The Problems of Arbitration

by Robert Miletsky

Arbitration was conceived as a faster, more efficient, and less costly alternative to litigation. But in my experience as an attorney, this is true only for small disputes. When used to resolve claims involving large sums and complicated proof, arbitration is a nightmare. Here are some of the reasons.

Arbitration doesn't always save time and money. Scheduling a hearing for a complex case can be difficult. If the matter isn't settled during the initial hearings, it becomes almost impossible for the three arbitrators, the parties, and their witnesses all to find a date to reconvene in the near future. I have seen arbitration proceedings stretch out for years, going beyond 30 hearings.

The costs of arbitration add up — filing fees, "maintenance" fees, cancellation fees, and arbitrator compensation fees often cost more than going to court. I know of one proceeding in which the parties agreed to pay the arbitrator $250 per hour. At that rate, there was no incentive to close the case.

Only parties directly involved in the dispute may participate. Generally, you may not bring into the matter someone who might also be responsible to you for your damages or who may be liable to the other contracting party. You can file counterclaims against the other party, but you cannot file cross claims or third-party claims against nonparties.

Arbitrators tend to split claims down the middle. While this practice is not as widespread as it is perceived to be, this "split-the-baby" mentality causes parties to inflate their claims, figuring that the award will be reduced anyway.

Arbitration usually does not permit discovery. The discovery phase of a court proceeding gives you an opportunity to determine the full basis for the claims being made against you before the case is heard. Arbitration, however, is more like a "trial by ambush." You have only a sketchy idea of what your adversary's claim is, so you cannot prepare a full and adequate defense.

The informal character of arbitration can backfire. One supposed benefit of arbitration is that you are not required to follow rules of evidence imposed by the courts. While this simplifies matters, it also permits arbitrators to rely on evidence that would not be permitted in a court of law. Similarly, arbitrators often give more weight to evidence than the evidence deserves.

Arbitrators who are also attorneys can create problems. Arbitration is intended to be informal, but in my experience, when an attorney is an arbitrator, there is a tendency for him or her to play judge and use formal court rules anyway.

Arbitrator's awards are rarely overturned by a court. This is true even if the court disagrees with the final factual or legal outcome.

What to Do

To minimize the disadvantages of arbitration, consider these recommendations:

- *Eliminate arbitration clauses from contracts* and agree to arbitrate only if you have no other choice. Generally, the courts do not force parties to use arbitration unless the parties' intent to relinquish the procedures and other safeguards of the court process are clearly stated in the contract.
- *Limit the issues that may be settled by arbitration.* If you agree, for example, to resolve by arbitration only issues of time and performance, a court generally won't force you to use arbitration to settle disputes about other issues.
- *Make it clear in the contract which tribunal is to administer the arbitration proceeding.* The typical clause recommended by the American Arbitration Association (AAA) says the parties agree to resolve their disputes in accordance with the rules of the AAA. But unless you also specify the use of AAA arbitrators, you may end up arbitrating before some other tribunal. I know of one contract which the court interpreted to mean that some tribunal other than the AAA could be used, even though the contract included the AAA's language. The court said the parties agreed only that the AAA rules should be used, not that the proceeding had to be administered by the AAA.
- *Consider using mediation.* A growing number of people see mediation as a preferable option for dispute resolution, because it is relatively inexpensive and nonbinding. ■

Robert Miletsky maintains law offices in New York City and Watertown, N.Y., and lectures frequently on construction law. *This article was adapted with permission from* Contractor's Business Management Report *(212/244-0360).*