20 Questions re Commercial Arbitration

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1. Why 20 Questions?

The library shelves are full of texts containing statutes, rules, court decisions, articles and learned treatises about the theory and practice of arbitration. Not a lot has been said in ordinary terms about what parties can expect from an Arbitrator or the arbitration process. As with my earlier "20 Questions re Mediation," I want to de-mystify arbitration so that it is better understood and accessed more easily. I thought a simple and frank conversation was the way to achieve those goals with respect to this important dispute resolution process.

2. What is commercial arbitration?

It is a consensual dispute resolution process that is put in motion by the parties to a transaction agreeing to have their disputes decided in an arbitral forum (versus in the courts). It is a private proceeding where the parties present their proofs to a neutral third party who renders a decision that resolves all issues related to the dispute. (NOTE: In complex matters, the parties may choose to have a panel of three arbitrators hear and decide the dispute.)

3. Is the Arbitrator a judge?

No. However, he/she functions in much the same way as a judge by issuing orders that direct the process, hearing the parties' evidence and argument, and determining whether a claim should be allowed and, if so, what relief should be granted.

4. How do disputes end up in arbitration?

By agreement between the parties to the dispute. As mentioned in Point 2, parties may agree to arbitrate their disputes in one of two ways: *Before a dispute arises*, by including an "arbitration clause" in their transaction agreement or entering into a separate arbitration agreement. *After a dispute arises* by agreeing to submit the dispute to arbitration (rather than commencing a lawsuit in a court of law). There are some circumstances where an arbitration agreement can be enforced against a non-signatory/non-party, but in the majority of instances, resort to arbitration requires an agreement between the contracting parties. Bottom line: Arbitration is a consensual process that is put in motion because the parties agreed to it.

5. What are the key defining features of arbitration?

I think there are five notable features that distinguish arbitration from court litigation: As mentioned in Point 2, *privacy* is a defining feature because arbitration is not a public process. The proceedings are not open to the public, there is no public record and in most instances the arbitration decision is not reported. *Reduced expense* is another feature because there is minimal discovery in arbitration and the merits hearing does not compete with a criminal calendar or other court business. *Finality* is another feature because arbitration awards are not appealable[1] and are subject to very limited judicial review. *Predictable forum* is a key feature because the inclusion of an arbitration clause in an agreement operates like a specialized forum selection clause and thus eliminates uncertainty over where to go to seek resolution of a covered dispute. Finally, the right of the parties to *select the arbitrator* is probably the most unique feature of arbitration. Parties to arbitration have the right to choose who is appointed to act as their arbitrator and, through that power, can make sure that they have someone at the end of the table who is familiar with the subject matter and laws related to their dispute.

6. Assuming one prevails in an arbitration, how is the arbitration award enforced?

If an award is not voluntarily adhered to, then the party seeking to enforce the award must look to the courts for help. Under the Federal Arbitration Act and the state arbitration acts (including the California Arbitration Act), there are simple procedures whereby the enforcing party files an application with the state or federal court to confirm the Award as a Judgment. Once an Award is confirmed, the Judgment is entered on the Court's docket and can then be enforced under the laws and rules governing enforcement of judgments (e.g., judgment debtor exams, recordation of an abstract of judgment, garnishment of wages, etc.).

7. If you agree to have your dispute decided through binding arbitration, do you give up the right to a jury trial?

Yes. Agreeing to arbitration vests exclusive authority in the arbitral tribunal to determine the covered disputes, which means that the parties give up their right to have a court hear and decide their disputes, as well as the accompanying right to request a trial by jury.

8. Is it a significant concession to forgo one's right to a jury trial?

Maybe, in simpler times when our courts were not so congested, but in the context of modern-day commercial disputes, I'm not so sure. Statistics show that very few civil disputes are decided by juries. For example, the statistics collected by the California Judicial Council show that, on average, Californians initiate approximately 1.4 million civil actions each year and that approximately 70 percent of those matters are dismissed or disposed of by means *other than trial*. Those statistic also show that of the civil matters that proceed to trial, only about *two percent* of the civil disputes filed are heard and decided by a jury. I would venture a guess that only a fraction of that two percent involves commercial/contract disputes. Against this backdrop, giving up the right to a jury trial in a commercial dispute does not appear to be a significant concession because it appears that parties to a commercial dispute rarely exercise that right.

9. Why do you think that jury trials are not the preferred resolution method for commercial disputes?

Several reasons: First, the cost of litigation is high and the rewards are uncertain, so most commercial disputes settle before trial. Second, it is more expensive and time-consuming to prepare and present a case to a jury than to a judge. Third, many business disputes involve complex subject matter that may be beyond the knowledge or expertise of the general populace which makes up a large proportion of the jury pool, so the parties may decide that they have a better chance of having their evidence on complex matters heard and understood by a judge versus a jury. This highlights one of the key features of arbitration mentioned in Point 6: namely, the parties' right to choose their decision maker.

10. What is the difference between presenting your case to an Arbitrator versus a Judge?

As mentioned in Point 9, the key difference is that in arbitration the parties can choose the person to whom they will present their case. In the court system, the judge is assigned based on his/her availability, not on the basis of subject matter or process expertise. Second, the parties do not compete for time on an Arbitrator's calendar. The days that are reserved for the parties' matter to be heard by the Arbitrator belong exclusively to them. That is not the case in a court system where civil trials must yield to the criminal calendar and other court business. Third, the hearing process is structured around the convenience and availability of the parties and their respective counsel and witnesses, rather than the convenience of the court. Finally, the process itself is more relaxed (e.g., pre-hearing problems are frequently sorted out via conference call with the Arbitrator), and the setting is more informal (e.g., proceedings are conducted in a conference room rather than a courtroom).

11. Some critics of arbitration contend that Arbitrators simply "split the baby" when rendering awards. Is that reality or myth?

Data published by the American Arbitration Association suggests that "split the baby" decisions are a myth. That study found that Arbitrators made a decision clearly in favor of one party 75% of the time and substantially denied 71% of all counterclaims.

12. How is the Arbitrator appointed?

The parties - if they can agree - have both the right and power to dictate who their Arbitrator will be. However, most parties look to a "provider" (e.g., the AAA) to assist them with the appointment of an Arbitrator. In the case of AAA, all of its panel members have been vetted and required to take several levels of arbitration training. The AAA provides the parties with a list of arbitrators – randomly selected based on geographic location and expertise – and the parties then strike 3 to 5 and rank 3 to 5 of the Arbitrators on the list. The Arbitrator with the highest ranking is appointed, assuming he/she is not disqualified due to conflicts.

13. Are there procedural safeguards to assure that an Arbitrator selected through the list method has no conflicts of interest?

This is a very complex topic that cannot be fully responded to in this Q&A paper. The short answer is "yes." Arbitrators – like judges – must disqualify themselves (absent consent by all parties) if they have a conflict based on a prior or current personal or professional relationship, a stake in the outcome of the dispute, or some other circumstance that might interfere with their ability to be impartial. Additionally, under California law, private arbitrators are required to provide an extensive list of disclosures and, based upon those disclosures, the parties have an absolute right to object to the proposed Arbitrator's appointment. (NOTE: California's disclosure requirements are more demanding than the disclosure requirements in other states.)

14. What are the most important skills an Arbitrator should have?

Based on a recent study by the AAA of what participants in arbitration like and do not like about the process, parties expect dispute resolution through arbitration to be less expensive and less time-consuming than litigation in the courts. So, I would have to say that the skills an Arbitrator needs to have to be effective from that vantage point are process expertise so as to direct and manage the process in a way that is expeditious; high energy so as to stay focused and engaged during a multi-hour/multi-day hearing in order to keep the matter moving forward; and flexibility so as to be responsive to the particular needs of the parties or the case.

15. With regard to the lack of appellate review of arbitration awards, what if the arbitrator makes a mistake?

Mistakes do happen. But if we look at the empirical data regarding appeals taken from court judgments (where parties believe the judge has made a mistake), that data suggests that mistakes (a) don't happen very often in terms of prompting the filing of an appeal, and (b) rarely rise to the level of warranting reversal of the judgment. As mentioned in Point 8, hundreds of thousands of civil actions are heard and decided each year in the courts. Yet the statistics compiled by the California Judicial Council show that only about 7,000 appeals are filed each year, and only half of those are briefed and decided by the courts of appeal. Of the cases heard and decided by appeal, only about ten percent end in a reversal of the judgment or order from which the appeal was taken. This suggests to me that the real value of the "right to appeal" is more strategic than remedial.

16. What do you think is the most misunderstood aspect of arbitration?

That the procedural and evidentiary rules governing court proceedings are applicable in arbitration. Arbitration is a separate and distinct process and is not subject to those rules – unless the parties' arbitration agreement expressly so provides. Having said that, most experienced arbitrators use the rules of evidence as a guide for determining admissibility of exhibits and the appropriateness of questions and testimony. But the Arbitrator can relax technical rules that seek to exclude evidence by allowing the proffered evidence "in," but then affording it such weight as the Arbitrator deems appropriate.

17. What is the most underutilized aspect of arbitration?

Party control over defining the rules that will govern the process. For example, in many contracts the arbitration clause simply states that the provider's rules will apply. In the case of providers like the American Arbitration Association and JAMS, their rules give the arbitrator the power to decide whether a dispute is arbitrable. Without that reference to the provider's rules, the arbitrability of particular disputes would have to be determined in a court of law. The provider rules are there to help parties define the rules that will govern the process, but they do not have to be accepted in total. Before a provider's rules are adopted, some thought should be given to including an express "carve out" to maintain court jurisdiction with respect to the arbitrability of any claim or dispute.

18. As an Arbitrator, what do you find to be the most taxing aspect of arbitration?

Three things really: First, cumulative evidence, meaning testimony from more than one witness and/or more than one exhibit offered to establish the same fact. Two, the use of adjectives instead of facts to make a point (in testimony or argument). Three, introducing voluminous documents or reports into evidence without testimony or explanation as to how such evidence is meaningful to the dispute or what issues such evidence proves or disproves and how/why.

19. Are there any circumstances where an arbitration award is more valuable than a judgment?

For businesses engaged in international commerce,[2] most definitely. The United States, along with more than 130 other nations, is a signatory to the United Nations Convention on the Recognition of Foreign Arbitral Awards that obliges each signatory nation to recognize and enforce arbitral agreements and awards. For a company based in the United States but doing business with a company based in another country, a judgment rendered by a court in the United States would not be entitled to recognition or enforcement because we have no treaties providing for reciprocity. However, an award issued by an arbitration convened in the United States or any signatory nation is entitled to recognition and enforcement in accordance with each country's laws concerning arbitration.

20. What can parties do to get the most out of their arbitration?

Two things really. First, before including an arbitration clause in a commercial contract, give consideration to the specific elements of the business transaction and relationship at hand. No single arbitration clause fits every situation. Things to think about when drafting an arbitration clause: Do the parties want any and all disputes between them to be decided by binding arbitration or only certain/narrowly defined disputes? Do the parties want a particular provider to handle the administration of the arbitration? What rules do the parties want to govern the arbitration? In what country, state or county do the parties want the arbitration to be conducted? Do the parties anticipate that they will want/need discovery from one another in the event of a dispute and, if so, how much? Are the parties entering into the business transaction based upon a particular set of laws and, if so, do they want that set of laws to govern the Arbitrator's determination of any dispute? Second, just like litigation, parties to an arbitration dispute should plan on being actively involved in all aspects of the proceeding from statement of the claims and defenses, to scheduling the evidentiary hearing, to voluntary exchange of information, to pre-hearing preparation for the evidentiary hearing. Just like litigation in the courts, parties and their representatives are welcome to attend all proceedings conducted as part of an arbitration. Party involvement generally leads to less delay and quicker resolution.

[1]There is currently a debate in the courts as to whether the parties can contract for appellate review (with the US Supreme Court saying "no" under the Federal Arbitration Act and the California Supreme Court saying "yes" under the California Arbitration Act), but the general rule is no appellate review.

[2] By "international," I mean the situation where the place where the transaction is to be performed is foreign to at least one of the parties, the parties to the transaction have their primary places of business in different countries, or at least one of the parties has significant assets in a country foreign to the other party (parties).