PROS AND CONS OF CONSTRUCTION ARBITRATION

By: William "Bill" Hopson
Construction Practice Group Leader
bill.hopson@troutmansanders.com • 404.885.3322

The use of private arbitration in lieu of the courts to resolve disputes has been prevalent in the construction industry for many years. In this article, we will review for you some of the advantages and disadvantages of arbitration, and comment on the extent to which arbitration has kept its promise of being a faster, cheaper and better alternative to litigation.

Cost of Arbitration and Litigation

Many in the construction industry embraced arbitration with the hope that arbitration would be a less-expensive alternative to a trial in the court system. Increasingly today, arbitration fails to keeps its "less expensive" promise.

For disputes handled through the American Arbitration Association ("AAA"), the most popular administrator of construction arbitrations, initial filing fees are required and range from a minimum of $750 (for claims less than $10,000.00) to more than $10,000 (for claims over $5 million but less than $10 million, a $10,000.00 filing fee applies). The AAA also charges administrative fees ($3,250 for claims between $1 million and $5 million) during the process. These fees do not include the arbitrators' professional fees and expenses, which often exceed several thousand dollars per day. In larger, more complex cases with multiple arbitrators, the various fees can become six digit expenses. In contrast, court fees for filing a lawsuit are usually no more than a few hundred dollars; and the taxpayers, as opposed to the disputing parties, bear the cost of the judges, juries and courtrooms.

Other ADR firms (e.g., the International Institute for Conflict Prevention and Resolution) charge a flat rate for administrative services regardless of the size of the claim. And, a few ADR firms (e.g., Closure ADR) do not charge large upfront fees or impose very restrictive refund policies on the users of their services. Still, the legal fees incurred in larger, complex arbitrations are frequently similar to those legal expenses experienced in litigation. Many of the high cost aspects of litigation (e.g., liberal discovery proceedings) have become commonplace in arbitration proceedings.

Speed of Dispute Resolution

The general perception is that arbitration is faster than litigation. More and more, arbitration is becoming nearly as time-consuming as the court system. In the larger and more complex cases, arbitrators frequently permit the parties to engage in a substantial amount of discovery—large document productions, depositions and the all-too-common discovery disputes. Also, coordinating the availability of multiple parties and arbitrators to schedule blocks of several days, weeks or more for hearings is often very difficult. It is not unusual for larger arbitrations to occupy more hearing days than would be experienced in a similar court proceeding, and for the arbitration matter to take more than a year to proceed from filing to first hearing. Recognizing that "justice delayed" is at least very expensive justice, owners and contractors often attempt to streamline the arbitration process through creative contract drafting. Earlier this year, the International Institute for Conflict Prevention and Resolution (CPR) crafted a set of Expedited Arbitration Rules. Troutman Sanders' Frank Riggs worked with CPR on the creation of these new rules for contractors and owner frustrated with the delay and high costs which plagued many arbitrations, the CPR model is worthy of consideration.

Privacy Concerns

Generally, arbitration is a private affair and the specifics of the dispute, documents, contracts, and other sensitive materials are kept out of the public eye. However, there is no guarantee that the losing party will not seek to have an award vacated by a court, thereby introducing much, if not all, of the proceedings into the public domain.

Quality of the Decision-Maker

One area in which arbitration generally is viewed as more attractive than the courts is the ability of the parties to select an arbitrator specifically qualified to hear a construction dispute. It is usually possible to find an arbitrator who has many years of experience in the construction industry and who will bring construction knowledge to the decision-making process—knowledge that most judges and all juries lack. It usually is quite difficult to explain the nature of construction contracts, industry standards and technical concepts to a judge or jury. By using an experienced construction arbitrator, a party increases its chances of getting a more informed resolution. This also can make the hearings more efficient, as the parties will spend less time and effort educating the decision-maker on the technical aspects of the case. Many also will argue that arbitration is more likely to avoid a wild and unpredictable result—the type of result that parties fear when they place their dispute in the hands of a lay jury.

Finality of the Result

Generally, if a trial judge or jury makes an error, the aggrieved party has right to appeal the decision through a formal, defined appellate process. One of the attractions of the arbitration concept, for those seeking a speedier process, is that there is generally no right to appeal the decision of the arbitrator. An award, if not immediately satisfied, can

be quickly turned into a court judgment and executed upon by the winning party. In recent years, losing parties have increasingly turned to the narrow band of statutory and common-law exceptions which allow a court to review an arbitration award for errors. Most states, as well as the federal judicial system, specify certain limited grounds upon which a losing party can request a court to overturn, or vacate, an arbitration award. Most of these grounds are quite rare and deal not with the "correctness" of the award, but the nature of the proceedings. For example, the Federal Arbitration Act allows an award to be vacated by a court where the award was procured by corruption or fraud, the arbitrator was partial or corrupt, the arbitrator wrongfully refused to postpone a hearing or hear evidence, or where the arbitrator exceeded his/her powers or simply failed to make a definite award.

Most federal courts, and some states, have added a ground for vacating an arbitration award where the arbitrator has "manifestly disregarded" the law. This has been a constant source of controversy, since it essentially requires that a court review the arbitration proceedings to determine if the arbitrator made a legally incorrect decision. Many parties have argued that this is simply nothing more than a second review of the merits of the case—a second bite at the apple and the kind of thing arbitration is designed to avoid. Some courts are starting to agree and are either limiting the cases in which they will review an arbitration award for "manifest disregard" or are threatening sanctions against parties who ignore the limited appeal standards.

A good example of this is the case of B.L. Harbert Int'l, LLC v. Hercules Steel Co., 441 F.3d 905(2006), an arbitration appeal in which the Troutman Sanders Construction Practice Group represented the prevailing party. After losing the case before the arbitrator, the contractor appealed the decision and argued that the arbitrator's interpretation of the contract scheduling requirements constituted a "manifest disregard" of the law. The United States Court of Appeals for the Eleventh Circuit (covering Georgia, Florida and Alabama) affirmed the lower court's rejection of the contractor's appeal. In so doing, the court warned future litigants and their attorneys that "if a party on the short end of an arbitration award attacks that award in court without any real legal basis for doing so, that party should pay sanctions." Other courts of appeal have made similar pronouncements. There is new hope that arbitration will realize its goal of becoming the last step—and not just a first step—in resolving construction disputes.

Conclusion

A party often will need to decide whether to enter into a contract with an arbitration provision long before any foreseeable dispute arises. A party must make this decision on a case-by-case basis after carefully analyzing the nature of the contract, the party they are dealing with, and the above-mentioned pros and cons of arbitration. A quality construction lawyer can assist in assessing the risks of arbitration, as well as offer ideas on drafting an arbitration provision that eliminates or limits some of the less desirable aspects of arbitration.