the use of the Internet to conduct the arbitral proceedings. The parties' autonomy allows setting deadlines for the arbitral proceedings and submission of evidence and pleadings.<sup>5</sup> This does help the parties to accelerate the online arbitral process.

The use of the Internet in conducting arbitral proceedings is cost-effective and quick.

As Rothchild puts it "the cost of making a communication over the Internet and the

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<sup>2</sup>D.V. Zhivotova, "International Commercial Arbitration and Online Dispute Resolution", in L.N. Shestakov, William E. Butler (eds & trs), *Theory of International Law*, (2<sup>nd</sup> edn, Wildy, Simmonds & Hill Publishing, London, 2003), p.482.

<sup>3</sup>The other ODR methods are online negotiation and online mediation. ODR also includes the new online methods of dispute resolution that are derived from these methods of dispute resolution. For example, blind bidding is a type of online negotiation that "is designed to facilitate settlement of disputes for an amount of money." The system allows both parties to place bids without knowing about the value of each other bids. When the bids match, the system will notify the parties. Credit Card Chargeback is another famous form of ODR in which a third party resolves the dispute but it is neither online arbitration nor online mediation. Upon the consumer complaint of non-delivery, the credit card company will not charge the payment unless the business proves that the product or the services were delivered to the consumer. M. Scott Donahey, "Current Developments in Online Dispute Resolution", (1999) 16(4) J.Int'l Arb. 115, 116. Victoria C. Crawford, "A Proposal to Use Alternative Dispute Resolution as a Foundation to Build an Independent Global Cyberlaw Jurisdiction Using Business to Consumer Transactions as a Model", (2001-2002) 25 Hastings Int'l & Comp. L. Rev. 383, 393. Mohamed Wahab, "The Global Information Society and Online Dispute Resolution: A New Dawn for Dispute Resolution", (2004) 21(2) J. Int'l Arb. 143, 149. (hereinafter global information)

<sup>4</sup>Jean-Raymond Fayat, Frederik Nevejan and Frederik Nordquist, "Consumer Confidence in E-commerce", 16th BILETA Annual Conference, April 9th - 10th, 2001, p.9. available at: <<http://www.bileta.ac.uk/01papers/fayat.html>> accessed on 13/06/2005. Lucille M. Ponte and Thomas D. Cavenagh, *Cyberjustice: Online Dispute Resolution (ODR) for E-Commerce*, (1st edn, Prentice Hall, 2004), p.84, (hereinafter cyberjustice). Alessandro del Ninno, "Alternative Dispute Resolution: Online Arbitration and Mediation in Italy and the European Union in Comparison with the United States", (2002) W.I.L.R. 22, 23.

<sup>5</sup>Frank A. Cona, "Application of Online System in Alternate Dispute Resolution", (1997) 45 Buff. L. Rev. 975, 981.



delivery time of a communication are independent of the geographic separation of the parties to the communication.”<sup>6</sup> Tyler and Bretherton stated that:

“The low cost of data transfer through electronic mechanisms potentially offers a mechanism for resolution of small value disputes, such as consumer disputes. Being able to electronically file and draft documents can lead to significant time savings, especially in arbitration.”<sup>7</sup>

Parties can participate in the online arbitral process without having to travel.<sup>8</sup> This means that there will not be travel costs such as flights and hotel bookings. What also makes online arbitration quick and cost-effective is the ease of obtaining experienced arbitrators. Caplin explained that:

“[P]arties are not restricted to the ADR services available in their locality. They can choose the ODR service best suited to their particular dispute from numerous options found in the Internet. This may be particularly important for parties in remote areas where skilled dispute resolution providers may not be available.”<sup>9</sup>

Parties will not be confined to the arbitrators who are located in the country of the consumer or the country of the business. This gives the parties’ a wider option to quickly choose the best arbitrator, at the best price, regardless of their location. The wide availability of arbitrators also allows the parties to choose an arbitrator who

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<sup>6</sup>John A. Rothchild, “Protecting the Digital Consumer: The Limits of Cyberspace Utopianism”, (1999) 74(3) Ind. L. J. 893, 912.

<sup>7</sup>Melissa Conley Tyler and Di Bretherton, “Research into Alternative Online Dispute Resolution”, Exploration Report prepared for the Department of Justice, Victoria, Australia, March 21, 2003, <<http://www.justice.vic.gov.au>> accessed on 12/06/2004.

<sup>8</sup>Margin C. Karamen, “ADR on the Internet”, (1996) 11 Ohio St. J. on Disp. Resol. 537, 548. Paul D. Carrington, “Virtual Arbitration”, (1999-2000) 15 Ohio St. J. on Disp. Resol. 669. Paul Motion, “Article 17 ECD: Encouragement of Alternative Dispute Resolution On-line Dispute Resolution: A View from Scotland”, in Lilian Edwards (eds), *The New Legal Framework for E-Commerce in Europe*, (Hart Publishing, Oxford, 2005), p.141. Alan Gaitenby, “The Fourth Party Rises: Evolving Environments of Online Dispute Resolution”, (2006-2007) 38 U. Tol. L. Rev. 371, 387.

<sup>9</sup>Lesley Caplin, “Resolving Consumer Disputes Online: A Review of Consumer ODR”, (2003) 10(8) Com. L. P. 207, 211.

can speak both the language of the business and the language of the consumer. This also reduces the cost of the arbitral process and makes it quicker because the parties do not have to retain a translator. In the case that the parties could not find an arbitrator who can naturally overcome any language barrier, the parties can rely on translation software. In fact, translation software is quick and cost-effective.

Another factor that makes online arbitration quick and cost-effective is that conducting the arbitral proceedings online allows for the keeping of electronic records. Katsh and Rifkin explained that:

“[O]ne of the significant benefits of ODR is that a record is kept of all exchanges. This has consequences... for building feedback and intelligence into the ODR process. It also has benefits in recreating who said what, what was said, and under what circumstances.”<sup>10</sup>

Records from online arbitral proceedings can be kept in different forms. It can take the form of electronic documents, audio records and video records. Keeping electronic records reduces the cost of the arbitral process because the parties and the arbitrator do not have to use paper documents and they do not need a secretary to arrange the documents. Electronic records also allow the parties and the arbitrator to quickly look up information, for example, what evidence has been introduced and exactly what parties have said. However, Caplin raised the concern that disparity in computer skills and access to the Internet can create a power imbalance between the business and the consumer. She explained that:

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<sup>10</sup>Ethan Katsh and Janet Rifkin, *Online Dispute Resolution: Resolving Conflicts in Cyberspace*, (1<sup>st</sup> edn, Jossey-Bass, San Francisco, 2001), p.81. (Hereinafter online dispute).

“[W]hile online communication eliminates some hierarchies, it creates others. Individuals who are comfortable using computers and online resources (often the commercial party) necessarily have an advantage over those who are less so (often the consumer). In relation to real-time dispute resolution processes, conducted in chat-rooms for example, research has shown that persons with good typing skills and a connection with high data flow can easily dominate meetings. In addition, persons with a physical or visual handicap would also be at a disadvantage.”<sup>11</sup>

In the context of offline arbitration, the attractiveness of the appearance, the racial group and the gender may form imbalances that may advantage one party over the other.<sup>12</sup> Using the Internet to conduct the arbitral proceedings does eradicate this type of imbalance. However, there is no doubt that the Internet itself creates novel imbalances between the business and the consumer. Commercial parties are likely to be more skilful in using the computer and the Internet than the consumers. This does favour the business over the consumer. This is because commercial parties are likely to deliver information and evidence in a better way than the consumers. However, this disparity in computer skills between the business and the consumer can be overcome by using software that simplifies participating in the online arbitral proceedings. In other words, the consumer should be given clear and simple instructions on how to file the case and how to continue with the rest of the procedures of the online arbitral process.<sup>13</sup>

However, despite the quickness and the cost-effectiveness of online arbitration it has not been successful as an e-commerce activity. In the next section the author will clarify the factors that may have led to the failure of online B2C arbitration.

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<sup>11</sup> Caplin, note 9 supra, p.211.

<sup>12</sup> Joseph Llewellyn Gibbons, Robin M. Kennedy and Jon Michael Gibbs, “Cyber-Mediation: Computer-Mediated Communications Medium Massaging the Message”, (2002) 32 N.M. L. Rev. 27, 44.

<sup>13</sup> Caplin, note 9 supra, p.210.

## 1.2 Online Arbitration has not been Successful as an E-commerce Activity

Online B2C arbitration has not been successful as an e-commerce activity. In other words, online B2C arbitration projects have rarely been used to resolve B2C e-commerce disputes.<sup>14</sup> Schultz explained that, “so far, the vast majority of ODR in consumer matters are mediation and negotiation and the small portion, of online arbitration, are non-binding.”<sup>15</sup> Hörnle explained that “online consumer arbitration, as opposed to online mediation (and other methods of ADR) is not very common.” Katsh and Rifkin explained that the Virtual Magistrate online arbitration project was “unsuccessful” in attracting cases.<sup>16</sup> They explained that Online Ombuds Office which is an online mediation project was more successful in attracting cases than the Virtual Magistrate because the mediation process is voluntary.

Katsh’s and Rifkin’s statement means that consumers do not desire online arbitration in order to not lose their right to litigate disputes with the online businesses, in a court of law. This interpretation comes from the following analysis. Binding and final award means that the parties cannot resort to a court of law to resolve the same

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<sup>14</sup> It should be noted that information about online cross-border B2C arbitration is not always published. One reason for this could be the confidentiality of arbitration proceedings. However, another reason for not publishing may be that online arbitration providers do not want to reveal that they are not receiving cases as this information may impact their reputation and credibility.

<sup>15</sup> Gabrielle Kaufmann-Kohler and Thomas Schultz, *Online Dispute Resolution: Challenges for Contemporary Justice*, (1<sup>st</sup> edn, Kluwer Law International, The Hague, 2004), p.169. (hereinafter Online Dispute)

<sup>16</sup> Katsh and Rifkin, (online dispute) note 10 supra, p.56. The Virtual Magistrate was a joint project of the Cyberspace Law Institute, the American Arbitration Association, and the National Centre for Automated Information Research and the Villanova Centre for Information Law and Policy. The Virtual Magistrate still exists as an arbitration project at the Chicago-Kent College of Law. For more information visit < <http://www.vmag.org/>>, accessed on 16/11/2004.

dispute that is resolved by the arbitral award.<sup>17</sup> In the context of B2C e-commerce, it cannot be said that the business is the party who does not desire the binding and final characteristic of the arbitral award. This is because, the fact that an arbitral award is final and binding, is one of the main characteristics of commercial arbitration which is the preferred method of resolving international commercial disputes.<sup>18</sup> There is no reason why business should not desire the arbitral award to be binding and final.

However, the consumer's desire in protecting the right to litigate disputes with the online business cannot be the reason behind the failure of online B2C arbitration. This reasoning clashes with the main driving force behind the creation of ODR. It is the unsuitability of court litigation for the resolution of cross-border B2C e-commerce disputes.<sup>19</sup> Bonnet and co-authors explained that:

“[C]ourts or traditional out-of-court dispute resolution mechanisms cannot reasonably resolve such conflicts. As a consequence, a new tool for dispute resolution has appeared, which is more efficient, more cost effective and more flexible than traditional approaches: this is Online Dispute Resolution (ODR). The parties to a deal that has gone awry are offered the possibility to solve their dispute over the Internet, communicating by means of emails, chat-rooms, videoconferences and other electronic means.”<sup>20</sup>

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<sup>17</sup>Vincent Fischer-Zernin and Abbo Junker, “Arbitration and Mediation: Synthesis or Antithesis?”, (1988) 5(1) J.Int'l Arb. 24. Alan Redfern and Martin Hunter, *Law and Practice of International Commercial Arbitration*, (3<sup>rd</sup> edn, Sweet & Maxwell, London, 1999), at p.10.

<sup>18</sup>Wahab, (The Global Information) note 3 supra, p.166. Steven Andersen, “Online Services of the International Centre for Dispute Resolution of the American Arbitration Association”, (2002) 27 Int'l Legal Prac.13.

<sup>19</sup>Alejandro E. Almaguer & Roland W. Baggott III, “Shaping New Legal Frontiers: Dispute Resolution for Internet”, (1997-1998) 13 Ohio St. J. on Disp. Resol.711, 712, 716. Mary Annepatton and Audun JØsang, “Technologies for Trust in Electronic Commerce”, (2004) 4 Electronic Commerce Research.4, 18. Graham Ross, “Challenges and Opportunities in Implementing ODR”, Proceedings of the UNECE Forum on ODR 2003, available at < <http://www.odr.info/unece2003> >, accessed on 20/6/2005.

<sup>20</sup>Vincent Bonnet, Karima Boudaoud, Michael Gagnebin, Jürgen Harms, and Thomas Schultz. “Online Dispute Resolution Systems as Web Services” *Proceedings of Hewlett-Packard OpenView*,

Court litigation cannot be an effective method of resolving cross-border B2C e-commerce disputes. This is because it is expensive. A consumer may have to travel to another country to bring an action or enforce a judgment. Court litigation may take a long time. A consumer may also be faced with language barriers. This limits the consumer's ability to obtain information and effectively participate in the litigation proceedings. As Varhrenwald put it:

“[T]he traditional cross-border litigation is time consuming and costly. The party which is not familiar with the court system in the member state where the litigation takes place may feel disadvantaged, because it is less able to access the state of the proceedings due to the lack of information, concerning the legal system, the geographical distance dependence on the advice of foreign advocates and, possibly, the use of foreign language.”<sup>21</sup>

However, this does not mean that court litigation does not have any role at all. Court litigation can have a supportive role to ODR methods particularly online arbitration. In other words, court litigation is not the primary means of resolving cross-border B2C e-commerce disputes but it is still important for the success of online arbitration. When consumers have cross-border B2C e-commerce disputes with businesses, they will not resort to court to get the disputes resolved. The disputes will be submitted to online arbitration. National courts will only interfere in the disputes relating to online arbitration agreements and processes. This issue is explained in depth in chapter six of this thesis.

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*University Association Workshop* (2002) <[www.online-adr.org/publications.htm](http://www.online-adr.org/publications.htm)>, accessed on 13/10/2004.

<sup>21</sup>Arnold Varhrenwald, “Out-of-Court Dispute Settlement System for E-commerce”, Report on Legal Issues, Part I: Parties to the Dispute, Published on the 29<sup>th</sup> May 2000, available at:

One can think of several factors that may have impacted the success of online B2C arbitration. One of these factors is the lack of consumer awareness of the online B2C arbitration services.<sup>22</sup> While there is no doubt that this factor has impacted the success of online B2C arbitration, it is not the major reason behind the failure of online B2C arbitration. This is because there has been a real attempt to make consumers aware of ODR, including online arbitration. The European Consumer Centers Network (hereinafter ECC-Net) provides the consumer with information and assistance in accessing an appropriate out-of-court dispute resolution scheme in any member state of the EU.<sup>23</sup> Another factor that may have impacted the success of online consumer arbitration is that as B2C e-commerce disputes are low-value, other ODR methods are more cost-effective than online B2C arbitration. Hörnle explained that:

“...the fees for consumer arbitration must be proportionate to the value of the claim. Since arbitration requires the intervention of a qualified and experienced human decision-maker, but consumer claims are mostly of small value, this may be difficult to achieve. For this reason, too, arbitration may not be the first choice for small and medium value consumer disputes.”<sup>24</sup>

Guaranteeing the quality of the online arbitration services does require retaining qualified and experienced arbitrators. This does make online arbitration less cost-

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<sup>22</sup>Aashit Shah, “Using ADR to Resolve Online Disputes”, (2004) 10 Rich. J.L. & Tech. 25, 6. It is important to draw the reader’s attention to the fact that this citation, which seems to be strange is the citation given on Westlaw Database.

<sup>23</sup>European Consumer Centers Network, available at: <[http://ec.europa.eu/consumers/redress\\_cons/index\\_en.htm](http://ec.europa.eu/consumers/redress_cons/index_en.htm)>, accessed on 15/05/2006. “The Network was created by merging two previously existing networks: the European Consumer Centres or ‘Euroguichets’, which provided information and assistance on cross-border issues; and the European Extra-Judicial Network or “EEJ-Net” which helped consumers to resolve their disputes through alternative dispute resolution schemes (ADRs) using mediators or arbitrators.”

<sup>24</sup>Julia Hörnle, “Online Dispute Resolution in Business-to-Consumer E-commerce Transactions”, (2002) 2 JILT), available at: < [http://www2.warwick.ac.uk/fac/soc/law/elj/jilt/2002\\_2.hornle/](http://www2.warwick.ac.uk/fac/soc/law/elj/jilt/2002_2.hornle/)>, accessed on 15/05/2004. (Hereinafter Business-to-Consumer).

effective than other ODR methods, such as negotiation and mediation. However, it cannot be said that online B2C arbitration has failed because businesses and consumers rely on other ODR methods, as these methods are more cost-effective than online arbitration. The reason is that other ODR methods are not suitable for every type of B2C e-commerce dispute. Evidence for this argument can be deduced from the report on the conference on the role of business-to-consumer dispute resolution in building trust in B2C e-commerce. This conference was organized by OECD, HCOPI, and ICC. The report explained that:

“[T]here is a range in online ADR programs from the fully automatic at one end to a formal arbitration setting at the other. It is recognized that each point along that spectrum has both advantages and disadvantages for consumers and businesses alike. While not every mechanism is appropriate for every dispute, the development of a wide variety of mechanisms can help address the breadth of disputes; such variety is enhanced by healthy competition among mechanisms.”<sup>25</sup>

The report affirms that all forms of ODR, including online arbitration, should be available to the business and the consumer. The reason is that one single form of ODR such as negotiation or mediation cannot be suitable for all types of disputes. This means that there are B2C e-commerce disputes that need to be resolved by arbitration. In the author's opinion online B2C arbitration has failed because it lacks

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<sup>25</sup>OECD, Committee on Consumer Policy, “Building Trust in the Online Environment: Business to Consumer Dispute Resolution. Joint Conference of the OECD, HCOPI, ICC. Report of the Conference”, DSTI/ICCP/REG/CP (2001)2, The Hague, 19 April 2001, p.4, available at: [http://www.oilis.oecd.org/oilis/2001doc.nsf/LinkTo/dsti-iccp-reg-cp\(2001\)2](http://www.oilis.oecd.org/oilis/2001doc.nsf/LinkTo/dsti-iccp-reg-cp(2001)2), accessed on 13/10/2004.



consumer confidence. Schultz explained that “ODR is in need for trust.”<sup>26</sup> Teitz observed that:

“ . . . ODR, like all of e-commerce, needs to have mechanisms to build consumer trust in the goods or services—here legal services in the form of dispute resolution—and to ensure consumer protection.”<sup>27</sup>

Working on raising consumer confidence in online arbitration should be prioritized because online arbitration has been less successful than other ODR methods. Building the consumer’s confidence in online arbitration requires two types of mechanisms. First, mechanisms to ensure that online arbitration as an e-commerce service is secure enough. In other words, the consumer will not be exposed to privacy violation and identity theft.<sup>28</sup> This issue will not be dealt with in this thesis because computer experts have already developed encryption software. The second type of mechanisms needed to build the consumer’s confidence in online arbitration is the one that ensures consumer protection. This is the topic of this thesis and it will be explained in the third part of this chapter which argues that raising the consumer’s confidence in online B2C arbitration requires regulation by an international convention.

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<sup>26</sup>Thomas Schultz, “Does Online Dispute Resolution Need Government Intervention? The Case for Architectures of Control and Trust”, (2004) 6(1) N.C. J.L. & TECH.71, 72. (hereinafter government intervention).

<sup>27</sup>Louise E. Teitz, “Providing Legal Services for the Middle Class in Cyberspace: The Promise and Challenge of On-Line Dispute Resolution”, 70 FORDHAM L. REV. 985, 1010 (2001).

<sup>28</sup>A European Initiative in Electronic Commerce: Communication of 15 April 1997 to the European Parliament, the Council, the Economic and Social Committee of the Regions COM(1997) 157 Final, para, 35.

### **1.3 Raising the Consumer's Confidence in Online Arbitration Will Increase the Volume of B2C E-commerce**

Raising the consumer's confidence in online arbitration will increase the volume of B2C e-commerce. It is true that the Internet has facilitated cross-border B2C commerce by allowing both the business and the consumer to conclude transaction without having to travel.<sup>29</sup> However, the volume of online cross-border B2C e-commerce is still very low. According to the European Information Technology Observatory, in the year 2004, about 90% of online dealings in the EU were between businesses.<sup>30</sup> This means that the value of consumer e-commerce transactions in the EU did not exceed 10% of the total value of the online dealings. As well as, in the year 2004, the EuroBarometer conducted research on 16,207 EU citizens. Only 16% of the surveyed sample has used the Internet to shop.<sup>31</sup> Lack of consumer confidence in e-commerce is one of the main reasons behind the modest volume of B2C e-commerce. The EU Commission observed that:

“[T]he first objective is to build trust and confidence. For electronic commerce to develop, both consumers and businesses must be confident that their transaction will not be intercepted or modified, that the seller and the buyer are who they say they are, and that transaction mechanisms are available, legal and secure. Building such trust and confidence is the prerequisite to win over businesses and consumers to electronic commerce.”<sup>32</sup>

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<sup>29</sup>Karen Stewart and Joseph Matthews, “Online Arbitration of Cross-Border, Business to Consumer Disputes”, 56 U. Miami L. Rev. 1111, 1113.

<sup>30</sup>European Information Technology Observatory, EITO-2004. available at: < <http://www.eito.com/index-eito.html>>, accessed on 12/05/2005.

<sup>31</sup>EuroBarometer, “European Union Public Opinion on Issues Relating to Business to Consumer E-Commerce: Executive Summary”, March 2004, available at: < [http://ec.europa.eu/public\\_opinion/archives/ebs/ebs\\_201\\_executive\\_summary.pdf](http://ec.europa.eu/public_opinion/archives/ebs/ebs_201_executive_summary.pdf) >, accessed on 11/11/2004.

<sup>32</sup>A European Initiative in Electronic Commerce, *supra* 28, para, 35.

The EU commission explained that lack of confidence in e-commerce, hampers both the business and the consumer from taking advantage of e-commerce. However, in the context of B2C e-commerce, attention should be focused on raising the consumer's confidence in e-commerce. Even members of the business sector have recognized this priority. The Paris Recommendations which are issued by the Consumer Confidence Working Group of the Global Business Dialogue states that:

“Industry associations should put a high priority on informing their members about electronic commerce and the need to build consumer confidence in electronic commerce.”<sup>33</sup>

Another reason that supports this argument is that businesses have more confidence in e-commerce than consumers. This clearly appears from the statistics stated above, which show that the volume of B2B e-commerce is much higher than the volume of B2C e-commerce. Pichler explained that instilling the consumer's confidence in e-commerce can be achieved either by establishing trust between the consumer and the business or by reliance.<sup>34</sup> The former means establishing mechanisms to encourage consumers to believe that a particular online business is trustworthy. An online rating system is an example of such a kind of mechanism.<sup>35</sup> It allows consumers to rate a particular online business according to their shopping experience with that

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<sup>33</sup>Global Business Dialogue on Electronic Commerce, Consumer Confidence Working Group, “The Paris Recommendations”, 13 September 1999, p.7.

<sup>34</sup> Rufus Pichler, “Trust and Reliance-Enforcement and Compliance: Enhancing Consumer Confidence in the Electronic Marketplace”, Stanford University, May 2000; available at <<http://www.law.stanford.edu/library/special/rufus.thesis.pdf>>, accessed on 15/06/2004. Clinton and Gore also emphasised that consumer confidence in e-commerce consists of the elements of trust and reliance. In the framework they issued on e-commerce, they explained that “consumer must have confidence ... that they will get what they pay for and that recourse or redress will be available if they do not.” Bill Clinton and Albert Gore, “A Framework for Global Electronic Commerce”, Washington, D. C., 1997.

<sup>35</sup>Ethan Katsh and Leah Wing, “Ten Years of Online Dispute Resolution (ODR): Looking at the Past and Constructing the Future”, (2006-2007) 38 U. Tol. L. Rev. 19, 26.

online business. Reliance means the availability of redress in case a dispute occurs between the consumer and the business. In fact, there is a growing consensus amongst governments, international organizations, industry associations and consumer advocacy groups that redress is pivotal for raising the consumer's confidence in e-commerce. As Consumers International puts it:

“[A]ll parties (businesses, consumers, and governments) recognize that, in order to facilitate the continued growth of electronic commerce, consumer confidence and trust in it must be improved, and that in order to improve consumer confidence, the problem of consumer redress in the event of cross border disputes must be resolved.”<sup>36</sup>

As explained supra, online arbitration is a quick and cost-effective method of resolving B2C e-commerce disputes. Therefore, raising consumers' confidence in online arbitration will raise their confidence in e-commerce.<sup>37</sup> This is because consumers will feel that there is a quick and cost-effective method of redress that can be used to resolve B2C e-commerce disputes. This will encourage them to shop on the Internet. This means that businesses will make more profit.<sup>38</sup> At the same time, businesses will be able to offer consumers cheap prices because of the savings

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<sup>36</sup>Consumers International, Office for Developed and Transition Economies, “Disputes in Cyberspace 2001: Update of Online Dispute Resolution for Consumers in Cross-Border Disputes”, p. 6, available at: <[http://www.consumersinternational.org/document\\_store/Doc517.pdf](http://www.consumersinternational.org/document_store/Doc517.pdf)> accessed, accessed on 1/2/2005.

<sup>37</sup>National Consumers League, the Electronic Privacy Centre, and Consumer Federation of America, “Alternative Dispute Resolution for Consumer Transactions in the Borderless Online Marketplace: Comments to the Federal Trade Commission and the US Department of Commerce, June 23, 2000, available at: <<http://www.ftc.gov/bcp/altdisresolution/comments/ncl.htm>>, accessed on 12/05/2004.

<sup>38</sup> Mohamed Wahab, “Globalisation and ODR: Dynamics of Change on E-commerce Dispute Settlement”, (2004) 12(1) I.J.L. & I.T. 123, 129. (Hereinafter Globalisation)

that they will make from using the Internet to transact and also arbitrate disputes with consumers.<sup>39</sup>

To sum up part one of this chapter, online B2C arbitration is quick and cost-effective. However, it has not been successful as an e-commerce activity. The main reason behind its failure is that consumers lack confidence in online arbitration. Raising the consumer confidence in the online arbitral process will increase the consumer confidence in e-commerce. This will increase the volume of B2C e-commerce. In other words, raising the consumer confidence is in the interest of both the consumer and the business.

## **2. Online Arbitration Lacks Consumer Confidence**

Schultz explained that consumers do not have confidence in ODR for the same reasons that prevent them from having confidence in e-commerce generally. These reasons are that the “lack of tangible features”; the “lack of social context and reputation”; and the “lack of predictable remedies”.<sup>40</sup> In order to explain how online commerce lacks tangible features Schultz quoted a few words from Nadler’s article which is also worth quoting in this thesis. She stated that:

“Websites lack many of the features that people typically rely on when making a judgment about whether a company is reputable. Physical storefronts allow customers to see, hear, smell, and touch products. Moreover, physical spaces have other cues that signal credibility. A fancy office with a push reception area could signal that the company is well capitalized, has an established clientele, and is likely to stand by its products or services. Furthermore, face-

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<sup>39</sup>Veijo Heiskanen, “Dispute Resolution in International Electronic Commerce”, (1999) 16(3) J. Int’l. Arb.29, 30.

<sup>40</sup>Schultz, government intervention, note 26 supra, p.80-86.

to-face meetings between company employees and customers can function to build confidence and resolve any problems that might arise.”<sup>41</sup>

Luxurious buildings and equipments indicate that a business has capital. This means that the business has a high volume of sales and the products sold meets the description given by the business. In offline B2C commerce, the consumer can also touch and try the goods and this is very crucial for the consumer’s confidence in the business. However, these “tangible features” do not exist in the online context. This is because the consumer cannot examine the goods or evaluate the services before concluding the contract.<sup>42</sup>

Schultz also explained that in offline B2C commerce, dealings occur within an identified community. Consumers who are members of the same community talk to each other about their shopping experiences. This will contribute to shaping the good or bad reputation of the business. A good reputation helps to build the consumer’s confidence in the business and a bad reputation prevents a consumer from having confidence in the business. However, in the context of B2C e-commerce, the consumer cannot effectively share information about online businesses. This is because of the geographical barriers. In other words, the consumers themselves are located in different communities.<sup>43</sup>

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<sup>41</sup>Janice Nadler, “Electronically-Mediated Dispute Resolution and E-Commerce”, (2001) 17 N.J. 333, 334.

<sup>42</sup>Schultz, government intervention, note 26 supra, p.80, 81.

<sup>43</sup>Ibid, p.82, 83.

The availability of predictable remedies means that there should be a quick and cost-effective method of resolving B2C e-commerce disputes.<sup>44</sup> One cannot deny that the “lack of tangible features” and the “lack of social context” may reduce the consumer’s confidence in online arbitration. However, they are not the major reasons that reduce the consumer’s confidence in online arbitration. The main “tangible feature” of offline B2C commerce is the opportunity to examine the goods or try the services before the consumer decides whether to take it. However, this is not so important in the case of obtaining online arbitration services. This is because, as opposed to other goods and services sold in the offline market, the consumer cannot examine or try offline arbitration services before he decides whether to use them. The lack of “social context and reputation” is also not important in the context of online B2C arbitration. The essence of social context and reputation is word of mouth which enables consumers to rely on other consumers’ shopping experiences in order to decide whether the business is trustworthy. In respect to online arbitration, consumers do not need word of mouth to decide whether the online arbitration provider is trustworthy. The consumer needs to see published arbitral awards. Publication gives the consumer the chance to look at other consumers’ experiences in arbitrating their disputes.<sup>45</sup> Publication of the arbitral awards also places both the arbitration provider and the arbitrator under an obligation to act impartially in order to avoid criticism by the public. This issue is explained in depth in chapter seven of this thesis. The lack of predictable remedies to resolve disputes arising from the online arbitral process does reduce the consumer’s confidence in online arbitration.

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<sup>44</sup>Schultz, government intervention, note 26 supra, p.82, 83.

<sup>45</sup>Caplin, note 9 supra, p.212.

However, it is part of the major reason that reduces the consumer's confidence in online arbitration. The reason is that online B2C arbitration is mainly governed by the laws that regulate arbitration between commercial parties. Shell explained that:

“[T]he model of arbitration that gained acceptance in the 1920s involved primarily resolution of disputes between members of an industry. In such cases, all parties are members of the community that established the arbitration process and all are likely to know and accept the norms and customs that govern the industry. There is no pressing need for legal accountability when the parties share a strong set of legally acceptable values and seek to use arbitration as a means of preserving and enhancing their relationship. But arbitration between an industry and “outsiders” pursuant to standard form contracts is quite a different matter. Here, arbitration is being imposed by an industry on another interest group that knows little of the industry's form of arbitration and understands less of the industry's customs”<sup>46</sup>

In commercial arbitration, both parties have relatively similar bargaining power. They are also sophisticated, as they are all likely to have experience of handling disputes. Commercial parties also share common customs that belong to their industry. Therefore, the current commercial arbitration laws are based on an important principle which is the parties' autonomy. The parties' autonomy allows businesses to shape the arbitral process in the way they want. However, the fact that online B2C arbitration is governed by the commercial arbitration model means that the business can easily take advantage of the consumer.<sup>47</sup> Online B2C e-commerce contracts are concluded via adhesion contracts which are introduced to the consumers on a take-it-or-leave-it basis.<sup>48</sup> In other words, in B2C e-commerce

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<sup>46</sup> Richard Shell, “The Role of Public Law in Private Dispute Resolution: Reflections on Shearson/American Express, Inc. v McMahon”, (1988) 26 Am. Bus. L.J. 397, 418, 419.

<sup>47</sup> Llewellyn Joseph Gibbons, “Creating a Market for Justice; A Market Incentive Solution to Regulating the Playing Field: Judicial Deference, Judicial Review, Due Process, and Fair Play in Online Consumer Arbitration”, (2002) 23Nw. J. Int'l L. & Bus. 1, 7, 8. (Hereinafter Creating a Market).

<sup>48</sup> Ibid, 7, 8.



contracts, consumers cannot negotiate terms with businesses. This means that the business can use the parties' autonomy to impose online arbitration on the consumer and also design the arbitral process in a way that serves its interests.<sup>49</sup> Business can determine the applicable substantive law.<sup>50</sup> Business can determine the court that has jurisdiction to review disputes over arbitration agreements and processes.<sup>51</sup> The business can also decide the procedures to be followed in the arbitral proceedings and decide the online arbitration provider and the arbitrators.<sup>52</sup> Therefore, in order to instil the consumer's confidence in online arbitration, a new model of online cross-border B2C arbitration that ensures consumer protection is needed. Gibbons explained that:

“[T]he commercial arbitration paradigm must change in the cyberspace context and provide substantive and procedural protection if it is to serve the need to create law and adjudicate disputes in cyberspace.”<sup>53</sup>

The coming part explains the elements of the protection that the new model should provide to the consumer. It also explains which mode of regulation should be adopted in order to guarantee that the consumer is really enjoying the protection.

### **3. Regulating Online B2C Arbitration**

In this thesis, raising the consumer confidence in online B2C arbitration means ensuring consumer protection. Four basic elements of consumer protection should be

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<sup>49</sup>Gibbons, (Creating a Market), note 47 supra, p.17-19.

<sup>50</sup>Ljiljana Biukovic, “International Commercial Arbitration in Cyberspace: Recent Developments”, (2002) 22 Nw. J. Int'l L. & Bus.319, 332.

<sup>51</sup>Ibid

<sup>52</sup>Gibbons, (Creating a Market), note 47 supra, p.17-19.

<sup>53</sup>Llewellyn Joseph Gibbons, “Rusticum Judicium?: Private “Courts” Enforcing Private Law and Public Rights: Regulating Virtual Arbitration in Cyberspace”, (1998) 24 Ohio N.U. L. Rev. 769, 774. (Hereinafter Rusticum Judicium).

provided. First, the consumer is not involuntarily taken to arbitration. It should also ensure that the protection afforded to the consumer under the law of his country of domicile is not excluded by a choice of substantive law clause. It should also ensure that the consumer always has the right to refer to the Courts of his country of domicile to resolve disputes relating to arbitration agreements and processes. It should assure the consumer that the arbitral procedures will be fair. These issues will be explained in the coming four subsections. Subsection five explains that online B2C arbitration should be regulated by an international convention in order to ensure that the consumer is really enjoying the protection.

### **3.1 Transparency in the Method of Introducing the Arbitration Clause into the B2C E-commerce Contract**

There is widespread opinion that an adhesive arbitration clause reduces the consumer's confidence in the online arbitral process. Ponte explained "it would be difficult to argue that restricting online consumer access to the courts, even through nonbinding but mandatory ODR programs, will actually help to promote consumer confidence in online transactions".<sup>54</sup> Ponte adopted the same point view of the European Commission. The Commission observed:

"[T]he use of any exhaustion principles for ADR (i.e. requiring a consumer to agree to exhaust all ADR remedies before being allowed to start a court action) would seriously undermine consumer confidence. An effective, fair and rigorous ADR scheme that gives consumers confidence will be used without the need for compulsion. The advantages to an efficient and well run ADR over court litigation are easy for anyone to see. By producing an agreement

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<sup>54</sup> Lucille M. Ponte, "Boosting Consumer Confidence in E-Business: Recommendations for Establishing Fair and Effective Dispute Resolution Programs for B2C Online Transactions", (2002) 12 Alb. L.J.Sci. & Tech. 441, 464. (Hereinafter Boosting Consumer).

that gives with one hand and takes away with another is unlikely to fill a consumer with confidence.”<sup>55</sup>

The European Commission’s statement means that an adhesive arbitration clause will reduce the consumer’s confidence in online arbitration. This is because an arbitration clause precludes the consumer from referring the dispute to a Court of law. The Commission also explained that if the ADR scheme is fair and effective, the consumer will voluntarily choose ADR without the need for imposing it through adhesion contracts. Other writers have also affirmed that consumer participation in the online arbitral process should not be pursuant to a binding arbitration clause. Benyekhlef and Gélinas explained ODR agreements should only be allowed if the agreement has been concluded after the dispute has arisen.<sup>56</sup> Kohler and Schultz explained that a unilateral arbitration clause that only binds the business can be used in online B2C e-commerce contracts.<sup>57</sup>

However, the author believes that an adhesive online B2C arbitration clause that binds both the business and the consumer should be admissible. This is for two reasons. First, the fact that an arbitration clause prevents the consumer from referring the dispute to a Court of law does not reduce the consumer’s confidence in online arbitration. This is because litigation is too expensive and too impractical for cross-border B2C e-commerce disputes, therefore, one cannot expect the consumer

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<sup>55</sup> Ibid, Ponte quoting the European Commission memorandum that was introduced to the Joint Workshop on ADR for Online Consumer Transactions hosted by the Federal Trade Commission. (May 30, 2000), the original document that included the paragraph, used to be available at: <http://www.ftc.gov/bcp/altresolution/comments/europeancommission.pdf>. However, this URL is not active anymore.

<sup>56</sup> Karim Benyekhlef and Fabien Gélinas, “Online Dispute Resolution”, (Summer 2005) 10(2) Lex Electronica.1, 69, available at: [http://www.lex-electronica.org/articles/v10-2/Benyekhlef\\_Gelinas.pdf](http://www.lex-electronica.org/articles/v10-2/Benyekhlef_Gelinas.pdf)., accessed on 12/06/2006.

<sup>57</sup> Kohler and Schultz, (Online Dispute), note 15 supra, p.154.

to be concerned about the right to litigate disputes in a Court of law.<sup>58</sup> Second, it is true that a fair and effective online arbitral process is likely to gain consumer acceptance after the dispute arises. However, if the dispute has already arisen, businesses may refuse to participate in the online arbitral process.<sup>59</sup> This is because in the B2C e-commerce, businesses usually receive payment before they send the purchased products to or provide the service for the consumers.<sup>60</sup> An arbitration clause that only binds the business but not the consumer is unlikely to be welcomed by the business sector. This is because businesses insert the arbitration clause in order to avoid litigation in many forums. In other words, they insert the arbitration clause to avoid “jurisdictional uncertainty”.<sup>61</sup>

Ensuring the consumer’s confidence in the online arbitral process requires informing the consumer about the arbitration clause before he accepts the contract.<sup>62</sup> This is because as Carrington and Haagen explained, knowledge about the existence of the arbitration clause is necessary to guarantee that the consumer has actually consented to arbitration.<sup>63</sup> However, as the author will explain in chapter three of this thesis, the business is not under an obligation to specifically notify the consumer about the existence of the arbitration clause in the B2C e-commerce contract. Therefore, a rule that places the business under an obligation to specifically notify the consumer about the existence of the arbitration clause should be in place. The author argues that the

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<sup>58</sup>See section 1.2 of this chapter.

<sup>59</sup>Hörmle, (business-to-consumer), note 24 supra.

<sup>60</sup>Mary Shannon Martin, “Keep it Online: the Hague Convention and the Need for Online Alternative Dispute Resolution in International Business-to-Consumer E-Commerce”, (2002) 20 B.U. Int’l. L.J. 125,130.

<sup>61</sup>Biukovic,note 50 supra, p.332.

<sup>62</sup>Ponte, (Boosting Consumer), note 54 supra, p.453-455.

<sup>63</sup>Paul D. Carrington and Paul H. Haagen, “Contract and Jurisdiction”, (1996) Sup. Ct. Rev.331, 340.

business should include a separate icon that includes the arbitration clause which the consumer has to accept if he wants to continue the contracting process. The arbitration clause should be written in clear language and provide the consumer with sufficient information about the arbitral process. In the fourth chapter, the author will argue that adopting a knowing and intelligent consent standard to the arbitration clause will facilitate the enforcement of online B2C arbitration clauses.

### **3.2 The Consumer Should Enjoy the Protection of the Law of his Domicile**

In the bricks and mortar B2C commerce, consumers enjoy the protection that is awarded to them under the law of the place where the bricks and mortar shop is located. This is usually the law of the consumer's country of domicile because the consumer mainly purchases from the bricks and mortar shops in his country. The OECD Guidelines on Consumer Protection states that:

“In considering whether to modify the existing framework, governments should seek to ensure that the framework provides fairness to consumers and businesses, facilitates electronic commerce, results in consumers having a level of protection not less than that afforded in other forms of commerce.”<sup>64</sup>

The OECD Guidelines affirm that when the consumer transacts online, they should obtain “a level of protection not less than” the one they obtain offline. In bricks and mortar commerce, the consumer enjoys the protection of the law of his domicile. Making consumer protection in e-commerce not less than the protection in bricks and mortar commerce means that the online consumer should enjoy the protection of the law of his domicile. However, as explained supra the online B2C adhesion

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<sup>64</sup>OECD Guidelines for Consumer Protection in the Context of Electronic Commerce, 1999.

contract enables the business to solely determine the law applicable to the merits of the dispute. The International Chamber of Commerce (hereinafter ICC) which represents the business sector's interests explained that business should be able to insert choice of law clauses into e-commerce contracts with consumers. The ICC noted:

“A primary goal of commercial law is to develop legal certainty for transacting parties. ICC supports freedom of contract as a general principle that should drive decisions regarding choice of law and forum. As the basis for all commercial law, contracts embody private agreements between parties, formalizing their intent to be bound by the terms of the contract as if these were the law between them. For reasons of compelling public policy, however, in the context of B2C disputes, governments typically place limits or conditions on private agreements in heavily regulated sectors, such as banking and investments. Courts and regulators may also override the terms of private agreements that appear to result from fraud or deceptive practices. ICC encourages governments to keep these limits on the applicability of party autonomy to a minimum.”<sup>65</sup>

It is true that a choice of law clause eliminates uncertainty about the applicable law to the merits of the dispute. Legal certainty is so important for the consumer's confidence in the online arbitral process.<sup>66</sup> However, a choice of law clause that deprives the consumer of the protection of the law of his domicile will not raise his confidence in the online arbitral process. Ponte explained that “if the ultimate goal is to boost e-consumer confidence, the selection of fora and laws that benefit only e-businesses do not promote that goal.”<sup>67</sup>

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<sup>65</sup>ICC, Policy Statement on Jurisdiction and Applicable Law in Electronic Commerce (June 6, 2001), available at :< <http://www.iccwbo.org/id478/index.html>> accessed on 12/06/2006.

<sup>66</sup>Kohler and Schultz, (online dispute), note 15 supra, p.82.

<sup>67</sup>Ponte, (Boosting Consumer), note 54 supra, p.487.

Ensuring consumer confidence in the online arbitral process requires the application of the law of his domicile to the merits of the dispute. If the consumer is sure that he will enjoy the protection of the law of his domicile, he will not hesitate to purchase from online businesses even if they are located in other countries. As Consumer International explained:

“if consumers are to take full advantage of the global shopping mall theoretically offered by the internet, they must feel confident of receiving a consistent standard of consumer protection wherever they shop.”<sup>68</sup>

The business should be willing to accept a new rule that stipulates the application of the law of the consumer domicile to the merits of the dispute that has been submitted to online arbitration. This is because “e-business cannot expect that the Web will offer unprecedented access to new markets and increased revenues without having to be accountable in those new markets, just like bricks and mortar firms.”<sup>69</sup> In the fifth chapter of this thesis, the author will explain that a choice of substantive law clause will deprive the consumer of the protection of the law of his country of domicile. Therefore, raising consumer confidence in online arbitration requires adopting a rule that stipulates the application of the law of the consumer domicile to the merits of the dispute.

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<sup>68</sup> Consumers International, “Consumers@shopping: An International Comparative study of Electronic Commerce”, London, September 1999, p.7.

<sup>69</sup>Ibid

### **3.3 The Consumer should be Able to Refer Disputes Related to Arbitration Agreements and Processes to the Court of his Domicile**

As mentioned supra, online arbitration is an e-commerce activity. An important element of confidence in e-commerce is the availability of an effective method of dispute resolution. This means that raising the consumer's confidence in online arbitration requires the availability of an effective method to resolve disputes arising from online arbitration agreements and processes. Schultz believes that disputes arising from ODR proceedings should be submitted to ODR. He noted that:

“[C]ourts are not likely to be the primary resolvers of most small- and medium-sized disputes occurring in cyberspace—which are the majority of e-commerce disputes involving ODR providers—because courts are too slow and expensive. This is a general problem caused by the ubiquity of cyberspace, which clashes with the territoriality of jurisdiction and judicial authorities. There is no reason this should be any different with disputes arising out of ODR outcomes—either disputes left unresolved, or parties disputing the findings of the ODR provider. Put differently, the only real resolvers of disputes arising out of ODR—and these disputes will inevitably come—are likely to be other ODR providers.”<sup>70</sup>

It is true that court intervention in the online arbitral process will incur extra costs and time. However, avoidance of this extra time and cost should not be the reason for abandoning Court supervision over online arbitration agreements and processes. This is for two reasons. First, most arbitral proceedings do not involve any court intervention and the arbitral award is voluntarily performed by the losing party.<sup>71</sup> This means that the extra cost and time that may come from court intervention will not appear in most online B2C arbitration proceedings. Second, abandoning Court

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<sup>70</sup>Schultz, (Government Intervention), note 26 supra, p.84, 85.

<sup>71</sup>Redfern and Hunter, note 17 supra, p.443.



intervention in the online arbitral process will reduce consumer confidence in online arbitration. This is because online arbitration will lose “its effectiveness” and credibility.<sup>72</sup> The consumer needs the court to enforce the online arbitration agreement. Court intervention might also be needed in the course of the online arbitral process to challenge an arbitrator or “to preserve evidence or to protect assets”.<sup>73</sup> Court intervention might also be needed to enforce or recognise the online arbitral award.

As Court supervision is important for consumer confidence in the online arbitral process, the consumer should be able to refer disputes resulting from online arbitration agreements and processes to the Courts of his country of domicile.<sup>74</sup> This is because the costs and other impracticalities of litigating disputes in a foreign forum will prevent the consumer from referring disputes, relating to the online arbitration agreements and processes, to the Court. This will limit the effectiveness of the online arbitral process and thereby consumer confidence in the online arbitral process will decrease.

However, the business can deprive the consumer of the right to refer disputes arising from online arbitration agreements and processes to the Court of his domicile.<sup>75</sup> This happens when the business inserts a choice of forum clause. The business can choose the Court of his place of business to review disputes over an online

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<sup>72</sup>Redfern and Hunter, note 17 supra, p.342.

<sup>73</sup>Ibid, p.345.

<sup>74</sup>Ponte, (Boosting Consumer), note 54 supra, p.487, 488.

<sup>75</sup>Nicolas de Witt, “Online International Arbitration: Nine Issues Crucial to Its Success”, (2001) 12 Am. Rev. Int’l Arb.441, 452.

arbitration agreement.<sup>76</sup> It is well-established that the Courts of the place of arbitration have the jurisdiction to supervise the online arbitral procedures and to hear challenges to the arbitral award.<sup>77</sup> This means that the business can choose a particular Court to supervise the online arbitral procedures or hear challenges to the arbitral award by determining the arbitral seat. Consequently, a rule that stipulate the exercise of jurisdiction of the Courts of the consumer domicile over online arbitration agreements and processes should be in place. This issue will be explained in-depth in chapter six of this thesis.

### **3.4 Perceived Fairness of the Online Arbitral Procedures**

Every consumer is entitled to an online arbitral process that is procedurally fair. Stewart and Matthews noted that “online arbitration involving consumers should be procedurally fair”.<sup>78</sup> The OECD Guidelines on Consumer Protection state that:

“Businesses, consumer representatives and governments should work together to continue to provide consumers with the option of alternative dispute resolution mechanisms that provide effective resolution of the dispute in a fair and timely manner and without undue cost or burden to the consumer.”<sup>79</sup>

The OECD explained that B2C ADR proceedings should be cost-effective, quick and fair. Hörnle explained that any standards seeking to regulate ODR should strike a balance between the cost-effectiveness of ODR and the “quality of the ODR procedures”.<sup>80</sup> However, instilling consumer confidence in the online arbitral

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<sup>76</sup>Witt, *supra* note 75, p.452.

<sup>77</sup>*Ibid.* Tiffany J. Lanier, Esq, “Where on Earth Does Cyber-Arbitration Occur?: International Review of Arbitral Awards Rendered Online”, (2000) 7 ILSA J. Int’l & Comp. L.1, 9,10.

<sup>78</sup>Stewart and Matthews, note 29 *supra*, p.1125.

<sup>79</sup>OECD Guidelines for Consumer Protection in the Context of Electronic Commerce, 1999.

<sup>80</sup>Hörnle, (business-to-consumer), note 24 *supra*.

process requires convincing the consumer that the online arbitral procedures will be fair. Vidmar explained that “if disputants do not see procedures as fair, they will not accord them legitimacy, will avoid them if possible, and if forced to use them, will not readily accept the outcome”.<sup>81</sup> Therefore, achieving cost-effectiveness and quickness should not be on account of the procedural fairness of the online arbitral process.

In order to encourage the consumer to perceive fairness in online arbitral procedures, the consumer should see that he will have the chance to present his case. This means that the consumer should be given the chance to present arguments and evidence and reply to the other party’s contentions. It is also important that the online arbitration provider and the arbitrator be independent and impartial. It is crucial to have effective court supervision on aspects of procedural fairness. All of these issues will be explained in detail in chapter seven of this thesis.

### **3.5 Regulation by an International Convention**

Self-regulation “are informal... rules imposed by a particular community”.<sup>82</sup> The community members comply with the self-regulation because of an “internal sense of duty or a fear of external non-legal sanctions, or both.”<sup>83</sup> Many authors argue that e-commerce and ODR should be left for self-regulation. Almaguer and Baggott explained that:

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<sup>81</sup>Neil Vidmar, “The Origins and Consequences of Procedural Fairness”, (1990) 15 Law & Soc. Inquiry 877, 879.

<sup>82</sup>Rafal Morek, “The Regulatory Framework for Online Dispute Resolution: A Critical View”, (2006-2007) 38 U. Tol. L. Rev.163, 167.

<sup>83</sup>Ibid.

“[A] self-regulatory scheme for dealing with Internet transactions goes hand in hand with the ideal goals of decreased government intervention and decreased litigation. In order to become a truly free-flowing information medium, the Internet must devise ways to hone its ability to regulate itself. As such, any self-regulatory mechanism that is accepted by the Internet community will promote dispute resolution; or rather, dispute resolution principles will drive the effort to self-regulate, obviating the need for governments to intervene and legislate along geopolitical lines.”<sup>84</sup>

Almaguer’s and Baggott’s statement means online B2C arbitration should not only be self-regulated but it should also be a means of implementing a self-regulatory framework for B2C e-commerce. In other words, the parties’ autonomy, which is the main principle in the commercial arbitration paradigm, can be used by the parties to regulate the online arbitral process without any intervention by the Court. Katsh, Rifkin and Gaitenby explained that online arbitration should be self-regulated and the Internet should be viewed as a separate jurisdiction. They noted:

“a marketplace could ... rely on an arbitration process... and use the threat of exclusion as the mechanism for enforcing the terms of the ruling... we increasingly felt that eBay could be considered to be a jurisdiction in itself, a legal authority in itself, an entity that might even be considered to be able to exercise a loosely defined sovereign power...”<sup>85</sup>

The author believes that the Internet should not be treated as a separate jurisdiction. The Internet does not abolish the borders and frontiers between countries. The Internet is merely a method of communication that eases concluding cross-border contracts between the business and the consumer who must have a physical presence within a particular jurisdiction. Treating the Internet as a separate jurisdiction limits the effectiveness of online arbitration. This is because, as explained *supra* the

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<sup>84</sup>Almaguer and Baggott, note 19 *supra*, p.714

<sup>85</sup>E. Katsh, J. Rifkin and Alan Gaitenby, “E-Commerce, E-Dispute, and E-Dispute Resolution: In the Shadow of eBay Law”, (2000) 15 Ohio. St. J. on Disp. Resol.705, 728.

effectiveness of online arbitration requires Court intervention in disputes related to the arbitral process and the enforcement of arbitration agreements and awards. Katsh, Rifkin and Gaitenby explained that the party who refuses to comply with the online arbitral award will be excluded from the eBay marketplace.<sup>86</sup> However, this enforcement system is not available with every online B2C arbitration award. This is because not all B2C e-commerce dispute occur within a marketplace like eBay. Many B2C e-commerce disputes arise from contracts concluded directly between the business and the consumer.

The author also believes that self-regulation cannot guarantee that the consumer is really enjoying protection. This is because, as mentioned *supra*, it is not binding on online arbitration providers and online businesses.<sup>87</sup> If they violate the self-regulatory rules, they will not face legal sanctions. It is true that online businesses and online arbitration providers might choose to comply with a new model of online B2C arbitration that is implemented through self-regulation. However, as self-regulation is not binding, the degree of compliance with the new model of online B2C arbitration will differ from one business to another and from one online arbitration provider to another. This will cause the consumer confusion and uncertainty which will eventually reduce his confidence in online arbitration. Coteanu explained that:

“... even if ODR is endowed with self-regulatory framework, in practice they would still lack effectiveness. These self-regulatory frameworks are too

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<sup>86</sup>Rifkin and Gaitenby, note 85 *supra*, p.728.

<sup>87</sup>Youseph Farah, “Critical Analysis of Online Dispute Resolutions: The Optimist, the Realist and the Bewildered”, (2005) 11(4) C.T.L.R.123, 125, 126.

general and any attempt to launch a workable self-regulatory system at international level will fail due to the diverging consumer protection rules existing at national level. Self-regulatory legal system in relation to ODR procedures might be essential in the preparatory work of national governments and in the formation of a 'customary cyber consumer law.' Nevertheless, if ODR is to play a challenging role in promoting electronic commerce on a real, international level, the regulation of ODR should be made through coordinated international governmental interventions aiming to establish effective legal rules of ODR in consumer transactions.”<sup>88</sup>

The present author believes that raising the consumer confidence in the online arbitral process requires regulating any new model of online B2C arbitration by an international convention. The reason is that an international convention will guarantee that the consumer enjoys the protection. An international convention is a binding type of regulation. This means that the adhering countries will enforce the new model of online B2C arbitration against online businesses and online arbitration providers.

#### **4. Conclusion**

Online arbitration is cost-effective and quick. However, it has not been successful as an e-commerce activity. The lack of consumer confidence in online arbitration is the main reason behind its failure. The lack of confidence resulted from the fact that online arbitration is governed by the legal framework that is designed for arbitration between commercial parties. Raising consumer confidence in the online arbitral process requires adopting an international convention that imposes a new model for online B2C arbitration. The new model should ensure transparency in the method of introducing the arbitration clause into the B2C e-commerce contract. It should also

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<sup>88</sup>Cristina Coteanu, *Cyber Consumer Law and Unfair Trading Practices*, (1<sup>st</sup> edn, Ashgate, Aldershot, 2005), p.91.

ensure that the consumer enjoys the protection of the law of his domicile. It should ensure the consumer's right to litigate disputes related to online arbitration agreements and processes in the Courts of his country of domicile. A new model of online arbitration that seeks to ensure consumer confidence in the online arbitral process should promote the consumer's perception of fairness in online arbitral procedures.

## **Chapter 3**

# **Transparency in the Method of Introducing an Arbitration Clause into the B2C E-commerce Contract**

An arbitration clause is an agreement that exclusively refers future disputes between the business and the consumer to arbitration.<sup>1</sup> Carrington and Haagen explained that the consumer knowledge about the existence of the arbitration clause is extremely important to ensure that the consumer has consented to arbitration.<sup>2</sup> Therefore, the consumer will not trust online arbitration if he is surprised by the commitment to resolve his dispute with the business by online arbitration. This is because the consumer will feel that he has involuntarily been taken to online arbitration.<sup>3</sup> This means that raising the consumer's confidence in online arbitration requires disclosing the existence of the arbitration clause to the consumer before he decides to accept the B2C e-commerce contract.

However, this chapter will argue that business is not under an obligation to specifically notify the consumer that the online B2C contract includes an arbitration clause. Therefore, a rule that obliges the business to notify and explain the arbitration clause to the consumer should be in place. The first part of this chapter explains that, as ordinary contract law rules govern the issue of consent to an arbitration clause, business is not under an obligation to notify the consumer about the existence of an arbitration clause. This is because under ordinary contract law, an

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<sup>1</sup>Gary B. Born, "Planning for International Dispute Resolution", (2000) 17(3) J. Int'l. Arb. 61, 62.

<sup>2</sup>Paul D. Carrington and Paul H. Haagen, "Contract and Jurisdiction", (1996) Sup. Ct. Rev. 331, 340.

<sup>3</sup>Ibid



objective consent standard is employed to determine whether the parties have consented to the contract terms. The second part explains that unfairness and unconscionability rules do not place a business under an obligation to give the consumer specific notice about the existence of an arbitration clause. The third part explains the benefit of using a separate icon in the B2C e-commerce contracts to disclose the existence of an arbitration clause to the consumer.

## **1. Consent to Arbitration Clauses is Governed by Ordinary Contract Law**

Ordinary contract law applies to determine whether a business and a consumer have consented to the arbitration clause.<sup>4</sup> The English Arbitration Act 1996 treats any B2C arbitration clause as unfair if the value of the claim is £5000 or less.<sup>5</sup> However, if the value of the claim is more than £5000 the validity of an arbitration clause will be governed by ordinary contract law rules.<sup>6</sup> In the US, §2 of the FAA states that:

“A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction,

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<sup>4</sup>Stephen J. Ware, “Arbitration Clauses, Jury-Waiver clauses, and Other Contractual Waivers of Constitutional Rights”, (Winter/Spring 2004) 67 Law & Contemp. Probs. 167, 170. (hereinafter Jury).

<sup>5</sup>§91(1), English Arbitration Act 1996. § 91(1) states that, “(1) A term which constitutes an arbitration agreement is unfair for the purposes of the Regulations so far as it relates to a claim for a pecuniary remedy which does not exceed the amount specified by order for the purposes of this section.” The sum of £5000 is determined by a statutory instrument which is The Unfair Arbitration Agreements (Specified Amount) Order 1999, SI 1999/2167.

<sup>6</sup> What should be mentioned here is that under both the English Arbitration Act 1996 and the FAA, the formal validity requirement does not place the business under an obligation to give the consumer a notice about the existence of the arbitration. This is because nowadays, formal validity requirements are Lenient. The issue of formal validity of the arbitration clause is dealt with in chapter four with a particular focus on New York Convention 1958. This will include detailed explanation of formal validity requirement under the English Arbitration Act 1996 and the FAA.

or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.”<sup>7</sup>

The US Supreme Court interpreted the language of section 2 of the FAA in the case of *Southland Corp v Keating*,<sup>8</sup> the Supreme Court provided that:

“We discern only two limitations on the enforceability of arbitration provisions governed by the Federal Arbitration Act: they must be part of a written maritime contract or a contract “evidencing a transaction involving commerce” and such clauses may be revoked upon “grounds as exist at law or in equity for the revocation of any contract.” We see nothing in the Act indicating that the broad principle of enforceability is subject to any additional limitations.”<sup>9</sup>

The Supreme Court statements mean that there are two limitations to the enforceability of an arbitration clause. The first is the commerce requirement and the second is the writing requirement. Apart from these two requirements, the enforceability of the arbitration clause is governed by ordinary contract law. The commerce requirement does cause an impediment to the enforcement in the context of B2C arbitration. This is because the meaning of the word commerce in §2 of the FAA has been interpreted expansively and it does include B2C transactions.<sup>10</sup> This means in the context of B2C transactions the validity of an arbitration clause is subject to ordinary contract law rules.<sup>11</sup> The fact that the issue of consent to arbitration clauses is governed by ordinary contract law means that business is not

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<sup>7</sup>§2, Federal Arbitration Act 1925.

<sup>8</sup>465 US 1, 11 (1984).

<sup>9</sup>Ibid

<sup>10</sup>F. Paul Bland, Jr., Michael J. Quirk, Kate Gordon, and Jonathan Sheldon, *Consumer Arbitration Agreements: Enforceability and Other Topics*, (4<sup>th</sup> edn, NCLC, Boston, 2004), p.11.

<sup>11</sup>Common contract law in the different states establishes a set of grounds that can be used to invalidate any contract and these are that waiver, duress, fraud, misrepresentation and unconscionability. Duress, waiver, fraud and misrepresentation are out of the scope of the author’s research because consumers rarely rely on them to strike out unfair arbitration clauses in online B2C adhesion contracts because they mostly fail to void an arbitration clause on these grounds; nevertheless, the author will focus on unconscionability which is the main means that consumers in the US use to invalidate unfair arbitration clauses.

obliged to notify the consumer about the existence of the arbitration clause. This is what the author is going to explain in the next section.

## 1.1 Objective Consent

A business is not obliged to give the consumer specific notice about the existence of an arbitration clause in a B2C e-commerce contract. This is because under ordinary contract law the objective consent standard is the general rule that is employed to decide whether the parties have assented to the contents of the contracts.<sup>12</sup> Under English Law, the reliance on the objective theory of consent can be deduced from the case of *Smith v Hughes*.<sup>13</sup> In this case Lord Blackburn asserted that:

“If, whatever a man’s real intention may be, he so conduct himself that a reasonable man would believe that he was assenting to the terms proposed by the other party, and that other party upon that belief enters into the contract with him, the man thus conducting himself would be equally bound as if he had intended to agree to the other party’s terms.”<sup>14</sup>

After the case of *Smith* several forms of limitation on objective consent have been developed. For example, control over certain types of contractual terms has been imposed by lawmakers. For example, Sections 12-15 of the Sale of Goods Act 1979 impose certain conditions regarding the title, correspondence with description, and satisfactory quality. Section 6 of the Unfair Contract Terms Act 1977 prohibits exclusion of these conditions by contractual clauses.

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<sup>12</sup>Ewan Mckendrick, *Contract Law: Test, Cases, and Materials*, (2<sup>nd</sup> edn, OUP, Oxford, 2005), p.24. Hugh Collins, *The Law of Contracts*, (3<sup>rd</sup> edn, Butterworths, London, 1997), p.112, 113. (hereinafter the law of the contract) Randy E. Barnett, “A Consent Theory of Contract”, (1986) 86 Colum. L. Rev.269, 273.

<sup>13</sup>(1871) LR 6 QB 597, Court of Appeal.

<sup>14</sup>*Ibid*, p.607.

Another limitation on objective consent approach can be seen in principles made by judges. If the term that is relied upon by the business is unusual in that type of contract, then the term must be specifically brought to the attention of the consumer. An illustration for that can be seen in the case of *Interfoto Picture Library Ltd v. Stiletto Visual Programmes Ltd*.<sup>15</sup> In this case Interfoto hired 47 transparencies to Stiletto. The transparencies were despatched to Stiletto in a bag containing a delivery note containing conditions printed in small visible lettering on the face of the document, including condition 2, which stated that a holding fee of £5 plus VAT per day will be charged for each transparency which retained longer than 14 days. The daily rate per transparency was many times greater than was usual. However, nothing was done by Interfoto to draw Stiletto attention to this unusual term. Stiletto returned the transparencies 4 weeks later and Interfoto claimed £3,783.50. The Court of Appeal held that the term was not incorporated because the Stiletto was given any notice of the term.<sup>16</sup>

The objective standard of consent also appears in §2 of the US Restatement Second of Contract (1981) (hereinafter Rest 2d Contr). §2(1) of the Rest 2d Contr states that:

“(1) A promise is a manifestation of intention to act or refrain from acting in a specified way, so made as to justify a promise in understanding that a commitment has been made.”<sup>17</sup>

Dalton explained that the term “manifestation of intention” means that objective consent standard applies to determine whether the parties have consented to the

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<sup>15</sup>[1989] Q.B. 433.

<sup>16</sup>Ibid, p.439, 445.

<sup>17</sup>Comment b on §2 of the US Restatement Second of Contract (1981).

contract.<sup>18</sup> In fact, that is true. The Comment on §2(1) of the Rest 2d Contr provides that:

“The phrase “manifestation of intention” adopts an external or objective standard for interpreting conduct; it means the external expression of intention as distinguished from undisclosed intention.”<sup>19</sup>

Opposite to the subjective consent theory, the objective consent theory “does not seek to examine the subjective state of mind of the parties”.<sup>20</sup> Objective consent “refers to party’s apparent intention reasonably interpreted from his conduct in all circumstances”.<sup>21</sup> Objective consent is not concerned with “whether the parties are in genuine agreement, but only whether they appear to be in agreement.”<sup>22</sup> This means that in the context of B2C e-commerce transactions, if the business discloses to the consumer the whole online B2C contract that includes the arbitration clause and the consumer accepts the contract, the consumer will be obliged by the arbitration clause regardless of whether the business has given him specific notice of the arbitration clause.<sup>23</sup> This situation is exemplified in the case of *Lieschke v RealNetworks, Inc.*<sup>24</sup> In this case, the United States District Court, N.D. Illinois held that an arbitration clause that was included in RealNetworks licensing agreement, which the user had to accept before downloading the software, enforceable.<sup>25</sup>

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<sup>18</sup>C. Dalton, “An Essay in the Deconstruction of Contract Doctrine”, (1985) 94 Yale. L. J.997, 1039, 1040.

<sup>19</sup>Comment b, note 15 supra.

<sup>20</sup>Mckendrick, note 12 supra, p.24.

<sup>21</sup>Mindy Chen-Wishart, *Contract Law*, (1<sup>st</sup> edn, OUP, Oxford, 2005), p.54.

<sup>22</sup>*Ibid*

<sup>23</sup> However, in limited situations US Courts have found the arbitration clause procedurally unconscionable when the business tried to prevent the consumer from knowing that there is an arbitration clause in the contract. See section 2.2 of this chapter.

<sup>24</sup>Not Reported in F.Supp.2d, Westlaw citation is only available, 2000 WL 198424 (N.D.Ill. Feb. 11, 2000)

<sup>25</sup>2000 WL 198424 (N.D.Ill. Feb. 11, 2000)

However, the use of objective consent to decide whether the consumer has consented to an adhesive arbitration clause will not raise consumer confidence in the online arbitral process. This is because it is well-known that consumers rarely read and understand the online adhesion contracts. This is what the author will explain in the coming section.

### **1.1.1 Reading and Understanding the Contract**

It is true that the consumer is under an obligation to read the online adhesion contract terms.<sup>26</sup> However, the unsophisticated consumer rarely reads adhesion contract terms. If they do read them, they may lack the experience and the knowledge to understand what is meant by arbitration clause and how it differs from court litigation.<sup>27</sup> Evidence for this argument can be deduced from §208(3) of Uniform Computer Information Transactions Act which states that, “(I)f a party adopts the terms of a record, the terms become part of the contract without regard to the party’s knowledge or understanding of individual terms in the record.”<sup>28</sup> The Act obliges the consumer by the contract terms even if the consumer does not read or understand the terms. This means that it is well-recognised that the consumer rarely reads or understands adhesion contract terms. In the same vein, Sternlight emphasised that a consumer rarely reads and understands the adhesion contract that includes the arbitration clause. She observed that:

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<sup>26</sup>E. Allan Farnsworth, *Contracts*, (3<sup>rd</sup> edn, Aspen Law & Business, 1999), p.297

<sup>27</sup>Zachary M. Harrison, “Just Click Here: Article 2B’s Failure to Guarantee Adequate Manifestation of Assent in Click-Wrap Contracts”, (1997-1998) 8 Fordham Intell. Prop. Media & Ent. LJ. 907, 908. William J. Condon, Jr., “Electronic Assent to Online Contracts: Do Courts Consistently Enforce Clickwrap Agreements”, (2003-2004) 16 Regent U. L. Rev. 433, 434.

<sup>28</sup>Uniform Computer Information Transactions Act. Uniform Computer Information Transactions Act aims to regulate software licensing agreements such as the agreement to use Realplayer or other computer operating systems.

“(F)ew, if any, would be foolish enough to argue that most employees and consumers actually read and understand the form contracts that they sign which commit them to binding arbitration.”<sup>29</sup>

David Schwartz also adopts a similar opinion when he explained that:

“Pre-dispute arbitration clauses are ..., in substance, immaterial to the core of the transaction, which would typically centre around price or, in an employment contract, wages. They thus receive little attention from the adherent. Even if the adherent bothers to read and understand the arbitration clause, she is extremely unlikely to be able to assess the value of a judicial forum for future disputes with the drafting party. Unlike the drafting party, who has had such disputes before, and has probably experienced both arbitration and litigation, the adherent is unlikely to have had any such experience and is also unlikely to undertake the time and expense to research the implications of an arbitration clause or obtain legal advice.”<sup>30</sup>

Sternlight explained that a consumer’s awareness of the arbitration clause consists of two elements; reading the adhesion contract which includes the arbitration clause and understanding the meaning of the arbitration clause. Schwartz added another issue which is that even if the consumer reads and understands the arbitration clause, he is not likely to have enough experience to appreciate the difference between arbitrating and litigating the dispute. In their article, published in 1996, Carrington and Haagen explained the effect of a consumer’s awareness of the arbitration clause on the reality of his consent to that clause.<sup>31</sup> They asserted that:

“It was ... perceived by at least some courts that the existence of genuine mutual assent was suspect when parties agreed to arbitrate a future dispute, and that a dispute resolution clause could be a trap for the unwary. As one court put it: “[b]y first making the contract and then declaring who should

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<sup>29</sup>Jean R. Sternlight, “Panacea or Corporate Tool?: Debunking the Supreme Courts Preference for Binding Arbitration”, (1996) 74 Wash. U.L.Q. 637, 676. ( hereinafter Panacea).

<sup>30</sup>David S. Schwartz, “Enforcing Small Print to Protect Big Business: Employee and Consumer Rights Claims in an Age of Compelled Arbitration”, (1997) Wis. L. Rev.33, 56-57. (hereinafter Enforcing).

<sup>31</sup>Carrington and Haagen, note 2 supra, p.340, quoting *Parsons v Ambos.*, 48 S.E. 696 (Ga. 1904)

construe it, the strong could oppress the weak, and in effect so nullify the law as to secure the enforcement of contracts usurious, illegal, immoral, or contrary to public policy.”<sup>32</sup>

In 1998, Prof. Ware wrote an article in reply to Carrington and Haagen and, in his article, he quoted the above mentioned quotation and he analysed it in this way. Carrington and Haagen highlighting two points; first, the consumer’s assent to an adhesive arbitration clause is not as genuine as the consent to a submission agreement because, when the consumer accepts a submission agreement he will pay more attention to the risks associated with choosing to arbitrate rather than litigate or using any other method of dispute resolution.<sup>33</sup> The second point that Carrington and Haagen made is that by including an arbitration clause in the adhesion contract, the consumer substitutes the judicial system with private dispute resolution and this might lead to the enforcement of contracts that would not be enforced in court.<sup>34</sup> Prof. Ware added that the enforcement of contracts that would not be enforced in court is also visible in arbitration conducted pursuant to a submission agreement. Prof. Ware concluded his analyses by saying that the two points that Carrington and Haagen made “collapse into one”<sup>35</sup> point which is that:

“(T)he case for denying enforcement to pre-dispute arbitration agreements rests on the belief that consumers signing such agreements do not ‘genuinely’ assent because they are inattentive to the hazards of dispute resolution and are unlikely to be well-advised”<sup>36</sup>

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<sup>32</sup>Carrington and Haagen, *supra* note 2, p.340, quoting *Parsons v Ambos.*, 48 S.E. 696 (Ga. 1904)

<sup>33</sup>Stephen J. Ware, “Consumer Arbitration as Exceptional Consumer Law (With a Contractualist Reply to Carrington & Haagen)”, (1998) 29 McGeorge L. Rev. 195, 198. (hereinafter Reply).

<sup>34</sup>*Ibid.*, p.199

<sup>35</sup>*Ibid.*

<sup>36</sup>*Ibid.*,p.200.



Prof. Ware also added that if we consider the consumer's consent to the arbitration clause to be non-genuine just because of the poor attention that the consumer gives to risks associated with these kinds of clauses at the time of contracting, this means that the consumer's consent to other types of clauses included in the contract of adhesion is also not genuine.<sup>37</sup> The reason is that consumers do not pay attention to the risks associated with many other clauses included in the adhesion contract.<sup>38</sup> Therefore, if we rely on the fact that consumers do not pay attention to the risks associated with the arbitration clause, to render it unenforceable, many other terms in the contract would also be considered unenforceable.<sup>39</sup>

At first glance, Prof. Ware's argument seems to be logical. However, if one thinks deeply about the risks associated with the arbitration clause, one will find that, unlike other terms in the contract, the risks associated with the arbitration clause might affect any right or obligation derived from other terms.<sup>40</sup> For example, an arbitration clause precludes a consumer's right to go to court, as has been mentioned above by Carrington and Haagen and approved by Prof. Ware himself, a contract might be abandoned by the court because it is illegal but, at the same time, if this contract is submitted to arbitration, it might be approved.<sup>41</sup> Such a situation may happen in arbitration and the reason is that the scope of challenging an arbitral award

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<sup>37</sup>Ware, Reply, note 33 supra,p.198.

<sup>38</sup>Ibid.

<sup>39</sup>Ibid.

<sup>40</sup>Shelly Smith, "Mandatory Arbitration Clauses in Consumer Contracts: Consumer Protection and the Circumvention of the Judicial System", (2000-2001) DePaul L. Rev. 1191, 1234.

<sup>41</sup>Ware, (Reply), supra note. 33, p.200. Also see - Carrington and Haagen, note 2 supra, p.340

on point of the law is very limited.<sup>42</sup> Furthermore, understanding the risks associated with the arbitration clause require more sophistication than understanding the risks associated with other terms in the contract. This sophistication needs experience and specialized legal knowledge which the consumer cannot be expected to have at the time of concluding the contract. This is because not every consumer has legal knowledge and it is too costly for him to obtain legal advice just to conclude a contract to buy household or personal use materials.<sup>43</sup>

In another article that has recently been published, Prof. Ware insisted that the fact that the consumer did not read or understand the arbitration clause should not be considered as affecting his acceptance of that clause. This is because the unknowing consent standard is an ordinary contract law rule that not only applies to arbitration clauses but also to other contractual terms. Prof. Ware observed that:

“As with contracts generally, courts find consent to arbitration in the vast majority of form contracts containing arbitration clauses. The nondrafting party (a consumer, for example) consents to arbitration by signing the form or by manifesting assent in another way, such as by performance of the contract. That the consumer did not read or understand the arbitration clause does not prevent the consumer from consenting to it. Nor does the consumer's ignorance that an arbitration clause is included on the form. These are statements of ordinary, plain-vanilla contract law. They are not statements of law peculiar to arbitration clauses. They are the way contract law treats form contract terms generally. The norm in contract law is consent to the unknown.”<sup>44</sup>

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<sup>42</sup>Mark E. Budnitz, “Arbitration of Disputes between Consumers and Financial Institutions: A Serious Threat to Consumer Protection”, (1995) 10 Ohio St. J. on Disp. Resol. 267, 284.

<sup>43</sup>Paul D. Carrington, “Regulating Dispute Resolution Provisions in Adhesion Contracts”, (1998) 35 Harv. J. on Legis. 225, 226.

<sup>44</sup>Ware, (Jury), note 4 supra, p. 171.

Prof. Ware views the use of the unknowing consent standard to validate adhesive arbitration clauses as legitimate because the unknowing consent standard is a rule of contract law that is not specifically designed to apply to an adhesive arbitration clause but it applies to all adhesive contract terms. In other words, Prof. Ware says that this is the general rule of contract law and it has to be applied to arbitration clauses since the FAA treats an arbitration agreement like any other contract. Those who resist the use of the unknowing consent standard to validate adhesive arbitration clauses should accept this fact because this is normal according to the principles of contract law. However, the problems that arise from the application of ordinary contract law principles to B2C adhesive arbitration clauses cannot be justified by the fact that these rules also apply to other different types of contracts. What is more, evidence on the inappropriateness of treating adhesive arbitration clauses like an ordinary contract can be derived from the legislative history of the FAA. The evidence is exemplified by the fact that the FAA was not enacted to apply to adhesive arbitration clauses. However, the policy that favours arbitration which the US Supreme Court created led to the application of the FAA to adhesive arbitration clauses.

The FAA was introduced to the US Senate in the course of the Sixty Seventh Congress;<sup>45</sup> in the fourth session, but the bill was not passed until the next session.<sup>46</sup> In the fourth session, Members of the Senate showed their concern that the FAA may be used to impose arbitration through adhesion contracts on consumers and

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<sup>45</sup>S. 4214, 64 Cong. Rec. 732 (1922).

<sup>46</sup>65. Cong. Rec. 8500 (1924).

employees. Mr. Platt who was the Chairman of the ABA Committee on commerce, trade and commercial law, testified before the Committee on the Judiciary when Mr. Furuseth showed concern that the FAA bill would allow employers to force their employees to arbitrate their disputes with them. Mr. Platt replied saying that:

“(I)t is purely an act to give the merchants the right or the privilege of sitting down and agreeing with each other as to what their damages are, if they want to do it. Now, that is all there is in this.”<sup>47</sup>

It is clear from Mr. Platt’s statement that the FAA was enacted to give effect to arbitration clauses included in commercial contracts between businesses with similar bargaining powers. In other words, the FAA was not designed to apply to arbitration clauses in B2C contracts where the bargaining power seriously differs between the business and the consumer. Senator Walsh of Montana raised the question of voluntarism and he noted:

“The trouble about the matter is that a great many of these contracts that are entered into are really not voluntarily [sic] things at all. Take an insurance policy; there is a blank in it. You can take that or you can leave it. The agent has no power at all to decide it. Either you can make that contract or you can not make any contract. It is the same with a good many contracts of employment. A man says "These are our terms. All right, take it or leave it." Well, there is nothing for the man to do except to sign it; and then he surrenders his right to have his case tried by the court, and has to have it tried before a tribunal in which he has no confidence at all.”<sup>48</sup>

Senator Walsh raised the concern that the provisions of section 2 of the FAA can be used to coerce consumers to arbitrate their future disputes with businesses through adhesion contracts that are introduced to the consumer on a take-it-or-leave-it basis,

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<sup>47</sup> Sales and Contracts to Sell in Interstate Commerce and Foreign Commerce, and Federal Commercial Arbitration: Hearing before a Subcomm. Of the Comm. On the Judiciary, S. 4213 and S. 4214, 67<sup>th</sup> Cong. 9 (1923).

<sup>48</sup>Note 45 supra.

and he gave an example of one of the most well-known B2C adhesion contracts in that time which is insurance policy. Senator Platt assured Senator Walsh that the FAA was not intended to cover insurance contracts. The protection of the weaker party, such as the consumer was also the subject of hot debate in the next congressional session in which the FAA was passed. The debate between the drafter of the bill and the chairman of the committee shows the issue of the protection of the weaker party, such as the consumer. In this debate, Mr. Cohen and the Chairman noted that:

“Mr. Cohen: But the fundamental reason for it [hostility to arbitration], when you come to dig into the history of it--the real fundamental cause was that at the time this rule was made people were not able to take care of themselves in making contracts, and the stronger men would take advantage of the weaker, and the courts had to come in and protect them. And the courts said, “If you let the people sign away their rights, the powerful people will come in and take away the rights of the weaker ones.” And that still is true to a certain extent . . . .

The Chairman: I just want to say this, in answer to what you have last said: There are certain contracts to-day [sic] between the railroads and the shippers in which there is an agreement to arbitrate, and the representation is made to the shipper, “You can take it or leave it, just as you please; but unless you sign you can not ship.”

Mr. Cohen: There is nothing to that contention, Mr. Chairman, for this reason: In the first place, we have the bills of lading act, and the bills of lading act contains the terms of the bill of lading. And that is a protection to the shipper.

And then we have the regulation of the Federal Government, through its regularly constituted bodies, and they protect everybody. Railroad contracts and express contracts and insurance contracts are provided for. You can not get a provision into an insurance contract to-day [sic] unless it is approved by

the insurance department. In other words, people are protected to-day [sic] as never before.”<sup>49</sup>

This debate shows that the FAA was not intended to apply to any adhesive arbitration clause. The reason is that the FAA does not expressly state that it does not apply to B2C adhesive arbitration clauses is that adhesion contracts were not so popular in B2C contracting by that time.<sup>50</sup> There is nothing in the legislative history of the FAA that supports the applicability of the FAA to B2C adhesion contracts.

The federal policy that favours arbitration, which the US Supreme Court created, is the reason for the application of the FAA to B2C adhesive arbitration clauses. The federal policy that favours arbitration as a method of dispute resolution started with the case of *Moses H. Cone Memorial Hospital v Mercury Construction*.<sup>51</sup> In this case, Justice Brennan from the US Supreme Court delivered the opinion of the court and he asserted that:

“questions of arbitrability must be addressed with a healthy regard for the federal policy favouring arbitration.... The Arbitration Act establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favour of arbitration...”<sup>52</sup>

The US Supreme Court explained that the FAA establishes a federal policy that favours arbitration. However, the Court did not explain how the FAA establishes this policy. In fact, the federal policy that favours arbitration is created by the US

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<sup>49</sup> Arbitration of Interstate Commercial Disputes: Joint Hearing before the Subcomm. of the Comm. on the Judiciary, 68<sup>th</sup> Cong. 17 (1924).

<sup>50</sup> The first research paper to define adhesion contract was published by Prof. Kessler in 1943. Friedrich Kessler, “Contracts of Adhesion-Some Thoughts about Freedom of Contract”, (1943) 43 Colum. L. Rev. 629, 632.

<sup>51</sup> 460 US 1 (1983)

<sup>52</sup> Ibid.

Supreme Court itself. In the case of *Circuit City v Adams*,<sup>53</sup> Steven J, dissented and asserted that:

“Times have changed. Judges in the 19th century disfavored private arbitration. The 1925 Act was intended to overcome that attitude, but a number of this Court’s cases decided in the last several decades have pushed the pendulum far beyond a neutral attitude and endorsed a policy that strongly favors private arbitration.”<sup>54</sup>

The FAA was simply enacted to stop the US Courts’ hostility towards arbitration clauses. In other words, its purpose is ensuring the enforcement of arbitration clauses. However, it is not intended to apply to all arbitration clauses. It only applies to “privately negotiated” arbitration clause. In the case of *Dean Witter Reynolds, Inc. v Byrd*,<sup>55</sup> Justice Marshall delivered the opinion of the US Supreme Court and he explained that:

“(T)he legislative history of the Act establishes that the purpose behind its passage was to ensure judicial enforcement of privately made agreements to arbitrate... The Act, after all, does not mandate the arbitration of all claims, but merely the enforcement ... of privately negotiated arbitration agreements.”<sup>56</sup>

Similarly, in the case of *Volt Info. Science v Leland Stanford JR. U.*,<sup>57</sup> Chief Justice Rehnquist delivered the opinion of the US Supreme Court and he asserted that “Arbitration is ... a matter of consent, not coercion”.<sup>58</sup> He also explained that “(T)he

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<sup>53</sup>532 US 105, 121, S. Ct. 1302, 1318, 149 L. Ed. 2d 234 (2001).

<sup>54</sup>*Ibid.*

<sup>55</sup>470 US 213 (1985).

<sup>56</sup>*Ibid.*

<sup>57</sup>489 US 468 (1989)

<sup>58</sup>*Ibid*

FAA ... simply requires courts to enforce privately negotiated agreements to arbitrate, like other contracts, in accordance with their terms.”<sup>59</sup>

One might say that arbitration clauses are freely negotiated even if they are included in an adhesion contract. This is because the consumer has the right to refuse the whole contract including the arbitration clause. Prof. Ware adopted this opinion and he explained that “[T]he consumer is free to put the pen down without signing the form”.<sup>60</sup>

However, the consumer’s ability to leave the contract is met with serious impediments. The seller might be the only provider for the type of goods or services the consumer needs<sup>61</sup> and if we say that the online market is competitive and the notion of monopoly is not present and the consumer can shop for better terms,<sup>62</sup> we will be faced by the fact that consumer may not know about the existence of the arbitration clause, especially as mentioned supra the consumer rarely reads the adhesion contract.

The federal policy that favours arbitration has been used to legitimise adhesive arbitration clauses in B2C and employment contracts. For example, in the case of *Gilmer v Interstate/Johnson Lane Corp.*,<sup>63</sup> the US Supreme Court relied on the federal policy that favours arbitration to enforce an arbitration clause in an adhesion

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<sup>59</sup>489 US 468 (1989)

<sup>60</sup>Ware, (Reply), note.33 supra, p.201.

<sup>61</sup>Kessler, note 50 supra, p.632.

<sup>62</sup>Henry H. Perritt, Jr., “Dispute Resolution in Cyberspace: Demand for New Forms of ADR”, (2000) 15 Ohio St. J. on Disp. Resol. 675, 699.

<sup>63</sup>500 US 20 (1991).



employment contract.<sup>64</sup> In the case of *Allied-Bruce Terminix Companies v Dobson*,<sup>65</sup> Breyer, J., relied on economic benefits to justify the inclusion of arbitration clauses in B2C adhesion contracts. He asserted that:

“We agree that Congress, when enacting this law, had the needs of consumers, as well as others, in mind.... (the Act, by avoiding the delay and expense of litigation, will appeal to big business and little business alike . . . corporate interests [and] . . . individuals).”<sup>66</sup>

The Supreme Court referred to an important point which is that the economic benefits that business gains from cheapness and quickness of arbitration will be transferred to the consumer. This is because business will be able to sell products and services for cheaper prices while still being able to make a profit.<sup>67</sup> Prior to *Allied-Bruce* this opinion was used by the US Supreme Court to justify the imposition of the forum selection clause on cruise tickets. In the case of *Carnival Cruise Lines, Inc. v Shute*,<sup>68</sup> the respondent, the couple Shute bought tickets for a sea tour from Carnival Cruise Lines. The tickets included a forum selection clause that obliged the parties to file any dispute in the courts of the state of Florida.<sup>69</sup> Mrs. Shute suffered injuries when she slipped on a deck mat.<sup>70</sup> The Shute couple brought an action in the Federal District Court of Washington which awarded summary judgment for Carnival.<sup>71</sup> The Court of Appeal reserved the judgment and refused to

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<sup>64</sup>500 US 20, 21 (1991).

<sup>65</sup>513 US 265 (1995).

<sup>66</sup>*Ibid*

<sup>67</sup>*Ibid*

<sup>68</sup>499 US 585, 111 S.Ct. 1522, 113 L. Ed.2d 622 (1991).

<sup>69</sup>*Ibid*

<sup>70</sup>*Ibid*

<sup>71</sup>*Ibid*

enforce the forum selection clause because it was not freely negotiated.<sup>72</sup> The US Supreme Court reserved the Court of Appeal decision and enforced the forum selection clause and it gave many justifications for its decision, one of which was the following:

“a clause establishing ex ante the forum for dispute resolution has the salutary effect of dispelling any confusion about where suits arising from the contract must be brought and defended, sparing litigants the time and expense of pretrial motions to determine the correct forum, and conserving judicial resources that otherwise would be devoted to deciding those motions... it stands to reason that passengers who purchase tickets containing a forum clause like that at issue in this case benefit in the form of reduced fares reflecting the savings that the cruise line enjoys by limiting the fora in which it may be sued.”<sup>73</sup>

The US Supreme Court has explained that the forum selection clause should be enforced because it will help both the business and the consumer to save time and money which they might incur by litigating to determine the correct forum, and the economic benefits which the forum selection clause introduces to the business will be transferred to the consumer through cheaper prices that the business offers the consumer. Advocates of consumer compelled arbitration such as Kaplinsky and Levin, and Christopher Drahozal use a similar rationale to the one mentioned in the case of *Carnival* to justify imposing arbitration clauses on consumer via adhesion contracts. Kaplinsky and Levin do not view compelled arbitration as “anti

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<sup>72</sup>499 US 585, 111 S.Ct. 1522, 113 L. Ed.2d 622 (1991).

<sup>73</sup>Ibid

consumer”, on the contrary, they say that it is beneficial for consumers because they benefit from the reduced costs.<sup>74</sup> Christopher Drahozal explained that:

“individuals may be better off agreeing even to one-sided arbitration clauses instead of retaining their right to go to court, if the resulting cost savings are passed on to consumer through reductions in the price of goods and services.”<sup>75</sup>

Drahozal says that consumer arbitration pursuant to an adhesive arbitration clause even if it unfairly favours the business on account of the consumer still being better off since the consumer gains economic advantages from the reduced prices.<sup>76</sup>

It is true that the business might be able to maximize their profit if the arbitral process proves to be cheap and quick. Furthermore, the inclusion of arbitration clauses in B2C adhesion contracts helps the business to make more accurate calculations for future profits. It is also true that this might encourage the business to give consumers reduced prices. However, for this economic rationale to be effective in attracting consumers to take e-commerce contracts with arbitration clauses, the knowing and intelligent standard of consumer consent to arbitration clauses should be applied. The reason is that consumer should know that the reduction in the price is rustled from the fact that the contract includes and arbitration clause.

To sum up this section, business is not obliged to disclose the existence of the arbitration clause to the consumer. This is because consumer assent to the arbitration clause is measured according to the objective standard of consent. Objective

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<sup>74</sup>Alan S. Kaplinsky and Mark J. Levin, “Consumer Financial Services Arbitration: Current Trends and Developments”, (1997-1998) 53 Bus. Law. 1075, 1076.

<sup>75</sup>Ibid

<sup>76</sup>Christopher R. Drahozal, “Unfair Arbitration Clauses”, (2001) U. Ill. L. Rev.696, 741.

standard of consent means that parties will be considered to have consented to the contract if they “appear to be in agreement”. Accepting the whole B2C e-commerce contract is sufficient to consider the consumer consented to the arbitration clause even if he did not read or understand the contract. It is true that consumer is under the obligation to read the contract. Nevertheless, consumers rarely read and understand the terms of B2C e-commerce contracts including the arbitration clause.

## **2. Unfairness and Unconscionability Rules**

Unfairness and unconscionability rules do not place the business under an obligation to give the consumer specific notice of the existence of the arbitration clause in the B2C e-commerce contract. This is because lack of notice alone is insufficient to hold the arbitration clause unfair or unconscionable. This part of the chapter is divided into two sections. The first deals with the UK Unfair Terms in Consumer Contracts Regulations 1999.<sup>77</sup> The second deal with the unconscionability test that is used in the US to strike unfair arbitration clauses.

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<sup>77</sup>Unfair Terms in Consumer Contracts Regulations 1999, (SI 1999/2083). What should be mentioned here is that the Unfair Contract Terms Bill if adopted will replace the 1999 Regulations. §4(1) of the Bill test includes the fairness test. It provides that “if a term of a consumer contract is detrimental to the consumer, the business cannot rely on the term unless the term is fair and reasonable”. However, it is not clear when courts will consider a contractual term fair and reasonable.

## 2.1 Unfairness

In the England, arbitration clauses in B2C contracts are subject to the unfairness test embedded in Regulation 5(1) of the Unfair Terms in Consumer Contracts Regulations 1999.<sup>78</sup> Regulation 5(1) states that:

“(1) A contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties’ rights and obligations arising under the contract, to the detriment of the consumer.”<sup>79</sup>

In the case of *Picardi v. Cuniberti*,<sup>80</sup> the Court held an adjudication clause that is included in a consumer construction contract to be unfair under Regulation 5(1). The reasons are that first, adjudication clauses are onerous and unusual in consumer construction contract and the adjudication clause was not specifically brought to the attention of the *Cuniberti*. Second, the adjudication costs are high and this caused significant imbalance in the parties’ rights and obligations arising under the contract, to the detriment of the *Cuniberti*. In the case of *Mylcris Builders Ltd v Buck*,<sup>81</sup> Buck had contracted with Mylcris to build an extension to her bungalow. She signed a standard contract, which included a clause referring all disputes to arbitration. Mylcris started work, but a dispute later arose between the parties. Mylcris submitted the dispute to arbitration, but following advice that the arbitration clause could be unfair, Buck refused to submit to the arbitration. Mylcris sought to enforce the award. However, the Court refused to enforce the award because it held the arbitration clause unfair. The Court explained that, the fees payable to the arbitrator

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<sup>78</sup>Unfair Terms in Consumer Contracts Regulations 1999, (SI 1999/2083).

<sup>79</sup>*Ibid*

<sup>80</sup>[2002] EWHC 2923 (QB).

<sup>81</sup>[2008] EWHC 2172 (TCC).

were significant compared with the claim. In addition, although Buck had signed the contract containing the arbitration clause, its impact would not have been apparent to a lay person and had not been apparent to Buck, as evidenced by her subsequent conduct. The requirement of fair and open dealing meant that the clause and its effects needed to be more fully, clearly and prominently set out than they were in the instant case. The arbitration clause was not binding on B and the award did not fall to be enforced.<sup>82</sup>

However, lack of notice alone does not render the arbitration clause unfair under the unfairness test embedded in Regulation 5(1). This is because the unfairness test under Regulation 5(1) is a combined test which consists of two requirements. These two requirements are good faith and significant imbalance<sup>83</sup> and both of them must be satisfied in order to consider the term unfair. In other words, an arbitration clause will only be considered unfair if it is introduced to the consumer in a way contrary to the requirement of good faith and, at the same time the arbitration clause significantly favours the business over the consumer.<sup>84</sup>

In trying to expand the protection awarded to the consumer by subsection 5(1), some academic writers have argued that subsection 5(1) can be interpreted in a way that

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<sup>82</sup>[2008] EWHC 2172 (TCC).

<sup>83</sup>Gianluca sepe, "National Models of European Contract Law: A Comparative Approach to the Concept of Unfairness in Directive 93/13", (1997) 5(4) Consum. L.J. 115, at p.116-117.

<sup>84</sup>What should be mentioned here is that schedule 2 of the Unfair Terms in Consumer Contract Regulations 1999 mentions a list of terms that may be regarded as unfair. Term (i) states that a term may be regarded as unfair if it is "irrevocably binding the consumer to terms with which he had no real opportunity of becoming acquainted before the conclusion of the contract". However, this term does not directly invalidate the contractual term with which the consumer has the chance to become familiar. The assessment of the fairness of the term has to be measured according to Regulation 5(1). This is because the list which includes the term is not binding. For more information about the nature of this list see section 2.3 of chapter 4.

would allow invalidating an arbitration clause even though it only satisfies one of the two requirements. Susan Bright explained that procedural unfairness is measured by the good faith doctrine and the substantive unfairness is assessed in accordance with the amount of imbalance in interests that a term causes to the consumer.<sup>85</sup> In Hugh Collins's point view, either of procedural or substantive bad faith is sufficient to consider the term unfair. He pointed out that:

“the directive proposes two tests of unfairness, one directed at the substance of the terms, and the other at their form. The most penetrating line of attack on unfair contract terms, however, is opened up by combination of form and substance.”<sup>86</sup>

Tenreiro, who participated in drafting the unfair terms directive, adopts an approach which is different from Collins's approach. Tenreiro pointed out that subsection 5(1) involves one test; nonetheless, this test is based on significant imbalance only. He observed that:

“the principle of good faith is not a supplementary requirement that must be added to the criterion of ‘significant imbalance’ as some author seems to consider. Let us be clear: there is no way that a contractual term which causes ‘a significant imbalance in parties’ rights and duties arising under the contract to the detriment of the consumer can conform with the requirement of ‘good faith’. Indeed, the opposite is true: a term is always regarded as contrary to the requirement of ‘good faith’ when it causes such an imbalance. What the principle of good faith adds is something that the criterion of significant imbalance alone could not provide us with: namely, decades of national case-law and doctrine.”<sup>87</sup>

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<sup>85</sup>Susan Bright, “Winning the Battle against Unfair Contract Terms”, (2000) 20(3) LS. 331, 347.

<sup>86</sup>Hugh Collins, “Good Faith in European Contract Law”, (1994) 14 O.J.L.S. 229, 246. (hereinafter Good Faith).

<sup>87</sup>Mario Tenreiro, “The Community Directive on Unfair Terms and National Legal System”, (1995) 3 Euro. Rev. Priv. L. 273,279.

Bright and Collins have adopted the widest possible interpretation for the fairness test. Tenreiro tried to draw our attention to that ‘significant imbalance’ is the main test for measuring unfairness of contractual term. In other words, if the term causes significant imbalance to the detriment of the consumer, then the term is unfair. This is because every term that causes significant imbalance is always against the requirement of good faith. The interpretation introduced by Bright, Collins, and Tenreiro cannot be acceptable. One reason is that the wording of subsection 5(1) does not support these interpretations. Regarding the interpretation which says that good faith and significant imbalance are two separate tests, Regulation 5(1) states that “A contractual term shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance... to the detriment of the consumer”. If good faith and significant imbalance are meant to be two separate tests, then the language of Regulation 5(1) would appear in a formulation which says that the contractual term is unfair if it is either contrary to good faith or it causes significant imbalance to the consumer. In other words, the formulation of the words in Regulation 5(1) does not support the separation between good faith and significant imbalance. Regarding the interpretation which says that the test is all about significant imbalance, if the test of unfairness is the ‘significant imbalance’, then why does subsection 5(1) mention the requirement of good faith? Moreover, the drafters of the directive, which the 1999 Regulations implement, have an intention to give good faith a role in deciding the fairness of any term in the B2C contract. This can be detected from recital 16 of the directive. The recital pointed out that:



“Whereas the assessment, according to the general criteria chosen, of the unfair character of terms, in particular in sale or supply activities of a public nature providing collective services which take account of solidarity among users, must be supplemented by a means of making an overall evaluation of the different interests involved; whereas this constitutes the requirement of good faith; whereas, in making an assessment of good faith, particular regard shall be had to the strength of the bargaining positions of the parties, whether the consumer had an inducement to agree to the term and whether the goods or services were sold or supplied to the special order of the consumer; whereas the requirement of good faith may be satisfied by the seller or supplier where he deals fairly and equitably with the other party whose legitimate interests he has to take into account;”<sup>88</sup>

Recital 16 involves some elements which have no real role in deciding the fairness of any term<sup>89</sup> such as reference to ‘sales and activities of a public nature’. Yet, recital 16 highlights a very important issue about the interpretation of the requirement of good faith in the directive. Recital 16 spells out the standards that should be used in evaluating the fairness of a term in B2C contract. All of these standards relate to the procedural phase of the contracting process such as difference in bargaining power and the opportunity to examine the terms. Consequently, the requirement of good faith in the regulation is mainly designed to examine the procedural fairness of the contracting process. The principle of good faith in the regulations is not equivalent to the general doctrine of good faith known in continental legal systems. Therefore, good faith principle in the directive does not transfer the doctrine of good faith known in civil law countries to other EU member states. Any term that contradicts the general doctrine of good faith will be regarded as unfair. However, the directive simply establishes a fairness test of which procedural good faith is part.

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<sup>88</sup>Recital 16 of the Unfair Contract Terms Directive.

<sup>89</sup>Geraint Howells, “Good Faith in Consumer Contracting”, in Roger Brownsword, Norma J. Hird and Geraint Howells (eds), *Good Faith in Contract: Concept and Context*, (Ashgate, Aldershot ,1999), p.94.

The strongest evidence to prove the fact that good faith and significant imbalance are two requirements that form one combined test can be found in the House of Lords' holdings in the case of *The Director General of Fair Trading v First National Bank Plc*.<sup>90</sup> Lord Bingham has made very important observations which established a principle in defining unfairness under the regulations. In this case, the First National Bank plc (hereafter 'the bank') is one of the biggest lenders in the UK market. It concludes loan agreements with borrowers using a standard form contract governed by the Consumer Credit Act 1974. One of the standard terms states that if the borrower fails to pay an instalment, the bank has the right to request the instalment plus the interest at the rate determined in the loan agreement. Moreover, in the situation where legal action is conducted, the interest would be payable at the same rate on the judgment. Banks usually insert this term because according to the Consumer Credit Act 1974, regulated consumer credit agreements are subject to the jurisdiction of the county court. County courts do not have the power to grant interest on the judgment, unless the Lord Chancellor gives the county court permission to do so. However, what usually takes place is that the dispute between the bank and the borrower is settled without hearing and the borrower agrees to pay off the debt by instalments. After the borrower pays off the debt by instalments, he finds that there is an extra sum to pay and this sum is interest on the judgment. The Director General (hereafter the Director) argues that this type of term is not unfair because, when the borrower took out the loan, the loan agreement did not provide the borrower with clear information that interest will be charged on the judgment. The Director also argued that borrowers did not have the chance to apply for time

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<sup>90</sup>[2001] WL 1171932 (HL)

orders under the Consumer Credit Act 1974 which could have provided that interest must not be collected on the judgment. The bank alleged that the fairness test in the regulations does not apply to the term in dispute and the term is not unfair. At the Court of First Instance Evans-Lombe J refused to consider the term unfair. The Court of Appeal rejected the Court of First Instance's decision and it found that the term is not fair because it "does create unfair surprise" to the borrower. The House of Lords rejected the Court of Appeal decision and held that the term is fair. However, since this case is the first case that involves a claim to invalidate a term in a B2C contract on the basis of the unfairness test, many important principles have been established through this case. At the Court of First Instance Evans-Lombe J observed that:

"The origin of the Regulations of 1994 is European Council Directive 93/13. It is clear therefore, that the words "good faith" are not to be construed in the English law sense of absence of dishonesty but rather in the continental "civil law" sense .... Given such construction of the words "good faith" as they appear in regulation 4(1) it may be thought that the words "causes a significant imbalance in the parties' rights" adds little. If the term complained of, either substantively or as a result of the procedure by which the consumer becomes subject to it, causes a significant imbalance in the parties' rights and obligations under the contract to the detriment of the consumer, it will be in breach of the requirement of good faith. In practice a court considering whether a given term of a contract is an "unfair term" will look at all the circumstances of the case and its judgment will be based on an amalgam of perceived substantive and procedural unfairness." <sup>91</sup>

Evans-Lombe J refused to consider the term unfair. However, the interesting thing about his judgment is the way he analysed the fairness test in the regulations. He considers 'good faith' as the main test and it should be construed according to its

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<sup>91</sup>[2000] 1 W.L.R. 98. This case was governed by the Unfair Contract Terms Regulations 1994. However, the fairness test in section 4(1) is the same test used in section 5(1) of the 1999 regulations.

civil law origins. As has been mentioned above ‘good faith’ in the civil system covers both procedural and substantive fairness. In this sense, either procedural or substantive bad faith is enough to render the term unfair. The Director then appealed to the Court of Appeal in which Peter Gibson, Waller and Buxton L.JJ ruled for the unfairness of the clause. However, the bank appealed to the House of Lords. In his judgment, the House of Lords has established a set of principles that are very important in examining the fairness of any term in B2C contracts under the regulations. Lord Bingham explained the fairness test. His Lordship observed that:

“the test laid down by the regulations 4(1), deriving as it does from article 3(1) of the directive, has understandably attracted much discussion in academic and professional circles and helpful submission were made to the House on it. It is plain from the recital to the directive that one of its objectives was partially to harmonise the law in this important field among all member states of the European Union. The member states have no common concept of fairness or good faith, and the directive does not purport to state the law of any single member state. It lays down a test to be applied, whatever their pre-existing law, by all member states. If the meaning of the fairness test were doubtful, or vulnerable to the possibility of differing interpretation in differing member states, it might be desirable or necessary to seek a ruling from the European Court of Justice on its interpretation. But the language used in expressing the test, so far as applicable in this case, is in my opinion clear and not reasonably capable of differing interpretations. A term falling within the scope of the regulations is unfair if it causes a significant imbalance in the parties’ rights and obligations under the contract to the detriment of the consumer in a manner or to an extent which is contrary to the requirement of good faith.... Regulation 4(1) lays down a composite test, covering both the making and the substance of the contract, and must be applied bearing clearly in mind the objective which the regulations are designed to promote.”<sup>92</sup>

Opposite to both the Court of First Instance and the Court of Appeal, Lord Bingham refused the presumption that the principle of ‘good faith’ should be interpreted according to its civil law origins. Lord Bingham asserted that the regulations are

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<sup>92</sup>[2001] WL 1171932 (HL).

very clear and it establishes one combined test. The components are good faith which he defines as “fair and open dealing”<sup>93</sup> and “significant imbalance” which in his opinion is satisfied if the term “so weighted in favour of the supplier as to tilt the parties' rights and obligations under the contract significantly in his favour”<sup>94</sup>.

## **2.2 Unconscionability**

Unconscionability is a contract law defence that invalidates an unfair contractual term. It originated in US common law of contract.<sup>95</sup> However, nowadays it is embedded in §2 and 2A of the United States Uniform Commercial Code (hereinafter UCC) which applies to the sale and lease of goods. Unconscionability is divided into procedural and substantive. The former examines the fairness of the contracting process and the latter examines the fairness of the substance of the contract.<sup>96</sup> It is possible to invalidate a contractual term because it is either procedurally or substantively unconscionable.

Few US Federal Courts have considered consumer knowledge of the arbitration clauses as reason for the unconscionability of that clause. However, the lack of specific notice of the arbitration clause alone would not lead to the procedural

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<sup>93</sup>[2001] WL 1171932 (HL).

<sup>94</sup>Ibid

<sup>95</sup>F. Paul Bland, Jr., note 10 supra, p.49. What should be mentioned here is that The Restatement (Second) of Contracts establishes a fairness test to meet the fact that consumers accept the adhesion contracts without reading contract terms. §211(3) of the Restatement states that “[W]here the other party has reason to believe that the party manifesting such assent would not do so if he knew that the writing contained a particular term, the term is not part of the agreement.” However, this test is rarely used to vacate arbitration clauses or any other adhesive contractual term. This is because it is hard to satisfy the requirement of this test. In respect of notice of the arbitration clause, lack of notice alone does not satisfy this test. This is because as the drafters of the Restatement explained, to invalidate a contractual term on the basis of this test “the terms must not only be surprising, but also highly adverse to the deal”. See Comment on §211 of the Restatement (Second) of Contracts 1981.

<sup>96</sup>Paul Bland, Jr., note 10 supra, p.55.

unconscionability of that clause. In the case *Geiger v Ryan's Family Steak Houses, Inc.*,<sup>97</sup> the plaintiffs argued that an arbitration clause that is included in an adhesion employment contract is procedurally unconscionable. The plaintiffs were high school graduates who had to fill out Ryan's standard employment application packets. The application packets included the agreement to arbitrate, the Rules of the arbitration provider which is EDSI, and Ryan's application for employment.<sup>98</sup> The United States District Court of South Indiana held the arbitration clause unconscionable and Baker J, explained that:

“We have major doubts that a typical high school graduate would be able to read the multiple documents provided to her at her interview, comprehend the Arbitration Agreement and the EDSI Rules well enough to formulate questions as to their substance, and ask those questions during that interview. Moreover, no ordinary applicant, especially a person seeking a job as a server, could never mind understand, the rights and obligations vested in Ryan's with respect to the arbitration process when she is never apprised of those rights and obligations. These inadequacies make enforcement of the Arbitration Agreement unconscionable against either Geiger or Sadler.”<sup>99</sup>

The Court considered two factors in reaching its conclusion about the unconscionability of the arbitration clause. First, the plaintiffs did not have the chance to read the arbitration clause at the interview. Second, the plaintiff would not understand the arbitration clause if he is not informed about it, as well as if it is not explained to him. The Court did not rely on the issue of specific notice of the arbitration clause alone to rule for the procedural unconscionability of the arbitration clause. The Court looked at the overall circumstances of the case including the issue of notice to decide that the arbitration clause is procedurally unconscionable. In

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<sup>97</sup>134 F.Supp.2d 985 S.D.Ind., 2001.

<sup>98</sup>Ibid, p.989.

<sup>99</sup>Ibid, p.999.

other words, the lack of specific notice of the arbitration clause alone would not render the arbitration clause procedurally unconscionable. The fact that the Court, when deciding the procedural unconscionability of the arbitration clause does not look for specific notice alone but looks at the overall circumstances and this also appears in the case of *Banc One Acceptance Corp. v Hill*.<sup>100</sup> In this case, Hill argued that the arbitration clause is procedurally unconscionable because of two reasons. First, Hill did not read the terms of the contracts that the sales representative asked her to sign and the sales representative did not tell her that she should read the terms of the contract. Second, “no one associated with East Ford ever told her that she was signing an arbitration agreement” or that she could object to the agreement, and no one explained the term “arbitration” to her.<sup>101</sup> The United States District Court for the Northern District of Mississippi accepted her allegations and held the arbitration clause procedurally unconscionable. Banc appealed to the United States Court of Appeal of Fifth Circuit and Edith H. Jones, Circuit Judge explained that:

“In this action, the district court correctly applied the Mississippi Supreme Court's ruling in *Taylor*, which held that an ... arbitration clause was procedurally unconscionable under Mississippi law for a variety of reasons, including the relative position of the parties, the nature of the contract at issue, and the appearance and placement of the arbitration clause relative to the rest of the contract.”<sup>102</sup>

In the case of *East Ford, Inc. v Taylor*,<sup>103</sup> which the Court referred to in the previous case, the Supreme Court of Mississippi explained that:

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<sup>100</sup>367 F.3d 426, 431, 432 (5<sup>th</sup> Cir. 2004).

<sup>101</sup>*Ibid.*

<sup>102</sup>*Ibid.*

<sup>103</sup>826 So.2d 709 Miss., 2002.

“The indicators of procedural unconscionability generally fall into two areas: (1) lack of knowledge, and (2) lack of voluntariness. A lack of knowledge is demonstrated by a lack of understanding of the contract terms arising from inconspicuous print or the use of complex, legalistic language, disparity in sophistication of parties, and lack of opportunity to study the contract and inquire about contract terms. A lack of voluntariness is demonstrated in contracts of adhesion when there is a great imbalance in the parties’ relative bargaining power, the stronger party’s terms are unnegotiable....”<sup>104</sup>

The Supreme Court of Mississippi determined two factors that must be satisfied to hold the clause procedurally unconscionable. First, the contract must be an adhesive contract. Second, the consumer should lack knowledge about the existence of the arbitration clause. However, the lack of knowledge is not directly satisfied by the lack of specific notice of the arbitration clause. The Court explained that lack of knowledge is satisfied by three factors the “inconspicuous print”, “the use of complex language” and “disparity in sophistication of the parties”.<sup>105</sup> None of these factors oblige the business to give the consumer specific notice of the arbitration clause in order to avoid procedural unconscionability.

Regarding the “inconspicuous print”, this refers to the type of font in which the arbitration clause appears compared with the rest of the contract terms and the placement of the arbitration clause compared to the rest of the contract terms. This means that if the arbitration clause is typed in the same font size as the rest of the contract and included in the body of the text of the contract, then it cannot be classified as “inconspicuous print”. An example of this can be seen in the case of *Harris v Green Tree Financial Corp.*<sup>106</sup> Harris argued that the arbitration clause is

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<sup>104</sup>826 So.2d 709, 715, 716 Miss., 2002.

<sup>105</sup>Ibid

<sup>106</sup>183 F.3d 173 C.A.3 (Pa.), 1999.



procedurally unconscionable since it appeared in fine print on the back of the relevant standard form contract. However, the United States Court of Appeal of the Third Circuit refused to hold the arbitration clause unconscionable because it is included in fine print.<sup>107</sup>

Regarding “the use of complex language” and “disparity in sophistication of the parties”, avoiding non-enforcement of an arbitration clause on these two bases does not oblige the business to give notice to the consumer of the existence of the arbitration clause. An evidence for this argument can be found in the case of *Washington Mut. Finance Group, LLC v Bailey*.<sup>108</sup> In this case, the defendants were illiterate people who signed a loan agreement with the plaintiff. The loan agreement contained an arbitration clause. However, the Plaintiff failed to specifically inform the defendants about the arbitration clause. For these reasons the United States District Court for the Northern District of Mississippi held the arbitration clause procedurally unconscionable. However the US Court of Appeal of the Fifth Circuit reserved the decision of the District Court and E. Grady Jolly, Circuit Judge, explained that:

“This case requires us to determine the effect of an individual's illiteracy on the enforcement of an arbitration agreement, which the individual admits he signed, but because of his illiteracy, denies he understood. The district court held that the individual's illiteracy, coupled with a lack of oral disclosure, rendered the agreement procedurally unconscionable. We conclude the district court erred and reserve.”<sup>109</sup>

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<sup>107</sup> 183 F.3d 173, 182, 183 C.A.3 (Pa.), 1999.

<sup>108</sup> 364 F.3d 260 (5th Cir. 2004)

<sup>109</sup> Ibid. p.262.

The Court of Appeal refused the allegation that the illiteracy of the defendants placed the plaintiff under the obligation to notify them about the arbitration clause. If the Court did not consider the business under an obligation to give notice to the consumer about the arbitration clause when the consumer is illiterate, the Court is unlikely to see that the complex language of the contract or the non-sophistication of the weaker party obliges the business to give notice to the consumer of the arbitration clause.

To sum up this section, the business is not obliged to give the consumer specific notice of the existence of the arbitration clause under the 1999 Regulations. This is because procedural bad faith in the contracting process alone does not satisfy the unfairness test embedded in Regulation 5(1). The unfairness test will only be satisfied if the method of introducing the arbitration clause to the consumer contrary to the requirement of good faith and, at the same time, seriously favours the business over of the consumer. In the US, it is possible to invalidate the arbitration clause on this basis of procedural unconscionability. However, the lack of specific notice of the arbitration clause alone does not make it procedurally unconscionable.

### **3. Knowing and Intelligent Standard of Consent is Needed**

In order to guarantee that the consumer is not surprised by the arbitration clause after the contract is concluded, a rule that stipulates knowing and intelligent standard of consent must be in place. The knowing and intelligent standard in this context means that the business must bring the consumer's attention to the arbitration clause and the business must explain the arbitration clause and its effect on the consumer's

legal rights such as the right to litigate disputes in a court of law.<sup>110</sup> After that, the consumer has the choice to either take the contract with the arbitration clause or leave the whole contract. This is the knowing and intelligent standard of consent which differs from the knowing, intelligent, and voluntary standard of consent. The latter would allow the consumer to take the contract even if he refused the arbitration clause.<sup>111</sup> However, such a standard is unlikely to succeed in the context of online B2C e-commerce. Businesses insert the arbitration clause in order to avoid being prosecuted in alien and unknown forums.<sup>112</sup> Therefore, although some businesses might allow the consumer to refuse the arbitration clause and take the contract, it is unlikely that such a model will find popularity amongst members of the business sectors.<sup>113</sup>

There are many ways of implementing the knowing and intelligent standard of consent. One component that must exist in any possible solution is the specific notice which informs the consumer that there is an arbitration clause. One solution is that the business advises the consumer to request the opinion of legal counsel about the arbitration clause and the arbitral process before he concludes the contract.<sup>114</sup> It is true that this approach will guarantee the consumer a greater understanding of the impact of the arbitration clause on his rights. However, this approach seems to be

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<sup>110</sup>F. Paul Bland, Jr., note 10 supra, p.35.

<sup>111</sup>Consumer Arbitration Protocol of the American Arbitration Association allows the consumer to opt out of the arbitration clause and refer to the small claims court.

<sup>112</sup>Born, note 1 supra, p.61.

<sup>113</sup>Some businesses do comply with the Consumer Arbitration Protocol of the American Arbitration Association and they do not oblige the consumer by the arbitration clause. Therefore, some businesses might accept a formulation that allows the consumer to take the contract without the arbitration clause. However, as mentioned in the text, it is unlikely that the business sector will welcome such solution.

<sup>114</sup>Christine M. Reilly, "Achieving Knowing and Voluntary Consent in Pre-Dispute Mandatory Arbitration Agreements at the Contracting Stage of Employment", (2002) 90 Cal. L. Rev. 1203, 1240.

impractical. If the consumer is advised by the business he is dealing with to see a legal counsel, he will probably do so. This will slow down the contracting process, whereas the whole e-commerce sector is based on speed in concluding and performing transactions. It will also increase the transaction costs to the consumer because the consumer's legal counsel will charge fees for their services. The best approach is that the business should consider a separate dispute resolution icon that the consumer must read and specifically accept in order to take the contract. The icon must include sufficient information about the arbitration clause and the arbitral process. The information must be written in clear and easily understandable language.<sup>115</sup> This approach will guarantee that the consumer knows and understands the arbitration clause before he accepts the contract. In other words, it will help to overcome the lack of knowledge and understanding resulting from the fact that consumers do not read the arbitration clause and if they do read it, they may not understand what is meant by arbitration.

#### **4. Conclusion**

In the context of B2C e-commerce, the business bears no obligation to disclose the existence of the arbitration clause to the consumer. The reasons are that first, consumer consent to the arbitration clause is measured according to the objective standard of consent. Objective standard of consent means that parties will be considered to have consented to the contract if they "appear to be in agreement". Accepting the whole B2C e-commerce contract is sufficient to consider that the consumer consented to the arbitration clause even if he did not read or understand

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<sup>115</sup>Reilly, note 114 supra, p.1251.

the contract. It is true that the consumer is under an obligation to read the contract. Nevertheless, consumers rarely read and understand the terms of the B2C contract, including the arbitration clause.

Unfairness and unconscionability rules do not oblige the business to notify the consumer about the existence of the arbitration clause. This is because the lack of specific notice of the arbitration clause alone does not render the arbitration clause unfair or unconscionable. Adopting an international convention that obliges the business to introduce the arbitration clause to the consumer through a special icon will help to notify the consumer about the arbitration clause before he enters into the e-commerce contract.

## **Chapter 4**

# **The Suggested Model for Regulating Arbitration Clauses in Online B2C Contracts Eliminates the Uncertainty about their Enforceability**

In the third chapter, the present author explained that ensuring consumer confidence in online arbitration requires giving him specific notice about the existence of the arbitration clause in the B2C e-commerce contract. However, the business is not under the obligation to do that. Therefore, raising the consumer confidence in online arbitration requires adopting a rule that stipulates the knowing and intelligent standard of consent to online B2C arbitration clauses.

Ensuring that the consumer and the business will agree to arbitrate their e-commerce disputes requires elimination of the impediments that may make them uncertain about the enforceability of the online arbitration clause. As this thesis focuses on raising the consumer confidence in online arbitration, one may say that why would the present author worry about the business. Securing the business consent to arbitrate e-commerce disputes online through an arbitration clause is so important for the consumer. The reason is that it is difficult to secure the business consent after the dispute arises.<sup>1</sup> In most e-commerce disputes, business is not the party that is seeking redress. It is the consumer who will be seeking redress.<sup>2</sup> This is because in most B2C e-commerce contracts, consumers pay before they receive the goods or

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<sup>1</sup>Ethan Katsh and Janet Rifkin, *Online Dispute Resolution: Resolving Conflicts in Cyberspace*, (1<sup>st</sup> edn, Jossey-Bass, San Francisco, 2001), p.56.

<sup>2</sup>Mary Shannon Martin, “Keep it Online: the Hague Convention and the Need for Online Alternative Dispute Resolution in International Business-to-Consumer E-Commerce”, (2002) 20 B.U. Int’l. L.J. 125,130.

the services.<sup>3</sup> A business inserts the arbitration clause into the B2C e-commerce contract in order to avoid uncertainty regarding the possible forum for litigating e-commerce disputes with the consumer.<sup>4</sup> It also helps the business in expecting future dispute resolution costs.<sup>5</sup> Therefore, if the business has doubts regarding the enforceability of the online B2C arbitration clause, the business will not insert it into the B2C e-commerce contract. So, it is safe to say that increasing the business certainty regarding the enforceability of the online B2C arbitration clause is in the interest of the consumer.

Currently, the enforcement of a cross-border online B2C arbitration clause is most likely to be governed by the rules of the New York Convention 1958 (hereinafter NYC).<sup>6</sup> This is because the NYC has more than 142 signatories.<sup>7</sup> This happens as long as the commercial or reciprocity reservations do not take effect in excluding the whole of the NYC from application.<sup>8</sup> Two issues in the NYC make the consumer or the business seriously uncertain about the enforceability of the online B2C arbitration clause. The first is that an arbitration clause included in an online B2C e-commerce contract may not satisfy the formal validity requirement under Article

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<sup>3</sup>Martin, note 2 supra, p.130.

<sup>4</sup>Gary B. Born, "Planning for International Dispute Resolution", (2000) 17(3) J. Int'l. Arb. 61.63.

<sup>5</sup>Ibid

<sup>6</sup>United Nation Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958.

<sup>7</sup> The list of adherents to the New York Convention 1958 is available at: < [http://www.uncitral.org/uncitral/en/uncitral\\_texts/arbitration/NYConvention\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention_status.html) > accessed on 12/01/2007.

<sup>8</sup>'Commercial Reservation' means that "the state will apply the NYC only to differences arising out of legal relationships, whether contractual or not, that are considered commercial under the national law". 44 out of 142 signatories to the NYC have declared the 'commercial reservation'. However, what should be mentioned here is that many countries include consumer contracts within the scope of definition of commercial. Information about the status of the NYC and commercial reservation is available at:

<[http://www.uncitral.org/uncitral/en/uncitral\\_texts/arbitration/NYConvention\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention_status.html)> accessed on 20/01/2007

II(1) & (2) of the NYC.<sup>9</sup> The violation of the public policy exception to the enforcement of an arbitration clause under the NYC is the second aspect, which may lead to the uncertainty regarding the enforceability of the online B2C arbitration clause. Many of the national mandatory rules of law that restrict or prohibit an arbitration clause in a B2C contract may come under this exception. This mainly makes the business uncertain whether the online B2C arbitration clause will be enforceable against the consumer.

This chapter explains that adopting a new rule that stipulates the knowing and intelligent standard of consent to an online B2C arbitration clause will help to avoid these two uncertainties. Part one of this chapter explains the uncertainty about the enforceability of online B2C arbitration clauses that both the business and the consumer may face because of the formal validity requirement under Article II(2) of the NYC. It also explains how the new rule will make both the consumer and the business certain that the use of the Internet to conclude the B2C arbitration clause will not make it unenforceable. Part two of this chapter explains the uncertainty about the enforceability of the online B2C arbitration clause that the business may face because of the public policy exception to its enforcement under the NYC. It also explains how the new rule will remove this uncertainty. In this chapter, reference will be made to case law applying the NYC from different jurisdictions and it is not going to be limited to England and the US.

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<sup>9</sup>Aashit Shah, "Using ADR to Resolve Online Disputes", (2004) 10 Rich. J.L. & Tech. 25, 33. Michael E. Schneider and Christopher Kuner, "Dispute Resolution in International Electronic Commerce", (1997) 14(3) J. Int'l Arb. 5, 17.



## **1. Uncertainty Resulting from Formal Validity Requirement under Article II(2) of the NYC**

Article II(2) of the NYC is a source of uncertainty about the enforceability of the online B2C arbitration clause. In order to enforce an online B2C arbitration clause under the NYC, the online arbitration clause must satisfy the formal validity requirement embodied in Article II(2). Article II(1) and (2) state that:

“1. (E)ach Contracting State shall recognize an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration.

2. (T)he term “agreement in writing” shall include an arbitral clause in a contract or an arbitration agreement, signed by the parties or contained in an exchange of letters or telegrams.”<sup>10</sup>

Article II(1) of the NYC stipulates that an arbitration clause must be in writing and Article II(2) explains what satisfies the writing requirement. Article II(2) provides that an arbitration clause is in writing if it is included in a contract signed by the parties or in contract concluded via exchange of letters or telegrams. Article II(2) does not indicate that the Internet is one of the communication means that can be used to produce legally recognized arbitration clauses.<sup>11</sup>

Ortiz observed that the ‘literal interpretation’ for the NYC will lead to the rejection of enforcement of the arbitration clause that has been concluded via the internet.<sup>12</sup>

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<sup>10</sup>Section (1) and (2) of Article II of the New York Convention 1958.

<sup>11</sup>Jasna Arsić, “International Commercial Arbitration on the Internet: Has the Future Come Too Early”, (1997) 14(3) J.Int’l.Arb. 209, 216, 217. Vera Van Houtte, “Consent to Arbitration Through Agreement to Printed Contracts: The Continental Experience”, (2000) 16(1) Arb. Int’l.1, 3.

<sup>12</sup>Alejandro Lòpez Ortiz, “Arbitration and IT”, (2005) 21(3) Arb. Int’l.343, 353.

The UNCITRAL noticed this problem and it has introduced a solution. The solution is embodied in the newly adopted United Nations Convention on the Use of Electronic Communications in International Contracts 2005,<sup>13</sup> which has not yet entered into force.<sup>14</sup> Article 8(1) of the E-Communications Convention 2005 states that “a communication or a contract shall not be denied validity or enforceability on the sole ground that it is in the form of an electronic communication”.<sup>15</sup> Article 20(1) of the same Convention states that:

“The provisions of this Convention apply to the use of electronic communications in connection with the formation or performance of a contract to which any of the following international conventions, to which a Contracting State to this Convention is or may become a Contracting State, apply: Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 10 June 1958)”.<sup>16</sup>

Article 20(1) extends the application of the E-Communications Convention 2005 which gives legal recognition to electronically concluded contracts, to the NYC. Article 20(1) of the E-Communications Convention 2005 makes electronically concluded arbitration agreements and clauses valid under the NYC. One might say that if the signatories to the NYC adhere to the E-Communications Convention 2005, the problem will be resolved. That is true but only for arbitration clauses included in the online business-to-business contracts. The question whether online B2C

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<sup>13</sup>United Nations Convention on the Use of Electronic Communications in International Contracts (adopted on 23 November 2005). (Hereinafter E-communication Convention 2005)

<sup>14</sup>Article 23(1) of the e-communications convention states that “this Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the third instrument of ratification, acceptance, approval or accession”. So far, the convention has not received any ratifications. All information available at:

[http://www.uncitral.org/uncitral/en/uncitral\\_texts/electronic\\_commerce/2005Convention\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/electronic_commerce/2005Convention_status.html)], accessed on 12/01/2007.

<sup>15</sup>Article 8(1) of the United Nations Convention on the Use of Electronic Communications in International Contracts (adopted on 23 November 2005).

<sup>16</sup>Article 20(1), Ibid

arbitration clauses satisfy the writing requirement under Article II(2) still constitutes a source of legal uncertainty for both the consumer and the business. The reason is that Article 2(1) (a) of the E-Communications Convention 2005 states that the convention does not apply to “contracts concluded for personal, family or household purposes”. This means that consumers’ contracts are excluded from the scope of application of the E-Communications Convention 2005.<sup>17</sup>

Consumer’s contracts have been excluded from the scope of application of the E-Communications Convention 2005 for several reasons. First, it is difficult to accommodate the differences between the rules of the conventions and the different consumer protections rules in the different countries.<sup>18</sup> Including the consumer within the scope of the E-Communications Convention 2005 will reduce the number of countries that might adopt the convention because consumer protection is usually connected with a political agenda.<sup>19</sup> Furthermore, making the rules of the convention consistent with consumer protection will make it difficult to produce rules suitable for the business-to-business transactions which are mainly based on the parties’ autonomy and the non-strict rules of formal validity.<sup>20</sup>

Academic writers and the UNCITRAL have suggested two solutions that can be applied to make online arbitration clauses enforceable under Article II(2) of the NYC. The solutions are, first, expansion of the term ‘Telegram’ in Article II(2) of

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<sup>17</sup>Chris Connolly and Prashanti Ravindra, “First UN Convention on eCommerce Finalized”, (2006) 22(1) C.L.S.R. 31, 34.

<sup>18</sup>John D. Gregory, “The Proposed UNCITRAL Convention on Electronic Contracts”, (2003-2004) 59 Bus. Law. 313, 321.

<sup>19</sup>Ibid

<sup>20</sup>Ibid

the NYC to include new means of communications such as the Internet.<sup>21</sup> Second, reliance on the most favourable law provision under Article VII(1) of the NYC.<sup>22</sup> In the subsequent subsection, the present author will explain that it is true that the second solution might be effective to some extent. Both the first and the second solutions do not eliminate the legal uncertainty caused by the text of Article II(2) of the NYC. Adopting a new rule that stipulates the knowing and intelligent standard of consent to online B2C arbitration clauses will effectively eliminate this uncertainty.

### **1.1 Regulating Online B2C Arbitration Clauses Effectively Eliminates the Uncertainty**

The question whether arbitration clauses concluded via the Internet satisfy the formal validity requirement under Article II(2) of the NYC has been discussed by academic writers. Some writers have suggested a practical solution for the problem. It is that the term ‘Telegram’ in Article II(2) of the NYC should be interpreted to include new means of communications such as the Internet. Arsić observed that:

“(B)earing in mind the state of communications technology at the time-when the fastest means of mass commercial communication was the telegram-it is clear that the delegates included the most modern technology without excluding future developments in ways to transmit written words... I believe that there is no obstacle to the interpretation of Article II of the New York Convention in recognizing the exchange of e-mail messages as a written form for the purpose of conclusion of arbitration agreements.”<sup>23</sup>

Richard Hill agreed with Arsić and he noted that:

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<sup>21</sup>Schneider and Kuner, note 9 supra, p.13.

<sup>22</sup>UNCITRAL Working Group II (Arbitration), 44<sup>th</sup> session, New York, 23-27 January 2006. p.3, 4.

<sup>23</sup>Arsić, note 11 supra, p. 216.

“Arsić has argued convincingly... that an exchange of E-Mail messages containing an arbitration clause satisfies the formal requirements of Article II(2) of the NYC, because an exchange of E-Mails can be equated to an exchange of telegrams. This argument is correct because, even though there are important technical difference between telegrams and E-Mails, the essential features of an exchange of telegrams can be reproduced through appropriate use of E-Mail.”<sup>24</sup>

It is true that by the time the NYC was adopted, the Internet was unknown<sup>25</sup> and the telegram was the most modern means of communications that could be used to conclude commercial contracts.<sup>26</sup> Furthermore, it is true that concluding a contract via the exchange of E-mails might be similar to concluding a contract by exchange of telegrams. However, this practical solution does not ensure parties that the enforcement of the arbitration clause will not be rejected just because it has been concluded via the Internet. First, from a practical dimension, online B2C contracts that include arbitration clauses are not concluded by E-mails.<sup>27</sup> Online B2C contracts are mainly concluded via click-wrap and browse-wrap agreements. Click-wrap agreement appears as a step in the online contracting process. The consumer has to accept the click-wrap agreement in order to complete the contract.<sup>28</sup> The browse-wrap agreement is different from click-wrap agreement. Accepting this agreement is not a mandatory step in the online contracting process. A separate hyperlink will take the consumer to another webpage where he will find the text of the contract. The text of the contract will indicate that the consumer will be obliged by this

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<sup>24</sup>Richard Hill, “On-line Arbitration: Issues and Solutions”, (1999) 15(2) Arb. Int’l. 199, 200.

<sup>25</sup>According to Barry M. Leiner and another, the first recorded scientific research envisioning a computer network like the Internet was conducted in 1962. For more information about the Internet history visit < <http://www.isoc.org/internet/history/brief.shtml#Introduction>> accessed on 12/01/2007.

<sup>26</sup>Arsić, note 11 supra, p. 216.

<sup>27</sup>William J. Condon, Jr., “Electronic Assent to Online Contracts: Do Courts Consistently Enforce Clickwrap Agreements”, (2003-2004) 16 Regent U. L. Rev. 433,435.

<sup>28</sup>Ibid.

agreement if he has completed the transaction with the business. So, the process of contracting in click-wrap or browse-wrap agreements is not based on exchanging documents.<sup>29</sup> The element of exchange of documents that Arsić and Hill<sup>30</sup> have relied on to say that E-mail satisfies the writing requirement under the NYC does not exist in click-wrap and browse-wrap agreements.<sup>31</sup>

Second, this technological interpretation of the writing requirement under the NYC might not be accepted by all courts of country-signatories to the NYC. Evidence for this can be seen in the decision of the Court of Appeals of Hålogaland in Norway.<sup>32</sup> The Court refused to recognize an arbitration award under Articles II and IV of the NYC. The Court justified its decision saying that the exchange of e-mails by the parties, which included the content of a contractual document that had not been signed, did not qualify as an original or certified copy of an arbitration agreement entered into in writing or as a result of an exchange of letters or telegrams.<sup>33</sup>

Accordingly, this practical solution does not eliminate uncertainty about the enforceability of online B2C arbitration clauses under Article II(2) of the NYC. This uncertainty may prevent both the business and the consumer from agreeing to arbitrate future e-commerce disputes.

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<sup>29</sup> Francis M. Buono and Jonathan A. Friedman, Maximizing the Enforceability of Click-Wrap Agreements, (1999) 4(3) J. Tech. L. & Pol'y, available at: <<http://grove.ufl.edu/~techlaw/citation.html>> accessed on 02/02/2006.

<sup>30</sup> Arsić, supra note. 11, p. 216; Hill, supra note 24, p. 199, 200.

<sup>31</sup> Buono and Friedman, supra note.29.

<sup>32</sup> [1999] 2 Stockholm Arbitration Reports 121. This court decision is cited in the UNCITRAL Working Group II (Arbitration), 44<sup>th</sup> session, New York, 23-27 January 2006. p.15

<sup>33</sup> Ibid.

The UNCITRAL has made a considerable effort to make online arbitration clause enforceable under Article II(2) of the NYC. The UNCITRAL Working Group suggested that Courts can rely on the most favourable law provision under Article VII(1) of the NYC to enforce arbitration clause concluded via the Internet. The UNCITRAL recommended that:

“article VII(1) of the Convention should be applied to allow any interested party to avail itself of rights it may have, under the law or treaties of the country where an arbitration agreement is sought to be relied upon, to seek recognition of the validity of such an arbitration agreement.”<sup>34</sup>

Article VII(1) of the NYC states that:

“The provisions of the present Convention shall not affect the validity of multilateral or bilateral agreements concerning the recognition and enforcement of arbitral awards entered into by the Contracting States nor deprive any interested party of any right he may have to avail himself of an arbitral award in the manner and to the extent allowed by the law or the treaties of the country where such award is sought to be relied upon.”<sup>35</sup>

Article VII(1) of the NYC aims to eliminate conditions for recognition and enforcement of an arbitral award in national law that are stricter than the rules of the Convention and, at the same time, allows the application of rules of national law that favours the enforcement of the award more than the Convention.<sup>36</sup> As the validity of the arbitration clause is one condition for the enforceability of the arbitral award, courts can rely on Article VII of the NYC to determine the formal validity of the arbitration clause according to the rules of the national law. This is when the

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<sup>34</sup> UNCITRAL Working Group II, ‘Article II (2) of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958)’, (14 Dec 2005) A/CN.9/WG.II/WP.139. p.22

<sup>35</sup> Article VII(1) of the New York Convention 1958.

<sup>36</sup> Ortiz, note 12 supra, p.354

national law gives legal recognition to the arbitration clause but not Article II(2) of the NYC.

Reliance on Article VII(1) can, to some extent, be an effective solution to overcome the uncertainty regarding the enforceability of online arbitration clauses under Article II(2) of the NYC. The reason is that many countries have adopted the UNCITRAL Model on International Commercial Arbitration<sup>37</sup>, as well as many countries have adopted either the UNCITRAL Model Law on E-commerce<sup>38</sup> or the EU Directive on E-commerce 2000/31/EC.<sup>39</sup> Article 7(2) of the UNCITRAL Model Law on International Commercial Arbitration validates an arbitration agreement entered into by ‘... means of telecommunication which provide a record of the agreement’.<sup>40</sup> Click-wrap and browse-wrap agreements are usually used to conclude online contracts between business and consumer.<sup>41</sup> Both click-wrap and browse-wrap agreements are capable of producing records. They can be printed out,<sup>42</sup> as well as copied and saved in the form of Microsoft Word and/or PDF documents which are easy to store and retrieve. In this sense an arbitration clause included in a B2C click-wrap and browse-wrap agreement satisfies the writing requirement under national laws that have adopted Article 7(2) of the UNCITRAL Model Law on International Commercial Arbitration.

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<sup>37</sup>UNCITRAL Model on International Commercial Arbitration (adopted on 21 June 1985).

<sup>38</sup>UNCITRAL Model Law on Electronic Commerce (adopted on 12 June 1996).

<sup>39</sup>Directive (2000/31/EC) of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market. [2000] OJ L178, p. 1–16.

<sup>40</sup>Ibid

<sup>41</sup>Steven c Bennett, “Click-Wrap Arbitration Clauses”, (2000) 14(3) I.R.L.C.T.397, 397.

<sup>42</sup>Buono and Friedman, *supra* note 29.



England did not adopt the UNCITRAL Model Law on International Commercial Arbitration. However, the English Arbitration Act 1996 is a good example of national laws that recognize electronically concluded arbitration clauses whenever the communication means produce records. Section 5(3) of the Arbitration Act 1996 states that:

“(2) There is an agreement in writing - (a) if the agreement is made in writing (whether or not it is signed by the parties), (b) if the agreement is made by exchange of communications in writing, or (c) if the agreement is evidenced in writing.”<sup>43</sup>

Section 5(4) of the Arbitration Act 1996 states that:

(4) An agreement is evidenced in writing if an agreement made otherwise than in writing is recorded by one of the parties, or by a third party, with the authority of the parties to the agreement.”<sup>44</sup>

An arbitration clause included in a click-wrap and browse-wrap B2C agreement does satisfy the writing requirement under section 5 of the English Arbitration Act 1996.<sup>45</sup> The reason as has been explained above is that click-wrap and browse-wrap agreements are capable of producing records. Similarly, both the UNCITRAL Model Law on E-commerce and EU Directive on E-commerce 2000/31/EC establish the principle of functional equivalence in the area of online contracting.<sup>46</sup> Both the model law and the directive provide that contracts should not be deprived of legal

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<sup>43</sup>Section 5(2) of the Arbitration Act 1996, (UK).

<sup>44</sup>*Ibid*

<sup>45</sup>Guillermo Aguilar Alvarez, “Article II(2) of the New York Convention and the Courts”, in Albert Jan Van Den Berg (ed) *International Council for Commercial Arbitration, Improving the Efficiency of Arbitration Agreements and Awards: 40 Years of Application of the New York Convention*, (Kluwer Law International, Hague, 1999), p.75

<sup>46</sup>Hisham Tahat, “Factors affecting E- commerce contract law”, (paper presented at the 20th British and Irish Law, Education and Technology Association Annual Conference 2005). Available at: <<http://www.bileta.ac.uk/Document%20Library/1/Factors%20Affecting%20E%20commerce%20Contract%20Law.pdf>> accessed on 10/05/2006

recognition just because they are concluded via electronic means. Article 5 of the UNCITRAL Model Law on E-commerce states that: “Information shall not be denied legal effect, validity or enforceability solely on the grounds that it is in the form of a data message”.<sup>47</sup> Article 6(1) states that:

“where the law requires information to be in writing, that requirement is met by a data message if the information contained therein is accessible so as to be usable for subsequent reference.”<sup>48</sup>

Article 9(1) of the EU Directive on E-commerce (2000/31/EC) states that:

“Member States shall ensure that their legal system allows contracts to be concluded by electronic means. Member States shall in particular ensure that the legal requirements applicable to the contractual process neither create obstacles for the use of electronic contracts nor result in such contracts being deprived of legal effectiveness and validity on account of their having been made by electronic means.”<sup>49</sup>

Many countries have adopted UNCITRAL Model Law on E-commerce<sup>50</sup> and EU countries have implemented the EU Directive on E-commerce. So, in the case that the national law applicable to the arbitration agreement is a law of one of the countries that have adopted the Model law or the Directive, an arbitration clause included in online B2C agreement will be considered valid.

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<sup>47</sup>Article 5 of the UNCITRAL Model Law on Electronic Commerce (adopted on 12 June 1996). Article II(a) of the Model Law defines Data message as meaning “information generated, sent, received or stored by electronic, optical or similar means including, but not limited to, electronic data interchange (EDI), electronic mail, telegram, telex or telecopy.” Section (b) of the same article defines EDI as meaning “the electronic transfer from computer to computer of information using an agreed standard to structure the information”.

<sup>48</sup>Article 6 of the UNCITRAL Model Law on Electronic Commerce (adopted on 12 June 1996).

<sup>49</sup>Article 9(1) of the EU Directive on E-commerce

<sup>50</sup>List of countries that adopted the UNCITRAL Model Law on E-commerce available at: <[http://www.uncitral.org/uncitral/en/uncitral\\_texts/electronic\\_commerce/1996Model\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/electronic_commerce/1996Model_status.html)>, accessed on 12/01/2006.

State courts have applied national law to enforce an arbitration clause that is not enforceable under Article II(2) of the NYC. An example of this can be seen in the case of *Petrasol BV (Netherlands) v Stolt Spur Inc. (Liberia)*,<sup>51</sup> the Court of First Instance, Rotterdam, explained that:

“the provisions of the New York Convention (particularly article II) do not preclude the application of article 1074 CCP, because of the more-favorable law provision in article VII of the Convention, to be applied by analogy”.<sup>52</sup>

Another example can also be seen in the case of *Gas Authority of India, Ltd v SPIE-CAPAG, SA (France), Nippon Kokan Corporation (Japan), Toyo Engineering Corporation (Japan)*,<sup>53</sup> the Delhi High Court explained that:

“The parties to an international commercial arbitration agreement can seek enforcement of an arbitral award on the basis of the domestic law instead of the Convention, notwithstanding the fact that they may have agreed to enforce the arbitration agreement under article II of the Convention. When the arbitration agreement does not result in an arbitral award capable of enforcement under the Convention, it can still be enforced under parallel domestic law of India, the Indian Arbitration Act”.<sup>54</sup>

It is clear that some States' courts rely on Article VII(1) to apply national laws and enforce arbitration clauses that are not enforceable under Article II(2) of the NYC. However, this solution cannot ensure parties that the enforcement of the online B2C arbitration clause will not be refused just because it is concluded via the Internet. The UNCITRAL, which recommends reliance on Article VII(1), has noted that there are certain issues that might limit the success of this solution. First, Article VII(1) provides that the most favourable law provision applies to the enforcement of the

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<sup>51</sup>Yearbook Commercial Arbitration, (1998) XXII, p. 762- 765

<sup>52</sup>Ibid

<sup>53</sup>Suit No. 1440 of 1990 and I.A No. 5206 of 1990, D – 15-10-1993

<sup>54</sup>Ibid

arbitral award and it did not mention the arbitration agreement.<sup>55</sup> There is no guarantee that courts of all state-signatories to the NYC will not literally interpret Article VII(1) and apply it to arbitration clauses as it is applied to arbitral awards.<sup>56</sup>

The second issue is that the ability to rely on Article VII(1) of the NYC to enforce an online arbitration clause is connected with the way that national courts interpret Article II(2) of the NYC.<sup>57</sup> In order to be able to rely on Article VII(1) to enforce an arbitration clause in an online B2C contract, Article II(2) of the NYC should not be interpreted as establishing a unified standard of formal validity of an arbitration clause or arbitration agreement.<sup>58</sup> It should be interpreted as setting maximum requirements for the formal validity of an arbitration clause.

However, there is a divergence on whether Article II(2) of the NYC establishes a unified standard for formal validity of the arbitration clause or maximum requirements of formal validity. Many Courts of member states to the NYC have taken the second approach and did apply their national law when it is less strict than Article II(2) of the NYC. In the case of *Progressive Casualty Insurance Co. v C.A. Reaseguradora Nacional de Venezuela*,<sup>59</sup> the Court of Appeals for the second Circuit ignored Article II(2) of the NYC and the Court only cited domestic cases and found that, under the State of New York law, the arbitration agreement was binding.

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<sup>55</sup> UNCITRAL Working Group II, 'Article II (2) of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958)', (14 Dec 2005) A/CN.9/WG.II/WP.139. p.20.

<sup>56</sup>Ibid.

<sup>57</sup>Ibid, p.15, 16.

<sup>58</sup>Ortiz, note 12 supra, p.354

<sup>59</sup>(1993) (991 F Supp 2d 42)

The German Court of Appeal of Cologne asserted that: “Article II(2) of the Convention does not provide for a uniform rule”.<sup>60</sup>

It is clear that Courts in the US and Germany interpret Article II(2) of the convention as establishing a maximum requirement for formal validity. Where the national law provides a more favourable treatment of the arbitration agreement, the national law should supersede. Nevertheless, other courts in other countries have insisted that Article II(2) establishes a uniform rule for formal validity that cannot be superseded by national law. The Federal Supreme Court of Switzerland asserted that:

“Article II(2) superseded any national law with respect to formal requirements and the principle of autonomous interpretation meant that national law could not be applied for the interpretation and scope of the arbitration agreement, whether more or less strict than Article II(2) concerning formal requirements.”<sup>61</sup>

This divergence in interpreting whether Article II(2) is a unified standard or maximum standard between courts of different countries, makes the possibility of relying on Article VII(1) connected to the place where the enforcement is sought.<sup>62</sup>

The Courts insist that Article II(2) establishes uniform rules for formal validity of an arbitration clause may refuse to rely on Article VII(1), and accept to rely on national law to give force to arbitration clauses concluded via the Internet. Therefore, it is safe to say that the most favourable law provision embedded in Article VII(1) of the NYC cannot ensure parties that the arbitration clause will not be unenforceable just

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<sup>60</sup>Danish buyer vs. German seller, 16 December 1992. (Yearbook Commercial Arbitration XXI (1996), p. 535)

<sup>61</sup>OLG Schleswig, 30 March 2000, 16 SchH 05/99

<sup>62</sup>Karen Stewart and Joseph Matthews, “Online Arbitration of Cross-Border, Business to Consumer Disputes”, (2002) 56 U. Miami L. Rev. 1111, 1135.

because it is concluded via the Internet. This situation creates a state of uncertainty for both the business and the consumer. The business and the consumer will not try to insert an arbitration clause into their contract if they feel that it is not going to be enforced just because it is in an electronic format.<sup>63</sup>

Adopting a new rule that stipulates the knowing and intelligent standard of consent to online B2C arbitration clauses will resolve this problem. Such a rule will validate online B2C arbitration clauses when the consumers have knowingly and intelligently accepted them. This means that the Internet will be recognised as valid mean of concluding B2C arbitration clauses. This will assure both the consumer and the business that the B2C arbitration clause will not be denied enforceability just because it is concluded via the Internet. What is more, such a solution seems to be more likely to be achieved than adopting an amending protocol to the NYC. A new amending protocol that aims to validate online B2C arbitration under Article II(2) of the NYC is not a likely solution for several reasons. The E-communications Convention 2005 has made it clear that business-to-business arbitration clauses that are concluded via the Internet are legal recognised. Currently, arbitration clauses and arbitral awards that are introduced to be enforced under the NYC are mostly arising from contracts between commercial parties. The success of the international commercial arbitration is attributed to the wide adoption of the NYC. It has been ratified by 142 countries in its 50 year of existence.<sup>64</sup> Adopting a new amending protocol will not only include amendment to the writing requirement. It will also

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<sup>63</sup>Stewart and Matthews, note 62 supra, p.1135.

<sup>64</sup>New York Convention was adopted in 1958 and there are now more than 142 parties to the convention.

include amendments to other NYC provisions that need to be revised.<sup>65</sup> It is going to take a long time before this protocol gathers the same level of popularity as the original Convention.<sup>66</sup> This may increase the ‘lack of harmony’ in interpreting the NYC and thereby reduce its success. Therefore, the UNCITRAL is not going to jeopardise the wide adoption of the NYC and amend it in order to eliminate the uncertainty about the enforceability of online B2C arbitration clauses under Article II(2).

The importance of adopting a new convention that regulates online B2C arbitration and that stipulates the knowing and intelligent standard of consent appears in this context. Adopting such a new rule will not affect the success of the NYC. The reason is that the suggested rule will not add any new provisions to the NYC that require ratification and thereby it will not cause any ‘lack of harmony’ in interpreting the NYC. The suggested convention aims to shift the enforcement of online B2C arbitration clauses from the NYC to the new convention. This will help to avoid any uncertainty resulting from whether an arbitration clause in an online B2C contract satisfies the writing requirement under the NYC.

To sum up this part of chapter four, the E-communications Convention 2005 has not eliminated the legal uncertainty regarding whether an online B2C arbitration clause satisfies the writing requirement under Article II(2) of the NYC. Technical interpretation of Article II(2) or reliance on Article VII(1) does not help to

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<sup>65</sup>UNCITRAL, “Report of the United Nations Commission on International Trade Law on the work of its thirty-second session”, (17 May 1999) 17(A/54/17), p.40-47. This report spells out some other provisions of the NYC that requires revision.

<sup>66</sup>Stewart and Matthews, note 62 supra, p.1137.

effectively eliminate this legal uncertainty. This is because both the technical interpretation and Article VII(1) are subject to different interpretation by the Courts of the state-signatories to the NYC. Adopting a protocol that amends the NYC may affect its success. Adopting an international convention that stipulates the knowing and intelligent standard of consent to online B2C arbitration clauses will resolve the problem. The new rule gives legal recognition to an online B2C arbitration clause when the consumer's consent is knowing and intelligent. Therefore, under this new rule, the use of the Internet to conclude B2C arbitration clauses is *prima facie* valid. This will assure both the consumer and the business that the enforcement of the arbitration clause will not be refused just because it has been concluded via the Internet.

## **2. Uncertainty Resulting from Public Policy Exception to the Enforcement of an Online B2C Arbitration Clause**

As explained *supra*, obtaining the business consent to arbitrate e-commerce disputes with the consumer through an arbitration clause is so important for the consumer. Business receives the payment from the consumer before giving the goods or the services. Therefore, in the case that a B2C e-commerce dispute arises, the business may not accept to arbitrate the dispute if there is no prior obligation to do that. In B2C e-commerce, the business concludes transactions with consumers from different countries. The business inserts the arbitration clause in order to avoid litigation in various forums. However, the business will not insert the arbitration clause into the B2C e-commerce contract if the online B2C arbitration clause is



unlikely to be enforced against the consumer. This is because it does not eliminate the uncertainty about the possible forums for litigation.

Article V(2)(b) of the NYC states that the enforcement of an arbitral award can be refused if the arbitral award violates the public policy of the place of the enforcement.<sup>67</sup> However, it is also possible to challenge an arbitration clause for violation of public policy of the country of law applicable to the arbitration clause or the law of the place of enforcement of the clause. This can be the consumer's country of domicile, the arbitral seat or, in some situations, the law of the place of performance of the contract.<sup>68</sup> Public policy exception to the enforcement of an arbitration clause under the NYC has been interpreted narrowly by many courts of state-signatories to the NYC. However, in the subsequent sections, the present author will explain that, despite this narrow interpretation, mandatory rules prohibiting or restricting an arbitration clause in a B2C contract come within the scope of the public policy exception to its enforcement under the NYC. This may discourage the business from agreeing to arbitrate future e-commerce disputes with the consumer via an arbitration clause. Adopting a new rule that stipulates the knowing and intelligent standard of consent to online B2C arbitration clause will resolve this problem. This is because different countries, when adhering to this Convention, will be under an obligation to enforce an online B2C arbitration clause regardless of whether their national rules allow or prohibit arbitration clauses in B2C

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<sup>67</sup>Article V(2)(b) of the NYC.

<sup>68</sup>Donna M. Bates, "A Consumer Dream or Pandora's Box: Is Arbitration a Viable Option for Cross-Border Consumer Disputes?", (2004) 27 Fordham Int'l L.J.823, 873. Audley Sheppard, "Interim ILA Report on Public Policy as a Bar to Enforcement of International Arbitral Awards", (2003) 19(2) Arb. Int'l. 217, 243.

contracts. In other words, rules that prohibit arbitration clauses in B2C e-commerce contract cannot be relied on to challenge the enforcement of the arbitration clause on basis of violation of public policy under the NYC.

## **2.1 Public Policy and International Public Policy Distinguished**

It is difficult to define what is meant by public policy or order public because of the various social, economic and political variables that might take part in articulating the elements of public policy. These do differ from one country to another.<sup>69</sup> However, as Prof. Van Den Berg explained, the wide notion of public policy includes mandatory legal rules, norms and primary principles that aim to protect the social, moral and economic values of a particular society.<sup>70</sup> Mandatory rules are divided into two types domestic and international. The first can be excluded by the choice of another country law, whereas the second cannot be excluded by the choice of another country law.

As has been mentioned above, it is possible to challenge an arbitration clause for violation of public policy.<sup>71</sup> Courts of many state-signatories to the NYC have interpreted the concept of public policy embodied in Article V(2)(b) of the Convention to mean international public policy of the forum.<sup>72</sup> Prof. Albert Van Den Berg explained that international public policy is narrower than domestic public

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<sup>69</sup> Albert Van Den Berg, "Distinction Domestic-International Public Policy", (1996) XXI *Yearbook* at p. 502.

<sup>70</sup> Ibid. R. Sever, "The Relaxation of Inarbitrability and Public Policy checks on US and Foreign Arbitration: Arbitration out of Control", 65 Tul. L. Rev. 1661, 1664.

<sup>71</sup> Bates, note.68 *supra*, p.873.

<sup>72</sup> Pierre Mayer and Audley Sheppard, "Final ILA Report on Public Policy as a Bar to Enforcement of International Arbitral Awards", (2003) 19(2) *Arb. Int'l.* 249, 251-253.

policy.<sup>73</sup> This means that not every rule of law that relates to the *order public interne* is necessarily part of the *ordre public externe* or international.<sup>74</sup> In other words, international public policy is the most basic principle of a country's legal system. These principles cannot be renounced under any circumstances and have to be applied even when the matter relates to an international arbitration clause.<sup>75</sup> International mandatory rules do come within the scope of the international public policy of the forum where the enforcement will take place.

What should be mentioned here is that, there is a difference between international public policy which is used to refer to the public policy exception under Article V(2)(b) of the NYC and the truly international public policy. The latter refers to “fundamental rules of natural law, principles of universal justice and *jus cogens* in public international law”. It also refers to “the general principles of morality accepted by what are referred to as civilised nations”.<sup>76</sup> Aspects that come under the truly international public policy usually pertain to drugs trafficking, human rights violations and corruption. These aspects do come within the scope of public policy exception under the NYC. Therefore, it is safe to say that the public policy under the

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<sup>73</sup>Robert Briner, “The Arbitrability of Intellectual Property Disputes with Particular Emphasis on the Situation in Switzerland”, *Worldwide Forum on the Arbitration of Intellectual Property Disputes* (March. 1994) available at: <<http://www.wipo.int/amc/en/events/conferences/1994/briner.html>> accessed on 12/12/2006

<sup>74</sup>Van Den Berg, note supra 69, p.502.

<sup>75</sup>Mayer and Sheppard, note 72 supra, p. 251-253.

<sup>76</sup>Audley Sheppard and Clifford Chance, “Public Policy and the Enforcement of Arbitral awards: Should there be a Global Standard?”, (2003) 1(2) Oil, Gas & Energy Law Intelligence. Available at: <[http://www.gasandoil.com/ogel/samples/freearticles/article\\_67.htm#\\_ftn4](http://www.gasandoil.com/ogel/samples/freearticles/article_67.htm#_ftn4)> accessed on 21/11/2006.

NYC includes the truly international public policy and international public policy of the enforcing state.<sup>77</sup>

## **2.2 Mandatory Rules Prohibiting or Restricting Arbitration Clauses in B2C Contracts and the Public Policy Exception under the NYC**

Many of the mandatory rules that prohibit or restrict arbitration clauses in online B2C e-commerce contract come with public policy exception under the NYC. Bates argues that the narrow interpretation of the public policy exception under the NYC or what is usually called the international public policy minimises the ability of the consumer to rely on mandatory rules that prohibit or restrict arbitration clauses in B2C contracts. This is because mandatory rules that prohibit or restrict arbitration clauses in B2C contracts do not come within the scope of international public policy.<sup>78</sup>

Bates' contention is true within the scope of her country's jurisdiction, which is the United States. In the US, the public policy exception to enforcement has not only been narrowed within the scope of the NYC but it has also been narrowed in a similar way on the US federal level. In the past, a dispute between a business and a consumer that is related to securities transactions could not be submitted to arbitration on the US federal level.<sup>79</sup> The reason is that the US Supreme Court interpreted Section 14 of the United States Securities Act 1933, which invalidates any 'stipulation' that waives compliance with the Act, as evidencing "a public policy

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<sup>77</sup>Mayer and Sheppard, note 72 supra, 251-253.

<sup>78</sup>Bates, note 68 supra, p.875-876.

<sup>79</sup>Katherine Van Wezel Stone, "Rustic Justice: Community and Coercion under the Federal Arbitration Act", (1998-1999) 77 N.C.L.Rev. 931, 996-1002.

which forbids referring the controversy to arbitration...”.<sup>80</sup> This was in the case of *Wilko v Swan*.<sup>81</sup> However, in the case of *Rodriguez de Quijas v Shearson/American Express, Inc.*,<sup>82</sup> the US Supreme Court overturned the public policy defence established in *Wilko*. In the case of *Rodriguez*, the US Supreme Court refused the allegation that Section 29(a) of the Securities Exchange Act of 1934, which invalidates any agreement that waives compliance with any provision in the Act, does not allow for waiving the right to resort to the Court stipulated in Section 27.<sup>83</sup> The US Supreme Court justified the decision on the grounds that there is a national policy that favours arbitration and this provision constitutes hostility to the enforcement of an arbitration clause which the FAA aims to eliminate.<sup>84</sup> The Supreme Court also based its decision on the fact that the arbitral process will not deprive *Rodriguez* of the “rights to which he is entitled”.<sup>85</sup> In this case, the US Supreme Courts has also relied on its decision in the case of *Scherk v Alberto-Culver*,<sup>86</sup> in which the Court refused the allegation that a foreign arbitral award that resolves a dispute arising from securities transactions between two businesses should be vacated because it violates the public policy of the US. The Supreme Court justified its decision saying that:

“parochial refusal by the courts of one country to enforce an international arbitration would not only frustrate the purpose of the agreement but would damage the fabric international commerce and trade and imperil to

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<sup>80</sup>346 US 427 (1953), 434,435.

<sup>81</sup>*Ibid.*

<sup>82</sup>482 US 220 (1987)

<sup>83</sup>*Ibid.*, 220,221

<sup>84</sup>*Ibid.*, p.225,226,227

<sup>85</sup>*Ibid.*, p.238

<sup>86</sup>417 US 506 (1974).

willingness and ability of businessmen to enter into international commercial agreements.”<sup>87</sup>

The Supreme Court’s approval for the arbitrability of securities disputes in *Scherk* represents reliance on international public policy as a defense to the non-enforceability of a foreign arbitration clause or award. However, the Supreme Court’s reliance on *Scherk* to eradicate the public policy defense in a domestic case, which is *Rodriguez*, indicates that the US’s domestic public policy has become as liberal as its international public policy.<sup>88</sup>

However, Courts from other jurisdictions have included mandatory rules that restrict or prohibit arbitration clauses in B2C e-commerce contracts within the scope of international public policy. English judges are hesitant to refuse the enforcement of the NYC arbitral clauses and awards on public policy grounds.<sup>89</sup> English judges have always affirmed the importance of the finality of the NYC award. For example, in the case of *Omnium de Traitement et de Valorisation SA v Hilmarton Ltd* (1999),<sup>90</sup> Hilmarton was engaged to approach public servants and Algerian government officials with a view to obtaining a drainage project in Algiers for OTV, such activity was in breach of Algerian law, which prohibited the intervention of middlemen in connection with any public contract within the ambit of foreign trade. Hilmarton brought a claim for unpaid consultancy fees. An arbitral tribunal applying Swiss law and sitting in Geneva made an award in favour of Hilmarton, finding that,

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<sup>87</sup>417 US 506 (1974).

<sup>88</sup>Alan Redfern and Martin Hunter, *Law and Practice of International Commercial Arbitration*, (3<sup>rd</sup> edn, Sweet & Maxwell, London, 1999), p.472.

<sup>89</sup>*Ibid*, p.471. Mustill and Boyd, *The Law and Practice of Commercial Arbitration in England*, (2<sup>nd</sup> edn., Butterworths, 1989), p. 65, 283; Sutton, Kendall and Gill, *Russell on Arbitration* (21<sup>st</sup> edn., Sweet & Maxwell, 1997), para. 8.022.

<sup>90</sup>[1999] 2 Lloyd’s Rep. 222.

in the absence of any evidence of bribery, the agreement was not unlawful under Swiss law. OTV sought to resist enforcement in England. Timothy Walker J. held:

“It may well be that an English arbitral tribunal, chosen by the parties, and applying English law as chosen by the parties, would have reached a different result. It may well be that such a tribunal would have dismissed Hilmarton's claim ... But I am not adjudicating upon the underlying contract. I am deciding whether or not an arbitration award should be enforced in England. In this context it seems to me that (absent a finding of fact of corrupt practices which would give rise to obvious public policy considerations) the fact that English law would or might have arrived at a different result is nothing to the point. Indeed, the reason for the different result is that Swiss law is different from English law, and the parties chose Swiss law and Swiss arbitration. If anything, this consideration dictates (as a matter of policy of the upholding of international arbitral awards) that the award should be enforced.”<sup>91</sup>

Ewan Brown gave a commentary on this case and he noted that:

“the decision of Walker J. in *Hilmarton* offers a welcome clarification of the limited scope for review by an English court on the grounds of public policy of a New York Convention award. Only if enforcement of an award conflicts with overriding public policy concerns such as the need to combat drug trafficking, fraud, corruption and terrorism at an international level, will an English court intervene. Domestic public policy concerns have no role to play at the enforcement stage.”<sup>92</sup>

Brown's analysis of the Court's decision in the case of *Hilmarton* narrows the scope of English international public policy to only include truly international public policy defences to the non-enforcement. However, this is not what Walker J. noted in the above quoted paragraph. Walker J. explained that the English court cannot refuse enforcement just because Swiss law is different to English law since the parties have chosen Swiss law. In other words, the English law that governs the type

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<sup>91</sup>[1999] 2 Lloyd's Rep. 222, p. 224, 225.

<sup>92</sup>Ewan Brown, “Illegality and Public Policy: Enforcement of Arbitral Awards in England”, (2000) 3(1) Int. A.L.R. 31 .p.35

of dispute resolved in the award does not come within the meaning of English international public policy.

Brown's analysis of the Court's decision in *Hilmarton* means that English mandatory rules that restrict the use of arbitration clauses in B2C contract do not come within the meaning of the public policy exception under the NYC. However, this is not true. Sections 89 and 91 of the English Arbitration Act 1996 that deal with arbitration clauses in B2C contracts come within the meaning of the public policy exception to the enforcement of an arbitration clause under the NYC.

Section 89 of the English Arbitration Act 1996 extends the application of the Unfair Contract Terms Regulations 1999<sup>93</sup> (hereinafter 1999 Regulations) on arbitration clauses in B2C contracts. This makes arbitration clauses in B2C contracts subject to the unfairness test embodied in the regulations. Section 91 of the Arbitration Act 1996 stipulates that any arbitration clause is unfair and is not binding on the consumer if the value of the claim is less than certain sum of money.<sup>94</sup> This sum is £5000.<sup>95</sup>

English courts have not yet reviewed any case involving a dispute over the enforcement of an international arbitral clause or award in an online B2C contract. Perhaps this is the reason for the lack of English case law explaining whether those

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<sup>93</sup>Unfair Contract Terms Regulations 1999, (S.I. 1999/2083). This statutory instrument has revoked the Unfair Contract Terms Regulations 1994 which was the first law that implemented the Unfair Contract Terms Directive 1993 into UK law.

<sup>94</sup>Section 91, the English and Welsh Arbitration Act 1996. Section 91 does not mean that consumer dispute with the value of less than £5000 is not arbitrable. It is arbitrable because the dispute can still be submitted to arbitration through post-dispute arbitration agreement.

<sup>95</sup>The Unfair Arbitration Agreements (Specified Amount) Order 1999. SI 1999/2167.



Sections come within the scope of the public policy exception to the enforcement under the NYC. However, there is strong evidence indicates that Sections 89 and 91 come within the scope of the public policy exception to the enforcement of an arbitration clause under the NYC. In other words, Section 89 and 91 are part of English international public policy.

The first evidence is mainly concerned with Section 89 of the Arbitration Act 1996. As explained above, Section 89 of the Arbitration Act 1996 extends the application of the 1999 Regulations to arbitration clauses in B2C contracts. At first glance, when one looks at the 1999 Regulations, one might say the 1999 Regulations cannot be part of English international public policy under the NYC. This is because Regulation 4(b) states that the 1999 Regulations do not apply to “the provisions or principles of international conventions to which the Member States or the Community are party”.<sup>96</sup> However, a recent judgment rendered by the European Court of Justice indicates that the protection awarded to the consumer from arbitration clauses under Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts<sup>97</sup> (hereinafter Unfair Terms Directive 1993), which is implemented in the UK through the 1999 Regulations comes within the meaning of public policy under the NYC. This means that the protection awarded to the consumer under the 1999 Regulations also come within the meaning of public policy

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<sup>96</sup>Regulation 4(b), Unfair Contract Terms Regulations 1999, (S.I. 1999/2083).

<sup>97</sup>OJ.L095 , 21/04/1993 P. 0029 – 0034.

under the NYC. This is because EU member states are under an obligation to vacate an arbitration clause when it clashes with the EU public policy.<sup>98</sup>

The European Court of Justice's (hereinafter ECJ) decision in *Elisa María Mostaza Claro v Centro Móvil Milenium SL*,<sup>99</sup> indicates that violation of the Unfair Terms Directive 1993 is a violation of public policy of the EU and it comes within the meaning of public policy under the NYC. This fact can be deduced from the analogy that the ECJ made in *Elisa* with the case of *Eco Swiss China Time Ltd v Benetton International NV*.<sup>100</sup> In the case of *Elisa*, the ECJ explained that:

“as the aim of the Directive is to strengthen consumer protection, it constitutes, according to Article 3(1)(t) EC, a measure which is essential to the accomplishment of the tasks entrusted to the Community and, in particular, to raising the standard of living and the quality of life in its territory. (See, by analogy, concerning Article 81 EC, *Eco Swiss*, paragraph 36).”<sup>101</sup>

In para.36 of *Eco Swiss* the ECJ explained that:

“according to Article 3(g) of the EC Treaty (now, after amendment, Article 3(1)(g) EC), Article 81 EC (ex Article 85) constitutes a fundamental provision which is essential for the accomplishment of the tasks entrusted to the Community and, in particular, for the functioning of the internal market. The importance of such a provision led the framers of the Treaty to provide expressly, in Article 81(2) EC (ex Article 85(2)), that any agreements or decisions prohibited pursuant to that article are to be automatically void.”<sup>102</sup>

The ECJ also explained that:

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<sup>98</sup>C-126/97 (ECJ 01.06.1999). Para.36

<sup>99</sup>C-168/05 (ECJ 26.10.2006).

<sup>100</sup>C-126/97 (ECJ 01.06.1999).

<sup>101</sup>C-168/05 (ECJ 26.10.2006). Para. 37.

<sup>102</sup>C-126/97 (ECJ 01.06.1999). Para.36

“For the reasons stated in paragraph 36 above, the provisions of Article 81 EC (ex Article 85) may be regarded as a matter of public policy within the meaning of the New York Convention.”<sup>103</sup>

Analysing the analogy that the ECJ made between the cases *Elisa* and *Eco Swiss* led to an important result. It is that the protection awarded to the consumer from unfair arbitration clauses in the Unfair Terms Directive 1993 comes within the scope of the public policy exception to the enforcement under the NYC. In the case of *Eco Swiss* the ECJ explained that ‘provisions of Article 81 EC may be regarded as a matter of public policy within the meaning of the New York Convention 1958’.<sup>104</sup> The ECJ justified this conclusion by referring to reasons mentioned in paragraph 36 of the case of *Eco Swiss*. In paragraph 36 the ECJ explained that article 81 of the EC Treaty represents a ‘fundamental’ provision that is important to achieve the ‘tasks entrusted to the community, in particular, for the functioning of the internal market’.<sup>105</sup> In the case of *Elisa* the ECJ explained that the Unfair Terms Directive 1993 is ‘fundamental’ to achieve one of the most important tasks delegated to the EU Community which is ‘raising the life standard and quality of life in the EU Community’. The analogy point between the two cases is the fundamentality.<sup>106</sup> The Unfair Terms Directive 1993 shares, with Article 81 of the EC Treaty, the characteristic of the fundamentality to achieve ‘tasks entrusted to the community’.<sup>107</sup> The fundamentality of the Unfair Contract Terms Directive 1993 for ‘raising the life standard and quality of life in the EU Community’<sup>108</sup> has made the violation of its

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<sup>103</sup>C-126/97 (ECJ 01.06.1999). Para.39.

<sup>104</sup>Ibid, Para.36

<sup>105</sup>Ibid

<sup>106</sup>Christoph Liebscher, “European Public Policy: A Black Box?”, (2000) 17(3) J. Int’l. Arb.73, 77.

<sup>107</sup>C-168/05 (ECJ 26.10.2006).

<sup>108</sup>Ibid

rules fall within the meaning of EU public policy and within the meaning of public policy exception under the NYC.

The protection awarded to the consumer by arbitration clauses under the Unfair Terms Directive 1993, which comes within the meaning of public policy under the NYC, according to the case of *Elisa*, is represented in the minimum standards of consumer protection from any unfair term in standard form B2C contract that the directive seeks to harmonise between the different member states laws.<sup>109</sup> The essence of these minimum standards that the directive establishes can be summarised in that the unfairness test embodied in Article 3 of the directive. Article 6(1) also provides that any unfair term is not binding on the consumer, as well as, Article 3 refers to a set of terms which ‘may be considered unfair’ that is included in an ‘indicative’ list annexed to the directive. Term 1(q) of the indicative list states that:

“excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration not covered by legal provisions”.<sup>110</sup>

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<sup>109</sup>Sally Wheeler and Jo Shaw, *Contract Law: Cases, Materials and Commentary*, (Clarendon Press, Oxford, 1994), p.664.

<sup>110</sup>Term 1(q) of the Indicative List Annexed to the Unfair Contract Terms Directive 1993. Term 1(q) has generated lots of criticism in academic literature. Term (q) specifies a particular type of arbitration that might be considered unfair, it refers to “... arbitration not covered by legal provisions...”. However, what is meant by “... arbitration not covered by legal provisions ...” and does this reference to arbitration not covered by legal provisions mean that arbitration covered by legal provisions is not unfair or less likely to be unfair. It seems that there is no agreement between legal scholars on the interpretation of wording of term (q). For more information see-William. W. Park. “Amending the Federal Arbitration Act”, (2002) 13 Am.RevInt’l.Arb.75, at p.130; also see-Christopher Kuner, “Legal Obstacles to ADR in European Business-to-Consumer Electronic Commerce”, available at: <http://www.ilpf.org/events/jurisdiction2/presentations/kuner%5Fpr/> accessed on 20/11/2004.

Although Term 1(q) expressly targets arbitration clauses in B2C contracts this does not mean that arbitration clauses in B2C contracts are prohibited under the Directive. The reason is that the list which includes Term 1(q) is only indicative, as the European Commission explained:

“since the list is indicative, a contractual term corresponding to one of the examples in the annex is not automatically deemed unfair. However, it is an invaluable tool both for courts, the authorities and the economic operators”.<sup>111</sup>

In the case of *Zealand & Zealand v Laing Homes Limited*,<sup>112</sup> Havery, J., described Schedule 3 of the Unfair Terms Regulations 1994<sup>113</sup> which transfers the indicative list of the directive into UK law as ‘merely guidelines’. Therefore, it can be said that these minimum standards of consumer protection embodied in the directive, which come within the meaning of public policy under the NYC, do not prohibit arbitration clauses in standard form B2C contracts. Yet, an arbitration clause that violates these minimum standards will violate the public policy of the EU. These minimum standards are transferred into English law through the provisions of the 1999 Regulations as mentioned supra. If a B2C arbitration clause introduced to the English Court to be enforced under the rules of the NYC, the English Court cannot enforce the arbitration clause if it violates the provisions of the 1999 Regulations that transfer these minimum standards of protection that are embodied in the directive. The reason is that, as explained above, violation of these minimum standards is a violation of the EU public policy within the meaning of the NYC and

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<sup>111</sup> Report from the Commission on the Implementation of Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts COM (2000) 248 final.

<sup>112</sup> 98TCC602 [1999], this case is unreported and it is only available via Lawtel Database.

<sup>113</sup> Unfair Terms in Consumer Contract Regulations 1994 has been revoked by the 1999 Regulations.

the ECJ has put EU member states under an obligation to vacate arbitral clauses and awards when they violate EU public policy. This what the ECJ explained in *Eco Swiss*. The ECJ asserted that:

“it follows that where its domestic rules of procedure require a national court to grant an application for annulment of an arbitration award where such an application is founded on failure to observe national rules of public policy, it must also grant an application where it is founded on failure to comply with the prohibition laid down in Article 81(1) EC (ex-Article 85(1)).”<sup>114</sup>

This means that EU member states hold the burden of protecting EU public policy in the same way as they protect their international public policy. In other words, EU public policy is part of each member state’s international public policy.

The second evidence indicates that not only Section 89 of the Arbitration Act 1996 but also Section 91 come within the meaning of English international public policy, and thereby comes within the meaning of public policy under the NYC. This factor is that Section 89(3) of the Arbitration Act 1996 provides that Sections 89 and 91 apply “whatever the law applicable to the arbitration agreement”.<sup>115</sup> Sections 89 and 91 are international mandatory rules. Morse explained the meaning of international mandatory rules and he wrote that:

“[A]n initial distinction needs to be drawn between rules which are mandatory in only a domestic context and rules which are mandatory regardless of the presence of relevant foreign elements on the case. Whether a rule belongs to the former or the latter category cannot be resolved by reference to any

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<sup>114</sup>C-126/97 (ECJ 01.06.1999). para. 49.

<sup>115</sup>The Arbitration Act 1996, S.89(3).

universal criteria. If the rule is contained in the statute, its nature may be expressly indicated in the statute itself.”<sup>116</sup>

Morse has drawn a distinction between rules that are mandatory on the domestic level and rules that are still applicable even when the foreign element is present. He said there is no fixed method which can be used to distinguish between the two types of mandatory rules. However, a mandatory rule is an international mandatory rule if the legislation that includes it does not allow excluding it from application by the choice of another country’s law.

Further evidence for the fact that Sections 89 and 91 of the English Arbitration Act 1996 come with the meaning of public policy under the NYC can be derived from its predecessor the Consumer Arbitration Agreement Act 1988.<sup>117</sup> The Consumer Arbitration Agreements Act 1988 is now invoked by Sections 89, 90 and 91 of the English Arbitration Act 1996. The 1988 Act prohibited arbitration clauses in B2C contracts when the value of the claim is within the jurisdiction of the County Court.<sup>118</sup> However, this law was only applicable to domestic arbitration agreements.<sup>119</sup> The 1988 Act expressly excluded the NYC arbitration agreements from its scope of application. Section 2(a) of the 1988 Act provides that this Act does not effect:

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<sup>116</sup>M. Rubino-Sammartano and C.G.J. Morse, *Public Policy in Transnational Relationship*, (Kluwer law & Taxation publishers, Boston, 1991), (England-p.17).

<sup>117</sup>The Consumer Arbitration Agreement Act 1988.

<sup>118</sup>Geraint G Howells, “Legislative Comment: Consumer Arbitration Agreement Act 1988”, (1989) 10(1)Comp. Law. 20-21.

<sup>119</sup>Ibid

“the enforcement of an arbitration agreement to which section 1 of the [1975 c. 3.] Arbitration Act 1975 applies, that is, an arbitration agreement other than a domestic arbitration agreement within the meaning of that section;”<sup>120</sup>

The aim of enacting the UK Arbitration Act 1975 was implementing the NYC into UK law. Section 1 of the UK Arbitration Act 1975 provides that the Act applies to the enforcement of non-domestic arbitration agreement. An arbitration agreement is not domestic if all parties to it are not habitually resident in the UK, as well as, the seat of arbitration must refer “expressly or by implication, for arbitration in a State other than the United Kingdom”.<sup>121</sup>

Sections 89 and 91 of the English Arbitration 1996 come within the meaning of public policy exception to enforcement under the NYC. This is because if the drafters of these sections did not want them to apply on NYC arbitration clauses, they would have expressly stated that in the same way as in the Consumer Arbitration Agreement Act 1988 or, at least, the drafters would not forbid the exclusion of Sections 89 and 91 from application by the choice of another country’s law. What is more, Lord Fraser of Carmyllie explained in *Hansard* that there should not be any link between the scope of application of Sections 89 and 91 of the 1996 Act and the definition of the domestic arbitration agreement embodied in Section 85 of the same Act.<sup>122</sup>

It is true that mandatory rules that prohibit or restrict arbitration clauses in B2C contracts aim to protect the consumer. However, the protection is sometimes limited

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<sup>120</sup>S. 1(a), the Consumer Arbitration Agreements Act 1988.

<sup>121</sup>Section 1(2), English Arbitration Act 1975.

<sup>122</sup>Lord Fraser of Carmyllie, *Hansard* HL Vol 571 No 72 columns 152 (2 April 1996).



as in the case of Section 91 of the English Arbitration Act 1995. It only protects the consumer if the value of the claim is £5000 or less. It is sometimes not effective as in the case of the unfairness test embodied in the 1999 Regulations. As explained in chapter two, the consumer knowledge about the arbitration clause is important for his confidence in online arbitration. However, the unfairness test of 1999 Regulations does not oblige the business to give the consumer a specific notice about the existence of the arbitration clause in the B2C e-commerce contract. What is more, the fact these mandatory rules come within the meaning of the public policy exception under the NYC may have negative impact on the business. Rules that prohibit arbitration clause in B2C contracts, such as Section 91 of the English Arbitration Act 1996 will prevent the business from inserting an arbitration clause into the B2C e-commerce contract. This is because the business will not be able to enforce the arbitration clause against the consumer. The same applies on the unfairness test embodied in the 1999 Regulations. The fact that the arbitration clause is subject to the unfairness test makes the business hesitant to insert an arbitration clause into the B2C e-commerce contract.

Adopting a new rule that stipulates the knowing and intelligent standard of consent to online B2C arbitration clauses will help both the consumer and the business. The rule will place the business under the obligation to disclose the existence of the arbitration clause in the e-commerce contract to the consumer. In the same time, such a new rule will assure the business that the arbitration clause is more likely to be enforceable against the consumer. The suggested rule permits arbitration clauses in cross-border online B2C contract when the clause complies with the criteria of

consent mentioned above. This means that if the suggested rule is implemented into an international convention that regulates online B2C arbitration, different countries, when adhering to this Convention, will be under an obligation to enforce a cross-border arbitration clause included in an online B2C contract regardless of whether their national rules of consumer protection allow or prohibit arbitration clauses in B2C contracts. This will encourage the business to insert an arbitration clause into the B2C e-commerce contract.

To sum up this section, in countries where arbitration clauses are prohibited or restricted, this prohibition or restriction is implemented through mandatory rules. It is true that the scope of public policy exception to enforcement of an arbitration clause under the NYC has been narrowed and it means international public policy. However, mandatory rules that prohibit or restrict arbitration clauses in B2C contracts come within the meaning of international public policy. This may prevent the business from enforcing an online B2C arbitration clause against the consumer. This may discourage him from agreeing to arbitrate future disputes with the consumer via an arbitration clause. If a convention that stipulate the knowing and intelligent standard of consent to online B2C arbitration clause is adopted, the business will be more certain about the enforceability of the online arbitration clause against the consumer. This is because this rule will override any national rule that prohibit arbitration clause in the B2C e-commerce contracts.

### **3. Conclusion**

In conclusion, both the consumer and the business will not be ready to agree on arbitrating future e-commerce disputes if they have serious doubts about the enforceability of the online B2C arbitration clause. The enforcement of an online B2C arbitration clause is most likely to take place under the NYC. Article II(2) of the NYC constitute a source of uncertainty for the consumer and the business about the enforceability of their online arbitration clause. Article II(2) states that an arbitration clause is in writing if it is included in a contract signed by the parties or in contract concluded via exchange of letters or telegrams. Article II(2) does not indicate that the Internet is one of the communication means that can be used to conclude legally recognized arbitration clauses. E-communications Convention 2005 has not eliminated the legal uncertainty resulting from the question of whether an arbitration clause in an online B2C contract satisfies the writing requirement under Article II(2) of the NYC. Expanding the term 'Telegram' in Article II(2) to cover the Internet or reliance on the most favourable law provision under Article VII(1) of the NYC does not help to effectively eliminate this legal uncertainty. This is because both solutions are subject to different interpretations by the courts of the state-signatories to the NYC.

Procuring the business consent to the online arbitration through an online B2C arbitration clause is so important for the consumer. This is because the business receives the payment before the performance of the e-commerce contract. Therefore, it is difficult to obtain the business consent to arbitrate after the occurrence of the dispute. However, the enforcement of an arbitration clause under the NYC may be

refused if the arbitration clause violates the public policy of the enforcing state. It is true that public policy exception to enforcement of arbitration clause under the NYC has been narrowed to mean international public policy of the forum and truly international public policy. However, mandatory rules that prohibit or restrict arbitration clauses in B2C contracts come within the meaning of international public policy of the forum. This makes the business uncertain whether the online B2C arbitration clause will be enforced against the consumer. This may discourage the business from agreeing to arbitrate future e-commerce dispute with the consumer.

Adopting a new convention that stipulates the knowing and intelligent standard of consent to online B2C arbitration clause will increase certainty about the enforceability of the online B2C arbitration clause. The suggested model convention gives legal recognition to arbitration clauses in online B2C contracts when the consumer has knowingly and intelligently consented to the online arbitration clause. Therefore, under this model, it is prima facie that the use of the internet to conclude the cross-border B2C arbitration clause is legally recognised. Adhering to a convention that implements the suggested rule will encourage the business to insert an arbitration clause into the B2C contract. This is because different countries, when adhering to this Convention, will be under an obligation to enforce an online B2C arbitration clause regardless of whether their national rules allow or prohibit arbitration clauses in B2C contracts.

## **Chapter 5**

# **The Application of the Law of the Consumer's Country of Domicile to the Subject Matter of the Dispute**

For the consumer to have confidence in online arbitration, the consumer must enjoy the protection that is awarded to him under the law of his country of domicile. The OECD members have been attentive to the fact that consumers are in need to the protection of the laws of their countries of domicile. The OECD Guidelines for Consumer Protection in the Context of Electronic Commerce 1999 asserted that when the consumer transacts online, they should obtain “a level of protection not less than” the one they obtain offline.<sup>1</sup> In bricks and mortar commerce, the consumer enjoys the protection of the law of his country of domicile. This means that, in the context of B2C e-commerce the consumer should also enjoy the protection of the law of his country of domicile. Ponte has also been attentive to fact that consumers need to enjoy the protection of the law of their countries of domicile when they transact online with cross-border businesses. He explained that “if the ultimate goal is to boost e-consumer confidence, the selection of the fora and the laws that benefit only e-businesses do not promote that goal.”<sup>2</sup>

However, this chapter argues that a choice of law clause imposed by the business deprives the consumer of the protection that is awarded to him under the law of his country of domicile. Therefore, in order to instil the consumer confidence in online

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<sup>1</sup>OECD Guidelines for Consumer Protection in the Context of Electronic Commerce, 1999.

<sup>2</sup> Lucille M. Ponte, “Boosting Consumer Confidence in E-Business: Recommendations for Establishing Fair and Effective Dispute Resolution Programs for B2C Online Transactions”, (2002) 12 Alb. L. J. Sci. & Tech.441, 487.

arbitration, a rule that stipulates the application of the law of the consumer's country of domicile to the subject matter of the dispute should be in place. Two reasons have encouraged the present author to choose the consumer's country of domicile as the criterion to determine the applicable substantive. First, no one can be without a domicile.<sup>3</sup> Every person has a domicile. Second, no one can have more than one domicile at the same time, whereas, a person can have more one residence, home, or nationality at the same time.<sup>4</sup> This means that reliance on the domicile as criterion gives more certainty to the parties.

The first part of this chapter explains that choice of substantive law clause deprives the consumer of the protection that is awarded to him under the law of his country of domicile. The first section of this part explains that arbitrators are not under the legal duty to comply with foreign mandatory rules. The second section explains that the arbitrator discretion does not always lead to the application of the mandatory rules of the consumer's country of domicile. The second part of this chapter explains that a rule that stipulates the application of the law of the consumer's country of domicile to the subject matter of the dispute should be adopted in order to raise the consumer confidence in online arbitration.

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<sup>3</sup> J. G. Collier, *Conflict of Laws*, (3<sup>rd</sup> ed, CUP,2001), p.38.

<sup>4</sup>Ibid

## **1. Choice of Law Clause Deprives the Consumer of the Protection of the Law of His Country of Domicile**

Consumer protection rules are usually divided into mandatory and non-mandatory rules. Mandatory rules are also divided into domestic mandatory rules and international mandatory rules.<sup>5</sup> The difference between the two is that the first can be excluded from application by a choice of law clause that designates a different country's law.<sup>6</sup> The second applies despite the fact that a different country's law has been selected by a choice of law clause.<sup>7</sup> In the context of the online arbitral process, a choice of law clause deprives the consumer of the protection awarded to him under all types of mandatory rules of the law of his country of domicile. The reasons are that arbitrators are not obliged to comply with legal rules imposing a duty<sup>8</sup> to comply with foreign mandatory rules.<sup>9</sup> The discretion of the arbitrator does not always lead to the application of mandatory rules of the consumer's country of domicile.<sup>10</sup> In the coming subsections, the current author will explain these two issues.

### **1.1 No Legal Duty to Comply with Foreign Mandatory Rules**

Domestic and international mandatory consumer protection rules usually include the essential protection awarded to the consumer. For example, the consumer's right to a

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<sup>5</sup>Nathalie Voser, "Mandatory Rules of Law as a Limitation on the Law Applicable in International Commercial Arbitration", (1996) 7 Am. Rev. Int'l Arb. 319,322.

<sup>6</sup>Ibid

<sup>7</sup>Ibid

<sup>8</sup>Pierre Mayer, "Mandatory Rules of Law in International Arbitration", (1986) 2(4) Arb. Int'l. 274, 275. (hereinafter Mandatory Rules)

<sup>9</sup>Foreign mandatory rules in this context means mandatory rules of law other than the law mentioned in the choice of law clause.

<sup>10</sup>Mohammad Reza Baniassadi, "Do Mandatory Rules of Public Law Limit Choice of Law in International Arbitration?", (1992-1993) 10 Int'l Tax & Bus. Law. 59, 65.

cooling-off period embedded in the mandatory rules of the Consumer Protection (Distance Selling) Regulations 2000.<sup>11</sup> However, a choice of law clause deprives the consumer of the protection awarded to him under both types of mandatory rules. An Arbitrator is not under the obligation to comply with mandatory rules other than those that belong to the law mentioned in the choice of law clause.<sup>12</sup> Legal rules imposing a duty to comply with foreign mandatory rules are not obligatory to arbitrators.<sup>13</sup> The NYC does not include any provision that explains the arbitrator's duty to comply with foreign mandatory rules.<sup>14</sup> Prof. Mayer explained that the absence of such provisions is attributed to the fact that mandatory rules of law were "hardly ever discussed" at the time the NYC was adopted.<sup>15</sup>

Other types of international and national conflict of laws rules do include rules that oblige the arbitrator to comply with foreign mandatory rules. In England, the Rome Convention 1980<sup>16</sup> embraces detailed provisions explaining the duty to comply with foreign mandatory rules. Articles 3, 5 and 7 of the Rome Convention 1980 include provisions to impose an obligation to comply with foreign mandatory rules even though there is a choice of law clause. In the US, §187(2)(b) of the Restatement (Second) of Conflict of Laws (1971) includes a rule explaining the duty to comply with foreign mandatory rules.<sup>17</sup> §1-301(e) of the Uniform Commercial Code also

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<sup>11</sup> Regulation 11, 12, The Consumer Protection (Distance Selling) Regulations 2000, SI 2000/2334

<sup>12</sup> Andrew T. Guzman, "Arbitrator Liability: Reconciling Arbitration and Mandatory Rules", (1999-2000) 49 Duke L. J. 1279, 1280.

<sup>13</sup> Mayer, note 8 *supra*, (Mandatory Rules), p.275

<sup>14</sup> *Ibid*

<sup>15</sup> *Ibid*

<sup>16</sup> This is implemented in the whole of the UK by the Contracts (Applicable Law) Act 1990.

<sup>17</sup> §187(2)(b), Restatement (Second) of Conflict of Laws 1971.



includes rules explaining the duty to comply with foreign mandatory rules when one of the parties is a consumer.

However, an arbitrator sitting in London is not obliged by the rules of the Rome Convention 1980 imposing a duty to comply with foreign mandatory rules.<sup>18</sup> An arbitrator sitting in New York is not also obliged by the rules recognised in the US federal law and which impose a duty to comply with foreign mandatory rules.<sup>19</sup> The reason is that rules establishing this duty are conflict of laws rules. With the influence of the delocalisation trend, the arbitrator is not obliged by any particular conflict of laws rules.<sup>20</sup> Section 46(3) of the English Arbitration Act 1996 states that an arbitrator is not obliged by any particular type of conflict of laws rules. Likewise, the FAA does not impose an obligation on the arbitrator to comply with foreign mandatory rules.<sup>21</sup> It also does not impose any conflict of laws rules on the arbitrator.

In England, if the Rome Convention 1980 was obligatory to arbitrators, a choice of law clause might not deprive the consumer the fundamental protection of the law of his country of domicile. This is, of course, when England is the place of arbitration. The Rome Convention 1980 includes three channels that might lead to the application of mandatory rules of the consumer domicile even though there is a choice of law clause. Article 3(3) of the Rome Convention 1980 includes rules that

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<sup>18</sup>C. M.V. Clarkson and Jonathan Hill, *The Conflict of Laws*, (3<sup>rd</sup> edn, OUP, Oxford, 2006) p.256.

<sup>19</sup>Peter V. Baugher and Steven M. Austermiller, "A New Way to Resolve International Business Disputes in Illinois", (2000) Illinois Bar Journal, available at: <  
<http://www.illinoisbar.org/IBJ/oct00lj/p582.htm>>, accessed on 12/06/2007

<sup>20</sup>Stewart R. Shackleton, "The Applicable Law in International Arbitration Under the New English Arbitration Act 1996", (1997) 13(4) J. Int'l. Arb.375, 375.

<sup>21</sup>Gary B. Born, *International Commercial Arbitration*, (2<sup>nd</sup> edn, Kluwer Law International, The Hague, 2001). (hereinafter international commercial).  
p.537.

can lead to the application of domestic and international mandatory rules of a particular country.<sup>22</sup> This is in the case that this country is the only country connected with “elements relevant to the situation at the time of the choice.”<sup>23</sup> However, it is highly unlikely all elements relevant to the choice of law clause in cross-border B2C e-commerce contracts are connected to one country. This is because both the business and the consumer take action to conclude the contract within different jurisdictions.<sup>24</sup> Article 5(2) is the most important for the consumer in respect to the applicability of mandatory rules of his country of domicile. It establishes a duty to comply with mandatory rules of the consumer habitual place of residence. It states that:

“2. ... a choice of law made by the parties shall not have the result of depriving the consumer of the protection afforded to him by the mandatory rules of the law of the country in which he has his habitual residence:

- if in that country the conclusion of the contract was preceded by a specific invitation addressed to him or by advertising, and he had taken in that country all the steps necessary on his part for the conclusion of the contract...”<sup>25</sup>

Article 5(2) stipulates the application of mandatory consumer protection rules of the consumer domicile. This is despite the fact that there is a clause in the contract pointing to another country’s law.<sup>26</sup> However, there are certain conditions that must be met in order to give effect to mandatory rules under Article 5(2). First, Article 5(2) does not distinguish between domestic and international mandatory rules of the

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<sup>22</sup>Art. 3(3), Rome Convention 1980

<sup>23</sup>Ibid

<sup>24</sup>Lorna E Gillies, “Choice-of-Law Rules For Electronic Consumer Contracts: Replacement of the Rome Convention by the Rome I Regulation”, (April 2007) J. P.Int’l. L. 89. 97. (hereinafter choice of law).

<sup>25</sup>Art. 5(2), Rome Convention 1980.

<sup>26</sup>Paul J. Omar, “Consumer Litigation: An International Perspective”, (1999) 10(5) I.C.C.L.R.148, 150.

consumer domicile.<sup>27</sup> In other words, domestic mandatory consumer protection rules can be applied according to Article 5(2). However, the mandatory rule must be a consumer protection rule.<sup>28</sup> Mandatory rules that do not relate to consumer protection cannot claim effect under Article 5(2).<sup>29</sup> Second, the consumer must be a 'passive consumer'<sup>30</sup>. For the consumer to be a passive consumer certain requirements must be met. The consumer will be considered a passive consumer if the conclusion of the contract has taken place in the country of the consumer's usual residence.<sup>31</sup> This has to be a consequence of a proposal or advertisement specially directed to the consumer. Eventually, the consumer has performed in that country all acts required for the execution of the contract.<sup>32</sup>

However, the application of these requirements on B2C e-commerce disputes may lead to novel difficulties. First, stipulating the conclusion of the contract in the country of the consumer clashes with the fact that websites and emails are accessible from everywhere.<sup>33</sup> It is possible today for the consumer to place an order for goods or services using websites or email while he is on an aircraft or a boat.<sup>34</sup> It is also

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<sup>27</sup>Reinhard Schu, "The Applicable Law to Consumer Contracts Made over the Internet: Consumer Protection through Private International Law", (1997) 5 Int'l J.L. & Info. Tech. 192, 209.

<sup>28</sup>Christopher Tillman, "The Relationship between Party Autonomy and the Mandatory Rules in the Rome Convention", (2002) J.B.L. 45, 52, 53.

<sup>29</sup>Ibid

<sup>30</sup>Axel Halfmeier, "Waving Goodbye to the Conflict of Laws? Recent Developments in European Union Consumer Law", in Charles E.F. Rickett and Thomas G. W. Telfer, *International Perspective on Consumers' Access to Justice*, (CUP, Cambridge, 2003), p.390.

<sup>31</sup>Art. 5(2), Rome Convention 1980

<sup>32</sup>Ibid.

<sup>33</sup>Denise Estrella Tellini, "Applicable Law and Electronic Consumer Contracts: a European Perspective", (2005) 16(1) I.C.C.L.R. 1, 3.

<sup>34</sup>Ibid.

easy for internet users to conceal their actual location.<sup>35</sup> Second, regarding invitation and advertisement, the fact that websites are accessible to everyone from everywhere on earth makes it very difficult to know whether the consumer searched to find the website. Or if he visited the website following an advertisement such as a banner or a link placed on other websites.<sup>36</sup> Furthermore, as Gillies explained a website does not come within the traditional meaning of advertising that the Giuliano Lagarde Report mentioned. The Report referred to various methods of advertising and sending offers which the website and email are not among them.<sup>37</sup> The Report refers to advertising in the press, on the radio or television or in the cinema or by catalogues. Alternatively, by an offer that is sent to the consumer through commercial representatives, or mail.<sup>38</sup>

Attempts have been made to distinguish between passive and active websites. A website that only gives the consumer information about the products and services offered by the business is not an active website. It is also unlikely to fall within the scope of Article 5(2) of the Rome Convention 1980, unless the consumer proves that an invitation to visit that website was sent to him. He then decided to conclude the contract with the business.<sup>39</sup> A website that allows consumers to place orders for goods and services is an active website. Such a website comes within the scope of

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<sup>35</sup>Lorna E. Gillies, "Adapting International Private Law Rules for Electronic Consumer Contracts", in Charles E.F. Rickett and Thomas G. W. Telfer, *International Perspective on Consumers' Access to Justice*, (CUP, Cambridge, 2003), p.371.

<sup>36</sup>Gillies, (Choice-of-Law), note 24 supra, p.102.

<sup>37</sup>Giuliano Lagarde Report.

<sup>38</sup>Ibid

<sup>39</sup>Tellini, note 33 supra, p.4.

Article 5(2) of the Rome Convention 1980.<sup>40</sup> The Rome Convention is currently under revision and it will be replaced by Rome I Regulation.<sup>41</sup> The Rome I Regulation Proposal gives the consumer more protection than the Rome Convention 1980. Article 5 stipulates the application of the law of the consumer's place of habitual residence in cross-border disputes. There is more certainty and protection under the proposed regulation than under the Convention. This is because under the Convention the mandatory rules of the consumer's place of habitual residence will be applied with the law chosen by the business.<sup>42</sup> Furthermore, the suggested regulation does not stipulate the conclusion of the contract in the country where the consumer habitually resides.<sup>43</sup> However, the Rome I Regulation Proposal requires an act of "targeting" by the business of the consumer.<sup>44</sup> Under the Rome I Regulation Proposal, the law of the consumer's place of habitual residence will be applied if the business has targeted the consumer's country by its activities.<sup>45</sup> The difficulties in determining whether the business targeted the consumer, in online context as explained above, still appear.

In the US, the choice of law rules also include rules explaining the duty to comply with foreign mandatory rules, which would also lead to the application of the law of the consumer's domicile if it was obligatory on the arbitrator. §187(2)(b) of the Restatement (Second) Conflict of Laws (1971) provides that the choice of law will

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<sup>40</sup>Tellini, note 33 supra, p.4.

<sup>41</sup>Commission of the European Communities, "Proposal for a Regulation of the European Parliament and the Council on the Law Applicable to Contractual Obligation (Rome I)", 2005/0261/COD

<sup>42</sup>Ibid, p.6.

<sup>43</sup>Ibid

<sup>44</sup>Gillies, (Choice-of-Law), supra note 24, p.100.

<sup>45</sup>E. B. Crawford and J.M. Carruthers, "Conflicts of Laws Updates", (2003) 16, S.L.T.A. 137-141.

be overridden by the laws that represent the fundamental public policy of another state.<sup>46</sup> This is in case the law of another state would be the applicable law in the absence of a choice of law clause.<sup>47</sup> §187(2)(b) does not specifically mention mandatory rules. However, mandatory rules, especially international mandatory rules, do reflect the fundamental public policy of the state.<sup>48</sup> Nevertheless, §187(2)(b) is of limited effectiveness in terms of obligation to comply with foreign mandatory rules. It only applies in the case of violation of the fundamental public policy of the state that its law would apply according to the standards embedded in §188(2) of the Restatement (Second) Conflict of Laws (1971) in the absence of the choice of law clause.<sup>49</sup>

The newly suggested amendments to the US Uniform Commercial Code also include clear rules that explain the duty to comply with mandatory consumer protection rules.<sup>50</sup> §1-301(e) provides that a choice of law clause shall not deprive the consumer of the protection that he enjoys under the international mandatory consumer protection rules of law of his country of domicile.<sup>51</sup> It also provides that if the consumer concludes a contract and receives the goods in another country, a choice of law clause should not deprive the consumer of the protection of international mandatory consumer protection rules of that country. Although the

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<sup>46</sup> §187(2)(b), Restatement Second of Conflict of Laws 1971.

<sup>47</sup> Ibid.

<sup>48</sup> Baniassadi, note 10 supra, p.62, 63.

<sup>49</sup> *Massengale v Transitron Electronic Corp*, 385 F.2d 83 C.A.Mass,1967.

<sup>50</sup> These amendments are suggested by the National Conference of Commissioners on Uniform State Laws (NCCUSL) and the American Law Institute (ALI).

<sup>51</sup> §1-301(e), United States Uniform Commercial Code. From the 29 states that have adopted the new suggested amendment on Uniform Commercial Code only the state of Virgin Islands has adopted §1-301(e).<sup>51</sup>

drafter of §1-301(e) of the UCC considered Article 5(2) of the Rome Convention 1980<sup>52</sup>, there is a difference between the two of them. §1-301(e) only awards the consumer the protection that he enjoys under international mandatory consumer protection rules of the law of his domicile, or the law of the place where he concluded the contract and received the goods. Whereas, Article 5(2) awards the consumer the protection that he enjoys under both domestic and international mandatory consumer protection rules. Unlike Article 5(2) of the Rome Convention 1980, §1-301(e) does not require any previous invitation from the business to the consumer in order to be applied.

To sum up this section, a choice of law clause deprives the consumer of the protection that is awarded to him under the law of his country of domicile. This happens because rules that impose a duty to comply with mandatory rules of the law of the consumer's country of domicile are not obligatory to arbitrators.

## **1.2 Arbitrator's Discretion**

The absence of a clear legal duty to comply with foreign mandatory rules makes the question of compliance with such rules subject to the arbitrator's discretion.<sup>53</sup> However, the arbitrator's discretion does not always lead to the application of the mandatory rules of the consumer's domicile.<sup>54</sup> This is because of two reasons. First, arbitrators might adhere to the view that arbitrators derive their authority from the parties' agreement and, thereby, they are obliged to comply with the choice of law

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<sup>52</sup>William J. Woodward, Jr., "Contractual Choice of Law: Legislative Choice in an Era of Party Autonomy", (2001) 54 S.M.U. L. Rev. 697, 732.

<sup>53</sup>Baniassadi, note 10 *supra*, p.66.

<sup>54</sup>*Ibid*, p.84

clause.<sup>55</sup> Second, the nature of B2C e-commerce disputes does not encourage the arbitrator to apply the mandatory rules of the consumer domicile in order to avoid rejection of enforcement of the arbitral award. In the coming two subsections, the author will explain these two issues.

### **1.2.1 Arbitrator Allegiance to the Choice of Law Clause**

An arbitrator may refuse to replace the law determined in the choice of law clause by the mandatory rules of the consumer domicile. This is because he derives his authority from the parties' agreement.<sup>56</sup> In other words, the arbitrator is only obliged by the choice of law clause.<sup>57</sup> He has no obligation to apply mandatory rules that do not constitute part of the chosen law.<sup>58</sup> Derains affirmed this view when he observed that: "(T)he principle whereby arbitrators are bound to apply the law chosen by the parties is sometimes all that is needed for them to set aside a mandatory rule foreign to that law."<sup>59</sup>

An illustration of this view can be found in the ICC Case No. 1399 of 1967.<sup>60</sup> In this case French law was applicable to a licensing contract between the French licensor and the Mexican Licensee. However, in order to perform the contract, Mexican customs regulations must be disregarded. The tribunal simply held that Mexican law

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<sup>55</sup>Baniassadi, note 10 *supra*, p.65.

<sup>56</sup>Daniel Hochstrasser, "Choice of Law and "Foreign" Mandatory Rules in International Arbitration", (1994) 11(1) *J. Int'l. Arb.* 57, 57.

<sup>57</sup>Yves Derains, "Public Policy and the Law Applicable to the Dispute in International Arbitration", (New York/1986) 3 *ICCA Congress*, p. 227, 247.

<sup>58</sup>Mayer, note 8 *supra*, p.282.

<sup>59</sup>Derains, note 57 *supra*, p.247.

<sup>60</sup>Award ICC Case No.1399 (1967), unpublished, see Lew, *Applicable Law*, p.550-552.



did not govern the contract. The contract was not illegal as a matter of French law.<sup>61</sup>

A similar situation can also be found in the decision issued by the Court of Arbitration of the Chamber of Foreign Trade of the German Democratic Republic GDR. The arbitrators had to rule on the validity of a licence agreement concluded between a company in the GDR and another firm in the Federal Republic of Germany (hereafter FRG). The second company claimed that the contract was invalid because it clashed with the competition law provisions of FRG and to Article 85 of the Treaty of Rome. The tribunal refused this allegation and asserted that: “The validity of the agreement must be judged under the law of the GDR designated in the arbitral clause as the law applicable to the agreement.”<sup>62</sup> The same approach was also adopted in the ICC case No. 6379 of 1990.<sup>63</sup> In this case a Belgian distributor and an Italian producer made their contract subject to Italian law. Seven years after the conclusion of the contract, the Italian provider sent a notice to the Belgian distributor telling him that the contract will be terminated after three months. Three months was the time stipulated in the contract.<sup>64</sup> However, basing his allegation on Belgian mandatory rules of law which provide that the notice should be made before 36 months, the Belgian distributor alleged that the termination clause in the distribution contract was not valid. The arbitrator sitting in Germany refused to apply the Belgian mandatory rules because the choice of law clause specified Italian law.<sup>65</sup> The view that an arbitrator is only obliged by the chosen law

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<sup>61</sup>Ibid

<sup>62</sup>G.D.R. Party -v- F. R.G. Party, 4 Y.B. Com. Arb. 198 (1979)

<sup>63</sup>ICC Case No. 6379 of 1990, 17 Y.B. COM. ARB. 212 (1992).

<sup>64</sup>Ibid

<sup>65</sup>Ibid

has produced a general trend in the arbitral practice that refuses the application of foreign mandatory rules.<sup>66</sup> Mayer noted that:

“one can discern more generally two opposing trends: one hostile to the application of mandatory rules of law, the other favourable. Given the relative scarcity of awards on point, it would be difficult to state which of these views is dominant. In fact, the impression is that they are roughly of equal force.”<sup>67</sup>

Mayer’s observation indicates that there is another view which accepts the application of foreign mandatory rules. This trend is almost of ‘equal force’ to the one that refuses the application of foreign mandatory rules. Voser explained that an arbitrator should apply foreign mandatory rules in order to avoid vacation of the arbitral award because of violation of public policy.<sup>68</sup> In fact, some arbitrators have applied foreign mandatory rules<sup>69</sup> because they are concerned about the enforceability of the arbitral award.<sup>70</sup> However, the nature of the B2C e-commerce disputes does not make the arbitrator concerned about the enforceability of the online B2C arbitral award. This is what the present author is going to explain in the coming section.

### **1.2.2 The Nature of B2C E-commerce Disputes Does not Make the Arbitrator Concerned about the Enforceability of the Online B2C Arbitral Award**

According to Article V(2)(b) of the NYC, recognition or enforcement of the arbitral award can be refused.<sup>71</sup> This is if the arbitral award violates the public policy of the

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<sup>66</sup> Mayer, note 8 supra, p.282

<sup>67</sup> Ibid

<sup>68</sup> Voser, note 5 supra, p.333-335

<sup>69</sup> Marc Blessing, “Mandatory Rules of Law versus Party Autonomy in International Arbitration”, (1997) 4(4) J. Int’l.Arb.23,39. (hereinafter Mandatory Rules).

<sup>70</sup> Andrew Barraclough and Jeff Waincymer, “Mandatory Rules of Law in International Commercial Arbitration”, (2005) 6 Melb. J. Int’l L. 205, 215.

<sup>71</sup> Art. V(2)(b), New York Convention 1958.

state where the enforcement is sought.<sup>72</sup> As explained in chapter four, public policy as an exception to recognition or enforcement under the NYC, has been interpreted to mean international public policy of the forum.<sup>73</sup> International mandatory rules might come within the scope of public policy exception to the enforcement under (NYC).<sup>74</sup> Arbitrators have shown a willingness to comply with the mandatory rules of the place of arbitration and the place where the enforcement of the arbitral award is likely to take place.<sup>75</sup> This is in order to avoid vacation of the arbitral award or the rejection of the enforcement of the arbitral award because of violation of public policy.

Many international mandatory rules of consumer protection might come within the meaning of public policy exception under the NYC. As explained in chapter four, in England, international mandatory consumer protection rules that represent the minimum standard of protection embedded in EU directives come within the scope of public policy under the NYC.<sup>76</sup> For example, the protection awarded to the consumer under Distance Selling Regulations 2000<sup>77</sup> comes within the meaning of public policy under the NYC.<sup>78</sup> An arbitral award that violates the said regulations might be annulled if England is the place of arbitration or the place of enforcement of the award.

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<sup>72</sup>Ibid

<sup>73</sup>For a detailed explanation of the scope and meaning of public policy under the NYC see section 2.1 of chapter four.

<sup>74</sup>Ibid

<sup>75</sup>Voser, note 5 supra, p.335.

<sup>76</sup>Arnold Vahrenwald, "Out-of-court dispute settlement systems for e-commerce". Report on legal issues. Part IV Arbitration. p.41. available at: < <http://www.vahrenwald.com/doc/part4.pdf> > accessed on 12/11/2005. (hereinafter Part IV Arbitration). See also at section 2.3 of chapter three. The explanation of the two decisions of the European Court of Justice in the cases of Eco Swiss and Elisa.

<sup>77</sup>The Consumer Protection (Distance Selling) Regulations 2000, SI 2000/2334

<sup>78</sup>Vahrenwald, note 76 supra, p.41.

However, the concern about the vacation of the online B2C arbitral award will not always motivate the tribunal to apply the mandatory rules of the consumer's country of domicile.<sup>79</sup> The reason is that the country of the consumer domicile is unlikely to be the place of arbitration or the place of enforcement of the arbitral award. The arbitration clause is usually accompanied by a choice of place of arbitration imposed by the business.<sup>80</sup> It is usually the country where the business headquarters is located.<sup>81</sup> Second, as Martin explained, in most B2C e-commerce disputes the consumer is the victim.<sup>82</sup> This means that in most cases the arbitral award will be enforced in the country where the business has assets. In other words, the consumer country of domicile is unlikely to be the place of enforcement of the arbitral award. Even in the rare case in which the consumer domicile is the likely place of enforcement, an arbitrator may not comply with the mandatory rules of the consumer domicile. This is because of the close connection test. As explained *supra*, consumers can conclude a contract with a business from different places in the world.<sup>83</sup> A consumer can even conclude a contract while he is aboard a ship or a

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<sup>79</sup>Voser, note 5 *supra*, p.335.

<sup>80</sup>Jean R. Sternlight, "Rethinking the Constitutionality of the Supreme Courts Preference for Binding Arbitration: A Fresh Assessment of Jury Trial, Separation of Powers, and Due Process", (1997) 72 Tul. L. Rev.1, 6. One might suggest there is no need to adopt a convention that stipulates the application of the law of the consumer domicile. This is because the suggested model of regulating online arbitration makes the country of the consumer domicile as the place of arbitration. This means that an arbitrator will comply with mandatory rules related to the applicable substantive law of the consumer domicile since it is the place of arbitration. However, making the consumer domicile as the place of arbitration will not always lead to the application of the mandatory of his domicile. This is because as explained in section 1.2.1 there is a trend in the arbitral practice that refuses to comply with mandatory rules that are not part of chosen law.

<sup>81</sup>*Ibid*, p.6.

<sup>82</sup>Mary Shannon Martin, "Keep it Online: the Hague Convention and the Need for Online Alternative Dispute Resolution in International Business-to-Consumer E-Commerce", (2002) 20 B.U. Int'l. L.J. 125,130.

<sup>83</sup>Tellini, note 33 *supra*, p.3.

plane. There are plenty of online services<sup>84</sup> which do not require delivery in the offline world. This means that it is likely that a consumer might conclude the contract and receive online services while he is away from his country of domicile.<sup>85</sup> In other words, it is possible that the only connection between the consumer domicile and the B2C e-commerce contract is that, it is the likely place of enforcement of the award. In such a case, the arbitrator might refuse to comply with the mandatory rules of the consumer domicile. This is because he might not consider the place of enforcement as sufficient connection. Article 9 of the Draft Recommendations on the Law Applicable to International Contracts (hereinafter Draft Recommendations of the ICC)<sup>86</sup> provides that:

“Alternative 2:

Even when the arbitrator does not apply the law of a certain country as the law applicable to the contract he may nevertheless give effect to the mandatory rules of the law of that country if the contract or parties have a close contact to the country in question especially when the arbitral award is likely to be enforced there, and if and in so far as under the law of that country those rules must be applied whatever be the law applicable to the contract.”<sup>87</sup>

The draft recommendation provides that in order to give effect to the mandatory rules of the place of enforcement, there should be a close connection between the country of the place of enforcement and the contract or the parties. One might argue that according to Draft Recommendations of the ICC, whenever the consumer domicile is the place of enforcement, the connection is established. This is because

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<sup>84</sup>Such as online journals.

<sup>85</sup>Tellini, note 33 supra, p.3

<sup>86</sup>This draft was prepared by the Working Group of the Commission on Law and Commercial Practices of the International Chamber of Commerce (ICC) in 1980

<sup>87</sup>Ole Lando, “Conflict of Law Rules for Arbitrators”, in *Festschrift für Konrad Zweigert* (1981), p. 176.

the consumer domicile is connected to one of the parties of the contract and this party is the consumer. However, the domicile alone is not sufficient to establish a connection, even if it is the likely place of enforcement. An illustration of this can be found in the arbitral award that was issued by the Amsterdam Grain Trade Association on 11 Jan 1982.<sup>88</sup> In this case a dispute arose from a contract for the sale of soya made between an Austrian company and a Dutch company. The Dutch law was applicable according to a choice of law clause. Although one of the parties is Austrian and Austria was the most likely place of enforcement of the arbitral award, the tribunal did not find sufficient connection with the currency law of Austria.<sup>89</sup> This is because the origin of the product sold and the nationality of the buyer were Dutch; the sale took place FOB Europoort,<sup>90</sup> through a German broker; and payment was requested to a German bank account. The application of Austrian law was, therefore, denied.

To sum up section 1.2 of this chapter, the arbitrator discretion does not always lead to the application of the mandatory rules of the consumer's country of domicile. The arbitrator derives his authority from the parties' agreement. In other words, he is only obliged by the choice of law clause. This is what the arbitral tribunal affirmed in the ICC Case No.6379 of 1990.<sup>91</sup>

Arbitral award can be vacated because of violation of public policy of the place of arbitration. The enforcement of the arbitral award can be refused if the arbitral award

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<sup>88</sup> Award of 11 January 1982, Vol. VIII Y. B. Com. Arb., 1983, p. 158, 160.

<sup>89</sup> Ibid

<sup>90</sup> Europoort is the Harbour of Rotterdam in Netherlands.

<sup>91</sup> ICC Case No. 6379 of 1990, 17 Y.B. COM. ARB. 212 (1992).

violates the public policy of the place of enforcement. Arbitrators have shown willingness to apply the mandatory rules of the place of arbitration to avoid vacation of the arbitral award because of violation of public policy. They have also shown willingness to apply the mandatory rules of the possible place of enforcement to avoid rejection of the enforcement of the arbitral award because of the same reason. Mandatory rules of consumer protection such the Distance Selling Regulations 2000<sup>92</sup> come within the scope of public policy exception to the enforcement of the arbitral award under the NYC. However, the fear about the vacation of the arbitral award or the fear about the rejection of the enforcement of the arbitral award will not encourage the arbitrator to apply the mandatory rules of the consumer's country of domicile. The business usually inserts a clause that designates the country where its headquarters are located as the place of arbitration. This means that the mandatory rules of the consumer domicile are not the mandatory rules of the place of arbitration. This means that, the mandatory rules of the consumer domicile do not constitute a source of concern about the vacation of the arbitral award because of violation public policy of the place of arbitration. The same also applies on the mandatory rules of the possible place of enforcement of the arbitral award. This is because in most B2C e-commerce disputes the consumer is the victim. This means that the consumer's country of domicile is not likely to be the possible place of enforcement of the online B2C arbitral award. Raising the consumer confidence in the online arbitral process requires adopting a rule that stipulates the application of the law of the consumer's country of domicile to the substantive issues of the dispute.

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<sup>92</sup>The Consumer Protection (Distance Selling) Regulations 2000, SI 2000/2334

## **2. Application of the Law of the Consumer's Country of Domicile to the Subject Matter of the Dispute**

As demonstrated in part one of this chapter, a choice of law clause deprives the consumer the protection that is awarded to him under the law of his country of domicile. However, as explained in the introduction to this chapter, for the consumer to have confidence in online arbitration, he must enjoy the protection that is awarded to him under the law of his country of domicile. Therefore, raising the consumer confidence in online arbitration requires adopting a rule that stipulates the application of the law of the consumer's country of domicile to the subject matter of the dispute. Adopting such a rule will at least guarantee the consumer the protection that is awarded to him under the mandatory rules of his country of domicile. This rule will also increase the consumer confidence because it eliminates the uncertainty that may arise despite the existence of the choice of law clause.

Uncertainty about the applicable substantive law to the dispute has negative impact on the consumer confidence in online arbitration.<sup>93</sup> This is because the consumer cannot know which law will determine his rights and obligations.<sup>94</sup> In other words, the consumer cannot be sure that he will enjoy the protection that is awarded to him under the law of his country of domicile. One of the important benefits of a choice of law clause is the certainty that it gives to the parties regarding the applicable substantive law.<sup>95</sup> However, uncertainties regarding the applicable substantive law still arise even though there is a choice of law clause. It appears in the case that a

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<sup>93</sup> Julian D M Lew Q C, Loukas A Mistelis, and Stefan M Kröll, *Comparative International Commercial Arbitration*, (1<sup>st</sup> edn, Kluwer Law International, Hague, 2003), p.412

<sup>94</sup> Ibid

<sup>95</sup> Ibid



choice of law clause is invalid.<sup>96</sup> It also appears in the case of a dispute over the existence, the formation or the scope of the choice of law clause itself.<sup>97</sup> The law applicable to the choice of law clause is not necessarily the same law stipulated in the clause.<sup>98</sup> This is because the choice of law clause is separable from the original contract.<sup>99</sup> Therefore, in the case of a dispute over the interpretation of the choice of law clause, the law applicable to the choice of law clause needs to be determined.

Gary Born observed that:

“(D)etermining what substantive contract law to apply to interpret and give effect to a choice-of-law clause necessarily requires resort to some set of rules of construction and enforceability, just as with other types of agreement. In turn, that requires application of some set of conflict of laws rules. Thus, even where the parties have agreed upon a choice-of-law clause, arbitrators will be required to select and apply some set of conflict of laws rules.”<sup>100</sup>

Prof. Born explains that arbitrators should rely on particular legal rules to conduct the interpretation of a choice of law clause. He suggested that an arbitrator will rely on conflict of law rules to determine the applicable substantive law which will apply to the interpretation of the choice of law clause.<sup>101</sup> In fact, determining the law applicable to the choice of law clause and determining the applicable substantive law to the contract in the case that the choice of law clause is invalid involves uncertainty. There are three main methods that an arbitrator can follow to determine the applicable substantive law to the choice of law clause. Those three methods are

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<sup>96</sup>A. F. M. Maniruzzaman, “Conflict of Laws Issues in International Arbitration: Practice and Trends”, (1993) 9(4) Arb. Int’l. 371, 372. (hereinafter Conflict of Laws).

<sup>97</sup>Born, (International Commercial ),note 21 supra, p. 551.

<sup>98</sup>Peter Nygh, *Autonomy in International Contracts*, (1<sup>st</sup> edn, Clarendon Press, Oxford, 1999), p.84. Reinhard Schu, note 27 supra, p.201

<sup>99</sup>Born, (International Commercial), note 21 supra, p.547.

<sup>100</sup>Ibid, p.551,552

<sup>101</sup>Maniruzzaman, (Conflict of Laws),note 96 supra, p.72

also used to determine the applicable substantive law to the contract in the case that the choice of law clause is invalid.<sup>102</sup> The first method is searching for an implied choice of law. Second is the reference to the conflict of laws rules.<sup>103</sup> The third is the direct application of a particular substantive law which the arbitrator considers appropriate.<sup>104</sup> In the following subsections, the author will explain how the arbitrator's reliance on any of these methods to determine the applicable substantive law can cause the consumer huge uncertainty. Whereas, adopting a convention that stipulates the application of the law of the consumer domicile will help parties to avoid such uncertainty. This is because the reference to the law of the consumer domicile will be made via a rule embodied in the convention. This means that there will not be a choice of law clause that refers the dispute to a particular law. This will help the consumer to avoid uncertainties that may arise even though there is a choice of law clause.

## 2.1 Implied Choice

One possible approach that an arbitral tribunal can use to determine the applicable substantive law to the contract or the choice of law clause is searching for an implied choice. An arbitral tribunal can try to find out whether the contract terms and the circumstances indicate to any implied choice of law.<sup>105</sup> A well-known practice by courts and arbitral tribunals is treating a choice of an arbitral seat as an implied choice of substantive law. This practice was “expressed in the maxim *qui*

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<sup>102</sup>Lew, Mistelis, and Kröll, (Comparative), note 93 supra, p.427

<sup>103</sup>Beda Wortmann, “Choice of Law by Arbitrators: The Applicable Conflict of Laws System”, (1998) 14(2) Arb. Int'l. 97, 98, 99. Maniruzzaman, (Conflict of Laws), note 94 supra, p.395.

<sup>104</sup>Born, (International Commercial), note 21 supra, p.552.

<sup>105</sup>Alan Redfern and Martin Hunter, *Law and Practice of International Commercial Arbitration*, (3<sup>rd</sup> edn, Sweet & Maxwell, London, 1999), p.130.

*eligit arbitrum eligit jus*; a choice of forum is a choice of law”.<sup>106</sup> In the English case of *Tzortzis v Monark Line A/B.*,<sup>107</sup> Swedish vendors sold a ship to a Greek purchaser. The contract provided that a deposit had to be paid into a Stockholm Bank. The contract also provided that the transfer of the ship to the purchaser would take place at a Swedish port. The contract was drafted based on a standard form that was in use in Scandinavia. Yet, the contract provided for arbitration in London and it did not provide any express choice of law. The English Court of Appeal held that:

“although ... the contract had its closest and most real connection with Sweden, the parties by choosing the City of London as the place of arbitration had impliedly chosen English law as the proper law of the contract.”<sup>108</sup>

It is clear from the *Tzortzis* case that the court simply considered the choice of place of arbitration as an implied choice of substantive law. In the US a similar practice can also be deduced from the Federal Court’s decision in the case of *Lummus Co. v Commonwealth Oil Refining Co.* The Court held that the choice of New York as a place of arbitration “indicates choice of law” of the State of New York.<sup>109</sup> Likewise, the Restatement (Second) Conflict of Laws (1971)§218 comment b (1971) explains the rationale for applying the substantive laws of the arbitral seat. It provides that:

“Provision by the parties in a contract that arbitration shall take place in a certain state may provide some evidence of an intention on their part that the local law of this state should govern the contract as a whole. This is true not only because the provision shows that the parties had this particular state in mind; it is also true because the parties must presumably have recognized that

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<sup>106</sup>Redfern and Hunter, note 105, p.130.

<sup>107</sup>[1968] 1 W.L.R. 406 (C.A.)

<sup>108</sup>Ibid, p.407.

<sup>109</sup>297 F.2d 80, 87-90 (2d Cir. 1961). As Gary Born explained, the question of whether a choice of place of arbitration implies a choice of law has generated less attention in the U.S.

arbitrators sitting in that state would have a natural tendency to apply its local law.”<sup>110</sup>

§218 comment b of the Restatement indicates that a choice of place of arbitration can lead to the application of the law of the place of arbitration for two reasons. First, the choice of place of arbitration verifies the parties’ intentions to make their contract subject to the law of that country. Second, arbitrators have a ‘natural tendency’ to apply the substantive law of the place of arbitration. However, the practice of considering a choice of place of arbitration as a choice of law has been severely criticised in other courts’ decisions.

Three years after the English case of *Tzortzis*, an important decision was issued by the English House of Lords in the famous case of *Compagnie d’Armement Maritime v Compagnie Tunisienne de Navigation*.<sup>111</sup> In this case a Tunisian company concluded a contract with French ship-owners for the shipment of oil from one port in Tunisia to another. The contract was concluded in Paris<sup>112</sup> yet the brokers used an English printed form contract to draft the contract. The contract referred any future dispute to arbitration in London. A choice of law clause provided that the contract shall be governed by the law of the flag of the ship carrying the goods which was 350,000 tons of oil.<sup>113</sup> However, since the ships used in transporting the oil were Norwegian, Swedish, French, Liberian and Bulgarian and all were chartered by the ‘shipowner’, the clause was considered incapable of application. Lord Morris of Borth refused the allegation that English law should govern the contract because the

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<sup>110</sup>Restatement (Second) Conflict of Laws §218 comment b (1971).

<sup>111</sup>[1971] AC 572.

<sup>112</sup>Ibid

<sup>113</sup>Ibid

choice of London as a place of arbitration implied the choice of English law. He observed that:

“(A)n agreement to refer disputes to arbitration in a particular country may carry with it, and is capable of carrying with it, an implication or inference that the parties have further agreed that the law governing the contract (as well as the law governing the arbitration procedure) is to be the law of that country. But I cannot agree that this is a necessary or irresistible inference or implication: there is no inflexible or conclusive rule to the effect that an agreement to refer disputes to arbitration in a particular country carries with it the additional agreement or necessarily indicates a clear intention that the law governing the matters in dispute is to be the law of that country.”<sup>114</sup>

Lord Morris explained that the choice of place of arbitration is of relevance when trying to determine the applicable substantive law. However, there is no rule that stipulates the application of the law of the place of arbitration. Such practice “is not necessary or irresistible”.<sup>115</sup> This means that an arbitral tribunal does not have to consider the choice of place of arbitration as an implied choice of law. Following the Court’s decision in the case of *Compagnie* two trends appeared. The first one assumes the abandonment of the practice of a choice of place of arbitration as a tacit choice of law.<sup>116</sup> The second one presumes the continuation of the practice.<sup>117</sup>

However, the two trends can cause uncertainty to the parties to the dispute in which a question of applicable law might arise. The reason is that arbitrators and judges have been influenced by the two trends. This means that the parties to the contract, taking the two trends into consideration, cannot expect that the arbitrator will consider their choice of place of arbitration as an implied choice of law.

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<sup>114</sup>Ibid, p.588.

<sup>115</sup>Ibid.

<sup>116</sup>Born, (International Commercial), note 21 supra, p.528.

<sup>117</sup>Kendall Sutton and Gill, *Russell on Arbitration* (21st edn., Sweet & Maxwell, 1997), p.68.

Proponents of the first trend such as the well-known scholars Redfern and Hunter,<sup>118</sup> Lew, Mistelis, and Kröll<sup>119</sup> argue that treating a choice of place of arbitration as an implied choice of law is an old trend. They also argue that nowadays, the choice of place of arbitration does not imply the choice of applicable law. They contend that the choice of place of arbitration is only a “general connecting factor which may be of relevance”<sup>120</sup> to the determination of applicable substantive law.<sup>121</sup> This is a very similar conclusion to the *Compagnie* case. Lando also adopts a similar view to the aforementioned scholars. He explained that the choice of a place of arbitration should not be considered as an implied choice of law. He bases his argument on the fact that parties choosing a particular country as the place of arbitration does not necessarily mean that the parties intend to make their dispute subject to the law of that country. Furthermore, he contends that the parties’ choice of a place of arbitration is usually made for practical convenience.<sup>122</sup> For example, parties look for the arbitration law of the arbitral seat and neutrality.<sup>123</sup>

This trend influenced the arbitrators’ decisions regarding the applicable substantive law. In ICC Case No. 5717 of (1988), the tribunal refused to consider the choice of London as a place of arbitration and English as the language of the contract as an

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<sup>118</sup>Redfern and Hunter, note 105 supra, p.130.

<sup>119</sup>Lew, Mistelis, and Kröll, (Comparative), note 93 supra, p.416.

<sup>120</sup>Ibid

<sup>121</sup>Ibid

<sup>122</sup>Lando, note 87 supra, p.107-109.

<sup>123</sup>Ibid

implied choice of English law.<sup>124</sup> In ICC Case No. 7717 of (1993) the arbitral tribunal reached a similar conclusion.

On the other hand, many arbitral awards and courts' decisions show that in a case where a question of applicable substantive law arises, courts and arbitral tribunals might still consider a choice of an arbitral seat as an implied choice of substantive law.<sup>125</sup> Arbitral tribunals have relied on this presumption to determine the substantive law applicable to the interpretation of a choice of law clause. In ICC Case No. 5505 of (1987), a dispute over the interpretation of a choice of law clause that refers the dispute to the English law arose. In this case, the arbitral tribunal sitting in Switzerland applied Swiss law and general principles of law to the interpretation of the choice of law clause.<sup>126</sup>

In the case of *Kress Corp. v Edw. C. Levy Co.*, the Court of Appeal of the State of Illinois held that the parties express agreement to arbitrate in Illinois implies a choice of the laws of the State of Illinois.<sup>127</sup> In the case of *Egon Oldendorff v Libera Corporation*.<sup>128</sup> The parties in this case were German partners and Japanese Corporation. They agreed on the charter of two bulk carriers to be built for the Japanese Corporation by Sasebo Heavy Industries. The German partners had the option to buy the built ships.<sup>129</sup> There were several contracts that governed the relationship between the parties. One of these contracts was a charter party based on

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<sup>124</sup>ICC Case No.5717 (1988), 1(2) "ICC Bulletin" 22 (1990).

<sup>125</sup>Redfern and Hunter, note 105 supra, p.130.

<sup>126</sup>5505 of 1987 XIII Y.B. Comm. Arb. 110 (1988)

<sup>127</sup>102 Ill. App. 3d 264, 430 N.E. 2d 593, 58 Ill. Dec. 561 (Ill. App. 1981)

<sup>128</sup>[1996] 1 Lloyd's Rep. 380

<sup>129</sup>Ibid

the New York Produce Exchange form.<sup>130</sup> The contract provided for arbitration in London. The German partners claimed damages for breach of contract.<sup>131</sup> They also claimed that the choice of London as a place of arbitration demonstrates a choice of English law within the meaning of Article 3 of the Rome Convention 1980. Article 3(1) provides that a choice of law must be “demonstrated with reasonable certainty by the terms of the contract or the circumstances of the case”.<sup>132</sup> Mr. Clarke Justice asserted that:

“on the facts of this case when set in the context of the terms of the contract as a whole and of the circumstances of the case the arbitration clause was a strong indication of the parties' intention to choose English law as the applicable law as well as the curial law; having agreed English arbitration for determination in London of disputes arising out of a well known English language form of charter which contained standard clauses with well known meanings in English law, it was to be inferred that the parties intended that law to apply.”<sup>133</sup>

Mr. Clarke Justice's statement clearly indicates that treating a choice of place of arbitration as a choice of law is still practiced. It is not abandoned as the aforementioned writers suggested. Mr. Clarke Justice's decision was based mainly on the choice of London as the place of arbitration. Other factors, such as using the English language to draft the contract and the point that the terms of the contract have meaning in English law, were not as important as the arbitration clause itself. The reasons are that first, the English language is frequently used to draft international commercial contracts. Second, it is true that the terms of the contract were considered as having a meaning in English law. The contract which includes

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<sup>130</sup>Ibid

<sup>131</sup>Ibid

<sup>132</sup>Article 3(1), Rome Convention 1980.

<sup>133</sup>[1996] 1 Lloyd's Rep. 380.



these terms is an American standard form called the New York Produce Exchange Form.

In the author's opinion, there is a new prominent trend that rejects the treatment of the choice of place of arbitration as the choice of law. This trend is obvious in courts' decisions, arbitral awards and written literature as applicable to arbitration. However, the old practice is not abandoned. As explained in the case of *Egon*, a choice of a place of arbitration can still be considered as an implied choice of law. This inconsistency can cause uncertainty to the consumer. It is because, in the case of a dispute over the formation of the choice of law clause itself, parties become unable to anticipate whether the law of the place of arbitration will be applied to the choice of law clause and the whole contract. The suggested model convention can help to avoid this uncertainty. It sets up a rule which stipulates the application of the law of the consumer domicile to the substantive issues of the dispute. This means that the reference to the law of the consumer domicile will be made according to a rule established in the convention. This means that there will not be a choice of law clause. Consequently, there will not be any uncertainty regarding the law applicable to the formation and existence of the choice of law clause or the whole contract.

## **2.2 Application of Conflict of Laws Rules**

Reliance on conflict of law rules to determine the applicable substantive law to the choice of law clause or to the whole contract can cause severe uncertainty to the

parties.<sup>134</sup> In order to determine the applicable substantive law a judge has to apply the choice of law rules of the forum.<sup>135</sup> Before the enactment of the English Arbitration Act 1996, an arbitrator sitting in London had to apply English choice of law rules to determine the applicable law to the dispute.<sup>136</sup> This is because the arbitrator's decision on choice of law matters was within the scope of the court's power to review an arbitral award on a point of law.<sup>137</sup> It was also presumed that an arbitrator is like a judge.<sup>138</sup> He is obliged to apply national conflict of laws rules of the place of arbitration. The application of choice of law rules of the place of arbitration provides the parties with an acceptable level of certainty.<sup>139</sup> The reason is that the parties know the conflict of law rules that lead to the applicable substantive law to the choice of law clause or the whole contract.<sup>140</sup>

However, in England the situation has changed. The arbitrator enjoys a greater discretion in determining the applicable conflict of law rules. The delocalisation trend, which calls to limit the influence of the choice of place of arbitration on the arbitral proceedings, has been taken into consideration.<sup>141</sup> Under the English Arbitration Act 1996 an arbitrator can still apply the English conflict of law rules.<sup>142</sup>

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<sup>134</sup> Elizabeth G. Thornburg, "Going Private: Technology, Due Process, and Internet Dispute Resolution", (2000-2001) 34 U.C.Davis L. Rev.151, 184.

<sup>135</sup> Carlo Croff, "The Applicable Law in International Commercial Arbitration: Is It Still a Conflict of Laws Problem", (1982) 16 Int'l L.613, 624.

<sup>136</sup> Sir Lawrence Collins, *Dicey, Morris & Collins on the Conflict of Laws*, (14<sup>th</sup> edn, Sweet & Maxwell, London, 2006), p.732.

<sup>137</sup> Clarkson and Hill, note 18 supra, p.255.

<sup>138</sup> Lew, Mistelis, and Kröll, (Comparative), note 93 supra, p.429.

<sup>139</sup> Wortmann, note 103 supra, p. 105.

<sup>140</sup> Ibid

<sup>141</sup> Ibid

<sup>142</sup> Clarkson and Hill, note 18 supra, p.256.

However, he is not obliged to do so.<sup>143</sup> Section 46(3) of the English Arbitration Act 1996 states that, “the tribunal shall apply the law determined by the conflict of laws rules which it considers applicable.”<sup>144</sup> Similarly, in the US, the FAA does not impose any choice of law rules on the arbitrator. Gary Born explained that an arbitrator sitting in the US to resolve an international dispute can apply conflict of law rules that he considers applicable.<sup>145</sup> This means that both laws grant the arbitrator discretion in choosing the applicable conflict of laws rules.

This huge discretion that the arbitrator enjoys can cause plenty of uncertainty to the parties regarding the applicable substantive law to the choice of law clause.<sup>146</sup> The parties cannot anticipate which law will govern any dispute relating to the choice of law clause or to the whole contract in the case that the choice of law clause is invalid.<sup>147</sup> The reason is that they cannot expect which conflict of law rules will be applied by the tribunal.<sup>148</sup> The difficulty in having an expectation results from the absence of real guidelines that govern the arbitrator’s discretion in determining the applicable conflict of law rules. Prof. Maniruzzaman explained that the choice of conflict of law rules should not be arbitrary.<sup>149</sup> He explained that arbitral practice has produced some sort of guidelines to determine the applicable conflict of laws rules. These guidelines can be employed by arbitrators. Prof. Maniruzzaman observed that:

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<sup>143</sup>Section 46(3), Arbitration Act 1996.

<sup>144</sup>*Ibid*

<sup>145</sup>Born, (International Commercial), note 21 *supra*, p.537.

<sup>146</sup>Wortmann, note 103 *supra*, p. 105.

<sup>147</sup>*Ibid*

<sup>148</sup>*Ibid*

<sup>149</sup>Maniruzzaman, (Conflict of Laws), note 96 *supra*, p.386.

“(T)he arbitrator's free choice should not be flawed by arbitrariness. Rather, he should ensure the best possible choice in the circumstances. To ensure that the freedom of the arbitrator to choose the applicable conflict of laws rules is not exercised arbitrarily, attempts have been made in arbitral practice to draw up certain guidelines which an arbitrator should follow... These principles or guidelines may be considered to be embedded in three competing views: one favours the cumulative application of the conflict of laws systems to which the subject matter of the arbitration proceedings has close contacts; a second view favours the application of international conflict of laws rules or general principles of private international law; a third view favours the determination of the applicable law by the arbitrator directly even without any express reference to a conflict of laws rule; this means dispensing with the conflict rules. Because these three methods borrow from the technique of conflict of laws, although they correspond in their formal aspect to different theoretical approaches, they can be used, by the same arbitrator, either alternatively, depending on the particular circumstances, or concurrently.”<sup>150</sup>

The principles that govern the arbitrator's choice are summarised in three methodologies, as Prof. Maniruzzaman explained. The cumulative application of all conflict of law rules that are connected to the dispute. An arbitrator might apply international conflict of law rules and general principles of conflict of laws. Eventually, an arbitrator can directly apply a particular substantive law without reference to any conflict of laws rules.

Although arbitral practice shows that many arbitrators usually follow these three methods, an arbitrator might not follow any of these methods. Parties cannot always assume that the arbitrator's choice for conflict of laws rules is limited by these guidelines. Prof. Hill explained that under the English Arbitration Act 1996 the tribunal has “unfettered discretion” to determine applicable conflict of law rules.<sup>151</sup>

Likewise, the Departmental Advisory Report on the Bill of the Arbitration Act 1996

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<sup>150</sup>Ibid

<sup>151</sup>Jonathan Hill, *International Commercial Disputes in English Courts*, (3<sup>rd</sup> edn, Hart Publishing, Oxford, 2005), p.692.

(hereinafter DAC Report) affirms that the arbitrator is not limited by any guidelines when choosing the applicable conflict of law rules. Para (225) of the DAC Report which specified for Section 46(3) of the Arbitration Act 1996 states that:

“(S)ub-section (3) caters for the situation where there is no choice or agreement... In such circumstances the tribunal must decide what conflict of law rules are applicable, and use those rules in order to determine the applicable law. It cannot simply make rules for this purpose. It has been suggested to the DAC that more guidance be given as to the choice of a proper law, but it appears to us that flexibility is desirable, that it is not our remit to lay down principles in this highly complex area.”<sup>152</sup>

It is clear from Para (225) of the DAC Report that, the drafters of the Arbitration Act 1996 preferred flexibility over the guidance. They refused to give any guidance on how to determine the applicable conflict of law rules. This means that the arbitrator is not limited by any guidelines. Thus, they can apply any conflict of law rules they consider applicable.

What also affirms that the arbitrators are not confined to these methods in order to determine the applicable law is the following: two of the three methods do not always present an effective solution to determine the applicable law. The cumulative application of conflict of law rules or what is called “false conflict” is not always an effective solution.<sup>153</sup> It is based on looking at the conflict of law rules connected with the dispute to see if they lead to the application of the same substantive law. If the result is the same substantive law, then the situation is called “false conflict”. After that the tribunal will apply that law. An illustration of this approach can be

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<sup>152</sup>Para. 225, “Departmental Advisory Committee Report on the Arbitration Bill” (1996), p.50

<sup>153</sup>Vitek Danilowicz, “The Choice of Applicable Law in International Arbitration”, (1985-1986) 9 Hastings Int’l & Comp. L. Rev.235, 266.

seen in the ICC Case No.1990 of 1972.<sup>154</sup> In this case an Italian claimant alleged that a Spanish Respondent had committed unfair competition. The tribunal looked at both Italian and Spanish conflict of laws rules. It then held that both laws lead to the application of the law of the place where the unfair competition occurred.<sup>155</sup>

However, the problem with this approach is that the different conflicts of laws rules connected with the dispute do not always lead to same applicable substantive law.<sup>156</sup>

In this case the arbitrator has to start a new search to see which one of these laws is the “most appropriate”.<sup>157</sup> The second method is the application of international conflict of law rules or the general principles of conflict of law. According to this approach the arbitrator will not look at the conflict of law rules of the countries connected to the dispute. The arbitrator will conduct a ‘comparative analysis of the conflict of law system’ of the key legal systems in the world. The purpose of this comparative analysis is finding the common principles of the conflict of law between these legal systems. After that the arbitrator will apply these principles to determine the applicable law to the dispute. An illustration of this approach can be found in the award issued by the Chamber I of the Iran–United States Claims Tribunal.<sup>158</sup> The tribunal relied on “centre of gravity” as general principles of “conflict of law” to establish that disputes over the validity of the contract were

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<sup>154</sup>ICC Case No.1990 (1972), 3 Y.B. Com. Arb. 217 (1972).

<sup>155</sup>*Ibid*

<sup>156</sup>Andrew Tweeddale and Keren Tweeddale, *Arbitration of Commercial Disputes: International and English Law and Practice*, (1<sup>st</sup> edn, OUP, Oxford, 2005 ) p.208

<sup>157</sup>Lew, Mistelis, and Kröll, (Comparative), note 93 *supra*, p.433.

<sup>158</sup>*Economy Forms Corporation v Government of the Islamic Republic of Iran*, Award 55–165–1 (June 13, 1983), 3 Iran–U.S. C.T.R. (1984), p. 42, at p. 48.

governed by United States law.<sup>159</sup> However, this approach is of limited effectiveness because there are few principles of conflict of law which, “are universally recognized”.<sup>160</sup>

Even if one assumes that the arbitrator will only follow one of the three methods that Prof. Maniruzzaman mentioned, huge uncertainty still arises. First as Prof. Maniruzzaman explained the arbitrator can either apply one of these methods, or apply more than one at the same time. This means that parties still cannot expect which conflict of law rules the arbitrator will apply. Thus, they cannot expect which law will govern the choice of law clause itself.

Born suggested a solution to find the applicable conflict of law rules to determine the law which governs the choice of law clause. He explained that conflict of law rules of the law mentioned in the choice of law clause itself should be applied.<sup>161</sup> This contention is based on two presumptions. First, a choice of a particular law might be considered as an intention of the parties to make themselves subject to the conflict of law rules of the chosen law.<sup>162</sup> In other words, a choice of substantive law can be interpreted as an implied choice of conflict of law rules of the chosen law. Second, one legal system must govern the various aspects of the parties’ dispute.<sup>163</sup>

This solution can provide the parties with some certainty regarding the law applicable to the choice of law clause. The reason is that it enables the parties to

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<sup>159</sup>Ibid

<sup>160</sup>Lew, Mistelis, and Kröll, (Comparative), note 93 supra, p.433.

<sup>161</sup>Born, (International Commercial), note 21 supra, p.552

<sup>162</sup>Ibid

<sup>163</sup>Ibid

know the applicable conflict of law rules. However, this solution faces a very strong counter argument. First, a choice of law clause does not have to necessarily refer to a national legal system. A choice of law clause can refer to trade usages, international rules of contracts, or *Lex Mercatoria*.<sup>164</sup> In this case, it cannot be said that there are particular conflict of law rules that are accompanied to the chosen substantive law. Second, even in the case that the choice of law clause refers the dispute to particular national law, a choice of law clause has been interpreted to exclude conflict of law rules of its scope.<sup>165</sup>

Section 46(2) of the English Arbitration Act 1996 states that “(F)or this purpose the choice of the laws of a country shall be understood to refer to the substantive laws of that country and not its conflict of laws rules.”<sup>166</sup> It is clear that Section 46(2) excludes conflict of law rules from the scope of the choice of law clause. In the US, Comment h on Section 187 of the Rest 2d Confl provides that:

“Reference is to “local law” of the chosen state. The reference, in the absence of a contrary indication of intention, is to the “local law” of the chosen state and not to that state’s “law” which means the totality of its law including its choice of law rules. When they choose the state which is to furnish the law governing the validity of their contract, the parties almost certainly have the “local law” rather than the “law” of that state in mind. To apply the “law” of the chosen state would introduce the uncertainties of choice of law into the proceedings and would serve to defeat the basic objectives, namely those of certainty and predictability, which the choice of law provision was designed to achieve.”

Maintaining the certainty associated with the choice of law clause requires the exclusion of conflict of law rules from the scope of that clause. This is the

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<sup>164</sup>Ole Lando, “The Law Applicable to the Merits of the Dispute”, (1986) 2(2) Arb. Int’l. 104, 106.

<sup>165</sup>Lew, Mistelis, and Kröll, (Comparative), note 93 supra, p.415.

<sup>166</sup>Section 46(2), Arbitration Act 1996.



justification that the Restatement gives for the exclusion of conflict of law rules from the scope of a choice of law clause. In fact, it is very reasonable to conclude that a choice of law clause excludes conflict of law rules of the chosen law. Parties insert a choice of law clause to avoid uncertainty about the conflict of law rules. Arbitral practice also shows that conflict of laws rules are excluded from the scope of the choice of law clause for the same purpose mentioned in the Restatement. In the ICC Case No. 5505 of 1987<sup>167</sup>, a dispute over the interpretation of a choice of law clause took place. The claimant was a Mozambique purchaser; the respondent was a Netherlands seller.<sup>168</sup> The parties concluded a contract for the sale of seed potatoes. The contract embraced a choice of clause which states that “the law applicable is that known in England.”<sup>169</sup> Arbitrator G. Muller asserted that: “it would have been contradictory and therefore unreasonable to choose at the same time a rule of conflict of laws and a substantive law, as this is assumed by the defendants...”<sup>170</sup>

To sum up this section, finding the law that governs the choice of law clause can be made through the application of conflict of law rules. When it comes to the application of conflict of law rules, arbitrators and tribunals enjoy huge discretion to determine the applicable conflict of law rules. Although this discretion eases the process of determining the applicable law to the choice of law clause or the whole contract, it can be a severe source of uncertainty. It makes the parties unable to expect the applicable conflict of law rules. Thereby, they cannot expect which law will govern any dispute related to the choice of law clause. Adopting a convention

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<sup>167</sup>Preliminary Award, ICC Case N. 5505 of 1987, XIII Y.B. Comm. Arb. 110.

<sup>168</sup>*Ibid*

<sup>169</sup>*Ibid*

<sup>170</sup>*Ibid*, 111.

that stipulates the application of the law of the consumer domicile will not expose the parties to such uncertainties. The reason is that the reference to the law of the consumer domicile will be made via the rules of the convention. Therefore, there will not be a choice of law clause over which to have a dispute about its existence or scope and, therefore, there will not be any need to apply a conflict of law system.

### **2.2.1 Connecting Factors Employed to Determine the Applicable Law and the Nature of B2C E-commerce**

Adopting a model convention that stipulates the application of the law of the consumer domicile will help avoid new uncertainties, particularly those that may appear when trying to determine the applicable law to a B2C e-commerce contract through the application of choice of law rules.<sup>171</sup> All choice of law rules include certain connecting factors that can be employed in order to determine the applicable law.<sup>172</sup> For example, Article 4(1) of the Rome Convention 1980 provides that the contract shall be governed by the law of the country with which it is most closely connected.<sup>173</sup> Article 4(2) provides that:

“it shall be presumed that the contract is most closely connected with the country where the party who is to effect the performance which is characteristic of the contract has, at the time of conclusion of the contract, his habitual residence, or, in the case of a body corporate or unincorporate, its central administration. However, if the contract is entered into in the course of that party's trade or profession, that country shall be the country in which the principal place of business is situated or, where under the terms of the contract the performance is to be effected through a place of business other than the

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<sup>171</sup>Schu, note 27 supra, p.221, 222.

<sup>172</sup>Ibid, p.220.

<sup>173</sup>Art.4 (1), Rome Convention 1980.

principal place of business, the country in which that other place of business is situated.”<sup>174</sup>

Article 4(2) refers to the law of the country of habitual residence or country of the place of business of the party who is liable for the “characteristic performance” of the contract. The Giuliano Lagarde Report defines “characteristic performance” as “the performance for which the payment is due”.<sup>175</sup> This means that the delivery of the goods or services is the characteristic performance. Applying this to a B2C e-commerce contract, the business is the party liable for the characteristic performance. This is because the business is the party that provides the goods or services. The role of the consumer is making the payment. This means that the law of the place of business is the applicable law.

The place of the business is a connecting factor among the various connecting factors that §188 of the Restatement (Second) Conflict of Laws (1971) recognise in order to determine the applicable law. §188(1) provides that, “(T)he rights and duties of the parties with respect to an issue in the contract are determined by the local law of the state which, with respect to that issue, has the most significant relationship to the transaction”.<sup>176</sup> This is what is usually called the centre of gravity test.<sup>177</sup> In order to determine the state that has most significant connection to the contract, §188(2) states that regard shall be given to certain connecting factors. These connecting factors are the place of contracting, the place of negotiation of the contract, the place

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<sup>174</sup>Ibid, Art.4(2).

<sup>175</sup>“Report on the Convention on the law applicable to contractual obligations” (1) by Mario Giuliano Professor, University of Milan and Paul Lagarde Professor, University of Paris I, OJ C 282, 1980, p.38.

<sup>176</sup>§188(1), Restatement Second of Conflicts of Laws 1971.

<sup>177</sup>Schu, note 27 *supra*, p.222

of performance, the location of the subject matter of the contract, and the domicile, residence, nationality, place of incorporation and place of business of the parties.<sup>178</sup> However, new types of uncertainties arise from the application of the existing choice of law rules on B2C e-commerce contracts. For example, is the location of the server of the business's website considered a place of business?<sup>179</sup>

Section 19 of the European Directive on E-commerce 2000 preamble states that “the place of establishment of a company providing services via an Internet website is not the place at which the technology supporting its website is located”.<sup>180</sup> In fact, the location of the web server is insufficient indication of the place of business. In the case of *Cleveland Museum of Art v Capricorn Arti*,<sup>181</sup> Mr. Justice Hirst asserted that in order for a company to have a place of business in Great Britain, there must be a, “visible sign or physical indication that the company has a connection with particular premises”.<sup>182</sup> The web server is a device that is, in a way, similar to a telephone or facsimile machine.<sup>183</sup> The server makes the website available or accessible to the users following the data that the website owner loads on to the server.<sup>184</sup> It is possible for the information to be passed via several web servers located in different countries before it is loaded on to the main web server. In other words, the web server can be located in a country different to the country where the

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<sup>178</sup> §188(2), Restatement Second of Conflicts of Laws 1971.

<sup>179</sup> Gillies, (Adapting International), note 33 supra, p.367.

<sup>180</sup> Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market, OJ L 178, 17.7.2000, p. 1-16.

<sup>181</sup> [1990] 2 Lloyd's Rep. 166, 196

<sup>182</sup> Ibid, p.169

<sup>183</sup> Gillies, (Adapting International), note 35 supra, p.367

<sup>184</sup> Ibid

business that controls this web server is located. It also seems that in the US the location of a web server cannot be considered as a place of business. In the case of *Amberson Holdings LLC v Westside Story Newspaper*,<sup>185</sup> the District Court of New Jersey refused the allegation that the web server that belongs to a Californian newspaper satisfied the minimum contact test to establish jurisdiction of the Court.<sup>186</sup> It is true that this court dealt with personal jurisdiction, yet it is a strong indication that the location of a web server is unlikely to be considered a place of business. The reason is that if the location of the web server alone is capable of being a place of business, the court would consider it sufficient to establish personal jurisdiction. This is because a place of business is usually sufficient to establish minimum contact for the purpose of establishing personal jurisdiction. Subsequently, it is safe to say that the location of the web server is not the place of business.

## 2.3 Direct Application

The new trend of delocalisation of international arbitration has produced a new approach to conflict of laws in international arbitration.<sup>187</sup> It is the direct application of appropriate substantive law or rules by an arbitrator without any reference to conflict of law rules.<sup>188</sup> Such a method exempts the arbitrator from experiencing conflict of laws complexities.<sup>189</sup> In fact, the direct application gives the arbitrator greater flexibility in determining the applicable law.<sup>190</sup> However, this direct

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<sup>185</sup> 110 F. Supp. 2d 332 (2000)

<sup>186</sup> Ibid, p.336.

<sup>187</sup> Shackleton, note 20 supra, p.375.

<sup>188</sup> Ibid

<sup>189</sup> Wortmann, note 103 supra, p.98.

<sup>190</sup> Born,(International Commercial), note 21 supra, p.530

application approach can be a source of uncertainty for the consumers.<sup>191</sup> It makes the consumer unable to expect which law will govern any dispute relating to the choice of law clause.<sup>192</sup> An arbitrator can apply any national law he finds appropriate.

One would say such practice is not allowed under the English Arbitration Act 1996. This is because § 46(3) of the English Arbitration Act 1996 stipulate the application of conflict of laws rules.<sup>193</sup> However, § 46 is not a mandatory provision of the Arbitration Act 1996.<sup>194</sup> This means that the parties can exclude section 46 from application by adopting rules of arbitral institutions.<sup>195</sup> For example, whenever parties agree to submit their dispute to the LCIA<sup>196</sup>, an arbitrator can rely on Article 22 of the 1998 LCIA Rules. It states that in the case of no choice of law made by parties, an arbitrator shall “apply the laws or rules of law which it considers appropriate”.<sup>197</sup> Likewise, Article 28(1) of the ICDR Procedures 2006 states that “the tribunal shall apply such law(s) or rules of law as it determines to be appropriate.”<sup>198</sup> Rules of both institutions refer to law and rules of law. The terminology law and rules of law is interpreted differently. The term ‘law’ includes national laws.<sup>199</sup> The phrase ‘rules of law’ will include general principles of the law of international contracts and *Lex Mercatoria*.<sup>200</sup> This means that the arbitrator is at

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<sup>191</sup>Ibid

<sup>192</sup>Ibid

<sup>193</sup>Section 46(3), Arbitration Act 1996.

<sup>194</sup>Ibid, Section 4. Shackleton, note 20 supra, p.384, 385.

<sup>195</sup>Section 4, Arbitration Act 1996.

<sup>196</sup>LCIA is London Court of International Arbitration

<sup>197</sup>LCIA Arbitration Rules adopted in 1998.

<sup>198</sup>Article 28(1) of the ICDR Procedures, amended and effective since 1 May 2006

<sup>199</sup>Shackleton, note 20 supra, p.384, 385.

<sup>200</sup>Ibid

liberty to apply any national or non-national rules of law that he finds appropriate. This is as far as the institutional rules allow direct application.

In the US, as mentioned earlier, the FAA does not impose any conflict of law rules on the arbitrator. The permissibility of direct application of substantive law under the FAA can be deduced from Article V of the Iran–United States Claims Settlement Declaration.<sup>201</sup> The Article sets up many methods for deciding the applicable law. It provides that, the arbitral tribunal can apply “such choice of law rules and principles of commercial and international law as the Tribunal determines to be applicable.” Prof. Maniruzzaman made a comment on Article V of the Iran–United States Claims Settlement Declaration. He said that this article enables the arbitrator to apply “any substantive law from whatever sources”<sup>202</sup> without any reference to conflict of law rules.

As mentioned earlier the direct application eases the process of determining the applicable law. Yet, it may cause severe uncertainty to the consumers. Whereas, adopting a convention that stipulates the application of the law of the consumer domicile will not expose the parties to such uncertainty. This is because reference to the law of the consumer domicile will be made via the rules of the convention. This means that there will not be a choice of law clause over which to have dispute.

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<sup>201</sup> Iran–United States Claims Settlement Declaration of 19 January 1981. Available at :< <http://www.iusct.org/claims-settlement.pdf> > accessed on 12/05/2007.

<sup>202</sup>Maniruzzaman, (Conflict of Laws), note 96 supra, p.392.

### **3. Conclusion**

A choice of law clause can reduce consumer confidence in the online arbitral process. This is because it might completely deprive the consumer of the protection awarded to him under the law of his country of domicile. This happens because the arbitrator is legally free from a duty to comply with mandatory rules that do not belong to the chosen law. The arbitrator's discretion will not always lead to the application of the mandatory rules of the consumer country of domicile. This is because the arbitrator might consider himself obliged to comply with the choice of law clause. Uncertainties regarding the applicable substantive law can arise even though there is a choice of law clause. In the case of dispute over the scope of the choice of law clause, the arbitrator has to determine the substantive law that governs the choice of law clause. The arbitrator may have to determine the law applicable to the contract if he finds the choice of law clause invalid. The process of determining the applicable substantive to the choice of law clause or the whole contract involves huge uncertainty. This is because the arbitrator can follow different method to determine the applicable law.

Adopting a convention that stipulates the application of the law of the consumer domicile to the substantive issues of the dispute will raise consumer confidence in the online arbitral process. This is because such a convention will oblige the arbitrator to apply the law of the consumer domicile. In other words, there will not be a choice of law clause that the arbitrator is obliged to apply. Similarly, there will not be any dispute over the validity of the choice of law clause which can lead to huge uncertainty.



## **Chapter 6**

### **The Consumer Country of Domicile as the Arbitral Seat**

As explained in section 1.3 of chapter two, raising the consumer confidence in e-commerce requires a cost-effective and quick method of resolving B2C e-commerce disputes. Online arbitration is an e-commerce activity. This means that instilling the consumer confidence in online arbitration requires a cost-effective and quick method for resolution of the disputes that relate to the online arbitration agreements and processes.

The Court supervision over the disputes that relate to the online arbitration agreements and processes is so important for the efficiency and the credibility of online arbitration.<sup>1</sup> The court litigation is important for the enforcement of the arbitration clause. Only the court can compel a party to participate in the online arbitral process if he has refused to voluntarily comply with the arbitration clause.<sup>2</sup> The Court litigation is also important to compel interim measures such as protecting the asset subject of the dispute or preserving important evidence relating to the dispute.<sup>3</sup> The Court is also entitled to hear disputes regarding the removal of an arbitrator. The Court is also entitled to hear challenges to the arbitral award.<sup>4</sup>

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<sup>1</sup> Alan Redfern and Martin Hunter, *Law and Practice of International Commercial Arbitration*, (3<sup>rd</sup> edn, Sweet & Maxwell, London, 1999), p.341-345.

<sup>2</sup>Ibid

<sup>3</sup>Ibid

<sup>4</sup>Ibid

Litigation over disputes that relate to the online arbitration agreements and procedures must take place in the Courts of a particular country. It is well-established that the Courts of the place of arbitration which is usually called the arbitral seat have the jurisdiction to hear disputes over the arbitration agreement; supervise the online arbitral procedures; and to hear challenges to the arbitral award. As mentioned supra, online B2C contracts are concluded via adhesion contracts. This means that the business can choose a particular Court to hear disputes over the online arbitration agreements and procedures by determining the arbitral seat. This is the connection point between this thesis which is about online arbitration and the rules regulating forum selection clauses in consumer contracts.

Litigating the disputes that relate to online arbitration agreements and processes in a foreign forum is inconvenient and too expensive for the consumer. Litigation in a foreign forum is too expensive for the consumer because of the travel costs. The consumer may also need to consult a legal adviser and this means that he has to pay legal attorney fees. The inconvenience results from the fact that the foreign forum might be far away from the consumer's domicile. It is also likely that the consumer will face language barriers and a different legal system. Therefore, in order to instil the consumer confidence in online arbitration, the consumer should be able to refer the disputes relating to online arbitration agreements and processes to the Court of his country of domicile. However, this chapter argues that a choice of an arbitral seat that is foreign to the consumer means that the consumer cannot refer the disputes that relate to the online arbitration agreements and processes to the Courts of his

country of domicile. Therefore, a rule that stipulates the consumer's country of domicile as the arbitral seat should be in place.

The first part of this chapter explains that raising the consumer confidence in online B2C arbitration requires a new rule that establishes the consumer's country of domicile as the arbitral seat. The second part of this chapter explains that, jurisdiction rules do not provide the consumer with a sufficient degree of protection with regards to litigation of disputes that relate to online arbitration agreements and processes. The third part explains that unfairness and unconscionability rules cannot effectively guarantee the consumer the right to litigate disputes related to online arbitration agreements and processes in the Courts of his country of domicile.

## **1. The Consumer's Country of Domicile as the Arbitral Seat**

Stipulating the consumer country of domicile as the arbitral seat is so important to raise the consumer confidence in the online arbitral process.<sup>5</sup> As explained *supra*, it is well-established that the Courts of the arbitral have the jurisdiction to supervise the arbitral process. Modern arbitration laws give the Courts of the arbitral seat or the Courts of the country that its law is applicable to the procedures, the authority to supervise the arbitral process.<sup>6</sup> Section 2(1) of the English Arbitration Act 1996 states that grounds for challenging an arbitral award embedded in Sections 67, 68

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<sup>5</sup> Lucille M. Ponte, "Boosting Consumer Confidence in E-Business: Recommendations for Establishing Fair and Effective Dispute Resolution Programs for B2C Online Transactions", (2002) 12 Alb. L. J. Sci. & Tech. 441, 487.

<sup>6</sup> Redfern and Hunter, note 1 *supra*, p.85, 439, 440.

and 69 of the same Act apply when England is the arbitral seat.<sup>7</sup> Likewise, grounds for vacation of the arbitral award included in Section 10 of the FAA only apply if the arbitral seat is in the US.<sup>8</sup> Article V(1)(e) of the NYC provides that the competent court to set aside an arbitral award is the court where an award was made or the Court under its law the award was made.<sup>9</sup> Prof Mann explained that an award is made at the arbitral seat. He asserted that:

“The award, it is submitted, is no more than a part, the final and vital part of a procedure which must have a territorial, central point or seat. It would be very odd if possibly without the knowledge of the parties or even unwittingly, the arbitrator had the power to sever that part from the preceding procedure and thus give a totally different character to the whole”.<sup>10</sup>

Conducting part of the arbitral proceeding outside the arbitral seat does not mean that the arbitral award is made at the other place where that part has been conducted. However, contrary to Prof. Mann’s view, in the case of *Hiscox v Outhwaite*,<sup>11</sup> Lord Oliver explained that an arbitral award was not made in England although it was the arbitral seat. His Lordship explained that the arbitral award was made in Paris because it was signed there.<sup>12</sup> However, the doctrine made in *Hiscox* is of little importance after the enactment of the English Arbitration Act 1996. This is because Section 53 of the said Act provides that whenever England is the arbitral seat the

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<sup>7</sup>Section 2(1), English Arbitration Act 1996.

<sup>8</sup>Section 10, US Federal Arbitration Act 1925.

<sup>9</sup>Article 5(1)(e), New York Convention 1958.

<sup>10</sup>FA Mann, “Where is an Award ‘Made’ ”, (1985) 1 Arb.Int’l.107, 108.

<sup>11</sup>[1992] 1 A.C. 562.

<sup>12</sup>Ibid, p.594-5

arbitral award is made there notwithstanding where it is signed, posted or delivered to the parties.<sup>13</sup>

The US Federal Court of the Southern District of New York decision in the case of *International Standard Electric Corporation v Bidas Sociedad Anonima Petrolera, Industrial Y Comercial*,<sup>14</sup> explains that an arbitral award is made at the arbitral seat. It also explains that the phrase under its ‘law the award was made’ in Article V(1)(e) of the NYC refers to the procedural law of arbitration. It does not refer to the substantive law applicable to the dispute. In that case, an Argentinean Company and an American Company signed a contract in which the Argentinean Company purchased 25% of one the American Company’s subsidiaries in Argentina. The contract included an arbitration clause that referred any future dispute to one or more arbitrators appointed by the International Chamber of Commerce (hereinafter ICC). The contract also included a choice of law clause that made the contract subject to the law of the state of the New York. A dispute arose between the parties and the ICC determined Mexico City as an arbitral seat and the Mexican law was applied to the procedures. After the arbitral process ended the American Company brought an action in the US Federal Court of the Southern District of New York to vacate the arbitral award alleging that the named court had jurisdiction to vacate the award because New York law was applicable to the contract. The Court refused this allegation. It stated that it had no jurisdiction to vacate the award. The reason is that the phrase under “laws of which the award was made” in Article V(1)(e) of the NYC

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<sup>13</sup>Section 53, English Arbitration Act 1996.

<sup>14</sup>745 F.Supp. 172 (S.D.N.Y. 1990)

referred exclusively to the procedural law and not to the substantive law.<sup>15</sup> The Court also explained that the only place to vacate the arbitral award was Mexico because it was the arbitral seat and its law was applicable to the procedures of the arbitral process.<sup>16</sup>

Fixing the consumer domicile as the arbitral seat also has an important benefit. In online arbitration, the parties and the arbitrators may not determine the arbitral seat because the arbitral process takes place online.<sup>17</sup> It is difficult for the Court to determine the arbitral seat if it has been left undetermined by the parties or the arbitrators. Section 3(c) of the English Arbitration Act 1996 states that, in order to determine the arbitral seat that is left undetermined all the relevant circumstances should be taken into consideration. In the case of *Dubai Islamic Bank PJSC v Paymentech Merchant Services Inc.*,<sup>18</sup> the House of Lords explained that factors that should be taken into consideration to determine the arbitral seat are the nationality of the parties; the place where the dispute occurred; the place where the hearing was conducted; and the place where the arbitral award was rendered.<sup>19</sup> These factors might not be helpful in determining the arbitral seat that has been left undetermined in the context of an online arbitral process. It might be difficult to determine the place where the dispute occurred and the place of the hearing. The reason is that the dispute might be a result of an online transaction that has been fully concluded and performed via the internet. The hearing and the rest of the arbitral procedures might

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<sup>15</sup>745 F.Supp. 172, 178 (S.D.N.Y. 1990).

<sup>16</sup>*Ibid.*

<sup>17</sup>Andrew Tweeddale and Keren Tweeddale, *Arbitration of Commercial Disputes: International and English Law and Practice*, (1<sup>st</sup> edn, OUP, Oxford, 2005), p.375

<sup>18</sup>[2001] 1 Lloyd's Rep 65.

<sup>19</sup>*Ibid.*, p.74.

also exclusively take place online while the parties and the arbitrator are located in a different jurisdiction.<sup>20</sup> Therefore, it is difficult to determine where that hearing or that part of the arbitral procedure has been conducted. Lanier suggested that the location of the server or ‘Lex Loci Server’ can be used to determine the arbitral seat.<sup>21</sup> However, as mentioned earlier, it is very likely that many servers located in different jurisdictions are engaged in the same arbitral process.<sup>22</sup> This makes it very difficult to rely on any of these servers to determine the arbitral seat.

To sum up this section, fixing the consumer domicile as the arbitral seat will guarantee the consumers the right to litigate disputes over online arbitration agreements and process in the Courts of his country of domicile. A further action is needed to prevent Courts foreign to the consumer from exercising jurisdiction to vacate an arbitral award on the base the parties have chosen its procedural law. In other words, the rules should stipulate that the arbitral procedures cannot be governed by a law other than the consumer country of domicile.

## **2. Jurisdiction Rules do not Provider the Consumer with a Sufficient Degree of Protection**

Nominating an arbitral seat that is foreign to the consumer means that the consumer cannot refer disputes related to online arbitration agreements and processes to the Court of his country of domicile. This is because jurisdiction rules do not provide the consumer with a sufficient degree of protection with regard to international

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<sup>20</sup>M.H.M. Schellekens, “Online Arbitration and E-commerce”, (2002) 9 E.C.L.Rev. 113, 122,123.

<sup>21</sup>Tiffany J. Lanier, Esq., “Where on Earth Does Cyber-Arbitration Occur?: International Review of Arbitral Awards Rendered On line”, (2000) 7 ILSA J. Int’l & Comp. L. 1, 6.

<sup>22</sup>Schellekens, note 20 supra, p.122.

disputes related to online arbitration agreements and processes. Under the English Law, the Brussels régime, which consists of the Brussels I Regulation<sup>23</sup>, the Brussels Convention 1968<sup>24</sup> and the Lugano Convention 1988,<sup>25</sup> includes rules which provide consumers with the right to litigate international B2C disputes in the country of their domiciles. Para (1)(c) and (2) of Article 15 of the Brussels I Regulation states that:

“1. In matters relating to a contract concluded by a person, the consumer, for a purpose which can be regarded as being outside his trade or profession, jurisdiction shall be determined by this Section, without prejudice to Article 4 and point 5 of Article 5, if:

(c) ... the contract has been concluded with a person who pursues commercial or professional activities in the Member State of the consumer's domicile or, by any means, directs such activities to that Member State or to several States including that Member State, and the contract falls within the scope of such activities.

2. Where a consumer enters into a contract with a party who is not domiciled in the Member State but has a branch, agency or other establishment in one of the Member States, that party shall, in disputes arising out of the operations of the branch, agency or establishment, be deemed to be domiciled in that State.”<sup>26</sup>

Para (1) and (2) of Article 16 of the Brussels I Regulation states that:

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<sup>23</sup>Council Regulation (EC) No 44/2001 of 22 December 2000 on Jurisdiction and the Recognition and Enforcement of Judgement in Civil and Commercial Matters O.J. 2001 No. L12, p.1. (hereinafter Brussels I Regulation)

<sup>24</sup>Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters 1968 O.J. 1972 No. L299, p.32. One of the reasons that led to the replacement of the Brussels Convention 1968 by the Brussels I Regulation is the need to address B2C e-commerce contracts. Committee on Legal Affairs and the Internal Market, “Report on the Proposal for a Council Regulation (EC) on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters”, (COM(1999) 348 final ‘C5—0169/1999’ 1999/0154 (CNS)).

<sup>25</sup>EC EFTA Convention on Jurisdiction and the Enforcement of Judgements in Civil and Commercial Matters Lugano adopted on 16 September 1988. In this chapter, it is to be presumed that the provisions of the Brussels I Regulation, Brussels Convention 1968, and the Lugano Convention 1968 work in the same way unless the contrary is indicated. Therefore, quotation will be made from the text of the Brussels I Regulation. In the case that the provisions quoted from Brussels I Regulation differ from the other two conventions, the difference will be explained in the footnote.

<sup>26</sup>Art.15, Brussels I Regulation



“1. A consumer may bring proceedings against the other party to a contract either in the Courts of the Member State in which that party is domiciled or in the Courts for the place where the consumer is domiciled.

2. Proceedings may be brought against a consumer by the other party to the contract only in the Courts of the Member State in which the consumer is domiciled.”<sup>27</sup>

Paras 1 and 2 of Article 16 give the consumer the discretion to bring any action related to the dispute either in the Courts of his domicile or in the Courts of the business’s domicile.<sup>28</sup> At the same time, the business cannot sue the consumer in a place other than the consumer’s domicile. In the context of a cross-border B2C e-commerce contract, a consumer cannot enjoy the protection awarded to him under Article 16, unless the online B2C contract satisfies the criteria embedded in Article 15. The first of these criteria is that the business must be domiciled in a member state of the EU or has a “branch, agency or other establishment” in an EU member state.<sup>29</sup> The second criterion is that the B2C e-commerce contract must be a result of commercial activities directed at the consumer domicile or to a group of countries including the consumer’s domicile.<sup>30</sup> In the case that the B2C e-commerce contract satisfies these standards, the consumer will have the option to litigate international

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<sup>27</sup>Ibid, Art.16.

<sup>28</sup>Ibid.

<sup>29</sup> This is determined in accordance with Articles 59 and 60 of the Brussels regulation.

<sup>30</sup> Articles 13, 14, and 15 of The Brussels Convention 1968 and the Lugano Convention 1988 include rules that protect consumers from forum selection clauses that nominate a foreign forum. The only difference between those rules and consumer jurisdiction rules embraced in Brussels I Regulation is para 1(c) of Article 15 of the Regulation. The application of the consumer jurisdiction rules embedded in the Brussels Convention 1968 and the Lugano Convention 1988 requires a specific invitation from the business to the consumer in the country of his domicile and the consumer must have taken the steps required to also conclude the contract in the country of his domicile. Article 15(1)(c) of the Brussels I Regulation does not require that the consumer takes the steps necessary to conclude the contract in the country of his domicile. However, it adopts the ‘country of destination principle’. In other words, the B2C e-commerce contract must be a result of commercial activities directed to the consumer domicile or to a group of countries including the consumer domicile. Difficulties in determining which online business might be considered directing its activities to the consumer and whether a web server can be considered a branch or establishment have been discussed in section 1 and 2.2.1 of chapter four of this thesis.

B2C disputes in the country of his domicile. However, if the B2C e-commerce dispute relates to online arbitration agreements or processes, the consumer cannot enjoy the protection that is awarded to him under the Brussels I Regulation. The reason is that arbitration is excluded from the scope of application of the Brussels I Regulation.<sup>31</sup> Article 1(2)(d) of the Brussels I Regulation states that, “The Regulation shall not apply to Arbitration”.<sup>32</sup>

Prof. Schlosser made comment on the arbitration exception under Article 1(2) of the Brussels Convention 1968. He suggested that the arbitration exception does not apply to Court proceedings relating to arbitration.<sup>33</sup> He observed that:

“Specific reasons exist for adopting a narrow construction of ‘arbitration’. Strictly speaking, ‘arbitration’ means proceedings before private persons empowered by the parties to decide their dispute. Court proceedings are not ‘arbitration’ even if they relate to arbitration. Some people might object to this approach on the basis that such an interpretation of ‘arbitration’ would make the provision superfluous. Indeed arbitration proceedings can never be tantamount to a ‘suit in the Courts’ for which the second title of the Convention provides jurisdiction; and an arbitral award can never be a ‘judgment given by a Court or tribunal of a contracting state’ the recognition and enforcement of which is foreseen in the third title.”<sup>34</sup>

In this statement, Schlosser limited the scope of the application of the arbitration exception to the meaning of the term arbitration. In other words, Schlosser suggested that the exception of arbitration does not apply to Court proceedings that relate to

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<sup>31</sup> Jean-Paul Beraudo, “The Arbitration Exception in the Brussels and Lugano Conventions: Jurisdiction, Recognition and Enforcement of Judgments”, (2001) 18(1) J.Int’l Arb. 13, 15. Jacomijn J. Van Haersolte-Van Hof, “The Arbitration Exception in the Brussels Convention: Further Comment”, (2001) 18(1) J.Int’l Arb. 27, 28. Dominique T. Hascher, “Recognition and Enforcement of Judgments on the Existence and Validity of an Arbitration Clause under the Brussels Convention”, (1997) 13(1) Arb. Int’l. 33, 35.

<sup>32</sup> Art.1(2) (d), Brussels I Regulation.

<sup>33</sup> Peter Schlosser, “The 1968 Brussels Convention and Arbitration”, (1991) 7(3) Arb. Int’l. 227, 230, 231.

<sup>34</sup> Ibid

arbitration. This is because arbitration is simply different from litigation and it is arbitration that is excluded from the scope of the Brussels Convention 1968. If Schlosser's argument were true, the consumer would be able to rely on Article 16 of the Brussels I Regulation to litigate disputes related to arbitration agreements and process in his country of domicile. This is because the Brussels I Regulation has the same scope of applicability as the Brussels Convention 1968.<sup>35</sup> Nevertheless, Schlosser's argument is not correct. The arbitration exception does extend to Court proceedings that relate to arbitration.<sup>36</sup> From a linguistic perspective, if arbitral proceedings are only excluded from the scope of the Brussels I Regulation, then the whole exception of arbitration becomes unnecessary. This is because arbitration is different from litigation and the Brussels I Regulation is designed to apply to litigation. Therefore, there is no point in excluding arbitration from the scope of a legal instrument that is not designed to apply to arbitration. In fact, the aim of Article 1(2)(d) of the Brussels I Regulation is to exclude Court proceedings relating to arbitration. Strong evidence for the applicability of the arbitration exception to Court proceedings related to arbitration can be seen in the case of *Marc Rich & Co AG v Societa Italiana Impianti PA*.<sup>37</sup> In that case, the European Court of Justice (hereinafter ECJ) had to determine whether Court proceedings to appoint an

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<sup>35</sup>EU Commission, "Proposal for a Council Regulation (EC) on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters", COM (1999) 348 final 99/0154 (CNS). Clare Ambrose, "Arbitration and Free Movement of Judgments", (2003) 19(3) Arb. Int'l. 3, 4. Hans Van Houtte, "Why Not Include Arbitration in the Brussels Jurisdiction Regulation?" (2005) 21(4) Arb. Int'l. 509, 513, 514. The Proposal on the Brussels I Regulation provides that the scope of applicability of the Brussels I Regulation shall have the same scope of applicability of the Brussels Convention 1968. This might be the reason that the arbitration exception appeared in the same formulation in Article 1(4) of the Brussels Convention 1968, Article 1(4) the Lugano Convention 1988, and Art.1(2) (d) of the Brussels I Regulation.

<sup>36</sup>Case C-190/89 [1991] ECR I-3855. 3903 (Para. 21).

<sup>37</sup>Ibid.

arbitrator come within the scope of the arbitration exception under the Brussels Convention 1968. The ECJ stated that:

“(B)y excluding arbitration from the scope of the Convention of 27 September 1968 on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters ... the Contracting Parties intended to exclude arbitration in its entirety, including proceedings brought before national Courts... the Convention does not apply to Court proceedings which are ancillary to arbitration proceedings, for example the appointment or dismissal of arbitrators”<sup>38</sup>

The ECJ explained that the arbitration exception extends to Court proceedings that are ancillary to arbitration. There are various Court proceedings that are ancillary to arbitration. Court proceedings are definitely ancillary to arbitration if its subject matter is recognition and enforcement of arbitral awards, or vacating an arbitral award.<sup>39</sup> Court proceedings whose subject matter is the appointment or dismissal of arbitrators, determining the place of arbitration are also ancillary to arbitration.<sup>40</sup> However, in the case of *Vanader Maritime BV v Kommoditgesellschaft in Firma Deco-Line*,<sup>41</sup> the ECJ explained that Court proceedings that order interim measures<sup>42</sup> in respect of a dispute that is submitted to arbitration is not ancillary to arbitration.<sup>43</sup> Nevertheless, even if Article 16 of the Brussels I Regulation applies to this kind of court proceedings that relates to arbitration, the degree of the protection is still very modest. This is because Brussels I Regulation does not apply to other

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<sup>38</sup>Ibid, (Para.18, 21).

<sup>39</sup>Professor Dr Peter Schlosser, “Report on the Convention of 9 October 1978 on the Association of the Kingdom of Denmark, Ireland and the United Kingdom of Great Britain and Northern Ireland to the Convention on jurisdiction and the enforcement of judgments in civil and commercial matters and to the Protocol on its interpretation by the Court of Justice”, OJ 1979 C59/71, 93, 94.

<sup>40</sup>Jonathan Hill, *International Commercial Disputes in English Courts*, (3<sup>rd</sup> edn, Hart Publishing, Oxford, 2005), p.62.

<sup>41</sup>C-391/95 [1998] ECR I-7091.

<sup>42</sup>A good example of interim measures is orders that intend to maintain the evidence or to protect an asset that is a subject of the dispute.

<sup>43</sup>C-391/95 [1998] ECR I-7091, para.21.

Court proceedings that relate to arbitration. In other words, the consumer cannot enjoy the protection that is granted to him under Article 16 of the Brussels I Regulation in most disputes that relate to online arbitration agreements and processes.

In the US, a choice of arbitral seat clause means that the consumer cannot refer disputes related to online arbitration agreements and processes to the Court of his domicile. This is not because jurisdiction rules designed to apply on the B2C e-commerce disputes do not apply on arbitration. The reason is that the notion of enabling the consumer to litigate international B2C disputes in his domicile is not well-established. For example, §2A-106(2) of the United States Uniform Commercial Code states that: “(I)f the judicial forum chosen by the parties to a consumer lease is a forum that would not otherwise have jurisdiction over the lessee, the choice is not enforceable.”<sup>44</sup> §2A-106(2) of the U.C.C does not provide the consumer with the right to litigate disputes relating to lease contract in his domicile. It only limits the number of fora that can be designated by a forum selection clause to the fora that have jurisdiction over the dispute.

To sum up this part of this chapter, a choice an arbitral seat that is foreign to the consumer means that the consumer cannot litigate disputes related to online arbitration agreements and processes in the Court of his country of domicile. The reason is that there is not a sufficient degree of consumer protection with regard to disputes that relates to online arbitration agreements and processes. Under the

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<sup>44</sup>§2A-106(2), Uniform Commercial Code.

English Law, insufficiency of the protection is attributed to the fact that Article 16 of the Brussels I Regulation does not apply to Court proceedings that relate to arbitration. In the US, the notion of protecting the consumer by allowing him to bring action in his domicile against a foreign business regardless the existence of a choice of forum clause is not well-established.

### **3. Unfairness and Unconscionability Rules**

The consumer can either rely on the unfairness and unconscionability rules in order to override a choice of foreign arbitral seat clause. However, both avenues cannot effectively guarantee the consumer the right to litigate disputes over online arbitration agreements and processes in the Courts of his country of domicile. In England, consumer can rely on the unfairness test which is embedded in the Unfair Contract Terms in Consumer Contracts Regulations 1999 <sup>45</sup> (hereinafter 1999 Regulations), to challenge a forum selection clause. Regulation 5(1) of the 1999 Regulations states that:

“[A] contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer.”<sup>46</sup>

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<sup>45</sup>Unfair Contract Terms in Consumer Contracts Regulations 1999, SI 1999/2083

<sup>46</sup>Ibid, Art.5(1). The meaning of good faith and significant imbalance and the matter that they form one requirement in this regulation have been explained in chapter two of this thesis. Schedule 2 of the 1999 Regulations annex mentions a few types of terms which might be considered unfair. Term (q) of the annex states terms might be unfair if it is “excluding or hindering the consumer’s right to take legal action or exercise any other legal remedy”. However, this list is only a guide and it does not mean that the forum selection clause is automatically invalid.

In the case of *Océano Grupo Editorial SA and Salvat Editores SA v. Rocío Murciano Quintero*,<sup>47</sup> the ECJ applied this unfairness test to a choice of Court clause and found that the clause is unfair. The ECJ explained that:

“It follows that where a jurisdiction clause is included, without being individually negotiated, in a contract between a consumer and a seller or supplier within the meaning of the Directive and where it confers exclusive jurisdiction on a court in the territorial jurisdiction of which the seller or supplier has his principal place of business, it must be regarded as unfair within the meaning of Article 3 of the Directive in so far as it causes, contrary to the requirement of good faith, a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer.”<sup>48</sup>

The Court has considered a choice of Court that confers jurisdiction of the Courts of the place of business as unfair. Although the *Océano* dealt with a choice of Court clause, there is no reason not to apply its rationale to a choice of an arbitral seat clause. However, the *Océano* case does not mean that a clause that designates an arbitral seat that is foreign to the consumer will always be regarded unfair. This is because Regulation 5(1) of the 1999 Regulations establishes a ‘composite test’ of unfairness which consists of two connected requirements. These two requirements are the contradiction of good faith which leads to the significant imbalance to the detriment of the consumer.<sup>49</sup> The test will only guarantee the consumer the right to litigate international B2C disputes in his domicile if the choice of an arbitral seat clause satisfies the two requirements. The clause must create a significant imbalance to the detriment of the consumer in a way contrary to the good faith. If the choice of

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<sup>47</sup>27 June 2000, Cases C-240/98 to C-244-98.

<sup>48</sup>Ibid

<sup>49</sup>*Director-General of Fair Trading v First National Bank Plc*, [2002] 1 Lloyd's Rep. 489, 496,497. See section 2.1 of chapter 3.

an arbitral seat clause causes significant imbalance to the detriment of the consumer without being contrary to good faith, the clause is valid.

An illustration of the above-described situation can be found in the case of the *Standard Bank London Ltd v Apostolakis & Anor.*<sup>50</sup> In this case, the defendants were a married couple, resident in Greece, who concluded a contract with the claimant bank which is the Standard Bank London (hereinafter SBL). The contract related to foreign exchange margin trading. The contract was drafted in English and it included a choice of forum clause that nominated England as the forum in which any future dispute should be litigated. The Greek defendants signed the contract in Athens at the offices of a financial adviser called Eurofinance SA ('EF'). The defendants had a poor command of the English language and they were not provided with a translation of the contract. Pursuant to the contract the Greek defendants entered into many transactions for the forward purchase of ECUs for Greek drachma. After that, the drachma's value was reduced and the SBL relied on a deposit of \$1.1m made by the defendants as a margin to close out the defendants' open position. The defendants brought an action in a Greek Court claiming that SBL's conduct was illegal. SBL brought an action in England seeking an injunction to restrain the Greek proceedings on the basis that the defendants had agreed to the jurisdiction of the English Court. The defendants claimed that the forum selection clause was unfair according to the 1999 Regulations.<sup>51</sup> The English Court held that the choice of

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<sup>50</sup>[2002] C.L.C. 939

<sup>51</sup>This has now been replaced by the Unfair Terms in Consumer Contracts Regulation 1999.



forum clause was unfair according to Regulation 5(1) of the 1999 Regulations.

David Steel J, delivered the judgment and he asserted that:

“The jurisdiction clause was also an unfair term within the 1994 and 1999 regulations. The jurisdiction clauses were unfair by reason of the imbalance of convenience between the parties. While in some cases the unfairness might be overcome by careful explanation of the meaning and effect of the clause, in this case the clauses were not explained or even translated. The purpose of the regulations was to protect consumers and the defendants were consumers. The present proceedings demonstrated the potential cost and inconvenience to the defendants of being bound to the English jurisdiction. The imbalance which had taken the defendants by surprise was contrary to good faith and accordingly the jurisdiction clause was not binding.”<sup>52</sup>

The English Court could not solely rely on the inconvenience that the forum selection clause caused to the consumer to presume that the unfairness test has been satisfied. The Court’s decision shows that the imbalance resulted from the inconvenience of the designated forum will not satisfy the fairness test if an explanation or translation of the forum selection clause was provided to the defendants. Consequently, the 1999 Regulations will not produce a situation in which the consumer can litigate a B2C dispute over arbitration agreements and process in his domicile unless the two requirements of the fairness test are satisfied. The fact that litigation abroad is inconvenient to the consumer is insufficient to establish a consumer’s right to litigate disputes over online arbitration agreements and process in his domicile.

In the US, unconscionability rules, which are embodied in §2-302 of the UCC, cannot effectively guarantee the consumer the right to litigate disputes over online arbitration agreements and processes in the Courts of his country of domicile. This is

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<sup>52</sup>[2002] C.L.C. 939

because the high cost and inconvenience of litigation in a foreign forum will rarely lead to the invalidation of a choice of an arbitral seat clause under the unconscionability rules. In the case of *Carnival Cruise Lines, Inc v Shute*,<sup>53</sup> a Washington couple called Mr. and Mrs. Shute purchased cruise tickets from a Florida-based cruise line. The tickets included a forum selection clause that provided that any dispute should be submitted to the Courts of the State of Florida which is 2500 miles away from Washington State.<sup>54</sup> The Shutes boarded the ship in Los Angeles. Mrs. Shute suffered injuries when she slipped on a deck mat while the ship was in international waters off the Mexican coast. The Shutes filed a suit in the Washington Federal District Court. Carnival alleged that the District Court lacked personal jurisdiction because Carnival's contacts with the State of Washington were insubstantial. The Federal Court of Appeal reserved the district Court's decision and it stated that Carnival had substantial contact with the state of Washington. After that, Carnival claimed that the Court of Appeal should stay the proceedings according to the forum selection clause included in the ticket. The Court of Appeal concluded that the forum selection clause should not be enforced because it was not freely negotiated.<sup>55</sup> The US Supreme Court reserved the Federal Court of Appeal decision and it held that:

“Court of Appeals erred in refusing to enforce the forum-selection clause... It would be entirely unreasonable to assume that a cruise passenger would or could negotiate the terms of a forum clause in a routine commercial cruise ticket form. Nevertheless, including a reasonable forum clause in such a form contract well may be permissible for several reasons. Because it is not unlikely that a mishap in a cruise could subject a cruise line to litigation in several

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<sup>53</sup>499 US 585 (1991).

<sup>54</sup>Ibid

<sup>55</sup>Ibid, p.586.

different fora, the line has a special interest in limiting such fora. Moreover, a clause establishing ex ante the dispute resolution forum has the salutary effect of dispelling confusion as to where suits may be brought and defended, thereby sparing litigants time and expense and conserving judicial resources. Furthermore, it is likely that passengers purchasing tickets containing a forum clause like the one here at issue benefit in the form of reduced fares reflecting the savings that the cruise line enjoys by limiting the fora in which it may be sued... It bears emphasis that forum selection clauses contained in form passage contracts are subject to judicial scrutiny for fundamental fairness. In this case, there is no indication that the petitioner set Florida as the forum in which disputes were to be resolved as a means of discouraging cruise passengers from pursuing legitimate claims... the petitioner has its principal place of business in Florida, and many of its cruises depart from and return to Florida ports....<sup>56</sup>

Although this case deals with a choice of Court clause, there is no reason not to apply it to choice of an arbitral seat clause. This case indicates that why the inconvenience of the foreign forum rarely leads to the invalidation of a choice of an arbitral seat clause under the unconscionability rules. The US Supreme Court approved the fairness of the business interests in fixing its place of business as the forum for any future dispute with the consumer. As mentioned supra, in this case the designated forum is 2500 miles away from the Shutes' home state. It cannot be said that the US Supreme Court is not aware of the fact that a forum that is 2500 miles away from the home state of the Shutes is inconvenient for them. This means that the Court will not view the choice of the place of business as an arbitral seat as unfair. The high costs of litigation in the Courts of the arbitral seat will rarely lead to the invalidation of the choice of an arbitral seat clause under the unconscionability rules. This is because proving the unconscionability of the choice of an arbitral seat clause requires proving a fact other than the fact that the cost of litigation in the foreign forum is too high. The consumer has to prove that the high costs make him

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<sup>56</sup>Ibid, p.585, 586,595.

financially incapable of litigating the disputes related to the online arbitration agreements and processes in a foreign forum. Evidence for this argument can be deduced from the application of the unconscionability rules on arbitration clauses in B2C contracts. In the case of *Livingston v Associates Fin. Inc.*<sup>57</sup>, a loan agreement included an arbitration clause. The Livingstons alleged that the arbitration clause should not be enforced against them because of the high costs of arbitration. However, the United States Courts of Appeal refused this allegation and it stated that:

“the Livingstons have not offered any specific evidence of arbitration costs that they may face in this litigation, prohibitive or otherwise, and have failed to provide any evidence of their inability to pay such costs”.<sup>58</sup>

The Court of Appeal explained that the livingstons failed to show that the arbitration costs are high and they also failed to show that these costs do not proportionate to their financial capabilities. It is clear from this case that the Court will not only rely on the high cost of arbitration to hold the arbitration clause unconscionable. The Court requires a proof that the consumer is financially incapable to cover these costs. Another evidence for this argument can be seen in the case of *Anders v Hometown Mortg. Services, Inc.*<sup>59</sup> In this case, the loan agreement between Anders and Hometown Mortgage included an arbitration clause. Anders alleged that the arbitration clause should not be enforced because he is financially incapable of meeting the costs of the arbitral process. The United States Courts of Appeal refused

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<sup>57</sup>339 F.3d 553, (7<sup>th</sup> Cir. 2003).

<sup>58</sup>Ibid, p. 557.

<sup>59</sup>346 F.3d 1024 C.A.11 (Ala.), 2003.

that contention and explained that Anders failed to prove that he is financially incapable of participating in the arbitral process.<sup>60</sup>

The practice shows that consumers frequently fail to meet this heavy burden of proving their financial incapability. In the case of *Green Tree v Randolph*,<sup>61</sup> the US Supreme Court held that an arbitration clause can be unconscionable if the costs of arbitration prohibit the consumer from participating in the arbitral process.<sup>62</sup> However, the US Supreme Court explained that the consumer bears the burden of proving that he is financially incapable to participate in the arbitral process.<sup>63</sup> Randolph failed to prove that she was financially incapable to arbitrate the dispute because of the costs of arbitration. In many subsequent cases consumers alleged that the arbitration clause were unconscionable because of high cost of arbitration. However, in most cases,<sup>64</sup> the consumers failed to prove that they were financially incapable of participating in the arbitral process.<sup>65</sup>

## 4. Conclusion

For the consumer to have confidence in online arbitration, the consumer should be able to litigate dispute related to online arbitration agreements and processes in the Courts of his country of domicile. However, an arbitral seat selection clause that nominates a country foreign to the consumer deprives the consumer the right to

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<sup>60</sup>Ibid, p.1028.

<sup>61</sup>531 US 79 (2000).

<sup>62</sup>Ibid, p.86-89

<sup>63</sup>ibid

<sup>64</sup>The case of *Olshan Foundation Repair Company v Ayala*, 180 S.W.3d 212 Tex.App.-San Antonio, 2005, is one of the rare cases in which the consumer managed to prove that he is financially incapable of participating in the arbitral process.

<sup>65</sup>F. Paul Bland, Jr., Michael J. Quirk, Kate Gordon, and Jonathan Sheldon, *Consumer Arbitration Agreements: Enforceability and Other Topics*, (4<sup>th</sup> edn, NCLC, Boston, 2004), p.56.

litigate disputes related to online arbitration agreements and processes in the Courts of his country of domicile. One reason is the non-applicability of jurisdiction rules that provide the consumer the right to litigate international B2C e-commerce disputes in his domicile on arbitration. This situation is exemplified in the Brussels I Regulation. Another reason is that the consumer's right to litigate international disputes with foreign businesses in his domicile is not well-established under the law of his domicile. This situation is exemplified in §2A-106(2) of the UCC.

Another reason is that Unfairness rules, the unconscionability rules, cannot effectively guarantee the consumer the right to litigate disputes over online arbitration agreements and processes in his country of domicile. The high costs and inconvenience of litigation in the foreign forum are the main defences that the consumer can use to challenge a forum selection clause. However, if the two defences do not come with bad faith in the method of introducing the forum selection clause into the B2C e-commerce contract, the two defences cannot lead to the invalidation of the forum selection clause under Regulation 5 of the 1999 Regulations. The two defences also rarely lead to the invalidation of the forum selection clause under the unconscionability rules. In the *Carnival* case, the US Supreme Court refused to consider the forum selection clause unconscionable. The Court explained that transacting with consumers from different jurisdictions makes the business subject to litigation in many forums. Therefore, the business has an interest in limiting the number of these forums. The US Supreme Court also explained that a choice of forum clause will allow the business to offer the consumer cheaper prices. The high cost of litigation in the foreign forum is insufficient to hold

the choice of an arbitral seat clause unconscionable. This is because the consumer has to prove that he is financially incapable of litigating the dispute in the designated foreign forum.

## Chapter 7

### Promoting the Consumer's Perception of Fairness of the Online Arbitral Procedures

Consumers will be ready to arbitrate their e-commerce disputes with businesses if they have confidence in the online arbitral process. Due process applies to all adjudicative methods of dispute resolution such as litigation and arbitration.<sup>1</sup> Due process consists of two main standards that seek to ensure the procedural fairness of the adjudicative dispute resolution proceedings. These standards are that each party should be given a reasonable chance to present his case and reply to the other party's submissions<sup>2</sup> and the tribunal reviewing the dispute should be impartial.

Procedural fairness that due process seeks to achieve can be divided into objective and subjective or perceived. Objective fairness means that the dispute resolution proceeding has, in fact, complied with the required standards of due process.<sup>3</sup> Regarding perceived fairness, the meaning of perceived fairness can be deduced from the European Court of Human Rights (hereinafter ECHR) decision in the case of *P C & S v United Kingdom*.<sup>4</sup> In that case P's lawyer stopped representing her. The judge refused her application for an adjournment to instruct a new lawyer. P complained to the ECHR claiming that the Court's refusal to adjourn the proceeding

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<sup>1</sup>Henry H. Perritt, Jr., "Dispute Resolution in Cyberspace: Demand for New Forms of ADR", (2000) 15 Ohio St. J. on Disp. Resol. 675, 677.

<sup>2</sup>Julia Hömle, "Online Dispute Resolution in Business to Consumer E-commerce Transactions", (2002) (2) J.I.L.T. available at: <[http://www2.warwick.ac.uk/fac/soc/law/elj/jilt/2002\\_2/homle/](http://www2.warwick.ac.uk/fac/soc/law/elj/jilt/2002_2/homle/)>, accessed on 15/12/2007

<sup>3</sup>Neil Vidmar, "The Origins and Consequences of Procedural Fairness", (1990) 15 Law & Soc. Inquiry 877, 879. John Thibaut and Laurens Walker, *Procedural Justice: A Psychological Analysis*, (Lawrence Erlbaum Associates, New Jersey, 1975), p.3, 4.

<sup>4</sup>(App No 56547/00) [2002] All ER



until she retain a new lawyer deprived her the legal representation and thereby violated her right to a fair trial under Article 6 of the Human Rights Convention.<sup>5</sup>

The ECHR accepted P's claim and it held that:

“the Court is nevertheless of the opinion that the procedures adopted not only gave the appearance of unfairness but prevented the applicants from putting forward their case in a proper and effective manner on the issues which were important to them.”<sup>6</sup>

The perceived fairness means that the arbitral procedures are not only fair but also appear to be fair. Perceived fairness is a central factor in raising the consumer confidence in the online arbitral process. Vidmar explained that “if disputants do not see procedures as fair, they will not accord them legitimacy, will avoid them if possible, and if forced to use them, will not readily accept the outcomes”.<sup>7</sup> The consumer who might be a prospective user of online arbitration will draw his perception of fairness of the online arbitral procedures from the laws that implement due process standards and the way online arbitral proceedings are conducted. If the online arbitral procedures appear to be fair, the consumer will have confidence in online arbitration, thereby he will be happy to arbitrate his e-commerce disputes with online businesses.<sup>8</sup>

However, this chapter aims to show that the current regulatory framework does not promote the consumer's perception of fairness of the online arbitral procedures. This chapter is divided into three parts. The first part explains that the consumer will see

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<sup>5</sup> Art.6 ,Convention for the Protection of Human Rights and Fundamental Freedoms (European Convention on Human Rights, as amended) (ECHR)

<sup>6</sup>(App No 56547/00) [2002] All ER

<sup>7</sup>Vidmar, note 3 supra, p.879.

<sup>8</sup>Ibid

the online arbitral procedures as fair if the rules implementing these procedures give him the impression that he will have the chance to present his case and reply to the other party's submissions. This part consists of three sections; the first explains that the consumer should be able to obtain legal representation. The second and the third sections explain that the consumer should have the chance to present evidence. The second part of this chapter explains that the online arbitration provider and the online arbitral tribunal should appear to be impartial in order to make the consumer perceive the fairness of the online arbitral procedures. This part consists of three sections. The first explains that the online arbitration provider should be independent. The second explains that both the business and the consumer should have equal voices in the selection of the arbitrators. The third explains that arbitral awards should be published. The third part of this chapter explains that in order to encourage the consumer to perceive fairness of the online arbitral procedures, there should be strict judicial review on aspects of procedural unfairness.

## **1. The Chance to be Heard and the Perceived Fairness of the Online Arbitral Procedures**

As explained *supra*, perceived fairness of the online arbitral procedures has an important role in raising consumer confidence in the online arbitral process. Adler and others compiled a report for the Institute of Civil Justice on the Pittsburgh Court Arbitration Program. They explained that:

“most litigants used a very simple standard for evaluating arbitration: they wanted an opportunity to have their case heard and decided by an impartial

third party. When this requirement was met, they reported that the arbitration process had been fair.”<sup>9</sup>

The parties deemed the arbitral process to be fair when they had been given the chance to present their cases and the chance to reply to the other party’s submissions. Therefore, the consumer will view the online arbitral procedures as fair if the rules implementing these procedures give him the impression that he will have the chance to present his case and reply to the other party’s submissions. Many factors have role in this. These factors are the chance to obtain legal representation; the chance to introduce evidence and the admissibility of electronic evidence. In the following sections the author will explain how these issues are currently dealt with and how they should be dealt with in order to persuade the consumer that he has the chance to present his case and reply to the other party’s submissions.

## **1.1 The Chance to Obtain Legal Representation**

In the case of *P C & S v United Kingdom*,<sup>10</sup> the ECHR held that the denial of the right to obtain legal representation prevented *P* from presenting her case.<sup>11</sup> Therefore, the chance to obtain legal representation is crucial to persuade the consumer that he will obtain a reasonable chance to present his case. However, the consumer may be denied the chance to obtain legal representation. Parties to the arbitral process can exclude the right to be represented by agreement. §36 of the English Arbitration Act 1996 states that, “unless otherwise agreed by the parties, a party to arbitral

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<sup>9</sup>Jane W. Adler, Deborah R. Hensler, Charles E. Nelson and Gregory J. Rest, *Simple Justice: How Litigants Fare in the Pittsburgh Court Arbitration Program*, (Rand, Santa Monica, 1983), p65. (hereinafter Rand Report).

<sup>10</sup>(App No 56547/00) [2002] All ER

<sup>11</sup>Ibid

proceedings may be represented in the proceedings by a lawyer or other person chosen by him.”<sup>12</sup> As mentioned supra, online B2C transactions are concluded via adhesion contracts. This means the business can include a clause in the contract that deprives the consumer of the right to obtain legal representation.

Hörnle raised the question of whether legal representation should be allowed at all. She explained that legal representation, “might be too expensive” for consumer disputes since these disputes are of low value.<sup>13</sup> She also explained that allowing “legal representation in consumers’ disputes may lead to further inequality of arms, as the supplier would be represented whereas the consumer would not.”<sup>14</sup> Gibbons also explained that “attorney fees may also make the process unaffordable” and it might increase the delay in the arbitral process.<sup>15</sup> Perritt’s opinion is similar. He observed that:

“Allowing counsel increases the cost of dispute resolution procedures. A party wishing to minimize costs nevertheless may be unwilling to suffer the disadvantage associated with being unrepresented while the opponent is represented. Moreover, use of counsel interposes delay. Parties must be allowed time to find and retain counsel, and counsel must be allowed time to become familiar with the case. When disputants act without counsel, they may proceed directly to define their dispute before the decisionmaker.”<sup>16</sup>

It is true that legal representation might be too costly for consumer disputes that involve low claims. It is also true that the high cost of legal representation might

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<sup>12</sup>§ 36, English Arbitration Act 1996.

<sup>13</sup>Julia Hörnle, “Disputes Solved in Cyberspace and the Rule of Law”, (2001) J.I.L.T, available at: <[http://www2.warwick.ac.uk/fac/soc/law/elj/jilt/2001\\_2/hornle/](http://www2.warwick.ac.uk/fac/soc/law/elj/jilt/2001_2/hornle/)>, accessed on 12/12/2007, (hereinafter Disputes Solved),

<sup>14</sup>Ibid.

<sup>15</sup>Llewellyn Joseph Gibbons, “Creating Market for Justice: A Market Incentive Solution to Regulating the Playing Field: Judicial Deference, Judicial Review, Due Process, and Fair Play in Online Consumer Arbitration”, (2002) 23 Nw. J. Int’l L. & Bus.1, 23. (hereinafter Creating Market).

<sup>16</sup>Perritt, note 1 supra, p. 681.

lead to a situation where the business is represented but the consumer is not. The high cost of legal representation might be the reason for the EU Commission's stance regarding the consumer's right to obtain legal representation. Principle IV of the EU Commission Recommendation (98/257/EC) states that the consumer should not be obliged to use legal representation.<sup>17</sup> However, forbidding legal representation in online B2C arbitration will deter the consumer from believing that he will be able to present his case. This will impact upon his perception of the fairness of online arbitral procedures and thereby reduce his confidence in the online arbitral process.

Perritt suggested that, "online arbitration system should allow for counsel, perhaps subject to control by the arbitrator, who may determine in simple cases that no counsel is permitted".<sup>18</sup> However, this solution will not help to increase the consumer's perception of the fairness of the online arbitral process. The reason is that as there is no clear criteria to determine which dispute is simple, the consumer will not be sure when he can obtain legal representation. The general rule should be to allow the parties to obtain legal representation whenever they want. Overcoming the high cost and "inequality of arms" requires a more effective role for consumer protection organisations in assisting the consumer to obtain legal representation.<sup>19</sup> Consumer protection organisations should be able to help consumers to obtain low-cost or free legal representation in online arbitral proceedings. Governments and

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<sup>17</sup>Principle IV, Recommendation (98/257/EC).

<sup>18</sup>Perritt, note 1 *supra*, p.681.

<sup>19</sup>Reporter's Comment on Principle 9, Statement of Principles of the National Consumer Disputes Advisory Committee, Consumer Due Process Protocol, available at [http://www.adr.org/sp.asp?id=22019#STATEMENT\\_OF\\_PRINCIPLES](http://www.adr.org/sp.asp?id=22019#STATEMENT_OF_PRINCIPLES), accessed on 12/12/2007. (hereinafter Consumer Due Process Protocol).

internet stakeholders should consider increasing financial support to consumer protection organisations in order to enable these organizations to assist the consumer in obtaining legal representation.

## 1.2 The Chance to Introduce Evidence

The method of producing evidence is the production of documents; testimony of witnesses and this can be either oral or written; opinions of expert witnesses and this can also be either oral or written; inspection of the subject-matter of the dispute.<sup>20</sup>

The production of documents is a very important tool in the presentation of the consumer's case.<sup>21</sup> The production of documents is important in B2C e-commerce disputes because the business is more likely to be the party who stores all the related documents and information about the e-commerce transaction.<sup>22</sup> Testimony by a witness and an expert witness is also an important tool for the presentation of the consumer's case or to defeat the other party's submissions.<sup>23</sup> If the consumer buys electronic equipment via the internet and then finds out that it is faulty, he might need the testimony of a witness or even an expert witness to prove his allegation. Inspection is also important. The consumer might buy a computer program via the internet but the program is defective or it has not been delivered to him at all.<sup>24</sup> In such a case, inspection of the consumer's computer is necessary to ensure the

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<sup>20</sup> Alan Redfern and Martin Hunter, *Law and Practice of International Commercial Arbitration*, (3<sup>rd</sup> edn, Sweet & Maxwell, London, 1999), p.315.

<sup>21</sup> Mark E. Budnitz, "Arbitration of Disputes between Consumers and Financial Institutions: A Serious Threat to Consumer Protection", (1995) 10 Ohio St. on Disp. Resol. 267, 314.

<sup>22</sup> Ibid, p.311.

<sup>23</sup> Nicolas de Witt, "Online International Arbitration: Nine Issues Crucial to its Success", (2001) 12 Am. Rev. Int'l. Arb. 441, 457-60. Principle III, Recommendation (98/257/EC).

<sup>24</sup> Gabrielle Kaufmann-Kohler and Thomas Schultz, *Online Dispute Resolution: Challenges for Contemporary Justice*, (1<sup>st</sup> edn, Kluwer Law International, Hague, 2004), p.182.

validity of his allegation. Therefore, the chance to rely on any one of these methods of producing evidence is crucial to persuade the consumer that he will have a reasonable chance to present his case. However, the consumer may be denied the chance to rely on a particular method of introducing evidence. Arbitration laws allow parties to articulate the arbitral procedures, including the methods of introducing evidence by agreement. §34 of the English Arbitration Act 1996 states that:

“(1) It shall be for the tribunal to decide all procedural and evidential matters, subject to the right of the parties to agree any matter.

(2) Procedural and evidential matters include -

(f) whether to apply strict rules of evidence (or any other rules) as to the admissibility, relevance or weight of any material (oral, written or other) sought to be tendered on any matters of fact or opinion, and the time, manner and form in which such material should be exchanged and presented.”<sup>25</sup>

In the US, the Federal Arbitration Act 1925 (hereinafter FAA) does not expressly award the parties the right to agree on procedural and evidential matters. However, under the FAA parties can agree on procedural and evidential matters in arbitration. In the case of *Card v Stratton Oakmont, Inc.*,<sup>26</sup> the United States District Court of D. Minnesota held that the parties’ choice of the Code of Arbitration Procedure of the NASD is valid.<sup>27</sup> As explained supra, online B2C e-commerce contracts are concluded via adhesion contracts. This means that the business can determine which methods of introducing evidence will be followed. If the business limits the number of methods that can be used to introduce evidence, it is difficult to persuade the

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<sup>25</sup>§34, English Arbitration Act 1996.

<sup>26</sup>933 F.Supp. 806, (D. Minn. 1996)

<sup>27</sup>Ibid, p. 814.

consumer that he will obtain a chance to present his case or reply to other party's submissions. This will deter him from perceiving the fairness of the online arbitral procedures and thereby reduce his confidence in online arbitration. Therefore, agreement on methods of introducing evidence should not be allowed before the dispute occurs. Such agreement should only be recognized if it is concluded after the dispute occurs. In the case that the business and the consumer do not achieve such an agreement, the arbitrator will decide which methods of introducing evidence will be allowed. The arbitrator shall practice this authority bearing in mind that he should treat the parties equally and at the same time try to avoid unnecessary delay and reduce the cost of the online arbitral process.

### **1.3 Admissibility of Electronic Documents and Records into Evidence**

Electronic evidence might take many forms.<sup>28</sup> It can appear in the form of typed documents. It can also take the form of scanned photos or scanned copies of the original paper documents. It can also take the form of simultaneous video or audio broadcasting which is usually called video or audio-conferencing.<sup>29</sup> In the context of B2C e-commerce disputes, electronic documents are important to prove the offer and the acceptance of the contract and the contract terms as well.<sup>30</sup> Video and audio-conferencing can also be important to present testimony by a witness to the arbitral

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<sup>28</sup>Witt, note 23 supra, p.458. Ethan Katsh, Janet Rifkin & Alan Gaitenby, "E-Commerce, E-Disputes and E-Dispute Resolution: In the Shadow of 'eBay Law,'" (2000) 15 Ohio St. J. on Disp. Resol. 705, 723.

<sup>29</sup>Witt, note 23 supra, p.458.

<sup>30</sup>Kohler and Schultz, note 24 supra, p.182.



tribunal.<sup>31</sup> However, the consumer may be denied the chance to introduce a particular type of evidence. As explained *supra*, online B2C transactions are concluded via adhesion contracts and parties can agree on evidential matters.<sup>32</sup> This means that the business can limit the type of evidence that the consumer can introduce. Such a situation will deter the consumer from perceiving that he will obtain a reasonable chance to present his case or reply to the other party's submissions. Therefore, agreements on which type of evidence parties can introduce should not be allowed before the dispute occurs.

With regard to the weight that arbitrators should give to electronic evidence, the arbitrator should not deny the admissibility of evidence just because it is in electronic form. Arbitrators are not obliged by rules of evidence as applicable in national courts.<sup>33</sup> However, these rules constitute a guide on the evidentiary weight that should be given to electronic evidence. Rule 31.4 of the English Civil Procedures Rules 1998 states that, "document means anything in which information of any description is recorded".<sup>34</sup> The definition of the term "document" in Rule 31.4 is wide enough to cover electronic documents, as well as audio and video records. Rule 34(a) of the US Federal Rules of Civil Procedures 2007 states that:

"A party may serve on any other party a request:

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<sup>31</sup>Julia Hörnle, "Online Dispute Resolution: the Emperor's New Clothes?: Benefits and Pitfalls of Online Dispute Resolution and its Application to Commercial Arbitration", (2003) 17(1) Int'l. Rev. L.Comp.27, 30, 31. (hereinafter *clothes*)

<sup>32</sup>§34, English Arbitration Act 1996. 933 F.Supp. 806, 814 (D. Minn. 1996)

<sup>33</sup>Kohler and Schultz, note 24 *supra*, p.190.

<sup>34</sup>Rule 31.4, English Civil Procedures Rules 1998.

(1) to produce and permit the requesting party or its representative to inspect, copy, test, or sample the following items in the responding party's possession, custody, or control:

(A) any designated documents or electronically stored information - including writings, drawings, graphs, charts, photographs, sound recordings, images, and other data or data compilations - stored in any medium from which information can be obtained either directly or, if necessary, after translation by the responding party into a reasonably usable form,”<sup>35</sup>

Rule 34(a) of US Federal Rules of Civil Procedures 2007 allows the request to produce electronically stored information. This means that electronic documents, video records and audio records can be admitted into evidence. In deciding the evidentiary weight of electronic evidence the arbitral tribunal should look at the reliability and trustworthiness of the evidence.<sup>36</sup> In evaluating the trustworthiness of electronic evidence the arbitral tribunal should take account of the authenticity element, especially whether an electronic signature has been used.<sup>37</sup> An electronic signature<sup>38</sup> does help in protecting electronic documents from alteration.<sup>39</sup>

## **2. The Apparent Impartiality of the Online Arbitration Provider and the Arbitral Tribunal**

As explained above, the perceived fairness of the online arbitral procedures is important to ensure the consumer's confidence in the online arbitral process.

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<sup>35</sup>Rule 34(a), US Federal Rules of Civil Procedures 2007.

<sup>36</sup>Kohler and Schultz, note 24 supra, p.190.

<sup>37</sup>Ibid, p.190.

<sup>38</sup>Article 2(a) of the UNCITRAL Model Law on Electronic Signatures 2001 states that an electronic signature “means data in electronic form in, affixed to or logically associated with, a data message, which may be used to identify the signatory in relation to the data message and to indicate the signatory's approval of the information contained in the data message. Article 2(c) defines “Data message” as “information generated, sent, received or stored by electronic, optical or similar means including, but not limited to, electronic data interchange (EDI), electronic mail, telegram, telex or telecopy; and acts either on its own behalf or on behalf of the person it represents.”

<sup>39</sup>Alejandro López Ortiz, “Arbitration and IT”, (2005) 21(3) Arb. Int'l.343, 356.

Tweedle and Tweedle explained that one way of deciding whether the arbitral tribunal is impartial is examining whether the procedures adopted are fair.<sup>40</sup> This means that the question of whether the arbitral tribunal appears to be impartial is one way of expecting whether the arbitral procedures will be fair. Therefore, raising the consumer's perception of fairness in the online B2C arbitral procedures requires that the arbitrator or the arbitral tribunal appears to be impartial. What is more, raising the consumer's perception of fairness of the online arbitral procedures requires the online arbitration provider to appear to be impartial. This is because the online arbitration providers "perform many functions which have a direct impact on the conduct of the dispute resolution process".<sup>41</sup> An example of these functions is that the arbitral institution decides whether time-limits for the arbitral process, embedded in the arbitration rules of that institution, should be extended.<sup>42</sup>

The apparent impartiality of the online arbitration provider requires its independence from the parties.<sup>43</sup> Apparent impartiality of the arbitral tribunal requires that both the business and the consumer "have an equal voice in the selection" of the arbitrator.<sup>44</sup> Apparent impartiality also requires transparency in respect to the procedural transcripts and publication of the arbitral awards. In the following sections the author will explain how these issues are dealt with and how they should be dealt

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<sup>40</sup> Andrew Tweedle and Keren Tweedle, *Arbitration of Commercial Disputes: International and English Law and Practice*, (1<sup>st</sup> edn, OUP, Oxford, 2005), p.770, 772.

<sup>41</sup> Reporter's Comments on Principle 3, Consumer Due Process Protocol. Schellekens explained that online arbitration services are offered by ODR providers. M. H. M. Schellekens, "Online Arbitration and E-commerce", (2002) E.C.L.Rev.113.

<sup>42</sup> Redfern and Hunter, note 20 *supra*, p.45.

<sup>43</sup> Principle I of Recommendation (98/257/EC).

<sup>44</sup> Reporter's Comments on Principle 3, Consumer Due Process Protocol.

with in order to ensure the apparent impartiality of the online arbitration provider and the arbitral tribunal.

## **2.1 Independence of the Online Arbitration Provider**

As explained above, the online arbitration provider should appear to be impartial in order to raise the consumer's perception of the fairness of the online arbitral procedures. Apparent impartiality of the online arbitration provider requires independence of the online arbitration provider from the parties.<sup>45</sup> Hörnle explained that the "ODR services provider... must be and must be seen to be independent."<sup>46</sup> However, arbitration laws do not require the independence of the online arbitration provider. Under the English Arbitration Act 1996 there is no duty of independence on the arbitration services provider. Para 101 of the Departmental Advisory Committee Report on the Arbitration Bill (hereinafter DAC Report) states that:

"It seems to us that lack of independence, unless it gives rise to justifiable doubts about the impartiality of the arbitrator, is of no significance. The latter is, of course, the first of our grounds for removal. If lack of independence were to be included, then this could only be justified if it covered cases where the lack of independence did not give rise to justifiable doubts about the impartiality, for otherwise there would be no point including lack of independence as a separate ground."<sup>47</sup>

Para 101 of the DAC makes it clear that there is no duty of independence on the arbitration provider. The applicable test is whether the arbitrator is impartial. In the same vein, under the FAA there is no duty of independence on the arbitration service provider. Evidence for this argument can be derived from the fact that bias of the

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<sup>45</sup>Principle I of Recommendation (98/257/EC).

<sup>46</sup>Hörnle, (business-to-consumer), note 2 *supra*.

<sup>47</sup>Departmental Advisory Committee on Arbitration Law, *Report on the Arbitration Bill 1996*.

arbitration provider alone is insufficient to establish the unconscionability of the arbitration clause. In the case of *Geiger v Ryan's Family Steak Houses, Inc.*,<sup>48</sup> the Federal District Court of Indiana found that an arbitration clause that referred disputes between Geiger and Ryan to Employment Dispute Services, Inc. (hereinafter EDSI) was unconscionable because of potential bias in the arbitral forum. Barker, District Judge, observed that:

“EDSI thus clearly has an incentive to maintain its contractual relationship with Ryan's and other such business partners while applicants or employees, such as Geiger and Sadler, have no leverage, having been presented with the arrangement on a take-it-or-leave-it basis. The imbalance is made even more painfully obvious by the fact that EDSI relies entirely on representatives of the employer to explain the Agreement's provisions to would be employees and to secure their signatures; Ryan's is EDSI's agent at this point and both are fully invested in the activities of the other. EDSI also retains full authority to select both the Rules for arbitration as well as the pools of potential arbitrators. Such power in the face of the potential for bias on the part of EDSI in favor of employers such as Ryan's renders it unlikely that applicants/employees will participate in an unbiased forum.”<sup>49</sup>

In this case, the ongoing referral from *Ryan's* to EDSI constituted a dependant relationship between the parties. What also augments the dependant relationship between *Ryan's* to EDSI is that Ryan's representatives explained the arbitration agreement to the prospective employees. In other words, Ryan's representatives worked as agents for EDSI. The Court viewed this relationship as bias on the part of EDSI towards Ryan's. However, the Court did not solely rely on the EDSI bias to conclude that the arbitration clause is unconscionable. The court looked at EDSI bias and its exclusive authority to appoint the arbitrator to conclude that it is “unlikely that applicants/employees will participate in an unbiased forum”. In other words, the

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<sup>48</sup>134 F. Supp. 2d 985, 995 (S.D. Ind. 2001)

<sup>49</sup>Ibid

court established its final decision on the unconscionability of the arbitration clause on the presumption that the arbitrator was unlikely to be impartial. If EDSI had arbitration rules that guaranteed the impartiality of the arbitrator, the court would not consider the arbitration clause unconscionable. Illustration for this can be seen in the case of *Bank One, N.A. v Coates*.<sup>50</sup> In this case Coates claimed the arbitration clause is unconscionable because the arbitration services provider which was the National Arbitration Forum (hereinafter NAF) was biased to the claimant which was Bank One. The Court did not find any bias on the part of NAF and the Court held that:

“In any event, the rules governing the conduct of NAF arbitrations belie defendant's speculation that suspected bias by the NAF has any realistic potential for affecting decisions of arbitrators in NAF arbitrations. In this regard, the court observes that the NAF does not conduct the arbitration itself, but rather appoints independent third-party arbitrators who actually conduct the proceedings; and those arbitrators may not be officers or directors of the NAF, they must take an oath to be “independent and neutral” and they must disclose any circumstances that might constitute a conflict of interest.”<sup>51</sup>

The Court explained that bias on the part of the NAF is immaterial because the NAF arbitration rules guarantee that a biased arbitrator will not be allowed to hear the dispute. If bias of the arbitration provider is solely insufficient to establish the unconscionability of the arbitration clause, lack of independence of the online arbitration provider will also be insufficient, especially in the case that lack of independence does not reach the degree of bias. The fact that lack of independence of the arbitration provider is solely insufficient to establish the unconscionability of the arbitration clause means that the online arbitration provider does not have to be independent. In the context of the online B2C arbitration, tolerability with the

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<sup>50</sup>125 F.Supp.2d 819 (S.D.Miss., 2001)

<sup>51</sup>*Ibid*, p. 835, 836.

independence requirements allows the online arbitration provider to become administratively and financially dependent on the business. In the context of online B2C e-arbitration, it is possible that the business about which the consumer has filed a complaint participates in the management of the dispute resolution provider. This situation may arise in the context of the online B2C arbitration that is offered through Trustmark Schemes. The Trustmark means that the seller is certified by a third party as being trustworthy transaction partner. The Trustmark means that the seller will comply with particular criteria set by the Trustmark issuer. One criterion is that the business will submit disputes with the online consumers to the dispute resolution system provided by the Trustmark issuer.<sup>52</sup> The business might subscribe to a particular Trustmark. At the same time the business has representatives on the board of directors of the Trustmark.<sup>53</sup> In the case of a dispute between business and consumer, the Trustmark managing board of directors appoint the arbitrator who will review the dispute.<sup>54</sup> Furthermore, under some B2C ODR schemes such as WebAssured, online businesses pay the dispute resolution costs.<sup>55</sup> The payment is taken either in the form of an annual membership fee paid for the subscription to the Trustmark as is the case for WebAssured or on a case by case basis.<sup>56</sup>

It is true that the fees paid by the business facilitate consumer access to the online arbitration services. However, if the online arbitration provider is administratively

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<sup>52</sup>Colin Rule, *Online Dispute Resolution for Business*, (Jossey-Bass, San Francisco, 2002), p.106.

<sup>53</sup> Benjamin G. Davis, "Disciplining ODR Prototypes: True Trust through True Independence", Proceedings of the UNECE Forum on ODR 2003, p.9, available at: <<http://www.odr.info/unece2003>>, accessed on 12/12/2007.

<sup>54</sup>Ibid

<sup>55</sup>Webassured is Trustmark and B2C online dispute resolution is offered under it. Available at:< [www.WebAssured.com](http://www.WebAssured.com) > accessed on 12/11/2007.

<sup>56</sup>Hörnle, (business-to-consumer), note 2 supra.

and financially dependent on the business, it is difficult to convince the consumer that the online arbitration provider is impartial. Therefore, rules that guarantee the independence of the online arbitration provider should be in place. Regarding the costs of the online arbitral process, there are many solutions that can be relied on to offer the consumer free or low-cost online arbitration services without sacrificing the independence of the online arbitration provider. One possible solution is that arbitral tribunal awards the costs for the winning party.<sup>57</sup> However, such a solution means that the consumer has to pay in order to start the arbitral process. Consumer claims are usually low-value. This means that if the costs of the online arbitral process are too high, the consumer will not try to arbitrate the dispute. What is more, the high costs of the online arbitration process can lead to the invalidation of the arbitration clause on the basis of unconscionability. This is what the 11th Circuit Court of Appeals has held in the case of *Green Tree Financial Corp. et al v Randolph Larketta*.<sup>58</sup> Therefore, it is safe to say that this solution is not effective. Balancing the cost-effectiveness of the online arbitral process and the independence of the online arbitration providers requires subsidising the online arbitration services by a third party who is outside the dispute. This requires financial support by the government. The online business sector can also support consumer protection organisations. After that consumer protection organisations can help consumers to cover the online arbitration costs.

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<sup>57</sup>Witt, note 23 supra, p.455.

<sup>58</sup>178 F3d 1149 (11<sup>th</sup> Cir. 2000)



## 2.2 “Equal Voice in the Selection” of the Arbitrator

Apparent impartiality of the arbitral tribunal requires that both parties “have equal voice in the selection” of the arbitrator.<sup>59</sup> Arbitration laws allow the parties to choose the arbitrators that will review the dispute. §16(1) of the English Arbitration Act 1996 states that “the parties are free to agree on the procedure for appointing the arbitrators, including the procedure for appointing any chairman or umpire.”<sup>60</sup> In the same vein, §5 of the FAA states that “If in the agreement provision be made for a method of naming or appointing an arbitrator or arbitrators or an umpire, such method shall be followed.”<sup>61</sup> Both laws provide that parties may agree on a procedure for appointing an arbitrator. One possible procedure is that the parties themselves appoint the arbitrator. With some degree of difference, most institutional international arbitration rules also give the parties the right to determine the arbitrator by agreement. The London Court of International Arbitration (hereinafter LCIA) allows the parties to appoint the arbitrator subject to its confirmation. Article 7(1) of the LCIA Arbitration Rules of 1998 states that:

“If the parties have agreed that any arbitrator is to be appointed by one or more of them or by any third person, that agreement shall be treated as an agreement to nominate an arbitrator for all purposes...The LCIA Court may refuse to appoint any such nominee if it determines that he is not suitable or independent or impartial.”<sup>62</sup>

The International Chamber of Commerce (hereinafter the ICC) also allows the parties to appoint the arbitrator subject to its confirmation. Article 9(2) of ICC

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<sup>59</sup>Ibid

<sup>60</sup>§16(1), English Arbitration Act 1996

<sup>61</sup>§5, US Federal Arbitration Act 1925.

<sup>62</sup>Article 7(1), Arbitration Rule of the London Court of International Arbitration of 1998.

Arbitration Rules of 1998 states that “the Secretary General may confirm as co-arbitrators, sole arbitrators and chairmen of Arbitral Tribunals persons nominated by the parties or pursuant to their particular agreements”.<sup>63</sup> In contrast, the American Arbitration Association avoids the interference in the parties’ agreement on the arbitrator. Article 6(2) of the International Dispute Resolution Procedures of the American Arbitration Association states that:

“The parties may mutually designate arbitrators, with or without the assistance of the administrator. When such designations are made, the parties shall notify the administrator so that notice of the appointment can be communicated to the arbitrators, together with a copy of these rules.”<sup>64</sup>

The parties’ choice of the arbitrator can take place before the dispute occurs.<sup>65</sup> This means that the arbitrator who will review any future disputes can be named in the arbitration clause.<sup>66</sup> Online B2C e-commerce transactions are concluded via adhesion contract. This means that consumers cannot negotiate the terms of the contract.<sup>67</sup> Therefore, the business can determine the arbitrator that will review the dispute in the arbitration clause that is included in the e-commerce contract.<sup>68</sup> In other words, the business can name the arbitrator of any future dispute with the consumer before the dispute occurs. If the arbitrator is solely appointed by the business, the consumer may doubt the impartiality of the arbitrator. This is because the consumer will take into consideration that the arbitrator is concerned with

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<sup>63</sup> Article 9(2), Arbitration Rules of the International Chamber of Commerce of 1998.

<sup>64</sup> Article 6(2), International Dispute Resolution Procedures of the American Arbitration Association. Available at: < [http://www.adr.org/sp.asp?id=28144#Appt\\_of\\_Arbs](http://www.adr.org/sp.asp?id=28144#Appt_of_Arbs)>, accessed on 12/12/2007.

<sup>65</sup> Redfern and Hunter, note 20 supra, p.196.

<sup>66</sup> Ibid

<sup>67</sup> Cristina Coteanu, *Cyber Consumer Law and Unfair Trading practices*, (Ashgate Publishing Limited, London, 2005), p.99, 100.

<sup>68</sup> Llewellyn Joseph Gibbons, “Rusticum Judicium?: Private “Courts” Enforcing Private Law and Public Rights: Regulating Virtual Arbitration in Cyberspace”, (1998) 24 Ohio N.U. L. Rev. 769, 791. (hereinafter Rusticum Judicium).

impressing the business in order to receive future referral from that business. Business is a repeat-player.<sup>69</sup> Business concludes thousands if not millions of transactions with consumers and such transactions are likely to produce many disputes. The consumer is a one-shot player because he concludes few transactions.<sup>70</sup>

One might say that there is no need to adopt rules that grant the consumer an equal voice in selecting the arbitrator. This is because whenever the arbitrator has been frequently chosen by the business, the consumer can rely on the issue of repeat-player to challenge the arbitrator's impartiality before the Court of law. However, it is difficult to prove that the repeat-player represents either actual or apparent bias on the part of the arbitrator.

In respect of actual bias, this requires more than frequency in choosing the same arbitrator by the business. It requires inspecting the "subjective state-of-mind of the arbitrator" to see whether the arbitrator is prejudiced or partial. In the case of *Locabail (UK) Ltd v Bayfield Properties Ltd and Another*,<sup>71</sup> the English Court of Appeal held that:

"[T]he rule with regard to actual bias is recognised as being on its own insufficient to protect against judicial bias since it is undesirable that the decision-maker's state of mind should be investigated..."<sup>72</sup>

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<sup>69</sup>David Schwartz, "Enforcing Small Print to Protect Big Business: Employee and Consumer Rights Claims in an Age of Compelled Arbitration", (1997) WISC. L. REV. 33, 61.

<sup>70</sup>Carrie Menkel-Meadow, "Do the "Haves" Come out Ahead in Alternative Judicial Systems?: Repeat Players in ADR", (1999-2000) 15 Ohio St. J. on Disp. Resol. 19, 52, 53.

<sup>71</sup>[2000] QB 451, CA.

<sup>72</sup>Ibid, p.461.

Proving actual bias requires knowing all the factors that might affect the arbitrator's mind. Some of these factors might be irrelevant to the dispute such as the colour or race of the disputants. The impact of such factors can only be known if one knows what the arbitrator is thinking about or the arbitrator acknowledges that he is biased. The former is impossible and the latter is extremely unlikely to happen and this is what Kaufman, Circuit Judge affirmed in the case of *Morelite Construction Corp. v N.Y.C. District Council Carpenters' Benefit Funds*,<sup>73</sup> he explained that:

“Bias is always difficult, and indeed often impossible, to “prove.” Unless an arbitrator publicly announces his partiality, or is overheard in a moment of private admission, it is difficult to imagine how ‘proof’ would be obtained.”<sup>74</sup>

In respect of apparent bias, apparent bias is the type of bias that can be deduced from the “external relations, statements, or actions” of the arbitrator.<sup>75</sup> In England, Courts no longer determine the existence of apparent bias from the viewpoint of a reasonable man as held in the case of *R v Gough*.<sup>76</sup> The new test that is used by English Courts to determine whether there is an apparent bias is the ‘independent and informed observer’.<sup>77</sup> According to this test the court will explore all the different facts connected to the allegation of bias. After that the court will determine if these facts make a ‘fair-minded member of the public’ suspect that ‘a fair trial was not possible’.<sup>78</sup> In the US, apparent bias exists if “a reasonable person would have to

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<sup>73</sup>748 F.2d 79 (2d Cir. 1984)

<sup>74</sup>Ibid, p.84

<sup>75</sup>Gary B. Born, *International Commercial Arbitration*, (2<sup>nd</sup> edn, kluwer Law International, The Hague, 2001) p.874.

<sup>76</sup>[1993] AC 646, 670.

<sup>77</sup>Tweedle and Tweedle, note 40 supra, p.641.

<sup>78</sup>Ibid.

conclude that an arbitrator was partial to one party to the arbitration.”<sup>79</sup> A very important principle that has been developed under this test is the automatic disqualification of the arbitrator when he has a financial interest in the outcome of the arbitral process.<sup>80</sup> “Repeat economic contacts” that have been used to request automatic disqualification of the arbitrator can be classified into the following categories:

“(1) Ongoing business relationships between an arbitrator and a party; (2) past business relationships between an arbitrator and a party; (3) ongoing business relationships between an arbitrator and a party’s counsel; (4) past business relationships between an arbitrator and a party’s counsel; and (5) relationships with a witness for one party.”<sup>81</sup>

The frequency in appointing a particular arbitrator by the same business, which is usually called repeat-player, represents a financial interest to the arbitrator.<sup>82</sup> It is more similar to the first category which is the ongoing business relationships between the arbitrator and a party than any other category mentioned in the quoted paragraph.<sup>83</sup> However, the arbitrator’s ongoing financial interest will only disqualify him from hearing the dispute if it is direct and substantial. In the case of *Locabail*

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<sup>79</sup>748 F.2d 79, 84 (2d Cir. 1984). Michael I. Kaplan, “Solving the Pitfalls of Impartiality When Arbitrating in China: How the Lessons of the Soviet Union and Iran Can Provide Solutions to Western Parties Arbitrating in China”, (2005-2006) 110 Penn St. L. Rev. 769, 773. What should be mentioned here is that under English Law the same test of bias applies on arbitrator and judges. This is what the Court held in the case of *R -v- Gough*, [1993] AC 646. There are authorities under the US Federal Law explaining that the test that applies to determine whether the arbitrator is biased is similar to the one that applies to judges. For examples in the case of arbitrator *Sanko S.S. Co., Ltd. -v- Cook Industries, Inc.*, the court explained that the court scrutiny on arbitrator bias should not be less than judges. 495 F.2d 1260, 1263.

<sup>80</sup>*AT & T Corporation And Another v Saudi Cable Co*, [2000] 2 Lloyd's Rep. 127, 127.

<sup>81</sup>Lisa B. Bingham, “On Repeat Players, Adhesive Contracts, and the Use of Statistics in Judicial Review of Employment Arbitration Awards”, (1997-1998) 29 McGeorge. L. Rev. 223, 248.

<sup>82</sup>*Ibid*

<sup>83</sup>*Ibid*

(*U.K.) Ltd. v Bayfield Properties Ltd. and Another*,<sup>84</sup> the English Court of Appeal held that:

“...where a judge had a direct personal interest, which was other than de minimis, in the outcome of proceedings bias was presumed to exist and he was automatically disqualified from hearing or continuing to hear the case and any judgment he had given would be set aside...”<sup>85</sup>

The case of *Locabail* makes it clear that the personal interest of the judge, which also applies to the arbitrator, should be direct and ‘substantial’.<sup>86</sup> Proving the substantiality of the economic interest will depend on the value of the dispute and the frequency in choosing the arbitral institution and the arbitrator by the business.<sup>87</sup> However, proving the directness of the arbitrator’s financial interest in the outcome of a dispute on the basis of repeat-player seems to be more problematic. In her article on employment arbitration which resembles online B2C arbitration, Bingham argued that a repeat-player can be classified as having a direct financial interest to the arbitrator, especially when the employer whose role resembles the role of the business in consumer arbitration has the power to nominate the arbitrator. She asserted that:

“Certain characteristics of employment arbitration rules might render an arbitrator’s economic interest more direct. In particular, where the employer has effective control over arbitrator selection, one can argue that the arbitrator’s economic interest in repeat business from that employer is a direct interest because there is a high probability that the employer can select the arbitrator in the future. An employer may have effective control over arbitration selection in several contexts. The employer may unilaterally

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<sup>84</sup>[2000] QB 451, CA.

<sup>85</sup>*Ibid*, p.452.

<sup>86</sup>John R. Allison, “A Process Value Analysis of Decision-Maker Bias: The Case of Economic Conflicts of Interest”, (1995) 32 *Amer. Bus. L. J.*481, 514-517.

<sup>87</sup>*Ibid*

designate a single permanent umpire or a small permanent panel. The employer may name a single, small third party arbitration service provider with a very small list of neutrals. The employer may have effective control because a person purporting to speak on behalf of both employer and employee requests a given arbitrator by name from a large roster, and that arbitrator is in fact appointed to hear the case whenever requested.”<sup>88</sup>

Bingham’s observation means that an arbitrator’s financial interest in repeat-player is direct because a business can follow different means to solely determine the arbitrator. There is no doubt that the business ability to solely appoint the arbitrator encourages the arbitrator to impress the business. The arbitrator can only guarantee a good income, if the business keeps choosing him to resolve its disputes with online consumers. However, the arbitrator’s financial interest in repeat-player is not direct. This is because any personal interest for the arbitrator in the outcome of the arbitral process will only be considered direct if the dispute itself concerns the arbitrator. In other words, the subject matter of the dispute should be connected to the arbitrator in a direct way. An illustration of that can be seen in the case of *AT & T Corporation And Another v Saudi Cable Co.*<sup>89</sup> In this case Mr. Fortier was a non-executive director of Nortel which is one of seven companies that placed bids to expand the telecommunication network in Saudi Arabia. While Nortel lost the bidding its competitor AT & T won. However, there was a condition in the agreement that the cable must be bought from Saudi Cable Co. (SCC). A pre-bid agreement regarding the cable was concluded between AT & T and SCC.<sup>90</sup> The pre-bid agreement provided that the parties shall negotiate, in good faith, a mutually satisfactory agreement. It also contained an arbitration clause that refers any future dispute to

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<sup>88</sup>Bingham, note 81 supra, p.254.

<sup>89</sup>[2000] 2 Lloyd's Rep. 127

<sup>90</sup>Ibid

arbitration before the ICC. The negotiations were fruitless and the parties moved to arbitrate the dispute. Each party appointed an arbitrator and the two arbitrators appointed Mr. Fortier as a chairman of the tribunal.<sup>91</sup> AT & T applied to the Court to vacate the tribunal awards on the basis of bias as Mr. Fortier was a non-executive director of Nortel which was a competitor of AT & T and had lost the bid. The Court refused to vacate the arbitration award because Nortel was not a party to the arbitration and therefore Mr. Fortier had no direct personal interest in its outcome.<sup>92</sup>

One might say that the repeat-player in arbitration should be considered an appearance of bias as it is similar to other types of employment relationships between one of the parties and the arbitrator. Bingham adopted this opinion when she observed that:

“The arbitrator can look to one party in employment arbitration for referral of future business: the employer... particularly if ... the employer pays the arbitrator’s fee. In this situation, it is hard to find a reasoned basis to separate employment as an arbitrator from employment as a consultant, as legal counsel, or as an expert witness. Many commercial and employment arbitrators perform this service as a means of supplementing their professional income as lawyers.”<sup>93</sup>

Bingham considered the relationship between the arbitrator and the parties as an employment contract similar to the relationship between the parties and their legal consultant. The parties can employ a legal consultant. However, the relationship between the parties and the arbitrator cannot be classified as an employment contract. It is true that the arbitrator is appointed by an arbitral institution that has been chosen

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<sup>91</sup>Ibid.

<sup>92</sup>[2000] 2 Lloyd's Rep. 127, 134.

<sup>93</sup>Bingham, note 81 supra, p.252.



by the parties, however, the arbitrator is not an employee that is working for the parties. Unlike employees, arbitrators cannot be fired directly by either the parties. The arbitrator's removal has to be made either through the Court or the arbitral institution and the application for removal should be supported by a particular ground that the Court or the arbitral institution might accept or not.<sup>94</sup> It is true that the parties' agreement is the source of the jurisdiction of the arbitrator to review the dispute. However, the arbitration agreement is not the only source that governs the arbitrator's rights and obligation. Arbitration law, regardless of whether they are national or international, places the arbitrator under an obligation to act judicially.<sup>95</sup> This makes the relationship between the arbitrator and the parties have less resemblance to an employment contract. It also distinguishes the role of the arbitrator from the role of an expert witness who does not have to act as judicially as an arbitrator.<sup>96</sup>

Consequently, rules that grant the consumer and the business an equal voice in selecting the arbitrator should be in place. One possible solution is awarding exclusive authority to appoint the arbitrator to the arbitral institution. This method is applied under the Chartered Institute of Arbitrator's Arbitration Scheme for Travel Industry.<sup>97</sup> Article 2(11) of the rules of this scheme states that:

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<sup>94</sup>Redfern and Hunter, note 20 supra, p.218, 219.

<sup>95</sup>Sir Michael J. Mustill and Stewart G. Boyd, *The Law and Practice of Commercial Arbitration in England*, (2<sup>nd</sup> edn, Butterworths, London, 1989), p.219-223. Acting judicially requires from the arbitrator to give each party the chance to present his case and to remain impartial.

<sup>96</sup>Ibid

<sup>97</sup>Chartered Institute of Arbitrator's Arbitration Scheme for Travel Industry, available at: < <http://www.idrs.ltd.uk/ABTA/home.asp> >, accessed on 15/12/2007.

“The Arbitrators selected for appointment are Chartered Arbitrators and existing members of the Chartered Institute of Arbitrators. All appointments are within the Administrator’s exclusive and unfettered control.”<sup>98</sup>

It is also applied by the Virtual Magistrate Online Arbitration Program. Virtual Magistrate Arbitration Rules provide that the administrator of the program will appoint the arbitrator.<sup>99</sup> However, this solution is encountered by the fact that the business can be solely responsible for the choice of the arbitral institution which will choose the arbitrator. This may also affect the perceived fairness of the online arbitral process. This is because such a situation opens the door for the business to solely choose the arbitrator in an indirect way. The business will choose a particular arbitral institution because a particular group of arbitrators works for that institution. A good solution might be that the arbitrator should be appointed by agreement between the business and the consumer that is concluded after the dispute has arisen. This solution is recommended by the Consumer Due Process Protocol of the American Arbitration Association.<sup>100</sup> Principle 3(d) of the named protocol states that both business and consumer “should have an equal voice in the selection of Neutrals in connection with a specific dispute.”<sup>101</sup> The parties’ agreement on the arbitrator can be achieved by direct negotiation between them. Alternatively, the arbitral

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<sup>98</sup> Arbitration Rules of the Chartered Institute of Arbitrator’s Scheme for the Travel Industry, available at:

< <http://www.idrs.ltd.uk/ABTA/Rules.asp> >, accessed on 15/12/2007

<sup>99</sup> Rules of the Virtual Magistrate Online Arbitration Program, available at

< <http://www.vmag.org/docs/rules.html> >, accessed on 15/12/2007.

<sup>100</sup> Consumer Due Process Protocol.

<sup>101</sup> Ibid, Principle 3(d).

institution can provide them with a list of arbitrators and each party can respond and tell the arbitral institution which of the arbitrators he considers acceptable.<sup>102</sup>

In case the parties fail to reach a post-dispute agreement on the arbitrator, the arbitral tribunal should not be allowed to choose the arbitrator directly. Instead, the arbitral institution should prepare a list of arbitrators and then choose an arbitrator from the list in a random way<sup>103</sup> by applying a sweepstake mechanism. It is true that the latter method is not as effective as the parties' agreement in promoting the consumer's perception of fairness. However, it is still better than giving the exclusive authority to appoint the arbitrator to the arbitral institution that is chosen by the business.

## **2.3 Publication of the Arbitral Award**

Publication of the arbitral award encourages the consumer to view the arbitrator as impartial. This is because the consumer takes into consideration that the arbitrator will try to act impartially in order to avoid criticism by the public. In fact, publication of the arbitral award forms an important means to monitor the impartiality of the arbitrator. Hörnle observed that "unless there is sufficient transparency through publication of results it is impossible to check the quality and impartiality of dispute resolution".<sup>104</sup> However, the arbitral award cannot be published if the arbitral tribunal and the arbitration provider are obliged to keep the arbitral award confidential.<sup>105</sup> Neither the English Arbitration Act 1996 nor the US FAA includes any express provisions imposing a duty to keep the arbitral award

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<sup>102</sup>Redfern and Hunter, note 20 supra, p.195

<sup>103</sup>Hörnle, (Business-to-Consumer), note 2 supra.

<sup>104</sup>Ibid

<sup>105</sup>Tweedle and Tweedle, note 40 supra, p.353.

confidential. NYC also does not include any provision imposing a duty of confidentiality.<sup>106</sup> Nevertheless, the arbitral tribunal and the arbitration provider's duty to keep the arbitral award confidential can arise from three sources and they are common law, the parties' agreement and institutional arbitration rules. The best example for duty of confidentiality that arises from common law can be seen under the English Law. In the case of *Ali Shipping v Shipyard Trogir*,<sup>107</sup> the parties arbitrated a breach of contract dispute. At the end of the arbitral proceedings an arbitral award was made in *Ali*'s favor. Afterwards, *Shipyard Trogir* arbitrated a dispute with Lavender Shipping, Leeward Shipping, and Leman Navigation. These companies are all sister companies of *Ali*. *Shipyard Trogir* tried to reproduce the arbitration award made in arbitration with *Ali*, as well as other documents that were produced in that arbitration. *Shipyard Trogir* alleged that the award and the documents from the previous arbitration with *Ali* were essential. *Ali Shipping* resorted to the Court to stop the production of the award and the documents on the basis that they were confidential. The Court issued an injunction stopping the production. *Shipyard Trogir* appealed. The Court of Appeal had to decide whether to allow *Shipyard Trogir* to produce the award and the documents from the first arbitration. Five facts made this case complicated. First, *Ali*, Lavender, Leeward and Leman were all companies that were 100 percent owned by the same parent company which was Greenwich Holdings. Second, *Ali Shipping* and its sister companies all shared the same lawyer. Third, all the ship-building contracts that

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<sup>106</sup>The reason is that the main aim of the NYC is to facilitate the enforcement of the arbitral award. It is not intended to regulate the arbitral process as in the case of national arbitration laws as the English Arbitration Act 1996 or the FAA.

<sup>107</sup>[1998] 1 Lloyd's Rep. 643.

were the subject of the dispute had been negotiated by the same people. Fourth, the sister companies had the same personnel. Fifth, *Shipyards Trogir* tried to reproduce the award and the documents from the arbitration with *Ali Shipping* to *Ali's* own sister companies and not to strangers. Despite these facts, the Court of Appeal held that *Shipyards Trogir* could not produce the award and the documents from the arbitration with *Ali*. This is because the documents and the award were protected by an obligation of confidentiality. The Court observed that the confidentiality of the arbitral awards and the documents is not dependent on the private nature of the material in question, nor is it dependent on custom, usage or business efficacy. Instead, confidentiality attaches to arbitration agreements as a matter of law. Potter LJ, observed that:

“It seems to me that, in holding as a matter of principle that the obligation of confidentiality (whatever its precise limits) arises as an essential corollary of the privacy of arbitration proceedings, the Court is propounding a term which arises ‘as the nature of the contract itself implicitly requires’ . . . a clear distinction is to be drawn between the search for an implied term necessary to give business efficacy to a particular contract and the search, based on wider considerations, for a term which the law will necessarily imply as a necessary incident of a definable category of contractual relationship. In my view an arbitration clause is a good example of the latter type of implied term.”<sup>108</sup>

Potter LJ, also explained that there were exceptions to this general duty of confidentiality. He observed that:

“English law has recognised the following exceptions to the broad rule of confidentiality: (i) consent i.e. where disclosure is made with the express or implied consent of the party who originally produced the material; (ii) order of the Court, an obvious example of which is an order for disclosure of documents generated by an arbitration for the purposes of a later Court action; (iii) leave of the Court. It is the practical scope of this exception i.e. the

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<sup>108</sup>[1998] 1 Lloyd's Rep. 643, 651.

grounds on which such leave will be granted, which gives rise to difficulty. However, on the analogy of the implied obligation of secrecy between banker and customer, leave will be given in respect of (iv) disclosure when, and to the extent to which, it is reasonably necessary for the protection of the legitimate interests of an arbitrating party. In this context, that means reasonably necessary for the establishment or protection of an arbitrating party's legal rights viz-à-viz a third party in order to found a cause of action against that third party or to defend a claim (or counterclaim) brought by the third party.”<sup>109</sup>

Potter LJ's, statements mean that under English Law, there is a general duty to keep the arbitral award confidential. This means that publication of the arbitral award is not allowed under English law. What is more, publishing the arbitral award is either invisible or not possible under any of the limited exceptions to the duty of confidentiality that Potter LJ spelled out. Potter LJ explained that parties can agree to exclude the confidentiality by agreement. However, achieving publication of the arbitral award is not visible under this exception. One of the factors that encourage business to rely on arbitration is the fact that the arbitral proceedings and arbitral awards will be kept confidential.<sup>110</sup> The business wants to protect its trade secrets and the way it deals with its customers. Therefore, the business is unlikely to accept the publication of the arbitral award by agreement. The second exception is the order of the Court to produce the award and documents in later Court proceedings. This is usually called disclosure in the interests of justice.<sup>111</sup> The publication of the arbitral award is not possible under this exception because it is only concerned with producing documents and evidence from previous arbitration to achieve justice in later court proceedings. In other words, it is designed to make sure that judicial

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<sup>109</sup>Ibid

<sup>110</sup>Tweedle and Tweedle, note 40 supra.

<sup>111</sup>Ibid, p.358

decisions are “reached upon the basis of the truthful or accurate evidence”.<sup>112</sup> The third exception is the Court’s leave to disclosure when there is a reasonable necessity to protect the legitimate interests of the parties to the arbitration. Publication of the arbitral award is not possible under this exception. This is because this is designed to allow a party to the arbitral process to use the arbitral award to protect this party’s rights against a third party. It is also possible to disclose the arbitral award in actions for enforcement or annulment of the award.

In the case of *United States v Panhandle Eastern Corp*,<sup>113</sup> the United States government tried to reproduce documents connected to earlier arbitral proceedings that were conducted according to the ICC arbitration rules in Geneva. The Court ruled that as the arbitration agreement and ICC arbitration rules did not provide for the confidentiality of the proceedings, the government could obtain access to the documents. This means there is no general principle of confidentiality of international arbitration proceedings and awards under the US Federal common law. However, it is possible for the parties to agree on making the arbitral proceedings and the arbitral award confidential. As mentioned earlier, online B2C contracts are concluded via adhesion contracts of which the consumer cannot negotiate terms. This means that the business can prevent the publication of the arbitral award. This can be done by including a term in the arbitration clause which states that the arbitral process and the arbitral award are confidential. Another way of making the arbitral award confidential by agreement is referring the dispute to a particular arbitral

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<sup>112</sup>Ibid

<sup>113</sup>118 F.R.D. 346 (D. Del. 1998).

institution. The reference to a particular arbitral institution usually incorporates the arbitration rules of that institution. As Witt explained “confidentiality is generally the rule promulgated by most of the large international arbitration institutions.” The illustration for this can be seen in the LCIA Arbitration Rules of 1998 which expressly state that the arbitral proceedings are confidential and the arbitral award are not subject to publication without the authorisation of the parties. Article 30(1) and (3) of the LCIA Arbitration Rules states that:

“30.1 Unless the parties expressly agree in writing to the contrary, the parties undertake as a general principle to keep confidential all awards in their arbitration, together with all materials in the proceedings created for the purpose of the arbitration and all other documents produced by another party in the proceedings not otherwise in the public domain - save and to the extent that disclosure may be required of a party by legal duty, to protect or pursue a legal right or to enforce or challenge an award in bona fide legal proceedings before a state court or other judicial authority.

30.3 The LCIA Court does not publish any award or any part of an award without the prior written consent of all parties and the Arbitral Tribunal.”<sup>114</sup>

Article 34 of the International Arbitration Rules of the American Arbitration Association states that “unless otherwise agreed by the parties or required by applicable law, the members of the tribunal and the administrator shall keep confidential all matters relating to the arbitration or the award.”<sup>115</sup>

Consequently, a rule that provides for the publication of the arbitral award should be in place. This is in order to encourage the consumer to see the arbitral tribunal as impartial. Interestingly, ICANN Rules for Uniform Domain Name Dispute Resolution provides for the publication of the decisions that are taken by dispute

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<sup>114</sup> Art. 30, LCIA Arbitration Rules 1998.

<sup>115</sup> Art. 34, International Arbitration Rules of the American Arbitration Association.



resolution panels in respect to domain name disputes. Article 16(b) ICANN Rules for Uniform Domain Name Dispute Resolution Policy states that “except if the Panel determines otherwise, the provider shall publish the full decision and the date of its implementation on a publicly accessible web site.”<sup>116</sup> However, in the context of the online B2C arbitration, a rule that is similar to Article 16(b) of the ICANN Rules will not encourage the consumer to expect that the arbitrator will be impartial. This is because it places the decision of whether to publish the award in the hands of the arbitrator. Encouraging the consumer to see that the arbitrator will be impartial requires a rule that always places the online arbitration provider under a duty to publish the arbitral award. The publication of arbitral awards will also help in developing e-commerce customary law.<sup>117</sup> B2C e-commerce contracts are concluded via adhesion contracts. This means that many consumers might be subjected to the same contract terms. Therefore, although arbitrators are not obliged to follow previous arbitral decisions, published and reasoned arbitral awards will guide the arbitrator in making a decision in respect of matters that have been previously reviewed in past arbitral awards.<sup>118</sup> What is more, publication of the arbitral award will help to reduce the impact of the repeat-player issue in respect of “access inequality”.<sup>119</sup>

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<sup>116</sup> Art.16 (b), ICANN Rules for Uniform Domain Name Resolution Policy. ICANN is the Internet Corporation for Assigned Names and Numbers. The Rules are available at: <http://www.icann.org/dndr/udrp/uniform-rules.htm> accessed on 12/12/2007.

<sup>117</sup> Llewellyn Joseph Gibbons, “Private Law, Public “Justice”: Another Look at Privacy, Arbitration, and Global E-commerce”, (2000) 15 Ohio St. J. on Disp. Resol.769, 789 (hereinafter Private Law).

<sup>118</sup> Ibid, p.786

<sup>119</sup> Ibid

As business is likely to resort to online arbitration more than the consumer, the business will be able to know how the arbitral tribunal will interpret the contract and apply the law,<sup>120</sup> whereas, the consumer is a “one-shot player”, therefore if the arbitral award is not published, the consumer or his representatives will have no chance to know how the contract will be interpreted and how the law will be applied.<sup>121</sup>

### **3. Judicial Review on the Basis of the Violation of Due Process**

As explained above, perceived fairness of the arbitral procedures is important to raise consumer confidence in the online arbitral process. The consumer may not perceive fairness in the online arbitral procedures if the arbitral award cannot be invalidated despite the violation of due process. This is because the consumer may fear that the arbitrator will not pay enough attention to “act fairly”. However, under the English Arbitration Act 1996, an arbitral award may only be vacated on the basis of the violation of procedural unfairness if the violation causes a significant difference in the outcome of the arbitral process. §68 of the English Arbitration 1996 allows the challenging of the arbitral award on the violation of §33 which embeds the principle of due process. §33 states that:

“(1) The tribunal shall -

(a) act fairly and impartially as between the parties, giving each party a reasonable opportunity of putting his case and dealing with that of his opponent, and

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<sup>120</sup>Hörnle, (business-to-consumer), note 2 supra.

<sup>121</sup>Ibid.

(b) adopt procedures suitable to the circumstances of the particular case, avoiding unnecessary delay or expense, so as to provide a fair means for the resolution of the matters falling to be determined.”<sup>122</sup>

However, the challenge will only be accepted if the violation causes “substantial injustice” to the applicant. An arbitrator’s bias is one type of the different irregularities that violate §33 of the English Arbitration Act 1996. English Courts have held that the arbitrator’s bias is sufficient to satisfy the ‘substantial injustice’ test under §68 of the English Arbitration Act 1996. In the case of *ASM Shipping Ltd of India v TTMI Ltd of England*,<sup>123</sup> Mr Justice Morison asserted that:

“If the properly informed independent observer concluded that there was a real possibility of bias, then that was a species of serious irregularity which had caused substantial injustice to the applicant. There was no need to inquire whether substantial injustice had been caused: there could be no more serious or substantial injustice than having a tribunal which was not, ex hypothesi, impartial, determine parties' rights. The right to a fair hearing by an impartial tribunal was fundamental.”<sup>124</sup>

In the case of *Norbrook Laboratories Ltd v Tank*,<sup>125</sup> the Court asserted that:

“where there was a sole arbitrator whose impartiality was shown to have been impaired to the effect that a fair minded and properly informed independent observer would perceive that there existed a real possibility of bias in any award already made, substantial injustice would normally be inferred and where an award had yet to be made substantial injustice would normally be anticipated.”<sup>126</sup>

Both cases explain that the existence of apparent bias is adequate to satisfy the ‘substantial injustice’ test and thereby the consumer will not be obliged by the arbitral award when the arbitrator is biased. As arbitrator’s bias is one type of

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<sup>122</sup> §33, English Arbitration Act 1996.

<sup>123</sup> [2006] 1 Lloyd's Rep. 375.

<sup>124</sup> Ibid, 376.

<sup>125</sup> [2006] 2 Lloyd's Rep. 485

<sup>126</sup> Ibid, p.486.

irregularity that violates §33 of the Arbitration Act 1996, one could say that by virtue of analogy other types of procedural irregularities that violate §33 will also directly satisfy the ‘substantial injustice’ test under §68. Therefore, the arbitral award will be vacated when the arbitral procedures are not fair. However, that is not true. The reason is that unlike the case of arbitrator’s bias, other procedural irregularities that violate §33 will not satisfy the “substantial injustice” test, unless the irregularity causes a “significant difference” in the outcome of the arbitral process.<sup>127</sup> The illustration for that can be seen in many decisions of the English Courts. In the case of *Aquator Shipping Ltd. v Kleimar N.V., (The 'Capricorn 1')*,<sup>128</sup> *Aquator* time-chartered its ship *Carpricon 1* to *Kleimar*. *Kleimar* subchartered the ship to Scanports. While the vessel was being loaded, the ship’s master noticed that there was ice on the cargo and he wrote this fact on the mate's receipt.<sup>129</sup> However, he did not record it on the bill of lading. This constituted a violation for clause 8 of the head charter party which places the master under an obligation to sign the bills of lading for cargo as presented in conformity with the mate's receipts. At the discharge port the cargo could only be discharged manually. This caused delay and extra costs.<sup>130</sup>

*Kleimar* claimed damages against Scanports and arbitrators were appointed. Alongside other arbitrators appointed by Scanports, Mr. Hamsher was appointed as an arbitrator by *Kleimar*. Scanports cross-claimed for damages because of the master's failure to issue a bill of lading in conformity with the mate’s receipt was a

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<sup>127</sup>Tweeddle and Tweeddle, note 40 supra, p.767.

<sup>128</sup>[1998] 2 Lloyd's Rep. 379

<sup>129</sup>Ibid

<sup>130</sup>Ibid

breach of contract by *Kleimar* and this had caused the delay. *Kleimar* claimed damages against *Aquator* in a separate arbitration on the basis that the master's failure to issue the bill of lading in conformity with the mate's receipt and requested any loss in the sums of money that it would receive from Scanports. Different arbitrators were appointed and *Kleimar* appointed Mr. Hamsher again in this arbitration. The arbitrator rendered "common reasons for award", dealing with both arbitrations at the same time and giving one set of reasons for both awards.<sup>131</sup> The arbitrators ruled for Scanports on the cross-claim in the arbitration against *Kleimar*. In the other arbitration, the arbitrators ruled for *Kleimar* on the claim for damages against *Aquator*. *Aquator* challenged the arbitral award on the basis that the reasoning used in the decision in the arbitration between *Aquator* and *Kleimar* had not arisen as an issue in that arbitration. It had been adopted from the arguments in the arbitration between *Kleimar* and Scanports, to which *Aquator* had not had an opportunity to respond. The Court held that:

"the course adopted by the arbitrators was procedurally defective; there had been no agreement to concurrent arbitrations; and the head charter disputes had not been referred to the same tribunal as the sub-charter disputes; even if they had been it was far too late to convert the procedure from two separate and insulated arbitrations into consolidated arbitrations; the only way to accomplish this was to obtain the consent of the parties to both arbitrations and this was never done... if it appeared to the Court that, even if the rules of natural justice had been adhered to, the arbitrators would be likely to have arrived at the same conclusion as they in fact did, there could be no justification in remitting the award, much less in setting it aside;"<sup>132</sup>

The Court explained that the procedures adopted by the arbitrator violated the principle of due process under §33 of the English Arbitration Act 1996. However,

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<sup>131</sup>[1998] 2 Lloyd's Rep. 379

<sup>132</sup>*Ibid*, 380.

since the outcome of the arbitral process will be the same, the arbitral award should not be vacated or remitted back to the tribunal. The focus on the significant difference appears very clear from the Courts holding in the case of *Egmatra AG v Marco Trading Corp.* In this case, Tuckey J explained that “substantial injustice” should not be understood as something little.<sup>133</sup> Similarly, in the case of *Groundshire Ltd v VHE Construction plc*,<sup>134</sup> Judge Bowsher explained that the word “substantial” should be interpreted as “essential”, or “of ample or considerable amount, quantity”. In the case of *JD Wetherspoon Plc v Jay Mar Estates.*,<sup>135</sup> the Court explained that the arbitrator’s reliance on his own experience to adjust the evaluation for a premises’ rent that is made by valuers does not constitute a procedural irregularity. Even if it constituted a procedural irregularity the award cannot be remitted back to the tribunal. This is because there will not be any significant difference in the result in the absence of that irregularity. Coulson J. observed that:

“I do not think that it could be fairly said that this arbitration had gone off the rails in any way. Even assuming an irregularity, the point arose in respect of an argument about (and an adjustment to) a rental figure on one comparable property, which was not the most relevant comparable for the reasons explained by the arbitrator. Furthermore, the evidence does not suggest that there was any further evidence available to JDW... which could or would have made any substantial difference to the result. During argument, Miss Taskis<sup>136</sup> properly accepted that it was difficult to say that, if the irregularity had not arisen, there would have been any significant difference to the result. It seems to me, therefore, that in the round the ‘substantial injustice’ test has not been made out in this case.”<sup>137</sup>

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<sup>133</sup>[1999] 1 Lloyd’s Rep 862.

<sup>134</sup>[2001] B.L.R 395

<sup>135</sup>[2007] EWHC 856 (TCC)

<sup>136</sup>Miss Taskis is the lawyer that appeared on behalf of Wetherspoon.

<sup>137</sup>[2007] EWHC 856 (TCC)

In contrast, under the FAA, a violation to due process requirement is sufficient to vacate an arbitral award. There is no need to show that the violation of fundamental fairness causes a significant difference in the outcome of the arbitral process. §10(a) of the FAA embeds the principle of due process of the arbitral process and it states that:

“a. In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration:

1. Where the award was procured by corruption, fraud, or undue means.
2. Where there was evident partiality or corruption in the arbitrators, or either of them.
3. Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced.”<sup>138</sup>

Every act or event that is classified as fraud, corruption,<sup>139</sup> bias or misconduct by the arbitrator will lead to the vacation of the arbitral award. This is what the US Federal Courts’ Judges have held when they dealt with §10(a) of the FAA. In the case of *Commonwealth Coatings Corp. v Continental Casualty Co.*,<sup>140</sup> the Supreme Court annulled an arbitral award because the “requirements of impartiality”<sup>141</sup> of arbitrators under FAA §10(a)(2) was not satisfied. The Court relied on one of the arbitrator’s failure to disclose his four-to-five year business relationship with

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<sup>138</sup>§ 10, Federal Arbitration Act 1925.

<sup>139</sup>Fraud and corruption are rarely relied on to vacate an arbitral award. This is because establishing fraud or corruption on the part of the arbitrator requires proving acts such as bribery and that is very difficult to prove. Born, note 74 supra, p.878.

<sup>140</sup>393 US 145 (1968)

<sup>141</sup>Ibid, p.146.

*Continental to Commonwealth*. Note that in *Commonwealth Coatings* there was no submission that the arbitrator was “guilty of fraud or bias in deciding this case.”<sup>142</sup> Rather, the only reason for annulling the arbitral award was the unrevealed business relationship with one of the parties. US Federal Courts dealing with §10(a) (3) did not consider every procedural mistake as misconduct by the arbitrator. In the case of *Fairchild & Co. v Richmond, Fredericksburg & Potomac RR Co.*,<sup>143</sup> Sirica, District Judge explained that:

“Arbitrators are charged with the duty of determining what evidence is relevant and what is irrelevant ... While they may err in their determination, every failure to receive relevant evidence does not constitute misconduct under the Act so as to require the vacation of the award. The error which would constitute misconduct so as to justify vacating an award must not simply be an error of law, but one which so affects the rights of a party that it may be said to deprive him of a fair hearing”.<sup>144</sup>

The Court’s statement in *Fairchild* shows that a procedural mistake will only be considered a misconduct if it deprives the applicant of a fair hearing. However, it shows that when there is a violation of due process, the arbitral award will be vacated. An illustration of this can be seen in the case of *Prudential Securities, Inc. v Dalton*.<sup>145</sup> In this case an arbitral award was vacated because the arbitrator refused to hear evidence that the court classified as “pertinent and material to the controversy”.<sup>146</sup>

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<sup>142</sup>Ibid, p.147.

<sup>143</sup>516 F.Supp. 1305 (D.D.C. 1981)

<sup>144</sup>Ibid, 1314.

<sup>145</sup>929 F.Supp. 1411 (N.D. Okla. 1996)

<sup>146</sup>Ibid, p. 1418.



Consequently, raising the consumer's perception of fairness in online arbitral procedures requires adopting rules that allow for invalidation of the arbitral award whenever the principle of due process is violated. §10(a) of the FAA can be a starting point for developing such a rule.

#### **4. Conclusion**

The consumer's perception of the fairness of the online arbitral procedure is necessary to ensure consumer confidence in the online arbitral process. Raising the consumer's perception of fairness of the online arbitral procedures can be achieved through convincing the consumer that he will have the chance to present his case and reply to the other parties' submissions. This can be done through granting the consumer the chance to obtain legal representation and introduce evidence. Apparent impartiality of the online arbitration provider and the arbitral tribunal is also important to raise the consumer's perception of the fairness of online arbitral procedures. Apparent impartiality can be ensured by guaranteeing the independence of the online arbitral provider, awarding both the business and the consumer an "equal voice in the selection" of the arbitrators and publication of the arbitral award. Eventually, effective judicial review on aspects of the violation of due process will help the consumer perceive fairness of online arbitral procedures. This is because the arbitrator will pay more attention to "act fairly". An effective judicial review is the one that leads to the invalidation of the arbitral award whenever the court decides that a violation of due process has occurred.

## **Chapter 8**

### **Conclusions and Recommendations**

In this study the present author has argued that the current legal framework of online cross-border B2C arbitration reduces the consumer confidence in the online arbitral process. Therefore, an international convention that imposes a new model of online cross-border B2C arbitration should be adopted in order to raise the consumer confidence in online arbitral process. In the first part of this chapter the present author will summarise the analysis which demonstrates that the current legal framework of cross-border online B2C arbitration reduces the consumer confidence in the online arbitral process. The second part includes recommendations for policy makers. It explains that raising the consumer confidence in online B2C arbitration requires a new model of online cross-border B2C arbitration. This model should be implemented through an international convention.

#### **1. The Current Legal Framework of Online Cross-Border B2C Arbitration Reduces the Consumer Confidence in the Online Arbitral Process**

The current legal framework of online cross-border B2C arbitration reduces the consumer confidence in the online arbitral process. The consumer knowledge about the existence of the arbitration clause in the B2C e-commerce contract is so important for his confidence in online arbitration. This is because if the consumer is surprised by the commitment to arbitrate after the occurrence of the dispute, he will feel that he has involuntarily been taken to arbitration. However, the third chapter of thesis demonstrated that under the current rules the business bears no obligation to

disclose the existence of the arbitration clause into the B2C e-commerce contract to the consumer. The English Arbitration Act 1996 treats any B2C arbitration clause as unfair if the value of the claim is £5000 or less. However, if the value of the claim is more than £5000 the validity of an arbitration clause will be governed by ordinary contract law rules. Under §2 of the FAA the validity of the arbitration clause will be governed by ordinary contract law rules. Under ordinary contract law, the consumer consent to the arbitration clause is measured according to the objective standard of consent. Objective standard of consent means that parties will be considered to have consented to the contract if they “appear to be in agreement”. Accepting the whole B2C e-commerce contract is sufficient to consider that the consumer consented to the arbitration clause even if he did not read or understand the contract. It is true that the consumer is under an obligation to read the contract. Nevertheless, consumers rarely read and understand the terms of the B2C e-commerce contract, including the arbitration clause. Unfairness and unconscionability rules do not oblige the business to notify the consumer about the existence of the arbitration clause. This is because the lack of specific notice of the arbitration clause alone does not render the arbitration clause unfair or unconscionable.

For the consumer to have confidence in online arbitration, the consumer should enjoy the protection that is awarded to him under the law of his country of domicile. However, chapter five demonstrated that under the current rules a choice of substantive law clause deprives the consumer of the protection that is awarded to him under the law of his country of domicile. Arbitrators are legally free from the duty to comply with mandatory rules that do not belong to the chosen law. The

arbitrator's discretion will not always lead to the application of the mandatory rules of the consumer domicile. The arbitrator derives his authority from the parties' agreement. In other words, he is only obliged by the choice of law clause. This is what the arbitral tribunal affirmed in the ICC Case No.6379 of 1990. Arbitral award can be vacated because of violation of public policy of the place of arbitration. The enforcement of the arbitral award can be refused if the arbitral award violates the public policy of the place of enforcement. Arbitrators have shown willingness to apply the mandatory rules of the place of arbitration to avoid vacation of the arbitral award because of violation of public policy. They have also shown willingness to apply the mandatory rules of the possible place of enforcement to avoid rejection of the enforcement of the arbitral award because of the same reason. Mandatory rules of consumer protection such as the Distance Selling Regulations 2000 come within the scope of public policy exception to the enforcement of the arbitral award under the NYC. However, the fear about the vacation of the arbitral award or the fear about the rejection of the enforcement of the arbitral award will not encourage the arbitrator to apply the mandatory rules of the consumer's country of domicile. The business usually inserts a clause that designates the country where its headquarters are located as the place of arbitration. This means that the mandatory rules of the consumer domicile are not the mandatory rules of the place of arbitration. This means that, the mandatory rules of the consumer domicile do not constitute a source of concern about the vacation of the arbitral award because of violation public policy of the place of arbitration. The same also applies on the mandatory rules of the possible place of enforcement of the arbitral award. This is because in most B2C e-

commerce disputes the consumer is the victim. This means that the consumer's country of domicile is not likely to be the possible place of enforcement of the online B2C arbitral award.

For the consumer to have confidence in online arbitration, the consumer should be able to litigate dispute related to online arbitration agreements and processes in the Courts of his country of domicile. However, imposing a foreign arbitral seat on the consumer means he cannot litigate disputes over the online arbitral process in the Courts of his country of domicile. One reason is the non-applicability of jurisdiction rules that provide the consumer the right to litigate international B2C e-commerce disputes in his domicile on arbitration. This situation is exemplified in the Brussels I Regulation. Another reason is that the consumer's right to litigate international disputes with foreign businesses in his domicile is not well-established under the law of his domicile. This situation is exemplified in §2A-106(2) of the UCC.

Another reason is that Unfairness rules, the unconscionability rules, cannot effectively guarantee the consumer the right to litigate disputes over online arbitration agreements and processes in his country of domicile. The high costs and inconvenience of litigation in the foreign forum are the main defences that the consumer can use to challenge a forum selection clause. However, if the two defences do not come with bad faith in the method of introducing the forum selection clause into the B2C e-commerce contract, the two defences cannot lead to the invalidation of the forum selection clause under Regulation 5 of the 1999 Regulations. The two defences also rarely lead to the invalidation of the forum

selection clause under the unconscionability rules. In the *Carnival* case, the US Supreme Court refused to consider the forum selection clause unconscionable. The Court explained that transacting with consumers from different jurisdictions makes the business subject to litigation in many forums. Therefore, the business has an interest in limiting the number of these forums. The US Supreme Court also explained that a choice of forum clause will allow the business to offer the consumer cheaper prices. The high cost of litigation in the foreign forum is insufficient to hold the choice of an arbitral seat clause unconscionable. This is because the consumer has to prove that he is financially incapable of litigating the dispute in the designated foreign forum. For the consumer to have confidence in online arbitration, the online arbitral procedures should appear to be fair. However, the seventh chapter demonstrated that many aspects related to the online arbitral procedures may prevent the consumer from perceiving fairness at these procedures. The business can deny the consumer the chance to obtain legal representation by inserting a clause stating that none of the parties can retain legal lawyers. The business can also insert a clause into the contract stating that only certain type of evidence can be introduced. The business can insert a clause into the B2C e-commerce contract that designates the arbitrator. This will discourage the consumer to view the arbitrator as an impartial third party who will act fairly. What also may destruct the consumer from perceiving fairness at the online arbitral procedures is that an arbitral award may only be vacated on the basis of the violation of procedural unfairness if the violation causes a significant difference in the outcome of the arbitral process. This situation is exemplified in §68 of the English Arbitration 1996.

## **2. Recommendations**

If a new paradigm of online B2C arbitration is going to be adopted in order to raise the consumer confidence in the online arbitral process, the paradigm must include the following rules. First, the paradigm must stipulate that the consumer will not be obliged by the arbitration clause unless his consent to the arbitration clause is knowing and intelligent. Adopting such a rule is so important. It is going to guarantee that the consumer is not involuntary taken to online arbitration. It will also eliminate the uncertainties about the enforcement of the online B2C arbitration clause that exist in the current enforcement regime. The enforcement of an online B2C arbitration clause is most likely to take place under the NYC. As demonstrated in chapter 4 of this study, Article II(2) of the NYC constitute a source of uncertainty for the consumer and the business about the enforceability of their online arbitration clause. Article II(2) states that an arbitration clause is in writing if it is included in a contract signed by the parties or in contract concluded via exchange of letters or telegrams. Article II(2) does not indicate that the Internet is one of the communication means that can be used to conclude legally recognized arbitration clauses. It is true that Article 20(1) of the E-communications Convention 2005 gives legal recognition to online arbitration clauses that are introduced to enforcement under the NYC. However, the E-communications Convention 2005 has not eliminated the legal uncertainty resulting from the question of whether an arbitration clause in an online B2C contract satisfies the writing requirement under Article II(2) of the NYC. This is because the E-communications Convention 2005 does not apply on B2C contracts. Expanding the term ‘Telegram’ in Article II(2) to cover the

Internet or reliance on the most favourable law provision under Article VII(1) of the NYC does not help to effectively eliminate this legal uncertainty. This is because both solutions are subject to different interpretations by the courts of the state-signatories to the NYC.

Procuring the business consent to the online arbitration through an online B2C arbitration clause is so important for the consumer. This is because in most B2C e-commerce contracts the business receives the payment before the performance of the e-commerce contract. Therefore, it is difficult to obtain the business consent to arbitrate after the occurrence of the dispute. However, the enforcement of an arbitration clause under the NYC may be refused if the arbitration clause violates the public policy of the enforcing state. It is true that public policy exception to enforcement of arbitration clause under the NYC has been narrowed to mean international public policy of the forum and truly international public policy. However, mandatory rules that prohibit or restrict arbitration clauses in B2C contracts come within the meaning of international public policy of the forum. This makes the business uncertain whether the online B2C arbitration clause will be enforced against the consumer. This may discourage the business from agreeing to arbitrate future e-commerce dispute with the consumer. The best approach to guarantee that the consumer's consent is knowing and intelligent is that the business should consider a separate dispute resolution icon that the consumer must read and specifically accept in order to take the contract. The icon must include sufficient information about the arbitration clause and the arbitral process. The information must be written in clear and easily understandable language. This approach will



guarantee that the consumer knows and understands the arbitration clause before he accepts the contract. In other words, it will help to overcome the lack of knowledge and understanding resulting from the fact that consumers do not read the arbitration clause and if they do read it, they may not understand what is meant by arbitration.

The new paradigm must stipulate the application of the law of the consumer's country of domicile to the subject matter of the dispute. Adopting such rule will not only protect the consumer, it will also eliminate any uncertainty about the applicable substantive law that may arise when the choice of law clause is invalid.

The new paradigm must stipulate the consumer country of domicile as the arbitral seat. This will enable the consumer to litigate dispute over online arbitration agreements and processes in the Courts of his country of domicile.

The new paradigm should raise the consumer's perception of fairness of the online arbitral procedures. This can be done through granting the consumer the chance to obtain legal representation and introduce evidence. The online arbitration provider and the arbitrators should appear to be impartial. This can be ensured by guaranteeing the independence of the online arbitral provider, awarding both the business and the consumer an "equal voice in the selection" of the arbitrators and publication of the arbitral award. Eventually, effective judicial review on aspects of the violation of due process will help the consumer perceive fairness of online arbitral procedures. This is because the arbitrator will pay more attention to "act fairly". An effective judicial review is the one that leads to the invalidation of the

arbitral award whenever the court decides that a violation of due process has occurred.

The above suggested paradigm will only raise the consumer confidence in online arbitration if it is implemented through an international convention. An international convention is a binding type of regulation. This means that the adhering countries will enforce the new online B2C arbitration against online businesses and online arbitration providers. In other words, an international convention will guarantee that the consumer enjoys the protection embedded in the paradigm. There is no doubt that an international convention that deals with consumer protection issues will not be easily adopted. Consumer protection is connected with political, social, and economic agenda. The variables that take part in formulating these agenda do differ from one country to another. For example, international efforts to set up special jurisdiction rules for consumer disputes have failed. The Hague Conference tried to develop a set of rules that could help to decide the jurisdiction over cross-border online B2C disputes. However, the disagreement between the US and EU countries on the way of establishing the jurisdiction deprived the world from developing international jurisdiction rules for consumer disputes. The EU countries tried to impose the same consumer jurisdiction rules included in the Brussels Regulation. The American delegation refused the European suggestion which is heavily influenced by Brussels I Regulation. It would also allow the European consumers to sue American businesses in their country of domicile. This is completely against the American businesses' interests since most of EU consumers use the internet to buy products and services from businesses domiciled in the US. In the year 2000, the EU

and USA held a summit in Washington. In that summit both parties declared that they are unlikely to agree on rules for jurisdiction in B2C e-commerce disputes in the near future.

The suggested model convention on online cross-border B2C arbitration is likely to be successful. The reason is that the suggested model strikes balance between consumer protection policies in the EU and the US. In the US, business sector strived a lot until they got to the stage where the US Supreme Court approved the legitimacy of arbitration clauses in B2C adhesion contracts. Therefore, it is very likely that business sector in the US will positively look at the suggested model convention and will also lobby to persuade the US government to adopt such a convention. In the EU, the suggested model is also likely to gain popularity. The reason is that it imports many of the consumer protection principles embedded in EU law on international B2C dispute resolution.

The suggested model convention covers particular issues of online cross-border B2C arbitration. This means that the enforcement of online cross-border B2C arbitration clauses and awards that covers these issues will not be made under the NYC.

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