Why businesses should include dispute prevention and de-escalation clauses in their agreements

Litigation and Dispute Resolution

Every business relationship carries with it the potential for disputes. Common experience has demonstrated that problems, difficulties, differences of opinion, disagreements, and disputes can

occur at any time, even in the best of families and businesses. Given this reality, at the time parties enter into a business relationship, they have a unique opportunity to decide that when future problems occur, they will proactively fix the problem, rather than reactively fixing the blame.

Unfortunately, in today's business climate, when parties enter into a relationship, most fail to make such a choice at all; and later, when problems do arise, many of them instinctively and reactively decide to fix the blame. This choice initiates a process in which the solution to the problem is postponed, and the parties engage in an adversarial dance of confrontation and blame. The problem then escalates into a difference of opinion, then an argument, and ultimately an intractable dispute that has to be referred to the conventional dispute resolution system for ultimate resolution in some form of mediation, arbitration, or litigation.

The inevitable result of this adversarial dance is an escalating state of confrontation that can lead to the expenditure of what the professor and barrister Richard Susskind describes in his book The End of Lawyers? as the "wildly excessive and disproportionate amounts of time, energy, and cash dispensed on dispute resolution."

There IS a better way.

A common-sense approach to preventing and resolving disputes

In 1975, Sutherland Asbill & Brennan LLP published the first edition of its Manual for Using Private Dispute Resolution Clauses in Business Agreements. The thesis of that Manual was that when parties are first entering into a business relationship, they have a unique opportunity to exercise control over any future problems or disputes. It recommended that the parties specify in their agreement that any problems that arise would be dealt with through a creative series of contract clauses that would assure that any problems that arise would be addressed and dealt with in an orderly way at the earliest possible time.

Set out below is an updated version of the introductory chapter of the Manual for Using Private Dispute Resolution Clauses in Business Agreements, which closely follows the text of the original edition.

Reasons for incorporating dispute prevention and resolution clauses into business agreements

1. Recognize the disadvantages of adversarial confrontation:

Resolution of a business problem through the adversarial processes of litigation, arbitration, or even mediation, has many obvious disadvantages:

It means loss of control of the dispute. Control has shifted to strangers to the dispute: lawyers, mediators, arbitrators, or a court.

It takes too long. It will take at least several months (and in some jurisdictions several years) to get a litigated case to trial; appeals can lengthen the process by a year or more. Arbitration can generally be somewhat quicker, but it inevitably involves delays before resolution can be achieved. While mediation can, if both parties and their lawyers agree, be conducted on an expedited basis, it can be concluded only if and when the parties have reached a final agreement. These delays can create

uncertainty in business planning, adversely affect cash flow, and have other disruptive effects on the business.

It's too expensive. It costs a lot to bring even the simplest business dispute to mediation, arbitration, or trial— in the transaction costs of lawyers' fees, discovery, costs of experts and consultants, and the time and energy of the business people who are involved in processing the dispute.

It's too uncertain. Litigation, and even arbitration before expert arbitrators, is a very blunt instrument. It is often very difficult to predict how a judge, appellate court, or arbitrator will ultimately resolve a case. Even mediation, although generally voluntary, will have uncertain results that cannot be accurately predicted.

It can lack expertise. The resolution of business and technical disputes requires expertise and sophistication. It is difficult to find judges, and even arbitrators or mediators, with the qualifications to resolve complex business issues.

It can be very public. Court filings and proceedings are matters of public record. They are valuable sources of information for business competitors; they are routinely reported in trade publications; and, if they are juicy enough or it's a slow news day, they can be reported in the popular media. Even arbitrated cases can sometimes garner publicity.

It's too disruptive of business relationships. The hostility engendered by confrontation in litigation, arbitration, and even mediation makes it difficult for business people to continue to carry on normal valuable business relationships and activities with each other.

2. Recognize the disadvantages of postponing a decision about how to deal with disagreements until after a problem or dispute has arisen:

Delaying decisions about how disputes will be dealt with reduces a party's options. Once a dispute has developed, it can often be difficult to get the participants to agree on the time of day, let alone discuss rationally the optimum method for resolving the dispute. At this point, the parties are likely to have different agendas and preferences as to how they would prefer to resolve the dispute. One party may want to emphasize the facts and equities, or sophisticated business realities; the other side may prefer to be in a court of law. One party may want a quick resolution; the other party may prefer delay. One party may want to avoid publicity; the other party might prefer public exposure of the controversy. If the parties are unable to agree on a method of dispute resolution, the only available dispute resolution system is litigation.

3. Recognize the advantages of proactively agreeing early on to a dispute prevention and resolution system:

Agreeing at the very beginning of a relationship on a method for prevention, quick processing, de-escalating, and final resolution of any future problems or disputes that may arise has many advantages.

Responsible business managers are accustomed to controlling costs, quality, and other aspects of their business relationships. Using private dispute prevention, de-escalation, and resolution techniques gives them an opportunity to control conflict and disputes as well.

The beginning of the relationship, when there is an atmosphere of businesslike cooperation, and before any disputes have arisen, is the time when the parties can most rationally discuss the optimum method for dealing with any disputes.

Including the subject of dispute prevention and resolution as an element in the negotiations leading to the establishment of the relationship helps to define an important aspect of the relationship. For example, if you learn that the other party does not want to agree to have an efficient dispute prevention and resolution system, this knowledge can affect how you negotiate other terms of the agreement – or whether you want to enter into the relationship at all.

Business people often have a real fear of a foreign legal system. Exhibiting a willingness during the negotiations to set up a rational, fair, and prompt dispute resolution system should have special relevance in an international transaction.

Agreeing early on a method for dealing with potential problems can lead to creative business-oriented results, be a cooperative and satisfying experience, and is likely to help to create and preserve a healthy and continuing business relationship.

The special importance of having a dispute prevention and resolution process already in place is often overlooked. An existing process will absorb the shock of unexpected events and problems. It channels them constructively, so they can be dealt with promptly, realistically, and ultimately be solved. In the absence of a process, the parties are left to flounder without direction, which can lead to confusion, chaos, and opportunities for mischief.

The ready availability of a fair, efficient, trusted, and quick method for preventing and processing disputes tends to discourage game-playing, posturing, and delaying tactics; may well encourage the parties to cooperate and deal realistically with each other; and should in most cases result in the parties resolving the problem by themselves, without having to resort to a dispute resolution procedure at all.

4. Overcome resistance to the use of dispute prevention techniques:

Despite the acceptance of mediation and arbitration as dispute resolution alternatives to litigation in many areas of business, there is still considerable resistance to the techniques for preventing and controlling disputes. However, knowledgeable business professionals should recognize and overcome the kinds of obstacles and attitudes that can discourage parties from agreeing in advance on a system for preventing and controlling disputes. Some of these sources of resistance are:

Not wanting to spoil the euphoria. Some people may fear that addressing the subject of dispute resolution during the early stages of a relationship is akin to suggesting to a happy engaged couple that they should enter into a pre-nuptial agreement. Business should not be an emotional relationship, however; and ignoring the fact that problems and disputes can routinely occur even between the nicest people is simply a triumph of hope over reality.

Traditional resistance to change. There is often a built-in resistance to any new idea. Given the relative newness of dispute prevention and de-escalation techniques, many contract and legal professionals have never before included these processes as a subject in their negotiation agendas and checklists. (Indeed, when alternative dispute resolution (ADR) processes were first introduced, many lawyers considered the acronym ADR to represent “Alarming Drop in Revenue”!) However, now that the successes, first of the conventional private dispute resolution process, and more

recently of prevention and de-escalation processes, have become better known, that resistance has diminished. An important argument for overcoming resistance is that the principal impetus for preventing disputes comes from business people who have learned that preventing disputes can save money, so contract and legal professionals would be well advised to keep up with their business clients.

A perception that multi-level dispute resolution slows down the process. Some people may feel that specifying more than one level of dispute prevention and resolution, such as partnering or standing neutral before resorting to mediation or arbitration, imposes an unnecessary and delaying process that will hinder the ultimate resolution of a dispute. However, sophisticated business people and lawyers know that the earlier the parties address a problem or dispute and deal with it realistically, the more likely they are to resolve it amicably; and that every dispute prevention and resolution system should contain a final and binding backstop resolution method of some kind, such as arbitration.

A perception by a party that it will benefit from an inefficient method of resolving disputes. A party that thinks that it has – or is seeking – superior bargaining power may think that it will benefit by denying the other party an opportunity to have a problem or dispute resolved promptly and efficiently. For example, a party that is obligated to pay money may, if the other party has no ready recourse, think that it can obtain leverage simply by withholding payment. Ordinarily, such a strategy only works once, because once it is exercised, the other party won't be tricked again. And if such an intended strategy is revealed during contract negotiations, the other party can increase its pricing to offset the risk that it may be deprived of the use of its money for an extended period of time, or it may refuse to enter into the business relationship.

Bottom line: In short, there is no rational excuse for responsible businesses which are entering into a relationship not to include in their agreement a system for preventing and processing disagreements as promptly and efficiently as possible.

Note: The original Manual for Using Private Dispute Resolution Clauses in Business Agreements contained an additional 25 pages describing in detail various dispute prevention and resolution methods, how they can be combined into systems, and texts of sample clauses that could be used in business agreements. Any readers of this article who would like to have an electronic copy of the current text of that portion of the Manual and sample clauses can obtain it from Eversheds Sutherland by contacting Kevin McKearney at kevinmckearney@eversheds-sutherland.com.

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He served for many years as the leader of the Construction and Dispute Resolution practices. Since his retirement, he has continued to be active, in addition to his practice as an arbitrator and mediator, as a researcher, writer, and speaker advocating the use of proactive dispute de-escalation and prevention practices in the construction industry and business in general. His most recent public service activity has been to support the work and results of the Global Pound Conference, whose worldwide participants overwhelmingly voted in 2017 that “pre-dispute and pre-escalation processes to prevent disputes” are the processes that should be prioritized to improve the future of commercial dispute resolution. He is currently compiling his lifetime writings on this subject into a book tentatively titled “Proactive Prevention Practices: Stopping Disputes Before They Happen.”