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The Positives and Negatives of Mandatory Arbitration Clauses in Contracts

(frequently a retired judge) who will decide the dispute and which decision will be binding on the parties as if the dispute was decided in a court of law by a judge or a jury. Mediation consists of a mediator attempting to resolve the dispute by meeting with the parties and persuading them to settle the dispute. Mediation is always available, if the parties agree to it, whether the dispute is to be resolved in a court of law or in an arbitration hearing. Mediation is not binding on the parties because, if the mediation is not successful, the arbitration or court proceeding simply continues.

Absent a provision in a contract (i.e., an Operating Agreement, a Purchase and Sale Agreement) requiring the parties to litigate disputes by arbitration, the parties will have their dispute settled by a court of law. Accordingly, the parties can control, by omitting or including a dispute resolution provision in the contract, whether future disputes between them will be arbitrated or tried in court.

If a client prefers arbitration and wants to exercise some control over the choice of the arbitrator(s), it is possible for the parties to agree in advance in the contract on not only the organization that will oversee the arbitration process but also on the particular arbitrator(s) who will decide the dispute. This is not typical but can be included in the contract.

Among the differences between arbitrations and court actions is the fact that arbitrations are confidential – court cases, in the absence of a confidentiality order, are not. If the client has an interest in maintaining confidentiality about the parties' disputes, that aspect of arbitration is an attractive feature. If, however, the client believes that potential adverse publicity relating to a dispute arising out of the contract could be used as leverage against the other party, that aspect of arbitration is less attractive.

In my experience, the client generally incurs fewer attorneys' fees in arbitrations as opposed to court actions. That is because, due to courts being overburdened, an arbitration hearing is usually scheduled far sooner than a trial would be, and that generally results in the parties incurring less costly pretrial discovery and motion practice. A counterbalancing consideration to that cost savings in arbitrations, however, is the fact that arbitrators, unlike judges, are compensated by the parties for their service. It is not uncommon for judges who arbitrate to charge in excess of $700 per hour and, if there are multiple arbitrators, the fees paid to arbitrators can be substantial. Arbitrators, just like judges, are involved in time-intensive pretrial discovery, status conferences, some motion practice and conducting the arbitration hearing – the difference is the arbitrators gets paid for those tasks. In addition, the filing fees for arbitration organizations that manage the arbitration, such as the American Arbitration Association, can be very substantial, especially if the amount of the claim is significant.

Unlike court actions, arbitration decisions cannot be appealed (other than for fraud or corruption on the part of the arbitrator(s)). By neither party being able to appeal the arbitrator's decision, the finality of that decision also serves to cut costs to the client but also exposes the client to be bound by a decision that, if palpably wrong, still cannot be appealed. Consequently, in deciding whether to agree to a mandatory arbitration provision in a contract, the client must give serious consideration to this bar on appealing an arbitrator's decision.

Juries are obviously unavailable in arbitration. Thus, if a client has a belief in and trust that a jury will come to a more fair result in the dispute than would an arbitrator, that client should resist including an arbitration provision in a contract.

As shown above, there are positives and negatives to including a mandatory arbitration clause in a contract. Indeed, some positives and negatives "cut both ways". The client should consider whether, in the client's particular circumstances relating to that contract, including a mandatory arbitration clause in the contract is or is not in the client's best interests. Most crucially, the client should be an active participant with the attorney drafting the contract in making that important decision.

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Fear Not – Lending on Environmentally Challenged Real Estate

By Douglas I. Eilender

In actively representing lenders that take security interests in real estate, we routinely encounter properties that have known or potential environmental issues. These issues run the gamut, from existing or former underground storage tanks, former manufacturing operations, dry cleaners, and other uses that now utilize or formerly utilized hazardous substances, as well as known soil and groundwater contamination. These issues could cause lenders to pause and shy away from the deal. However, in our experience, whatever the environmental issue, in concert with the proper environmental and insurance professionals, we are able to efficiently assess and manage the environmental risks associated with the collateral.

The first step is to conduct adequate environmental due diligence utilizing seasoned environmental consultants, who understand the environmental risks, but have the necessary business acumen to make reasonable findings and conclusions. Once we have our arms around the issues, we can manage the environmental risks in several ways, including one or more of the following: (i) affirmative covenants by the borrowers to address the known environmental issues or issues discovered during the term of the loan; (ii) holding back environmental reserves to secure the environmental obligations; or (iii) obtaining environmental insurance policies that cover claims for clean-up costs, property damage, bodily injury and business interruption for all known conditions and any new conditions that are identified on, at, under or migrating from the real estate. Environmental insurance can be successfully used even in situations where the financial strength of the borrower is sound, as borrowers would prefer to pay a small premium and deductible, rather than have a large environmental escrow held back to secure an affirmative obligation.

Thus, the takeaway, as with most commercial real estate transactions, is to conduct adequate environmental due diligence with the assistance of counsel to be in a position to assess and allocate the environmental risks and responsibilities associated with the collateral amongst the parties in order to successfully close the transaction.

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