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Billionaires' battles teach arbitration lessons

Method doesn't always deliver best and cheapest solution to legal disputes

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Business disputes between companies, their executives and owners are as inevitable as Dallas' oppressive August heat. Many companies, wary of courts and juries, contractually mandate that disputes be resolved through "private" arbitration. Recent high-profile battles involving Dallas billionaires Mark Cuban and Harold Simmons and their companies demonstrate that arbitration, long touted as cheaper, faster, confidential and less risky, does not always deliver on these promises.

Lesson One: Arbitration often is not cheaper than a civil court trial. In the deferred compensation dispute between former Mavericks Coach Don Nelson and Mark Cuban's Dallas Mavericks, an arbitrator awarded Nelson $6.3 million in compensation and $800,000 for his attorneys' fees in this two-day arbitration proceeding. Assuming Cuban and the Mavericks matched Nelson's spending on attorneys, the two sides together paid $1.6 million in legal fees on a $6.3 million dispute, or about $1 in fees for every $4 of damages awarded. What's more, those attorneys' fees keep ringing up as the matter works its way through a court system appeal following the arbitration. While both Nelson and Cuban had excellent, high-profile attorneys and the battle was hard-fought, the fees are not unusual for a dispute of this magnitude — even one without a billionaire. More to the point, however, that fee amount is in line with what you could expect through a jury trial.

Lesson Two: Private arbitration is not truly private — and is becoming even less so. Both Dallas and national news outlets recently trumpeted the intimate details of Cuban's the sworn testimony from their arbitration became public with Cuban's court challenge to the arbitrator's decision. Moreover, absent an agreement to keep arbitration papers confidential, any party to an arbitration proceeding may reveal transcripts, as well as arbitrators' written decisions.

Lesson Three: Arbitration is not always fast. Filed in March 2007, the Mavericks/Nelson arbitration was not heard until June 2008. Now, in August 2009, nearly 2½ years later, the matter still has not been resolved. Although the arbitration decision is almost a year old, the Mavericks appealed the court confirmation of the arbitrator's decision, and that appeal is still pending in Texas' 5th Court of Appeals in Dallas.

Lesson Four: Arbitration agreements are not always enforced. While you may think you have agreed in writing with the other side to arbitrate all disputes, a court may decide differently. For example, in July of 2009, a Dallas County jury awarded a group of shareholders $178.7 million against NL Industries Inc., some of its officers and Dallas billionaire Harold Simmons, including $33.7 million in compensation damages and $140 million in punitive damages. Before the trial, the NL parties asked the court to refer this dispute over the shareholders' stock value to a private appraiser, per the shareholders' signed agreement. After the court denied this request, the NL parties asked the court to refer key valuation issues to an arbitrator, as provided in another contract the shareholders relied on but had not signed. The court denied that request as well, and a judge and jury decided the entire these agreements were signed that either an appraiser or an arbitrator would determine any valuation disputes. In fact, courts enforce contractual arbitration provisions in most cases. But there is always the risk that your arbitration provision will not quite fit the dispute or the opponent you are facing, and the court will put you in a bear hug and not let go.

Lesson Five: Choosing arbitration trades one set of risks for another, possibly greater set of risks. An arbitrator or appraiser would not have tagged the NL parties with $140 million in punitive damages. In theory they could. In reality they don't. Arbitration does minimize the risk of a huge punitive damage award. The trade-off is that you are usually stuck with whatever the arbitrator ultimately decides, even if it is demonstrably wrong. Because their case was tried in the civil court system, the NL parties can count on the traditional, fairly broad rights to appeal the jury's verdict. And in Texas, eye-popping jury verdicts often are pared down or overturned altogether by a higher court. But Cuban and the Mavericks' right to appeal the arbitrator's decision for Nelson is extremely limited. Courts cannot adjust an arbitrator's decision except to correct clerical or math errors. And courts cannot overturn an arbitrator's decision unless there is truly egregious conduct within the arbitration process, such as corruption or fraud, evident arbitrator partiality, a refusal to hear evidence or where the arbitrator exceeded his powers. The U.S. Supreme Court recently indicated that not even an arbitrator's "manifest disregard of the law" supports vacating an arbitration decision. Thus, while arbitration usually "works" and minimizes certain risks, taking a case to arbitration is kind of like flying in a single-engine plane. As long as that one engine works for you, everything's OK. But if it fails ... .

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