

## Comparing arbitration and litigation

By Nancy A. Chillag

It seems like almost every construction contract I am asked to review includes an arbitration provision. When I ask the client why he/she wants to arbitrate disputes, their response is usually "I don't know" or "I heard it is better."

The first question to ask is, "Is arbitration better?" The second question is, "Better than what?" This article will attempt to explain arbitration, the alternatives to arbitration and what may be best for a contractor.

### 1. What is Arbitration?

Arbitration is a method used by parties to a transaction to resolve disputes that arise as a result of the contractual relationship. It is the process whereby a neutral third party hears both sides of the controversy and then makes a decision. In most jurisdictions arbitration can only be used if authorized by statute, agreed to by the parties or provided for in the contract.

### 2. What Alternatives Exist?

The only real alternative to arbitration is litigation. Litigation is the use of the court process to resolve a dispute. Mediation is often discussed as an alternative, but mediation only involves a third party acting as a facilitator to discussions between the parties, and

unless the parties agree to resolve their dispute, no decision is made by the mediator. The balance of this article, therefore, will compare arbitration to litigation and discuss the pros and cons of each.

### 3. Commencing the Action

Under an arbitration agreement the parties usually designate an "arbitration organization" to handle the dispute. When a dispute arises, one party needs to contact the organization and file a claim. The organization then contacts the other party for a reply. In litigation an action is commenced by filing a complaint with the court and serving a copy (by process server) on the other party.

### 4. Cost considerations

Most people are under the impression that arbitration is less expensive than going to court. That is not necessarily true. A complaint in court can be filed for around \$200. Arbitration fees, on the other hand, are tied to the amount in controversy with filing fees that could be in excess of \$1,000. In addition, for arbitration you pay a per day fee for the actual hearing, an arbitrator fee on an hourly basis, which could be \$400 to \$500 per hour, and additional costs for administration of the case if it takes longer than a few months.

Some court jurisdictions have started charging for trials in excess of one day, but usually this is minimal compared to arbitration.

When arbitration was originally introduced it was much cheaper because most people did not hire lawyers to represent them. Today it is highly unusual to participate in arbitration of any complex matter, such as construction, without the assistance of legal counsel. And attorneys, who are trained in the area of litigation, usually employ similar tactics in arbitration (i.e., requesting and obtaining some discovery, hiring expert witnesses, etc.) which increase the cost.

### 5. Discovery

In litigation there is a formal set of procedural rules to allow the parties to obtain all the evidence the other side has in support of their



case. This prevents surprise and also promotes settlement because you can determine whether your evidence is stronger than your opponent's, and thus, whether you have a chance of winning. If a party fails to produce the information requested, the court can sanction them or in extreme cases, throw out their case. In arbitration you may or may not be entitled to discovery. The rules are not as clear and the decision is usually up to the arbitrator. Furthermore, there is very little you can do to force the other side to comply.

## 6. The Decision

In litigation the case is decided by a judge or jury. In arbitration the decision is made by a single person or a panel (usually three) familiar with the area in controversy (a contractor for example), a lawyer or a retired judge.

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Theoretically, the parties should not need to hire expert witnesses because the arbitrator or panel are presumed to be experts in the field. This, however, rarely works as planned. Because of an arbitrator's past experience, he/she may be biased in favor of one side or the other from the start (i.e., an attorney that specializes in representing homeowners). Furthermore, if the arbitrator is retired, he/she may not be as up to date with the standards of the industry as the parties would expect.

## 7. Appeal

In litigation, if the judge makes a "bad decision," you can appeal to a higher court which will review the trial transcripts and the decision. In arbitration there is virtually no right to appeal a "bad decision," absent fraud. The basic rule is that absent fraud, neither errors of fact nor errors of law (or both) are sufficient to set aside an award of an arbitrator. In addition, an arbitrator is not required to, and generally does not, make any detailed findings. In other words, it is sufficient to issue an award with no stated rationale. So if you lose, you may not even be told why you lost.

## 8. Multiple Actions

Arbitration is even more problematic in the construction arena. The general contractor may enter into a contract with an owner which contains an arbitration provision. But most contractors hire their subcontractors or suppliers on a handshake or, at best, a quote sheet, which does not contain an arbitration

provision. So if a controversy arises, such as a construction defect, the owner will file a claim against the contractor in arbitration. The contractor, however, cannot force the subcontractor that is responsible for the defect to arbitrate along with him. He will need to proceed with the owner in arbitration and then bring a separate lawsuit against the subcontractor for reimbursement. That will certainly add to the overall cost.

## 9. Subcontractors beware

If the terms of the contract between the general contractor and owner are incorporated by reference into your contract, you may be bound to arbitrate any disputes, even though your contract does not contain such a clause.

And if you are the winning party, guess what, you still need to file an action in court to have the arbitration award confirmed in order to be able to enforce it. So the court still gets its filing fee. An arbitration award is not worth the paper it is written on without a court judgment to go along with it.

## 10. Timing

One area in which arbitration usually has the advantage over litigation is the speed with which you receive a decision. Arbitration does not have a procedure whereby the parties can make motions, there is no jury selection process, little or no discovery, and this makes the process move more quickly. Many people are willing to sacrifice a good decision for a speedy resolution.

Do not treat the decision to arbitrate or litigate lightly. Investigate the arbitration organizations in your area, consult with your attorney and make an informed decision. **QR**

