Assessing the process of arbitration

A brief overview of the development and expansion of arbitration since the time of King Solomon

By Nancy Neal Yeend

Arbitration has been around for centuries, with King Solomon one of the earliest advocates of the process in 950 BCE, and Native Americans were using arbitration to settle inter-tribal disputes long before the Colonists brought the process from Europe. Massachusetts Colony created an arbitration statute in the 1630s, which predates England's first arbitration law by nearly 50 years. There was an effort to avoid the Revolutionary War by trying arbitration, and George Washington even had an arbitration clause in his will.

By the 1780s New York City was becoming the center for international trade, and the Chamber of Commerce, along with various guilds and trade groups were using arbitration to resolve commercial disputes. President Theodore Roosevelt used arbitration to help resolve a major coal miners' strike in 1902. In 1925 the Federal Arbitration Act became law, and a year later the American Arbitration Association was founded.

Arbitration developed a loyal following of merchants and traders because these individuals liked having someone who had an understanding of their businesses decide their disputes, and for the same reasons that arbitration is used today – it is typically faster and cheaper than litigation. Another concern for businesses regarding litigation is the loss of good will and continued working relationships. Arbitration can often help repair those important business interactions.

Evaluating arbitration

There are at least four significant factors one must consider when evaluating the pros and cons of arbitration: participation, procedures, fairness and finality. Historically, arbitration has enjoyed the reputation of providing results faster than litigation and at a significantly reduced cost, and yet it is invariably influenced by these other four factors.

When people freely negotiate a contract, including an arbitration clause, or when they negotiate after a dispute arises to use arbitration, the process is voluntary. Negotiating the terms of the arbitration process, including confidentiality, location of the arbitration session, identification of the arbitrator or arbitration panel, along with other procedural issues statistically enhances the probability of ending the dispute. The participants are more likely to consider the arbitration process as fair, and are less likely to protest a decision, thus ensuring finality, no matter whether the arbitration is binding or non-binding.

Participation

Voluntarily initiated arbitration agreements, made before people start to do business together, or when negotiation sessions are started after a dispute arises, and that also provide an opportunity for the participants to tailor the arbitration process to meet their specific needs, have higher compliance rates. Mandatory, binding, arbitration clauses can be used to prevent litigation, thwart efforts challenging debt collection laws, and has become a popular method to avoid class action litigation.

Resistance to participate in arbitration or to accept an arbitrator's decision increases when arbitration is mandated – whether court-ordered or because of boilerplate clauses in contracts. Court-ordered arbitration, which is non-binding, nationally experiences over a 90 percent appeal rate, which in turn increases the costs associated with arbitration.

Procedures

Fundamental procedural elements, including, but not limited to understanding the process, who makes the decisions and upon what it is based, location of where the arbitration takes place, confidentiality, and what happens if a person does not like

the outcome must be clarified prior to agreeing to arbitration.

Not having the opportunity to select the arbitrator can be problematic, especially if there is no guarantee that the arbitrators have any understanding or experience related to the particular points of disagreement. On the other hand, having experience, such as a contractor arbitrating a construction case, may raise the question of impartiality or bias. Many clauses dictate that the arbitration will take place in a particular location, for example city where the corporate offices are located. In those instances, travel hardships may impact the client or customer – not to mention that the company benefits from the "home field" advantage.

Depending on the type of case, even confidentiality may be problematic, especially for disputes involving product defects. Confidentiality may also protect the corporation or business from experiencing "copycat" cases.

Being able to decide, in advance of agreeing to arbitration, whether or not the arbitrator's decision will be binding or non-binding, can impact the parties' perception of fairness and even their willingness to select arbitration. Clarifying the pros and cons of binding and non-binding arbitration is very important.

Arbitration can be unfair

Without being able to engage in determining some of the previously mentioned topics, the participants are more likely to distrust the process and the decision of the arbitrator or panel. Again, not being involved in the selection of the arbitrator may give the impression that the arbitrator cannot be objective. In addition, large corporations are benefitted by their mandatory arbitration clauses, and the typical employee or customer does not have the financial wherewithal or expertise to object.

Presently, most businesses have a mandatory arbitration clause in their contracts. Banks, retail businesses and car dealerships regularly incorporate arbitration clauses in their contracts, which may leave the client or customer in a "take it or leave it" situation (contracts of adhesion). Some contracts provide for using a particular organization or arbitrator, and it has been shown that those entities have given preference to the company who regularly hires them.

Not all contracts have an obvious "opt out" clause or process. With more use of online contracts, potential clients and customers are more likely to "click" on the "accept" button without reading the contract. When "opting out" is available, some people are doing just that. They can always decide later to try the arbitration, should a dispute arise.

Although arbitration is often represented as cheaper than litigation, that may not always be the case. Private arbitration administrative fees may be substantially higher than court filing fees, and arbitrator fees are typically billed on a daily basis of around $3500 and may go up significantly from there.

There is a lingering question for some whether arbitration is fair, since the arbitrator is not required to follow the rules of civil procedure. In a trial, *"damages must be proven with reasonable certainty; in an arbitration proceeding, proof of damages can be based on speculation and conjecture."* Of course arbitration provides a benefit, since the arbitrator can tailor the decision, based on the uniqueness of the case.

Another benefit of arbitration is that it is faster and can be scheduled more quickly than getting a trial court date; however, with the shorter period of time, the question becomes, "Will there be sufficient time to conduct discovery, if it is necessary?" On the other hand, for some arbitrations, cases under a certain dollar amount may not be afforded any discovery opportunity.

Finality

Even if binding arbitration is used, it does not mean that a person may not try to appeal a decision that they perceive as unjust or illogical. Not all appeal rights are automatically waived when using binding arbitration. There are very limited grounds for appeal; however, if arbitrators exceed their powers or there is misconduct or corruption, then their decision may be overturned.

Arbitrator decisions take on added meaning when confirmed by a court. Having a court confirm the arbitrator's decision by issuing a judgment aids enforcement and encourages compliance.

Summary

Arbitration has served individuals, companies and organizations well for many centuries. Statistically, it is a dispute resolution process that conserves time, money and other resources. There are many advantages and disadvantages related to the arbitration process, and attorneys and their clients are well served to review the process and consider the essential four elements: participation, procedures, fairness and finality when considering engaging in the process.


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Endnotes

[1] Jones, William C., Three Centuries of Commercial Arbitration in New York: A Brief Survey, Washington University Law Review, issue 2, 1956.

[2] For a fascinating historical review of arbitration: Wolaver, Earl S., The Historical Background of Commercial Arbitration, University of Pennsylvania Law Review, December, 1934.

[3] *Kindred Nursing Centers v. Clark*, 2017, US Supreme Court. California, Second District ruling enjoined officials from implementing a new California law (2020).

[4] Product defect cases were typically resolved using arbitration over the years; however, after significant litigation involving auto manufacturers, tobacco companies and medical implants products increased, Federal product defect legislation was passed.

[5] Repa, Barbara Kate, Arbitration Pros and Cons, Nolo, 2010.

[6] *Neaman v Kaiser Foundation Hospital*: No. B057055. Second Dist., Div. Three. Sept. 22, 1992.

[7] Finn, Robert F., The Top 10 Pros and Cons of Arbitration, Construction Executive, August 5, 2014.