# Alternative Dispute Resolution for Real Estate Disputes

## *Is ADR Really Faster, Better, and Cheaper?*

**By Michael F. Donner and Dennis L. Greenwald**

"ADR"—an acronym for alternative dispute resolution—is a general, colloquial term that, literally read, refers to any methodology for resolving a legal dispute other than litigation in a court of law. Its common usage, however, usually refers only to "nonbinding" mediation and "binding" arbitration. Although ADR has long been favored by the courts for its dual advantage of both thinning judicial dockets and promoting settlement, lawyers have not always shared this view. For example, many believed that, if they could not negotiate a settlement themselves, they should not bother with an expensive "counseling session" such as nonbinding mediation. Litigators also historically eschewed arbitration because they preferred the courtroom and its well-settled rules of civil procedure and evidence to the less formal setting of arbitration and believed that trial judges were more experienced and willing to "pull the trigger" on tough rulings than arbitrators.

Times have changed. Today ADR methodologies, like mediation and arbitration, are increasingly embraced by lawyers and clients as effective alternatives to litigation. Demand for ADR has risen, and ADR clauses now are routinely included in all manner of agreements relating to real estate and many other transactions. A lawyer can hardly open his or her mail, or a legal journal, without noticing the profusion of advertisements for various ADR organizations and their services. Although in the past the American Arbitration Association was the primary (if not the exclusive) game in town for ADR, the relatively recent surge in demand has spawned the creation of many other ADR organizations. The ranks of professional mediators and arbitrators now swell with seasoned, retired judges and lawyers—and even nonlawyers—who compete for ADR business. Much of this demand for ADR has been driven by the popular belief that ADR is *faster, cheaper*, and *better* than litigation.

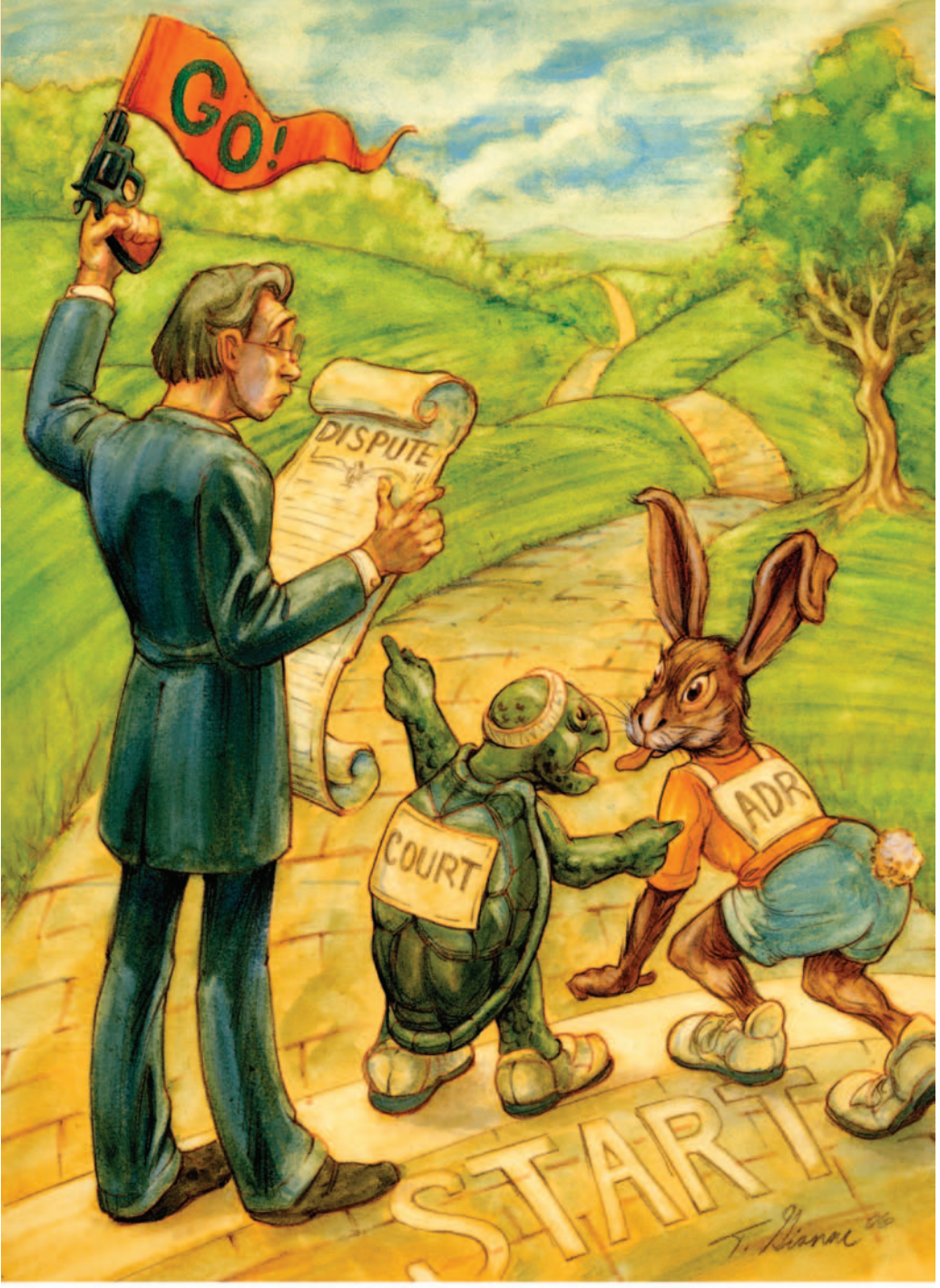
This article examines the commonly held belief that ADR is faster, cheaper, and better than litigation when it comes to resolving real estate disputes. In the great tradition of the legal profession, the authors conclude with a resounding: "It depends." As advantageous as ADR can be, it is *not* appropriate for all clients, all real estate transactions, or all disputes. Lawyers should consider numerous factors before including an ADR clause in a real estate contract or agreeing to mediate or arbitrate when no such clause exists. Whether (and when) ADR is advisable requires a separate analysis of mediation and arbitration.

### The Mediation Process

Mediation is a nonbinding proceeding in which the parties attempt to come to a consensual resolution of their dispute with the assistance of a neutral third-party. Contrary to what many clients and more than a few lawyers believe, mediation is relatively informal. The parties generally are not required to do anything except merely show up and talk to the mediator (unless, of course, their contract or the rules of the ADR organization selected by the parties require them to do more). Typically, the parties, their lawyers, and a mediator convene at an office and are asked to wait in separate conference rooms while the mediator shuttles between each side to discuss the dispute. There is no stenographer, no discovery, and no evidence or testimony. There are no rules of engagement. Indeed, the presence of lawyers is not necessarily even contemplated.

The selection of an experienced mediator is imperative, particularly if the parties' dispute involves a particular business or legal issue. Lawyers can draft mediation clauses in contracts to anticipate such disputes and to require the parties to retain a specifically identified mediator, ADR company, or *type* of mediator (for example, a retired judge or

Michael F. Donner is of counsel to the San Francisco, California, firm of Stein & Lubin LLP and vice-chair of the Real Property Retail Leasing Committee. Dennis L. Greenwald is a member of the Santa Monica, California, firm of Greenwald, Pauly, Foster & Miller.




Tom Gianni

an engineer). In the absence of such a clause, lawyers also should consider doing advance research on, and proffering a list to opposing counsel of, potential mediators who have knowledge about the substantive area or law at issue, experience with mediations, a reputation for achieving settlements, an acceptable fee rate, and, most important, time to conduct the mediation.

Although the parties are not required to file any formal "pleadings," they often voluntarily submit mediation briefs to the mediator in advance of the proceedings. The parties also frequently exchange their briefs with the other side. Mediation briefs are helpful because they can educate the mediator about the facts and legal issues, pave the way for settlement talks with the other party, and save money and time at the mediation. Despite these advantages, litigators sometimes are reluctant to share briefs with the other side because they want to control what their client's adversary learns about the dispute and their legal theories and strategies. Essentially, these lawyers view the briefs as an unfair pre-litigation "discovery" opportunity. Litigators also often dislike mediation briefs because, unless the parties agree or the applicable state law or ADR rules provide otherwise, all communications made or evidence presented before, during, and after a mediation might be admissible in a later lawsuit.

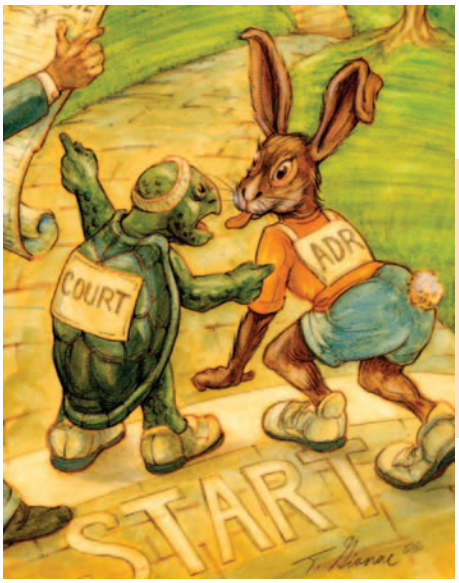
Once the mediation is concluded (whether or not a consensual resolution of the dispute has been achieved), usually the mediator's job is done. The lawyers are left to their own devices to continue the parties' settlement dialogue or document any agreements reached by the parties. If the mediation results in a settlement, it is advisable to memorialize the settlement in writing while the parties are still at the mediation (even if a more formal settlement agreement will follow). A signed settlement agreement can be enforced by the court if the other party changes its mind after the mediation. Practitioners should include in the agreement an express waiver of all confidentiality protections or privileges for the purpose of enforcing and interpreting the settlement. Under the laws of many states, settlement agreements are mediation "communications" and, as such, are privileged and cannot be introduced in court as evidence unless the privilege has been waived.

### Deciding Whether to Mediate

The question of whether to mediate typically will arise at two junctures: during the contract drafting process when the lawyer must decide whether to include a provision requiring mediation as a condition to commencement of any litigation or arbitration, or after a dispute has arisen and the parties must elect whether to voluntarily mediate because their contract does not require mediation.

Lawyers should consider their clients' possible future strategies and objectives before including a media-

tion provision in the parties' contract. Contractually mandated mediation generally will delay the ultimate adjudication of a dispute. It may be a bad idea, for instance, for a real property lender to include a mediation requirement in its loan documents because, following a default by the borrower, the lender typically will want to move as quickly as possible to foreclose on its security. A mediation provision in a lease




similarly may restrict or delay the landlord's ability to evict a tenant and frustrate the landlord's desire to obtain immediate possession of the leased premises. On the other hand, mediations are useful in resolving disputes that do not require the parties to seek an expedited enforcement of their rights. Disputes involving discrete issues, such as the interpretation of a specific lease clause, for example, often can be resolved more quickly and more cheaply with the help of an experienced mediator than through litigation or an arbitration. Accordingly, before including a mediation clause in a contract, lawyers should consider the nature of the parties' relationship and their own client's tolerance for expense and possible need to expedite the adjudication of any future disputes.

The issue of whether to voluntarily agree to mediate a dispute (in the absence of a contractual provision requiring mediation) will depend principally on whether the dispute is of a nature suited to mediation and whether the parties are inclined to mediate. If the dispute is not one in which mediation is likely to be successful or if one of the parties refuses or is not likely to mediate in good faith, then there is little point in having a mediation.

### So, Is Mediation Faster, Cheaper, or Better?

The question of whether mediation is a faster, cheaper, and better mechanism for resolving disputes than litigation or arbitration does not lend itself to a simple answer. It is somewhat axiomatic to say that, if a mediation results in a settlement, it necessarily was the faster, better, and cheaper mechanism to resolve the dispute. Although fast results can be achieved in litigation (where, for example, a lawsuit can be disposed of on an expedited basis before trial through various motions), mediation will almost always be faster and cheaper than either litigation or arbitration. So, the question of whether mediation will be "better" depends on the tautology of whether it is likely to be fast and likely to result in a settlement. (One can almost assume that faster translates into "cheaper" by virtue of lower legal fees.) The odds of resolving a dispute are significantly increased through mediation when three factors coalesce: (1) a skilled mediator, (2) knowledgeable and pragmatic attorneys, and (3) clients who are motivated to settle.

Lawyers and their clients should nonetheless understand that, even if the mediation does not lead to a settlement, it might still have conferred something of value on the parties. For example, even if the parties advanced only slightly down the road to settlement during the mediation, the parties and counsel might gain a better understanding of the strengths and weaknesses of their position as well as the other side's position. In addition, lawyers also can size up the advocacy skills of opposing counsel.

*The issue of whether to voluntarily agree to mediate a dispute will depend principally on whether the dispute is of a nature suited to mediation and whether the parties are inclined to mediate.*

### The Arbitration Process

Arbitration is a binding adjudication of the parties' claims and defenses by a neutral arbitrator (or group of arbitrators). The arbitrator's ruling or award is ultimately binding on the parties as if it were rendered by a court as a final judgment. Unlike a judgment, however, the award has no force of law behind it. The judgment is a private determination and the arbitrator has no lawful authority to compel enforcement of the award.

Unlike mediation, arbitrations have a formal procedure. Arbitration demands and responses are filed, discovery often is conducted, and evidence and testimony are marshaled and preserved. The case is then tried and an award is rendered. The whole process can take days, weeks, or months, depending on the complexity of the dispute, the number of parties, and the schedules of the parties, the lawyers, and the arbitrators.

### Deciding Whether to Arbitrate

Lawyers and their clients should consider the following when deciding whether to include a mandatory arbitration clause in a real estate contract or, in the absence of such a clause, voluntarily submitting a dispute to arbitration.

First, the decision of the arbitrator will be fully binding on the parties. This might be obvious to some, but many clients do not understand the difference between the *nonbinding* nature of mediation and the *binding* nature of arbitration.

Second, arbitration awards generally can be appealed only on extremely narrow grounds, such as if the arbitrator committed fraud in rendering the award. Non-appealability is a double-edged sword. On the one hand, the parties will lose a potential right that they would otherwise have in litigation. On the other hand, the parties might benefit by the elimination of a lengthy, expensive appellate process. When considering this issue, practitioners should determine whether possible future disputes between the parties might involve areas of unsettled law (which ultimately might lend themselves to adjudication by an appellate court). Under those circumstances, it may be advisable to avoid arbitration and preserve the client's right of appeal. Alternatively, some practitioners provide a limited form of appellate relief in their ADR clauses.

Third, an award rendered by an arbitrator is not self-executing because the arbitrator typically will have authority to issue only a ruling, not an enforceable judgment. Therefore, if the losing party in the arbitration does not voluntarily satisfy the arbitrator's award, it will be necessary for the prevailing party to commence a court action to convert the arbitrator's award into a judgment issued by a court. The judgment can then be enforced by means of, among other things, a judgment lien or a court order compelling specific performance. This will take additional time and money.

Fourth, by electing arbitration, the parties will lose any right they otherwise had to a jury trial. This is an important consideration for clients who may *want* a jury trial, or conversely, clients who want to *avoid* a jury trial. For example, a foundation for orphans may want to have its lease dispute with a corporate landlord adjudicated by a jury rather than arbitrated, particularly if the jury might sympathize with the foundation's situation. On the other hand, a Fortune 500 residential planned community developer may insist that the parties contractually waive their rights to a jury trial and arbitrate all construction defect disputes. Such a company reasons that, if a dispute were litigated, a jury might sympathize with the homeowners in a "David and Goliath" situation.

Fifth, if the parties want to keep their dispute out of the public eye, arbitration has the benefit of being more private than litigation because it is a private dispute resolution process and, therefore, the pleadings and proceedings are not part of any public record and generally no members of the media or third parties are allowed to attend.

Sixth, arbitration often (but not always) can be more procedurally efficient and move more quickly than a lawsuit. Fewer procedural hurdles exist; the parties tend to file fewer motions; and there can be fewer overall delays. An expeditious process may be useful when there is a risk that one party will be irreparably harmed by delay or when injunctive or other relief may be necessary. On the other hand, litigators often require substantial time to learn about the dispute, research the client's position and claims, draft an arbitration demand or demand responses, identify and prepare witnesses, marshal documents, complete discovery (if any is permitted), and conduct all pre-arbitration law and motions (such as motions in limine that can narrowly focus the scope of the arbitration by excluding issues and evidence). A client's desire to quickly and efficiently submit the parties' dispute to an arbitrator for adjudication could backfire if its counsel does not have sufficient time to effectively prepare for the proceeding.

Seventh, because rules of civil procedure and evidence often are not applied or enforced in arbitrations (unless the parties' contract or the rules of the selected ADR company require otherwise), arbitral proceedings can take off into unforeseen directions. Some arbitrators have been known to allow the introduction of tangential or irrelevant testimony and impermissible argument, all for the purpose of making the proceedings "fair." This can potentially lengthen the proceedings and affect a client's case by allowing embarrassing or prejudicial facts to surface. To avoid this risk, parties frequently agree in their contract to apply a particular state's or ADR company's rules of civil procedure and evidence.

Finally, mandatory contractual arbitration can be problematic if the parties need to seek equitable or injunctive relief (such as an injunction or specific performance) at some point during

their relationship. In certain states, arbitrators lack the authority to grant such relief. Even if state law allows arbitrators to grant injunctive relief, arbitrators (particularly ones who are not retired judges) often are reluctant to compel a party to do or not to do something. Some arbitrators also have little, if any, experience in drafting injunctive orders. For this reason, some practitioners include a carve-out in their arbitration clauses that allows the parties to seek equitable or injunctive relief from the courts under certain circumstances.

### So, Is Arbitration Faster, Cheaper, and Better?

There is still much debate among litigators about whether arbitration is faster and less expensive than litigation. Because arbitrations generally tend to be more procedurally streamlined than litigation and the parties ordinarily have only limited appellate rights (if any), arbitrations often can be faster and cheaper than court actions. Many litigators still say, however, that they can get to trial in court as fast (or faster) than they can have a dispute arbitrated. The speed with which a dispute can be adjudicated by a court will depend on a number of factors, not the least of which is the court's calendar and local fast-track rules.

The expense of an arbitration is another thing that the lawyer should consider with the client. In many jurisdictions, the "hard costs" of a trial (such as the judge's and clerk's salaries and other administrative expenses) are paid by taxpayers. In an arbitration, however, the parties typically pay for the arbitrator's costs and other administrative expenses. If the parties have a fee and cost recovery clause in their contract, the losing party may end up paying all of the costs of arbitration *and* the attorney's fees and costs incurred by the prevailing party.

Perhaps one of the more compelling arguments for arbitration has nothing to do with timing or expense. It has to do with "peace of mind." Because arbitration is conducted in an environment that is less formal and intimidating than litigation (for example, arbitrations usually take place in conference rooms instead of courtrooms filled with jurors, clerks, and bailiffs), the client's level of anxiety sometimes is reduced in an arbitral setting.

Arbitrations have one other benefit that frequently is overlooked. The arbitral process can be used by parties to resolve issues that have not necessarily evolved into a legal dispute. For example, the parties can submit to an arbitrator the issue of determining what a certain fair market rent might be under a lease provision that allows the tenant to elect to extend the term at fair market rent. An arbitrator also can decide what a certain "fair market purchase price" might be for a parcel of real property under a contract that requires one party to buy out another's interest in the real property at the "fair market purchase price." If the parties cannot agree on these amounts themselves, then it is often efficient to have an arbitrator (who may be experienced with such issues) make the determination for them so they can avoid a lawsuit.

*The arbitral process can be used by parties to resolve issues that have not necessarily evolved into a legal dispute.*

### Conclusion

Although most lawyers believe that ADR is a faster, cheaper, and better mechanism for resolving disputes than litigation, ADR sometimes is none of those things. Practitioners should consider numerous factors before including, or agreeing to include, an ADR clause in a real estate contract. If lawyers fail to take the time to effectively consider these factors before the parties enter into the contract, the results could be disastrous—for both the lawyers and their clients.

Lawyers also should carefully draft ADR clauses and resist the urge to merely copy a boilerplate ADR provision from one contract and insert it into another. Although cutting and pasting may be efficient, serious consequences can result from the use of boilerplate ADR clauses that have not been vetted to address the particular needs of a transaction or client. Lawyers who fail to tailor ADR clauses to the requirements of a specific transaction or client can undermine what is perhaps the best thing about ADR: like clay, the parties and their counsel can shape and sculpt the format and scope of an ADR clause and determine before a dispute arises where, when, and how ADR will be employed in the future.

Finally, lawyers should not assume that their clients are sophisticated regarding ADR. Even CEOs of large multi-national corporations have preconceived notions (that are sometimes unfounded) about mediation and arbitration. Practitioners should take the time to walk through the ADR clause with their clients. They should satisfy themselves that their clients understand the advantages and disadvantages of the ADR mechanism they are promising to use when and if a dispute arises under the contract. ■