Arbitration Beware !

by Sewall “Spike” C. Cutler, Jr.

Most subcontract agreements have dispute resolution provisions which call for either mandatory arbitration, or arbitration at the option of the general contractor. Agree to mandatory arbitration at your risk!

Arbitration is touted by its proponents for various reasons, principally revolving around alleged savings in cost and time. Arbitration fans tout cost savings, but savings can only be realized in arbitration by removing the procedural protections inherent in litigation. Most commonly removed: the right to comprehensive discovery, the ability to ask questions, see documents and examine witnesses, all to gather information needed to prosecute or defend your dispute. Arbitration discovery is substantially limited compared to that allowed in litigation, and while this may sound appealing, it is almost always prejudicial to subcontractors.

In commercial construction, subcontractors are subject to all of the conditions of the job, expected to assume every risk, financial or casualty, of the construction process. In arbitration, discovery is generally limited to exchanging "relevant" documents and a very limited right to conduct depositions. For the subcontractor, it means that digging into the general contractor's and owner's files to find out what really happened (i.e. why you are not getting paid, or why the project failed) is often practically impossible. The deck is stacked against the subcontractor.

Savings in time can be realized in the arbitration process, because when the subcontractor agrees to arbitrate, and select an arbitrator, matters move pretty quickly; this can be a real benefit compared to extremely-crowded court dockets which are common these days. Speed can be beneficial, but it comes at a price, the loss of the procedural protections inherent in litigation. Another arbitration problem is direct cost. Disputes between subcontractors and general contractors and/or owners usually include substantial sums owing to subcontractors for work performed. A claiming subcontractor must pay the arbitration administrator a substantial filing fee (the greater the amount in controversy, the higher the fee) just to begin the process, and then, has to pay the finder of fact (the arbitrator) by the hour for all of the work he or she does on the case. If the subcontract arbitration clause mandates a three (3) arbitrator panel, the costs have just increased by three-fold. All this, after having endured the expense of performing the work, in the first place.

There are many skilled arbitrators, or "neutrals," as they are sometimes called in the arbitration community, but by its nature, a subcontractor will find more who are more aligned with owners and general contractors, than with subcontractors. It doesn't mean they are purposely biased, but a lifetime of seeing things a particular way can affect the decision. Arbitration can be highly beneficial for disputes of limited scope and value; our firm often recommends that dispute resolution provisions in the subcontract be modified to provide for mandatory arbitration for disputes up to a limited dollar amount, perhaps $25,000 (the number can vary based on the size of the project), with arbitration of larger disputes only by mutual agreement at the time of the dispute.

The best way to address arbitration provisions is with comprehensive contract review, which our firm provides to its clients. We have reviewed and negotiated thousands of contracts from many general contractors in state and out of state, and can usually obtain some favorable changes. For more information or to speak to one our attorneys, please call us.

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