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ManagingRISK

Arbitration clauses – controlling your legal destiny

Commercial litigation can be best described as a battle where the party most able to retain its financial resources throughout the long torturous process wins. In an effort to devise a dispute resolution system that acknowledges this fact, Congress and New York State Legislature have enacted laws endorsing arbitration agreements in parties' contracts.

Arbitration clauses typically require litigants to submit their disputes to an arbitrator or panel of arbitrators, most often comprised of litigation attorneys or a retired judge who presides as "judge and jury" over the law and the facts in the case. In theory, this arrangement serves the public purpose of unclogging overburdened courts. More importantly, it provides a much more expedient means of resolving disputes. Arbitrations can be completed within a few months of the eruption of a business dispute, whereas litigation can drag on for years.

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Daily Record Columnist

Keep in mind, however, when drafting an agreement, the subject of which may someday prompt litigation, that mandatory arbitration clauses are unenforceable in contracts involving the sale of consumer goods, General Business Law § 399-c (McKinney's 2013). The courts have construed the term "consumer goods" broadly to prohibit enforcement of arbitration agreements relating to home construction and renovation, as well, *Ragucci v. Professional Const. Services*, 803 NYS2d 139 (2nd Dept. 2005); *Byrnes v. Castaldi*, 898 NYS2d 640 (2nd Dept., 2010).

Similarly, arbitration agreements that are unconscionable, are executed under duress, or are the result of fraud are unenforceable, *Hayes v. County Bank*, 185 Misc2d 414 (2000).

Subject to these limitations, the federal courts have stated that "the strong federal policy in favor or arbitration requires courts to resolve any doubts regarding the scope of arbitrable issues in favor of arbitration," *Provident Bank v. Kabas*, 141 F. Supp. 2d 310 (E.D.N.Y. 2001).

The state courts interpreting the state arbitration statutes are in agreement. If the client agrees that a particular dispute may better be resolved by arbitration rather than litigation, inclusion of a broad arbitration clause is recommended. Arbitration clauses defining disputes as any "arising out of" or "in connection with" the agreement between the parties raises the presumption that the dispute is arbitrable, *Provident Bank*, supra. p.316

Couple an arbitration provision with a choice-of-laws and forum selection provision and you have created a strong framework for resolving a dispute arguably to your advantage. In such a scenario, a party is able to select the "judge" trying the case, choose the law that applies to govern the issues to be decided, and determine where the trial will take place, all simply by including a few simple contract provisions. Clearly, as well, it is beneficial to have the ability to select an arbitrator who possesses some level of expertise in the subject matter at issue.

And while all of our own New York judges are worthy jurists, in a litigated matter you may be assigned a judge who spent the last few years sitting in the criminal or matrimonial part.

Arbitration is also designed to be relatively inexpensive. In one large commercial case, the arbitration filing fee would have amounted to over $200,000 according to the contract. The court refused to enforce the agreement as this clearly exceeded the reasonable arbitration administrative expenses, *Matter of Teleserve Systems, Inc.* 230 A.D.2d 585 (4th Dept. 1997).

Are there any disadvantages to arbitration, you may ask. Clearly, the same advantage to arbitration may serve as a disadvantage, namely, the cost. If you are placed in a defensive posture in a potential suit and the agreement contains no provision for recovery of costs and attorneys' fees, your opponent will be required to fund a lawsuit.

The obvious question then arises — who is better positioned to fund lengthy litigation? The sheer cost of litigation rather than

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arbitration may serve as a deterrent to an adverse party who may be equivocating about filing suit.

The second disadvantage exists by reason of the absence of full discovery in arbitration cases. Parties waive their rights to full discovery in arbitrated matters absent any contractual provision to the contrary. In complex commercial cases, this could amount to trial by ambush.

Trial attorneys are denied their typical tools of litigation, depositions and disclosure, in the streamlined process of arbitration. Of course, if you are considering an arbitration provision in an agreement which may lead to complex commercial arbitration, you are well advised to provide for discovery within the provision, if the benefits of discovery will outweigh the additional costs to your client.

By design or by accident, some litigants have pursued discovery in litigation, and then only later requested arbitration. The courts have stated that they do so at their peril. If you cause your opponent to incur significant litigation costs by pursuing discovery, you may be deemed to have waived your right to enforce an arbitration agreement, *Byrnes v. Castaldi*, 72 AD 3d 718 (2nd Dept 2010).

Arbitration, therefore, must be viewed as an appropriate method of dispute resolution in the correct context. It must be examined carefully, however, as the prudent business person knows that the path to the outcome is often as important a concern as the outcome itself.

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