Alternative Dispute Resolution in the Hospitality Industry

Outline

Because of the significant and rising costs involved in civil litigation, many business organizations are increasingly turning to Alternative Dispute Resolution (ADR) as the preferred way of settling conflicts that arise either from contractual agreements or in operations. ADR has become popular because of its focus on fair and reasonable outcomes that are arrived at expeditiously, at less cost than through litigation and in a more cordial, less confrontational atmosphere. And while hospitality may have been slower to embrace the concept than other industries, it is now becoming time to bring this important process to bear on the growing burden of litigation on the industry.

Introduction

Effective risk management calls for the resolution of issues before they become full-fledged disputes. The authors encourage organizations with stakes in the hospitality sector to use ADR. An ADR plan that provides for issue review, mediation and arbitration brings not only financial and economic benefits but also intangible ones, including the preservation and improvement of important business relationships. Best practice legal departments in well-managed business organizations understand the economic and non-economic benefits of effective conflict management through ADR.

In order to benefit from an ADR plan, organizations need to agree upon the forum, the procedures to be used and the so-called "providers" who will administer the process before entering into contracts. But even if such a plan is not memorialized in a contract, this should not prevent parties in a relationship from agreeing to a defined ADR process in order to resolve a dispute.

Alternative approaches to ADR may be viewed from the perspective of the increasing use of time and commitment to the outcome, from the pre-emptive (Issue Review Boards), to the facilitated (Mediation) and on to the final and binding (Arbitration). There are thus three principal approaches to ADR:

The Issue Review Board™ – an informal forum that recommends non-binding solutions to issues before they become disputes;

Mediation – a facilitative or evaluative process to resolve disputes with agreement reached by the parties and enforceable through arbitration or litigation; and

Arbitration – the final, binding and enforceable resolution of disputes (although occasionally arbitration may be defined as non-binding, with the prior agreement of the parties).

The Value of Industry Experts in Hospitality ADR

With the increasing popularity of ADR in all areas of business, it was inevitable that the hospitality industry would take note of its advantages. With the escalating costs associated with litigation, organizations involved in the hospitality sector are increasingly recognizing that disputes that arise between parties may be reasonably, fairly and economically resolved through ADR. Hotel management and franchise agreements, for example, have frequently included arbitration and mediation provisions, but they generally have referred to standard rules and used third-party providers with little background in the industry.

Arbitrators and mediators have thus been brought into hospitality dispute resolution with little understanding of the history and dynamics of the sector. And while neutrality has generally been assured, there has been frustration associated with the frequent lack of understanding of the issues involved on the part of the key players in the process – the arbitrators and mediators.

Recognizing this reality, the International Society of Hospitality Consultants (ISHC) has responded to serve this important need by facilitating customized dispute resolution training programs to industry experts. This exercise has resulted in a panel of highly experienced and qualified arbitrators and mediators with extensive experience in dealing with hospitality industry issues – the best of both worlds.

Thus, the industry now has a supply of industry experts, the vast majority of them being current or former ISHC members with 10 to 40 years of industry experience – who have been trained and certified as commercial arbitrators, mediators and Issue Review Board members, and who are ready to support the resolution of disputes, from the simplest to the most complex.

A wide variety of complex business and real estate disputes in the hospitality industry are now arbitrated, ranging from the parties' respective rights and obligations under management contracts and franchise agreements to disputes concerning capital improvements, annual budgets and the calculation of incentive and other fees, to disputes concerning allocation of chain-wide costs, and even the composition of competitive sets.

ADR Providers

A "provider" organization is usually needed to administer the dispute resolution process, such as a hearing. There are numerous providers of these services, including organizations such as the American Arbitration Association (AAA), JAMS, the International Chamber of Commerce (ICC), and the Institute of Conflict Management (ICM), which has provided the training and certification of ISHC panel members to date. While ICM is currently the ISHC's preferred vendor relationship for the provision of support services in ADR, all panel members are prepared to serve with any provider in the ADR field where the circumstances dictate or are appropriate. Some existing contractual agreements within the hospitality industry, for example, provide for the application of AAA or JAMS rules, under which all panel members would serve. It is

important to note, however, that the parties involved can agree to use any provider organization to resolve a dispute, even if it is not named in the original contract.

Neutrality and Experience

Regardless of the provider, it is critical to the resolution of the disputes that the "neutrals", those individuals empowered to resolve the disputes, possess both impartiality and industry experience. The clear advantage of using members of ISHC's ADR Panel is to bring not only neutrality and independence to the process, but to ensure that industry experience and understanding is applied when reviewing facts, analysis and testimony, and in arriving at findings and conclusions, solutions and awards. ISHC members are professionals who abide by strict professional standards of independence that have been well established and recognized by the hospitality industry for many years. It is thus their independence, industry knowledge and professional expertise that is brought to the ADR process and makes an ISHC solution to ADR so desirable.

One of the primary advantages of the ISHC is that its members bring vast experience covering all areas of the hospitality sector, ranging from the technical (architecture, engineering, construction, appraisal, and real estate development) to marketing, operational, financial and economic areas, to the strategic, organizational, people, process, technology, capital and real estate property markets. The ISHC is the single most comprehensive organization to find experts to resolve disputes in the many disciplines of the hospitality industry.

Arbitration

Arbitration is a well-established form of dispute resolution that provides the parties with a final and legally binding decision. The decision is enforceable by a court of law typically after only a very limited review and may not be appealed except under very limited circumstances. Occasionally, the parties may agree to a non-binding arbitration, but this is the exception rather than the rule.

For years arbitration was viewed as an effective alternative to litigation and trial through the court system only in certain types of disputes, such as construction and design, labor and employment, disagreements over the purchase and sale of residential real property, consumer stock brokerage, and medical care. Early on, arbitration was pushed primarily by certain industries, such as stock brokers, architects, construction professionals, labor unions and hospitals, who perceived arbitration as an effective alternative to trial for a variety of reasons: they had a large number of lawsuits largely involving repetitive, cookie-cutter issues; they wanted to achieve some uniformity of result; they wanted confidentiality to the extent possible; and they wanted their disputes to be "tried" by an arbitrator with industry savvy, if not industry expertise.

These industries recognized early on that the risks they were hoping to avoid could be contained more effectively in an environment in which disputes could be aired with greater confidentiality and speed than was possible in the court system. Additionally, due

to the repetitive nature of the disputes facing those industries, they found that certain economies and greater predictability could be achieved by trying their disputes to an arbitrator knowledgeable in their particular industry. They also found that the arbitration environment allowed their disputes to be tailored and customized in a way that the one-size-fits-all environment of the court system would not allow.

Despite the demonstrable benefits of arbitration to address industry-specific disputes, it took years for arbitration to catch on as a legitimate alternative to court litigation in business and real estate disputes of any complexity. First, the lawyers had to become convinced of the efficacy of arbitration so that they would recommend it to their clients, both at the transactional stage and at the post-dispute stage. For years there was a predominant chauvinism that a jury of "twelve in a box" was the universally superior method of dispute resolution. This continues to be true in disputes where punitive damages are possible, or where one party's best hope of winning lies in fanning the flames of emotion and passion. Over the course of time, however, most lawyers have gained enough experience in arbitration to learn that with the right arbitrator and efficient rules, their clients are at least as satisfied with arbitration when efficiency, costs, and speed are factored in with the ultimate judgment.

Most commercial arbitration is provided for in a contract where the parties have agreed that if they do have a dispute, rather than pursuing their remedies within the public court system, they will have it resolved in a less formal, private way. And most arbitrations are indeed private – the deliberations, materials used and testimony of experts and advocates are retained on a strictly confidential basis. Arbitration language in a contract may provide for conditions when the arbitration can be initiated, and set limitations, in terms of time, amount of discovery, etc. Others may call for arbitration to be preceded by preliminary steps, such as good faith negotiation or mediation.

In the absence of contractual language, the parties to a dispute may nevertheless jointly initiate the process by executing an arbitration agreement that will define the rules and procedures and may deal with other details such as the provider, discovery process, etc.

The arbitrator is chosen by the parties to the contract and is viewed as being neutral and independent. In some instances, a panel of the three arbitrators will be called for in the agreement, whereby one party selects one arbitrator, the other party selects a second, and the two "party-appointed" arbitrators go on to select a third "neutral". The parties in more complex matters generally use attorneys, but in more simple arbitrations may represent themselves. Unlike litigation, the rules of evidence in arbitration proceedings are not restrictive, and the arbitrators have great flexibility as to what evidence to consider.

The arbitrator will rule on discovery requests and disputes, read briefs submitted by the parties, review documentary evidence, hear testimony during a hearing, and finally render an opinion on liability and damages, as appropriate. This opinion will be rendered as an "award" after the hearing has been completed, and may be presented with or without the reasoning that supports it. The award may then be confirmed by a court in the appropriate jurisdiction and subsequently entered as a judgment, thus becoming legally binding on

the parties involved.

The Federal Arbitration Act, read in conjunction with state arbitration law (where such exists), generally governs the arbitration process. The arbitration provided for in a contract may limit the types of issues to be resolved, the scope of the relief and a number of the procedures to be used.

If arbitration is provided for in a contractual agreement, the rules to be applied are generally defined in the contract as those of a selected provider of arbitration services. Parties to the arbitration will generally have varying needs for information, which is produced through a process of "discovery". This process can range from the informal exchange of information in smaller, less complicated cases, to a highly formalized discovery process in larger or more complex cases.

Where the parties have retained experts who in turn undertake investigations and have a need for information and access to people, the process of discovery can become extensive and costly. In order to mitigate the costs, some parties will agree to an abbreviated schedule of depositions of key experts and fact witnesses, with rights reserved to continue discovery if a settlement is not reached early in the process. Agreements of this type may be difficult for the parties to agree to, in which event the process can be mediated by the neutral. There is also a need to consider the appropriate balance between the cost of discovery to the respective parties and the benefits of more complete information.

Occasionally, where the parties have agreed, there may be a provision for a particular form of arbitration. Alternative forms include bracketed, baseball and night baseball arbitration. In "bracketed arbitration", the damage awards are limited within a pre-defined range, where both a floor and a ceiling are agreed upon. In this manner, awards that are higher than the maximum are reduced to the ceiling and conversely those that are lower than the floor, are increased. In "baseball arbitration" (also known as "final offer arbitration"), the arbitrator must select one of two possible damage awards presented respectively by the two parties. In "night baseball arbitration", the concept is the same, except that the figures are not revealed to the arbitrator. In this latter instance, the parties agree to accept the high or low figure closest to that of the arbitrator's.

The parties to hospitality disputes often want to keep their dispute confidential from hotel employees, lenders and other third parties who may perceive themselves to be affected by the dispute, but whose involvement is not necessary to (or in fact would be counterproductive to) its resolution.

Arbitration provides a much greater potential for confidentiality than court proceedings. First, the parties can agree that their proceedings will be kept confidential, and all arbitration provider organizations will respect that request. Second, in an arbitration environment, all of the pleadings and other written papers filed in connection with the arbitration, and also all testimony given at hearings, can be provided under the cloak of confidentiality. Contrast that with a court proceeding in which one must first attempt to seal the file during litigation (a task which is not easy and which many courts will not

grant except only on an extraordinary showing of need). Even if one can successfully seal a court file, it is virtually impossible to keep the actual hearings and trial confidential except only in very unusual circumstances such as extraordinarily high profile criminal trials – which one can only hope will not involve the hotel industry!

Arbitration by the Rules

The rules for arbitration that are promulgated by those organizations that provide arbitration services generally cover much of the same ground, including the following:

The jurisdiction and authority of the provider;
the scope and application of its rules and their amendment;
the fees for administering the process;
the limitations of liability;
the application of waivers;
the alternative forms of arbitration;
the agreement of the parties;
the initiation of arbitration, filing of a claim, and amending the claim;
communications;
confidentiality;
qualifying and appointing the arbitrator or panel of arbitrators;
representation of the parties by attorneys;
preliminary conferences;
disclosure;
the exchange of information and discovery process;
the scheduling, noticing and conduct of the hearing;
the discontinuance and postponement of proceedings;
notices and oaths;
pre-hearing submissions;
evidence;
witnesses;
post-hearing filings; and
the scope, form and delivery of the final award.

The rules of all major ADR provider organizations were drafted to accomplish the objectives outlined above: flexibility, selection of the best arbitrator or arbitrators for a particular dispute, confidentiality, expedited resolution and other efficiencies. At least one provider organization's rules are so loose in an effort to provide the parties with this flexibility that they say little more than that the parties are encouraged to fashion their own hearing rules, tailored to the unique needs of their individual cases. Most organizations, however, have a set of structured rules that can be found on each provider organization's web site. Despite this lack of uniformity, most provider organization's rules cover at least the following topics:

Rules to Select the Arbitrator or Arbitrators

It is critical to the integrity of the ADR process that the arbitrator be neutral, which means he or she must not have any financial relationship with any of the parties or counsel, must not have any social relationship with any of the parties or counsel that is not disclosed to and waived by all parties, and must not have any biases or prejudices toward any party, any counsel, or concerning any issue that will be presented at the arbitration. As an example, if an arbitrator has for 30 years represented only labor unions and has written extensively about the inherent correctness of labor unions' positions and the inherent fallacy of managements' positions, it is hard to see how such a person could possibly be a non-partisan neutral in an arbitration concerning employment issues affecting an individual or a class of hotel workers.

The rules of all major provider organizations provide a mechanism by which such prejudices can be revealed and vetted, and they also provide the parties with the ability to challenge arbitrators and to strike them. The rules to challenge and strike an arbitrator are significantly looser than is the challenge process in court litigation. It is much easier to strike potential arbitrators than it is to strike potential judges.

While these rules may have been drafted primarily to ensure the integrity of the ADR process and the impartiality of arbitrators, they also make it easier for parties in industry disputes to select an arbitrator with industry expertise. As mentioned above, there is no promise (and often no hope) that the parties to civil court litigation will be assigned a trial judge with any industry expertise. Do the parties to a complicated management contract dispute really want their judge's sole experience in the hospitality industry to be as a consumer while on business or vacation?

Rules Designed to Focus And Narrow the Issues and to Restrict Discovery

The procedural codes of many states provide that in arbitration there is little or no discovery allowed, unless the parties' contract or the ADR provider organization's rules allow for discovery, in which case discovery will be limited in accordance with such rules or contract provisions. The radical curtailment or elimination of discovery is probably acceptable in cookie-cutter disputes such as most construction and employment matters, or matters involving guest dissatisfaction.

The more complex the dispute, however, the greater the need for discovery. This is especially true because in many disputes the documents and witnesses are largely controlled by one side, and thus a no-discovery rule puts the other party at a significant comparative disadvantage. That is not to say, however, that the almost limitless discovery allowed in civil court litigation is necessary or appropriate for the vast majority of disputes, and certainly for most disputes affecting the hospitality industry. The rules of most ADR provider organizations attempt to reconcile the need for discovery in complex disputes to the goals of speed and efficiency.

Rules to Administer the Dispute

Most ADR provider rules contain procedures for the things that in the court process

would take place between filing the complaint and the trial. Other than discovery, these matters include rules for: compelling attendance of witnesses; service of briefs and other papers; presentation of motions and other hearings; and such things as cost allocation, location, changes to claims and counter-claims, replacement of an arbitrator, representation by counsel, and ex parte (one-sided) communication with the ADR neutral.

Although the rules of various ADR providers are by no means uniform on these matters, they all have the goal of providing the parties and their counsel with predictable guidelines to make the process fair, fast and economical.

Rules to Conduct the Arbitration Trial and Post-Trial Matters

The provider rules also cover what can (or must) take place at the arbitration trial. In many jurisdictions, there is no right to appeal an arbitrator's award, or the right to appeal is limited. Nevertheless, some ADR providers' rules set forth how a party may seek clarification of an award, or even challenge the award in the context of the arbitration, prior to any challenge a party might attempt through the courts after the arbitrator issues the award.

After the trial, the arbitrator (or panel of arbitrators) will issue a written award. Many of the ADR providers' rules set forth detailed procedures and time requirements that the arbitrator must follow in respect to the award. The arbitrator's issuance of the final award typically marks the end of the arbitration.

Case Studies for Arbitration

1. Every time the owner of a resort asked for information, the operator forced the requested info to pass through their attorneys before being released to the owner. As performance declined, the owner lost trust in his operator, whom he thought was hiding something. As the market slumped, this situation deteriorated to the point where the owner filed a demand for arbitration, seeking to void the management agreement based on breach of fiduciary duties.

The case went to a panel of three arbitrators, all of whom had experience in the industry. The three panelists had skills in the disciplines of hotel operations, law and finance. A two-day hearing was held, evidence was submitted and reviewed, and the panel was able to distill the various claims down to the real problem, which was a dysfunctional relationship that stemmed from the owner's lack of fair access to books and records. As part of the Order, the arbitrators wrote a procedure for such access (which prevented the requested data from passing through the operator's attorneys before reaching the owner). The Order also created an Issue Review Board™, whose chair was empowered to sit on the hotel's Executive Board, and act as a liaison between the owner and the operator on future issues, resolving them before they grew into full-fledged disputes.

2. Another hospitality industry veteran was asked to arbitrate a dispute between a ground

lessor and his lessee, who was obligated to develop a mixed-use resort (hotel, golf and residential) on the lessor's property. The economics of building a luxury hotel, however, were not favorable, so the lessor proceeded to build the residential and golf components first. The lessor sued to force the lessee into building the hotel as well, claiming breach of contract, even though the contract was quite vague as to phasing and timing of the components of development.

The arbitrator held a hearing, reviewed the contract, and was able to run an economic and financial feasibility model to illustrate to both parties that the economics of the resort development would allow the hotel to be built, but only after the homes were sold and the golf course was stabilized. He was able to set up a schedule that both parties could agree to for the entire resort to be developed, in a manner that would optimize the return to the lessee, and still achieve the ultimate build-out desired by the lessor.

Mediation

Like arbitration, mediation is conducted in private, but involves a neutral who assists the parties to a dispute in reaching their own settlement. While mediation is mostly a voluntary process, it can be mandated by a court of law, or provided for in a written contract between the parties. It is a relatively straightforward process where the parties may represent themselves or use advocates. In mediation, the dispute may involve two or more parties. The neutral may either facilitate the process of the parties reaching their agreement, or be called upon to evaluate the arguments and evidence, and advise on a resolution.

A skilled mediator, while not having authority to impose a settlement, may have an important impact on the outcome by setting the ground rules, the ways in which the parties understand and analyze their respective positions, and the demeanor and dynamic of the process. The mediator's task is to improve communication between the parties, ensuring that there is an effective exchange of information, and then assist in the development of alternative solutions. The mediator's evolving understanding of the parties' respective interests is also helpful in placing focus on the issues at hand.

As the mediation process progresses, the mediator should be attempting to determine the level of resolution that parties will be willing to jointly accept. This may range from the simple halting of animosity between the parties, through a resolution of the underlying basis for the dispute, and on to a repair and reconciliation of the relationship. The end result may fall anywhere along this spectrum, and may nevertheless constitute success, from the perspective of the parties themselves.

The process typically involves the mediator convening the parties, meeting separately with each side and listening carefully to their stories. This enables the identification and ranking of the key issues, shuttling between the parties, maintaining confidences when called for, facilitating a solution, and bringing the mediation to closure, preferably with a written agreement prepared and executed by the parties. It is important to have individuals representing the parties actually in attendance at the mediation, or supported

by those available by phone, who have authority to negotiate and to execute a settlement agreement.

Mediation as a process is less formal than arbitration, has no rules of evidence, and has little structure in terms of how the facts and positions are presented. Mediation can be designed in whichever way appears appropriate to the parties and to their mediator, with a view to moving the process forward, while producing the optimum exchange of facts, opinions and interests that will support negotiation and resolution.

The challenge for the mediator is to avoid becoming evaluative when the role calls for mere facilitation. The time for evaluation is when the mediator is asked to provide it by the parties and when such assistance is needed. It is more frequently used in larger, more complex matters, where the gap between the parties is very wide. On such occasions, the mediator may provide an assessment of the case, evaluating its strengths and weaknesses, its value and the likely outcome, if the process were to move to arbitration or litigation. But, unlike arbitration, this evaluation, and the conclusions that may be drawn from it, does not produce a binding outcome, unless the parties agree to make it so.

A successful mediator needs to bring some important qualities to the task, in order to be effective. They include, among other traits, sincerity, trustworthiness, honesty, integrity, maturity, tact, the ability to appear and behave in an independent and neutral way, open-mindedness, a positive and optimistic attitude, the ability to ask relevant questions, and the ability to listen carefully. Supplementing these personal traits, it clearly helps if the individual has the ability to quickly grasp complex business matters that may involve strategic, marketing, organizational, process, technology, financial or economic issues. It is especially beneficial if the person has experience with the particular type of business involved and understands the industry context within which it operates.

Mediation tends to have a high success rate, since the parties are involved in the process, have more control over the outcome, and are more inclined to follow through and comply with the settlement agreement. In addition to whatever economic or financial considerations are at stake, the preservation of valuable relationships is often just as important.

Because of the time-consuming and costly nature of litigation, mediation offers the parties a potentially appealing alternative even when litigation is underway. Summary judgment motions, for example, while designed to bring a matter to prompt closure in court, often take some time, and where the outcome is in doubt, it may be the moment to attempt settlement and use mediation to bring a mutually acceptable resolution to the dispute.

As with arbitration, the mediation process may be subject to a provider’s rules and procedures. These rules tend to be less extensive than those of arbitration, but provide an appropriate framework within which the process can be directed and managed.

Case Studies for Mediation:

1. A group cancelled their reservation at a hotel shortly after 9/11 because many of its out-of-town members did not want to travel to the company's annual conference. The hotel operator allowed the group to reschedule the meeting for a few months later without penalty, maintaining the same room rate and size of room block, and asking for a second deposit of 25% of the total expected amount of charges. The problem arose when the group cancelled a second time, indicating that many of the group's members were still reluctant to travel. The hotel owner decided to enforce its cancellation policy, and sued the group for the lost revenue for the two events. The group disputed the damage claims, insisted it was really only one event, and the two parties went into pre-trial mediation.

The mediator, as a hospitality industry veteran, understood the issues, and was able to objectively assess the damages claimed by the hotel owner. He was able to reduce the claims down to a more supportable level of incremental lost profits, and facilitated an agreement between the parties where the group committed to holding two additional events over the next three years at the subject hotel. The hotel owner would hold the deposits and apply them to the rescheduled event costs. Both sides agreed, and the litigation was dropped.

2. Another dispute that was resolved using an experienced hospitality industry mediator involved a partnership comprised of a group of unsophisticated Limited Partnership (LP) investors (owners) vs. a hotel management company (operator). The operator, acting as General Partner (GP), developed the hotel, and presented projections of anticipated operating revenues and profit distribution to the owners. Several years after the hotel was built and operational, however, the projected distributions to the owners did not materialize as presented, and the income and return to the GP was significantly in excess of those of the owners. Predictably, the owners had lost trust in the operator, and sued for misrepresentation, breach of fiduciary duty, etc. Both sides agreed to a pre-trial mediation.

The mediator was able to apply his hospitality industry financial expertise and duplicate the model originally used by the operator when "selling" the deal to the LPs. He evaluated the relative cases of both parties, indicating where their claims or defenses were weak, and brought both sides toward the middle in terms of a settlement amount. Finally, he was able to show the operator, based on its own projections of future performance, how it could achieve a decent internal rate of return by buying out the LPs' interests for close to their original investment. By regaining control of the real estate, the operator could then flip it to a third-party REIT. The LPs agreed to accept the settlement, exit the partnership, and the operator lined up a new owner, whose investment in the real estate paid off the LPs.

Issue Review Board™ (IRB™)

An Issue Review Board™ is ideally suited to those on-going business relationships where there is a need to quickly resolve issues before they become disputes. Used historically in the construction industry, where time-sensitive projects must move forward promptly,

and where delays for dispute resolution can have significant economic impacts, the IRB™ also has application in operational environments. Within the hospitality industry, these may be used, for example, not only for development projects, but also with owner/operator issues that might arise out of a management agreement.

Promulgated by the Institute for Conflict Management (ICM), IRB™ procedures may be amended by the parties to a relationship to suit their particular needs. The intention is that any party may refer an issue to the Board that is within its purview. The IRB™ is designed to function quite independently of the parties' interests, and render a non-binding recommendation for resolution of the issue. While the recommendation is non-binding per se, it may be admissible as evidence in the event the parties subsequently take the issue further into the dispute resolution process. This provides some teeth to the recommendations.

The IRB™ itself typically comprises a panel of three members, whose two party-appointed members, like an arbitration panel, are selected first by each of the parties. These two members then select a "neutral" third member who will generally serve as Chairperson. Since the IRB™ serves at the pleasure of the parties, it may be dissolved by mutual consent of the parties, generally upon completion of the project in the development context, or at the end of the contract, if it is being used in an operational context.

Meetings of the IRB™ can occur with as much frequency as the parties deem appropriate, but will generally involve a monthly or bi-monthly sequence for a project in development, and quarterly for operational groups. Within the operational context, an IRB™ is especially useful for large projects where the "asset management" function representing an owner's interests is interfacing with an operational team from the management company. And while such relationships tend to bring very knowledgeable people together to deal with operational issues, there are nevertheless frequent occasions when an issue requires resolution in an independently organized forum such as an IRB™.

The formation of an IRB™ is ideally conceived of during contract negotiation stages, so that the process for referring issues for resolution is institutionalized from the very outset. Contract language would, among other elements, provide for the selection of the Board's members, the nature of the agreement between the Board and the parties involved, the process for referring issues to the Board, the application of a defined set of rules and procedures, the frequency of meetings, the treatment of fees and expenses, notice and communications, immunity, the basis for Board member substitution or replacement, and finally, the Board's dissolution.

Case Studies for Issue Review Boards™:

1. The owner and operator of a full-service, first-class resort were unable to agree on items in the annual budgets and capital expenditure (Cap Ex) programs. Instead of involving the general counsel of both organizations, the parties utilized the Issue Review Board™ process to resolve these disputes.

Whenever the parties could not agree on these types of issues, each party prepared a short brief outlining their position on the disputed budget or Cap Ex item, and submitted it to the chair of the IRB™. The chair reviewed the briefs, conducted his own limited investigation into the matter, and ruled as to whether the item should be included or not, and if so, to what level and when in the cycle. Both parties agreed to abide by the decision for the current budget year.

2. Another issue that an IRB™ chair decided upon was the composition of the Competitive Set. The Operator's Performance Test involved comparing its RevPar performance at the subject hotel to a pre-determined Competitive Set. After 5 years of operation, both parties agreed that the original Competitive Set was no longer valid, but could not agree on which properties should be included in the updated Set. The parties each submitted a list of 5 comps to the IRB™ chair, who visited all of the properties and selected a competitive set from the ten properties included on the two lists. Both parties agreed to use that competitive set for the following five years, as it pertained to the Performance Test.

The ISHC Panel

In responding to the need for ADR in the hospitality industry, the ISHC has formed a panel of arbitrators, mediators and IRB™ members to serve the industry in a neutral and independent manner to help resolve disputes that arise within the industry. The ISHC panel today comprises approximately 30 members, all of whom have been trained in dispute resolution, and are certified to serve in this capacity. The ISHC plans to add additional members to this panel of individuals with deep hospitality industry knowledge and experience, who bring to the process of dispute resolution an understanding of the context of the business arrangements within the sector and how they function.

Cornell University's Survey on the use of ADR

In a comprehensive study of the use of ADR in American industry, Lipsky and Seeber surveyed the corporate counsel of the 1000 largest U.S. Corporations and found that the vast majority of corporations had used one or more ADR procedures in recent years. A total of 88 percent of the 606 respondents had used mediation, and 79 percent had used arbitration. Most respondents furthermore indicated that they believed that use of ADR would grow significantly in the future. Over 84 percent said they are likely or very likely to use mediation in the future, while 69 percent said the same about their future use of arbitration. The survey did not ask about the use of Issue Review Boards™.

Corporate policy appeared to vary, but most respondents indicated that they either litigate first and then move to ADR, or litigate only in cases where it seems appropriate to do so, and used ADR for all others. Smaller companies appeared to be more litigious, while larger ones more "pro-ADR". Aside from the economic motivation to using ADR, respondents in the Cornell survey suggested a desire to gain greater control over the process and the outcomes, especially given their general concerns about the risk and uncertainty of litigation. High levels of respondent satisfaction with the results achieved

through ADR also support the study's conclusion concerning the future growth that may be anticipated, as ADR is increasingly adopted as an alternative to litigation.

Of particular interest in the Cornell study was the concern respondents expressed relating to the qualifications of mediators and arbitrators. A majority believed that they were "somewhat qualified" and concerning arbitrators in particular, almost half stated that they lacked confidence in the arbitrators. Nearly 30 percent reported that there was a shortage of qualified arbitrators. There did not appear to be a shortage of ADR neutrals, but rather a shortage of qualified neutrals – individuals with expertise in both the process and the topic.

In preparing for the development of its panel of ADR neutrals, the ISHC conducted an informal survey of the General Counsels of a number of hospitality companies, most of whom confirmed what was already apparent from Cornell University's more general survey of U.S. companies at large – that there was a favorable attitude toward ADR as a process, but concern about the lack of qualified arbitrators and mediators. In responding to this concern, it is believed that the ISHC program will provide the necessary framework for a higher utilization of this process in the hospitality industry in the future.

Dispute Resolution Matrix: Suggested Processes
(see attachment "ADR_Chapter_Exhibit.pdf")

The selection and confirmation of a Dispute Resolution Process should be completed as soon as possible, and ideally before a project begins. The time sensitivity of a project will determine how quickly the dispute needs to be resolved. Evaluating the type and timing of the relationship will help the parties determine which process best fits the situation when an issue or dispute arises.

No single dispute resolution process fits all issue or dispute scenarios. The matrix in Exhibit 1 (see attachment "ADR_Chapter_Exhibit.pdf"), which was designed by Mr. Dave Armstrong of the Institute of Conflict Management (ICM), provides a guideline for suggested dispute resolution processes to use when writing the dispute resolution clause of a contract. Following these steps with the matrix will allow the best process to be designed for each unique situation:

Locate a relationship in the left side column, similar or the same as the subject relationship. (i.e., owner and franchisee; contractors and client, etc.)
Determine at what stage/time frame the relationship is currently or will be operating.
Follow that row across from left to right to determine the types of dispute resolution processes and sequence of use, appropriate to your situation.
Write the dispute resolution clause for your contract according to the suggested processes.

Components of the various processes are described below:

Conciliation: An informal dispute resolution process in which a third-party neutral is

selected by the parties to review issues arising during the course of a project or relationship, to make a non-binding recommendation for immediate resolution. This process can be implemented by the parties even after a project is already underway

Components Include:

The Provider submits names of potential conciliators, and parties will agree on one.
The neutral shall have experience in the industry in which the issues occurred.
The Conciliator will be on call as needed during the project/relationship.
Process includes on-site visits and meetings.
Recommendations by the Conciliator can be made the same day, even during the meeting, if requested by the parties.
No formal documentation is required.
The cost of resolution is split equally by all parties.

Issue Review Board™ (IRB™): As discussed, the IRB™ is a pro-active issue resolution process in which a panel of three neutrals, with extensive knowledge and expertise in a particular industry, is selected to serve as available resolutionists when an issue arises during the project/relationship. One of the three experts acts as the chair of the panel, and together they render non-binding recommendations (which are admissible as evidence in any future court/arbitration proceeding) regarding the issues. By addressing the issues as they arise, major disputes between the parties can be avoided.

Components include:

IRB™ is established before project begins (during contract development).
The Provider submits names of potential IRB™ panelists.
The panelists shall be experts from the industry.
IRB™ panel is organized before the project/relationship begins.
Copies of pertinent contracts and documents are kept on file with the Provider.
IRB™ panelists are on call as needed during the project/relationship.
Process includes on-site visits and meetings.
Cost of resolution is split equally by both parties.

For smaller projects, a single-member Issue Review Board™ can also be established prior to the start of the project.

Arbitration: As noted earlier, a dispute resolution process in which a third-party neutral listens to statements made by various parties and then renders a binding award enforceable by courts.

Components include:

The Provider proposes names of prospective arbitrators, and either the parties agree on one, or the Provider selects the arbitrator – whichever the contract designates.

The arbitrator shall have extensive experience in the industry.
Discovery is limited to the production of documents (unless otherwise noted).
Parties can pre-determine the length of the process.
Arbitration can be used anytime during the life of the project.

An expedited version of the Arbitration process is also available – this process stipulates that the arbitration shall be held within a pre-set number of days of the initial filing, and that the arbitrator's decision will be submitted to the parties within a pre-set number of days after the initial filing.

Mediation: As noted, a dispute resolution process in which a third-party neutral facilitates discussions among the parties to help the parties design their own solution. NOTE: The mediator makes no decisions or rulings.

Components include:

The Provider selects the mediator, unless the parties have already agreed upon another mediator.
The mediator shall have extensive experience in the industry.
Discovery is limited to the production of documents (unless otherwise noted).
Parties can pre-determine the length of the process.
Mediation can be used anytime during the life of the project.

An expedited version of the Mediation process can be adopted where parties agree that the mediation will be held within a pre-set number of days after the initial filing.

Frequently Asked Questions

In this section, the authors provide answers to the most frequently asked questions about ADR.

What is the distinction between arbitration and mediation?

An arbitration is a process that produces a (generally) binding resolution to a dispute, decided by an arbitrator or panel of arbitrators based upon an examination of evidence and the hearing of testimony. By contrast, a mediation may or may not produce a tangible result, and involves the facilitation of a dialogue to bring the disputing parties to a mutually acceptable resolution.

What is an Issue Review Board™?

An Issue Review Board™ comprises a panel of independent experts brought together as needed to produce non-binding recommendations concerning issues between parties to an agreement before they rise to the level of a dispute.

How do arbitration and mediation proceedings get initiated?

Arbitration and mediation proceedings may be promulgated by contract, in which case one party to an agreement has the right to call for a proceeding to help resolve a dispute. In cases where there is no such contractual right, then the parties may agree between themselves to go to arbitration or mediation. In either circumstance, the parties will follow an agreed-upon process of arbitrator and mediator selection and the appointment, if and as necessary, of an organization (Provider) to manage the process.

What are the key advantages of arbitration and mediation?

The principal advantage of both arbitration and mediation is the avoidance of a time-consuming and expensive litigation process through the judicial system. Generally faster and less expensive than litigation, the results of arbitration are for the most part binding and recognized by the judicial system as such. Mediation is a less complex and therefore less expensive process than arbitration, and is to be favored where the parties have faith in the process and the mediator involved, as well as some sense that such a process might produce a satisfactory result.

What are the discovery rules in the typical arbitration?

There are generally no explicit discovery rules in an arbitration, although some arbitrators will look to the rules of civil procedure for guidance. Arbitrators may rule on discovery disputes between the parties as part of the process.

How are IRBs™ useful in development and operations within the hospitality sector?

Issue Review Boards™ are of value to hotel development by dealing with issues as they arise, preserving critical relationships, avoiding lengthier dispute resolution, and mitigating the risk of delays in a project's completion. Within operating agreements, for example, between management entities and owners, such Boards assist in the preservation of the relationships, and provide a venue for dealing with issues that should not be left unresolved and may not be significant enough (yet) to trigger a more formal dispute resolution process.

What is the role of an ADR "provider" organization?

An ADR provider is an organization designed to administer an arbitration or mediation process. Such an organization will generally provide rules by which the parties agree to abide, will assist in the appointment of the arbitrator(s) or mediator, and will communicate with the parties on administrative matters such as arrangements for hearings, billing for services and the issuance of rulings and findings.

How is independence assured in an arbitration and mediation process?

In an arbitration, the parties will generally have decided upon either a single arbitrator or

a panel of arbitrators (typically three). In the latter instance, the parties appoint their respective arbitrators, and these two "party-appointed" arbitrators will select a third neutral. The panel will then function using majority rule. Arbitrators and mediators who are members of professional organizations, such as the International Society of Hospitality Consultants (ISHC), or are affiliated with ADR provider organizations such as ICM, AAA and JAMS have been selected for such membership through a rigorous process. Such arbitrators have agreed to abide by strict standards of professional conduct and are required to disclose to the parties any real or perceived conflicts of interest that might be seen as impairing their independence. Users of arbitration and mediation services are clearly also obligated to ensure that they understand their appointees' background and independence of standing regarding the parties and the dispute in question. If an appearance of bias is present in a neutral, the parties can replace him or her immediately.

Why should arbitration clauses be incorporated into hospitality industry agreements, and if so, what should they cover?

Investors, lenders, developers, management companies and franchisors, among others, are well-advised to incorporate standard arbitration clauses into their agreements, because of the significant advantages of arbitration over litigation. Since the stakes are generally high and the value of relationships so critical, providing for alternative dispute resolution processes makes very sound business sense. Although counsel should be consulted in drafting and negotiating such provisions, among the most important provisions to include are: (a) providing for the provider organization of your choice; (b) specifying the rules for conduct of the arbitration if no provider is to be identified; (c) determining how much discovery will be allowed, and the limits on such discovery; (d) whether costs and fees are to be allocated to the prevailing party; and (e) whether there is any right to appeal.

Do arbitrators and mediators require a professional certificate or designation to practice?

There are no formal requirements for arbitrators and mediators to be licensed, either at the state or Federal level. However, the imprimatur of an affiliated organization such as the ISHC ensures that such individuals have: 1) undergone training in the process of dispute resolution; 2) continue to take professional education coursework to remain current in the field; 3) have valuable industry experience; and 4) are committed to abiding by strict standards of professional performance.

How are arbitrators appointed?

There are several ways that arbitrators may be appointed. In the instance where the parties have agreed to use a provider organization to handle the arbitration process, then this organization will present candidates or provide access to a list of such candidates. There will then follow a formal selection process that will often provide for a timetable for completion. In the absence of a designated provider organization, the parties may have nevertheless agreed to appoint a panel of three members. In this case, each party will appoint their respective arbitrator, and these two "party-appointed" arbitrators select

a neutral third member. In the absence of any pre-existing agreement regarding arbitration, then once the dispute has been identified and defined, the parties will need to come to an agreement to appoint either a single arbitrator that they can agree upon, or a panel in the manner described previously.

What laws govern the practice of arbitration and mediation?

The laws of each state govern the arbitration of claims that would have been brought in a state court absent an arbitration clause. Similarly, if a claim would have been brought in Federal Court absent an arbitration clause, the Federal Arbitration Act (FAA) will generally govern. The US Supreme Court ruled in 2003 that to be covered by the FAA, the agreement must be a "contract evidencing a transaction involving commerce," a definition that undoubtedly sweeps in most disputes in the hospitality industry.

What is the role of the International Society of Hospitality Consultants in the ADR process?

A group of ISHC members have been certified as arbitrators and mediators and are also certified to serve on Issue Review Boards™. These ISHC members have taken the requisite training and continuing education, are well versed in ADR processes, have extensive hospitality industry experience and knowledge, and are committed to alternative dispute resolution and its growth and development in the industry. The ISHC is therefore well-equipped as an organization to serve this important need, and is ready to provide its roster of competent, certified ADR practitioners to third parties in need of such service. The ISHC provides background information and knowledge on the practice of ADR, and can assist third parties in identifying the available resources to complete a successful arbitration or mediation, or organize an Issue Review Board™.

If my arbitration clause designates a provider that I don't have confidence in, what should I do?

If all parties to the arbitration clause agree to do so, they may designate whatever provider they like, or they can dispense with the provider entirely and designate whatever arbitrator(s) they want to. A provider organization such as AAA, ICM or JAMS is not necessary. Only the arbitrator(s) and a set of agreed-upon rules for conducting the arbitration are required. If, however, a contract designates a provider and all parties do not agree to an alternative to the contractual terms, then the contract will govern.

Are the decisions final and binding?

This depends on the language of the ADR clause and the prior agreement of the parties. That said, typically, decisions reached by arbitrators are final and binding. Arbitration orders are usually confirmed by the parties with the local courts, so that they can be enforced by local laws. By contrast, agreements reached by Mediation are typically non-binding and voluntary. IRB™ recommendations are also usually non-binding, but tend to have more force behind them, as they are admissible in any subsequent litigation, and a

non-cooperating party would be at a disadvantage to show why they did not follow the panel's recommendations.

Where will the arbitration or mediation occur?

The location of the venue should be identified in the ADR clause of the contract. Typically the ADR process occurs in the county where the property is located, although both sides could agree to hold it at a more convenient place.

Why is it important to have someone knowledgeable in the hotel industry arbitrate or mediate these disputes?

Historically, both parties are better off having a neutral who is both knowledgeable about the hospitality industry, and trained in dispute resolution processes. This eliminates the need to educate the neutral about the industry; takes advantage of the neutral's many years of experience in industry-related disputes; and avoids the problem of one party attempting to hide information or confuse the neutral about the key issues. Most retired judges are extremely knowledgeable about the law, for example, but have little to no working knowledge of the economics of the hospitality industry, and their direct hotel experience may be limited to simply having been a guest at a related facility.

Sample Standard ADR Clauses

In an effort to assist parties in establishing workable dispute resolution processes, the authors have compiled the following Standard ADR Clauses, and encourage their use in most agreements, such as management contracts, franchise agreements, employment contracts, development agreements, partnership agreements, construction contracts, and other related agreements.

Issue Review Board™: The Parties hereby agree to establish an Issue Review Board™ (IRB™) in accordance with the Issue Review Board Rules and Procedures of the Institute for Conflict Management, LLC (ICM), (www.icmneutrals.com), and the "Rules", which are incorporated herein by reference. The IRB™ shall have [one/three] member[s] appointed pursuant to the Rules set forth by ICM.

All disputes arising out of or in connection with the present Contract shall be submitted, in the first instance, to the IRB™ in accordance with ICM's Rules. For any given dispute, the IRB™ shall issue a Recommendation in accordance with ICM's Rules. If any Party fails to comply with a Recommendation when required to do so pursuant to the Rules, the other Party may refer the failure itself to arbitration under the Arbitration Rules and Procedures of ICM by one or more arbitrators appointed in accordance with ICM's Rules of Arbitration.

If any Party sends a written notice to the other Party and the IRB™ expressing its dissatisfaction with a Recommendation, as provided in ICM's Rules, or if the IRB™ does not issue the Recommendation within the time limit provided by ICM's Rules, or if the

IRB™ is disbanded pursuant to ICM's Rules, the dispute shall be finally settled under the Arbitration Rules and Procedures by one or more arbitrators appointed in accordance with the Arbitration clause presented below.

Mediation: In the event of any controversy or claim between the parties to this Agreement arising out of or relating to this Agreement [expressly excluding any claim for_____], and including without limitation any legal or equitable claim, and if the parties are unable to agree to a settlement of such disputes by direct negotiations, the parties shall promptly mediate any such disagreement or dispute in (City/State) under the rules of (the International Society of Hospitality Consultants or its designee/other ADR provider organization) (ADR Provider), with a mediator selected from a list of mediators with experience in the hospitality industry proposed by the ADR Provider.

Arbitration: If the parties are unable to resolve any such disagreement or dispute through mediation, then such disagreement or dispute shall be submitted to binding arbitration in (City/State) under the ADR Provider's rules. The ADR Provider or its designee shall administer the arbitration proceedings.

A panel of (one/three) neutral arbitrator(s) shall be appointed pursuant to ADR Provider rules, (each of who/who) shall be qualified as (an) arbitrator(s) through training programs approved by ADR Provider, and have extensive experience in the hospitality industry. From the date the panel has been appointed and has agreed to serve, a preliminary hearing date shall be set within thirty days. Time is of the essence in the resolution of any dispute, and the panel shall be mindful of that in setting all dates related to the arbitration, unless all parties to the Agreement agree to a more relaxed schedule for the conduct of the arbitration hearings and discovery.

At the preliminary hearing, the arbitrator(s) and the parties shall establish an expedited schedule for any discovery that may be provided pursuant to the ADR Provider's rules or by stipulation of the parties. At that time, the arbitrator(s) shall also establish an arbitration hearing date following at least twenty days after the cutoff of discovery.

Ten days before the arbitration hearing date, each party shall exchange briefs and any reports prepared by expert witnesses upon whom such party intends to rely at the arbitration hearing. Ten days before the arbitration hearing date, each party will also exchange copies of all documentary evidence upon which such party will rely at the arbitration hearing, and a list of the witnesses such party intends to call to testify at the hearing.

In addition, the parties shall exchange, on the date set by the arbitrator(s), but at least five days in advance of the arbitration hearing, any documents that the arbitrator(s) determine(s) to be relevant to the issues to be arbitrated. Each party shall also make its respective experts available for deposition by the other party prior to the hearing date, according to a schedule to be ordered by the arbitrator(s).

The parties' intention is that for most disputes under this Agreement, the arbitration hearing shall be concluded no later than one hundred twenty days after the preliminary hearing date. The arbitrator(s) shall make (his/their) award within thirty days after the conclusion of the arbitration hearing and the final submission of any post-hearing briefs. (In the event of a three-member panel, the decision in which two of the members of the arbitration panel concur shall be the award of the arbitrators.)

In the event the hearing cannot be concluded within the specified one hundred twenty days after the preliminary hearing date, and the parties cannot mutually agree on an extension of the date for the conclusion of the hearing, the arbitrator (chair of the arbitrator panel) may prepare a declaration setting forth the reasons why an extension of time which shall not exceed sixty days is required for any deadline for concluding hearings or issuing an award. Either party may then present the declaration and an application to a court of competent jurisdiction requesting an extension of the date by which the hearing is to be completed for good cause shown, and which motion may be brought on five days notice or on an order shortening time, if necessary. The parties to this Agreement expressly authorize a court of competent jurisdiction to extend the time limits provided for this arbitration proceeding for good cause shown, and to do so on shortened time, if necessary.

Except as otherwise specified herein, there shall be no discovery except such limited discovery as may be permitted by the arbitrator(s), who shall authorize only such discovery as is shown to be necessary to insure a fair hearing, and no such discovery shall in any way conflict with the time limits contained herein unless otherwise agreed by the parties in writing or extended by a court.

The arbitrator(s) shall not be bound by the rules of evidence or civil procedure, but rather may consider such writings and oral presentations as reasonable businessmen would use in the conduct of their day-to-day affairs, and may in (his/their) discretion preclude the presentation of redundant or cumulative evidence of material. It is the intention of the parties to limit live testimony and cross-examination to the extent necessary to insure a fair hearing to the parties on the significant matters submitted to arbitration. The parties have included the foregoing provisions limiting the scope and extent of the arbitration with the intention of providing for prompt, economic and fair resolution of any dispute submitted to arbitration.

The arbitrator(s) (is/are) authorized to consider and to dispose of issues by motions for summary judgment or for summary adjudication provided the party opposing any such motion has received reasonable notice and a fair opportunity to conduct discovery of facts relevant to the motion and a fair opportunity to respond to any such motion, or, where the matter can be disposed of purely as a matter of law without determination of any facts. With respect to a motion for summary judgment or summary adjudication, the parties shall comply with the applicable procedural rules and/or statutes for making and opposing such motions of the state in which the arbitration is taking place, except that the arbitrator(s) may shorten the time limits specified in such rules

and/or statutes, and notwithstanding any other provision herein to the contrary, the rules of evidence shall apply with respect to the disposition of any such motion.

The arbitrator(s) shall have the discretion to allocate in (his/their) award the costs of arbitration, arbitrator fees and the respective attorneys' fees and costs, including expert witness and consultant fees and costs, of each party between the parties as (he/they) believe(s) is appropriate under the circumstances.

Judgment upon the award entered by the arbitrator(s) may be entered in any court having jurisdiction thereof.

Notwithstanding the parties' agreement to mediate or arbitrate their disputes as provided in this Agreement, any party may seek emergency relief or provisional remedies in a court of law without waiving the right to arbitrate or mediate the merits of the dispute provided no arbitration panel has yet been convened, or, if it is not practicable for such application to be considered and determined by the arbitration panel. If the arbitration panel has been appointed and is available to consider and rule on the application in a timely fashion, any such application for provisional or emergency relief shall be made to the arbitration panel and the panel shall be vested with the same power as a court to award such provisional relief.

The arbitrator(s) (is/are) hereby specifically authorized to hear, consider and rule on motions to dispose of issues if there are no material disputed issues of fact, and/or if an award is appropriate as a matter of law without the necessity of an arbitration hearing and hearing live witness testimony.

The arbitrator(s) shall make (his/their) award based upon the applicable legal principles and based on the documents and testimony presented by the parties, and at the request of any party prior to conclusion of the hearing, shall provide a reasoned award and shall include in (his/their) award findings of fact and conclusions of law supporting such award. Statutes of limitation under the applicable state law shall be applied by the arbitrator(s).

The arbitrator(s) may not by (his/their) award change any terms of the underlying business agreement in which this arbitration clause is embedded.

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Additional information about ADR in the Hospitality industry may be found on the ISHC web site www.ishc.org

David B. Lipsky and Ronald L. Seeber, "The Appropriate Resolution of Corporate Disputes: A Report on the Growing Use of ADR by U.S. Corporations"; Cornell University; 1998.