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1-1-2009

# The Case Against the Arbitration Fairness Act

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## Repository Citation

Peter B. Rutledge, *The Case Against the Arbitration Fairness Act*, 16 *Disp. Resol. Mag.* 13 (2009),  
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# POINT

## The Case Against the Arbitration Fairness Act

By Peter B. Rutledge

The Arbitration Fairness Act is a well-intended but ultimately misguided attempt to address a system of dispute resolution that has largely worked well. The bill currently being considered by Congress rests on a series of flawed empirical premises. This article addresses three. First, though the bill posits that arbitration leaves consumers and employees worse off, data demonstrate individuals overall are often better off under a system with enforceable predispute arbitration agreements than a system without them. Second, although the bill promises improved access to justice, the proposal actually erects more impediments. Third, though the bill suggests that postdispute arbitration will provide a continued outlet for this system of dispute resolution, it fails to recognize the significant structural impediments to a successful system of postdispute arbitration.

First, it now appears to be common ground that the policy debate over the Arbitration Fairness Act should focus on empirical data. We all can harness our success stories and horror stories about arbitration (or any other system of dispute resolution). Yet the Arbitration Fairness Act does not simply address the bad cases while preserving the good. Instead, it proposes a systemic overhaul that categorically bans predispute agreements entirely. Thus, to assess the bill's impact, a systematic view of the empirical data is appropriate.

Interestingly, the data frequently show that predispute arbitration in general produces better outcomes for individuals. In March, the Searle Institute of Northwestern University Law School published a thorough study



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of consumer arbitrations conducted by the American Arbitration Association. Contrary to the cries of arbitration's critics, individuals fared quite well, prevailing in a significant number of arbitrations and recovering a reasonable share of the damages that they sought. This study represents simply the latest chapter in a growing body of empirical literature suggesting that arbitration largely reaches a fair result for individuals in their disputes against companies.<sup>1</sup>

To be sure, not all studies are as sanguine. Some research suggests that low-income individuals in arbitrations under promulgated (as opposed to individually negotiated) arbitration agreements fare poorly.<sup>2</sup> Such results, though, simply beg the question about what causes such outcomes. Is it that arbitration is stacked against the individual? Or something in the nature of the claim that gives rise to a low likelihood of success, whether in arbitration, litigation, or some other forum?

Not only are the data mixed, but they are also incomplete. Although the Arbitration Fairness Act broadly addresses employment, consumer, and franchise arbitration, gaps exist in all three areas, especially franchise arbitration, in which few studies are available and almost none address outcomes.

The upshot here is simply that Congress should tread cautiously when contemplating a systematic overhaul of a system that, by some measures, produces favorable results and, in other important respects, has an incomplete empirical record.

Second, eliminating predispute arbitration agreements impedes rather than improves an individual's access to justice. For one thing, individuals may find it more difficult to find a lawyer if they are forced to litigate their claims. The high costs of our civil litigation system mean that

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to agree to a process that was truly better and more efficient for all.

In the end, the most practical way to ensure that arbitration is fair is to make it voluntary on a postdispute basis. Once a dispute has arisen, consumers, employees, and other “little guys” will be able to make knowledgeable determinations as to whether the proposed arbitration is efficient and fair for all concerned. The proposed Arbitration Fairness Act in this sense would use the free market to ensure that arbitration is fair and just. ♦

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## Point

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lawyers generally will demand high recoveries and a high prospect of success before they are willing to undertake a case. By contrast, the lower costs of arbitration and the procedural flexibility enable an individual to obtain judgment at a lower cost.

Apart from access to counsel, arbitration improves access to justice in another respect. Individuals achieve results faster. Every major empirical study on arbitration has found that it produces results faster than litigation. For individuals who seek recovery, the speed to resolution may be a valuable advantage of this system of alternative dispute resolution. By eliminating predispute arbitration, Congress may worsen access to justice and end up hurting the very classes of people whom it purports to protect.

For society as a whole, the costs of resolving disputes without arbitration would rise. Consider the thousands of disputes currently resolved by arbitration. If those disputes no longer were arbitrable, where would they go? “To the courts” is the obvious answer. But any self-respecting lawyer or judge would tell us that the court dockets are already overburdened. Shuttling these cases out of arbitration simply lengthens the line at the courthouse for everyone.

Some defenders of the Arbitration Fairness Act try to turn these arguments on their head by arguing that arbitration deprives plaintiffs of the ability to bring class actions and thereby deprives those plaintiffs “access to justice.” There is some surface appeal to this argument, but it ultimately does not support adoption of the Arbitration Fairness Act. For one thing, the argument assumes the widespread adoption of class action waivers, and although some evidence suggests its use in certain industries (such as the cellular telephone industry), I am unaware of any systemwide evidence on this point. For another thing, even assuming the problem is widespread, the argument further assumes that a large number of cases exist that would satisfy Federal Rule of Civil Procedure 23’s exacting standards—again, I am unaware of any empirical evidence on this point. Finally, even assuming that these two preceding hurdles can be overcome, the argument does not support the wholesale invalidation of arbitration clauses—a more calibrated solution would simply invalidate class action waivers but not the arbitration

## Endnotes

1. Alan S. Kaplinsky & Mark J. Levin, *Excuse Me, But Who’s the Predator? Banks Can Use Arbitration Clauses as a Defense*, *BUS. L. TODAY* (May–June 1998) at 24.
2. *E.g.*, *Doctors Associates Inc v. Casarotto*, 517 U.S. 681 (1996) (holding that the FAA preempted Montana law specifying that an arbitration clause be printed at page one of a contract and be provided in capital letters and underlined).
3. The currently pending bills, S. 931 and H.R. 1020, would also prohibit franchisors from imposing mandatory arbitration on franchisees, on the theory that many franchisees require protection from the more powerful franchisors.

clauses themselves. Organizations such as the American Arbitration Association have begun to develop extensive experience administering class arbitrations, and there is no principled reason why the purported benefits of a class action cannot also be realized through the mechanism of an arbitration. Thus, at bottom, the class action argument is a bit of a ruse—at best it is an argument for the invalidation of class action waivers; at worst, it is self-interested politicking by class action plaintiffs’ lawyers masquerading as policy making in the public interest.

*Third*, defenders of the Arbitration Fairness Act often argue that postdispute arbitration mitigates these and other risks of eliminating enforceable agreements. Yet postdispute arbitration is not a viable alternative to predispute arbitration agreements. One problem is psychological—parties are simply far more willing to agree on matters before a dispute has arisen; once a dispute arises, the opportunities for cooperation dwindle. The second problem is structural: the parties’ incentives in the postdispute context fundamentally differ from the predispute context. Postdispute parties have more information, which enables them to make more calculated decisions regarding which form of dispute resolution better promotes their interests or effectively hinders the individual’s interests. Conversely, in the predispute context, parties have an incentive to enter into arbitration. An individual’s incentive is that arbitration is an affordable forum with superior chances for a favorable result. A company’s incentive is that arbitration can lower the company’s litigation costs.

At bottom, the Arbitration Fairness Act applies a meat cleaver to an issue that requires a scalpel. The solution is not for Congress to prohibit predispute arbitration agreements in employment, consumer, and franchise contracts. Instead, Congress should encourage and await additional empirical research. Research may show minor additions to the regulatory repertoire are necessary. However, wholesale, retroactive elimination of predispute arbitration agreements would effectively make worse off the individuals whom Congress, through this legislation, seeks to protect. ♦

## Endnotes

1. See generally Peter B. Rutledge, *Whither Arbitration?* 6 *GEORGETOWN J. L. & PUB. POL’Y* 549 (2008).
2. See Alexander J.S. Colvin, *Empirical Research on Employment Arbitration: Clarity Amidst the Sound and Fury?* 11 *EMPL. RTS. & EMPLOY. POL’Y J.* 405 (2007).