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ARBITRATION IN INSURANCE COVERAGE DISPUTES: PLUSES AND MINUSES

By Peter A. Halprin

Deciding whether to proceed with arbitration, either after the denial of a claim or when procuring the placement of a policy, requires an understanding of arbitration and its advantages and disadvantages. This article analyzes the perceived advantages and disadvantages of arbitration.

Policyholders may be surprised to find that their insurance policies contain an arbitration provision. Deciding whether to proceed with arbitration, either after the denial of a claim or when procuring the placement of a policy, requires an understanding of the advantages and disadvantages of arbitration.

The Perceived Advantages of Arbitration

Although there are many definitions, arbitration has best been described as:

A process by which parties consensually submit a dispute to a non-governmental decision-maker, selected by or for the parties, to render a binding decision resolving a dispute in accordance with neutral, adjudicatory procedures affording each party an opportunity to present its case.¹

Broadly stated, there are a number of perceived advantages to arbitration over litigation, which include finality, enforceability, party autonomy and procedural flexibility, and neutrality.

Finality

Finality refers to the general absence of extensive judicial review of arbitral awards. As a general rule, the decisions of arbitrators are final and binding. The benefit of limited appellate review is a reduction in litigation costs and delays.

Enforceability

This is particularly valuable in the context of international arbitration as it is generally easier to enforce foreign arbitral awards than foreign court judgments. This is due, in large part, to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, which provides for mutual recognition and enforcement of arbitral awards by contracting states, and limits the defenses that may be raised in opposition to the confirmation of an award, the goal being to eliminate litigation following an arbitration.

Party Autonomy and Procedural Flexibility

Arbitration facilitates party autonomy in that it allows parties broad freedom to agree on the laws, procedures and rules applicable to their disputes.

Neutrality

Party autonomy is understood to open a space for neutrality of venue. In arbitration, the parties can potentially avoid concerns about the potential biases associated with going to court in the home jurisdiction of the other party.

Additional perceived advantages of arbitration include the confidentiality of the procedure (depending on the jurisdiction and stage of the proceedings), the reduction of forum shopping and parallel lawsuits, maintenance of the parties' business relationship, and cost and speed.

The Perceived Disadvantages of Arbitration

The perceived disadvantages of arbitration represent the flipside of the advantages. Finality and enforceability can limit a party's recourse in the event of an unfair decision. Party autonomy and flexibility, as well as neutrality, may result in a lack of legal protections, which typically hurts the weaker party (which lacked the bargaining power to select the procedure applicable to the dispute when negotiating the agreement). Confidential proceedings limit a party's ability to obtain precedent from a favorable ruling and to use statements made in the arbitration against a party at a later date. As to cost and speed, these advantages may be limited in complex proceedings.

The disadvantages can be particularly pronounced for policyholders² In particular, arbitration clauses in insurance policies are often drafted to benefit the insurance company.³ For example, some arbitration provisions in insurance policies eliminate *contra proferentum*, the principle that language deemed ambiguous should be construed against the drafter (generally the insurance company) and in favor of the policyholder.

Negotiating Arbitration Provisions

If policyholders prefer arbitration, or are unable to avoid it, they can take advantage of the perceived benefits. For example, if an arbitration clause permits the policyholder to select an arbitrator, the policyholder can get the benefits associated with the selection of a neutral party with subject matter expertise. This means that the outcome will be decided, at least in part, by someone with dispute-specific expertise, something that is not guaranteed in court.

As a result of the disadvantages described above, some policyholders find it prudent to avoid arbitration entirely. This is best achieved through the purchase of insurance that does not contain an arbitration clause. Waiting to challenge a clause until after a dispute arises is difficult, as courts favor arbitration and often look for ways to enforce such agreements.

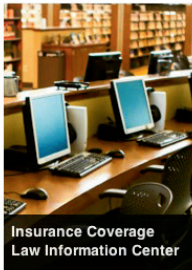
Endnotes

1. Gary B. Born, *International Arbitration: Law and Practice*, at 4.
2. See, "Arbitration of Insurance Coverage Disputes: A Policyholder's Definitive Survival Guide," *The John Liner Review* (Fall 2010).
3. See, "Arbitration Clauses Can Make Dispute Resolution Arbitrary," *The Metropolitan Corporate Counsel* (July/August 2014).

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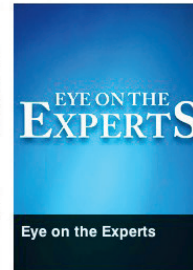
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