To Arbitrate or Not to Arbitrate? That's a Good Question!

A Guide for the Perplexed on the Incorporation of Arbitration Provisions in Commercial Contracts

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Introduction

Long before the establishment of formal arrangements of justice that evolved into our state-sponsored court system, persons in conflict sought out respected individuals to sit in judgement of their disputes. What we now call private commercial arbitration has a long and respectable history and, today, it continues to enjoy a privileged place in the panoply of dispute resolution mechanisms.

Hundreds of articles have been written highlighting the many advantages of arbitration, especially as a means of resolving commercial disputes. Most of those articles have been written by people who, like me, are advocates of arbitration and are active in the field, serving as arbitrators or arbitration counsel. As a result, the overwhelming majority of those writings zealously promote private commercial arbitration, while paying scant attention to potential pitfalls and concerns. Over the years, this has translated into many standard form or precedent contracts incorporating arbitration clauses into their provisions as commercial lawyers have become convinced that arbitration is "always" preferable to litigation in the courts and that it is, indeed, the better way to deal with contractual disputes. As a firm believer in the benefits of arbitration, I, however, subscribe to the view that it is usually best utilized when it is selected as an informed choice by both parties after the nature and scope of the dispute is known, and not simply because, as is often the case, a solicitor has decided to use a well-worn precedent contract which happened to have an arbitration clause buried amongst the other boilerplate terms.

Indeed, it is not uncommon that the first time one or both parties to a contract learn that they are compelled to arbitrate their disputes is after a dispute arises. As is often the case, they failed to carefully read the contract they signed, or at least not the dozens of pages of technical standard terms and conditions. Even if they did read every word, there

is a good chance that they would lack the knowledge necessary to evaluate the pros and cons of committing to arbitration. Moreover, their solicitor may have failed to point out and discuss the inclusion of a private dispute resolution provision in the agreement.

For all its many potential benefits, as will be discussed more fully below, arbitration involves a number of important trade-offs with possible negative consequences. In my view, commercial lawyers have a duty to carefully review the pros and cons of this process with clients before depriving them of access to the state-sponsored and funded legal system. Although it is beyond the scope of this article, I go so far as to suggest that the failure to obtain clear instructions (preferably in writing) before incorporating an arbitration clause into a contract, may, in many circumstances, expose a solicitor to a charge of professional negligence.

I will argue that, while arbitration is an excellent method of dispute resolution, the inclusion of mandatory arbitration provisions in business contracts is not always advisable. The principal purpose of this article is to equip commercial solicitors, including in-house counsel, with the necessary knowledge to properly advise clients in this regard. To that intent, I have tried to keep this article accessible to laypersons, with a minimum of legal jargon or reference to case law, in the expectation that lawyers may wish to share it with their clients as part of the process of giving advice on this point.

Although many of the following observations are equally applicable to international agreements between contracting parties in different countries, this article is primarily focused on domestic contracts involving parties both of which are in Canada. In international agreements, where one or both parties may lack confidence in the courts of the other party or, indeed, their own courts, institutionally supervised arbitration may not only be advisable, it may be the only sensible option, especially where there is a need for extra-territorial enforcement of an award. Nonetheless, despite the focus on domestic contracts, some of the issues discussed here may also be relevant to international agreements.

As noted above, the ultimate purpose of this discussion is not to answer the question of whether to arbitrate or litigate any given dispute but only, whether, at the contract

formation stage, to include a provision that would compel the parties to arbitrate all or certain disputes that may arise under the agreement. To be clear, even absent a contractual commitment to do so, parties are free to submit any dispute to binding arbitration by mutual agreement after the fact. Presumably, if arbitration was considered to be a desirable approach when the contract was formed, it should still be attractive when a problem arises, even if the contract does not require it. The main difference is that neither party would be able to compel the other to do so.

My approach will be to systematically discuss each of the commonly cited benefits of arbitration and, in the course of doing so, identify any points of qualification or concern. Ideally, this will equip the reader to evaluate whether arbitration is the best approach for resolving the disputes that may arise under any given contract and whether to include a mandatory provision to arbitrate. In the alternative, where parties do elect to proceed with a mandatory arbitration provision, this article may inform the specific terms of that provision with respect to issues such as the ability to compel non-contracting parties to participate in the arbitration, the choice of arbitrator, provisions for confidentiality, and appeal rights, among other things.

The Potential Benefits of Arbitration

When asked, many corporate counsel or commercial lawyers will explain that they routinely include arbitration provisions in their commercial agreements because they have been told that arbitration is quicker and cheaper than going to court. Moreover, because it is difficult to set aside or appeal an arbitration award, finality is achieved at an early stage, without endless court proceedings challenging the outcome.

They may also point out the benefits of being able to select a decision-maker with specialized knowledge or expertise in the subject matter of the dispute. In the court system, by contrast, parties are stuck with whichever judge is assigned to the case, regardless of their familiarity with the nature of the dispute or the industry or commercial enterprise from which it arises.

And others will point out that arbitration, unlike the court system, is private. The parties to the contract need not air their dirty laundry in a courtroom open to the public and media or expose all of their proprietary processes and documents to scrutiny by customers and competitors.

Most knowledgeable advocates of arbitration will also identify perhaps the most significant advantage of arbitration: the ability of parties represented by savvy arbitration counsel, working in conjunction with a skilled and experienced arbitrator, to design a procedure most appropriate to the nature of their dispute. The principal advantage of arbitration is that, unlike the system of court-based litigation that exists in most jurisdictions, arbitration is flexible and allows the parties to develop efficient and cost-effective practices that will provide for a just and fair determination of the issues with a minimum of unnecessary procedure. This concept of "party autonomy" is a hallmark of arbitration and, perhaps, its most attractive feature.

While each of these presumed attributes present attractively on paper, it is more accurate to suggest that they are, in practice, "potential" benefits. Each is dependent on the willingness of the parties and their legal counsel to adjust their behaviour when a dispute arises to utilize the process in such a way that the benefit of these features is realized. And, as will be discussed below, in some cases, factors beyond the control of either party may negate these benefits or even impose a stumbling block to the final determination of all issues arising from the dispute.

Is arbitration is quicker and cheaper than going to court?

The rules that govern court processes are necessarily broad, as they must be able to address all manner of legal disputes. Like an article of clothing purchased off the rack, they must be able to accomodate a broad array of disputes that may come before the courts. But, as the late and great advocate, Clarence Darrow, once noted, "Laws should be like clothes. They should be made to fit the people they serve." One of the principal advantages often cited for arbitration is that it allows parties to customize the procedural protocols and evidentiary rules utilized to best fit the needs of the dispute.

Yet, in practice, few domestic arbitrations fully embrace the opportunity to custom design a time- and cost-efficient process suitable to the dispute. Far too many arbitrations fall into the trap of becoming ersatz litigation, with pre-hearing processes and procedures modelled on the local court rules of civil procedure and an evidentiary hearing that is effectively a trial conducted in a boardroom, rather than a courtroom. In these circumstances, arbitration may not achieve the goal of being quicker or more expedient than the state-subsidized court system.

Nor will it necessarily be less expensive. In our court system, the judge, the courtroom, and the attendance of a court reporter are all paid for by the state. Parties to an arbitration must pay the arbitrators, hire the facilities in which the case will be heard, and, if a transcript is to be obtained, retain the services of a verbatim reporter. For a moderately complex commercial arbitration with a hearing lasting ten or twelve days before a sole arbitrator, these costs can easily exceed $400,000, inclusive of the arbitrator's time organizing the procedure, dealing with pre-hearing motions, preparing for the hearing, attendance at the hearing, and preparing an award. If the matter is being heard by a panel of three arbitrators, a multiple of that amount can be expected. While all of these additional costs may be warranted in some cases, in drafting their contracts, parties and their legal representatives should consider whether the nature of the potential disputes that might arise under the contract and the other inherent benefits of arbitration justify these additional costs.

It is true that the legislation governing arbitration provides arbitrators with a significant degree of control over the process and some ability to discipline parties or counsel that do not manifest behaviours consistent with the objectives of expediency and efficiency. Regrettably, in practice, arbitrators often exercise this authority reluctantly and sparingly. There are at least three reasons for this reluctance to impose discipline on the process. First, and foremost, arbitrators are inclined to respect party autonomy as an underlying principle of arbitration and allow the parties to dictate the procedure and pace of the process. Only when parties and their counsel disagree will the arbitrator be forced to intervene.

Arbitrators are also concerned with protecting the process from nullification by a court, if procedural fairness is not perceived to have occurred. Although it is difficult to set aside an arbitral award in court, the grounds for doing so often involve allegations that the parties have not been treated equally and fairly. By way of example, lawyers who practice primarily in the litigation world are accustomed to extensive pre-trial documentary production and examinations for discovery. This is less common in arbitration practice. But, in deciding whether to allow, for example, pre-hearing examinations under oath (i.e. discoveries) or whether to require the production of significant volumes of documents, arbitrators will often err on the side of caution to avoid a subsequent allegation that one party or another was deprived of the means to present its case or defend the case against it. A judge on subsequent review will never overturn an arbitral award because the arbitrator was too lenient in this regard, but may do so if the pre-hearing disclosure was determined to be too restrictive.

Finally, arbitrators, unlike state-appointed judges, are in the business of resolving disputes. The success of that business may depend, in part, on being selected by both legal counsel. As a result, it is not uncommon to hear complaints from lawyers who practice primarily in the arbitration field that some arbitrators are more concerned about being perceived as "nice" than with exercising appropriate discipline over the process. This concern is reflected in the following comment found in an excellent publication entitled *Protocols for Expeditious, Cost-Effective Commercial Arbitration* published by The College of Commercial Arbitrators: "Some have even suggested that a reluctance to limit discovery may reflect an arbitrator's desire to avoid offending anyone in the hope of securing future appointments."[ii]

Commercial lawyers drafting contracts that include arbitration clauses may do so with the intention that the parties will make good faith efforts to cooperate in the achievement of cost-efficiency and expediency, but they are rarely the lawyers who represent the parties once a dispute has arisen. Typically, the matter is handed over to litigation counsel who may have greater comfort with the court rules and employ tactical or strategic manoeuvers that may be inconsistent with achieving those benefits. Absent strong

intervention from the client or the arbitrator to counteract those tendencies, the matter may take just as long to be resolved and cost considerably more than traditional litigation.

Does arbitration ensure closure and finality?

Many parties are attracted to arbitration because of the the notion of obtaining a "final and binding" decision. In the past, they may have been frustrated by multiple levels of court intervention in the litigation process, including pre-trial motions, mandatory mediation, and pre-trial case conferences, as well as interlocutory appeals and the possibility of appeals from a final judgment to both the provincial Courts of Appeal and the Supreme Court of Canada. In arbitration, by contrast, the arbitrator deals with all the pre-hearing matters in a less formal and more expeditious fashion, and appeals from the final award are both rare and rarely successful.

This, of course, is something of a two-edged sword. Successful parties value finality, but the same is not always true of the unsuccessful party. Again, either because corporate counsel are not thoroughly versed in arbitration or have failed to properly advise their clients, it sometimes happens that parties do not discover that they have no appeal rights until after they receive the arbitral award. This is one of those instances where lawyers are well advised to ensure that their clients provide informed consent when entering into such a contract.

In Ontario, there are only two possible ways to overcome an unhappy outcome in domestic arbitrations. The first is by way of appeal, where available. Arbitration clauses in contracts can deal with appeals in several different ways. The most common approach is to provide that the award is both final and binding with no rights of appeal. Sometimes, the arbitration agreement is silent on the issue, in which case the legislation provides a limited right of appeal on a pure question of law, but only with leave of the court, if certain prerequisites are met.

Parties can also stipulate in their arbitration agreements for rights of appeal on questions of fact, mixed fact and law, or questions of law alone, in which case they will have an absolute right of appeal to a Superior Court judge and, possibly, a subsequent appeal,

with leave, to the provincial apellate court. Finally, parties can, by agreement, provide for an appeal to a private arbitration appellate tribunal, rather than to the civil court system. In practice, few standard arbitration clauses provide for either of these forms of subsequent review.

Where appeals are provided for, however, it should be noted that the courts have, in recent years, taken an extremely deferential approach to arbitral decisions and intervene only reluctantly in the clearest of cases or where some public policy consideration, such as the interpretation of a statute, would benefit from a jurisprudential pronouncement. In most cases, issues arising out of contractual disputes are perceived to involve questions of mixed fact and law and, therefore, will not qualify for a right of appeal on a pure question of law where the arbitration agreement has not provided for broader appeal rights. Only where some distinct pure legal issue can be discerned will leave be granted.

Aside from the difficulty of getting in front of an appellate court, once there, courts are reluctant to intervene on behalf of the unsuccessful party. This deference to the arbitrator is sometimes said to be based on the choice of the parties to select a decision-maker with specialized knowledge in the subject matter of the dispute and, in other cases, courts respect the principle that parties have chosen arbitration with a view to closure and finality. There is a sense that, if appeals are granted on the same basis as would be the case with a decision of a lower court, this principle will be undermined.

As a result, courts will hardly ever interfere with a factual determination by an arbitral tribunal. As an aside, appeals of this kind may be even more difficult because many arbitration hearings occur without the benefit of a verbatim reporter and a resulting transcript. In such circumstances, the record available to a court for review may be extremely limited. Even where questions of law are concerned, in most cases, the accepted standard of review is not one of correctness, as in the case of similar appeals from lower court decisions, but, rather, reasonableness. With the exception of situations involving statutory interpretation or where broader public interests are involved, the appellate court generally will only overturn an arbitral decision on a point of law where it

finds that the arbitral decision was unreasonable. Suffice it to say that there are very few appeals from arbitral awards and even fewer successful ones!

The second approach is to ask the court to nullify or "set aside" an award based on narrow grounds provided for in the legislation. In general, these grounds will only be invoked where one of the parties was under a legal incapacity when it entered into the agreement, the agreement itself was invalid or ceased to exist, the issue determined was outside the scope of the arbitration agreement, the tribunal otherwise exceeded its jurisdiction or failed to comply with legislation, or it failed treat both parties fairly and equally. Because of the usual limitations on appeal rights, it is not uncommon to see parties attempt to overturn an award by shoehorning it into one of these limited grounds. Rarely are they successful.

Should the dispute be of the "bet the farm" type, the consequences can be devastating. Since this will not generally be known at the time that the contract is entered into, the inclusion of a broad and far-reaching arbitration clause in a contract may lead to a party's future hinging on the decision of a single individual arbitrator with no opportunity for subsequent review. Perhaps, as noted above, it would be better to decide if arbitration is the way to go once the nature and consequences of the dispute are better understood.

In light of these restrictions, parties entering into a contract with an arbitration clause should either negotiate and clearly stipulate the scope of appeal rights available to the unsuccessful party or accept the fact that the determination will be effectively final and binding. For parties looking for that kind of finality, in any event of the outcome, arbitration may be the way to go, but they should do so with their eyes wide open. In most instances, parties will get one, and only one, kick at the can!

While on the topic of finality and closure, arbitration is best suited to situations involving disputes between only two parties. An arbitrator or panel of arbitrators has jurisdiction only over parties who have agreed to have their dispute resolved in this fashion. It will have no jurisdiction over any other party, no matter how necessary their involvement may be to the proper resolution of the dispute. In the court system, by contrast, necessary parties may be added as defendants or third, fourth, or fifth parties, without their consent.

Any decision will be binding on those parties. In the case of arbitration, additional parties will only be bound by an arbitral award, if they agree to be part of the process.

Imagine, by way of example, a dispute between the purchaser of manufacturing machinery and the supplier of that equipment. The equipment has not performed in accordance with expectations, and the purchaser makes a claim against the equipment supplier. The supplier believes that the difficulty rests with the design specifications provided to it by the purchaser's mechanical engineer or, in the alternative, that the malfunction is the result of the failure of one of the components that it purchased from a parts supplier. The purchase contract contains an arbitration clause, but no similar provision exists in the contracts between the purchaser and its mechanical engineer or between the equipment manufacturer and the parts supplier.

In a lawsuit before the courts, all of these parties could be joined in a single action with a resulting judgement binding on all participants. A single proceeding could resolve all issues of liability and damages. In arbitration, however, only the two principal parties have agreed to submit their dispute to a private decision-maker and, unless the other parties volunteer to participate in the arbitration and be bound by that decision, they cannot be compelled to do so. Even if a third party agrees to be involved in the arbitration at the instance of one of the original parties, it is likely that the consent of the other originating party would also be required. Accordingly, in many such cases, the principal parties will be required to resolve their dispute through arbitration, and then, depending on the outcome of the case, commence separate court proceedings against any other parties that may be ultimately responsible for the loss suffered.

To continue the example, if the arbitrator finds that the real problem was related to the design specifications, the purchaser of the machinery would be obliged to commence an action against the mechanical design engineer to recover damages. Similarly, if the arbitrator finds that the problem was the result of a faulty part, the machine supplier will be found liable and have to go after the parts manufacturer in a separate lawsuit to recover the damages paid to its customer. In these situations, instead of finality and closure, one or both parties may find themselves faced with a multiplicity of expensive

and duplicative proceedings and resultant delay. And, a court later dealing with the same situation may, on the evidence before it, reach a different conclusion than the one reached by the arbitrator. In these situations, arbitration is neither quicker, nor cheaper, nor does it bring closure and finality to the dispute.

While many cases will involve only the two parties to a contract, the above-noted example is far from uncommon. Similarly, it will often be difficult for parties to predict, when entering into a contract, whether the resolution of any dispute that may arise will require the participation of other necessary parties. If the contracting parties have bound themselves to a mandatory arbitration clause, they will not be able to escape from that commitment simply because one or both would like to involve other unwilling parties. In such situations, it would have been better not to have a mandatory arbitration clause in the contract and to only proceed with arbitration if all necessary parties agree to participate and be bound by that process. Again, this suggests that arbitration should be pursued only after the nature and scope of the dispute is known, rather than be compelled by virtue of an arbitration clause in the contract.

Does arbitration provide privacy and the protection of confidential information?

Except in the rarest of cases, in our court system, justice is dispensed in public. Our courtrooms are open and, even where individuals choose not to attend a hearing, they are entitled to come to the court office and review the entire record of proceedings, including the pleadings, the documents filed in evidence and order a complete transcript of the hearing. Many businesses and individuals find the prospect of providing this kind of access to their customers, employees, suppliers, competitors, and regulatory or taxation authorities extremely unattractive. Indeed, the threat of such exposure can be used as a tactical device by one of the parties to encourage early capitulation by the other.

Arbitration, on the other hand, offers the *possibility* of privacy and the protection of confidential information. It is a common fallacy, however, that arbitrations are inherently private and confidential. In fact, although some institutional rules require private hearings and the maintenance of confidentiality over materials filed, transcripts of evidence, and the award itself, nothing in the domestic or international legislation in many jurisdictions

mandates this. Arbitrations simply have the "potential" to be private and confidential. For this to occur, the parties must provide for it in the arbitration agreement in their contract or through the adoption of institutional rules that incorporate those requirements. Unfortunately, however, because many lawyers suffer under the misapprehension that the process is automatically private, the majority of standard arbitration clauses do not contain this requirement.

Even when privacy and confidentiality are provided for, however, it is not assured. The potential still exists for either party to take the dispute into the public realm by improperly commencing a court action, moving to set aside an improperly commenced court action, seeking or challenging the appointment of an arbitrator, challenging the impartiality or the jurisdictional ruling of an arbitrator, moving for a declaration that the arbitration agreement is invalid, appealing an award, moving to set aside an award, or bringing proceedings to enforce an award. In each of these cases, material will be filed with the court that may disclose some or all of that which the other party wishes to keep private and, in most cases, it will be difficult to protect that information from public disclosure. Accordingly, while arbitration proceedings will often be private and confidential, it is, practically speaking, generally impossible to ensure that this will always be the case.

Do parties always have the right to choose an appropriate and acceptable arbitrator?

In litigation, parties rarely have the ability to influence the selection of the judge that will hear the case. By contrast, arbitration provides an opportunity for the parties to appoint an arbitrator or panel of arbitrators best suited to decide the issues in dispute. This can be an extremely valuable feature of arbitration. Technical cases can be decided by arbitrators with specialized knowledge in the subject matter of the dispute. Not only will the quality of the decision likely be enhanced, but the parties will not need to spend time during the hearing educating the arbitrator on the technical knowledge and terminology underlying the disputed issues or the common practices in the relevant industry.

Even when the dispute primarily involves issues of law, the parties will be free to select arbitrators with specialized legal knowledge in that area. For example, construction disputes can be put before individuals with significant knowledge of construction law and

practice, just as matrimonial disputes can be determined an arbitrator who has practised extensively in that area. The parties and their lawyers may be able to select individuals in whom they both have confidence.

On the other hand, state-appointed judges have typically been carefully vetted by selection committees that provide the government with shortlists of highly qualified and respected candidates for the bench. By contrast, anyone can be appointed as an arbitrator. No certification or specific training is required. And, because arbitration proceedings are typically conducted in private with little subsequent judicial oversight, a party's ability to independently evaluate any particular arbitrator's qualifications and suitability will be limited to whatever word-of-mouth feedback can be obtained from the legal community.

As well, judges are completely independent of the parties. They are salaried employees of the state with security of tenure, typically until age 75. While most judges will be inclined to want to earn the respect of the bar and their peers by the fairness of the proceedings they preside over and the quality of the judgements they render, they do not need to worry about where their next case is coming from, and they are free from any need to curry favour with parties or their counsel. And, while there are many regularly appointed and busy arbitrators, few will ever gain the judging experience of a person who presides over a courtroom hundreds of days each year.

By comparison, arbitrators are sometimes suspected of side-stepping hard decisions and "splitting the baby" to avoid negative career consequences. Indeed, a 2011 study conducted by the Rand Corporation found that a majority of corporate counsel in the U.S. believe that "professional arbitrators tend to split awards rather than rule strongly in favour of one party."[iii] Undoubtedly, this concern is more a matter of myth than reality, and its practice would, in any event, be a short-sighted approach to career building. Nonetheless, the belief persists and may have some basis in fact. Fortunately, while it is difficult, if not impossible, to gather meaningful empirical evidence on the point, a 2016 survey conducted by the American Arbitration Association throws significant doubt on the accuracy of this perception.[iv]

Where the case is to be decided by three arbitrators, selection is rarely a problem. Usually, each party appoints one arbitrator of their choosing and the party appointees then select the chair for the panel. So long as the individual party appointees have no actual or apparent conflicts, those choices will be respected. In practice, party appointees rarely have difficulty settling on the choice of an appropriate panel chairperson. While the use of a panel obviates any difficulty with arbitrator selection, it does have certain disadvantages. Obviously, the need to pay three arbitrators will result in a costlier process. Moreover, the conflicting calendars of counsel, the parties' representatives, and three rather than one arbitrator may make scheduling more arduous and result in delay.

Where the issue is to be decided by a single arbitrator, however, it is often hard to get agreement on the selection of a mutually acceptable choice. If one party puts forward a name, the other side may get suspicious that some relationship exists between that arbitrator and the proposing party or its counsel. When that party's proposals are rejected, it may adopt a similar attitude with respect to any counterproposals. While these situations usually sort themselves out, they often result in a compromise selection that neither party really favours and results in the appointment of someone who may not be the best person for the job. In other cases, the parties may have to resort to the use of an institutional appointing authority or go to court to resolve an impasse.

Accordingly, while the ability to select a knowledgeable and qualified arbitrator or arbitration panel can be a significant benefit of this method of dispute resolution, it can also be a source of delay and, in some cases, expose an otherwise private process to court (and public) scrutiny. One antidote to this is for the parties to provide in their contractual terms for the selection of the arbitrator to be carried out by an arbitral institution, with or without specific guidelines as to the necessary qualifications of the appointee. This, however, may involve additional cost to the parties and result in the appointment of an arbitrator that neither party favours. Another approach, but one rarely utilized, is for the parties to preselect an arbitrator or short list of arbitrators acceptable to both parties at the time they enter into their contract.

Of course, these problems only pertain to situations where arbitration is mandated by the underlying contract from which the dispute arises. By contrast, where the agreement does not require arbitration, parties and their legal counsel may, nonetheless, freely choose to submit a dispute to arbitration after it arises, if they can agree on a choice of arbitrator or panel, failing which they can always utilize the court system. As a result, if control over the choice of arbitrator is important to one or both parties, it is advisable to either make specific provision for how that is to be accomplished in the arbitration clause of the contract or leave the decision of whether or not to arbitrate until after a dispute arises.

Conclusion

As will by now be clear, arbitration offers many potential advantages as a method of dispute resolution. Indeed, parties engaged in a dispute should always at least consider choosing it over litigation in the courts. But, enthusiasm for arbitration must be tempered by the recognition of certain practical constraints, some of which have been discussed above. The problem is that many of the potential concerns cannot be effectively evaluated at the time the business agreement is being negotiated between the parties. And many of the issues discussed may only present concerns in relation to some disputes, but not others.

For example, where the dispute involves a relatively small sum of money, closure and finality may trump rights of appeal, but where the disagreement results in a “bet the farm” contest, many parties will be prepared to sacrifice closure for access to appellate review. Again, the problem is that parties to a contract negotiation are rarely able to predict the nature and scope of all the disputes that may arise under the contract. Moreover, they are frequently optimistic regarding the success of the business relationship and prone to pay scant attention to dispute resolution mechanisms.

Similarly, when entering into a commercial agreement, contracting parties will rarely be able to predict with certainty whether the resolution of that dispute will necessitate the joinder of individuals or entities that are not parties to the contract. Again, where one disputant wishes to join additional parties, an arbitration clause in a contract will constrain

that ability, possibly resulting in a multiplicity of proceedings with a duplication of costs, resulting delay, and potentially inconsistent results.

To the extent that the decision to arbitrate should be an informed and consensual choice based on its suitability to any given dispute, incorporating an arbitration clause in a contract before the precise nature of the dispute is known is, perhaps, a case of putting the cart before the horse. The parties are committing themselves to a method of dispute resolution before knowing whether that method is well-suited to the nature of the dispute. They do so before knowing whether they are going to be able to agree on a choice of decision-maker or agree on a procedural protocol that will ensure that the process is quicker and less expensive than traditional litigation.

This is not to say that including a mandatory arbitration clause in a contract is never a good thing. Certain contracts will lend themselves to that approach, especially when the nature of the disputes that might arise can be easily predicted or where the arbitration provision is restricted to certain kinds of disputes. For example, many leases that include renewal provisions provide for arbitration of the renewal rental rate based on fair market value, when the parties cannot agree. This situation is ideally suited for arbitration since it should never involve more than two parties, it is well suited to adjudication by someone with appraisal expertise, and the outcome will usually be within a predictable range. Any other disputes arising under the lease can be submitted to arbitration, if the parties agree, but will otherwise be dealt with through other established processes.

In the end, the only conclusion that should be taken from this discussion is that business lawyers advising clients at the time of contract formation should ensure that their clients are fully informed with respect to the benefits and potential consequences of including a mandatory arbitration provision in their contracts and that the pros and cons of that decision are carefully evaluated. All of this should be done against the backdrop of awareness that the absence of a mandatory arbitration clause in a contract will never prevent the parties from choosing to submit a dispute to arbitration after it arises, when they both agree that arbitration is the best way to resolve the disagreement. While it is true that one party desiring arbitration will not then be able to compel the other party to

do so, situations where parties do not both see arbitration as desirable are probably not well suited to that method of private dispute resolution, in any event.

Checklist of Considerations

When negotiating a contract, in deciding whether to include a mandatory arbitration provision, the parties and their lawyers should consider, among other things, the following issues:

1. *Are the disputes that are likely to arise under this contract ones that would benefit from being decided by an individual with specialized knowledge or training in the subject matter of the dispute or the legal framework under which it arises? If so, it may be advisable to include a requirement in the arbitration provision ensuring that the appointed arbitrator has the necessary qualifications. The agreement should clearly set out the protocol for selection of an arbitrator or arbitration panel. Consideration should be given to identifying a short list of mutually acceptable arbitrators and including that in an addendum to the contract.*

2. *Should arbitration be mandatory for all manner of disputes that may arise under or in connection with the contract, or be restricted to only certain kinds of disagreements? For example, parties may wish to provide for mandatory arbitration of post-closing adjustments in a business acquisition agreement, but not impose arbitration on other disputes that may arise under the contract. Similarly, in a shareholders' agreement, it may be desirable to reserve share valuation disputes to arbitration, but leave it to the parties to decide how they wish to adjudicate other disputes after they have arisen.*

3. *Are the disputes that arise under the contract of a nature that a final and binding decision by an arbitrator or arbitration panel will take precedence over benefits of a right of appeal by the unsuccessful party? If some right of appeal is determined to be desirable, the right to and scope of such appeals should be explicitly set out in the agreement. Where appeals are contemplated, the agreement should be explicit regarding whether they are only on points of law, on questions of mixed fact and law, or on questions of fact. In some cases, the parties may determine that appeals will only be available when the arbitral award exceeds some prescribed monetary value. Finally, consideration should be given to whether the appeal is to the courts or to a private arbitral tribunal.*

4. *Are the disputes that may arise under the contract likely to be those that will involve only the contracting parties? If not, consideration should be given to including provisions in the agreements with other potentially necessary parties compelling them to participate in an arbitration between the principal contracting parties. In reality, however, this is often difficult to achieve. So, where it is likely that other*

parties will need to be joined in the process, a mandatory arbitration provision may not be the best choice.

5. *How important to the parties is an expeditious and cost-effective resolution of any dispute that may arise under the contract? If this is an important factor, consideration should be given to either building in a procedural protocol or adopting the rules of an arbitral institution that minimizes unnecessary procedural steps and pre-hearing discovery processes. If the types of disputes that may arise are likely to require urgent disposition, some institutional rules provide for interim relief and expedited procedures.*

6. *If there is a significant likelihood that injunctive relief or a vesting order may be required, especially if it is to affect the rights of non-contracting parties, then arbitration is probably not the best option. Arbitrators do not have the same ability to enforce such remedies as do the courts.*

7. *How important to the parties is the privacy and confidentiality of the proceedings and the materials filed in connection with it? If these are important considerations, explicit provisions should be incorporated into the arbitration agreement. If appeal rights are to be included, consideration should be given to preserving confidentiality by utilizing an arbitral appellate tribunal, rather than having recourse to the courts.*

8. *Will it be important to one or both parties to have a determination that will provide binding legal precedent in other disputes? If so, then arbitration is not likely the best choice, since awards are private and not generally admissible or binding on any other court or arbitrator.*

9. *Although beyond the scope of this article, mandatory arbitration clauses may foreclose class actions, especially in non-consumer commercial contracts.*

10. *If an arbitration clause is included, should it mandate the use of a specific arbitral institution to facilitate arbitrator selection and procedural rules? If so, commercial lawyers should familiarize themselves with the features of different arbitral institutions, including matters such as fees charged, procedural protocols, appointment processes, the availability of interim and emergency measures, and confidentiality provisions.*

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[i] Stephen Morrison is a Chartered Arbitrator and Mediator based in Toronto at Arbitration Place. He is regularly retained to assist in the resolution of a wide range of domestic and international commercial disputes.

[ii] https://www.americanbar.org/content/dam/aba/administrative/litigation/materials/sac_2012/04-2_protocols_for_commercial_arbitration.authcheckdam.pdf at page 7.

[iii] https://www.cpradr.org/news-publications/articles/2011-01-18-still-splitting-the-baby-new-rand-report-on-why-corporate-attorneys-use-adr-jan-18-updated

[iv] http://www.sacarbitration.com/blog/arbitrators-dont-split-baby-studies-show/