CHAPTER 8

An Overview of Commercial Arbitration

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Synopsis

§ 8.01. Introduction.

Arbitration is "[t]he reference of a dispute to an impartial (third) person chosen by the parties to the dispute who agree in advance to abide by the arbitrator's award issued after a hearing at which both parties have an opportunity to be heard."[(1)] Although arbitration has been around for thousands of years, only in the last 70 years has arbitration become a popular means of dispute resolution in the United States.

Arbitration has several distinct advantages over litigation in the courts. The proceedings are generally focused on a relatively small number of issues. The finder of fact and ultimate judge of the parties' claims and defenses is typically an individual who possesses a level of expertise in the particular field in which the dispute arises. Arbitration generally encourages the use of stipulations and discourages prolonged and costly discovery. Arbitrators have broad discretion in determining what evidence will be admitted during an arbitration hearing; the parties are generally spared the expense associated with motions *in limine*, bench memoranda, and trial planning that revolves solely around the admissibility of evidence. Arbitrators also have broad discretion in fashioning a remedy. Their decisions are accorded extreme deference by courts.

On the other hand, arbitration is not without risk. It generally contemplates a cooperative process where the parties have a mutual interest in a speedy resolution of their dispute. However, when business relationships go bad, it is often because one party has unilaterally embarked on a course of action in furtherance of its own economic interests and to the detriment of its business partner. Under these circumstances, the aggrieved party clearly has an incentive to press for an expeditious resolution of the dispute. That incentive may not be shared by the party who precipitated the controversy. The potential for frustration is apparent. While one party tries to invoke the cooperative process of arbitration to end the matter, the other may feel no compulsion whatsoever to cooperate. Finally, an arbitration award generally cannot be appealed solely because of an error of law, a misconstruction of a contract, or even an erroneous finding of fact. Hence, whatever the result of arbitration, the parties generally have to accept it.

This Chapter will briefly discuss the evolution of arbitration in the Anglo-American legal system, enactment of the Federal Arbitration Act[(2)] (FArbA), and some practical observations about the arbitration of commercial disputes. For purposes of illustration, reference will occasionally be made to specific provisions of the FArbA and to the American Arbitration Association Commercial Arbitration Rules[(3)] (AAA Rules).

§ 8.02. Historical Background.

The earliest recorded arbitration proceedings occurred around 2550 B.C. in the civilizations of Mesopotamia and Ur.[(4)] In ancient Greece and Rome, arbitration was a common means of resolving differences for Greek and Roman merchants.[(5)]

Early English courts enforced agreements to arbitrate disputes. The earliest written records of arbitration proceedings in England date to the twelfth century. English cases from the early thirteenth century (cases decided in 1224, 1231, and 1233) denied parties access to the law courts if they had already submitted the case to arbitration.[(6)] Members of Merchant Guilds and Craft Guilds were required to arbitrate their disputes before being permitted access to the courts.[(7)]

However, later English courts were hostile toward arbitration agreements. Around the end of the seventeenth century, English courts routinely held that executory arbitration agreements were revocable by either party at any time before the issuance of an award.[(8)] By the middle of the eighteenth century, English courts pronounced that arbitration agreements were against public policy because they deprived the courts of jurisdiction to resolve disputes. Lord Campbell stated that the hostile attitude of the English judges toward arbitration was due to their desire to avoid losing income. At that time, a judge's income consisted almost entirely of fees earned from hearing cases. Thus, to prevent the loss of fees, English judges refused to