DRAFTING/NEGOTIATING A DISPUTE RESOLUTION CLAUSE WITH CUSTOMERS/SUPPLIERS

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What are the significant factors to consider in drafting/negotiating a viable dispute resolution clause to assist in ensuring on-time delivery of goods/services? This session will highlight the current practices of domestic and international companies in addressing dispute resolution clauses including a multi-step approach—from negotiation to mediation through arbitration—or alternative dispute resolution (ADR).

First a threshold question: Should a Company use an ADR provision or merely resort to the courts for litigation to resolve a dispute? A couple of recent studies should assist in that analysis…

- The American Arbitration Association (AAA) in 2003 built upon a very important earlier study undertaken by Cornell University, "The Appropriate Resolution of Corporate Dispute: A Report on the Growing Use of ADR by US Corporations." This 2003 AAA-sponsored study took a "fresh look/update" on arbitration and mediation trends. The AAA study concluded, in part, that "there are, indeed, a number of specific benefits associated with dispute-wise business management practices along with some interesting parallels between dispute-wise business management and specific economic benefits." Findings is that survey reflected, in part, the following
  - Key benefits in being "dispute-wise" involves management practices that include stronger relationships with customers/suppliers, appreciation of the fairness/speed of ADR processes, and a reflection of lower legal costs.
  - The AAA study "confirms a consistency in use of both mediation and arbitration among *Fortune* 1000 companies… (and) findings suggest that satisfaction with ADR process and neutrals is substantial and continues to grow."

  The complete report is available at http://www.adr.org/si.asp?id=2423

- The Wall Street Journal on November 25, 2006, had an article entitled, "Litigation Nation," where an overview is provided of the latest "Litigation Trends Survey" undertaken by a major international law firm. This survey involved over 300 in-house counsel for public companies with revenues over $1 billion. The top reported corporate lawyer litigation category "of concern" was "employment" disputes. The category of "contract disputes" was a close second.

  The section in this Survey on the topic of "International Disputes" was noted with particular interest where "considering the ongoing process of globalization, it can be assured that these numbers (frequency of international litigation) are likely to grow in the years ahead." Significant, and somewhat surprising, findings in the international area of this Survey include the following: International litigation/arbitration costs are generally perceived as about the same, time to resolve disputes through litigation and arbitration is about the same, and the "ease of enforcing an arbitration award is about the same as a court judgment." The American Arbitration Association/International Centre for Dispute Resolution was the preferred arbitral provider.

And, it was noted that "formal multi-step (ADR) resolution processes" increased from prior findings with significant savings noted by using same.

The full report of this Survey, "Litigation Trends Survey Findings," is located at http://www.fulbright.com/mediaroom/files/2006/FulbrightsThirdAnnualLitigationTrendsSurveyFindings.pdf.

- Finally, the 2006 PriceWaterhouseCooper sponsored independent study by a highly recognized international University resulted in a finding that multinational companies are using arbitration rather than litigation in resolving international disputes and citing "greater flexibility, finality and confidentiality." Key messages from this study include the following…
  - Majority (73%) of corporations prefer arbitration for international contract disputes.
  - Advantages of international arbitration (flexibility, NY Convention—see below, etc.) "clearly" outweigh the disadvantages (e.g. expenses).
  - Having a corporate dispute resolution policy provides several strategic advantages.
  - Well-drafted contractual arbitration clauses provide tactical advantages (escalating clauses, venue, selection of arbitrators, etc.).
  - Institutional arbitration (e.g. ICC, London Court, and AAA) verses *ad hoc* verses regional arbitration institutions are analyzed.
  - Why arbitration venue is a crucial factor (procedural law, etc.) and which venues are the most popular (England, Switzerland/US, and then France).
  - Corporations overwhelmingly favor the finality of arbitration awards (limited grounds to appeal, etc.).
  - Cost of international arbitrations may be "more" expensive.
  - Why the outlook for international arbitration is positive (95% of corporations currently using arbitration will continue to use).

  The full report of this Survey is located at
  http://www.pwc.com/extweb/pwcpublications.nsf/docid/0B3FD76A8551573E85257168005122C8

With the above as background, it seems clear the answer is "yes, to a need to develop an ADR approach to resolving disputes—especially in an international context." Finally, the benefits of the so-called "New York Convention" or treaty covering the enforcement of international awards cannot be overlooked.

In the past the trend has been more and more multi-step approaches in the design of an ADR clause, i.e. one with escalating approaches to resolution, e.g. expressly providing for negotiation, then mediation, and then arbitration. Some entities even have more ADR steps and, of course, with timeframes, etc. specified in order to have the process "move along toward resolution," which is usually some form of final binding arbitration. Yet, there is a growing concern by some suppliers about the added cost and the perceived value in having multiple steps, i.e. "if we can't settle it by negotiation, then let's go to arbitration." In the opinion of this author there should be some sensitivity to that concern. Finally, do local court decisions—which the ADR provision may be "subject to"—support the desired approach?

While several arbitral providers suggest a "standard" arbitration clause, the one advocated by AAA (which is not atypical) provides as follows:

> "Any controversy or claim arising out of or relating to this contract, or the breach thereof, shall be settled by arbitration administered by the AAA under its Commercial Arbitration Rules, and judgment on the award rendered by the arbitrator(s) may be entered in court having jurisdiction thereof."

The selected arbitral association rules "fill the gap," if you will—not unlike what the Uniform Commercial Code does—on a number of issues, most of which are procedural, but they should be consulted and understood by customers/suppliers. Having a "standard" clause may help in issues going to the validity of the clause, e.g. is it "unconscionable?"

However, in order to come to the conclusion that a "standard" clause is preferred, what are some of the common items considered in designing an expanded arbitration provision? A "checklist" covering critical aspects/considerations in drafting arbitration clauses will be discussed during this ISM workshop and will include topics in this paper and the following…

- Scope of arbitration clause: Broad verses Narrow
- Should all disputes be arbitrable?
- Clause "self-enforcing"?
- Any clause enforcement issues? Will it be enforced as drafted?
- Does the clause clearly state applicable arbitral rules?
- Number/composition of the arbitration panel? Use of "Party-Appointed" arbitrators
- "Significant" procedural issues that should/not be addressed in clause?
- Importance of arbitration location—venue
- Choice of law issues
- Will the award be confirmed?
- Fees, Costs, Attorney Fees Recovered?
- "**Baseball Arbitration**" as an ADR tool that facilitates the negotiation process

ADDITIONAL REFERENCES/BACKGROUND MATERIAL:

- AAA Commercial Arbitration Rules and Mediation Procedures (Including Procedures for Large, Complex Commercial Disputes) located at http://www.adr.org/sp.asp?id=22440

- Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention) located at http://www.adr.org/sp.asp?id=22096

- "Having Trouble Getting to the Negotiation Table? Try Baseball Arbitration," a two-part series on incentivizing parties to negotiate, appears in NCMA *Contract Management* magazine, October and November 2002. Also available at www.Rumbaugh.net

- "Preliminary Hearings," a three-part series on the preliminary hearing process that is associated with the introductory stages of commercial arbitrations appears in NCMA *Contract Management* magazine, January to March 2002. Also available at www.Rumbaugh.net

- "Mediations," a two-part series on mediations by Charles E. Rumbaugh and Michael Powell; *AAA Dispute Resolution Times* ADR Tips Series of articles, July 1999 and January 2000 issues.

- "Using Alternative Dispute Resolution Methods to Resolve Government, Prime Contractor, and Subcontractor Disputes." by Charles E. Rumbaugh and Steven Shapiro; NCMA *Contract Management*, July 1997, 23-25.

- "Alternative Dispute Resolution: Recent Initiatives and Techniques for the Professional," by Charles E. Rumbaugh and Steven Shapiro; NCMA *Contract Management*, January 1997, 4-7.