ANALYSIS

Following Years of Growth, Clients Are Increasingly Wondering If Arbitration Is Still Worth It, Litigators Say

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Commercial Litigation

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Arbitration has long been a preferred method for companies hoping to litigate their claims quickly, quietly and cheaply, and the popularity of venues like the American Arbitration Association and JAMS have only increased since the onset of the pandemic, when courts were hobbled coast to coast.

But several commercial litigators say they are increasingly fielding questions from clients who seem more eager to take their disputes into the public court system rather than through the binding and confidential arbitration system, representing something of a departure from the business world's typically preferred method for sorting out disputes.

Litigators and arbitrators point to several forces at play behind the trend, and say that, regardless of the factors impacting the decision, it is key to walk clients through their options and talk over whether their arbitration clauses are meeting their needs.

"I'm still a believer in arbitration, and still a believer that your clause and your selection of the arbitrator are critical," Casey Laffey, co-chair of Reed Smith's global commercial disputes group, said. "I think you shouldn't remove the arbitration clause, but you should be more creative in how it's written."

Bucking the Trend

Both JAMS and the American Arbitration Association (AAA), which are two of the largest U.S.-based arbitration venues, have been reporting consistent growth over the last several years.

According to filings from JAMS, the number of arbitrations the company handled grew from 3,500 in 2017 to more than 7,000 in 2021. AAA, meanwhile, grew the number of cases it handles from 9,737 in 2019 to 10,273 in 2022, according to records.

Arbitration clauses are included in contracts governing any number of agreements, including employment, licensing and purchasing agreements. The process is touted as more streamlined and cheaper than going to trial. The process has dramatically grown in popularity in recent years with the federal courts looking very favorably on the practice, with an even larger boost during pandemic-era court shutdowns.

However, litigators say they are seeing clients from various arenas begin to wonder if the process is as fast and inexpensive as it used to be, and whether they should be removing arbitration clauses from their contracts.

The change, litigators said, seems to be happening broadly, both in business-to-business and class action litigation.

Dechert's Christina Sarchio, who is co-chair of the firm's U.S. business disputes and trials practice and has also worked as an arbitrator with AAA for the past decade, said she has noticed her litigation practice growing while her arbitration practice has started shrinking somewhat.

"Companies are thinking through these issues a lot more," Sarchio said. "It can be death by a 1,000 paper cuts in arbitration."

Fox Rothschild's Lauren McKenna, who focuses on commercial litigation, said she has some clients showing more interest in getting into court, but, she said, it is usually on a client-by-client, or case-by-case basis.

Now that courts have largely bounced back from the pandemic-era backlogs, she said some clients are expressing that they've waited long enough, and would like to see their cases head directly to court.

"The conversation I often have is, if you're going to arbitrate, are you served by having something that is binding? And what are the risks to binding arbitration?" she said. "In some cases it's driven by the court. We're back in full business."

Laffey estimated about 20% of his clients are now raising concerns about arbitration and questioning whether they might want to go to court instead.

Overall, he said, he still advises that arbitration is the better option for his clients, but noted court can be more beneficial in certain circumstances, such as when a third party might be able to provide key testimony, which can be tricky to secure in arbitration, whereas in court the party could be subpoenaed.

But either way, he said, it's important for companies to take a close look at their contracts.

"I'm always telling clients it costs half a day in fees to have a firm closely review their arbitration clauses," he said. "There's just so much value in that."

Rising Costs

A significant factor underlying this trend is that costs are rising—and not because of the venues, but because of the parties.

Attorneys and arbitrators agree that they are increasingly seeing the streamlined arbitration process devolve into both sides insisting on onerous discovery and depositions, which can stretch proceedings out for months and add significantly to the fees parties must already pay to the arbitrators.

“Over time a thread of litigation vibrato, or work-up, has entered into the proceedings—more aggressive motion practice, requests for more robust discovery,” former Philadelphia Judge Annette Rizzo, who joined JAMS in 2015, said.

Depending on the types of cases, arbitrators may want to keep a tight schedule, or give a little latitude to help ensure the parties feel that their grievances are being aired out, much the way they would in a courtroom setting, Rizzo said.

“The choice of neutral is important,” she said. “Not just in applying the law, but also they have to have a good sense of case management.”

Sarchio said she has also seen this in her role as an arbitrator, where parties are increasingly seeking more depositions and more onerous discovery.

“The parties are spending a lot of time and money litigating almost as if they’re in court,” Sarchio said, noting that one recent arbitration involved some 72 document requests. “I keep telling them, this is arbitration. It’s supposed to be streamlined.”

Also, on the consumer side, defendants are finding themselves facing high filing fees in connection with so-called mass arbitrations—fees that have gotten so high, retail behemoth Amazon recently stopped including arbitration clauses in their contracts.

Following the U.S. Supreme Court’s 2011 decision in *AT&T Mobility v. Concepcion*, which gave the court’s blessing on arbitration agreements that require consumer complaints to proceed individually, many consumer-facing companies increasingly began including arbitration agreements as a way of side-stepping potential class actions. However, instead of succeeding in dissuading plaintiffs from suing, the plaintiffs’ bar, led largely by Keller Lenkner, began filing mass arbitration actions, which then slammed the defendant companies with massive fees.

For example, in 2020, 5,000 individual workers entered filings against DoorDash alleging the company misclassifies them as contractors. Facing huge arbitration fees, the company tried unsuccessfully to back out of the agreements.

Amazon also faced more than 75,000 claims from customers claiming its smart speakers recorded them without permission before deciding to phase out the arbitration clauses. The filings meant Amazon was on the hook for millions in fees alone.

“Companies just got overwhelmed with these arbitration demands,” Sarchio said. “They couldn’t control that. In court at least you can do an MDL and coordinate it.”

‘Pick Your Battles’

Laffey said it is important for companies and attorneys advising their clients to remember that arbitrations are a “creature of contract,” so many of the time and cost problems can likely be headed off with the right language.

For example, he said, having a single arbitrator, rather than three, can help. Also, he said, clauses can specify parameters for discovery, or cap the number of depositions.

But potentially most important, he said, is the selection of arbitrator, which he said outside counsel rarely spends enough time considering.

“Some are traditionalist arbitrators, who don’t believe arbitration is court, and don’t think you should have wide-ended discovery,” he said, adding in the alternative, “If a judge is right off the federal bench and all they know is court, they’re going to apply the same practice to arbitration. So who you chose is critical.”

Litigators also said there is sometimes a fear that an arbitrator will “split the baby,” rather than coming down hard on one side or the other. This can especially be the case when a suit arises in a novel area of law where the arbitrators have little guidance. And with almost no avenue for appeal, that is a risk many companies don’t want to take, one litigator said.

Confidentiality is also usually a benefit, but attorneys said that in some instances, companies are becoming more eager to have their stories heard, and having a public trial is one way to do that. This might be especially true in some personal injury cases, where sympathetic plaintiffs have started seeing a large uptick in verdict awards.

In one recent example, two hospitals in Philadelphia recently hit with large jury verdicts are arguing in post-trial motions that the awards will negatively affect care in the area.

Obermayer Rebmann Maxwell & Hippel’s Henry Noye, whose practice focuses on commercial litigation and catastrophic loss, said being able to bring an argument like that to a jury may be preferable to bringing it to an arbitrator.

“Obviously that’s impactful. Everybody needs a doctor. If you live in Philadelphia, with Hahnemann closing, in that scenario it’s definitely an advantage,” he said.

Also, if a claim raises a novel issue that could be widely advantageous for similar claims, a defendant may want to go to trial, Noye noted. Since litigation is always a cost for a defendant, it could be more advantageous to have persuasive caselaw that can be used to stop future lawsuits before they happen, he said.

“You’ve got to pick your battles,” he said. “The plaintiff’s bar certainly does.”

Sarchio offered a similar sentiment, adding that federal courts have also become more business-friendly in general.

She pointed to a recent study of U.S. Supreme Court cases, which found that companies have a 63% win rate before the court under Chief Justice John Roberts, which is 15% higher than the win rate under former Chief Justice William Rehnquist.

“Judges are now more on our side,” she said, “so we’ve got a better chance in court than we used to.”