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Making the World Safe for Predatory Capitalism

By Dean Baker
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You can't live in the United States without hearing celebrations of capitalism and the wonders of entrepreneurship. People such as Steve Jobs and Bill Gates are lauded for making it possible to buy low-cost computers to put on our desks or carry around. The wizards at Google made it possible to search the huge offerings on the web in a fraction of a second. And Jeff Bezos made an Amazon.com click the first and last stop on tens of millions of shopping trips.

All of these successes have dark sides. Jobs used old-fashioned anti-raiding agreements to keep competitors from enticing away his workers. Gates and Google have both engaged in anti-competitive practices that likely would have brought antitrust enforcement in prior decades. And Amazon has prospered not only because of low prices and good service, but also by being exempted from the requirement to collect the same sales tax as its brick-and-mortar competitors.

But in these cases, and many others, there clearly have been huge benefits to consumers and the economy as a whole as the result of innovative capitalists. However, in today's economy, getting rich does not necessarily require better serving your customers. A series by the *New York Times* on arbitration clauses in contracts shows that one of the best ways to make money is to find ways to rip off your customers.

The point of these arbitration clauses is to take away the right of consumers to bring class action lawsuits against improper practices. For example, if a telephone company charges an outlandish fee for ending a contract early, without clear notification in the initial agreement, an arbitration clause may prevent customers from bringing suit.

The point of getting the case into arbitration is not just to get a referee that is likely to be sympathetic to the company; arbitration also hugely tilts the playing field in their direction. As a practical matter, it is unlikely to make sense for an individual customer to hire a lawyer to try to win back \$500 or \$1,000 that a phone company is improperly charging. Legal fees can easily exceed these sums and of course there is no guarantee of winning.

The most common form of redress is to bring a class action suit. This allows hundreds or thousands of people who were victimized by the same clause to join together to bring a legal case. But the arbitration clauses specifically block legal actions. This means arbitration is the only form of redress.

The latest Times article in this series reports on how debt collectors are taking advantage of these clauses. They can use the courts for abusive forms of debt collection, and then hide behind arbitration clauses to prevent their victims from suing back.

The way this works is that a debt collector will buy up from tens of millions of dollars of debt from a major company, such as Verizon or Citibank, at a few cents on the dollar. These companies have largely given up hope of recovering these debts, many of which may just be bookkeeping errors by the company.

The debt collectors then go to court to try to get a judgment against the alleged debtor. This requires bringing suit and notifying the person against whom they are making a claim. Many of the people being sued may get their notification along with a pile of advertisements and just throw them out with the rest of their junk mail, never realizing that they are being sued. When the date of the hearing comes, the judge is pretty much required to rule in favor of the debt collector if the defendant does not show up in court.

The debt collector can then take advantage of this ruling to seize money from a bank account or other assets or to have a paycheck garnished. This can allow them to collect the face value of debt for which they just paid a few cents on the dollar. And it doesn't even matter if the initial debt was improperly calculated. Once the court has ruled in the debt collector's favor, the original status of the debt is irrelevant.

The recourse against this sort of abusive behavior would ordinarily be a class action lawsuit against the debt collector for failing to give proper notification of the suit. Since debt collectors

are doing the same thing to hundreds or even thousands of people at a time, there would be many potential plaintiffs for such a suit.

But this sort of legal action is prevented by the arbitration clauses in the initial contract. Even though no one has signed an arbitration agreement with the debt collectors, the courts have ruled that this provision is transferred to the debt collectors, which means that people cannot sue them in court for even the most abusive collection practices.

The outcome is not only unfair in allowing these debt collectors to prey on many low- and moderate-income people, but it also represents a real failure by the legal and economic system. In a capitalist economy we expect people to be motivated by the desire to make money. But we should be structuring incentives so that the best way to make money is by developing better technology, better products or better ways to service customers.

Instead, recent Supreme Court rulings holding up these arbitration scams mean that one of the best ways to make money is to rip people off in writing contracts. Expertise in writing deceptive contracts is not a way to a better economy or a better country.