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A Non-Improvement In Arbitration Of Construction Disputes

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A Non-Improvement In Arbitration Of Construction Disputes

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By David E. Boelzner, Esq.

In the past, I have pointed out the disadvantages of arbitration as a means for resolving construction disputes. I argued that there are important rights given up when parties waive access to the courts, not least of which is the benign hovering presence of a reviewing court to keep the adjudicator on the straight and narrow, particularly as to procedure. The arbitration

clauses ubiquitous in standard construction contracts do not, in my experience, yield significant cost savings over traditional litigation in court, despite the sacrifice of these protections.

I continue to believe this is sound advice. But there are two phenomena that complicate the matter and, unfortunately, preclude the full relationship of trust and shared interest implied by the term "partnering."

If it isn't cheaper, then there can be very little to recommend it. Arbitration is often quicker, though not necessarily so, and it is usually final, as there are no practical grounds for appeal. But that can also be its shortcoming, for a judge with no constraint based on his decision being reviewed can act capriciously. The theory is that this allows for rough justice, without all the niggling technicalities that plague formal litigation. But technicalities such as the rules of evidence - generally treated quite cavalierly in arbitration or ignored altogether - exist to protect the reliability of the decision-making. Far too often a client is frustrated by an arbitrator's ad hoc acceptance of some written statement by a person not present and therefore not subject to challenge. The hearsay rule protects against this sort of abuse in court; but an arbitrator is apt to say, "I'll give it appropriate weight in view of the circumstances." You'll never know how much weight it was given because arbitrators seldom explain the reasoning behind their awards. Even if they did, there is no appeal to correct errors of reasoning, anyway.

One of the drawbacks I mention in evaluating the tradeoff is the cost of paying the arbitrator(s) and the overhead fees of the arbitration administrator, which in many cases is the American Arbitration Association. AAA has sought to address this problem of expense in certain kinds of cases, and its new rules (viewable at www.adr.org) are worth a look.

Why Shouldn't a Lawyer Dislike Arbitration?

Before discussing this topic, however, I should confront the cry of "sour grapes." Isn't it natural that a lawyer, one who plies his trade in ponderous and wasteful court adventures, would be hostile to an "alternative" dispute mechanism that circumvents him and his machinations? The simple answer to this reasonable question is that in cases involving any significant amount of money, lawyers are not eliminated by going to arbitration: they simply handle a different sort of case. At any given time, a third to a half of my construction cases are arbitrations. If there's real money at stake, clients will rely on lawyers, no matter the forum.

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The fact of lawyer involvement is admittedly a principal reason arbitration isn't the bargain it is sometimes thought to be. Though of lesser magnitude than legal fees, these expenses can be a genuine impediment to seeking adjudication. AAA's initial filing fee for a claim between \$75,000 and \$150,000, a quite common range for construction claims, is \$1,250; any counterclaimant will pay the same fee, and a case administration fee of \$750 will also be assessed. Then there is the arbitrator's fee, which can run from \$150 to \$350 or more per hour. In court you don't have to pay the judge - in fact it is decidedly frowned upon!

Two years ago, in the case of *Green Tree Financial Corp. v. Randolph*, the United States Supreme Court raised the possibility of an arbitration agreement being invalidated because the arbitration fees (which were AAA's) were too high and effectively precluded access to the dispute-resolution mechanism. In light of this case, AAA issued its consumer rules to address this problem. The rules are clumsily drafted, however, and only benefit "consumers" with small claims; small businesses doing work for consumers - such as architects and engineers - actually end up carrying more of the cost.

Consumer claims are classified according to the amount of the demand. Up to \$10,000, consumers pay no administrative fee, the business pays the entire \$500 fee, and the parties split the arbitrator's fee, capped at \$250 for a desk arbitration, i.e. a submission on papers only, and \$750 for a hearing. Between \$10,000 and \$75,000, the business again pays the entire administrative fee, \$750, half of the first day's capped arbitrator fee of \$750, and all of the fee thereafter. Over \$75,000, the claims follow AAA's usual commercial fee structure. Under this reform, then, the architect doing work for a consumer renovating her home could end up footing the major portion of the bill for arbitrating a dispute over the project.

Sometimes Arbitration Doesn't Follow Legal Precedent

One of the flaws lawyers see in arbitration is the arbitrator's frequent disregard of law or contract terms. AAA makes a stab at addressing this objection in its new rules, but it is a feeble thrust. The rules say the arbitrator "should apply any pertinent contract terms, statutes, and legal precedents" The problem is that the word "should," especially when compared to the use of the word "shall" in the preceding paragraph, seems to render this a mere exhortation rather than a rule.

Similar language ambiguity casts doubt on the effect of a provision that allows a party to opt out of arbitration entirely despite an arbitration clause in a contract. The consumer rules state that "parties can still take their claims to small claims court." Does the plural noun mean all parties must consent to abandon arbitration? If so, the statement is superfluous, since the parties jointly always have that right. The intent of the drafters seems to have been to allow a party unilaterally to opt out, but which party? A parallel footnote in the Commercial Rules suggests that only the consumer has this option.

This attempt by the leading arbitration organization to reduce the burden of arbitration and enhance its value in resolving smaller disputes fails to convince me. While the new supplementary rules may make arbitration more accessible to consumers, they actually increase the burden on most of the readers of this publication. And they do nothing to remedy the more substantive problems that so often make arbitration arbitrary. My advice remains: purge arbitration clauses from your contracts unless (1) any foreseeable dispute will involve so little money you would not engage a lawyer and (2) you value finality over soundness of the judgment.

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