

THE FUTURE OF CIVIL LITIGATION

# THE FUTURE OF ARBITRATION

BY MARK A. SHANK AND JOHN L. TURNER, JR.

In a time of increasing complexity and connectivity, arbitration is well established as the leading alternative to traditional litigation. Its recognized virtues of speed, informality, and low cost make it so. Yet, as arbitration's popularity has increased, so have its detractors, which has caused reform legislation to be introduced in Congress and the Texas Legislature.



At its core, arbitration has always been about effectuating a mutual choice between parties. It allows parties to avoid the formalities and expense of ordinary litigation, and, at its best, enables parties to design their own process to resolve these disputes.<sup>1</sup> As a conscious public policy choice, however, arbitration only works if the process is both fair and perceived as fair.

In the 60-plus years since the passage of the Federal Arbitration Act (FAA), federal and state courts have favored an expansive interpretation of the reach and scope of the FAA. As originally envisioned, the FAA's primary focus was the regulation of disputes between commercial actors of similar bargaining power. But as judicial interpretation has significantly curtailed a party's right to challenge an arbitration clause,<sup>2</sup> disputes arising out of, or relating to, a contract containing an arbitration clause are rarely challenged successfully in the courts. This is a direct product of expansive interpretation of the FAA to involve all manner of disputes.

Paradoxically, it is this strong preference for arbitration that threatens to undermine the public's trust in the fairness of the procedure. Secure in the knowledge that they can avoid the courthouse, some businesses — especially those competing in markets characterized by high-volume transactions — have been inserting arbitration clauses into all manner of consumer contracts. Likewise, since the U.S. Supreme Court's decision that employers may require employees to arbitrate employment claims, including statutory and tort-related claims,<sup>3</sup> employers now routinely require prospective employees to agree to arbitrate all disputes. To the extent that the result is a faster, less expensive, and fair resolution of disputes, the result is unassailable.

The worry is that by forcing these less-sophisticated parties to arbitrate against a more-experienced adversary, the courts' fealty to arbitration clauses runs the risk of trumping one party's rights. This concern is particularly apt when the party is forced to arbitrate before a specialized industry group, which may favor the interests of its member-parties over those of the non-member, or before a private arbitration company that handles a high volume of transactions for the same client. One study supports this notion.<sup>4</sup>

Without balance, the arbitration procedure will be viewed as unfair. Critics contend that the current regime allows sophisticated commercial actors to manipulate the process to the detriment of parties who neither contract often nor appreciate the nuances of arbitration provisions when they do. Such one-sidedness is undesirable and, if public perception continues on its current trajectory, unsustainable.

For these reasons, the current trend seems to tilt the balance away from the FAA's hard line toward enforcing arbitration clauses. In both the courts and Congress, a movement is afoot to create limitations on what can be included in an arbitration clause. In one recent example, a federal appeals court held that a franchise agreement arbitration clause allowing only the franchisor to litigate certain claims created an unenforceable contract of adhesion.<sup>5</sup> The notion that arguably one-sided arbitration contracts are unconscionable is gaining traction in some courts.

Lawmakers are contemplating striking at the source. The Fairness in Arbitration Act pending before Congress is a good example. It would abrogate many of the courts' interpretations of the FAA.<sup>6</sup> Specifically, the act would allow for the repudiation of adhesion contracts in the areas of employment, consumer, or franchise disputes. Thus, if the act were passed, mandatory arbitration clauses in employment contracts would likely diminish greatly, and brokerage firm contracts requiring arbitration would be unenforceable absent the customer's consent. At the time of writing, the Texas Legislature was considering similar measures.

The policy motivations underpinning the act reflect, as its name suggests, a desire to level the playing field. The drafters' stated concerns are that private arbitration companies have devised rules favoring their repeat corporate clients; that consumers and employees often fail to appreciate the boilerplate arbitration text appearing in their agreements; and that private arbitration companies will continue to devise rules favoring their repeat corporate customers. The act's drafters also believe that overreliance on arbitration prevents courts from developing important precedents.

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We should guard, however, against the well-intentioned urge to overcompensate for arbitration's perceived shortcomings. Some of the commentary about the so-called problems with the procedure may not be supported by firm foundations. For example, an advocate for less arbitration will make much of the high percentage of awards for creditors in consumer lending arbitrations, but is likely to omit that the consumer fails to even appear in the majority of such cases. The point being that while arbitration procedures and boundaries might need reform, the procedure itself remains true to its core attributes of being an efficient and cost-effective method for dispute resolution.

Every choice has unintended consequences, and a decision to place more cases in the public courts is no different. In arbitration, the parties cover the costs, not the public. Today, many court systems are inundated with filings that might be more efficiently adjudicated in arbitration. For example, Blair County, Pa., was recently forced to establish a special "Credit Card Court" due to the incredible surge in civil filings for collections and mortgage foreclosures.<sup>7</sup> If we make a collective decision to demand that certain disputes be adjudicated in a public forum, will there be sufficient public revenue to support it?

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Notwithstanding its challenges, the need for arbitration today is more compelling than at any time in the past. As our world grows more complex, the nature of litigation evolves in the same direction. Whereas a common business lawsuit in Texas in the 1930s might have been a straightforward breach of an oilfield services contract, today it might involve complex intellectual property issues that require a level of specialized training not found in the typical jury pool. This complexity portends the rising demand for arbitration and the need for arbitrators who are experts in fields with particularly high frequencies of litigation.

Arbitration also has an important place in our globalized economy. International arbitration is already the preferred method of dispute resolution in international transactions, particularly in the area of project finance, and the volume should only increase.<sup>8</sup> The challenge will be to preserve this valuable and proven dispute resolution process, while repairing it to the extent necessary to make it workable and fair. The magnitude and scope of large international infrastructure projects — with labor provided from Asia, raw materials from a company in South America, and financed by the sale of asset-backed securities in Europe — mean that multiple jurisdictions' laws are implicated in such disputes. In such circumstances, the best choice — if not the only choice — is to agree beforehand on when, where, and how such disputes will be adjudicated.

### Notes

1. See *New Process Steel Corp. v. Titan Indus. Corp.*, 555 F. Supp. 1018, 1021 (S.D. Tex. 1983).
2. See, e.g., *Prima Paint v. Flood & Conklin Mfg.*, 388 U.S. 395, 388 (1967) (holding that federal court should not adjudicate claim of fraudulent inducement unless the fraud was "in the inducement of the arbitration clause itself"); *Dean Witter Reynolds v. Byrd*, 470 U.S. 213, 217 (1985) (holding that arbitration clause should be enforced even where a multiplicity of proceedings may result from its enforcement).
3. *Glimmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 24–26 (1991).
4. See "How Credit Card Companies Ensnare Consumers," *Public Citizen*, September 2008. Available at: <http://www.citizen.org/documents/ArbitrationTrap.pdf>.
5. *Ticknor v. Choice Hotels Int'l, Inc.*, 265 F.3d 931, 940–41 (9th Cir. 2001).
6. S. 1782; H.R. 3110.
7. *Altoona Mirror*, "Blair Forms New Credit Card Court," by Phil Ray, Dec. 2, 2008. Available at: <http://www.altoonamirror.com/page/content.detail/id/513757.html?nav=742>.
8. See Sharif A. Touray, "Arbitration In International Project Finance: Drafting the Arbitration Provision." Available at: <http://library.findlaw.com/1999/Jan/1/128559.html>.

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