Kluwer Arbitration Blog

Respondents Play with Advance on Costs as a Strategy: Do Claimants as Well?

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Earlier I discussed a possible response to a Respondent's tactical approach to refuse to pay an advance on costs, referring to a previous article I published. This post invited a reaction from readers which I thought worth noting: What do you do when you represent the Respondent who simply cannot afford the fees? I would argue that this is typically not a concern as Respondents may be very happy for the proceedings to simply stop; however, some Respondents, although the financial underdogs, may feel they have both legitimate defenses and even valid counterclaims. Below I discuss a recent case and ask some questions about possible motivations. In this post, I hope to invoke some responses and insights from readers on this issue.

It may be that the current economic crisis is leading to new situations – Claimants avoiding multiple actions by refusing to pay costs themselves and Respondents basically going into bankruptcy trying to both defend themselves and assert valid counterclaims.

On November 19, 2009, the US Fifth Circuit Court of Appeal issued a ruling on a Respondent's obligation to pay the arbitral costs. In this particular case, Dealer Computer Services Inc. ("DCS") v. Old Colony Motors, Inc (No. 09-20049), the parties were involved in arbitral proceedings under the auspices of the AAA Commercial Arbitration Rules. As I understand it, they were to the point of the final oral hearing, and, thus, presumably the parties had expended a chunk of the money to cover the AAA fees and associated expenses ("deposit"). However, likely a result of the economic crisis, the Respondent Old Colony Motors ran out of money and was on the verge of bankruptcy. The arbitrators ordered DCS to cover the remaining fees, but it refused to do so, looking instead to the local trial court to force Old Colony Motors to cover its portion of the deposit. On appeal, however, the Fifth Circuit Court of Appeal held that the decision on who paid what with respect to the arbitration rested with the arbitrators.

Although this case may not present anything new, it is interesting that DCS continued to refuse to cover the deposit on Old Colony Motors' behalf. It argued that it had paid its portion, which sufficiently covered the fees necessary to hear its claims. The problem was that Old Colony Motors had a counterclaim against DCS. In my previous blog post, the situation was considered from the perspective of the Claimant seeking to pursue the agreed upon proceedings when a Respondent, for tactical reasons, refuses to cover its portion of the costs. What about the Respondent's perspective? What if the Respondent feels that it has valid defenses and strong counterclaim(s) against the Claimant? In other words, it has its own motivation to continue with the proceedings but fees and arbitrator's expenses prohibit it from doing so? Are there any tactics a Respondent may employ to

ensure continuation of the arbitral proceedings?

In DCS v. Old Colony Motors, mentioned above, DCS was in the business of providing computer systems to car dealerships worldwide and part of the sales agreement involved an on-going purchase arrangement of regular system updates. Old Colony Motors was one of its customers, but at some point in the business relationship, DCS claimed that Old Colony Motors had breached their agreement. It is not difficult to imagine that in light of the current economic climate and the sever hit the automobile industry took as a result, that these parties, particularly the small dealership, were in financial distress. It may have been for this reason that Old Colony Motors simply could not pay its portion of the fees.

What I ask readers of this blog is: what are some options for the Respondent? One possibility is to consider asking the arbitral tribunal to issue an interim award which orders the Claimant to pay the entire deposit (of course, some substantive argument is necessary there) and then take this interim award before the court with jurisdiction and seek enforcement. Of course, the problem with this approach, amongst other reasons, is that it costs more money.

My next question is, particularly in light of this economic crisis – is arbitration, especially through a possibly expensive arbitral institute, truly cost effective? In addition, is it difficult to get an unbiased award from arbitrators when it directly involves their fees? What about those Claimants who have several arbitrations going or are at least frequently before the same arbitral institute, and, thus, the arbitral institute receives a lot of business from the party? Normally, with respect to the final question, I wouldn't assume it matters, but what about when the arbitral institute has a rule which states it will consider lowering fees when a party is experiencing severe hardship? Do they ever do so?

These are certainly issues which may more frequently arise when representing parties during these economically trying times.

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