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Arbitration begins with the contract

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Arbitration, one form of alternative dispute resolution, is an integral part of the fabric of many technology agreements. How an arbitration clause is drafted can have a significant impact in the event of a dispute involving the agreement.

Many contract drafters place the ADR provision into the category of contract boilerplate. Frequently the time-worn "standard arbitration language" is inserted into the contract and the parties may give little additional thought to the ADR provision. Possibly this is because the parties focus, as they should, on the success of the subject of the contract and the arbitration provision speaks to the possible failure of the transaction.

For several reasons, I suggest that, in most cases, the arbitration provision should be given more consideration by the parties.

First, if a breach of the agreement is subsequently alleged, the agreement will most likely be read by a third party unfamiliar with the specific negotiations and background of the transactions. Second, that third party may be a judge or an arbitrator trying to figure out what the parties intended in the agreement. Third, in most cases, thoughtful attention to the drafting of the arbitration provision gives the parties an opportunity to shape how their dispute will be resolved in the event of a breach.

There are multiple factors that may be considered by the parties in deciding whether or not to include an ADR provision in their agreement. But, when the choice is made to include an ADR provision, the parties should carefully consider the alternatives in drafting the particular elements of the ADR provision. As the U.S. Supreme Court stated in *Preston v. Ferrer*, No. 06-1463, decided Feb. 20, 2008):

"... [T]he Federal Arbitration Act (FAA or Act), 9 U. S. C. §1 et seq. (2000 ed. and Supp. V), establishes a national policy favoring arbitration when the parties contract for that mode of dispute resolution. ... When parties agree to arbitrate all questions arising under a contract, the FAA supersedes state laws lodging primary jurisdiction in another forum, whether judicial or administrative."

Like most contract provisions, there is no "one size fits all" in the drafting of the ADR provision — the ADR clause in one agreement may contain inappropriate language for the next transaction. The ADR clause must be carefully drafted to fit the specific transaction.

The contract drafter, who may be one of the parties or their lawyer, after a careful legal analysis of the particular facts of the specific transaction will make certain decisions concerning what to include, or not, in the drafting of this provision. The following is not an exhaustive list of all possible considerations for the drafting of an ADR provision for arbitration, but will provide you with a starting point:

Arbitration administration (for example, administered by the American Arbitration Association, one of the other arbitration administration entities, or a private arbitrator).

Number of arbitrators (one or three).

Method of selection of arbitrators (neutral selection process or "party-appointed" arbitrator selection).

Arbitrators' qualifications (for example, knowledgeable in information technology and/or computer law, licensing, copyright law, and/or the computer industry).

Scope of arbitration clause. (Will it cover all disputes or just certain types?)

Is a stepped ADR process appropriate (include mediation steps, C-level management involvement)?

If the contract is to be formed online, what form of acceptance will be needed to bind the other party to the contract in general, and the ADR provision in particular?

"Entry of judgment" language.

Location of the hearing.

Choice of law provision.

Type of damages available (e.g., injunctive relief, specific performance, money damages).

Will preliminary relief be available? (Note, this is permitted under the AAA Commercial Rules.)

Discovery (pre-hearing discovery scope including number of depositions, time limits, discovery period, and so forth).

Form of award (a detailed written ["reasoned"] opinion — but note, it may increase the cost of the arbitration because of the additional arbitrator's time involved).

Multiple parties issues (for example, disputes involving third parties who were strangers to the arbitration agreement).

Remedies (for example, delineate the scope of arbitrator authority in award, but be careful in limiting the arbitrator's ability to award any statutory remedies).

If this is an international transaction, consider specifying the language of the hearing.

For some additional drafting elements to consider, you may want to take a look at the AAA's "Drafting Dispute Resolution Clauses: A Practical Guide" as one reference. Again, this is not an exhaustive list, and the contract should be prepared and reviewed by knowledgeable legal counsel.

The bottom line is to remember that the arbitration provision is one way to manage your legal risks, so be mindful when drafting ADR clauses, avoid the "it's just boilerplate" trap, and be prepared for the contract negotiations of the ADR clause. ■

Additional details concerning Mr. Wernick's practice, his published writings and public lectures are available at WWW.WERNICK.COM.