

Franchise Arbitration: Selected Best Practices

By Peter Silverman, Shumaker, Loop & Kendrick LLP

For thirty-two years, I have been an arbitrator and franchise lawyer. I have seen (and made) many mistakes, some of them repeatedly, and I have seen ways arbitration could be handled better than it is usually done. Based on lessons learned and preferences developed, I would like to share a few thoughts on best practices about drafting the arbitration clause, choosing the arbitrator, and making your case at the hearing.

A. DRAFTING THE ARBITRATION CLAUSE

1. Confidentiality

Under AAA and JAMS rules, non-parties do not have the right to obtain access to the proceedings or pleadings from AAA/JAMS staff or arbitrators, and arbitrators have authority to enter confidentiality orders to govern discovery and admission of evidence at hearings. (AAA Statement of Ethical Principles; AAA Rules 23(a), P(2)(x); JAMS Rule 26(a), (b)). However, parties have no obligation of confidentiality regarding the arbitration. If you want more confidentiality, include that in your clause. The AAA Clause Builder (<https://bit.ly/2DfVAzH>) suggests: “Except as may be required by law, neither a party nor an arbitrator may disclose the existence, content, or results of any arbitration hereunder without the prior consent of both parties.” The exception for legally-mandated disclosures should be used so as to cover the required FDD disclosures. Another confidentiality issue that arises is when, in a later case, a party makes a discovery request for discovery or pleadings in the arbitration. Courts tend to be skeptical of the relevance of such requests, but do not consider themselves bound by the parties’ prior arbitration confidentiality agreement.

2. Who decides?

The law is in flux as to who—an arbitrator or the court—should decide whether a matter is arbitrable. If you want to have the arbitrator decide this, say so in your clause. See, e.g., *Schein, Inc. v. Archer & White Sales, Inc.*, 139 S.Ct. 524, 2019

U.S. LEXIS 566 (2019) (parties to a contract may agree to have an arbitrator decide not only the merits of a particular dispute, but also gateway questions of arbitrability). Here is language I have used: “Any dispute arising out of or in connection with this arbitration provision, including any question regarding its existence, validity, scope, or termination, shall be decided by arbitration.”

3. Speed

If you want to resolve your dispute quickly, specify a time period. For example: “Absent exceptional circumstances or both parties’ agreement, any hearing pursuant to this clause shall be held within six months of the filing of the demand.” Considering that complete cases are routinely prepared for preliminary-injunction hearings and tried in two-three weeks, it is reasonable to specify a six-month deadline for arbitration.

4. Discovery limits

Because different kinds of cases call for different levels of discovery, I think it is a mistake to put specific limits on discovery into your arbitration clause. When you are first entering a franchise agreement, you do not know what kind of dispute, if any, will arise. The best way to make sure that discovery will be proportional to the dispute that actually arises is to choose a good arbitrator. Good arbitrators have the professional judgment to ensure speed and economy while allowing for reasonable discovery tailored to the issues and proportional to what is at stake.

5. Arbitrator qualifications

The AAA has a large, complex case panel that is limited to its most experienced arbitrators. If you want to choose from this panel, state in your clause: “The arbitrator(s) shall be selected from the AAA’s large, complex case panel.” You do not need a similar clause for JAMS because all its arbitrators are full-time and either very experienced arbitrators or retired trial judges.

If you want arbitrators knowledgeable in franchise law, say so in your clause. This is not



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always a great filter, though, as many arbitrators will list franchise experience based on exposure in just a few cases, and the AAA may include anyone listing that experience. But there will be many experienced practitioners on the list as well.

6. One or three arbitrators

One of arbitration's benefits is that you can select an exceptional individual to be your arbitrator instead of being stuck with the judge you arbitrarily draw. You can do your homework on experienced arbitrators to find out their substantive or procedural leanings (including discovery limits), and whether they are open-minded.

I think one arbitrator—like the one judge in a trial court—is usually enough. Still, no matter how much due diligence you do, selecting a single arbitrator means you are relying on one person and there is a chance of getting an opinion significantly outside the bounds of what you reasonably expected. And, unlike court proceedings, there is no meaningful opportunity to overturn an arbitrator's decision.

Having sat on a number of three-arbitrator panels with outstanding colleagues, I have seen how differently top professionals can view the same evidence and arguments.

Three-arbitrator panels reduce the risk of an anomalous decision. The panelists discuss the evidence and their conclusions at length. Where their views differ, they challenge each other. Principled disagreement is the rule, not the exception. The chair frequently seeks to harmonize views to reach a consensus award without a dissent. This results in maverick views being tempered, increasing the likelihood of a reasonably foreseeable award.

The downside to three-arbitrator panels is that they cost more than single-arbitrator arbitrations—by a factor of five in some cases according to the AAA. (See http://go.adr.org/Streamlined_Panel_Option.html). That is because the parties are not only paying three arbitrators, they are paying for the three to confer among themselves and reach consensus on all interim matters and the final award. Three-arbitrator panels also take longer because of the need to accommodate more people's calendars.

If you want the advantages of a three-arbitrator panel without all the costs, consider specifying one arbitrator for cases up to a certain dollar amount, and three arbitrators for an amount over that. And for cases where you do specify three arbitrators, consider some form of the AAA's streamlined three-arbitrator panel procedures. There are several options based on the general principle that pre-hearing matters will be decided by the chair, while the final decision will be made by the full panel. *Id.*

B. CHOOSING THE ARBITRATOR(S)

1. Franchise experience

It is smart to pick an arbitrator with significant franchise experience. There is a good deal of custom and accepted practice in the franchise sector, and with an arbitrator who has significant experience in the field, you do not need a franchising expert to explain that custom and practice. You can, for example, dive right into a case on financial performance representations without explaining the original impetus for franchise legislation, the thinking behind Item 19, or the changing terminology.

For a long time, most arbitrators who were experienced in franchising came from firms that represent only franchisors, and franchisee counsel were concerned that these arbitrators' views reflected their clients' interests. This has changed. A number of franchisee-side lawyers now are on panels. But the biggest change is the growth in the number of lawyers who represent both franchisors and franchisees, a number of whom are on panels as well. Also, the franchise bar is small enough that you can get a good sense of which arbitrators would be scrupulously open-minded regardless of whether they have represented primarily franchisors or franchisees in their practice. Many of the panel members who represent primarily franchisors or franchisees as advocates are fair to both sides as arbitrators.

2. Ask, ask, ask

If you are selecting among arbitrators active in franchising and you do not have personal knowledge about them, e-mail colleagues and ask about the arbitrators. Reach out especially to those in bigger firms; if they have not appeared before a given arbitrator, one of their colleagues may have. If the prospective arbitrators are from

a certain geographical area, e-mail your Forum colleagues in that area for insight.

The AAA offers an enhanced arbitrator selection process for large complex cases that allows pre-screening for conflicts and qualifications, requests for supplemental description of arbitrators' experience, and oral or written interviews of candidates. If you have any concerns regarding potential arbitrators, use these procedures.

If you suspect that some arbitrators may be inclined to side with a franchisor over a franchisee because the franchisor is more likely to hire that arbitrator again, you can investigate. Arbitrators are required to disclose whether they have ruled on a case involving either party or its counsel, but the optional procedures might allow you to ask how many cases they have ruled on between any franchisor and a franchisee. You could also ask for the name of counsel in those cases, and you could then interview the counsel. (Asking for counsel names is not yet an approved process, but I encourage you to ask for it if you want it.)

3. Choosing a wing arbitrator

In clauses that provide for each side's appointing a wing arbitrator, the first step is to determine whether the arbitrator is required to be neutral. (It is rare for a clause to provide for non-neutral wings, and the clause must do so explicitly.) Once you determine that issue, you are entitled to interview prospective wing arbitrators. The scope of the discussion should be governed by Canon III of the Code of Ethics for Arbitrators in Commercial Disputes (ABA 2004). Basically, you can discuss parties, witnesses, counsel, the general nature of the case but not its merits, and selection of the chair. (For further description, see P. Silverman, *Party-Appointed Arbitrators: Ethical Concerns*, *The Franchise Lawyer*, Spring 2014, at 6.)

Look for someone who is open-minded about the position you will be advocating, but who also has the integrity to vote against you. If your evidence and arguments persuade your wing, you want your wing to bring along the other two arbitrators. Wings who lack integrity or are clearly biased on how the law should be applied will have a hard time convincing the other two arbitrators. Along the same

lines, look for a wing who is a decent person and a persuasive advocate. The panel spends a lot of time together discussing the case and exchanging views in writing. Jerks do not fare well in that environment.

4. Your case administrator is your friend

In an administered arbitration, there will be an assigned case administrator. These are very knowledgeable people who also have access to superiors for questions they cannot answer themselves. If you have any questions about the process (even after selection of the arbitrator), call or e-mail the administrator.

C. THE HEARING

1. Speed and economy

For all experienced arbitrators, the watchwords of arbitration have become speed and economy. Arbitrators will welcome parties jointly proposing a case schedule that is swift and economical. If the parties cannot agree on one, and your client wants speed and economy, press for that with the arbitrator. While good arbitrators will want to be fair to both sides, they should be far more favorable to requests for speed and economy than a court would be.

2. You can ask for early views and questions

As part of the focus on speed and economy, the modern trend is that arbitrators should be open to helping the parties resolve the dispute voluntarily. One way to do this is for the parties, at some point, to ask arbitrators to share their initial impressions of the case and the questions on which they are focused.

Arbitrators have traditionally disfavored offering early views, as it is inconsistent with the idea that decision makers should keep an open mind until all the evidence is in. But the reality is that arbitrators have initial impressions, and it may help parties settle if the arbitrators are willing to share these views. Also, even absent settlement, learning the arbitrators' initial views and questions helps the parties focus on the issues that will persuade the arbitrators. And if the arbitrators do not mention an issue that you think is important to your client's case, that may prompt you to put in the work it will take to show the arbitrators that that issue is important.

A more aggressive approach would be to ask the arbitrator to try to mediate the case, and then to serve as the arbitrator if the parties do not reach agreement. (You could also ask this of one member of a three-member panel.) Traditionally, arbitrators disfavored this approach because it requires changing hats and there is a concern that parties will not be forthcoming in mediation if they know the mediator may become the arbitrator. But the modern trend is to be more open to serving in this dual capacity.

3. The CCA Guide is your friend

Much of arbitration procedure is governed by custom, and it is to your advantage to know the generally-accepted customs. The College of Commercial Arbitrator publishes a Guide to Best Practices containing chapters written by highly-regarded College arbitrators. Regardless of whether your arbitrator has been admitted to the College, the Guide is considered a thoughtful discussion of best practices that you can cite persuasively.

4. Presenting the facts

Any fool can present facts in chronological order, using simple declarative sentences, and avoiding adverbs and adjectives. Be a fool. Plus if you prepare a one-page, neutral, easy-to-read chronological time line, you may well see the arbitrators keep it in front of them every day of the hearing.

5. Third-party subpoenas

Compelling third parties to testify is difficult and takes time, and the requirements differ by Circuit. If you expect to need documents or testimony from an uncooperative witness, request your subpoenas right away so you have time to seek court assistance to compel the testimony or documents.

6. Deposition testimony

Generally, there should be no reason to read deposition testimony in an arbitration hearing unless there is part of the transcript that is essential to your case. Instead, consider asking the arbitrators if you can give a short summary at the point in the hearing when you would otherwise submit the transcript to be read or viewed. You would say something like: "This is where Jones' deposition testimony becomes pertinent, and we've submitted it for you to read. Jones worked for the franchisor, but is with a new

employer now. He provides the detail on how the franchisor calculated its Item 19 by cherry-picking the pool of franchisees from which it derived its averages."

Along similar lines, if you have a number of live witnesses, you may want to work out with the arbitrators that before you start questioning a witness, you can give a short summary of the witness's expected testimony and how it fits into the case.

7. Damages

Proving damages in a court case is difficult, in part, because of the evidentiary burdens related to the data on which the damages witness is relying. Because arbitration is usually not governed by the rules of evidence, it is much easier to admit and use the underlying data in arbitration.

Do not take this too far, however. Arbitrators still need to know the underlying data and be comfortable that it is reliable. The data you give them should be stipulated to. Make sure it is easily accessible and organized because arbitrators often need to go back through it independently to see how it aligns with their ruling on the substantive legal issues.

Do not limit your damages case to the result that should follow if the arbitrators find for you on all your claims and disputed factual issues. Give the arbitrators guidance on how damages would differ if they do not accept every part of your case. If the evidence is strong enough, you can ask the panel to trim your damages request based on rough justice, but offer the panel plenty of data and guidance so they are not speculating.

8. Ask for post-hearing guidance on important facts and issues

Ask your arbitrators to give you guidance for closing argument or post-hearing briefing on the factual and legal issues they are focused on. Urge them to be as specific as they can be. This allows you to focus on what will be most persuasive in winning your case or highlighting something that the arbitrators hadn't yet deemed important.

9. Criticizing opposing counsel

Don't. Stick to the issues. Personal criticism usually turns into a WWE wrestling match, and arbitrators do not want to referee attorney brawls.

The only exception is if the behavior is so egregious as to call for severe sanctions. Beware, though, if you call for severe sanctions and do not have strong, near-uncontestable support, you will strongly weaken your credibility.

10. Rules of evidence

The common practice in arbitration is not to apply the rules of evidence unless the arbitration clause requires it. But do not assume that will be the practice at the hearing. AAA rule 34(a) provides that “[c]onformity to legal rules of evidence shall not be necessary.” So ask arbitrators how they will handle evidentiary objections at the hearing. And, if you want the arbitrators to apply the rules, try to persuade them to do so.

If the arbitrators will not apply the rules, save your objections for matters that should be excluded based on general notions of justice. Arbitrators are reluctant to exclude evidence because one ground for vacating an award is that

the arbitrators were “guilty of misconduct... in refusing to hear evidence pertinent and material to the controversy.” Thus prudent arbitrators may simply accept the evidence for what it’s worth. Nonetheless, raising the objection will give you the chance to make your point as to why the evidence should be disregarded.

Two last comments: First, arbitration clauses in franchise agreements may be up to twenty years old and outdated. Or, regardless of when the clause was drafted, it may not provide for the best procedure suited to your dispute. If that is the case, ask your opposing counsel to consider changing the procedure.

Second, and the best suggestion I have to offer, if you are new to arbitration or even if you are experienced and have questions or concerns, reach out to other Forum members. This is an incredible group of lawyers who regularly offer help to others—you just need to ask. ■

