Debunking Misperceptions

The Upsides of Commercial Arbitration

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Arbitration sometimes gets a bad rap. Critics challenge provisions that bar a consumer or employee from pursuing an individual lawsuit or class action. They gripe about the privatization of our justice system, the secrecy of the proceedings, and the at times arbitrary conduct of arbitrators. Some judges question the fundamental effectiveness and legitimacy of the entire process.

Proponents point to the beneficial attributes of arbitration, which led the American Bar Association earlier this year to adopt a resolution supporting its use as an efficient and economical method of resolving business-to-business disputes. Supporters also note the increasingly widespread use of commercial arbitration by the business community, illustrated by an American Arbitration Association (AAA) report finding that in 2019, and again in 2020, nearly 10,000 commercial arbitrations were filed, with aggregate claims each year totaling about $18 billion.

Detractors push back. They say that not all perceived advantages of commercial arbitration truly exist. They note that arbitrating a dispute can be more expensive and time-consuming than litigating in court. Some criticize the lack of an automatic review mechanism.

Much of the current controversy focuses on the use of arbitration to resolve consumer complaints and employment disputes. There are legitimate questions about the fairness and enforceability of forced arbitration agreements, some featuring class action waivers. Those issues deserve careful scrutiny.

But attempts by some skeptics to paint all forms and aspects of arbitration with a broadly negative brush stack the deck. Without acknowledging any of its benefits, they risk undermining the business community's positive perceptions about a process that has proven effective and efficient at resolving commercial disputes.

Business arbitration should be evaluated on its own merits. Let's start with this premise: Neither arbitration nor litigation is best suited for every commercial dispute. But that doesn't mean that those charged with selecting a dispute resolution process should just flip a coin to choose between them. The distinctions are significant, and the potential ramifications of choosing one over the other are substantial and may affect the outcome.

A series of simple questions designed to flesh out which process is best for resolving a particular type of dispute suggests that commercial arbitration is a viable and often preferable choice for resolving business-to-business disputes. Much of what others perceive as its failings are in fact among its virtues. Let's test that proposition.

Assume a transaction between two commercial entities engaged in the sale and purchase of goods or services. A monetary dispute arises over whether the seller breached the contract,

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which does not specify a method of dispute resolution. Each side is open to litigating or arbitrating the dispute. Their business representatives meet, along with their counsel, to try to reach consensus on the forum that would best suit their needs. The attorneys begin to pose questions to their clients.

Questions

Is it important to be able to select who will decide your dispute?

"Absolutely," says the seller. Participating in the selection inspires confidence that the decision maker has the requisite background, experience, and temperament to be fair. It removes any lingering doubt that the seller's fate would be placed in the hands of a randomly assigned judge or jury unfamiliar with the nature of his business and the subtleties of the dispute.

The purchaser agrees. She would have more faith in a process that gives her a direct say in who decides her case.

It's impossible to overstate the importance of being able to participate in the selection of the decision maker. No one doubts that a litigation plaintiff will try to pick a favorable venue or that the defendant may seek to transfer or remove a case if there is a perceived advantage in doing so. In court, judge shopping is anathema. But in arbitration, vetting potential candidates and selecting one or more with the most appropriate credentials are not just expected but encouraged.

Sophisticated parties properly devote considerable time and effort to the selection process. That may include speaking to colleagues who are familiar with the candidates, their experience, and their reputations; conferring with counsel who appeared before them in other proceedings; reviewing their curricula vitae, websites, publications, and speaking engagements; obtaining

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detailed written disclosures of their existing and previous contacts with the parties, counsel, and potential witnesses to preclude disqualifying conflicts of interest; and even participating with adverse counsel in interviewing the finalists. Taking comparable ownership of the dispute-resolution process in court by selecting the decision maker is simply not possible.

Should your dispute be decided by someone with the knowledge, experience, and expertise to fully understand it?

"That must be a rhetorical question," says the seller. "Of course, it should." The factual and industry-specific background may be fairly complicated. The seller wants assurance that the decision maker can comprehend the relevant plans and specifications, and has heard other cases involving similar issues. Again, the purchaser agrees. If she were not confident in the validity of her position, she would settle rather than fight. She wants to know she has a decent chance of obtaining a result that is consistent with her reasonable business expectations.

In arbitration, the parties' ability to screen for qualified decision makers enhances the likelihood that the dispute will be decided on its merits and not skewed by a misunderstanding of a piece of evidence or a subjective evaluation of the appearance or demeanor of a witness. Of course, that expertise comes at a cost. The parties pay the arbitrator's fees. In court, by contrast, the parties don't pay for the time spent by the judge or jury. But isn't the additional cost of compensating a skilled arbitrator worth it, especially taking into account the attorney fees that can be saved by participating in a process generally accompanied by less discovery and motion practice, and managed by a well-trained and knowledgeable decider?

Arbitration also provides the parties with options to limit their expenses for arbitrator compensation. Arbitrator billing rates are readily available and vary widely. Parties can save costs by selecting a single arbitrator rather than a panel. Sometimes the parties can have the best of both worlds. Programs such as the AAA's Streamlined Three-Arbitrator Panel Option provide that the panel chair will handle all prehearing matters solo until shortly before the evidentiary hearing. If the other two panelists are selected at the outset, they can be activated later, soon before the hearing; if not, they can be chosen as the hearing approaches. Similar savings can be achieved merely by agreeing that the panel chair will resolve all prehearing discovery disputes.

Is the only way to get a fair shake to have your dispute decided by a judge or a jury?

Having never participated in an arbitration, both parties look to their counsel for advice in responding. Court proceedings are dramatized on television and in the movies. Neither the purchaser nor the seller recalls seeing a single show featuring an arbitrator.

To be sure, most civil lawsuits are litigated in state courts. In many of those jurisdictions, judicial candidates are nominated, with significant input from political parties, and then elected by the public. That doesn't mean those judges lack the requisite knowledge, skill, and independence to decide cases correctly; but it also doesn't ensure that a judge is better equipped to reach a proper result than a well-trained, experienced arbitrator.

The judge's legal experience may have been in an area of the law far removed from the subject of the dispute. A judge whose previous experience was as a divorce lawyer may not be the best choice for a complex commercial case. By contrast, arbitrators on the panels of the AAA, JAMS, and other leading institutional providers are drawn from the ranks of accomplished attorneys and former judges with credentials in specific areas, as well as industry experts and business owners.

Federal district court cases took more than 12 months longer to get to trial than disputes resolved by arbitration.

As their awards generally cannot be overturned for legal error, arbitrators are sometimes characterized as being above the law. But there is no evidence that arbitrators disregard the law or make legal mistakes with any greater frequency than do judges. Most commercial arbitrators have had distinguished careers as attorneys or judges and fully understand the importance of following the law. They are keenly aware that the contracts they are being asked to interpret generally contain choice-of-law provisions, requiring them to apply the laws of a particular state, and that they are obligated to enforce the parties' selection of the governing law. And issuing an award inconsistent with applicable law would impair an arbitrator's reputation and be bad for business.

Is it better to engage in a process that automatically includes appellate review, permitting the loser to challenge and possibly overturn the decision?

The seller says he's not interested in a process that allows a second bite at the apple. He's practical. Once each side has had a fair chance to present its case and the dispute has been decided, it should be over. The purchaser says she just wants the opportunity to show why she's right and the seller is wrong.

She's not looking to create new case law precedents. The losing party needs to accept the result and move on. That's something astute business executives understand.

Trial court determinations are, of course, subject to appeal. In some jurisdictions, even pretrial rulings can be appealed on an interlocutory basis, so any case could involve multiple appeals. Appeals can add years to the final disposition of a dispute and dramatically increase costs. In arbitration, the emphasis is on efficiency, certainty, and finality, which have a lot of value and appeal to businesses. An alternative dispute resolution process cannot accomplish those goals and, at the same time, accommodate an automatic fresh review after the parties have presented their cases and an award has been issued.

While the grounds for setting aside an arbitration award are extremely limited, the losing party is not entirely without recourse. If an award is infected by bias or corruption, or reflects that the arbitrator has exceeded his or her authority, the award generally can be scrutinized by the court on a motion to vacate. Also, in many jurisdictions, an award can be set aside for manifest disregard of the law, even when that is not specifically mentioned as a statutory basis.

Selecting an arbitrator familiar with the subject of the dispute and armed with relevant experience and expertise doesn't just reduce the risk of an unjust result. It also avoids the expense of an appeal by a disgruntled loser based on the types of purely technical grounds that can be pursued in court, such as challenges to the judge's evidentiary rulings or jury instructions.

Commercial disputes are most often resolved on the basis of what the parties did or did not do in their dealings with each other, whose fact witnesses are more credible, or whose expert witnesses and attorneys are more persuasive. The assessment of those matters is within the province of the fact finder and generally is not a viable basis for appeal, even in court.

Moreover, if the parties really do wish to preserve a right to challenge the arbitrator's decision on the traditional grounds afforded by appeals courts, they may incorporate an institutional provider's appellate option in their contract. Those rules typically delegate to a separate appellate panel, on an expedited basis, the task of determining whether the award was based on material and prejudicial errors of fact or law. Notably, institutional providers report that the appeal process is rarely invoked.

Is strict adherence to the procedural and evidentiary rules of court needed to reach a fair and just resolution?

The seller says he doesn't know; he'd have to ask his lawyer. The purchaser is less concerned about procedure than she is about getting to the merits of her case, without spending any more time and money than is absolutely necessary.

Unless the parties' arbitration agreement requires it, arbitrators are not constrained to strictly follow traditional evidentiary rules. Institutional provider rules afford them the discretion to admit testimonial and documentary evidence as they see fit and to assign appropriate weight, which may be none at all.

How many commercial disputes warrant time-consuming and expensive challenges to the admission of purportedly irrelevant documents or hearsay testimony? Attorneys make those challenges in court because they are worried about a jury's ability to separate the wheat from the chaff. Skilled arbitrators are fully capable of considering only authentic and probative evidence and ignoring the rest. The chances are remote that a sophisticated arbitrator will be unduly swayed or influenced by inadmissible hearsay or other inappropriate evidence.

Do you want a flexible, innovative process that can save time, reduce costs, and get to the finish line more quickly?

For the seller, that's a no-brainer. He's not concerned about which process is more innovative. He just wants to present his case expeditiously, obtain a ruling swiftly, and then get back to work. He wants whomever is deciding the dispute to treat it as a priority. The purchaser agrees. She wants the decider to act with alacrity on all issues whenever they arise. After all, she says, disputes are like sharks—unless they're constantly moving forward, they die.

Experienced, well-trained arbitrators recognize that the parties selected them, and are paying them, to be fully attentive to their case. Unlike in court, where it can and often does take weeks or months to resolve discovery-related matters, counsel can quicky seek a telephone or videoconference with an arbitrator and have the issue resolved promptly, perhaps even without written submissions. Arbitrators who are lax in dealing with prehearing issues, or in actively managing the case in a way that promotes speed, efficiency, and cost-savings, should not be surprised when they are no longer being selected to arbitrate disputes.

Arbitrators are trained by institutional providers to manage the arbitration process proactively, to ensure a fair, expeditious, efficient, and economical resolution. The oft-cited College of Commercial Arbitrators' *Protocols for Expeditious, Cost-Effective Commercial Arbitration* and *Guide to Best Practices in Commercial Arbitration*, as well as guidelines issued by bar associations and institutional providers, establish best practices for achieving those goals.

A 2015 study conducted by the economic research firm Micronomics on behalf of the AAA found that, on average, federal district court cases took more than 12 months longer to get to trial than disputes resolved by arbitration. Data from the Micronomics study support the commonsense assumption that the longer a case drags on, the greater the attorney fees and associated costs. With federal and state court filings increasing each year, and no commensurate increase in the number of judges able to handle them, perhaps that gap has widened.

Add COVID-19 to the mix and the difference grows. While most courts effectively suspended operations during stay-at-home orders, arbitration hearings were proceeding via secure videoconference platforms within weeks. In most jurisdictions, pandemic-related court backlogs have become so severe that parties in some lawsuits transferred their cases to arbitration.

Arbitration parties can also avail themselves of a host of user-friendly and cost-saving procedures, including the submission of written witness statements in lieu of direct oral testimony, site visits, simultaneous testimony of expert witnesses, and chess clocks that allocate an equal and reasonable amount of time to each side to present its case. These types of tools are not as readily available in court.

Is the best process the one that permits a party, often without limitation, to avail itself of all the discovery it can get and to engage in unchecked motion practice?

The seller says he has no intention of using a leave-no-stone-unturned strategy, and he does not want to suffer through a war of attrition that results in increased costs and delay. The purchaser notes that if the process is overly time-consuming and expensive, any victory will be Pyrrhic and neither side's business needs will be met. She wants her lawyers to take only those steps that are absolutely necessary to put her in a position to prevail.

Arbitration recognizes that, at times, the perfect is the enemy of the good. Prehearing discovery is permitted, but the key question is how much discovery is truly needed. Three considerations are the size of the claim, the complexity of the dispute, and the proportionality of the requested material to the reasonable needs of the case. Institutional provider rules grant arbitrators significant discretion, with input from the parties, to define the appropriate scope of discovery by targeting key issues and avoiding costly fishing expeditions.

Discovery motions are actively discouraged in arbitration. Expedited procedures for resolving those disputes are favored. Dispositive motions are available, but pursuant to institutional provider rules or in the exercise of their discretion, experienced arbitrators generally require that a party first obtain their permission by demonstrating a likelihood of success and that, if granted, the motion will narrow the issues, shorten hearing time, and reduce costs.

Some might argue that eliminating a party's unilateral right to file dispositive motions is a negative aspect of the arbitral process, but if a party cannot convince the arbitrator in a pre-motion letter that its proposed motion has legs, how likely is it that the arbitrator will grant the motion? And how many months and dollars can be saved by declining to entertain a motion that will most likely be denied? The same can be said for requests for interrogatories, admissions, and oral depositions of multiple deponents, all of which are typically shunned in commercial arbitration unless the case truly justifies it or the parties' agreement expressly authorizes it.

Here again, the flexibility of arbitration is a virtue. While enabling parties to limit the expenses associated with extensive discovery in cases that don't warrant it, arbitration allows the parties to avail themselves of substantial discovery in cases that do. For example, if the ability to conduct a specific number of depositions is important to the parties, their arbitration agreement can so state and the arbitrator will be obligated to abide by that stated preference. Arbitration is the parties' process; if the parties' agreement omits something that they later jointly decide they want, they can so inform the arbitrator during the preliminary case management hearing.

The flexibility of arbitration is a virtue.

That flexibility stands in sharp contrast to the practice in court. While guided by principles of proportionality, court procedural rules offer unfettered access to myriad devices that can lead to unnecessary expense and protracted delay. Trial lawyers, and the parties who pay their bills, are well aware of the time and expense involved in drafting discovery requests and responses, taking and defending depositions, making and opposing motions, and preparing for trial in such a manner that every document offered into evidence and every question posed to a witness will withstand objections by opposing counsel as to relevance, foundation, or form.

Is it important for your dispute to be decided privately and for confidential business dealings to be secured against access by customers, competitors, and the public?

The seller views the dispute as a private business matter. It doesn't involve any public policy or safety issues. There are no reasons it should be battled out in a public forum, where all the testimony and documents are accessible, including to customers and industry competitors. He figures what happens in Vegas should stay in Vegas. The purchaser agrees; she does not wish to air her private disputes in public. Doing so is not her style. And it would be bad for business.

Arbitration is a private dispute resolution process. Whether the proceeding is treated as confidential is entirely up to the parties. By their agreement, the entirety of the proceedings, including the information and documents exchanged during the case, can be kept confidential. If, however, the parties wish to tell others what happened in the arbitration, they can agree to retain that ability by forgoing a confidentiality agreement.

By contrast, no such flexibility exists in court. Unless the parties can meet the strict criteria for sealing court records and limiting public access to trial proceedings, confidentiality is not an option. The pleadings, motions, briefs, affidavits, court orders, and trial testimony are available and accessible to anyone interested in learning about the dispute and its resolution.

Do you need to know the reasons one party won and the other party lost?

The seller is result-oriented; he just wants to know if he won or lost and how much money is being awarded. In defeat, he wouldn't need or want to see a multipage opinion chastising him and vindicating the purchaser. That would not be fun to read, and, worse yet, it could serve as damaging precedent in future disputes in which he might become involved.

The purchaser thinks that the decision maker should be required to explain in detail the basis and reasoning behind each part of the decision, including what evidence was credited and discredited. For her, it's all about accountability.

Because arbitration is a creature of contract, the parties can direct the arbitrator to render an award in any form they desire. It can be a standard award, which states the arbitrator's finding on each element or component of each claim and any amount of money to be recovered by the prevailing party; or it can be a reasoned award that also includes an explanation of why the arbitrator ruled as he or she did on each claim. If the parties desire, the award can even include findings of fact and conclusions of law.

That flexibility doesn't exist in court. There is no written opinion following a jury trial. And a judge's opinion following a bench trial may or may not be satisfying. For the loser, there is always the risk that the opinion may be used as precedent in future cases.

Do you want input into when your dispute will be heard and decided?

The seller says he needs to know with reasonable certainty when the evidentiary hearing will start, how long it will take, and when a decision will be rendered. He cannot shut down his business to accommodate a substantial number of sequential hearing days. The purchaser agrees; she cannot be away from her place of business for long, uninterrupted periods. She wants the dispute resolved promptly, one way or the other. "Enough already!" she says.

In court, the parties need to be prepared for trial whenever the court wants to hear the case. Trial lawyers are all too familiar with the experience of being trial-ready but having to stand by for openings on the court calendar. Often the parties, their counsel, and their witnesses must be poised to proceed on short notice.

Most trial lawyers have experienced downtime, interruptions, and seemingly endless waiting when trying a case. Sometimes it can take days just to pick a jury. Fact witnesses and expensive experts sit in courthouse hallways for hours, sometimes days, waiting their turn to testify. How would a judge react if a party or its counsel tried to dictate when the trial would begin, how often the court would convene to take testimony, and how long it would take to get to a final decision?

Parties in arbitration can accommodate their practical business needs by consensually tailoring their arbitration agreement to specify when they will proceed to hearing and how long it will last. The arbitration agreement is the source of the arbitrator's jurisdiction and authority to act; arbitrators are obligated to abide by those terms.

If, for example, the parties want their hearing to be conducted three days a week, or every other week, to enable them to run their businesses without undue interruption, their agreement can so provide. Similarly, if they want the hearing to take no more than a stated number of days from start to finish, their contract can so state. Moreover, most institutional providers require that awards be issued promptly following the closure of the record. If an arbitrator cannot accommodate the parties' joint expectations and requirements, he or she should decline the case.

Do you want your dispute to be decided by someone who may "split the baby"?

The seller wants the decision maker to just call it as he or she sees it. The purchaser agrees that the dispute should be decided on the merits, not compromised. She wants to know who is more likely to compromise a decision—a judge, a jury, or an arbitrator?

Perhaps the most unwarranted yet widely disseminated criticism of arbitration is that arbitrators are prone to feel sympathy for the losing party or otherwise lack the fortitude to rule fully in favor of one party. The available statistical evidence belies that charge. According to a 2018 study by the AAA-International Centre for Dispute Resolution, commercial arbitrators decided entirely in favor of one party or the other 94.5 percent of the time. Further, this criticism erroneously assumes that juries do not render compromise verdicts. Ask any seasoned trial lawyer who has polled juries following their verdicts if that's correct. It's not.

At the end of the day, arbitration is a viable alternative to, not a substitute for, litigation. Sophisticated businesses in industry sectors as varied as construction, energy, entertainment, financial services, life sciences, real estate, and technology, among others, have selected arbitration as their dispute resolution method of choice. Might it be that those businesses have learned from experience that arbitration offers the kind of self-determination that is not available in court?

Isn't the answer self-evident? ■