

An Introduction to Arbitration

By Richard Bales

If you haven't arbitrated a case before, you probably will soon. Arbitration agreements are becoming ubiquitous. They've been around for years in collective-bargaining agreements and in the securities industry, but now they've gone mainstream – if you own a credit card or have taken out a mortgage recently, you almost certainly are a party to an arbitration agreement. Don't be surprised if you even start seeing arbitration agreements covering slip-and-falls on grocery-store receipts and customer-card agreements!

Arbitration is a proceeding, governed by contract, in which a dispute is resolved by an impartial adjudicator, chosen by the parties, whose decision the parties have agreed to accept as final and binding. It differs from mediation in that the arbitrator imposes a resolution, unlike a mediated settlement which must be agreed to by the parties. It differs from litigation because it is informal: arbitration occurs in a conference room rather than a courtroom, the rules of procedure and evidence are loosely applied, and both discovery and motion practice are limited.

Advantages

Arbitration has three advantages over litigation. First, arbitration is much faster. Employment cases, for example, can be arbitrated in half to a third the amount of time that they otherwise would be litigated.¹ Second, arbitration is much less expensive, since less lawyer-time is needed for discovery and motion practice. Third, arbitration is much less formal than litigation, making it easier and less time-consuming to prepare a case.

Concerns

Traditionally, arbitration agreements were the product of meaningful negotiation between parties of roughly equal bargaining power, such as commercial entities entering into a contract or employers and unions entering into a collective bargaining agreement. The recent proliferation of arbitration, however, has occurred in the form of adhesive arbitration agreements imposed by a party of superior bargaining power upon a party (such as an employee or consumer) whose only alternative to acceptance is to walk away from the job or the transaction. This has led to two concerns.

The first is that adhesive arbitration agreements are "involuntary," either because the weaker party lacks adequate notice or consent (an example is the employer that gave arbitration agreements written in English to Spanish-speaking employees²) or because the weaker party has no meaningful alternative (since arbitration agreements now are nearly universal in credit card agreements, anyone wanting a credit card must agree to arbitration). But the United States Supreme Court has stated that arbitration agreements must be enforced to the same extent as other agreements are enforced

under state contract law,³ and state contract law generally permits the enforcement of adhesive contracts absent substantive and/or procedural unconscionability. In Kentucky, a party seeking to avoid enforcement of an arbitration agreement must show fraud *in the inducement of the arbitration clause*, and not merely fraud in the inducement of the contract as a whole.⁴

The second concern is that parties drafting adhesive arbitration agreements will draft lopsided agreements that "place every conceivable obstacle in the path of those seeking redress in the hope of discouraging potential claimants from pressing any actions at all."⁵ For example, many consumer arbitration agreements prohibit consumers from bringing a class action;⁶ some employers have imposed high filing fees, sometimes payable directly to the employer.⁷ Though courts have refused to enforce the most egregious of these lopsided agreements, many consumers and employees continue to be deterred from pursuing legitimate claims because they correctly perceive that the playing field is irrevocably tilted against them and that the cost of leveling the playing field (by a judicial challenge) far exceeds the value of the claim.

Controlling Law

Common law was traditionally hostile to arbitration. The Federal Arbitration Act (FAA), 9 U.S.C. §§ 1-16, was enacted in 1925 to provide a basis for enforcing commercial arbitration agreements. The U.S. Supreme Court extended the FAA to employment contracts tentatively in 1991 and definitively ten years later.⁸ The Court has recognized a strong federal policy favoring arbitration since the mid-1980s.⁹

The Kentucky Arbitration Act (KAA) is at KRS 417.050-.220. KRS 417.050 exempts employment agreements and insurance contracts from the general rule that arbitration agreements are enforceable. However, the FAA broadly preempts state statutory and common-law restrictions on the enforceability of arbitration agreements.¹⁰

Choosing Arbitrators

Arbitrators are chosen by the parties. If an arbitral service provider (such as the American Arbitration Association or the National Academy of Arbitrators) is specified in the arbitration agreement, that provider will give advocates a list of potential arbitrators from which to choose. Start by assessing the case and considering the appropriate type of arbitrator. Would a lawyer or an industry expert be better? A big-picture person or a detail-oriented person?

Gather information on potential arbitrators from multiple sources. If the potential arbitrators haven't voluntarily provided information, ask for it. The California Judicial Council has imposed extraordinarily strict disclosure rules on arbitrators (17 categories and 21 subcategories of disclosure).¹¹

Though these rules don't apply in Kentucky, nothing stops Kentucky advocates from requesting disclosure. If the arbitrator doesn't comply, find another arbitrator.

Then, do some independent research. Circulate the list of potential arbitrators among your colleagues and ask their opinions. Google the arbitrators to research their backgrounds and current affiliations. Search legal databases for past arbitral decisions. Once an arbitrator has been selected, read everything that person has written to find out how he or she thinks.

Tips for the Advocate

First, buy a good reference guide. The most comprehensive is ELKOURI & ELKOURI, *HOW ARBITRATION WORKS* (6th ed. 2003, ISBN 1-57018-335-X). A good article is Marvin Hill & Anthony V. Sinicropi, *Improving the Arbitration Process: A Primer for Advocates*, 27 WILLAMETTE L. REV. 463 (1991). Both of these guides are written with labor arbitration in mind, but the ideas apply equally to arbitrating other types of disputes.

Second, prepare a pre-hearing brief to familiarize the arbitrator with the facts and issues.

Third, at the hearing, lay off the posturing. Your audience is a skilled arbitrator, not a lay jury.

Fourth, understand that evidentiary objections serve a different purpose in arbitration than they do in litigation. For example, you can object if the opposing party attempts to introduce hearsay testimony, but expect the arbitrator to let the testimony in "for what it's worth." Use objections not to exclude testimony, but to call the arbitrator's attention to evidentiary weaknesses.

Fifth, understand the concept of credibility and how credibility determinations are made. Accept that some facts will be "bad" for your case, and instruct your witnesses to do the same. Concede the bad facts and concentrate on the good ones – don't risk your witnesses' credibility by allowing them to insist on facts that the arbitrator will find unbelievable. Arbitrators frequently are presented with conflicting testimony; arbitration decisions frequently turn on who the arbitrator believes.

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Sixth, prepare a post-hearing brief discussing the facts and legal arguments.

Finality

The FAA limits the grounds for vacating an arbitral award to corruption, fraud, partiality, or misconduct by the arbitra-

tor.¹² The U.S. Supreme Court has stated that an arbitral award additionally may be vacated for "manifest disregard" of the law,¹³ but this requires a showing *both* that (1) the arbitrator knew of the applicable law and refused to apply it, and (2) the law was well-defined, explicit, and clearly applicable to the case.¹⁴ The KAA is similarly deferential toward arbitration awards.¹⁵ Consequently, arbitral awards are, for all practical purposes, unreviewable.

Conclusion

Arbitration is quickly becoming a mainstream method of resolving legal disputes – it's not just for labor and securities lawyers anymore. Arbitral advocacy often requires different skills than advocacy in litigation or mediation. Advocates should hone these skills now. ■

ENDNOTES

1. See, e.g., Lewis L. Maltby, *Private Justice: Employment Arbitration and Civil Rights*, 30 COLUM. HUM. RTS. L. REV. 29, 55 (1998). For a complete summary of the empirical data on employment arbitration, see Richard Bales, *A Normative Consideration of Employment Arbitration at Gilmer's Quinceañera*, <http://ssrn.com/abstract=863804>.
2. *Prevot v. Phillips Petroleum Co.*, 133 F. Supp. 2d 937, 939–41 (S.D. Tex. 2001) (refusing to enforce arbitration agreement).
3. *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 687 (1996).
4. *Louisville Peterbilt, Inc. v. Cox, Ky.*, 132 S.W.3d 850 (2004), *overruling* *Marks v. Bean, Ky. App.*, 57 S.W.3d 303 (2001). For criticism of this "severability doctrine" as applied by federal courts, see Richard Bales, *Contract Formation Issues in Employment Arbitration*, __ BRANDEIS L.J. __ (forthcoming spring 2006).
5. Stephan Landsman, *ADR and the Cost of Compulsion*, 57 STAN. L. REV. 1593, 1612 (2005).
6. Jean R. Sternlight, *As Mandatory Binding Arbitration Meets the Class Action, Will the Class Action Survive?*, 42 WM. & MARY L. REV. 1 (2000).
7. *Shankle v. B-G Maint. Mgmt.*, 163 F.3d 1230, 1234 (10th Cir. 1999); *Ingle v. Circuit City Stores, Inc.*, 328 F.3d 1165, 1175–77 (9th Cir. 2003).
8. *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105 (2001). In *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 33 (1991), the Court compelled arbitration of an age discrimination case, but expressly left open the scope of the FAA's "contracts of employment" exclusion.
9. See, e.g., *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 625 (1985).
10. *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 687 n.3, 688 (1996) (holding that the FAA preempts any state law (whether legislative or judicial) that is targeted specifically to void arbitration agreements, and not contracts in general, even if the purpose of the law was to promote the knowing choice of arbitration).
11. See, e.g., Jay Folberg, *Arbitration Ethics – Is California the Future?* 18 OHIO ST. J. DISP. RESOL. 343 (2003).
12. 9 U.S.C. § 10(a).
13. *Wilko v. Swan*, 346 U.S. 427, 436 (1953), *rev'd on*

other grounds, *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989).

14. *See, e.g.*, *Jacada (Europe), Ltd. v. International Marketing Strategies, Inc.*, 401 F.3d 701, 713 (6th Cir. 2005); *DiRussa v. Dean Witter Reynolds, Inc.*, 121 F.3d 818, 821 (2d Cir. 1997).
- 15 KRS 417.160.