ARBITRATE, DON'T SURRENDER!

Just about all the commercial contracts you sign have an arbitration clause. Where an arbitration clause resides in your contract, one or both parties may be prohibited from filing a lawsuit in the state of federal courts until the arbitration is completed. Or litigation may be prohibited completely, at any time.

The arbitration clause was once heralded as a means to limit legal fees and the cost of resolving disputes for all parties to a contract. It was intended to streamline dispute resolution and put economically weaker parties on relatively equal footing with their deeper pocketed opponents. But the arbitration clause often operates to impose added cost and expense on the economically weaker party, only, by layering an additional stage of dispute resolution.

At worst, one party to your deal will insert a totally one-sided arbitration clause that severely limits your rights and remedies to arbitration, only, while leaving the more powerful party to choose court over arbitration. Imagine agreeing to play tennis against a stronger opponent, but only after conceding that your opponent is the only one permitted to appeal the line judge's decision on your serves and points. The one sided arbitration clause is just as bad. On February 26, 2013, the United States Court of Appeals for the Fourth Circuit applied Maryland contract law to strike down just such a one-sided arbitration clause.

Noohi v. Toll Brothers involved a homebuyer's lawsuit against the homebuilder, and the homebuilder's attempt to throttle the lawsuit by asserting a very one-sided arbitration clause. Mr. and Mrs. Noohi had plunked down $77,000 as a down payment toward a house, to be built by Toll Brothers. But when the financing did not come through, they canceled the contract and requested return of their deposit. Toll Brothers kept the money, and the Noohis sued.

Toll Brothers filed a motion in court to stop the case, and for an order forcing the homebuyers into binding arbitration. The arbitration clause was boilerplate that required the homebuyers to arbitrate any and all disputes with Toll Brothers. The same arbitration clause granted Toll Brothers the freedom to bring it's disputes against the

homebuyer directly to court or to arbitration, at Toll Brothers' sole election. Judge Richard Bennett denied the motion to force arbitration on the economically weaker homebuyers, declaring that the arbitration clause was "quite simply one-sided and onerous."

The appellate court agreed with Judge Bennett, while applying Maryland's law of contracts. Quite simply, a legal and enforceable arbitration clause requires "mutuality of consideration." That means that both sides must give something in exchange for the other side's promises to arbitrate. And most importantly, the court acknowledged and accepted Maryland's requirement that an arbitration clause operates like a contract-within-a-contract. It must be supported by its own consideration, independent of the consideration for the overall contract.

A good example of this is the employment contract that requires an employee to accept the arbitration policy of the employer, while the employer retains sole discretion to make unilateral changes to that policy after the employee starts working. In this example, the exchange of consideration for employment is illusory. The employee cannot count on the arbitration policy to stay the same even for one minute after starting on the job. The employer has surrendered nothing to the employee, and has not agreed to maintain one certain policy of arbitration. In this example, the exchange of promises that create the overall employer/employee relationship are not consideration for the contract to arbitrate placed within the employment contract.

What's this mean for you and your business? **Don't immediately accept that the arbitration clause in your contract is enforceable against you to limit your remedies against the other side for breach.** When a dispute arises, the deal must be examined to determine whether there is mutuality of consideration for the arbitration clause, as if it stands alone, separate and apart from the contract in which it is buried.

Consider this an equalizer for the party with not-so-deep pockets. After all, you signed a contract, not an instrument of surrender.