ARBITRATION, BENCH TRIAL, OR JURY TRIAL? A FUNCTIONAL GUIDE FOR IN-HOUSE COUNSEL

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1. Introduction

Over two decades ago, the then-president of the American Arbitration Association touted arbitration as "an idea whose time has come" because, according to him, arbitration gave parties "speedy and inexpensive justice" that was otherwise "hard to come by in American courts."[1] The U.S. Supreme Court reflected this view in decisions like *Shearson/American Express v. McMahon*, [2] which abandoned the "mistrust" that the Court had expressed in earlier decisions such as *Wilko v. Swan*.[3]

Today, lawyers representing both plaintiffs and defendants have begun to question the suitability of arbitration for many disputes. As leading arbitration scholar Gary Born has observed, lawyers often criticize arbitration as "both slow and expensive" because of expensive administration costs, arbitrator fees, and difficulties in scheduling, among other things.[4]

The 1980s trend toward arbitration reflected a faith that arbitration would help reduce not only costs, but also uncertainty in dispute resolution. That faith failed to account for the inherent flaws in any process for dispute resolution. As Judge Jerome Frank observes in his book *Courts on Trial*, any process for resolving disputes "is, and always will be, human, and therefore fallible. It can never be a completely scientific investigation for the discovery of the true facts."[5]

In truth, the value of arbitration versus court litigation depends on the case, the facts, and the parties. Moreover, parties typically must decide to arbitrate at a contract's inception, when the parties generally expect that their deal will succeed, not fail. Indeed, the parties preparing the contract predominately use transactional lawyers, not litigators. As a result, the parties and the lawyers documenting the deal may lack trial experience that could help make an informed decision. In this article, we provide an overview of different instances in which parties entering into a contract may decide to forgo arbitration or choose one type of arbitration over another. We also remind the reader that the choice of dispute resolution, while important, cannot replace the core consideration of whether the transaction makes sense in the first place.

2. What Are the Choices?

Parties to a commercial contract have at least three broad choices as to dispute resolution: (a) jury trial (the default option); (b) bench trial; (c) arbitration under the American Arbitration Association or other arbitral entity, as well as *ad hoc* arbitration and "baseball" style arbitration.

a. Jury Trial: The Default Option

Corporations shy away from jury trials. Many corporate lawyers share the view of Dean Erwin Griswold of Harvard, who observed that "[t]he jury trial is the apotheosis of the amateur. Why should anyone think that 12 persons brought in from the street, selected in various ways, for their lack of general ability, should have any special capacity for deciding controversies between persons?"[6]

Many corporate lawyers and executives give little weight to the large number of mediocre verdicts, let alone the large number of trial-court cases that result in defense verdicts or settle confidentially (for reasonable, not dramatic, sums) before a jury decides them.

Another source of corporate anxiety about jurors comes from the media. Because large verdicts receive the majority of media attention, corporate executives, like most other people, often overestimate the proportion of large verdicts. The problem of so-called "silent evidence" skews our perception of the trial process by consistently underreporting the vast majority of verdicts and judgments that award far less dramatic sums than the mainstream media suggests. Indeed, journalists are "industrial producers" of the distortion.[7] Courthouses abound with the silent evidence of juries that award small awards or nothing at all. Many corporate lawyers and executives give little weight to the large number of mediocre verdicts, let alone the large number of trial-court cases that result in defense verdicts or settle confidentially (for reasonable, not dramatic, sums) before a jury decides them.

Consider the example of Fred Bartlit's defense of Dun & Bradstreet against an antitrust claim brought by a competitor, National Business Lists. In defending the case, Bartlit contended not only that Dun & Brandstreet never violated the antitrust laws, he counterclaimed against NBL for copyright infringement because NBL for decades had used D&B's books for NBL's own competing products. Bartlit relied on D&B executives to testify, whom he had discovered were not arrogant high-flyers, but rather modest and approachable. In the end, Bartlit and D&B prevailed, defeating NBL's antitrust claim and obtaining a $7.7 million verdict on D&B's copyright counterclaim. Summing up the experience, Bartlit observed that "[a]s usual, the jury was more interested in these three or four main points and in the 'bad guy-good guy' material than in the nuances. . . . Simplicity w[ins] the day."[8]

Some corporate counsel might take Bartlit's observation and insist on arbitration on the grounds that arbitrators are more nuanced and less prone to emotional appeals than a jury. That belief may exaggerate the differences between arbitrators and jurors. More than a century ago, Francis Wellman, in his classic *The Art of Cross Examination*, noted the sophistication of juries that applies equally to arbitrators: "Present day juries, especially in large cities, are composed of practical business men accustomed to think for themselves, experienced in the ways of life, capable of forming estimates and making nice distinctions, unmoved by the passions and prejudices to which court oratory is nearly always directed."[9]

Although juror composition has changed in the past century, Wellman's perspective is not much different than Bartlit's: civil juries tend to come to far more practical and common-sense results than many observers give them credit for. Runaway verdicts are the exception, not the rule.

b. Bench Trials

Many commercial parties include jury trial waivers in their contracts and assign the fact-finding function to a sitting judge. Again, corporate lawyers may overestimate the difference in outcomes between jury trials and bench trials. As one study showed, reviewing four thousand civil trials, in 47% of all cases both judge and jury found in favor of the plaintiff and in 31% they found in favor of the defendant. When there was disagreement, 10% of the time the judge favored the plaintiff and 12% of the time the judge believed the defendant should have won although the jury chose for the plaintiff.[10]

The anecdotal evidence also indicates little difference in outcomes. Famed trial lawyer Louis Nizer explained his experience in his classic *My Life in Court*:

> Although jurors are extraordinarily right in their conclusion, it is usually based upon common sense 'instincts' about right and wrong, and not on sophisticated evaluations of complicated testimony. On the other hand, a judge, trying a case without a jury, may believe that his decision is based on weighing of the evidence; but . . . he, too, has an over-all, almost compulsive 'feeling' about who is right and who is wrong and then supports this conclusion with legal technology. Because judges, sometimes, consciously reject this layman's approach of who is right or wrong and restrict themselves to the precise legal weights, they come out wrong more often than the juries.[11]

Corporate lawyers should bear Nizer's advice in mind: no method of dispute resolution can insulate itself from human nature and the morality play that underlies any case.

c. Arbitration

As the reader may suspect by now, the authors are skeptical that arbitration provides a panacea from the imperfections in the trial process. Within the general category of arbitration, commercial parties generally choose among (i) traditional arbitration before the American Arbitration Association or other arbitration authority; (ii) *ad hoc* arbitration that the parties organize outside of arbitration; including (iii) expedited "baseball" style arbitration. Each has its merits and its flaws.

(i) Traditional Arbitration

Despite the prediction that AAA arbitration would give parties "speedy and inexpensive justice,"[12] many trial lawyers – for both plaintiffs and defendants – have lost faith in full-scale AAA-sponsored arbitration.

The most common criticism of AAA-sponsored arbitration is the cost. Good arbitrators charge fees comparable to the fees that large-firm lawyers charge. The AAA requires, in most cases, that the parties to the arbitration make a deposit for arbitrator fees that will compensate the arbitrators through the final hearing (trial). This figure often exceeds $30,000.[13]

Take, for example, the Second Circuit's decision in *Blue Tee Corp. v. Koehring Co.* [14] That case involved a dispute over a garden-variety asset-purchase agreement. But because the transaction involved two separate contracts containing different arbitration provisions, the parties' dispute became mired not only in the commercial issues, but also in the threshold procedural questions of which arbitration provision

governed. That question then led to further disputes about whether the court or the arbitrators had the power to decide these threshold issues. Without question, the presence of arbitration provisions complicated, rather than simplified, the case. As the Second Circuit observed, "[t]his appeal . . . makes one wonder about the alleged speed and economy of arbitration in resolving commercial disputes."[15] The Second Circuit observed in another case almost seventy years ago: "The more enthusiastic of [its] sponsors have thought of arbitration as a universal panacea. We doubt whether it will cure corns or bring general beatitude. Few panaceas work as well as advertised."[16]

Yet for many disputes, arbitration probably is the lesser of many evils. This includes international arbitration, construction arbitration, and other complex cases.

(ii) *Ad hoc* Arbitration

Many parties choose to opt out of AAA arbitration and instead employ arbitrators outside of the AAA structure. This reduces administrative fees, which can be considerable, and in the experience of many lawyers, the AAA adds little to the process besides access to its roster of neutrals. Further, the AAA has no online filing database comparable to the PACER or state-court equivalents, and combined with inherent scheduling complexities, sometimes inefficient administration, and all parties, including the fact-finders, billing by the hour, can quickly become too expensive.

(iii) "Baseball" style-arbitration

Baseball arbitration may take several forms. Most commonly, the parties restrict the arbitrator's choices to one of two proposed awards: one from the claimant or plaintiff, and the other from the respondent or defendant. The arbitrator has no other choices, even if the arbitrator believes another choice would produce a fairer or more just outcome. "The arbitrator, in other words may not 'split the baby.'"[17] "Night baseball arbitration" provides another version under which the arbitrator never learns the parties' final offers. The arbitrator enters a decision and the party that has made its (undisclosed) offer closer to the arbitrator's final award wins and that parties' offer becomes the award.[18]

Baseball arbitration, at least according to theory, encourages parties to adopt compromise positions and, perhaps, simply to settle their disputes.[19] In commercial transactions, baseball arbitration works well in single-event or one-time transactions that have reasonably predictable outcomes. A common example arises in mergers or acquisitions in which the final closing price remains subject to adjustments or in an agreement requiring a future appraisal of value. There, the final closing price may depend on the target's performance or the future appraisal of value, which in turn depend on macroeconomic factors.

In situations like this, baseball arbitration for certain provisions within the contract increases the predictability of the range of outcomes should a dispute arise. If both sides are generally sophisticated and reasonable parties, including baseball arbitration forces them to enter into the dispute with a reasonable position and keeps them from the temptation of swinging for the fences.

3. Concluding Thoughts: Tailor the Choice to the Type of Contract

As Yogi Berra reportedly said, it's hard to make predictions, especially about the future. Choosing among jury trial, bench trial, or type of arbitration requires a case-by-case judgment. No one-size-fits-all solution exists for corporate counsel.

Another way corporate counsel might consider the decision about whether to contract out of a jury trial would include consideration about whether to do the deal at all. Warren Buffett observes: "We've never succeeded in making a good deal with a bad person."[20] In the authors' collective experience, Buffett's advice is sound. But Buffett also reminds us why we or our clients want to do deals, sometimes bad deals, in the first place: "Dealmaking beats working. Dealmaking is exciting and fun, and working is grubby. . . . That's why you have deals that make no sense."[21]

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In short, although the type of dispute resolution provision that the parties put into a contract may have a significant impact on a potential case, corporate counsel and other executives involved in the dealmaking process should keep in mind that the differences among types of dispute resolution procedures may not be as great as they think. From our experience in seeing such matters fall into dispute, the dealmakers should put the merits of the deal first, and then, after considering the likely type of outcomes possible, tailor the dispute resolution provision accordingly. Most importantly, no dealmaker or advisor should ever depend on a dispute resolution clause, no

matter how expertly crafted, to protect against an otherwise bad deal.

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1 "Arbitration Offers Speedy Alternative to Costly Litigation," Deseret News, Jan. 21, 1990.
2 Shearson/American Express v. McMahon, 482 U.S. 220 (1987).
3 Wilko v. Swan, 346 U.S. 427 (1953).
4 Gary Born, International Commercial Arbitration: Commentary and Materials 9-10 (2d ed. 2001).
5 Jerome Frank, Courts on Trial, quoted in Ephraim London, The Law as Literature 731, 750 (1960)
6 Erwin Griswold, Harvard Law School's Dean's Report (1963).
7 Nassim Nicholas Taleb, The Black Swan 102 (2007).
8 Emily Couric, The Trial Lawyers 38 (1988)
9 Francis Wellman, The Art of Cross Examination 21 (1903)
10 H. Kalven, The Dignity of the Civil Jury, 50 Virginia Law Review 1055-1075 (1964), cited in Valerie Hans & Neil Vidmar, Judging the Jury 117 (1986).
11 Louis Nizer, My Life in Court 359 (1978)
12 "Arbitration Offers Speedy Alternative to Costly Litigation," Deseret News, Jan. 21, 1990.
13 Kerr, International Arbitration v. Litigation, 1980 J. Bus. L. 164, 164-65 175-78 ("Arbitral tribunals have to be paid, whereas court fees are often negligible. In important cases, three arbitrators, or two and an umpire, are usually preferred to a single arbitrator, and greatly adds to the costs and complexities. If the arbitrators are busy men, as they usually are, arbitration can be much more protracted than litigation…."), quoted in Born, supra note 4, at 10.
14 Blue Tee Corp. v. Koehring Co., 999 F.2d 633 (2d Cir. 1993).
15 *Id.*
16 Kulukundis Shipping Co. v. Amtorg Trading Corp., 126 F.2d 978, 987 n.32 (2d Cir. 1942).
17 Abraham J. Gafni, "Baseball Arbitration" and the Trial of Socrates, The Legal Intelligencer, Feb. 28, 2011, reprinted in Texas Lawyer, Feb. 28, 2011.
18 *Id.*
19 *See id.*
20 Warren E. Buffett, The Essays of Warren Buffett: Lessons for Corporate America 99 (1st rev. ed. 2001).
21 *Id.* at 164.