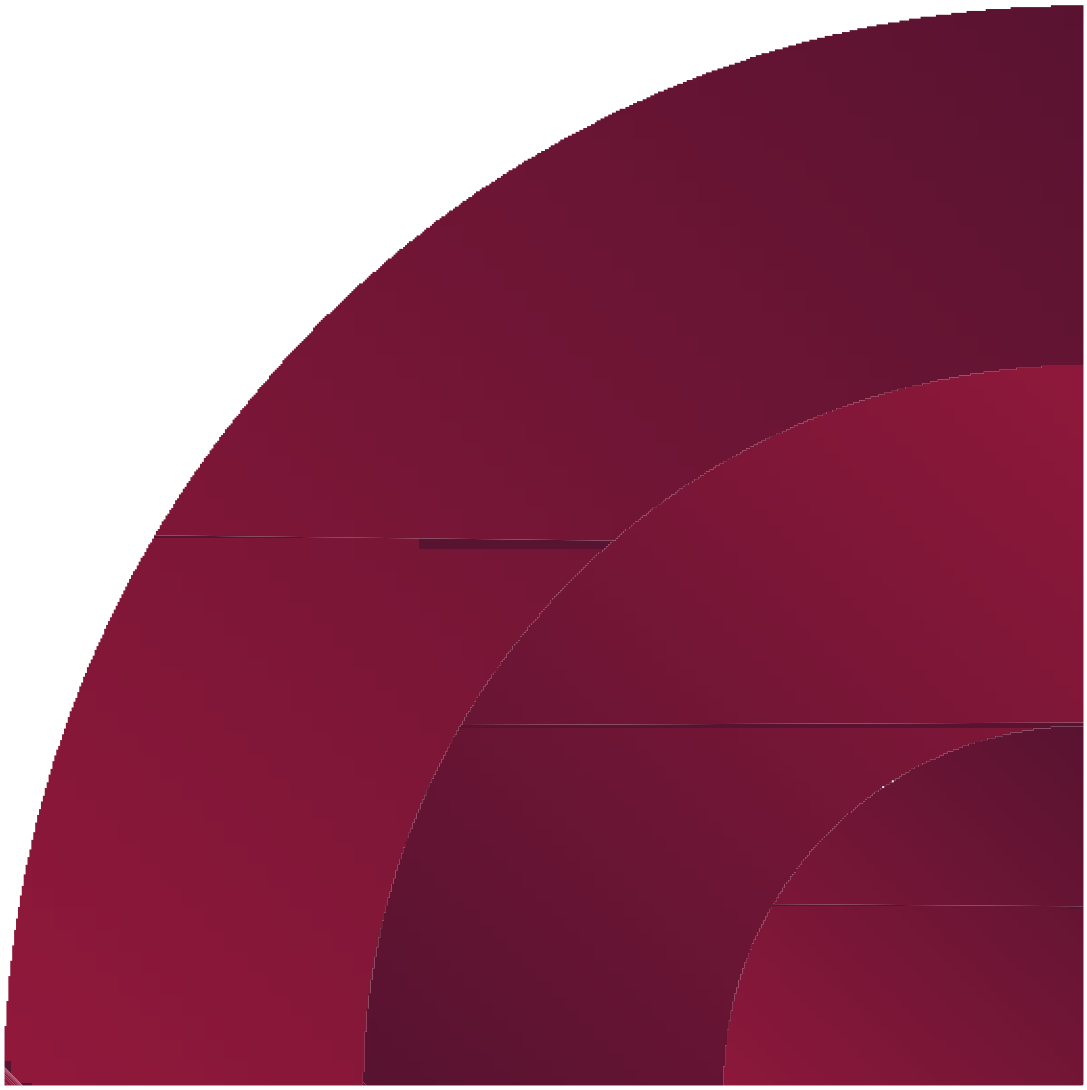
Loney Stewart Holland

A Litigator's Guide to…

Alternative Dispute Resolution Clauses



Alternative Dispute Resolution ("ADR") is a loose term encompassing various methods that have developed to try and resolve a dispute without resorting to a full court trial. In the right circumstances, ADR clauses in contracts can help parties resolve a dispute. In other circumstances, they have the potential to operate as a 'straitjacket', restricting tactical choices or, in extreme cases, limiting remedies.

In this guide, we take a look at some common binding and non-binding ADR provisions and share our thoughts on when they are best utilised (and avoided) and give some overarching views on ADR provisions generally.

We should add that we are firmly of the view that finding a way to resolve a dispute is usually far preferable than the alternative. It will save time, money and stress. The question is whether a particular route should be chosen at the outset of a contract or left to be determined if a dispute arises.

Non-Binding Routes (i.e., methods of facilitating negotiation and agreement)

Mediation

Mediation is probably the most common type of express ADR provisions. Mediation is essentially a method of negotiation through 'shuttle diplomacy' with the help of a trained independent third-party. Mediation can certainly be effective in the right case.

However, we find that mandatory mediation provisions can also prove problematic. Mediation can be an expensive exercise and ultimately, most cases we deal with can be resolved by traditional negotiation, without the need for a formal mediation process.

We also find that mediation is most effective when both parties voluntarily agree to the process, rather than being forced into it, when it has the potential to be ineffective and even. Usually this is because the issues have not been sufficiently 'cooked' so that both parties understand fully the merits and risks of the case, and therefore are not in the mindset where they are ready to compromise on their positions.

Mediation might nonetheless be suitable in some commercial settings, where your client may benefit from mandatory steps before court proceedings can be commenced, and provided your client is content to run the risk of possible wasted time or fees.

'Tiered' escalation procedures

This is where disputes are escalated through tiers of management in the hope that a commercial resolution can be found before a dispute becomes fully entrenched. This can work most effectively for contracts which are ongoing projects that require continuous cooperation and where there is a lot to lose if the relationship breaks down. Where It works, it will avoid legal fees and potentially salvage a business relationship.

The potential downside is the 'straitjacket' effect that could fetter or delay one party's ability to pursue its rights in circumstances where the parties are already entrenched or the contract has come to an end. There is of course nothing to stop any parties to a contract engaging at a senior level if it might help solve a problem.

Binding Routes i.e., alternative routes to impose a solution on parties

Arbitration

This is a private forum involving an arbitrator making a final and binding judicial decision on the parties. The principal reasons you might propose arbitration clauses are because:

- there is a particular reason the parties might want a dispute to be kept confidential; or
- the subject matter will require specialist knowledge and so you want to pick an arbitrator with appropriate industry expertise. Insurance and technology contracts are common scenarios.

The potential advantages to arbitration can also be potential disadvantages, depending on the circumstances. The relative flexibility can lead to quicker, cheaper outcomes. Equally, that's not always the case. Arbitration can add additional layers of expense, not least because the arbitrator's fees are payable in addition to lawyer's fees. Furthermore, without a clearly defined procedural route (like we have with the courts), there is the potential for additional uncertainty and satellite disagreements over matters such as disclosure. In our view, the court process is usually the preferred default unless there are very good reasons to favour arbitration.

Adjudication

Adjudication is most commonly associated with construction contracts and involves the referral of a dispute to a third-party adjudicator who will make a determination. Adjudication is imposed by statute in some cases and, in others, parties might nonetheless agree to utilise it. This is effectively a more 'rough and ready' procedure to court proceedings or arbitration, which can in principle help to keep fees down and deliver a comparatively quick outcome in a matter of weeks. It is an effective method in the construction industry where fairly low-level disputes are common and cashflow is tight.

However, in more complex cases and other industries, it tends not to work quite as well. Adjudication moves quickly, fees can build up and the momentum perhaps doesn't always allow the parties time to try and resolve disputes through traditional means. Most businesses usually want the confidence that, if the dispute cannot be resolved informally, there will be an opportunity for a more robust Judge-led court procedure to determine the case.

Expert determination

This is another process where a particular individual is appointed to effectively take the place of a Judge. Usually, it is only appropriate where a dispute is likely to be confined to a particular technical question, rather than more complex or wide-ranging factual or legal questions.

A good example might be a decision to appoint an accountant specifically to resolve a dispute over completion accounts in a Share Purchase Agreement. It wouldn't be appropriate for that expert to rule on *all* potential disputes that might arise under the SPA, but this would be a narrow question within their expertise.

Appropriate Carve Outs

In most contracts, even if you think a ADR process will be appropriate, it will still be sensible to consider when it shouldn't apply. Depending on the commercial context and type of ADR provisions being considered, these might include:

- where a party wants to seek injunctive relief. This will usually be an urgent remedy and would be frustrated by following an alternative process first;
- where limitation or time limits might be an issue; and/or
- Pure debt claims where, again, momentum can be key to applying pressure and debtors will commonly use set procedures as delaying tactics.

So do commercial contracts need ADR provisions at all?

As litigators, we certainly don't envy commercial lawyers who face a tough task drafting any agreement and trying to envisage how a relationship might go wrong. Our advice would be that, if you can identify a good reason for a particular method, then go for it. But otherwise, we would suggest that the default should be to avoid express provisions because, if a problem does arise, it gives flexibility to choose the right strategy for the circumstances.

An imposed negotiation procedure will not usually create the right conditions to settle a claim. An alternative judicial procedure (adjudication, arbitration or expert determination) can have advantages in specific types of cases, but in other they may lead to unintended consequences – usually increased costs or rough justice.

The litigation system is certainly fraught with problems. It can be expensive, time consuming and involve significant risk and delay. However, oddly enough, these inbuilt inefficiencies often work to encourage parties to voluntarily settle disputes between themselves sooner rather than later. In our experience and assuming the right strategy is adopted, most commercial disputes can be resolved without the need for any form of court proceedings and usually via traditional informal negotiation methods.

How We Can Help

We are always happy to have a chat to fellow professionals about whether ADR provisions might be appropriate in a specific commercial setting. We can give a perspective on how things might play out if a contract goes wrong and help decide how best to plan for that.

If a dispute does arise, we are always available to speak informally in the first instance and, if our help is needed, we can develop the right strategy to resolve the situation favourably. Our fee structures are transparent, and we offer a high level of service from our experienced team. So, please get in touch if you would like our help.

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