Reimagining Arbitration

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The growth of commercial arbitration over the past three decades is principally attributable to the U.S. Supreme Court's broad embrace of the arbitration process and its rejection of legal doctrines that attempt to limit its effective use. Arbitration was transformed in the 1980s and 1990s by a series of decisions interpreting the Federal Arbitration Act (FAA) that have made arbitration more accessible and its enforcement more predictable. This development in turn has encouraged business users to consider arbitration for many of their larger and more important disputes and has encouraged arbitrators and providers to promote arbitration as an effective alternative to the court system.

Popularity has not been without drawbacks. As counsel have become more sophisticated in dispute process design, arbitrations now often incorporate many elements of a court trial, which, in turn, has complicated the management and conduct of those proceedings. Litigation constructs such as pleadings, broad-based discovery, provisional relief, dispositive motions, and formal rules of evidence are now commonly a part of arbitration, as is the review of arbitration orders and awards on the merits and for procedural error. One only has to consider the number of process issues included in the 2000 revision of the Uniform Arbitration Act to see this dynamic change. This trend also explains why there are so many more decided cases addressing arbitration issues. Arbitration is now often referred to as the "new litigation" or by such portmanteau terms as "Litarbigation," as recently featured in an advertisement for the JAMS arbitration practice.

One consequence of these changes has been increased expense and delay. Many traditional users of arbitration have realized that they cannot have their cake and eat it too. The more processes parties employ, the slower and more expensive the arbitration. It is even possible that such an arbitration will take as much time as, or more time than, equivalent court litigation. In these circumstances, where there is no effective right to appeal arbitral awards, the litigation choice may become preferable.

What has caused this shift of opinion about commercial arbitration, and what changes to the process will again make it a viable alternative to litigation? To preserve the benefits of arbitration, it is necessary to address the processes that drive expense and delay, such as discovery and motion practice. Each of the stakeholders in the arbitration process—business users and inside counsel, outside counsel, arbitrators, and provider organizations—has a role to play in addressing solutions that restore vitality and efficiency to arbitration.

Business users and their inside counsel are in the best position to determine how and when arbitration will be used to

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settle a business dispute and what form that process ought to take. They act most effectively by including dispute resolution clauses in their transactional documents but also by proposing arbitration after a dispute has arisen and where no pre-dispute agreement exists. But often these choices are made without much thought, particularly where the transaction's focus is the venture's future success and not the possibility of conflict. Often a "boilerplate" arbitration clause is inserted in the document at the eleventh hour, or a decision is made (consciously or inadvertently) not to address dispute resolution at all.

Careful and timely efforts at dispute assessment and design can ensure an effective process. Such a process likely will include a negotiation or mediation step, reasonable limits on the scope of discovery, overall time limits on the arbitration, and the designation of one rather than three arbitrators whenever possible. Selection of outside counsel to conduct the arbitration is also crucial. Some counsel understand the arbitration process and how it differs from litigation and are willing to conduct the process with the goals of achieving economy and efficiency.

Several choices are critical for house counsel in drafting the arbitration clause and managing the process. First, use arbitration in a way that best serves economy, efficiency, and other business priorities. Be deliberate about choosing between "one-size-fits-all" arbitration procedures with lots of "wiggle room" and more streamlined or bounded procedures. Opt for clauses that require at least one pre-arbitration settlement step, such as negotiation or mediation. Make that clause effective by requiring that it be complied with before arbitration can start, but design it so that it does not delay the process unduly. (Model clauses and clause drafting guides are published by the American Arbitration Association (AAA) and JAMS and are available on their respective websites, www.adr.org and www.jamsadr.com.)

Next, limit discovery to what is essential; do not simply replicate court discovery. Decisions about discovery in the arbitration clause cannot accurately anticipate the scope of the eventual proceeding, so generic choices are most prudent. The administering institution selected in the clause, and its rules, will initially define the scope of discovery. The clause may add restrictions or additions to rules-based discovery. It sets the tone for the later discussions in the course of the arbitration about what discovery then appears to be reasonable and necessary for the proper preparation for the hearing. The key is to choose a scope of discovery that is proportionate to the magnitude of the dispute and particularly to limit excessive e-discovery.

Set specific time limits on arbitration and make sure they are enforced. There are a number of techniques for imposing time limits on the arbitration process. An outside limit could be specified (for example, one year from the commencement of the arbitration to the issuance of the final award) or the provider's rules may be relied on where they impose such limits (such as JAMS Expedited Procedures described below). Care should be taken not to set limits that are not achievable, and discretion should be accorded to the arbitrator to vary these limits in exceptional circumstances.

Use "fast-track arbitration" in appropriate cases. Some institutional rules provide streamlined versions of their standard rules (such as AAA's Expedited Procedures within its Commercial Rules or JAMS Streamlined Rules). Care should be taken to opt into these fast-track procedures only in appropriate cases, and pre-dispute agreements must be reassessed after the dispute arises to confirm that the pre-dispute choice is consistent with the attributes of the actual case.

Stay actively involved throughout the dispute resolution process to pursue speed and cost-control as well as other client objectives. It is one thing to draft a thoughtful clause, but it is another to stay involved in the process once it has been turned over to outside counsel. Direct participation in the pre-hearing conference, regular monitoring of the progress of the arbitration, and participation in strategic decisions all will help to effectuate the earlier structural choices. Lessons learned will help to guide decisions in the next case.

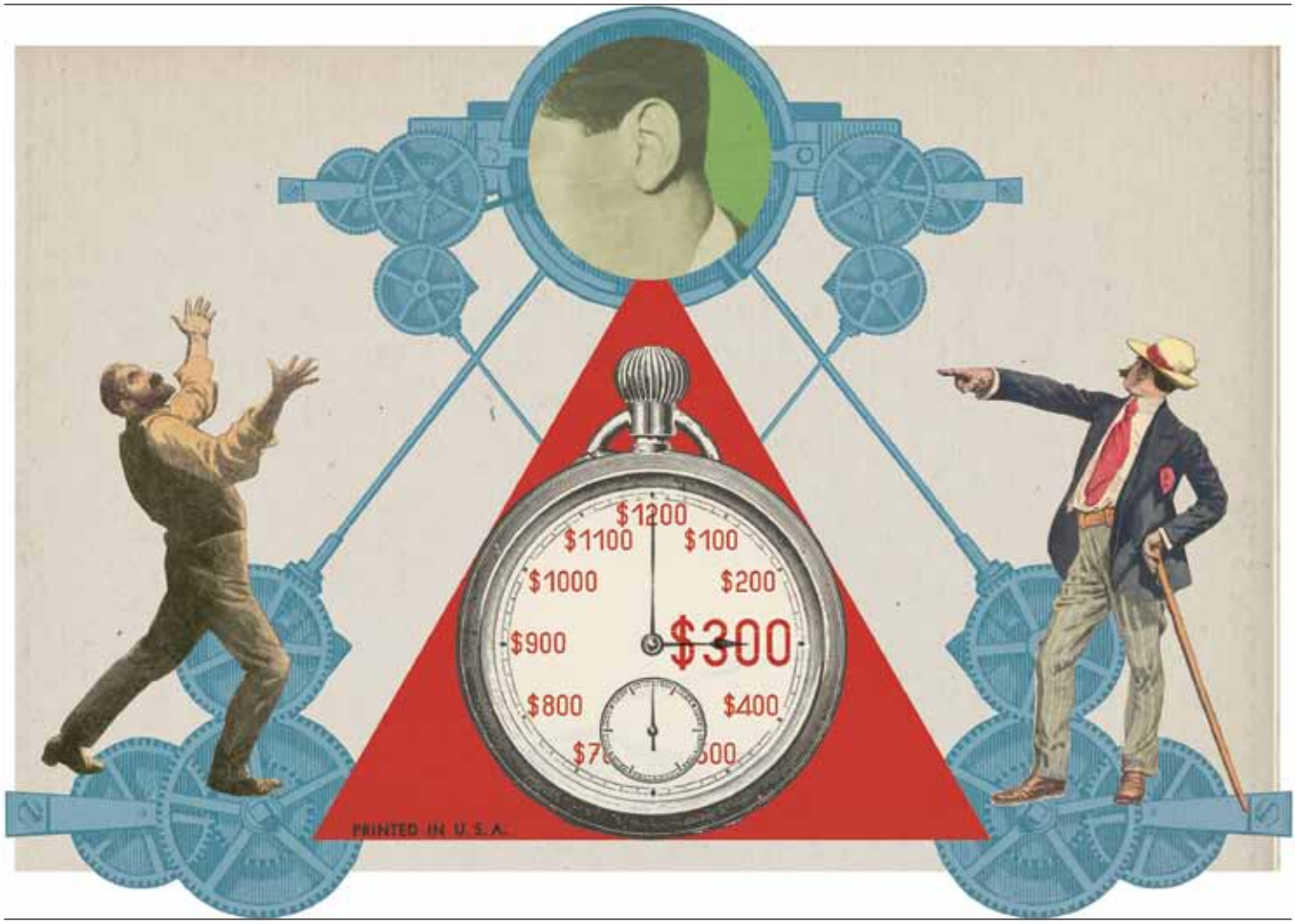
Selecting Participants

Select outside counsel for arbitration expertise and commitment to business goals, and select arbitrators with strong case-management skills. The selection of an arbitrator willing and able to participate in the design process and effectively manage the chosen process is crucial in achieving economy and efficiency. The experienced managerial arbitrator can also advise against inappropriate process choices.

Establish guidelines that allow for issues, claims, defenses, and parameters for arbitration to be fleshed out early in the process. There are many opportunities for sequencing or limiting issues. Case management conferences and carefully drafted scheduling orders will help guide the parties through the necessary steps.

Use a single arbitrator in appropriate circumstances. It is often difficult for the parties to admit that their case does not warrant the added expense of a tripartite panel, but in fact most commercial cases are more efficiently handled by a sole arbitrator. Pre-dispute clauses that require three arbitrators (drafted at a time when the magnitude of the dispute is necessarily unknown) often place the parties in a process that is too expensive for the dispute that arises. It is a better practice to provide for a sole arbitrator in most cases and then agree on a tripartite panel in those relatively rare cases in which the magnitude of the dispute appears to warrant a panel.

Finally, specify the form of the award, and do not provide for



judicial review for errors of law or fact. Most commercial arbitration awards are reasoned because parties want to understand the basis of the decision. Some arbitration clauses seek to authorize courts to review arbitration awards for errors of fact or law. These provisions are usually not enforceable under the FAA, but even when they are, they usually entail significant additional process costs and delays without commensurate benefits. Most business users should accept the limited judicial review provided in the grounds for vacatur set forth in the FAA. Alternatively, a tripartite panel provides some protection against aberrational awards of a sole arbitrator, and some providers (such as JAMS) offer a well-designed appellate arbitration procedure.

Outside counsel also play an important role in working with the other stakeholders, including the arbitrators, to design a process that is both fair and efficient. Flexibility is one of the main benefits of arbitration. Because arbitration is contractual, the parties are free to stipulate to appropriate procedures, but even experienced counsel do not always take advantage of their ability to tailor the arbitration process to fit a particular case. Here are some ways for outside counsel to ensure a fair and efficient process.

First, prepare a clear statement of claims. At the time of filing, and certainly before a preliminary conference, it is important to file a statement of the case, including a short summary of the background facts and a list of all claims. While the damages claim may not be complete and may have to be calculated after working with experts, the numbers can be brought up to date later. The arbitrator can establish a procedure for specifying and quantifying damages.

Lengthy litigation-style formulaic pleadings are neither required nor helpful. Claims, answering statements, and counterclaims should be written in a straightforward and concise manner. What is important is that counsel and the arbitrator are clear on the claims and defenses asserted. Virtually no pleadings are "required" in arbitration, but this is often the only statement of the case the arbitrator will see until briefs are submitted shortly before the evidentiary hearing.

Next, give the preliminary conference ample attention. The preliminary conference is extremely important to the arbitration process. At this meeting, the participants discuss the particulars of the case and the parties' goals. Moreover, they can begin to collaborate with the arbitrator to design an effective

Illustrations by Mark Lazenby

process to suit the case. This conference is the time to agree on a range of items, including the hearing dates and location, the appropriate scope of discovery and the time for counsel to submit a discovery plan, and the dates for exchanging witness lists, arbitration exhibits, and pre-hearing briefs. The arbitrator will also discuss the form of the award so that all participants are clear on what to expect. These arrangements are crucial to laying the foundation for efficient hearings.

The preliminary conference is the first opportunity in most cases for the arbitrator to interact with counsel and the parties and to express carefully considered views about possible process alternatives, to comment on issues raised by the clause or submission agreement, and to begin the process of focusing on possible limitations on key aspects of the process such as limited discovery and e-discovery and potential bifurcation or other structural issues. The determinations made at the preliminary conference will be documented in a scheduling order prepared by the arbitrator. In all of these matters, arbitrators are empowered to manage the process and to make the necessary rulings if counsel cannot reach agreement.

Arbitrators usually work from agendas or checklists that are sent to counsel before the conference, and they expect counsel to meet and confer on these issues at that time. It is common for such checklists to include at least the following points: arbitrability (as to parties and issues) and resolution of disputes as to the arbitration's scope; status of party-appointed arbitrators (neutral/non-neutral); compliance with applicable disclosure process and confirmation of arbitrator's appointment; governing law; applicable rules; applicable arbitration law (FAA or state arbitration act); venue of the arbitration hearing; exchange of information (document exchange, securing documents in the possession of third parties, depositions, e-discovery issues, designation and discovery of expert witnesses, protection of confidentiality of documents exchanged for the hearing, and the like); procedures to resolve discovery disputes; dispositive motions; identification of witnesses and use of witness statements in lieu of direct examination; identification of exhibits and format for presentation at the hearing (notebooks, electronic storage only, and the like); applicability of the rules of evidence; hearing times and possible limitations; transcript and designation of an "official record"; bifurcation of issues; briefing pre- and post-hearing, and provision for final argument; remedies sought and form of award; attorney fees and costs; and any agreed appellate procedure.

After the preliminary conference has been held and the arbitrator has issued a comprehensive case management order setting forth the procedures and schedule that will govern the arbitration, outside counsel can take several additional steps to ensure a fair and efficient process. First, set hearing dates and stick to the schedule. Arbitration hearings are best held on consecutive days. Efficiency goes out the window when the hearing is not continuous. It may make sense to schedule an extra day or two in case the hearings take more time than expected, because continuances can be extremely expensive. A huge cost is involved in preparing for hearings and then having to remobilize months later. Not only is a continuous hearing more efficient for counsel, but also it allows arbitrators to base decisions on their recollection of testimony and argument. Also, it often is difficult to reschedule because the calendars of parties, counsel, witnesses, and arbitrators must be considered.

Second, limit motion practice. Motions in limine and dispositive motions can be wasteful at arbitration, especially if there has been little discovery. Dispositive motions involving issues of fact are rarely granted in arbitration, but there are some matters for which a motion for partial summary disposition might provide an opportunity for shortening, streamlining, or focusing the arbitration process—as, for example, where arbitrators are able to rule on a statute of limitations defense, determine whether a contract permits claims for certain kinds of damages, or construe a key contract provision. One of the grounds for vacating an arbitration award is the arbitrator's refusal to hear relevant evidence. *See* FAA § 10(a)(3). Arbitrators want to prepare an award that ultimately will be confirmed, and their rulings will be influenced by an interest in protecting the final award.

Separating Hearings

Third, consider whether the hearings should be bifurcated into liability and damages phases, for example, or otherwise set to move forward in phases. The attorneys may want to confer with the arbitrator to reach agreement on the order of proof so that the hearings proceed smoothly. For example, in a complex case involving claims of breach of fiduciary duty and fraud arising from the handling of partnerships and other entities, claimant and respondent may agree to divide the hearings into phases. Thus, each discrete issue may be decided before moving to the next phase, rather than adhering to the usual order in which claimants present their entire case and respondent's case follows. Finally, if there are witnesses who may be unavailable, discuss how to preserve their testimony or make plans to have them testify via video or Skype. Most arbitrators allow these arrangements to assist counsel in presenting the case efficiently.

The next important step is to limit discovery. In the early days, arbitration discovery was limited to a broad exchange of relevant and nonprivileged documents as well as witness information. As arbitration has become more like litigation, there has been more discovery in business cases. Discovery is the

most expensive part of any arbitration, especially now that so much of it involves electronically stored information. There is widespread agreement that the principal culprit in overly long and expensive arbitration is excessive discovery and e-discovery.

It is in the parties' best interests to rein in costs. Establish a discovery plan, being mindful that discovery should be proportional to the complexity of the dispute. Agree to limit electronic discovery to avoid excessive costs.

Both sides will be required to identify witnesses and, for expert witnesses, to establish a procedure for exchanging biographies and reports. If percipient witnesses will also give expert testimony, that information should be disclosed. Counsel sometimes request an opportunity to serve interrogatories and requests for admission, but because it can be expensive and often fails to elicit significant information, written discovery is not favored in arbitration.

Taking some depositions may save hearing time. Experienced arbitrators know that listening to an attorney examine a witness extensively can be a poor use of hearing time. Agree on some depositions, limited in number and in duration. If agreement is not possible, an experienced arbitrator can make a ruling and, for example, allow each side a specific number of depositions, not to exceed a prescribed duration for each.

The discovery process should be designed for the efficient exchange of information. Arbitrators have a duty to help the parties achieve a level of information exchange that ensures a fair hearing, is proportionate to the case, and does not cause undue delay or expense. Arbitrators are empowered to manage discovery and avoid scorched-earth maneuvers. *See* CPR Non-Administered Arbitration Rules, Rule 11; JAMS Comprehensive Rule 17(d); AAA Commercial Rule R-21. That power may include the power to sanction, and it certainly includes the right to draw adverse inferences.

The arbitrator should assess the discovery permitted by the applicable rules and the clause and should engage the parties in discussion of their need for particular information. That task continues as the arbitrator manages the process to hearing and engages the parties whenever there is a dispute about the scope of discovery or the execution of the agreed discovery plan. Arbitrators should promptly address and resolve any issues that might disrupt the case schedule. Efficient dispute resolution procedures (letter briefs or oral submissions rather than formal motions, and telephone calls rather than formal hearings) help to keep things on track and demonstrate that the arbitrator is committed to managing a successful process.

Outside counsel should also agree on a limited number of hearing days. The "chess clock" approach, whereby the parties divide time equally, is one of the best ways to avoid unnecessary costs. This approach has the added benefit of ensuring that the arbitrators will hear a clear and concise presentation of claims and defenses. Limited time also ensures that hearing time will not be wasted in rambling and confusing cross-examinations. This approach worked well in a recent licensing dispute involving patents for medical devices. The attorneys were able to adhere to the schedule and present the case with some time left over. Time limits discipline everyone to focus on the most important documents and testimony.

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There are many other approaches to encouraging efficiency. Sometimes counsel will present percipient or expert direct testimony in writing with an opportunity for live cross-examination. Also, documents can be admitted without formalities if there are no objections to items on the exhibit list. Demonstrative exhibits, shared with opposing counsel in advance of the hearings, can help arbitrators get up to speed quickly on the chronology of events or on damages theories.

Because the rules of evidence generally do not apply in arbitration, raising numerous objections is not useful. It may be important to object to hearsay to alert the arbitrator or the panel to it, but that objection will only go to the weight of the evidence and will not preclude it. Save objections for important matters and avoid repeated interruptions.

None of these techniques for making arbitration economical will work unless the arbitrators are experienced, decisive, and willing to make necessary rulings. Good arbitrators actively manage the proceeding and should be skilled at moving the hearings along and making rulings as needed in accordance with the rules. Active arbitrators assist in dealing effectively with cumulative evidence and avoiding gamesmanship. Counsel should review the biographies of the proposed arbitrators, including examples of cases they have handled, and ask for references. Particularly in large cases, it is customary to interview potential arbitrators—not ex parte, of course, but jointly with opposing counsel. During these interviews, arbitrators should not be asked about any of the issues in the case but, rather, about their experience, style, and managerial skills.

The skills required of the arbitrator as manager of the process are threefold: an understanding of the process elements of arbitration, a willingness to work with the parties and counsel to design a process well suited to the particular case, and the ability to manage the chosen process through the hearing. Sophisticated parties understand the importance of these skills and regard their opportunity to choose the arbitrator as perhaps their most important "process" choice. Arbitrators who possess these skills are referred to as "managerial arbitrators." A managerial arbitrator assumes the primary responsibility for managing the chosen process to achieve the parties' goal of an effective and efficient proceeding and to strike a balance between efficiency and fairness. These responsibilities and the techniques to achieve them are well understood in the profession.

As criticism of costly arbitration has grown stronger, some providers are responding by offering more than one kind of arbitration procedure and revising their rules with the goal of helping the parties design a process to fit the case. The AAA has fast-track rules for small-dollar cases as well as rules for large and complex cases, and these rules give arbitrators the power to control the process. The Center for Public Resources offers an Economical Litigation Agreement and rules aimed at providing an efficient process. JAMS has Streamlined Rules aimed at managing some of the smaller cases in which no claim or counterclaim exceeds $250,000.

Counsel perform an important role in selecting the right arbitrator, but the post-appointment interaction with the arbitrator is even more important. Preliminary conferences have already been addressed. The arbitrator plays an important role in establishing a workable and proportionate discovery plan and managing discovery to achieve economy in the exchange of information necessary to allow effective presentation of claims and defenses. He or she also controls the extent of motions permitted or filed and avoids unnecessary pre-hearing disputes about legal issues. Finally, an effective arbitrator creates a professional atmosphere and insists that counsel cooperate with each other and with the arbitrator in all procedural aspects of the arbitration.

Careful pre-dispute planning and thoughtful process choices after the dispute actually arises will ensure that the parties achieve their objective of a tailored, efficient process that presents the opportunity for a reliable but economical resolution of their dispute. The flexibility of arbitration, including the ability of attorneys and parties to work with the arbitrators to tailor the process to fit a particular case, can be an enormous benefit to all participants. With the efforts of all stakeholders, commercial arbitration will be "reimagined" to truly meet the needs of business users. ■