New York Law Journal

NEW YORK LAW JOURNAL SPECIAL REPORT

An ALM Publication

Alternative Dispute Resolution

WWW.NYLJ.COM

VOLUME 259—NO. 52

MONDAY, MARCH 19, 2018

Five Reasons to Include Arbitration Clauses in Business Contracts ... And Five Reasons to Reconsider

BY JENNIFER B. ZOURIGUI

SHUTTERSTOCK

Whether a dispute will be litigated or arbitrated is usually determined long before the dispute even arises—at the time a contract is negotiated, drafted, and executed. Companies and practitioners alike routinely include an arbitration provision in business contracts as an almost knee-jerk reaction during the drafting process. Arbitration is often thought of as faster, cheaper, and less risky. But is this accurate? And is this "one size fits all" attitude of inserting arbitration clauses in most business contracts really the best approach to the resolution of disputes that arise out of business transactions? There are sometimes advantages to arbitration over litigation but there also can be disadvantages in arbitration. Both warrant discussion and evaluation prior to the selection of a forum.

JENNIFER B. ZOURIGUI *is a partner at Ingram Yuzek Gainen Carroll & Bertolotti.*

Five Advantages of Arbitration

(1) Participation in the selection of the arbitrator(s). Unlike the process in court where a judge is typically randomly assigned to each case, the parties to an arbitration have an opportunity to participate in the selection of the arbitrator or the panel of arbitrators. Whether through joint agreement or selection by ranking, you have an opportunity to consider which arbitrators you think will be the best fit. This can be of great value if a party is able to, for example, select or eliminate arbitrators with experience in a particular field or whose background

you believe may lead to a disadvantageous perspective. Resumes are typically provided to parties and other research regarding the arbitrator can be beneficial as well, such as reviewing articles the arbitrator may have authored or analyzing the types of speaking engagements in which he or she participated. By talking with colleagues that have had firsthand experience with the arbitrator, information about the arbitrator's approach to the process can be gleaned. This can include, for instance, attitude towards discovery disputes or dispositive motions. Whatever approach parties and their attorneys take in the arbitrator selection process, there is a strategic decision to be made with arbitration that would be unavailable in the courtroom.

(2) Faster process. A large component of the litigation process is discovery. It can be time consuming and very costly. But discovery in connection with an arbitration can be much more limited either by the arbitration rules, the arbitrator, or even by limits set forth by the parties in the arbitration agreement. The result can be a much faster process with less burdensome document discovery and the absence of other discovery tools such as depositions. Motion practice, another time consuming aspect of litigation, can also be more limited—or not permitted at all—in an arbitration. Absent motion practice, such as dispositive motions, the arbitrator can set more compressed deadlines than litigation in the courthouse might dictate.

(3) Lower costs. Less discovery and fewer motions not only speed up the process but it can lower the overall costs. Tighter reigns on discovery can reduce the attorney's workload for review and can also help keep discovery disputes to a minimum. Also, with the removal of certain customary components of litigation, such as dispositive motions, attorneys' fees can be much lower than a long protracted litigation.

While you cannot foresee all the possible scenarios that could occur, it is well worth pausing and questioning whether an arbitration provision really belongs in a particular business agreement.

(4) More comfortable setting. Whereas litigants are bound by courtroom formalities, arbitration typically takes place in more informal surroundings. Conferences with the arbitrator usually occur by telephone and the arbitration hearing is scheduled in a conference room. The more informal setting can be less intimidating to the client and other witnesses. While the arbitration hearing is still formal, parties may feel more at ease to express themselves in less formal surroundings. (Of course, whether this will be a benefit with your client is something that may be tough to determine before a dispute even arises.)

(5) Privacy. Arbitration also offers a more private forum for resolution of the dispute. Unlike pleadings in litigation, arbitration filings are not made through a public filing system. Also, non-parties to the arbitration agreement do not attend the hearings absent consent of the arbitrator and the parties. This can all help in keeping unwanted attention away from the parties and the dispute. This does not mean that the arbitration or the decision are confidential, but the parties can include a confidentiality provision in the arbitration clause for those businesses where confidentiality, or particular confidential information, is a concern.

Overall, there are significant benefits to arbitrating claims. But before deciding to agree to arbitrate, the risks or disadvantages of arbitration should also be discussed.

Five Disadvantages of Arbitration

(1) Unpredictability. While much of the detail regarding how the arbitration will flow can be set forth in an arbitration clause long before any dispute arises, most arbitration clauses stick to designating arbitration in a certain location or through a certain arbitration association. Since the rules for

arbitration are often more flexible than civil procedure rules, there is more room for attorneys to find things to fight about. And without a firm set of rules, or even a large body of case law, to rely on, there can be uncertainty and unpredictability as to how an arbitrator will rule on these procedural matters.

(2) Limitations on the process. Litigation offers multiple avenues to discover information before trial, including document discovery, depositions, and interrogatories. Limited discovery in an arbitration proceeding may move the process along at a faster pace, but it can also prevent the attorney from gaining valuable pre-hearing ammunition. Limited discovery can thwart a full understanding and evaluation of an adversary's strengths and weaknesses.

(3) Cost may be higher than anticipated. Parties to an arbitration are often less inclined to reach an early settlement given the general belief that the arbitration process will be faster and cheaper than litigation. Arbitrators may also be less inclined to entertain dispositive motions. Therefore, arbitration is less likely to yield an early resolution and although potentially shorter than a litigation through trial and appeal, the costs of arbitration can be higher than clients may expect. Clients are often surprised to learn that they must contribute to the cost of not just the filing of the arbitration but also the arbitrator's fees. Depending on the complexity of the matter, arbitrator's fees can be quite substantial. Discovery in an arbitration also may not be as streamlined as imagined. Depositions may be permitted. Electronic discovery is becoming the norm in commercial disputes and, even if narrowed by the arbitrator, can still lead to large quantities of documents to be reviewed. All of this can contribute to a very expensive arbitration.

(4) The decision is non-appealable. Courts give tremendous deference to arbitrators and the awards they issue. Arbitration awards can be vacated or modified only upon very limited grounds. Under the New York Civil Practice Law and Rules, those grounds are: (1) corruption, fraud, or misconduct; (2) partiality of the arbitrator; (3) the arbitrator exceeded his or her power; or (4) failure to follow the procedures of Article 75 of the CPLR. The Federal Arbitration Act gives similar deference to arbitrators and also provides limited grounds for vacating an award. Thus, absent a showing of fraud, bias, bad-faith or misconduct, a court is unlikely to overturn an arbitration award.

(5) The arbitrator is not bound by the law. Notably absent from the limited grounds upon which a court may vacate an arbitration award is errors of law by the arbitrator. There is also no ground for vacating or modifying an award if an arbitrator deviates from a contract's plain language. Therefore, unlike the appeal process available in litigation, if a party believes the arbitrator got it wrong, recourse is limited and that decision will likely still stand. This can be shocking to a client and a difficult conversation for an attorney to have with them if the arbitration award takes an unexpected turn.

There are drawbacks to arbitration that should not be ignored. Including an arbitration clause in business contracts as a mere habit in the drafting process can be risky. Whether a dispute should be litigated or arbitrated is not a simple question and the answer is not black and white. The type of claims that can arise out of the contract at issue, as well as the parties to the contract and their respective businesses, should all be carefully examined and discussed on a case-by-case basis when deciding if arbitration is appropriate. While you cannot foresee all the possible scenarios that could occur, it is well worth pausing and questioning whether an arbitration provision really belongs in a particular business agreement.