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Arbitration Fairness Act of 2009

By Mark M. Lee

On February 12, 2009, Congressman Hank Johnson of Georgia, together with numerous co-sponsors in both Houses of Congress, introduced the Arbitration Fairness Act of 2009 (the "Act") in the United States House of Representatives. If passed, the Act would limit the scope of the Federal Arbitration Act of 1925 (the "FAA") in ways that potentially could have a significant impact on the financial services industry. The Act would render pre-dispute arbitration agreements – defined in the Act as "any agreement to arbitrate disputes that had not yet arisen at the time of the making of the agreement" – invalid or unenforceable if such agreements require arbitration of: (1) an employment, consumer, or franchise dispute; or (2) a dispute arising under any statute intended to protect civil rights. Arbitration provisions in collective bargaining agreements are exempt from the Act. Parties to disputes affected by the Act would still have the option to choose arbitration over a jury trial, however, such a choice would necessarily be made post-dispute. The Act also requires that the validity or enforceability of arbitration agreements be determined in court, under Federal law, as opposed to during arbitration. Section 5 of the Act makes clear that its amendments to the FAA would take effect on the day that the Act is signed into law and would apply to "any dispute or claim" that arises on or after the date of enactment. Even arbitration clauses executed prior to the Act becoming law would no longer be enforceable.

The Act is a bold attempt by Congress to narrow the judicially defined scope of the FAA by invalidating many of the pre-dispute arbitration clauses that have become common in business- to- consumer financial transactions. Supporters of the Act assert that the FAA was originally intended to apply to disputes between commercial entities of "similar sophistication and bargaining power," but now, due to a series of United States Supreme Court decisions, the FAA "extends to disputes between parties of greatly disparate economic power, such as consumer disputes and employment disputes." The Congressional findings supporting the Act indicate that "consumers and employees have little or no meaningful option whether to submit their claims to arbitration." Indeed, supporters express concern that consumers and employees usually have little choice in whether to enter into an agreement regarding pre-dispute arbitration. The Act's sponsors also express concern that high costs, lack of due process protections, and an apparent absence of judicial review all make arbitration an unfair forum for consumers. Moreover, proponents cite to what they see as the pressures exerted on arbitrators to render favorable decisions to companies that tend to use their businesses repeatedly as another reason to reform the FAA.

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Critics of the Act argue that it would harm the very groups of people that it seeks to protect. They point to potential increases in both the number of cases filed and the costs of litigating in federal court as factors that would have the unintended consequence of giving consumers and employees fewer meaningful ways to recover in disputes against businesses that have more financial resources at their disposal. Indeed, in the view of opponents, mandatory pre-dispute arbitration levels the playing field as businesses are unable to use their resources to increase their advantage over consumers. Critics also submit that the Act does little to mitigate the effects of the disparities in bargaining power, as consumers or employees may still be vulnerable to being pressured into entering post-dispute arbitration agreements. There is also some concern that the Act, as drafted, would not cover all "consumers" in financial transactions.

While the merits of pre-dispute arbitration clauses remain a subject of debate in the United States Congress, one thing remains clear – the Act, if passed, will fundamentally alter the way in which financial service organizations approach business-to-consumer contracts. Financial service companies have traditionally relied on pre-dispute arbitration clauses when dealing with consumer or employment contracts in order to avoid the potential exposure to the costs associated with excessive litigation, including excessive jury awards and class action liability. Over time, arbitration has proven to be a faster and a generally more cost-effective way of dealing with consumer disputes. If enacted in its present form, the Act would most certainly alter those practices as consumers and employees would now have the option to evaluate the merits of arbitrating disputes on a case by case basis. Businesses likely will need to revisit assumptions regarding both the content of pre-dispute arbitration agreements and their dispute resolution strategies to accommodate changes in the FAA. ◆

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