Arbitration v Litigation

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No sensible person wishes to be involved in a commercial dispute. Disputes are time-consuming, costly and often jeopardise important commercial relationships. Unfortunately, disputes are a fact of life, particularly in complex construction projects. The choice of dispute resolution process is therefore crucial, to ensure the fastest, cheapest and fairest outcome.

It is possible to categorise the dispute resolution process into two stages:

(a) Consensual Dispute Resolution (loosely described as Alternate Dispute Resolution ("ADR"), such as mediation; and

(b) a Non-Consensual Resolution based upon a final and binding determination by an independent third party, such as litigation or arbitration.

In relation to virtually all disputes, ADR should be explored as an option for dispute resolution, before parties resort to litigation or arbitration. Successful ADR will generally result in a quicker and cheaper outcome than either litigation or arbitration, and often ensure that the potential animosity generated by litigation and arbitration is reduced, thus preserving a valuable commercial relationship.

However, ADR will only be a successful form of dispute resolution if both parties have a genuine desire to resolve the dispute. Both parties must make compromises if a solution is to be reached. Mediators often say a fair settlement has been reached if neither party is happy with the outcome.

In recent times the construction industry has favoured arbitration over litigation, where a commercial settlement could not be achieved. As a result, it is now common practice to incorporate an arbitration clause in construction agreements (see standard form contracts such as JCC and AS2124 based suite). This article explores the efficacy of entering into an "arbitration agreement'' at any time prior to a particular dispute arising, and in particular, at the time of entering into the main agreement.

Arbitration v litigation - a brief comparison

Traditionally, arbitration was perceived to have certain advantages over litigation, namely speed, cost, technical expertise in the decision-maker, and privacy.

In recent years, these perceived advantages have been eroded, particularly in relation to larger and more complex disputes. In fact, the larger and more complex a dispute becomes, the narrower the gap between litigation and arbitration, until a point is reached where litigation may be the preferred method of dispute resolution. It is not possible to determine the most suitable form of dispute resolution until all the circumstances of a dispute are analysed.

Further, a significant amount of the Courts' time, and the parties' money, has been taken up with preliminary disputes relating to whether the arbitrator has jurisdiction to determine the dispute. That is, Courts have been asked to decide on threshold issues such as whether a particular clause is an "arbitration agreement" or not, and whether a particular dispute is in relation to the matters dealt with under the arbitration agreement. This has resulted in arbitration losing some of its appeal.

Speed and cost

Speed and cost are intimately linked - the longer a matter takes before it is resolved, the greater the cost (both in legal fees and costs to the business, e.g. management time in attempting to resolve the dispute). Originally, arbitration was perceived to be a quicker and cheaper form of dispute resolution and litigation essentially because:

- an arbitration hearing could take place as soon as the parties were ready, whilst Courts, with a backlog of cases, have quite a waiting list; and
- arbitrators, under the uniform *Commercial Arbitration Act*, have flexibility as to the pre-hearing procedural steps which the parties are to take, and thus, may do away with procedural steps which are unnecessary in relation to a particular dispute.

In the more complex and larger construction disputes, these time and cost advantages have largely disappeared. It is unusual, and in many large and complex cases it may be inappropriate, for an arbitrator to exclude steps normally associated with litigation, such as pleadings, discovery and permitting Counsel to represent the parties. It is these steps which are costly and time-consuming, but which are essential to uncovering the facts and presenting the case. In addition, if a party refuses to accept the arbitrator's directions, or disagrees with them, in relation to procedural matters, it will be necessary for the aggrieved party to apply to the Court for an order, either compelling compliance or overturning the arbitrator's direction. This obviously represents a delay in the proceedings, as well as increased costs.

Further, as arbitration is generally a private form of dispute resolution, each party must pay the arbitrator for his/her time. If the arbitrator is a QC, this may be as much as $5,000 per day, although more likely to be between

$1,500 and $2,000. The parties are also responsible for other associated costs such as room hire.

Finally, the Victorian and New South Wales Courts have recently introduced specialist procedures for dealing with construction disputes (''Building Cases lists"). The Judges, who have particular expertise in complex construction-law issues, only hear construction law disputes. Further, there are special procedural rules to ensure that disputes are heard quickly, and cost-effectively, including Directions Hearings (where Judges set down a time table for pre-trial steps) and a discretion on the part of the Judge to do away with procedural steps which are not necessary for a fair resolution of the dispute. These changes bring construction litigation closer to the original ideal of arbitration.

Technical expertise

As mentioned above, the Victorian and New South Wales Courts have introduced specialist construction law Judges who have particular experience in construction law disputes. In addition, these Courts have the power to refer all or part of a matter to a Special Referee who is required to either make a determination or supply a report to the Court. This enables the Judge to have access to unbiased expert information on complex technical issues. The New South Wales Courts have been more prepared than their Victorian counterpart to adopt, without review, the determination or findings of the Special Referee.

These changes go a long way toward countering the argument that arbitrators are better placed than the Courts because the former have access to better technical skills.

Finally, often arbitrators are excellent technicians, but do not have a strong legal training or background. Accordingly, if a dispute involves complex issues of law, often the Courts are superior to arbitrators in making the correct legal determination. Of course, an arbitrator may refer a point of law to the Courts for determination, but this adds to the time and expense required to resolve the dispute.

Privacy

Until recently it was believed that the parties involved in arbitration were assured of strict confidentiality in relation to the dispute and its outcome which contrasts with the Courts, where confidentiality is generally denied, based on the principle of open justice. This aspect of arbitration was particularly appealing to parties in disputes which involved potentially embarrassing or sensitive situations.

However, the recent decision of the High Court of Australia in *Esso Resources & Ors v The Honourable Sidney Plowman (The Minister for Energy and Minerals)* (see (1996) ACLN #46, p57) has reduced the scope of this advantage. The Court decided that arbitrations should be heard in private, in the sense that strangers should be excluded unless the parties consent to the presence of the stranger. However, there is no absolute duty of confidentiality preventing the parties, witnesses or the arbitrator from disclosing the existence of the proceedings, or documents and information provided in and for the purposes of the arbitration, except that documents which are the subject of discovery are protected by the usual undertaking not to use them for any purpose other than in relation to the arbitration in which it is disclosed.

Obviously, if the parties have entered into an express confidentiality agreement in relation to the arbitration, this will lead to an obligation of confidentiality imposed on all persons who executed the confidentiality agreement.

The lesson here is always to include a confidentiality clause in an arbitration agreement, and require all persons who attend an arbitration to execute a confidentiality agreement, otherwise they will be free to disclose information gained from the proceedings.

Third parties

As the authority of an arbitration is essentially gained from the "arbitration agreement", it is not possible to join as parties to the arbitration people who are not parties to the arbitration agreement. It is true that under the uniform *Commercial Arbitration Acts*, it is possible to consolidate two or more arbitrations which deal with the same issues. However, if one party has a claim against a stranger (that is, a person with whom the party does not have an arbitration agreement), such as a consultant, the party will be forced to commence separate litigation proceedings to enable it to recover from the stranger.

Conclusion

It is clear, from the above, that at least with respect to larger, more complex construction law disputes, there are some drawbacks in the arbitration process, and that in some cases litigation may be the preferred option. The purpose of this article has not been to outline the circumstances where one form of dispute resolution is preferred to the other, but to raise awareness that the best time to decide on the second stage of the dispute resolution process (that is, binding determination) may be when a particular dispute has arisen, rather than at the date of executing the main agreement.

The above is emphasised by the recent High Court of Australia decision in *PMT Partners Pty Ltd v Australian National Parks & Wildlife Service,* High Court, 11 October 1995 (see (1995) ACLN Issue #45, p4). In this case, the Court found that a clause which had traditionally been recognised as not committing the parties to arbitration until such time that one party took a particular step (which was always after a dispute had arisen), did in fact commit the parties to arbitration in relation to all disputes which arose out of the main agreement. Accordingly, parties may now be bound, at the outset, to a dispute resolution process which, may be inappropriate for the particular dispute.

As a result, there is a view amongst some practitioners and members of the construction industry that parties to an agreement should be reluctant to enter into a contract which contains an arbitration clause.

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Editorial Note:

For balance, it should also be considered that not every Court Reference will have a happy outcome. The parties may become locked into a protracted, expensive Reference process. Further, there are examples where Referees' Reports have been rejected by the courts, with unfortunate wasted time and costs.

- **J.T.**