

The Best Way to Resolve Real Estate and Construction Disputes

Litigation, Arbitration, or Mediation?

By Paul M. Lurie and Stanley Sklar

When was the last time someone involved in a real estate or construction business dispute told you enthusiastically how cost effective the court system was in resolving that dispute? Or that the judge or the jury charged with resolving the dispute fully understood the relevant underlying issues? Chances are you have never heard such praise for traditional litigation-based dispute resolution. But there is hope. For parties to real estate transactions and those involved in construction projects, alternative dispute resolution methods, including binding arbitration and non-binding mediation, offer proven and successful alternatives to an often inefficient and expensive court system. As this article illustrates, alternative dispute resolution requires utilizing trained, experienced, and cost-conscious mediators or arbitrators who are much better at resolving real estate disputes than are the inefficient and often ineffective courts.

Unfortunately, disputes are common among parties to real estate transactions and construction contracts. This article 1) identifies likely subjects of such disputes; 2) describes the disadvantages inherent in utilizing traditional litigation-based dispute resolution; 3) explains many of the myths surrounding mediation and arbitration; and 4) concludes by suggesting that non-binding mediation and/or binding arbitration often ensures that parties have a more efficient and satisfactory outcome.

TYPES OF COMMON REAL ESTATE DISPUTES

Disputes involving construction projects commonly include arguments over responsibility for cost overruns, defective construction, condo owner warranty claims, and delays in project completion. Parties to real estate leases frequently feud over the commencement of rent payments, repair obligations, valuations for rent calculations or purchase options, expense escalation obligations, and common area maintenance charges. Parties to lease and purchase transactions often dispute

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brokerage commission entitlement. All of these disputes have a common thread: The interested parties want and need speedy resolution, at minimum expense, and with the confidence that the outcome will meet the parties' agreed-upon expectations and be in accordance with generally accepted industry standards.

THE PROBLEMS WITH COURTS, JUDGES, AND JURIES

Despite both parties' need for a speedy, efficient, and cost-effective resolution to a real estate dispute, few people can give examples of disputes that the courts have helped resolve in such a manner. More importantly, even fewer can cite instances where court-based dispute resolution reached a result that all parties found to be in accordance with the parties' commercial expectations.

Unlike mediation or arbitration processes, most trials are slow and inefficient. For example, trials involving real estate disputes in Chicago courts can take as long as two to three years from beginning to end. Most businesspeople find the uncertainty that accompanies such delay unacceptable. Moreover, by rule, courts utilize expensive and time-consuming procedures in an attempt to protect litigants from arbitrary decisions by judges and juries and to ensure the efficacy of the adversarial process. These court-mandated procedures include such discovery devices as interrogatories, depositions, restrictions imposed by the rules of evidence, motion practice and, in some cases, use of the appeals process. Finally, most judges and juries do not understand the customs and usages of the real estate and construction industries, thereby severely limiting their ability to adjudicate real estate disputes fairly and efficiently. In fact, most cases never get to use these trial

procedures because so many disputes settle before going to trial, often on the eve of trial. Unfortunately, these late-settling cases are often only resolved after the litigants have incurred significant expenses paying for experts, court reporters, and attorneys' fees. Indeed, some litigants resist settlement, even where it would be in their self-interest to avoid trial, simply because pretrial expenses are so high.

MEDIATION AND ARBITRATION

Modern real estate and construction executives know that mediation and arbitration better meet their need for prompt and efficient dispute resolution. Arbitrators and mediators, selected by the disputing parties for their experience in and knowledge of the relevant industry and trained to resolve disputes fairly and promptly, rarely rely on time-consuming and expensive practices so common in court-based dispute resolution.

The American Arbitration Association ("AAA") is a nonprofit organization that has been providing a forum for commercial dispute resolutions for almost a century. The AAA's National Real Estate Industry Dispute Resolution Council and the National Construction Disputes Resolution Committee, composed of industry representatives, have developed specialized procedures for their industries. At the heart of these procedures are the concepts that neutrals should be experienced and respected in their industry and that neutrals must participate in rigorous training to remain on the AAA panel. These procedures, as well as resumes of AAA mediators, can be found on the AAA Web site at www.adr.org.

It is much more likely that these procedures will be used if they are contained in the pre-dispute transaction documents. This is the reason why mediation and arbitration clauses are contained in many standard form agreements such as those published by the American Institute of Architects, the Associated General Contractors of America, and the Design Build Institute of America. However, disputes can also be submitted to AAA procedures after the dispute has arisen. Under these pro-

cedures, the parties to a dispute attempt to resolve their differences by first using non-binding mediation and then, if unsuccessful, resorting to arbitration. While court judgments are years away, arbitration awards occur much more quickly. That knowledge often is an impetus to a successful mediation.

MISPERCEPTIONS

Although mediation/arbitration is widely used (with high degrees of satisfaction) to resolve many real estate and construction disputes, it is also sometimes avoided due to certain persistent misperceptions. Often these misperceptions are disseminated by those who stand to gain the most and would prefer to use the more costly and inefficient court system. Below we identify and then debunk these misperceptions.

1) "Arbitrators do not adhere to the parties' contracts or the law. Instead, they simply 'split babies.'"

As previously stated, most judges and juries will not understand the complexities and idiosyncratic customs of the real estate or construction matters in dispute, relying instead upon counsel who may or may not succeed in educating them. AAA arbitrators, however, have substantial industry-specific experience, often having served as executives in the relevant real estate or construction industry. They continue to gain knowledge and hone their resolution skills by attending mandated continuing mediation/arbitration education. Further, recent AAA studies refute the misperception that when a party in an arbitration files counterclaims, arbitrators automatically "split the baby" so that both parties are able to walk away with "something."

2) "There is no discovery available in arbitration or mediation."

Mediators and arbitrators are conscious of the need for the parties to obtain information relevant to the prosecution or defense of a claim. However, in their training, these persons learn creative ways of satisfying the needs of the parties without imposing the expense of traditional court-mandated discovery. One reason these costs are usually

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less expensive than their court counterparts is that mediators and arbitrators create a cooperative, rather than an adversarial, paradigm. Nevertheless, where testimony, particularly from third parties not involved in the dispute, is not otherwise available, mediators and arbitrators will frequently allow the disputing parties to engage in depositions. Even then, such depositions are efficiently managed by imposing strict time limits and, where possible, employing remote technologies such as telephone and live video hookups in order avoid travel expenses.

3) “You cannot appeal an arbitration or mediation award if you lose.”

An arbitration award can be set aside on appeal to a court if there is evidence that a party’s fundamental due process rights were violated during the proceedings. For example, certain awards have been overturned when later-uncovered evidence revealed undisclosed and improper relationships between a party and an arbitrator or mediator.

What is different is that arbitration awards are not reviewable on the merits. However, the availability of an expensive appellate review of court judgments is seldom a practical remedy. Higher courts rarely overturn the lower court’s judgments in commercial cases involving expert testimony and complex factual sce-

narios, as are so common in real estate and construction disputes.

4) “We are too far apart and mediation will be a waste of time.”

The fact that the parties are “far apart” does not preclude a successful mediation. The success of mediation is based on the desire of the parties to resolve the dispute on a sound business basis with the assistance of a mediator who helps the parties assess their positions and evaluate their alternatives to a settlement. In the experience of the authors, wide divergence in initial “positions” almost always can be overcome by reality testing. A prime factor in the success of mediation is the direct involvement of party stakeholders in position evaluation. In court procedures, the lawyer usually does this evaluation. The client is seldom exposed to the views of its adversary before trial. That exposure, and the opportunity for catharsis and dialogue, is why mediation settles disputes.

5) “Arbitration is just as costly as a court case.”

A common myth is that arbitration is just as expensive as court litigation. For most of the thousands of cases administered by the AAA, this is not true. There are several reasons for the cost effectiveness of arbitration:

a) Traditional deposition practice does not occur. In pre-hearing conferences, arbitrators encourage agreements among the lawyers that provide for depositions that are limited in number and scope. Arbitrators often act as “discovery masters” available at

any time to resolve discovery disputes that arise. Judges do not have the time flexibility to do that efficiently.

b) The numerous court appearances involved with status calls and scheduling of court motions do not occur. Arbitrators make extensive use of teleconferences to manage the pre-hearing procedures.

c) Arbitration hearings are more quickly concluded. This is because arbitrators encourage hearings on consecutive days — with full days set aside for hearings; and during the arbitration, since the rules of evidence do not literally apply, no time is wasted on evidentiary motions.

d) As mentioned earlier, since arbitration rightly assumes that arbitrators are experienced in construction law and trained in hearing procedures, the need for appellate review of the law or facts decided by the arbitrators is not needed to the same degree it is with courts.

CONCLUSION

We can learn a lesson from Voltaire, who said he had been ruined twice in his life: once when he lost a lawsuit and once when he won a lawsuit. Voltaire would have liked modern mediation and arbitration.



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