Nobody Asked Me, But…. No. 27

Mediation, Arbitration or Litigation?

By Stanley Turkel, MHS, ISHC

Many hotel franchise agreements stipulate arbitration over litigation. At first glance, this may appear to be more beneficial to franchisees but nothing could be further from the truth. Compulsory arbitration protects franchisor interests while diluting franchisee remedies.

What are the disadvantages of arbitration?

First, in court you can obtain a jury trial assuming that you have not waived this right elsewhere in the agreement. Having a dispute resolved by a jury of your peers is a valuable right which should not be underestimated. Arbitrators are usually lawyers who may be friendly with your franchisor or its attorneys since arbitration clauses typically require arbitration to take place in the city where the franchisor's headquarters are located.

Second, arbitration is very expensive, even as compared to litigation. Unlike state and federal courts where judges are compensated by taxpayer dollars, you must pay the arbitrators by the hour (from approximately $250 to 500 per hour), and must pay significant additional filing and administrative fees for the arbitration process.

Third, the discovery process, during which each side gathers its evidence (depositions, documents, etc.) for a trial, is very limited. This aspect hurts a franchisee disproportionately because he or she has the "burden of proof," and usually needs additional facts and documents in possession of the franchisor to build the case.

Fourth, the normal rules of evidence and procedure do not apply in the same way as they would in federal or state court. Instead, the law affords the panel a great deal of flexibility and discretion in conducting the arbitration hearing, and a reviewing federal court will rarely, if ever, reverse the panel's decision – even if it is legally and/or factually incorrect.

The bottom line is – do not agree to arbitration if you can possibly avoid it.
A close cousin of the arbitration clause, the "no jury" clause, requires that the franchisee waive what would otherwise be its right to a trial by jury. Franchise companies believe that jurors may be "sympathetic" to a franchisee who has been mistreated. At the very minimum, the franchisee should be the one to decide whether to have a jury trial. Do not forfeit this option unknowingly when the franchise agreement is signed.

Who are the arbitrators?
Usually, each side selects an arbitrator and then the two arbitrators pick the third one. Arbitrators are usually certified by a Bar Association committee. They are local business people and/or lawyers who have at least two major drawbacks:

1) Since the arbitration usually takes place in the headquarter city of the franchisor, the arbitrators are likely to know the franchisor's attorneys.

2) While the pool of arbitrators may have general business experience, very few have knowledge of the hotel franchise format.

A December 4, 2006 decision by the Ninth Circuit Court of Appeals (Nagrampa v. MailCoups, Inc.) found that an arbitration clause in a franchise agreement was uneforcable under California law. Some observers believe that if the arbitration clause in this case in unenforceable, then no arbitration commitment is safe. This decision calls into question all arbitration clauses. Be sure to have your attorney check it out.

Is there a better way to resolve problems?
Yes there is and it's called mediation. It can solve many business problems quickly, cheaply and on terms acceptable to all sides.

Unlike arbitration, mediation is non-binding. Because the mediator doesn't decide anything, the parties can, if they choose, ignore anything he or she says. A mediator is a go-between who tries to help the parties come to an agreement, not to tell them who is right or wrong. Mediations

usually last one day and either result in agreement between the parties or continuation of the dispute, not an award, decision or judgment. Either party is free to file a lawsuit. Mike Amin, former Chairman of the Asian American Hotel Owners Association said, "Fostering dialogue is a necessity in the pursuit of a healthy system and non-binding mediation between the franchisor and franchisee could be a "win-win" situation. Not only is it a less costly process, but it's also a system that could foster a stronger partnership between the parties rather than the adverserial roles that can come with legal intervention."

F. Peter Phillips, senior vice president of the CPR Institute for Dispute Resolution, says, "Mediation works in almost every case. Of the franchise disputes that have been formally submitted to the National Franchise Mediation Program, more than 80 percent were resolved amicably."

The NFMP has earned the endorsement of the International Franchise Association, the American Association of Franchisees and Dealers, the National Franchise Council and the Asian American Hotel Owners Association.

Here's how mediation works: With CPR's help, the parties decide who the mediator will be, how much the mediator will be paid, when the mediation will take place, how long it will take and other details. Control of the process is a key feature of mediation. Parties can use a mediator listed with the program or pick one of their own choosing who is not affiliated with it.

Disputing parties who decide to use the program split the administrative fee and usually also split the fee of the mediator. In the course of negotiation and mediation, the parties may agree to reallocate the fees.

In actual practice, a mediator will typically meet with both parties separately to get their complaints or points of view and then bring the two parties together to attempt to reach compromise that will result in a solution. A good mediator will listen to both sides of the story and try to discern common threads among the arguments. Mediators are free to devise solutions that a judge or even an arbitrator might not be able to suggest. Judges are bound by legal

precedent and arbitrators by the terms of the arbitration agreement. But mediators have much more latitude.

Ronald K. Gardner, Jr. of Dady & Garner, a well-known Minneapolis law firm, warns that in order for mediation to be successful, the decision makers from both sides have to be present. For the franchisee that's not usually a problem but franchisors do not always send a decision maker to an individual mediation. "You need someone high enough up, that they don't have to make a call to the home office," Gardner said.

You can find out more about this important program by logging on to www.franchisemediation.org.

Quote of the Month

Omar Khayyam, the poet and prophet writing more than 800 years ago said: "In the four parts of the earth, there are many that are able to write learned books, many that are able to lead armies, and many also that are able to govern kingdoms and empires, but few there be that can keep a hotel."

Mark Twain in the appendix to his
A Tramp Abroad written in 1878.

Stanley Turkel, MHS, ISHC operates his hotel consulting office as a sole practitioner specializing in franchising issues, asset management and litigation support services. Turkel's clients are hotel owners and franchisees, investors and lending institutions. Turkel serves on the Board of Advisors at the NYU Tisch Center for Hospitality, Tourism and Sports Management. He is a member of the prestigious International Society of Hospitality Consultants. His provocative articles on various hotel subjects have been published in the Cornell Quarterly, Lodging Hospitality, Hotel Interactive, Hotel Online, AAHOA Lodging Business, Bottomline, New York Times, etc. If you need help with a hotel operations or franchising problem such as encroachment/impact, termination/liquidated damages or litigation support, don't hesitate to call 917-628-8549 or email stanturkel@aol.com.