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THINKING BIGGER PICTURE: WHEN TO SACRIFICE THE BENEFITS OF ARBITRATION IN FAVOR OF LITIGATION

Smart Business Chicago

PEOPLE

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Many business managers include arbitration provisions in their companies' contracts. The prevailing philosophy being that arbitration is preferable to traditional litigation via the court system because it is private, speedier and less expensive. Under certain circumstances, however, a party may prefer to litigate a particular dispute in court even though it previously included an arbitration provision in the relevant contract.

"In such a situation, depending on the dispute and the arbitration provision, a party may be able to avoid arbitration and assert or defend its claim in a state or federal courtroom," says Joshua E. Liebman, a partner at Novack and Macey LLP.

Smart Business spoke with Liebman about choosing traditional litigation despite the existence of an arbitration provision.

Why would a company choose not to arbitrate?

There are many reasons why a company may prefer to litigate in court as opposed to resolving its dispute via arbitration. For example, it may believe that it needs the broad discovery permitted by the courts, which is typically limited in an arbitration proceeding. Or, a party may believe that it has a strong technical legal defense that is more likely to be enforced by a court bound by the law than by an arbitrator who is not subject to review by the appellate court and may be inclined to seek a more equitable resolution. Also, a party may want to avoid arbitration if there is too much at stake. The substance of an arbitrator's award is not subject to review on appeal. Rather, a court's review of an arbitration award is limited to whether

the arbitrator acted within the scope of his or her authority and whether the award is consistent with the terms of the underlying contract. A party may prefer to have the protection of appellate review in a substantial dispute.

Can a party that prefers litigation be forced to arbitrate?

Arbitration is contractual by nature. That means that if a party contracts to arbitrate a dispute, it is bound by its agreement to do so. On the other hand, a party cannot be forced to arbitrate any dispute that it has not agreed to submit to arbitration. Accordingly, even if a valid and enforceable contract containing an arbitration provision exists, a party may refuse to arbitrate when the dispute is beyond the scope of the arbitration provision.

Based on the previously mentioned prevailing philosophy that arbitration is preferable, contractual parties often attempt to nullify a 'beyond the scope' argument by inserting broad, all-encompassing language into their arbitration provisions that subject to arbitration 'any and all disputes arising out of or relating to the agreement.' However, if instead of using this broad stock language the parties take the time to draft a narrowly tailored arbitration provision that identifies certain disputes

for arbitration or excludes certain disputes from arbitration, then courts will not force a party to arbitrate a dispute that is beyond the provision's scope.

Who decides whether a claim is subject to the parties' arbitration agreement?
Under federal law, a court determines whether the parties are bound by a given arbitration agreement and whether that agreement to arbitrate applies to a particular type of controversy. Under Illinois law, if the arbitration agreement is clear, the court makes the initial determination. If the language is broad or uncertain, the arbitrator decides. In all events, parties can contract to submit the question of 'arbitrability' to the arbitrator.

What can business managers do to avoid arbitrating disputes that they prefer to adjudicate in the courts?

It begins and ends with the arbitration provision. If there are specific categories of disputes that a company prefers to resolve in the courtroom, it must identify those disputes and draft an arbitration provision that excludes them. It is crucial that business managers think about the effect of including arbitration provisions in their contracts and craft those provisions to meet their companies' needs. Arbitration provisions are not one size fits all.