benefits of

ARBITRATION

FOR COMMERCIAL DISPUTES

AMERICAN BAR ASSOCIATION
Section of
Dispute Resolution

BENEFITS OF ARBITRATION FOR COMMERCIAL DISPUTES

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WHAT IS ARBITRATION?

Arbitration has been part of the dispute resolution landscape for centuries: some commentators date arbitration back to the time of the Phoenician merchants; Alexander the Great's father, Phillip the Second, used arbitration as a means for resolving border disputes; George Washington had an arbitration clause in his will; and the English used arbitration for commercial disputes as early as 1224.

Arbitration is preferred by many as a way to resolve commercial disputes. It has many advantages over litigation in court, such as party control of the process; typically lower costs and shorter time to resolution; flexibility; privacy; awards which are final and enforceable; decision makers who are selected by the parties on the basis of desired characteristics and experience; and broad user satisfaction.

PARTY CONTROL

Unlike litigation in court, arbitration is a creature of contract. This means that parties can agree to design the arbitration process to accommodate their respective needs and can continue to do so as the proceeding moves forward. Both at the contractual stage and after the arbitration has commenced, the parties can determine the nature and scope of discovery (including whether to allow depositions), the conduct of the hearing (including testimony by live video), the length of time for the entire process, as well as pre-screening the arbitrators for disclosure issues and availability.

LENGTH OF TIME

According to statistics furnished by the largest arbitration providers, the average time from commencement of a domestic, commercial arbitration to issuance of a final award ranges from **7 months to 7.3 months**.[i]

By contrast, in 2011, the median length of time from filing through trial of civil cases in the U.S. District Courts was 23.4 months and considerably longer in some of the busier courts.[ii]

The median length of time in 2011 from filing of a civil case in district court to disposition of appeal by the U.S. Circuit Courts of Appeal was 30.8 months and considerably longer in some of the busier courts.[iii]

The Bureau of Justice Statistics reports that for state court contract cases in the 75 largest U.S. counties, the average length of time from case filing to trial in jury cases was 25.3 months and for bench trials 18.4 months.[iv] Appeals times are not reported.

EXPENSE

Attorneys' fees and expenses are by far the most significant cost of litigation, and they increase in direct proportion to the time to resolution of the case. Attorneys' fees and expenses can be minimized in arbitration because arbitrations are generally concluded in far less time than cases in court.

While cases litigated in court do not have arbitrator or institutional charges, the International Chamber of Commerce reports that those charges represent only 18% of the cost of arbitration.[i] This 18% (and substantially more) can be recouped quickly because of the increased speed and efficiency of arbitration and the ability to tailor the arbitration to the specific needs of the parties.

Court cases generally require more counsel time and, thus, more expense for preparation and trial than is needed in arbitration. For example, broad pre-trial motion practice and exhaustive discovery pursuant to rules of civil procedure are not common in arbitration. Many hearing related matters which consume time and money in court are usually not part of arbitration such as extensive evidentiary issues, *voir dire*, jury charges, proposed findings of fact, endless authentication of documents, qualification of experts, and cumulative witnesses. Finally post hearing appeals and court proceedings are far more limited in arbitration than in court.

Arbitration is a flexible process which permits parties to organize procedures, and schedule hearings and deadlines to meet their objectives and convenience.

FLEXIBLE PROCESS

Arbitration is a flexible process which permits parties to organize procedures, and schedule hearings and deadlines to meet their objectives and convenience. Common practices which result from arbitration's flexibility include choosing a location for the hearing that will minimize costs; taking witnesses out of order or interrupting a witness to accommodate individual needs; continuing a hearing outside of normal business hours in order to complete a witness or to finish the hearing; taking testimony of distant witnesses by video conference or by telephone; ordering testimony so that all experts on a topic testify directly after one another or even all at the same time; and using written witness statements for some or all of the witnesses in lieu of time-consuming, oral direct testimony.

When negotiating their underlying commercial contract, parties often include provisions in the arbitration clause which will enhance the efficient conduct of any arbitration that might thereafter arise. Most commonly, such clauses set time limitations for concluding the entire arbitration, as well as limitations on interim phases such as discovery and commencement of the hearing. It is far easier for the parties to agree on such matters when they negotiate their commercial contract than when a dispute has actually arisen and the parties are in an adversarial relationship.

The flexibility of arbitration fosters a relatively informal atmosphere. Together with the privacy of the arbitration proceeding, this serves to reduce the stress on the witnesses and on what are often continuing business relationships between the parties.

CONFIDENTIALITY

Arbitral hearings are held in private settings and are attended only by those designated by the parties and their counsel, in contrast to trial proceedings held at the court house, which are open to the public.

The parties can agree to maintain the confidentiality of the arbitration proceeding, unlike in court, where requests to seal the record are seldom granted. Most arbitral institutions have specific rules regarding the confidentiality of proceedings and awards and the laws of some jurisdictions provide for confidentiality. As long as the proceeding stays in the arbitration forum, confidentiality can be preserved by agreement of the parties.

Confidentiality is an important feature for many corporations, particularly when dealing with disputes involving intellectual property and trade secrets or when there are concerns about publicity or damage to reputation or position in the marketplace.

ARBITRATOR SELECTION

A great benefit of arbitration is that the parties can select their arbitrators, both under the party appointed system and the list system, and thereby choose arbitrators with qualifications tailored to the needs of the arbitration in question. These desired qualifications can include attributes such as subject matter expertise; reputation for competence; temperament; number of years of experience; number of arbitrations chaired; availability; and commitment and ability to conduct an efficient, cost-effective arbitration.

The ability of parties to select arbitrators with desired specific expertise and competence contrasts with most court cases where judges are assigned randomly without regard to whether they possess qualifications particularly suited to the dispute in question.

An additional benefit is the parties' ability to provide for a panel of three arbitrators to hear complex and/or high-dollar disputes.

Arbitration permits the parties to choose adjudicators with the necessary special expertise.

DISCOVERY & RELATED MATTERS

Unless specifically agreed otherwise by the parties, discovery and related procedures are considerably more limited in arbitration than in litigation.

In court litigation in the United States, the governing Federal Rules of Civil Procedure or parallel state court rules often allow for broad, burdensome and expensive discovery, including lengthy depositions and the extensive production of electronic data.

The parties in arbitration may limit discovery and engage in other cost-efficient procedures by adopting guidelines such as the New York State Bar Association's *Guidelines for the Arbitrator's Conduct of the Pre-Hearing Phase of Domestic Commercial Arbitrations and International Arbitrations*.[vi] Among other things, these Guidelines contain significant suggested limits on processes including document discovery, e-discovery, depositions, discovery motions and dispositive motions. Guidelines like these are binding when adopted by the parties. But even if they are not adopted, arbitrators often rely on these Guidelines as a framework for the efficient conduct of the pre-hearing phase of arbitration.

Arbitrators are actively involved in the management of the case and can conduct a telephonic or in person supervised session to assure expeditious proceedings much more promptly than is often the case in our overburdened courts.

FINALITY

In many cases it is important that commercial disputes be resolved quickly and finally because drawn-out indecision significantly increases costs and may cause business paralysis. Arbitration provides finality and does so quickly and economically because lengthy, expensive appeals like those encountered in court are not available under the Federal Arbitration Act ("FAA") and state arbitration statutes. These statutes severely limit a court's ability to vacate arbitration awards except on narrow grounds, which are difficult to prove and rarely succeed.

In some cases, parties to a large dispute may want a more comprehensive appeal than is permitted under the FAA and state arbitration statutes. They can accomplish this (without sacrificing the efficiency of arbitration) by providing for an appeal to a second arbitrator or panel of arbitrators on traditional legal grounds. An appeal within the arbitration framework can be conducted quickly and cost effectively, without significantly delaying the final resolution of the case.

DECISIVE RESULT

Studies have repeatedly and conclusively shown that arbitrators do not split the baby. For example, a 2007 study showed that in only 7% of the cases were damages awarded in the mid-range of 41-60% of the amount claimed, results almost identical to a similar study conducted six years earlier.[vii]

INTERNATIONAL COMMERCIAL DISPUTES

Arbitration permits the parties to choose adjudicators with the necessary special expertise to decide a cross-border dispute, a choice which is not available in court. This special expertise can include knowledge of more than one legal tradition (e.g., common law and civil law), experience, understanding and ability in harmonizing cross-border cultural differences between parties, and fluency in more than one language.

In the international context, arbitration provides a uniquely neutral forum for dispute resolution and enables the parties to select decision makers of neutral nationalities or of recognized neutrality who are detached from the parties and

their respective home state governments and courts. Thus, arbitration avoids any perceptions of potential bias and provides reassurance that the rule of law will be observed. Arbitration also avoids delays in court which, in some jurisdictions, can exceed five or even ten years.

A critical feature of international arbitration is the existence and effective operation of the New York Convention to which over 140 nations are parties. The Convention enables the enforcement of international arbitration agreements and awards across borders. In contrast, judgments of national courts are more difficult and often impossible to enforce in other countries.

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STUDIES PROVE THAT ARBITRATION IS AN EFFECTIVE PROCESS

Satisfaction - Studies have shown that a majority of users believe arbitration is better, cheaper and faster than litigation.[viii]

Fairness - Studies have shown that 80 per cent of attorneys and 83 percent of business people report that arbitration is a fair and just process.[ix]

International - Studies have shown that 86% of corporate counsel are satisfied with international arbitration.[x]

Expertise- Studies have shown that the majority of parties find arbitrators, since they can be chosen by the parties, to be more likely to understand the subject of the arbitration than judges.[xi]

Lack of bias - Studies have concluded that three arbitrators are less likely to be influenced by unconscious biases than is a single decision maker.[xii]

Compliance with awards - Studies have shown that the rate of voluntary compliance with arbitral awards is over 90%.[xiii]

Financial benefits - Studies have shown that speedier resolutions result in significant financial benefits to all parties as parties know what they owe or are owed and can move forward with their lives and businesses.[xiv]

i
Data on file with the ABA Section of Dispute Resolution

ii
Judicial Business of the U.S. Courts, U.S. District Courts— Median Time Intervals From Filing to Disposition of Civil Cases Terminated, by District and Method of Disposition, Table C-5, at http://www.uscourts.gov/uscourts/Statistics/JudicialBusiness/2011/appendices/C05Sep11.pdf

iii
Judicial Business of the U.S. Courts, .U.S. Courts of Appeals—Median Time Intervals in Months for Merit Terminations of Appeals Arising From the U.S. District Courts, by Circuit, Table B-4A,(median for "other civil appeals" which excludes prisoner petitions) at http://www.uscourts.gov/uscourts/Statistics/JudicialBusiness/2011/appendices/B04ASep11.pdf http://www.uscourts.gov/uscourts/Statistics/JudicialBusiness/2011/appendices/B04ASep11.pdf

iv
Civil Justice Survey of State Courts, Bureau of Justice Statistics 2005, available at http://www.ojp.usdoj.gov/bjs/pub/pdf/cbjtsc05.pdf

v
International Chamber of Commerce Commission on Arbitration, *Techniques for Controlling Time and Costs for Arbitration*, available at http://www.iccwbo.org/uploadedFiles/TimeCost_E.pdf.

vi
Guidelines for the Arbitrator's Conduct of the Pre-Hearing Phase of Domestic Commercial Arbitrations and International Arbitrations, available at http://www.nysba.org/ArbitrationGuidelinesBooklet.

vii
American Arbitration Association, *Splitting the Baby:* a New AAA Study, available at http://www.adr.org/aaa/ShowPDF?doc=ADRSTG_014040

viii
Rand Institute for Civil Justice, *Business to Business Arbitration in the United States, Perceptions of Corporate Counsel ("Rand")*, p. 1, 30 (2011).

ix
Id.

x
PriceWaterhouseCoopers, *International Arbitration, Corporate Attitudes and Practices*, ("PWC"), p. 8 (2008).

xi
Rand, *supra* note viii at p. 32.

xii
Chris Guthrie, *Misjudging*, 7 Nev. L.J. 420, 451-453 (2007).

xiii
PWC *supra* note x at p. 8.

xiv
See B. Roy Weinstein & Stevan Porter, *Economic Impact on the County of Los Angeles and the State of California of Funding Cutbacks Affecting the Los Angeles Superior Court* (Dec. 2009), available at http://www.micronomics.com/articles/LA_Courts_Economics_Impact.pdf.

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