

# BUSINESS COURTS AND THE FUTURE OF ARBITRATION

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## I. INTRODUCTION

Not surprisingly, discussions of the future of arbitration tend to focus on arbitration—its characteristics, how it is changing, the governing legal regime, and so forth. For example, a commonly expressed sentiment, at this symposium<sup>1</sup> and elsewhere,<sup>2</sup> is that arbitration is becoming too formal—with too much discovery, too many motions, and the like.<sup>3</sup> As a result of its increasing formality (and the corresponding increase in cost), users reportedly are becoming more and more disenchanted with arbitration.<sup>4</sup>

But a focus on arbitration takes in only part of the picture. In deciding whether to agree to arbitration, parties necessarily are comparing it to the alternative—litigation.<sup>5</sup> Changes to arbitration

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<sup>1</sup> Such as the presentations by Tom Stipanowich and John Wilkinson during the panel on “Whither Arbitration? A Look into the Future of Arbitration.”

<sup>2</sup> See, e.g., Michael McIlwrath & Roland Schroeder, *The View from an International Arbitration Customer: In Dire Need of Early Resolution*, 74 *ARB.* 3, 10 (2008) (“frustration with the length and expense of the arbitration process is increasingly cited as the rationale for favouring court resolution (or at least for no longer favouring arbitration.)”; Gerald F. Phillips, *Is Creeping Legalism Infecting Arbitration?*, *DISP. RESOL. J.*, Feb./Apr. 2003 at 37 (survey of “leading commercial arbitrators”) (reporting that 72% of respondents (31 of 42) “believe[d] that arbitration is becoming too much like litigation”).

<sup>3</sup> The sentiment is not a new one. See, e.g., *INTERNATIONAL ARBITRATION IN THE 21ST CENTURY: TOWARD “JUDICIALIZATION” AND CONFORMITY?* ix (Richard B. Lillich & Charles N. Brower eds. 1994) (discussing the “judicialization” of international arbitration, “meaning both that arbitrations tend to be conducted more frequently with the procedural intricacy and formality more native to litigation in national courts and that they are more often subjected to judicial intervention and control”).

<sup>4</sup> See, e.g., Thomas J. Stipanowich, *Arbitration: The ‘New Litigation’* (2008), available at <http://ssrn.com/abstract=1297526> (“it seems discontent with commercial arbitration has never been more palpable if not more widespread.”); Lou Whiteman, *Arbitration’s Fall from Grace*, *LAW.COM*, July 13, 2006, available at <http://www.law.com/jsp/ihc/PubArticleIHC.jsp?id=1152695125655> (referring to “backlash against arbitration”); Beth Bar, *Some Attorneys Questioning Advantages of Arbitration*, *N.Y.L.J.* (May 18, 2007), available at <http://www.law.com/jsp/ihc/PubArticleIHC.jsp?id=900005481480> (“arbitration may be losing some of its luster”).

<sup>5</sup> Litigation is the default forum for dispute resolution. Matthew T. Bodie, *Questions About the Efficiency of Employment Arbitration Agreements*, 39 *GA. L. REV.* 1, 9 (2004) (“In our sys-

certainly affect this comparison.<sup>6</sup> But changes to litigation likewise can affect the comparison. Thus, any discussion of the future of arbitration must consider both litigation and arbitration, not arbitration alone. Indeed, a discussion that considers only arbitration implicitly assumes that litigation will remain unchanged, an assumption that obviously is unrealistic.

The list of changes to the litigation process that might affect the future of arbitration is a long one, far too long to consider fully here. Instead, I focus on one change in particular: the growth of specialized business courts. Business courts use specialized judges and expedited case management procedures to provide a more expert and faster dispute resolution process, incorporating some of the selling points of arbitration into litigation.<sup>7</sup> Thus, ironically, at the very time some are concerned that arbitration is becoming too much like litigation, business courts illustrate the opposite trend—they provide an example of litigation becoming more like arbitration, what might be called the “arbitralization” of litigation.<sup>8</sup>

Supporters of business courts commonly cite the need for courts to compete more effectively with arbitration as a justification for the creation of business courts. For example, Chief Justice John T. Broderick, Jr. of the New Hampshire Supreme Court stated that “[t]he impetus behind the bill [creating business courts] is that the state is losing market share . . . . The number of commercial disputes we are seeing ha[s] diminished.”<sup>9</sup> Broderick states, “I

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tem of dispute resolution, litigation is the ‘default rule’—the result that will take place unless the parties agree to a different alternative.”); Stephen J. Ware, *Employment Arbitration and Voluntary Consent*, 25 HOFSTRA L. REV. 83, 135 n.270 (1996) (referring to “default rule that disputes are resolved by litigation, not arbitration.”).

<sup>6</sup> Indeed, such a comparison is implicit in the term “judicialization,” see *supra* note 3, which suggests that arbitration is becoming more like litigation.

<sup>7</sup> See *infra* text accompanying notes 29–52.

<sup>8</sup> See Thomas E. Carbonneau, *At the Crossroads of Legitimacy and Arbitral Autonomy*, 16 AM. REV. INT’L ARB. 213, 247 (2005) (referring to “arbitralized court procedures”); see also Georges Abi-Saab, *The International Court of Justice as a World Court*, in FIFTY YEARS OF THE INTERNATIONAL COURT OF JUSTICE 1, 9–10 (Vaughan Lowe & Malgosia Fitzmaurice eds. 1996) (discussing “speculation about a tendency towards an ‘arbitralization’” of the ICJ). For analyses of the ability of parties to enter into contracts that make litigation more like arbitration, see Henry S. Noyes, *If You (Re)Build It, They Will Come: Contracts to Remake the Rules of Litigation in Arbitration’s Image*, 30 HARV. J.L. & PUB. POL’Y 579 (2007); Michael L. Moffitt, *Customized Litigation: The Case for Making Civil Procedure Negotiable*, 75 GEO. WASH. L.REV. 461 (2007); Elizabeth Thornburg, *Designer Trials*, 2006 J. DISP. RESOL. 181 (2006).

<sup>9</sup> Shir Haberman, *Chief Justice Fights for Business Court*; Broderick: State Losing Market Share, SEACOASTONLINE.COM, June 3, 2008, <http://www.seacoastonline.com/apps/pbcs.dll/article?AID=/20080603/BIZ/806030377/-1/biz&sfad=1> (quoting Chief Justice John T. Broderick, Jr., New Hampshire Supreme Court).

want us to be competitive so that people have a real choice. Arbitration can be very expensive. The court system might be able to offer its own version of arbitration or mediation for less money. I am confident we can.”<sup>10</sup> Other judges likewise have identified competition from arbitration as a reason for the creation of business courts,<sup>11</sup> as have lawyers<sup>12</sup> and legal trade journals.<sup>13</sup>

This article examines the extent to which competition from business courts is likely to impact the future of arbitration.<sup>14</sup> Part II provides a brief overview of the growth of business courts in recent years. Part III sets out a structural comparison of arbitration with business courts, highlighting the similarities and differences between the two. Part IV provides empirical evidence on the relationship between the availability of business courts and the use

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<sup>10</sup> *A Conversation with the Chief Justice*, N.H. B. J. (2005), available at <https://secure.nhbar.org/publications/archives/display-journal-issue.asp?id=265> (quoting Chief Justice John T. Broderick, Jr., New Hampshire Supreme Court).

<sup>11</sup> *Making a Business Court a Reality*, METRO. CORP. COUNS., May 2003, at 47 (quoting Hon. Suzanne V. DeVecchio, Chief Justice, Massachusetts Superior Court) (“we were losing a body of law in Massachusetts because people were going to private dispute resolution versus keeping these cases in the court”); Mitchell L. Bach & Lee Applebaum, *A History of the Creation and Jurisdiction of Business Courts in the Last Decade*, 60 BUS. LAW. 147, 184 (2004) (“The [Nevada] Business Court thus provides another vehicle for dispute resolution, where the parties might otherwise choose private mediation or arbitration.”) (citing Letter from the Honorable Gene T. Porter to Mitchell L. Bach, Esquire (Sept. 19, 2003)).

<sup>12</sup> Lee Applebaum, *Complex Litigation Courts and Business Courts: Some Brief Observations on Connections and Similarities*, Aug. 13, 2007, <http://www.abanet.org/buslaw/newsletter/0063/materials/pp3.pdf> (“Under such circumstances [i.e., doubts about the court system’s reliability], litigants and lawyers may well turn to other forums (arbitration, mediation, federal court or even other states’ business courts) to obtain a greater sense of order and predictability. The specialized business court is aimed, in part, at reducing this doubt and stopping this flight.”); *A Specially Suited Forum for Business Cases*, METRO. CORP. COUNS., May 2003, at 50 (quoting Gael Mahony, co-chair of Business Litigation Session Resource Committee) (“When business clients are not comfortable with a court system they tend to move to alternative dispute resolution. For a case raising important issues that have ramifications beyond that case, a real loss results when the case goes to arbitration.”).

<sup>13</sup> *Musical Benches*, 147 N.J.L.J. 1250 (1997) (editorials) (“Increasing competition from alternative dispute resolution furnished the impetus for Essex County’s experiment. . . . It is an amusing illustration of Adam Smith’s invisible hand that the justice system has felt it necessary to improve efficiency in order to prevent consumers from flocking to the competition.”).

<sup>14</sup> The idea that business courts compete with arbitration is not a new one. Professor Tom Stipanowich made the point over a decade ago:

[Arbitration] may soon face increasing competition as an adjudicative alternative. The concept of a commercial court, long a fixture in many civil law jurisdictions, has recently spurred interest in the United States . . . . If the concept catches on and displaces much of private arbitration, it may represent a modern development akin in many respects to the absorption of equity by the common law courts.

Thomas J. Stipanowich, *Punitive Damages and the Consumerization of Arbitration*, 92 Nw. U.L. REV. 1, 50 n.277 (1997).

of arbitration clauses. Overall, the evidence provides little indication that parties are switching from arbitration to business courts. The evidence is far from definitive, however, and highlights the need for additional research on the topic.

## II. THE GROWTH OF BUSINESS COURTS

As defined by Ralph Peeples and Hanne Nyheim, “a business court means a division of a larger court (typically a trial court) with a jurisdiction limited to some, but not all, kinds of business disputes, presided over by only a few specialist judges, with an emphasis on aggressive case management and use of alternative dispute resolution (ADR).”<sup>15</sup> Other courts, which specialize in complex civil litigation generally, commonly are grouped together with business courts in discussions of the subject.<sup>16</sup>

Business courts are not new.<sup>17</sup> The oldest currently operating business court in the United States is also likely the best known—the Delaware Court of Chancery.<sup>18</sup> However, most business courts that are currently operating were established beginning in the 1990s.<sup>19</sup> Figure 1 shows the substantial growth in the cumulative number of business courts in the United States from 1992 to the present.<sup>20</sup>

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<sup>15</sup> Ralph Peeples & Hanne Nyheim, *Beyond the Border: An International Perspective on Business Courts*, BUS. L. TODAY, Mar.–Apr. 2008.

<sup>16</sup> See, e.g., Randall T. Shepard, *The New Role of State Supreme Courts as Engines of Court Reform*, 81 N.Y.U. L. REV. 1535, 1550 (2006) (“In other efforts to contribute to the business climate in their states, Nevada, New York, and others have created specialized business courts or complex litigation dockets.”).

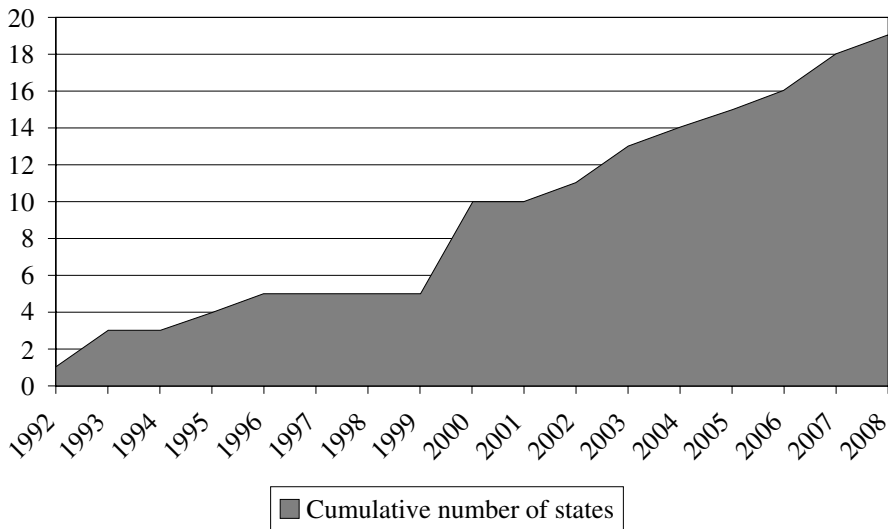
<sup>17</sup> Other countries also have specialized business courts, including a number that have established such courts in recent years. See, e.g., Peeples & Nyheim, *supra* note 15. Thus, although this paper focuses on domestic arbitration, analogous issues arise for international arbitration as well.

<sup>18</sup> Lee Applebaum, *The “New” Business Courts*, BUS. L. TODAY, Mar.–Apr. 2008 (“Delaware’s Court of Chancery remains the bright star in this firmament, and it sets the standard to which other courts aspire”). See generally William T. Quillen & Michael Hanrahan, *A Short History of the Delaware Court of Chancery—1792–1992*, 19 DEL. J. CORP. L. 819 (1993) (describing history of Delaware Court of Chancery).

<sup>19</sup> For a detailed recounting of these developments, see Bach & Applebaum, *supra* note 11.

<sup>20</sup> Figure 1 includes both specialized business courts and complex civil litigation courts. The dates used in Figure 1 are from Anne Tucker Nees, *Making a Case for Business Courts: A Survey of and Proposed Framework to Evaluate Business Courts*, 24 GA. ST. L. REV. 477, 505–11 (2007). In some cases, it might be possible to use different dates, but the results would not change materially. For another collection of information on business courts, see University of Cincinnati College of Law, Corporate Law Center, Summaries of Business and Complex Litigation

FIGURE 1. CUMULATIVE NUMBER OF STATES WITH BUSINESS COURTS AND COMPLEX LITIGATION COURTS



The statute creating the New Hampshire business court illustrates the sorts of cases commonly heard by business courts:

- (a) Claims arising from breach of contract or fiduciary duties, fraud, misrepresentation, business tort, or statutory violations arising out of business dealings or transactions.
- (b) Claims arising from transactions under the Uniform Commercial Code.
- (c) Claims arising from the purchase, sale, and lease of commercial real or personal property or security interests therein.
- (d) Claims related to surety bonds.
- (e) Franchisee/franchisor relationships and liabilities.
- (f) Malpractice claims of non-medical professionals in connection with rendering services to a business enterprise.
- (g) Real estate title petitions.
- (h) Shareholder derivative actions.
- (i) Commercial class actions.
- (j) Commercial bank transactions.

- (k) Actions relating to the internal affairs or governance; dissolution or liquidation rights[;] obligations between and among owners, including shareholders, partners, or members; or liability or indemnity of managers, including officers, directors, managers, trustees, or members or partners functioning as managers, of corporations, partnerships, limited partnerships, limited liability companies or partnerships, professional associations, business trusts, joint ventures, or other business enterprises.
- (l) Business insolvencies and receiverships.
- (m) Other complex disputes of a business or commercial nature.<sup>21</sup>

The actual number of cases heard by business courts varies widely. While some business courts have (relatively) large caseloads,<sup>22</sup> others, while approved, have never gotten off the ground<sup>23</sup> or have dwindled in size in recent years.<sup>24</sup>

Business courts vary in other respects as well. Some business courts have minimum amount-in-controversy requirements; others do not.<sup>25</sup> Some business courts have statewide jurisdiction or accept transfers from other courts in the state. Others are limited to particular counties (although commonly those counties are major commercial centers in the state).<sup>26</sup> Some business courts provide for automatic assignment of cases to the court; others require the motion of a party or the recommendation of a judge.<sup>27</sup> A common

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<sup>21</sup> N.H. REV. STAT. ANN. § 491:7-a (VI). For data on the breakdown of actual caseloads of business and complex litigation courts, see, e.g., National Center for State Courts, Evaluation of the Centers for Complex Civil Litigation Program 46 (June 30, 2003) (California), available at [http://www.ncsconline.org/wc/publications/res\\_busets\\_complexcivil litigationpub.pdf](http://www.ncsconline.org/wc/publications/res_busets_complexcivil litigationpub.pdf); *Roundtable: Corporate Counsel Applaud Session's Success*, METRO. CORP. COUNS., May 2003, at 56 (Massachusetts).

<sup>22</sup> Bach & Applebaum, *supra* note 11, at 163 (Cook, County, IL).

<sup>23</sup> Nees, *supra* note 20, at 510.

<sup>24</sup> Complex Civil Litigation Court Evaluation Committee, Minutes 2 (May 19, 2008), available at <http://www.supreme.state.az.us/courtserv/ComplexLit/CCLminutesmay192008.pdf> ("Specifically, from the inception of the program through 2003, 37 cases entered the program. In 2004, 2005, 2006, and 2007, the respective number of cases admitted to the program were 20, 12, 9, and 7. For 2008, to date, no new cases have gone into the complex program."). On January 22, 2009, the Arizona Supreme Court issued an administrative order extending the term of the pilot project until December 31, 2009. Admin. Order No. 2009-11 (Ariz. Sup. Ct., Jan. 22, 2009), available at <http://www.supreme.state.az.us/orders/admorder/Orders09/2009-11.pdf>.

<sup>25</sup> Nees, *supra* note 20, at 512-13.

<sup>26</sup> *Id.* at 513.

<sup>27</sup> *Id.* at 515.

theme, however, is the use by business courts of specialized judges and expedited procedures, as discussed in the next part.<sup>28</sup>

### III. STRUCTURAL COMPARISON BETWEEN BUSINESS COURTS AND ARBITRATION

In important respects, business courts seek to mirror key characteristics of the arbitration process, making it more likely that for at least some parties business courts may be an effective alternative to arbitration.<sup>29</sup> But business courts also differ from arbitration in important respects, some of which make business courts a more effective competitor and some of which make them a less effective competitor.

In summary form, business courts and arbitration can be compared as follows:

- Business courts and arbitration both involve decision makers who have specialized knowledge of business matters. Business court judges specialize in particular types of cases, and so can develop (and may already have) specialized knowledge of business matters.<sup>30</sup> Similarly, parties can choose arbitrators with specialized knowledge of business matters generally, or, indeed, industry-specific knowledge relevant to the dispute.<sup>31</sup>

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<sup>28</sup> See *infra* text accompanying notes 30–31.

<sup>29</sup> Thus, business courts would seem to fare well under the following approach, suggested by Landes and Posner:

Because arbitration is a voluntary service provided in a competitive market, it may appear that any procedures widely used in arbitration must be efficient procedures for deciding the type of dispute in question. If so, arbitration procedures can be used as a criterion for evaluating the efficiency of the public judicial system in areas such as contract and commercial law where most arbitrable disputes arise.

William M. Landes & Richard A. Posner, *Adjudication as a Private Good*, 8 J. LEGAL STUD. 235, 249 (1979).

<sup>30</sup> Governor's Task Force on Civil Justice Reform, Final Report, Report of the Committee on Business Courts 11, 11 (Colo. July 24, 2000), available at <http://www.state.co.us/cjrtf/report/report1.htm> [hereinafter cited as "Colorado Governor's Task Force"] ("expertise [in business law] may be found in judges who come from private practices focused on business law, and are therefore more adept at hearing commercial cases").

<sup>31</sup> David B. Lipsky & Ronald L. Seeber, The Appropriate Resolution of Corporate Disputes: A Report on the Growing Use of ADR by U.S. Corporations 17, 26 (1998) (reporting that 49.9% of survey respondents agreed that companies use arbitration because it "[u]ses [the] expertise of [the] neutral").

- Arbitration permits the parties to choose the individual or individuals who will resolve their dispute;<sup>32</sup> business courts do not.<sup>33</sup> Indeed, in some business courts, a judge controls whether to permit the case to be filed in, or transferred to, the business court.<sup>34</sup> Thus, parties retain greater control over the decision maker in arbitration than in business courts.
- Business courts and arbitration both seek to provide an expedited dispute resolution process. I am unaware of any empirical comparison of the time it takes to resolve disputes in arbitration and business courts.<sup>35</sup> Studies have found that creation of a business court tends to reduce how long it takes to resolve disputes as compared to how long it took prior to creation of the court.<sup>36</sup> Meanwhile, the increasing judicialization of arbitration, to the extent it is occurring,<sup>37</sup> presumably tends to make the time for resolving disputes in arbitration closer to the time it would take in litigation.
- Arbitration permits parties to avoid a queue (to some extent at least), depending on the person they choose as arbitrator. In business courts, parties still wait in line behind previously filed cases. To the extent parties choose arbitrators who already are serving as arbitrators on other cases, which seems likely, this advantage of arbitration is less significant.<sup>38</sup>
- Business courts have lower upfront fees than arbitration. In arbitration, parties must pay the arbitrators and the admin-

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<sup>32</sup> STEPHEN C. BENNETT, *ARBITRATION: ESSENTIAL CONCEPTS* 6 (2002).

<sup>33</sup> See, e.g., Final Report of the Committee to Study Complex Litigation 10–11 (Sept. 2002) (Arizona), available at <http://www.supreme.state.az.us/courtserve/ComplexLit/ComplexLitFinal.pdf> (describing case assignment practices).

<sup>34</sup> Nees, *supra* note 20, at 515; see, e.g., Admin. Order No. 2007-09-07-01 (S.C. Sept. 7, 2007), available at <http://www.sccourts.org/courtOrders/displayOrder.cfm?orderNo=2007-09-07-01> (“Assignment of cases to the business court may be made by the Chief Justice *sua sponte* or at the request of counsel.”).

<sup>35</sup> For a study comparing dispute resolution time (and cost) for arbitration to state and federal courts generally, see Herbert M. Kritzer & Jill K. Anderson, *The Arbitration Alternative: A Comparative Analysis of Case Processing Time, Disposition Mode, and Cost in the American Arbitration Association and the Courts*, 8 JUSTICE SYS. J. 6, 17 (1983) (finding that “the American Arbitration Association offers the possibility of relatively fast adjudication (compared to relatively slow nonadjudication in the courts)”).

<sup>36</sup> See, e.g., Bach & Appelbaum, *supra* note 11, at 154 (New York) & 162–64 (Cook County, IL).

<sup>37</sup> See *supra* text accompanying notes 1–4.

<sup>38</sup> CHRISTOPHER R. DRAHOZAL, *COMMERCIAL ARBITRATION: CASES AND PROBLEMS* 28 (2d ed. 2006).

istrative fees of any arbitration provider.<sup>39</sup> The government subsidizes the comparable costs in litigation; parties pay only a small filing fee.<sup>40</sup> The additional filing fees for business courts, if any, tend to be insignificant.<sup>41</sup> The more important question, of course, is not merely the upfront costs of the process, but the total costs of the process, including attorneys' fees.<sup>42</sup> There is likely to be a strong correlation between the time the process takes to resolve the dispute and the total cost.

- Arbitration enables parties to avoid juries.<sup>43</sup> Most business courts permit jury trials,<sup>44</sup> although parties may be able to waive their right to jury trial by contract.<sup>45</sup>
- Dispute resolution in business courts is a public process, with parties' privacy protected only by the power of the courts to enter protective orders. Arbitration is a private

<sup>39</sup> For a description of the fees for one arbitration provider (the American Arbitration Association), see Christopher R. Drahozal, *Arbitration Costs and Contingent Fee Contracts*, 59 VAND. L. REV. 729, 736–42 (2006).

<sup>40</sup> Stephen J. Ware, *The Case for Enforcing Adhesive Arbitration Agreements—with Particular Consideration of Class Actions and Arbitration Fees*, 5 J. AM. ARB. 251, 285 (2006).

<sup>41</sup> Miss. Sec'y of State, Div. of Pol'y & Research, Executive Summary of Business Courts/Complex Litigation Courts/Specialized Dockets by State or Local Jurisdiction 1–2 (July 17, 2008), available at [http://www.sos.state.ms.us/policy\\_research/Policy%20PDF/Business%20Courts%20Roundtable%20Discussion.pdf](http://www.sos.state.ms.us/policy_research/Policy%20PDF/Business%20Courts%20Roundtable%20Discussion.pdf). When business courts charge additional filing or transfer fees, the fees tend to be low. See, e.g., Report on Activities of the North Carolina Business Court 2 (2006–2008), available at <http://www.ncbusinesscourt.net/New/links/2008%20Report%20to%20General%20Assembly.Final.doc> (Notice of Designation for business court “is accompanied by a \$200 non-refundable fee”).

<sup>42</sup> Drahozal, *supra* note 39, at 733–34.

<sup>43</sup> Christopher R. Drahozal, *A Behavioral Analysis of Private Judging*, 67 LAW & CONTEMP. PROBS. 105, 105 (2004).

<sup>44</sup> For an exception, see Notice to the Bar Re: Pilot Program for Handling Complex Commercial Cases in General Equity (N.J. June 21, 2004), available at <http://www.judiciary.state.nj.us/notices/n040624a.htm> (“Criteria for transfer into the pilot program are: . . . a written waiver of jury trial signed by all parties and their attorneys must accompany the request.”).

<sup>45</sup> Stephen J. Ware, *Arbitration Clauses, Jury-Waiver Clauses and Other Contractual Waivers of Constitutional Rights*, 67 LAW & CONTEMP. PROBS. 167 (2004). Eisenberg and Miller found that most of the corporate contracts they studied did not include a clause waiving the right to jury trial. Theodore Eisenberg & Geoffrey P. Miller, *Do Juries Add Value?: Evidence from an Empirical Study of Jury Trial Waiver Clauses in Large Corporate Contracts*, 4 J. EMPIRICAL LEGAL STUD. 539 (2007) (finding only twenty percent of contracts in sample included a jury trial waiver). One possible explanation for their results is that disputes arising out of the types of contracts they studied typically may result in claims for equitable relief, and hence no right to jury trial. See, e.g., Theodore Eisenberg & Geoffrey Miller, *Ex Ante Choices of Law and Forum*, 59 VAND. L. REV. 1975, 1982 (2006) (“disputes in merger contracts often will be resolved through equitable relief (for example, a motion for a preliminary injunction)”).

process and more likely to result in a confidential resolution of the parties' dispute.<sup>46</sup>

- Parties in business courts, like parties in other courts, have a right to appeal. Arbitration typically does not have an appeals process, unless the parties agree by contract to create one.<sup>47</sup> Courts review arbitration awards only on narrow, usually procedural, grounds,<sup>48</sup> and the United States Supreme Court has curtailed the ability of parties to expand that review by contract.<sup>49</sup>
- Business courts often, although not always, publish opinions that serve as precedent.<sup>50</sup> Arbitration awards ordinarily are not published and do not have any binding precedential effect.<sup>51</sup>

Overall, this discussion suggests the following: (1) business courts seek to emulate some of the characteristics parties most prefer about arbitration; (2) business courts are a closer substitute for arbitration than nonspecialized courts; (3) arbitration retains some advantages over business courts, while business courts retain some

<sup>46</sup> Noyes, *supra* note 8, at 589–91 (“arbitration is more confidential than litigation”) (citing *Union Oil Co. v. Leavell*, 220 F.3d 562, 568 (7th Cir. 2000)) (“People who want secrecy should opt for arbitration. When they call on the courts, they must accept the openness that goes with subsidized dispute resolution by public (and publicly accountable) officials.”).

<sup>47</sup> Christopher R. Drahozal, *Judicial Incentives and the Appeals Process*, 51 *SMU L. REV.* 496, 501 (1998).

<sup>48</sup> *Id.*; *see, e.g.*, 9 U.S.C. § 10 [2009].

<sup>49</sup> *Hall Street Assocs., L.L.C. v. Mattel, Inc.*, 128 S. Ct. 1396, 1400 (2008). *But see* *Cable Connection, Inc. v. DirectTV, Inc.*, 190 P.3d 586, 589 (Cal. 2008) (holding that parties can contract for expanded review as a matter of state law, and that the FAA does not preempt the state law rule); *Edstrom Indus. v. Companion Life Ins. Co.*, 516 F.3d 546, 552–53 (7th Cir. 2008) (distinguishing *Hall Street* and holding that arbitrator exceeded authority by ignoring state law when arbitration clause required arbitrator to “strictly apply rules of law applicable” to the contract).

<sup>50</sup> Nees, *supra* note 20, at 521 (“About one-half of the states publish business court opinions on the court’s website or in some other fashion. This is notable because trial court-level opinions are rarely published.”). Indeed, the creation of precedent is one of the reasons often cited for the establishment of business courts. *See, e.g.*, Colorado Governor’s Task Force, *supra* note 30, at 15 (concluding that “[c]reating a business court could . . . provide an opportunity to develop a body of common law for commercial cases,” and noting that “[t]he trend toward resolving commercial cases outside the judicial system exacerbates this scarcity of [business law] precedent”).

<sup>51</sup> Richard M. Alderman, *Consumer Arbitration: The Destruction of the Common Law*, 2 *J. AM. ARB.* 1, 11 (2003) (“Unlike court opinions, which are published, most decisions of arbitrators are kept secret, often not even accompanied by a written opinion. Even when published and made available to the public, the decision of one arbitrator, or a panel of arbitrators, is in no way binding on any other arbitrator or panel.”). Of course, the precedential value of a decision tends to be external to the parties to the case, such that they may have insufficient incentive to agree to dispute resolution processes that create precedent. Landes & Posner, *supra* note 29, at 238–39.

of the same advantages courts have over arbitration; and (4) the extent to which parties choose business courts over arbitration likely will vary with the type of contract and type of dispute because the importance of the factors described above varies with the type of contract and type of dispute.<sup>52</sup>

#### IV. EMPIRICAL ANALYSIS

As the previous Part suggests, the availability of business courts no doubt will influence at least some parties not to include arbitration clauses in their contracts. The important question for the future of arbitration is how many parties will switch from arbitration as a result of competition from business courts.<sup>53</sup> This Part offers some simple empirical insights into that question, based on an examination of the use of arbitration clauses in several different types of contracts.<sup>54</sup>

##### A. Corporate Transactions

A dispute arising out of a corporate financing transaction or merger would seem to be the paradigmatic case for a business court to decide, and such cases certainly would be within the jurisdiction of business courts.<sup>55</sup> The resolution of such cases by business courts, however, is likely to have little effect on the future of arbitration because few such contracts currently include arbitration clauses.

A recent study by Theodore Eisenberg and Geoffrey Miller examined a sample of over 2800 contracts submitted by businesses as exhibits to their filings with the Securities and Exchange Com-

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<sup>52</sup> For a more general discussion of this point, see Drahozal & Ware, *Why Do Businesses Use (and not Use) Arbitration Clauses?* (Jan. 2, 2009) (unpublished manuscript, on file with author).

<sup>53</sup> Another way to formulate the question is: what proportion of the caseload of business courts comes from (1) cases that otherwise would be filed in court; (2) cases that otherwise would be filed in arbitration; and (3) cases that otherwise would not be brought at all. Such an empirical undertaking is beyond the scope of this article.

<sup>54</sup> The types of contracts were selected solely on basis of the availability of data on those types of contracts.

<sup>55</sup> Nees, *supra* note 20, at 505–10 (listing subject matter of cases within jurisdiction of business courts).

mission in 2002.<sup>56</sup> Eisenberg and Miller found what they characterized as a “surprisingly low frequency of arbitration clauses”—10.6% in the entire sample—in the contracts studied.<sup>57</sup> Table 1 summarizes their findings for particular types of contracts, including merger agreements, credit commitments, and underwriting agreements. Given the low percentages of such contracts that include arbitration contracts,<sup>58</sup> the availability of business courts seems likely to have little effect on the future use of arbitration to resolve disputes arising out of those contracts.<sup>59</sup>

## B. Executive Employment Contracts

A second type of contract commonly included within the jurisdiction of business courts is employment contracts.<sup>60</sup> The expertise

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<sup>56</sup> Theodore Eisenberg & Geoffrey Miller, *The Flight from Arbitration: An Empirical Study of Ex Ante Arbitration Clauses in the Contracts of Publicly Held Companies*, 56 *DEPAUL L. REV.* 335, 335 (2007).

<sup>57</sup> *Id.* An important reason for the low frequency of arbitration clauses was the types of contracts Eisenberg and Miller studied. See Drahozal & Ware, *supra* note 52.

<sup>58</sup> A small percentage of contracts with arbitration clauses does not necessarily mean that a small percentage of arbitrations arise out of such contracts. The available evidence, however, albeit only from international arbitration, suggests that disputes arising out of corporate financing and restructuring transactions do not make up a substantial percentage of arbitrated cases. For example, the only type of contract in the Eisenberg and Miller sample listed as commonly giving rise to arbitrations before the International Court of Arbitration of the International Chamber of Commerce in 2007 was shareholding agreements, which gave rise to 8.3% of ICC arbitrations. 2007 *Statistical Report*, ICC INT’L CT. ARB. BULL. 5, 8 (Spring 2008).

<sup>59</sup> That said, it is possible that the limited use of arbitration clauses in such contracts at present is, at least in part, a consequence of the existence of business courts. During the period studied by Eisenberg and Miller, business and complex litigation courts existed in Delaware, New York, and California, the top three states chosen in forum selection clauses in merger agreements in the sample. See Eisenberg & Miller, *supra* note 56, at 365 tbl. 10 (reporting that 65.28% of merger agreements provided for disputes to be resolved in court in Delaware, New York, or California). Indeed, one reason given for the creation of a business court in New York in the 1990s was to stop the flight of cases from New York courts to other forums, including arbitration. See Boston Bar Ass’n, BBA Public Policy—Adjudication of Complex Commercial Cases, available at [www.bostonbar.org/pp/bbaia/fl/rogers\\_proposal.htm](http://www.bostonbar.org/pp/bbaia/fl/rogers_proposal.htm) (last visited Jan. 22, 2009) (Prior to creation of New York’s Commercial Division, “the New York community had become increasingly dissatisfied with its state courts, and members were voting with their feet, going to Delaware whenever they could, or to federal court, or to private litigation.”) Eisenberg and Miller’s study did not address this possibility because it did not examine the change in the use of arbitration clauses over time. Of course, an important reason for the limited use of arbitration clauses was the types of contracts studied by Eisenberg and Miller. Drahozal & Ware, *supra* note 52,.

<sup>60</sup> See, e.g., 22 N.Y.C.R.R. § 202.70(b)(1) (“employment agreements not including claims that principally involve alleged discriminatory practices”); *Notice to Bar*, 29 *MASS. LAW WEEKLY* 268, ¶ a (Oct. 2, 2000) (“employment agreement disputes”).

TABLE 1. USE OF ARBITRATION CLAUSES BY CONTRACT TYPE

Contract Type	No Arbitration Clause	Arbitration Clause	n
Mergers	81.02%	18.98%	411
Securities purchase	88.26%	11.74%	460
Asset sale purchase	80.57%	19.43%	314
Credit commitments	97.69%	2.31%	216
Underwriting	99.72%	0.28%	351
Bond indentures	99.35%	0.65%	155

of business courts would seem to be especially useful for disputes arising out of one type of employment contract in particular—contracts between businesses and their executives. The available empirical evidence suggests, however, that if anything, the use of arbitration clauses in executive employment contracts is increasing in recent years, not decreasing. As one study reported:

Whereas a total of 50.5% of the contracts in our sample include an arbitration provision, this masks an upward trend in the use of arbitration over time from a low of 35.9% of contracts in 1997 to 60.4% of contracts in 2005. A simple linear regression of the percent of contracts containing arbitration each year against time indicates a statistically significant upward slope (t-statistic on slope = 3.84).<sup>61</sup>

The likely explanation stems from an important difference between arbitration and business courts—arbitration provides a greater degree of confidentiality for the parties<sup>62</sup>—which is likely to be particularly important for disputes between corporations and their executives.<sup>63</sup>

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<sup>61</sup> Randall Thomas et al., *When Do CEOs Bargain for Arbitration?: A Theoretical and Empirical Analysis* 21 (Vanderbilt Law of Econ., Working Paper No. 08-23, 2008), available at <http://www.ssrn.com/abstract=1247843>.

<sup>62</sup> See *supra* text accompanying note 46.

<sup>63</sup> Theodore Eisenberg, Geoffrey P. Miller & Emily Sherwin, *Arbitration's Summer Soldiers: An Empirical Study of Arbitration Clauses in Consumer and Nonconsumer Contracts*, 41 U. MICH. J.L. REFORM 871, 887–88 (2008)

In the case of employment contracts, we conjecture that both parties perceive a need for confidentiality in the resolution of the dispute. The senior employees covered by these contracts are often in the public eye. Neither the employer nor the employee stands to gain in terms of reputation [if] the dirty linen of their dispute is aired in public.

*Id.*

## C. Franchise Agreements

Disputes arising out of franchise agreements also likely fall within the jurisdiction of business courts.<sup>64</sup> This section uses a sample of dispute resolution clauses from the 2007 franchise agreements of leading franchisors to examine whether the availability of business courts affects franchisor choice of dispute resolution forum.<sup>65</sup> The study finds no evidence of any effect.

First, none of the dispute resolution clauses themselves gives any indication that the availability of a business court influenced the franchisor's choice between arbitration and litigation. No franchise agreement specified a business court as the forum for resolving disputes. To the contrary, three of eight (or 37.5%) of the exclusive forum selection clauses from franchisors in jurisdictions with business courts specified that the dispute was to be resolved in federal court if that court had subject matter jurisdiction. Business courts, of course, are state courts.

Second, franchisors located in states with business courts are statistically no more likely to use an exclusive forum selection clause in their franchise agreements than to use an arbitration clause.<sup>66</sup> Table 2 shows that 25% (8 of 32) of franchisors in jurisdictions with business courts included exclusive forum selection clauses, while 16.7% (5 of 30) included arbitration clauses, a difference that is not statistically significant.<sup>67</sup> The results are similar when complex litigation courts are also included, as shown in Table 3.<sup>68</sup>

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<sup>64</sup> See, e.g., N.H. REV. STAT. ANN. § 491:7-a (VI)(e) ("Franchisee/franchisor relationships and liabilities").

<sup>65</sup> For a more detailed description of the sample, see Christopher R. Drahozal & Quentin R. Wittrock, *Is There a Flight from Arbitration?*, 37 *HOFSTRA L. REV.* 71, 90-94 (2008).

<sup>66</sup> In Tables 2 and 3, the franchisor was classified as being from a jurisdiction with a business court when either (1) the business court had statewide jurisdiction and the franchisor's home office was in the state; or (2) the business court had county-wide jurisdiction and the franchisor's home office was in the county. Expanding the latter category to include franchisors located in the same state as the business court (rather than only in the same county) does not materially affect the results.

<sup>67</sup> The Pearson's Chi-squared statistic is 0.649 (DF = 1 and  $p = 0.421$ ), which does not allow rejection of the null hypothesis that choice of dispute resolution forum is not associated with whether the franchisor is located in a jurisdiction with a business court.

<sup>68</sup> The Pearson's Chi-squared statistic is 0.186 (DF = 1 and  $p = 0.667$ ), which does not allow rejection of the null hypothesis that choice of dispute resolution forum is not associated with whether the franchisor is located in a jurisdiction with a business or complex litigation court.

TABLE 2. DISPUTE RESOLUTION CLAUSE CHOSEN BY  
FRANCHISORS LOCATED IN JURISDICTIONS WITH  
AND WITHOUT BUSINESS COURTS

	<b>Business Court</b>	<b>No Business Court</b>
<b>Arbitration Clause</b>	5 (16.7%)	25 (83.3%)
<b>Exclusive Forum Selection Clause</b>	8 (25.0%)	24 (75.0%)

TABLE 3. DISPUTE RESOLUTION CLAUSE CHOSEN BY  
FRANCHISORS LOCATED IN JURISDICTIONS WITH AND  
WITHOUT BUSINESS COURTS OR COMPLEX  
LITIGATION COURTS

	<b>Business/Complex Litigation Court</b>	<b>No Business/ Complex Litigation Court</b>
<b>Arbitration Clause</b>	7 (22.6%)	23 (77.4%)
<b>Exclusive Forum Selection Clause</b>	9 (28.1%)	23 (71.9%)

Third, changes in the use of arbitration clauses between 1999 and 2007 reveal no influence of the growth of business courts over that period. In 1999, 45.1% of the franchise agreements included arbitration clauses; in 2007, 43.8% of the franchise agreements included arbitration clauses.<sup>69</sup> The net change was that only one fewer franchise agreement included an arbitration clause in 2007 than in 1999.<sup>70</sup>

The very small overall change in the use of arbitration clauses masks some changes in the use of arbitration clauses by individual

<sup>69</sup> Drahozal & Wittrock, *supra* note 65, at 95.

<sup>70</sup> Even that difference likely overstates the aggregate change. Quick Lube, one of the franchisors in the 1999 sample, merged with Jiffy Lube, another of the franchisors in the sample. The Quick Lube franchise agreement included a forum selection clause, while the Jiffy Lube franchise agreement included an arbitration clause. After the merger, all of the Quick Lube franchises were converted to Jiffy Lube franchises. Because Quick Lube no longer exists as an independent entity, it is not included in the 2007 sample, but Jiffy Lube is included in the sample. Effectively, the result of the merger is that the franchise agreements for all the Quick Lube franchisees will (eventually) be switched from forum selection clauses to arbitration clauses, although that fact does not appear in the results. *Id.* at 94–95.

franchisors in the sample. Four franchisors that used arbitration clauses in 1999 had switched to exclusive forum selection clauses by 2007. Meanwhile, five franchisors that did not have any dispute resolution clauses in 1999 added dispute resolution clauses by 2007. Three of those franchisors added an arbitration clause, one added an exclusive forum selection clause, and one added a non-exclusive forum selection clause. Thus, while in the aggregate only one fewer franchisor used an arbitration clause in 2007, four franchisors in fact switched from arbitration clauses to exclusive forum selection clauses and three switched from no dispute resolution clauses to arbitration clauses.<sup>71</sup>

Examining the switching franchisors provides no indication that the availability of business courts influenced the decisions to switch. Of the four franchisors that replaced arbitration clauses with exclusive forum selection clauses between 1999 and 2007, one specified the court where the franchisee was located; two specified the franchisor's home state, which did not have a business court; and one specified the franchisor's home state, which had a business court but specified that federal court, rather than state court (i.e., the business court), was the preferred forum.

By comparison, three of the five franchisors that had added a dispute resolution clause to their franchise agreement by 2007 were located in jurisdictions with business courts.<sup>72</sup> Only one of the three added an exclusive forum selection clause; that clause specified that any dispute was to be resolved in federal court if that court had subject matter jurisdiction. Another added an arbitration clause, while the third added a nonexclusive forum selection clause, permitting but not requiring litigation to take place in the specified forum.

Certainly, the choice between arbitration and litigation is more complex than this analysis reflects.<sup>73</sup> At the very least, however, this analysis finds no evidence that the availability of business courts is influencing franchisor choice between arbitration and litigation.

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<sup>71</sup> *Id.* at 96–97.

<sup>72</sup> The other two were located in the same state as a business court, but not in the same county. Those franchisors both added arbitration clauses to their franchise agreements.

<sup>73</sup> For a more sophisticated empirical analysis, see Christopher R. Drahozal & Keith N. Hylton, *The Economics of Litigation and Arbitration: An Application to Franchise Contracts*, 32 J. LEGAL STUD. 549 (2003).

V. CONCLUSION: BUSINESS COURTS AS  
COMPETITORS TO ARBITRATION

The future of arbitration depends not only on arbitration but also on its competitors—the public courts, including business courts. The creation of business courts incorporates some of the preferred characteristics of arbitration (in particular, expert decision making and expedited case management) into litigation, making litigation a more effective competitor to arbitration. Litigation in business courts has some advantages over arbitration (such as lower upfront costs), while arbitration retains some of its advantages over litigation (such as choice of decision maker and confidentiality).

Given this structural comparison, one would expect on the margin for business courts to make litigation a more attractive forum for resolving business disputes than arbitration. But the limited empirical evidence available does not show any significant move away from arbitration to business courts as yet. Certainly the analysis here does not resolve as an empirical matter the potential effect of business courts on the future of arbitration. Rather, my hope is to begin the discussion, and to prompt others to examine the issue more systematically.

