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Online dispute resolution for cross-border electronic commerce transactions: draft procedural rules

Proposal by the European Union observer delegation

Note by the Secretariat

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I. Introduction

1. During the course of the twenty-seventh session of Working Group III (Online Dispute Resolution), the European Union observer delegation submitted to the Secretariat the following text, which is reproduced below in the form in which it was received by the Secretariat.

II. Proposal by the European Union observer delegation

A. The discussions of Working Group III: Where do we stand today?

1. UNCITRAL's mandate

In 2010, UNCITRAL entrusted its Working Group III with developing a legal standard on Online Dispute Resolution ("ODR") for cross-border electronic commerce transactions, including business-to-business and business-to-consumer transactions.[1] Working Group III has since discussed drafts of Rules for an ODR process for cross-border low-value, high-volume electronic commerce transactions (the "ODR Rules"). It has agreed that the ODR Rules would take the form of generic contractual Rules that would be agreed upon by online merchants and their online customers in the context of an electronic commerce transaction.[2] The idea is that the possibility to settle potential disputes arising from an electronic commerce transaction through an ODR procedure that complies with an internationally recognized standard — i.e. with the "UNCITRAL ODR Rules" — would increase buyers' and vendors' confidence in buying and selling online and across borders.

The broad scope of the initiative (not only business-to-business transactions, but also business-to-consumer transactions) reflects two basic realities of low-value, high-volume electronic commerce transactions:

First, low-value, high-volume transactions very often involve consumers. One can even say that low-value, high-volume transactions are a paradigm case for consumer transactions;

Second, online transactions are different from offline transactions. While in offline transactions the vendor usually knows whether the transaction is a business-to-business or a business-to-consumer transaction, in online transactions the online vendor simply puts his terms and conditions on his website and those terms and conditions get agreed by the buyer ticking the relevant box — no matter the category the buyer falls into (business or consumer).[3]

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[1] Report of the 43rd session of the UNCITRAL Commission (2010), A/65/17, para. 257, confirmed by Report of the 44th session of the UNCITRAL Commission (2011), A/66/17, para. 218 and Report of the 45th session of the UNCITRAL Commission (2012), A/67/17, para. 79.

[2] See Report of the 25th session of Working Group III (New York, May 2012), A/CN.9/744, para. 16.

[3] This means that, in online transactions, even if the terms and conditions stipulated that they only apply when the buyer is a business (business-to-business transaction), in fact they would also be agreed upon when the buyer is a consumer — unless there was a mechanism in place that would allow the online vendor's website to categorize the buyer (as being a business or a consumer).

Against this background, UNCITRAL has instructed its Working Group III to be particularly mindful of consumer protection legislation and, in general terms, to consider specifically the impact of its deliberations on consumer protection.[4] This mandate also responds to another fundamental fact: consumers — in developing countries and in developed countries — are key drivers for the economy worldwide[5] and especially for tapping the potential of electronic commerce. In order to achieve the goal of instilling confidence in these key players in buying online and across borders, the ODR Rules need to meet their expectations.

2. The design of the ODR Rules — Arbitration as a model for designing a global standard for ODR for low-value, high-volume electronic commerce transactions?

ODR processes and the mechanisms ensuring compliance with their outcomes can be designed in a multitude of ways. Up to its 26th session (Vienna, November 2012), Working Group III engaged in intensive discussions on whether or not the ODR Rules should be designed so as to end in an arbitration phase. In that context, it was also discussed whether a potential arbitration process could be designed on the assumption that relevant arbitration agreements — when concluded at the time of the transaction, i.e. before the dispute has arisen ("pre-dispute arbitration agreements") — would in all instances be binding on both parties.

Focussing the discussions on a potential arbitration model proved to be controversial for two reasons:

First, designing the ODR Rules on an arbitration model only would not have reflected the current reality of ODR processes worldwide. Indeed, many successful ODR processes today are not designed on the model of arbitration.[6] Other than arbitration processes, they do not provide for outcomes which are binding on the buyer, while compliance with the procedural outcome is ensured through private enforcement mechanisms. Furthermore, arbitration processes are "heavy" procedurally, and the added value of online arbitration in terms of cross-border enforcement of arbitral awards under such a process is doubtful. It is doubtful if arbitral awards rendered under such a process would be capable of being enforced under the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.[7] Even assuming that this was the case, it is unrealistic to believe that arbitral awards rendered in the context of low-value, high-volume transactions could be enforced across borders under the 1958 New York Convention. This is particularly true when the claimant is a consumer or a small or medium-sized business. In that context, it should be noted that being awarded an arbitral decision does not mean that the claimant can automatically enforce that award against the other party. In order to enforce an arbitral award, the award

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[4] See Report of the 44th session of the UNCITRAL Commission (2011), A/66/17, para. 218.

[5] In the European Union, for example, consumer expenditure accounts for 56 per cent of the European Union's GDP.

[6] See Vikki Rogers, *Managing Disputes in the Global Market Place. Reviewing the Progress of UNCITRAL's Working Group III on ODR*, to be published in the Spring issue of "Dispute Resolution Magazine" (draft version accessible via: http://blogs.law.stanford.edu/codr2013/files/2013/03/Dispute-Resolution-Magazine-Final-Draft.pdf [accessed on 6 May 2013]).

[7] See background note A/CN.9/WG.III/WP.110 in which the UNCITRAL Secretariat draws attention to a number of open questions in that regard.

creditor (claimant) needs to go to the local enforcement court at the place where the award debtor (respondent) has his assets and request that the award be declared enforceable. In other words, in order to enforce his award, the claimant needs to revert to the judicial system. This is problematic in cases where the judicial system at the place where the respondent resides or otherwise has his assets does not perform well.[8] Furthermore, requesting a court to declare an arbitral award enforceable is costly. The costs are even higher when the award debtor (respondent) is in another country. Especially in a context like that envisaged by the ODR Rules — i.e. in the context of cross-border low-value, high-volume transactions — it is very likely that the cost of enforcing an arbitral award is much higher than the sum awarded. It would therefore be disproportionate for award creditors (claimants) — especially when they are consumers or small or medium-sized businesses — to try and enforce their awards.

Second, regarding business-to-consumer transactions, the legal standard concerning the effect of pre-dispute arbitration agreements on consumers is split among States. There are two diverging standards:

> In one group of states ("Group I States") pre-dispute arbitration agreements are considered binding on all parties, irrespective of whether one party is a consumer or not.[9]
>
> In another group of states ("Group II States") pre-dispute arbitration agreements are considered not binding on the consumer or can be invalidated by him. However, consumer arbitration agreements are considered binding on both parties (i.e. including on the consumer) when they are entered into *after* the dispute has arisen.[10]

3. The outcome of the 26th session of Working Group III (Vienna, November 2012)

As having an arbitration track in the Rules was important for some "Group I States" and as "Group II States" underlined that — if the ODR Rules were to contain an arbitration track — regarding pre-dispute consumer arbitration agreements, the ODR Rules as a *global* standard for an ODR process could not be designed on the

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[8] The UNCITRAL ODR initiative is intended to also help the development of electronic commerce in countries where the judicial system does not perform well. If the UNCITRAL initiative is designed in a way that sends award creditors (claimants) back to those judicial systems, parties from those countries lose out.

[9] Such jurisdictions include the United States of America and a number of other States. Regarding the situation in the United States, however, it should be noted that on 7 May 2013 a bill for an "Arbitration Fairness Act of 2013" was tabled in the United States Senate. The bill foresees to amend Title 9 of the United States Code, inter alia, by adding a new § 402, according to which "*[…] no pre-dispute arbitration agreement shall be valid or enforceable if it requires arbitration of […] [a] consumer dispute […]*." If the Arbitration Fairness Act gets adopted, the United States would no longer be a "Group I State", but rather fall within the category of "Group II States".

[10] Such jurisdictions include Japan, the Member States of the European Union (in accordance with the recently adopted European Directive on alternative dispute resolution for consumer disputes), Canadian jurisdictions, a number of Latin American States and some African States. South Korea has a legal standard which is similar to that of the jurisdictions stated. If the "Arbitration Fairness Act of 2013" (see previous footnote) gets adopted, the United States would equally fall into this group of States.

model of the standards of one group of States alone, Working Group III agreed on the following compromise at the end of its 26th session:

1. The Rules should adopt a "two-track approach", meaning that they should be designed flexibly so as to provide for one procedural track leading to arbitration ("arbitration track") and one procedural track not leading to arbitration ("non-arbitration track");

2. In the arbitration track, the Rules would need to reflect the divergent standards in Group I States and Group II States concerning pre-dispute consumer arbitration agreements. This would mean in practice that the arbitration track could be designed on the assumption of binding pre-dispute consumer arbitration agreements whenever the transaction involved a consumer from a Group I State. Whenever a consumer from a Group II State was involved in the transaction, the arbitration track would need to respect the relevant standard of Group II States.[11]

B. The issue: Respecting divergent standards concerning pre-dispute consumer arbitration agreements in the "arbitration track"

1. Why Working Papers 119 and 119/Add.1 do not fully implement the outcome of the 26th session of Working Group III

The Working Papers (WPs) published by the UNCITRAL Secretariat in preparation of the 27th session of Working Group[12] only partially implement what the Working Group had agreed at its preceding 26th session:

1. It is to be welcomed that WPs 119 and 119/Add.1 implement the so-called "two-track approach";

2. However, as concerns the so-called "arbitration track" of the Rules (called "Track I" in the WPs), the WPs fail to ensure respect for the standard concerning pre-dispute consumer arbitration agreements applicable in "Group II States". Instead, the ODR Rules as they stand in WPs 119 and 119/Add.1 are drafted on the basis of the "Group I State" standard alone.

The Working Group had agreed, that if the ODR Rules would include an arbitration stage, they would need to include a mechanism that also respects the standards of Group II States concerning pre-dispute consumer arbitration agreements.[13] Group II States had made it clear that this would need to entail that consumers from such States must not "be put on the arbitration track of the Rules", meaning that if the online buyer was a consumer from a Group II State, the Rules should make sure that either an arbitration track cannot be agreed upon in the first place, or — if the consumer agrees to the arbitration track of the Rules (e.g. because the online seller only offers Track I of the Rules) — the ODR provider should not be able to start the

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[11] See Report of the 26th session of UNCITRAL Working Group III, A/CN.9/762, paras. 18, 19 and 22.

[12] More specifically, WPs 119 (A/CN.9/WG.III/WP.119) and 119/Add.1 (A/CN.9/WG.III/WP.119/Add.1).

[13] See Report of the 26th session of UNCITRAL Working Group III, A/CN.9/762, paras. 18, 2nd sentence, 22.

arbitration phase of the procedure unless the consumer agrees to start that arbitration phase *after* the dispute has arisen (e.g. by a "second click").[14]

2. Why saying that the ODR Rules are only contractual in nature is not enough — a practical example

Simply saying that the Rules are intended to be only contractual in nature (i.e. not part of a Convention or a Model Law) and that they therefore are incapable of setting aside consumer protection legislation in Group II States, is not enough. Although being factually correct as a statement, this finding does not solve the problem. This becomes evident from the following example:

Example: If a consumer from a Group II State enters into an "arbitration track agreement" as currently envisaged by WPs 119 and 119/Add.1 with an online merchant established in a Group I State and they agree to submit relevant disputes to an ODR provider established in a Group I State, the consumer protection legislation of the Group II State concerned does not apply to relevant ODR proceedings. Of course, the ODR Rules do not affect the relevant Group I State consumer protection legislation; but if the relevant Group I State legislation does not apply, it does not help the consumer that the consumer protection legislation of his country is not prejudiced by the ODR Rules.

In the above scenario, the ODR provider might render an arbitral award against the consumer and order him to pay, e.g. $200. The online seller would then try to enforce this award against the consumer in the Group II State in which the consumer is resident. This would mean in practice: The consumer would receive — from his own enforcement court/authority — a writ informing him that an award has been issued against him ordering him to pay $200 and that he has to pay on that award unless he raises objections before the enforcement court/authority within a specified period of time.

The overwhelming majority of consumers (who are not lawyers specialized in international arbitration) would be much intimidated and would simply pay — because they would not know what to do or because the cost for hiring a highly specialized lawyer (who would tell them that under the relevant Group II State legislation the arbitration agreement was not binding on or could be cancelled by them and that therefore they could oppose recognition and enforcement of the arbitral award and would not have to pay the $200) would be too high.

- In practice, therefore, the relevant consumer protection legislation would not be applied and therefore would not protect relevant consumers, if they had agreed on the "arbitration track" of the Rules as they currently stand.
- As has been seen above,[15] UNCITRAL instructed Working Group III not only to be mindful of the need not to displace consumer protection legislation. The Commission also decided that, in general terms, in the implementation of its mandate, the Working Group should also consider specifically the impact of its deliberations on consumer protection. Simply arguing that the Rules are contractual in nature and therefore cannot displace consumer protection

[14] See Report of the 26th session of UNCITRAL Working Group III, A/CN.9/762, para. 22.
[15] See point A.1. of this document.

legislation would therefore fail to respect the Commission's mandate to also consider the practical impact of the draft Rules.

- Finally, the scenario described above (consumer gets confronted with foreign arbitral award, is intimidated and pays without raising objections to the recognition and enforcement of the award), would ultimately lead to consumers abstaining from shopping online and across borders. Rather than instilling consumer confidence in shopping online and across borders, the ODR Rules would thus deter consumers from using the potential of electronic commerce. This would run counter the rationale of the UNCITRAL ODR initiative as stated by the UNCITRAL Commission.
- If the Rules were designed as currently set out in WPs 119 and 119/Add.1, Working Group III would therefore fail to fulfil its mandate.

C. The challenge: Ensuring that online buyers are "put on the right track"

In a situation of divergent standards concerning arbitration, the easiest way forward for designing a global standard on ODR could be to envisage — in line with the current reality of many ODR systems — an ODR process not modelled on arbitration.

If, however, the Working Group opts to retain an arbitration track in the Rules, the challenge is to ensure that online buyers are "put on the right track". "Putting online buyers on the right track" means that the Rules would include a mechanism that would ensure that in the event that the buyer is a consumer from a Group II State the ODR process would not end in arbitration, unless the consumer agrees on an arbitration track after the dispute has arisen.

D. The way forward: Including technology in our deliberations

At the outset, two ways forward appear to offer themselves:

1. A mechanism ensuring that online buyers are "put on the right track" could lie with the ODR provider. The ODR Rules could contain a definition of "consumers" and two annexes listing Group I States and Group II States, while the — to be developed — principles for ODR providers could foresee that ODR providers would have to ensure that if the dispute involves a consumer from a Group II State, the ODR process would not move to an arbitration stage, unless the consumer gave his agreement to do so post dispute.

2. As some delegations stressed that it is important for them that it be clear — at the time of the transaction — if an ODR process ending in arbitration has been agreed, those delegations might not consider the above solution as a way forward. The mechanism ensuring that online buyers are put on the right track would therefore need to lie at the time of the transaction, i.e. when the parties agree on the ODR clause. As the ODR clause is offered on the online merchant's website and agreed when the buyer ticks the "I agree" box, the mechanism needs to bite exactly here, i.e. on the online merchant's website.

The Mechanisms described at (2) above would allow the online merchant's website to identify if the buyer is from a Group I State or a Group II State and — in the event that the buyer was from a Group II State — if the buyer is qualified as a business or as a consumer. In the event that the website identified the buyer as a Group II State consumer, it would automatically offer the "non-arbitration track" (Track II) of the Rules, otherwise it would offer the track the online merchant offers for transactions with other buyers (Track II or Track I).

In the ODR Rules, the above approach could be implemented as follows:

The Rules would contain two Annexes:

- Annex I listing Group I States;
- Annex II listing Group II States.

States would notify the UNCITRAL secretariat, prior to adoption of the ODR Rules, if they intend to be listed in Annex I or Annex II.

- In Article 2 of the draft Rules, a definition of "consumer" would be added. A number of international instruments contain a definition of "consumer" (e.g. Article 2 of the Hague Convention on Choice of Court Agreements); these definitions could serve as a model.
- The Rules would stipulate that in the event that the buyer is a consumer from a Group I State, Track I can be agreed only after the dispute has arisen.

In essence, therefore, the mechanism described would mean that the online merchant's website has the potential of choosing whether Track I or Track II of the ODR Rules is offered to the buyer. Implementing such a mechanism on online merchants' websites is very easy in terms of IT and does not constitute a burden for online merchants. In that regard, it is important to note:

- All online merchants maintain a website that contains an order form in which buyers need to fill in their address (shipment/billing). Online merchants' systems therefore already dispose of the data they would need to ascertain whether the buyer is from a Group I State or a Group II State.
- Collecting the data necessary for establishing whether or not the buyer is a consumer could be collected in a very simple way: when the system establishes (from the address the buyer fills into the order form) that the buyer is from a Group II State, the system would ask the buyer a question — in accordance with the definition of "consumer" in Article 2 of the ODR Rules — that would allow it to establish his quality as a business or a consumer (e.g. "Are you making this purchase for your personal or for your professional purposes?").
- Connecting the result of the above data collection with the choice of Track I or Track II of the ODR Rules is a very straightforward IT operation.
- Online merchants that intend to offer the UNCITRAL ODR Rules on their websites will have to rework their websites anyway. Including a straightforward mechanism as described here, in effect, does not constitute an additional burden.