

AMERICAN BAR ASSOCIATION

**BUSINESS LAW SECTION
TASK FORCE ON ALTERNATIVE DISPUTE RESOLUTION IN COMMERCIAL FINANCE
TRANSACTIONS**

and

**SECTION OF DISPUTE RESOLUTION, ARBITRATION COMMITTEE
SUBCOMMITTEE ON ADR IN COMMERCIAL FINANCE TRANSACTIONS**

FINAL REPORT

AND

**SUPPLEMENTARY ARBITRATION RULES
FOR
COMMERCIAL FINANCE TRANSACTIONS**

April 1, 2011

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FINAL REPORT
Of
BUSINESS LAW SECTION
TASK FORCE ON ALTERNATIVE DISPUTE RESOLUTION IN COMMERCIAL FINANCE
TRANSACTIONS
(the “BLS Task Force”)
and
SECTION OF DISPUTE RESOLUTION, ARBITRATION COMMITTEE
SUBCOMMITTEE ON ADR IN COMMERCIAL FINANCE TRANSACTIONS
(the “DRS Subcommittee”)

April 1, 2011

I. History and Exposure Draft for Comment:

The activities of the BLS Task Force and the DRS Subcommittee sprang from a long-standing effort by the American College of Commercial Finance Lawyers, Inc. to integrate alternative dispute resolution techniques¹ into commercial finance transactions. In the 1990’s this effort was a joint project of this College with the American Arbitration Association (“AAA”) that resulted in the drafting of a 1998 publication titled “*Resolving Commercial Financial Disputes – A Practical Guide*” (the “AAA Guide”). The AAA Guide included mediation and arbitration rules crafted specifically for a dispute involving “any commercial financial arrangement, product or other matter or conduct related thereto”. The AAA guide included provisions for the AAA to designate a National Roster of qualified arbitrators to arbitrate such disputes and was a complete, self-contained set of mediation and arbitration rules that the parties could adopt for resolution of such disputes. The AAA Guide also included model draft mediation and arbitration clause that was admittedly “written from the lender’s perspective” but which could be modified to suit the nature of the particular transaction and the negotiations of the parties.

In general, while a few lenders attempted using the rules and procedures in the AAA Guide², anecdotal evidence suggests that the vast majority of lenders have either stopped using them, citing inconsistent results and ‘push-back’ from borrowers, or rejected their use in the

¹ Although the phrase ‘alternative’ may not be considered ‘politically correct’ to members of the Section of Dispute Resolution, these remedies and techniques have largely been rejected by the commercial finance bar and is generally considered to be ‘alternative’ in the commercial finance community.

² Most notably Bank of America’s standard forms for significant commercial loan transactions recently included an arbitration clause (again, written from the lender’s perspective) adopting the rules in the AAA Guide.

first instance³. Ten years after its publication, most counsel for lenders and borrowers appear to be unaware of the AAA Guide or the rules therein. Anecdotal evidence suggests that business lawyers negotiating on behalf of borrowers resist arbitration clauses as one-sided, favoring lenders, and counsel for lenders regard the use and benefit of these techniques as unproven. Most business lawyers tell ‘horror stories’ of arbitration proceedings run amok and there is a wide perception that the process involves arbitrators that are not familiar with the law or practices in the commercial finance area and that, consequently, make inconsistent or ‘split the baby’ decisions. Their common theme is that significant changes would have to be made to the customary arbitration process and the benefits of ADR techniques must be demonstrated before the commercial finance community will adopt them or devote the resources to negotiate them into their agreements.

In recent interviews by the Chair with senior counsel for a number of lenders, a number of common perceived complaints and issues with use of arbitration for commercial disputes were repeated. These comments and complaints included the following:

- Arbitrators are not properly knowledgeable about the areas of law governing lending disputes, including Uniform Commercial Code, suretyship and bank regulatory law and similar issues.
- Arbitrators are not bound to apply the law to the determination of the dispute and there is no appeal from any clearly errant decision.
- Arbitrators tend not to be able to restrain the tendency of litigators to employ ‘leave no stone unturned’ discovery – leading to costs that are approaching that of traditional litigation in courts.

In 2007, the Board of Regents of the American College of Commercial Finance Lawyers determined that the College should revisit this topic. A member of the Board of Regents, Attorney Thomas J. Welsh, was charged with the task of preparing a colloquium⁴ between the American Bar Association Sections of Business Law and Dispute Resolution on these topics. A small panel of experts in dispute resolution and business finance was invited to discuss ADR techniques and benefits at the Spring Meeting of the Business Law Section, held in Dallas, Texas in April of 2008. This panel consisted of (a) Michael Greco, former President of the ABA, acting as the chairperson of the panel and colloquium; (b) James Roethe, former General Counsel of Bank of America and ADR practitioner, speaking on the considerations for and against ADR techniques in commercial finance transactions; (c) Professor Lela Love, speaking on mediation techniques and advantages; (d) Sandra Partridge, Vice President of AAA, speaking about the perspective of AAA as an ADR service provider; and (e) Thomas Welsh, in his capacity as Regent of the American College of Commercial Finance Lawyers,

³ For example, an article in the *Journal of Equipment Lease Financing* in 2006 noted that an informal poll on the Equipment Leasing Association’s listserv showed that most respondents were not inclined to use alternative dispute resolution and did not provide for it in their documents. Ytterberg, *Arbitrating and Mediating Equipment Lease Finance Disputes*, 24 *JOURNAL OF EQUIPMENT LEASE FINANCING*, No. 2 (Spring, 2006).

⁴ The term ‘colloquium’ was chosen to describe the process of discussion that we envisioned between the two ABA Sections and legal communities – this process was intended as a discussion and exchange of views and information rather than a rule-making process.

commercial finance attorney and the Reporter for the Colloquium, speaking about the commercial finance perspective and to present a discussion draft of a new set of model supplementary arbitration rules to spark discussion. The same panel reprised the colloquium discussion at the Spring Meeting of the Dispute Resolution Section on April 15, 2009.

The leadership of the College and sponsoring BLS committees enthusiastically received this colloquium panel presentation and, as a consequence, the BLS Task Force was formed on this topic, naming Thomas Welsh as the Chair. Thereafter, the Arbitration Committee of the Section of Dispute Resolution also requested Thomas Welsh to Chair the DRS Subcommittee, and Sandra Partridge to be the Vice Chair. Since that date joint meetings of the BLS Task Force and of the DRS Subcommittee (collectively referred to in this report as the “**Joint Committees**”) were held. The meetings of the Joint Committees were held on March 17, 2009 and April 15, 2009 at the American Arbitration Association offices in New York City and a final telephone conference call on June 15, 2009. The Joint Committees considered and modified the Discussion Draft of the Supplementary Arbitration Rules for Commercial Finance Transactions that had been presented at the Colloquium sessions in 2008 and 2009 and prepared an exposure draft dated April 1, 2010 (the “**Exposure Draft**”) for consideration and comment by the interested constituencies before the final draft was approved for publication and for potential use.

The participants in the meetings of the Joint Committees were largely experienced arbitrators and seasoned professionals in alternative dispute resolution. Unfortunately, despite wide dissemination of the meeting notices, very few participants from the Business Law Section or from the financial services industry attended the meetings or otherwise participated in the consideration of the proposed rules. Consequently, the Joint Committee determined that the best course was to prepare the Exposure Draft of the proposed rules and to attempt to get more input from potential users and affected parties, such as financial services associations, commercial finance and dispute resolution law practitioners and providers of alternative dispute resolution services.

The work of the Joint Committees is posted on a web page sponsored by the Business Law Section. For ease in accessing this information and providing comments on the attached exposure draft, the Joint Committees obtained the following simple web address to make access to the site easier:

<http://ABA-Finance-Arb.org>

The ‘red-lined’ versions of the successive drafts of the revised version of the initial Model Supplementary Arbitration Rules and the Exposure Draft are available on this site, together with Commentary and Committee Notes discussing changes to the text resulting from the Task Force meetings, as well as any comments received. Noted after virtually each section of the Exposure Draft is official Commentary on the Exposure Draft, which have been retained in the draft of the final rules, and Joint Committee Revision Notes, which detail the discussions of the Joint Committees as well as any remaining disagreements within the Joint Committees. The Joint Committees hoped that these materials would ignite debate and comments, particularly relating to some provisions that depart from usual arbitration practice.

Since publication of the Exposure Draft very few comments were received. Comments were primarily received from ADR practitioners and litigators and virtually none were received from business law practitioners. This final report and the attached final draft the Supplementary Arbitration Rules for Commercial Finance Transactions (the “**Final Draft**”) for publication is to encourage discussion and consideration of the use of these techniques in commercial finance transaction and for potential future use by the commercial finance industry, practitioners and alternative dispute resolution service providers.

II. Why the Commercial Finance Community Should Consider ADR in Commercial Finance Transactions:

1. *The System of Civil Litigation In The United States Has Serious Problems – Arbitration Can Address these Problems Now*: The American College of Trial Lawyers and the Institute for the Advancement of the American Legal System published a final report in 2009 relating to discovery and other problems in the American legal system the “**Trial Lawyers Report**”) ⁵. The Trial Lawyers Report reported on a survey of Fellows of the American College of Trial Lawyers in the United States and Canada stating that “[a]lthough the civil justice system is not broken it is in serious need of repair” and reported that today’s system “takes too long and costs too much” – leading to the failure to bring deserving cases and the settlement of cases that should be tried, simply because it costs too much to litigate them. They also pointed out that existing court rules do not lead to early identification of contested issues to be litigated, resulting in promoting full and unbridled discovery – in which full discovery is regarded as “a value above almost everything else”. The Trial Lawyers Report identified a number of Principles to guide future revisions to state and federal court rules to address these problems and noted that the fact that trial lawyers feel that here are serious problems in the civil system generally is emphasized by “the emergence of various forms of *alternative dispute resolution . . .*” (emphasis added)

The process of revising court rules to address problems identified in practice typically takes decades to accomplish. Therefore, if they wish to address these problems in the shorter-term the commercial finance industry and practitioners must use alternative dispute resolution techniques to refine issues, restrain discovery and allow issues to be heard and resolved in a time- and cost-effective manner. Alternative dispute resolution techniques, such as mediation and arbitration, are the result of contract and agreement between and among the parties that are generally given effect under state and federal law. The parties can agree on the methods of resolving disputes and such limitations – whether before or after a dispute has arisen. These techniques are available under current law.

2. *Forum Selection Clauses Often Result in Litigation and Uncertainty*: A brief review of cases and articles shows substantial litigation over the application and effectiveness of forum selection clauses in contracts. The general standards for enforceability of such

⁵ FINAL REPORT ON THE JOINT PROJECT OF THE AMERICAN COLLEGE OF TRIAL LAWYERS TASK FORCE ON DISCOVERY AND THE INSTITUTE FOR THE ADVANCEMENT OF THE AMERICAN LEGAL SYSTEM, March 11, 2009 (rev. April 15, 2009).

clauses were set forth by the United States Supreme Court in the case of M/S Bremen v. Zapata Off-Shore Co., 407 U.S. 1 (1972) which stated that “a forum selection clauses is prima facie valid and should be enforced unless enforcement is shown by the resisting party to be ‘unreasonable’ under the circumstances.” *Id.* at p. 10. The Supreme Court noted that a forum selection clause may be unreasonable if: (a) it is the result of fraud or overreaching; (b) serious inconvenience would result from litigating in the selected forum; or (c) enforcement would result in contravention of a strong public policy in the selected forum. *Id.* at 15-17. Based on this analysis Circuit Courts, such as the Second Circuit Court of Appeals⁶, have adopted similar tests for determining whether such clauses should be enforced – depending largely upon the specific circumstances, whether in domestic or international commerce and whether enforcement of such clauses would be permitted upon a showing that enforcement would be “unreasonable or unjust, or that the clause was invalid for such reasons as fraud or overreaching” (*Phillips* case, cited in footnote 6 below, at 383-384). In recent cases application of such clauses has been upheld in international trade⁷, to require a contract dispute by a U.S. individual to be litigated in Amsterdam courts⁸ and to require litigation in a particular geographical area, although a specific court within that area was not specified⁹. In other recent cases, however, courts have refused to apply such cases in “core” matters in bankruptcy¹⁰, in cases under the U.S. Carriage of Goods By Sea Act¹¹ and when such clauses are incorporated into bylaws of a corporation¹². Clearly such clauses, while generally enforced, tend to leave substantial room for litigation over the ‘reasonableness’ of enforcing them under the U.S. Supreme Court standard.

3. Arbitration Awards Are Easily Enforceable Over National Boundaries But Court Judgments Are Generally Not: Arbitration awards are enforceable over 120 national boundaries under the widely-adopted 1958 Convention on Recognition and Enforcement of Foreign Arbitral Awards. The 1971 Hague Convention on the Recognition and Enforcement of Foreign Judgments in Civil and Commercial Matters, which went into effect in 1979, was not adopted by the United States or any major commercial country¹³, so such court judgments are

⁶ For example, *Phillips v. Audio Active, Ltd.*, 494 F.3d 378 (2^d Cir. 2007) (“*Phillips*”)

⁷ For example, *Export-Import Bank of the U.S. v. Hi-Films de C.V., et al.*, Case No. 09 Civ. 3573, 2010 U.S. Dist. LEXIS 100927 (S.D.N.Y., Sept. 24, 2010)

⁸ *Baker v. Adidas America, Inc.*, 335 Fed. Appx. 356, 2009 U.S. App. LEXIS 14162 (4th Cir., June 30, 2009), unpublished

⁹ *Nahigian v. Juno-Louduon, LLC*, 2009 U.S. Dist. LEXIS 89133 (E.D. Va., Sept. 28, 2008).

¹⁰ *Charys Liquidating Trust et al. v. McMahan Securities Co. (In re Charys Holding Company, Inc. and Crochet & Borel Services, Inc.)*, 2010 Bankr. LEXIS 2636 (Bankr., Del., August 27, 2010), relating to a engagement letter relating to private placement of \$150 million in convertible notes requiring litigation of all issues in Connecticut.

¹¹ *Kanematsu USA, Inc. v. MV Ocean Sunrise*, 2003 AMC 2200, 2003 U.S. Dist. LEXIS 11575 (E.D. La., 2003), invalidating a forum selection clause in a Bill of Lading requiring litigation in Japan.

¹² *Galaviz v. Berg*, 2011 U.S. Dist. LEXIS 1626, *Fed. Sec. L. Rep.* (CCH) P90,004 (N.D. Cal., Jan. 3, 2011), *contra.*, *In re Revlon, Inc. Shareholders Litigation*, 990 A.2d 940, 960 (Del. Ch., 2010).

¹³ This Convention was ratified only by Albania, Cyprus, Netherlands, Portugal and Kuwait.

typically not given effect across national boundaries. The signature, on January 19, 2009, by the United States of the 2005 Hague Conference on Private International Law Convention on Choice of Court Agreements heralds the future day when judgments of courts selected by the parties in their agreements may be more widely recognized and enforced – however to date only the United States has signed it (with Mexico being the only other party currently) and we are years, if not decades, away from this convention entering into force.

4. *Attorneys Have Ethical Obligations to Consider and Advise on ADR*: Most transactional lawyers negotiating and advising their clients on commercial finance matters have little or no knowledge or experience in mediation, arbitration or other forms of dispute resolution.¹⁴ This inexperience sometimes leads to shunning these techniques entirely or making bad process choices or including provisions for judicial review or similar remedies for ‘irrational’ awards that can create even worse problems.¹⁵ These dispute resolution provisions are a frequent feature in business agreements, including in agreements by borrowers with account debtors that are being financed in commercial finance transactions. It is clear that lawyers advising clients on these matters have an ethical obligation to competently advise their clients relating to managing conflicts and agreement provisions.¹⁶ In addition, a number of specific states provide specific requirements for attorneys licensed in those states to advise their clients relating to dispute resolution options – for example, Michigan, Texas and Georgia have such specific provisions¹⁷. Unless transactional lawyers are willing to negotiate and to competently advise their commercial finance clients on these matters, experienced litigators and other parties with experience in these matters should be employed to provide adequate advice and to determine the clients’ goals and objectives, and potential risks, in these transactions.

III. Summary of Points and Comments Regarding Supplementary Arbitration Rules:

Attached is a set of proposed Supplementary Arbitration Rules (the “**Supplementary Arbitration Rules**”) for consideration and possible use by parties. The purpose of these rules was to address the specific issues and concerns that had been communicated in the recent Colloquium sessions and to members of the Joint Task Force. Existing arbitration rules of established service providers create a complete and self-consistent body of rules to address a wide variety of commercial disputes, therefore providing an ‘overlay’ of supplementary rules to address particular issues and concerns of the commercial finance industry is a useful method to

¹⁴ See Thomas J. Stipanowich, *Arbitration and Choice: Taking Charge of the “New Litigation”* (Symposium Keynote Presentation), DePaul Symposium “Winds of Change: Solutions to Causes of Dissatisfaction with Arbitration,” DePaul University College of Law, March 5-6, 2009, 7 DEPAUL BUSINESS & COMMERCIAL LAW JOURNAL 401 (2009) (the “*Stipanowich Lecture*”) at 407 and cases and authorities cited therein.

¹⁵ *Id.* at 408.

¹⁶ See, for example Model Rules of Professional Conduct Rule 1.1 (2007)

¹⁷ *Stipanowich Lecture*, footnote 60 and cites set forth therein.

promote discussion and understanding of specific drafting techniques and choices to address these issues and concerns. These Supplementary Arbitration Rules focus on the particular policy choices to be considered by parties and the commercial finance industry in designing dispute resolution methods that are appropriate and effective for the particular transactions at issue. Whether the techniques employed in these Supplementary Arbitration Rules are adopted by a ‘short-hand’ reference to them in commercial documents or are the subject of more extensive and negotiated specific terms and provisions in detailed arbitration clauses, the purpose of these Supplementary Arbitration Rules is to provide a checklist of issues and techniques for consideration by the parties and the commercial finance industry to promote thinking and discussion on whether and how to use them in specific commercial finance transactions.¹⁸

A brief summary of the major points of the attached Supplementary Arbitration Rules follows:

- **Expanded Scope of Applicable Commercial Finance Transactions:** The initial draft of the Model Supplementary Arbitration Rules contemplated that the rules would be applicable to a relatively narrow scope of traditional commercial lending transactions. Since the appointment of the BLS Task Force and the DRS Subcommittee, however, the credit crisis gripped the world financial community and major financial institutions have failed or been absorbed by other institutions. In particular the collapse and bankruptcy of Lehman Brothers, Inc. illustrated the uncertainty of the dispute resolution clauses (usually involving resort to courts) involving derivative transactions (such as interest rate and credit risk swaps) across national boundaries¹⁹. As the result of this situation the Joint Committees redrafted the earlier Model Supplementary Arbitration Rules to include a wider range of potential commercial finance related transactions. The Exposure Draft now expressly includes, in addition to borrower-lender disputes under commercial loans, disputes under commercial loan intercreditor agreements, participations and syndications as well as credit and interest rate swap agreements and other derivatives, as well as transactions and disputes (other than consumer disputes) that are specified by the parties. The Final Draft is now directly applicable to the disputes relating to the recent credit crisis – they may be adopted by parties ‘opting-in’ after a dispute has arisen or initially as part of adoption in the initial transaction documentation.
- **Availability of Wider Selection of Underlying Base Rules and Service Providers:** The Supplementary Arbitration Rules set forth in the Final Draft are not intended to be

¹⁸ An excellent discussion of the vital role of these choices in tailoring dispute resolution processes to serve particular needs in specific transactions is discussed in Thomas J. Stipanowich, *Arbitration: The “New Litigation”*, U. ILL. L. REV. Vol. 2010, No. 1, 1 (2010).

¹⁹ Many of these situations involve the calculation of breakage fees and similar damage amounts – which is an obvious area where arbitration proceedings would not only result in a faster and more informed determination by an expert arbitrator, but arbitration awards would also have better enforceability across over 120 national boundaries (under the widely-adopted 1958 Convention on Recognition and Enforcement of Foreign Arbitral Awards) than a judgment of a court.

a complete set of rules for all aspects of the arbitration. These supplementary rules are intended to be supplementary to a set of ‘base’ arbitration rules specified by the parties and to be administered by a service provider selected by the parties – so they are not limited to a single provider or a single set of ‘base’ arbitration rules²⁰.

- **Inapplicability to Consumer Transactions:** The Supplemental Arbitration Rules are not intended for consumer transactions or disputes and customary consumer protection provisions in arbitration rules have not been provided in these Final Rules. Use of these rules will be void if included in arbitration agreements relating to consumer transactions.
- **Small Matter “Opt-Out”:** Due to some of the enhanced provisions of these Supplementary Arbitration Rules, the cost of arbitration under these rules is expected to be somewhat greater than under usual arbitration ‘base rules’. Consequently, if the amount at issue in the dispute does not exceed \$100,000 a right is provided for either party to ‘opt out’ of the Supplementary Arbitration Rules within 14 days after the answer is received – in which case the arbitration will proceed under the ‘base rules’. The parties may, however, agree to change this trigger amount or require arbitration notwithstanding this general provision.
- **Arbitrator with Knowledge of Commercial Finance Transactions Required:** In addition to the usual requirements of impartiality and independence, at least one of the arbitrators under the Supplementary Arbitration Rules must have demonstrated knowledge and experience in commercial finance transactions. The requirement that an arbitrator have some knowledge and experience in these transactions was a clear comment from a number of business law practitioners and finance clients. The commentary makes clear that Fellows of the American College of Commercial Finance Lawyers and members of rosters of arbitrators with similar qualifications prepared by service providers are deemed to have these credentials.
- **Number of Arbitrators:** The Supplementary Arbitration Rules provide that the case will be decided by one (1) arbitrator unless the amount at issue is at least \$5,000,000, in which case three (3) arbitrators will be required. The parties may, however, agree to change this trigger amount or to specify the number of arbitrators in advance.
- **Required Application of Substantive Law and Adherence to Statute of Limitations and Privilege Rules:** The Supplementary Arbitration Rules require the arbitrator to give effect to the applicable substantive law applied to the facts that it shall find and may grant any legal, equitable or other remedy or relief provided by law in deciding the matter. This requires the application of the substantive law that the parties assumed when they were documenting their commercial finance transactions (for example, the

²⁰ Unlike the AAA Guide, the Supplementary Arbitration Rules set forth in the Exposure Draft may be used with virtually any base rules or service provider, so to expand support of other service providers for use of these techniques.

Uniform Commercial Code), since a number of ‘base rules’ only require the arbitrator to fashion a result that is ‘just and equitable’.

- **Self-Help and Interim Remedies Generally Permitted**
- **Punitive Damages Not Allowed Unless Expressly Provided By Statute**
- **Confidentiality of Awards Unless Parties Expressly Provide Otherwise:** As a controversial change, the Exposure Draft of the Supplementary Arbitration Rules provided that awards would not be confidential and may be disclosed and shared with case reporters. The rationale for this change was that publication of the reasoned awards will assist in the development of commercial law and is customary for such commercial disputes. The Exposure Draft, however, provided that the parties may require the awards to be confidential if they expressly provide for confidentiality in their arbitration agreement. Most of the experienced arbitrators and service providers that were members of the Joint Committees objected strongly to this change in the confidentiality rules and this draft of the Supplementary Arbitration Rules reversed the earlier position and now provides that all awards will be confidential unless the parties expressly agree otherwise in their arbitration agreement. The Supplementary Arbitration Rules now reflect the usual rule of confidentiality in most Base Rules.
- **Optional Right to Appeal Legal Matters:** The Supplementary Arbitration Rules allow the parties to “opt in” to an appeal procedure for determination of an appeal as to matters of applicable law and application of law to the facts found. If the parties agree that the appeal process is applicable an award must contain a statement of the facts found and the application of the applicable substantive law to the facts and the award will not be final for 15 days thereafter. Within the 15 day period either party may file a notice of appeal of an award and counter-appeals thereafter. The appeal will be before three (3) arbitrators with commercial finance experience based solely upon whether the arbitrator applied the correct substantive law to the facts found. The appeal panel may affirm or modify an award, or, if additional facts must be found, may vacate the award and return it for determination of the additional facts and application of the correct substantive law.
- **Agreement of Parties Allowed to Modify Rules:** As a guiding principle, the Supplementary Arbitration Rules and the associated model arbitration clauses may be freely modified and fashioned to suit the particular desires and requirements agreed upon by the parties.
- **Sample Forms of Arbitration Clauses Invoking the Rules Provided:** The Final Draft includes two sample forms of arbitration clauses for consideration and use in the context of a larger agreement. One form adopts the Supplementary Arbitration Rules without modifying the default provisions and the other provides an outline of changes that the parties may desire to make to the rules. Experienced practitioners have pointed out that the simple forms will likely not be used by institution lenders, since they will prefer to limit the range and scope of matters that can be arbitrated. This Report and

these Supplementary Arbitration Rules take no position on what issues should or should not be arbitrated and leave the commercial finance industry and borrowers and other parties to negotiate the range and scope of matters to be arbitrated or to be litigated before courts.

IV. Acknowledgements

As the Chair of the Joint Committees I would like to thank the many people who assisted in this Colloquium and Joint Committee process. Although naming individuals presents the risk of inadvertently omitting someone, the contributions of these individuals must be recognized. In particular, I would like to thank my Vice Chair of the DRS Subcommittee, **SANDRA PARTRIDGE**, Vice President of the American Arbitration Association located in New York City, for her encouragement, sage counsel and vast experience and for sponsoring our meetings in the AAA Manhattan office. I would also like to thank the following individuals:

Members of the 2008 and 2009 Colloquium panels at the BLS and DRS Spring Meetings:

MICHAEL GRECO, K&L Gates LLP, Boston, MA – former President of the ABA and Colloquium Chair;

JAMES ROETHE, J.Roethe ADR Services, Orinda, CA – former General Counsel of Bank of America and ADR practitioner;

PROFESSOR LELA LOVE, Benjamin N. Cardozo School of Law, Yeshiva University, New York, NY – Professor and writer on ADR matters and later Chair of the ABA DRS Section;

SANDRA PARTRIDGE, V.P., American Arbitration Association, New York, NY – Vice Chair of DRS Subcommittee;

PROFESSOR WILLIAM W. PARK, Boston University School of Law, Boston, MA – Professor and one of the first writers on ADR matters in finance transactions.

Other members of the Joint Committees that regularly attended the meetings and contributed mightily to this effort:

WILLIAM AIKEN, CPA, Financial Consultant, New York, NY

DAVID ALBALAH, Bracewell & Giuliani, New York, NY

WILLIAM L. D. BARRETT, Butzel Long, New York, NY

ARTHUR D. FELSENFELD, Andrews Kurth LLP, New York, NY

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JOHN WILKINSON, JAMS, New York, NY

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LYNN A. SOUKUP, Chair, ABA Business Law Section Commercial Finance Committee, Pillsbury Winthrop Shaw Pittman LLP, Washington, D.C.

The leadership of the Arbitration Committee of the ABA Dispute Resolution Section that encouraged and supported the DRS Subcommittee, particularly:

KURT L. DETTMAN, Co-Chair, Arbitration Committee, ABA Dispute Resolution Section, Constructive Dispute Resolutions, Hingham, MA

Respectfully submitted as of the 1st day of April, 2011.

THOMAS J. WELSH, CHAIR

**ABA BUSINESS LAW SECTION TASK FORCE AND
DISPUTE RESOLUTION SECTION SUBCOMMITTEE
ON ADR IN COMMERCIAL FINANCE TRANSACTIONS**

SUPPLEMENTARY ARBITRATION RULES
FOR
COMMERCIAL FINANCE TRANSACTIONS²¹

April 1, 2011

These supplementary arbitration rules are intended to amend and supplement commercial arbitration rules selected by the parties in arbitration clauses providing for arbitration of Commercial Finance Disputes (as that term is defined herein), whether such clauses are agreed upon by parties prior to such a dispute or after a dispute has arisen. These model rules are not intended to constitute a ‘stand-alone’ set of rules for arbitrating such disputes but are intended to allow parties to shorten and stream-line arbitration clauses and agreements by adopting these standard provisions and amendments that otherwise must be expressly stated in arbitration clauses or agreements to be effective.²²

Commentary

These Model Rules are intended to address the concerns of commercial finance industry lenders (including finance companies and banks) as well as borrowers and other ‘debtors’ under Revised Article 9 of the Uniform Commercial Code, to create a faster, less expensive and informed process for deciding disputes relating solely to commercial lending and borrowing transactions. Concerns and comments of parties relating to use of arbitration to decide such disputes

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²² Some arbitration practitioners have commented that a default set of rules, such as the UNCITRAL arbitration rules, should be specified, so to provide a default in the event parties fail to specify the base rules. This draft intentionally avoids any predisposition toward any particular rules or ADR service provider, so to allow parties to make their own choice and to promote acceptance of a single set of supplementary rules. In the event that base rules are not specified by the parties, an arbitrator may be appointed, under the Federal Arbitration Act (Title 9, United States Code) or any applicable state arbitration act (such as the Revised Uniform Arbitration Act (2000)), and will determine the applicable procedure, in accordance with the parameters of such law.

include: (a) a desire for the arbitrators to be knowledgeable in matters of commercial law and lending practices, consistent, of course, with the degree of impartiality required by arbitration law and rules; (b) a requirement that arbitration awards conform with principles of law governing these transactions and disputes (including the Uniform Commercial Code); (c) providing for a relatively fast right of appeal to an independent tribunal, limited solely to review of the law and application of law to the facts found by the initial panel; (d) limiting awards to compensatory damages, unless other awards or penalties are expressly specified in statutory law governing the dispute; (e) limiting unnecessary or abusive discovery, motion practice and dilatory methods to delay an award or enforcement; (f) allowing parties to effectively use provisional remedies until disputes are decided; and (g) permitting arbitration decisions in such transactions to be compiled and reported so to contribute to the development of commercial law and the law of commercial finance arbitration.

These Model Rules are not intended as a comprehensive statement of arbitration rules for the adjudication of a dispute. They are intended to modify and supplement a set of “base” arbitration rules selected by the parties. These Model Rules contemplate that the parties will select a set of ‘base’ arbitration rules and an arbitration service provider in their arbitration agreement. These ‘base rules’ provide the comprehensive rules to adjudicate a dispute with the relatively few changes set forth in these Model Rules or as otherwise specified by the parties. No attempt has been made to prefer one set of rules or service provider to another – to accomplish this, these Model Rules set the parameters and modify any base arbitration rules to provide the elements desired by the parties in a Commercial Finance Dispute. As with any arbitration scheme these Model Rules are the product of the agreement of the parties and may be modified – samples of a simple draft arbitration clause that allows changes (as well as to simply adopt the Model Rules in their entirety) are included at the end of these materials. As with any model clause, the attached formats should be used as a checklist for drafting an agreement that is applicable to the particular situation.

Joint Committee Revision Notes

These revisions will have Notes at the end of revised sections to aid the joint Committees in the discussions and reaching consensus, if possible, on issues. These Notes will be deleted in the final draft and joint Committees’ report. However, the foregoing Commentary is intended to be included in the final draft to explain and assist in the interpretation of the final Model Rules.

1.0 Definitions:

As used in these Model Supplementary Arbitration Rules, the following capitalized terms shall have the following meanings:

1.1 Arbitration Agreement: The arbitration clause or agreement of the parties providing for arbitration of a Commercial Finance Dispute pursuant to these Model Rules.

1.2 Arbitrator: The arbitrator or arbitration panel, if more than one arbitrator, selected to decide a Commercial Finance Dispute pursuant to these Model Rules.

Commentary

An arbitrator may be selected in a number of different ways. For example, (a) the parties may, in their arbitration agreement, select a particular person or persons to be the arbitrator or panel; (b) the arbitration agreement may provide a particular procedure for the appointment of arbitrators by each party or by an independent party; (c) the arbitration agreement may specify the application of ‘base’ commercial arbitration rules that have a procedure for the selection of arbitrators, or (d) if the arbitration agreement by the parties fails to provide a method for selecting an arbitrator the court (under the Federal Arbitration Act (Title 9, United States Code) or under a state arbitration statute, such as the Uniform Arbitration Act (1955) or Revised Uniform Arbitration Act (2000)), will designate and appoint an arbitrator.

1.3 Article 9 of the Uniform Commercial Code: Revised Article 9 of the Uniform Commercial Code 1999 Official Text promulgated and approved by the National Conference of Commissioners of Uniform State Laws and the American Law Institute and the comments thereto, as adopted in the jurisdiction whose law is selected or determined to govern the particular issue.

1.4 Award: The final award issued by the Arbitrator in an arbitration proceeding under these Model Rules.

1.5 Base Rules: The commercial arbitration rules selected by the parties to govern the arbitration of disputes as set forth in the arbitration clause or other agreement providing for arbitration.²³

1.6 Commercial Finance Dispute: Unless otherwise defined by the parties in the Arbitration Agreement, the term “Commercial Finance Dispute” shall mean any and all disputes between or among the parties, whether arising in contract, tort or by statute, arising from or related to Finance Agreements and any conduct arising from or related to such Finance Agreements, provided that application of these Model Rules is agreed upon by the parties and that any such disputes are not Consumer Disputes.

²³ See the comment relating to selection of base rules and the effect of failure to select base rules in footnote 22.

Commentary

The arbitration clauses and rules of some parties and providers attempt to limit the kinds of transactions that may be the subject of arbitration. The effect of these clauses is to bind the borrower to arbitrate any claim for monetary relief against a lender while allowing the lender to pursue any and all remedies against a borrower or guarantor in any forum it chooses and requiring the parties to go to a court for specific performance or other non-monetary relief. It is no surprise that these provisions, in particular, and use of arbitration, in general, are often contested by borrowers and their counsel²⁴. This clause provides a more ‘standard’ and even-handed approach to arbitration of these disputes – permitting arbitrators to hear and determine all disputes relating to the commercial finance agreements and to fashion relief accordingly. These Model Rules also expand the range of disputes which might be the subject of arbitration, including disputes involving transactions under participation and syndication agreements, intercreditor agreements and swap and derivative agreements – provided that they are agreed upon by the parties and are not consumer transactions. Since many of these Model Rules were drafted assuming that a dispute would involve a commercial finance transaction, the parties should evaluate whether these Model Rules should be made applicable to particular situations.²⁵

The scope of the term “Commercial Finance Dispute” should be interpreted broadly to include all controversies or claims between or among the parties relating to lending, borrowing, leasing or other financing transactions between or among them, or the negotiation or closing of these transactions, whether or not such loans, borrowing, leasing or other financing transactions or negotiations were consummated or completed before or after the date of the Arbitration Agreement; provided, however, that such transactions were permitted in or by the Finance Agreements or contemplated therein. The parties may agree that these Model Rules shall govern, and in such case the term “Commercial Finance Dispute” will include, in addition to lending, borrowing and

²⁴ A question may also arise as to whether clauses that go too far are illusory and will not be given effect. See, for example, *Stevens/Leinweber/Sullens, Inc. v. Holm Development and Management, Inc.*, 165 Ariz. 25, 795 P.2d 1308 (1990), in which a unilateral right for one party to compel or to reconsider arbitration was held to be unenforceable for lack of mutuality – cases are split on the consideration argument used in this case, but it illustrates the reluctance of courts to enforce one-sided agreements.

²⁵ For example, the 2002 Master Agreement promulgated by the International Swaps and Derivative Association, Inc. provides for jurisdiction in the courts of England if the agreement is governed by English law and in the courts located in the State of New York if New York law governs the agreement. Such choice of forum clauses are generally enforceable -- see *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972) A judgment rendered in either of these courts may not be recognized or enforced in the other country – however an arbitration award would be recognized and enforceable under the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. This Convention became effective for the United Kingdom on December 23, 1975 and for the United States on December 29, 1970, which means it became operative between the two countries on December 23, 1975. Enforcement of arbitral awards is by summary procedure in both the United States and England. Therefore an arbitration clause in this context would be advisable.

lease transactions, disputes relating to sales and purchases of, or participations in, or syndications of, loans under Finance Agreements, as well as intercreditor agreements, interest rate and credit swap agreements and other agreements relating to commercial loans, provided that application of these Model Rules is agreed upon by the parties and that any such disputes are not Consumer Disputes.

Joint Committee Revision Notes

*The consensus of the joint Committees was to make the definition of Commercial Finance Dispute as simple and as broad as possible, with discussions of the intended broad scope and potential uses left to the Commentary. One commentator suggested that the United States Supreme Court decision in **Shearson/American Express, Inc. v. McMahon**, 482 U.S. 220, 107 S.Ct. 2332, 96 L.Ed.2d 185 (1987) might limit the ability to use arbitration to vindicate statutory rights in such matters as secured transactions involving multiple parties and replevin and foreclosure statutes and suggested that affirmative ‘carve outs’ for these transactions should be provided in these Model Rules. Some debate ensued in the Committee over whether or not the **McMahon** case required such a result. Since these Model Rules are applicable to a wide variety of transactions, including unsecured transactions and since multiple party cases are routinely handled in arbitration matters, these Model Rules were not modified to require any form of mandatory ‘carve out’. Practitioners should evaluate the applicability of **McMahon** and other case law to determine whether limitations on the ability to adjudicate specific disputes under their specific circumstances might make the arbitration mechanism (or any other contractual limitation of substantive rights) fail.*

1.7 Consumer Dispute: Any controversies or claims between or among the parties wherein the transaction which is the subject of the dispute is: (a) providing financing to or another transaction with a natural person primarily for personal, family or household purposes; (b) a “consumer transaction” as defined in Article 9 of the Uniform Commercial Code; or (c) a “consumer-goods transaction” as that term is defined in Article 9 of the Uniform Commercial Code.

Joint Committee Revision Notes

The consensus of the joint Committees was to clean up and simplify this definition.

1.8 Finance Agreements: Unless otherwise limited by the parties in the Arbitration Agreement, the term Finance Agreements shall mean: (a) the loan or financing agreements, or other agreements that are the subject of the Arbitration Agreement between or among the parties to the Arbitration Agreement; (b) any security agreements or documents relating thereto providing for any security for the payment or performance of an obligation, including, without limitation, guaranty agreements by or among parties to the Arbitration Agreement; and (c) any

other documents related to any of the foregoing documents (including, but not limited to, any renewals, extensions or modifications of such agreements).

Commentary

The definition of Finance Agreements is broad enough to encompass any and all documents and other agreements evidencing the agreements or rights of the parties in arbitration relating to a commercial finance transaction. This definition will also allow agreements among creditors or other parties relating to loan transactions to be the subject of these Rules even if they are not strictly financing agreements – for example to settle disputes among co-creditors under intercreditor agreements or among lender participants or purchasers of loan transactions under syndication, swap or purchase and sale agreements – provided that such agreements are the subject of the Arbitration Agreement and are not consumer transactions. Finance Agreements might also include agreements with third parties (for example, investment security control agreements or escrow agreements) that are not parties to the arbitration – however, these model rules cannot alter the fact that the arbitration proceeding cannot bind one that is not a party to the arbitration agreement or that did not consent to participate in the arbitration proceeding. Therefore, although guaranty agreements by third parties may be considered “Finance Agreements” under this definition, third party guarantors cannot be bound by an arbitration award unless they have consented to arbitration, whether by an arbitration clause in the guaranty agreement or by a consent to arbitrate after a dispute has arisen.²⁶

Joint Committee Revision Notes

The consensus of the joint Committees was to change this definition from the term “Loan Agreements” to reflect the fact that it relates to a broader range of documents and transactions than simply loan agreements. Also, they felt that examples of what transactions might be included should be left to the Commentary and not included in the text of the Model Rules.

1.9 Model Rules: The supplementary arbitration rules set forth herein.

1.10 Service Provider: The person or organization, or the authorized representative of an organization, selected by the parties in the Arbitration Agreement, whether directly or pursuant to the provisions of the Base Rules, to administer the arbitration proceeding using the Base Rules. In the event of the appointment of the Arbitrator by a court and if the parties have not specified a Service Provider, the Service Provider shall be the person or organization, if any,

²⁶ See Section 11.0 of these Model Rules relating to consolidation of arbitration cases. Although one might expect that it would be most efficient to determine the rights of the obligors and guarantors in one arbitration proceeding, unless care is taken in the drafting of arbitration clauses in each of the loan documents this option might not be available.

selected by the court or other appointing authority to perform such functions, and, if none is selected the Arbitrator shall be the Service Provider.

1.11 Statement of Amount In Demand: The statement by a party of its good faith estimate of the monetary amount of any claim or counterclaim or a designation that the relief sought is not monetary as set forth in Section 4.0 of these Model Rules.

2.0 Governing Rules:²⁷

The parties to a Commercial Finance Dispute shall be deemed to have made these Model Rules a part of their arbitration agreement whenever they have specified in the Arbitration Agreement that these rules shall apply, in which case, unless otherwise specified in the Arbitration Agreement, these Model Rules shall apply in the form in effect at the time the arbitration is commenced. To the greatest extent possible these Model Rules shall be interpreted to be consistent with the Base Rules and in the event of any irreconcilable inconsistency between these Model Rules and the Base Rules the provisions of these Model Rules shall prevail.

Commentary

Practitioners should note that these Model Rules neither are a complete set of rules for the conduct of an arbitration case nor contain all of the terms and provisions that should be included in an Arbitration Agreement. Consequently, practitioners are advised to include in the Arbitration Agreement adopting these Model Rules, among other things, a designation of the Base Rules to be employed, a designation of any Service Provider and a designation of the governing law for the transaction to be applied by the Arbitrator.

Joint Committee Revision Notes

The consensus of the joint Committees was to provide that if the parties did not specify otherwise in their Arbitration Agreement the designation of governing Model Rules should be those in effect on the date that the arbitration proceeding is commenced.

3.0 Non-Applicability to Consumer Disputes:

These Model Rules shall not apply to a Consumer Dispute. If these Model Rules are specified in an Arbitration Agreement relating to any Consumer Dispute the parties shall be deemed to have agreed to arbitration pursuant only to the Base Rules.

²⁷ Arbitration rules adopted by reference in commercial contracts are as effective as if fully recited in the arbitration agreement. *P&P Indus., Inc. v. Sutter Corp.*, 179 F.3d 861 (10th Cir., 1999).

Commentary

These rules are only intended for the determination of commercial finance disputes. Consequently, customary provisions in consumer law arbitration rules have not been provided in these Model Rules and they should not be used to determine consumer disputes. These rules are made expressly inapplicable to, and will be void if included in arbitration agreements relating to, consumer transactions. Reference to ‘consumer transactions’ and ‘consumer goods transactions’, as defined in Article 9 of the Uniform Commercial Code, are used in Section 1.7 to define a “Consumer Dispute” that is excluded from arbitration under these Model Rules.

4.0 Commencement of Arbitration and Counterclaims – Statements of Amounts in Demand:

In the event that the Base Rules do not provide a corresponding requirement, any written notice by a party giving notice of a claim or a counterclaim, and any notice of any new or different claim or counterclaim, pursuant to the Base Rules shall include a statement of such party’s good faith estimate of the monetary amount of such claim or a designation that the relief sought is not monetary. The Statement of Amount in Demand by a party under these Model Rules shall not limit the amount or nature of the relief that may be granted by the Arbitrator; however, the parties, the Service Provider and/or the Arbitrator may rely upon the Statements of Amount in Demand in determining the number of arbitrators and the applicability of the provisions in Section 5.0 of these Model Rules to ‘opt-out’ of arbitration under these Model Rules. In the event the Arbitrator determines that the Statement of Amount in Demand by any party was incorrect, was not provided in good faith and caused increased costs to another party in the arbitration, the Arbitrator may include it its Award appropriate sanctions for such conduct as may be provided in the Base Rules.

Commentary

As an administrative matter, the parties are required to provide a good-faith estimate of their monetary claims. This is needed for the ‘opt-out’ option for de minimus claims and to allow the Service Provider to know whether a three-arbitrator panel might be required. The estimate of monetary claims does not constrain the amount that may be recovered by a party. Fee- and cost-shifting provisions have been included, however, to allow the arbitrator to compensate an injured party for increased costs if the Arbitrator finds that an incorrect estimate was provided in bad faith. Most arbitration service providers require similar disclosures for administrative purposes (and to set their fees) from all parties making an affirmative claim– in which case these estimates may be used for the purposes of this Section.

Joint Committee Revision Notes

There was considerable and ongoing discussion of the need for such a statement and the wisdom of the 'opt-out' provision and the provision allowing an arbitrator's award to exceed the amount of the initial demand. The Committee desired for this definition to be amended and left open for further discussion.

5.0 Small Matter "Opt-Out" of Arbitration:

Unless otherwise provided in the Arbitration Agreement, if the Statements of Amount in Demand sent by all parties requesting monetary relief show that no party is claiming in excess of one hundred thousand dollars (\$100,000.00) from any other party to the arbitration, any party to the arbitration may, by written notice sent within fourteen (14) days after the Statement of Amount in Demand by the last party filing a monetary claim is received by the Service Provider, terminate the arbitration under these Model Rules. Unless otherwise provided in the Arbitration Agreement upon such termination of the arbitration under these Model Rules the arbitration shall proceed pursuant to the Base Rules. The written notice of election under this Section to terminate the arbitration under these Model Rules shall be sent to the Service Provider if an Arbitrator has not yet been appointed and shall be sent to the Arbitrator and to the Service Provider if an arbitrator has been appointed. In the event that the written notice of termination is not sent within said fourteen (14) day period (time being of the essence with respect to such time limit), this option to terminate the arbitration under these Model Rules shall lapse and terminate and the arbitration shall proceed pursuant to the Base Rules and these Model Rules. Notwithstanding a timely termination of the arbitration proceeding pursuant to this Section 5.0, the fees and costs owing to the Service Provider, and the fees and costs owing to the Arbitrator accrued up to the date such notice of termination is received by the Service Provider and/or the Arbitrator, shall be due and payable by the parties notwithstanding such termination.

Commentary

There is a point where a de minimus claim should not require the time and expense of arbitration under these Model Rules – particularly in light of the increased requirements for Awards and appeal rights set forth herein. These Model Rules allow any party to 'opt out' of arbitration under these Model Rules if the amount of the estimated claim of any party does not exceed \$100,000.00. In this case, unless the parties provide otherwise in their Arbitration Agreement, the arbitration shall proceed under the specified Base Rules. Of course, this 'opt out' trigger can be adjusted, or the 'opt-out' eliminated entirely, in the arbitration agreement. The parties could also agree to resort to court litigation, as an alternative to arbitration under the Base Rules, if they expressly provide for this contingency in the arbitration clause.

Joint Committee Revision Notes

The consensus of the joint Committees was to provide that the effect of the small matter 'opt-out' would be to allow the arbitration of the dispute under the specified Base Rules, since the parties had agreed upon arbitration in the first instance, unless the Arbitration Agreement provides otherwise.

6.0 Qualifications of the Arbitrator(s):

The arbitrators acting as Arbitrator under the Base Rules and these Model Rules shall be impartial and independent and shall be subject to disqualification as provided in the Base Rules.²⁸ Unless the parties have expressly specified another method of selection or qualifications in the Arbitration Agreement, the Arbitrator shall have demonstrated knowledge and experience in commercial finance transactions. In the event that a panel of more than one arbitrator is appointed, at least one member of the arbitration panel is required to have such demonstrated knowledge and experience in commercial finance transactions. The parties to an arbitration case under these Model Rules shall notify the Service Provider of any objections to the Arbitrator or members of any arbitration panel promptly within the time specified for any such challenges under the Base Rules.

Commentary

Specific qualifications or expertise requirements for arbitrators are not required under most arbitration rules unless incorporated into the arbitration agreement or agreed upon by all of the parties. The qualifications and knowledge of an arbitrator are particularly important in Commercial Finance Disputes and are a constantly mentioned concern of the finance industry. This provision requires an arbitrator (or at least one member of a multi-arbitrator panel) with knowledge and experience in such transaction – consistent, of course, with the requirement that the arbitrators be impartial and independent. Fellows of the American College of Commercial Finance Lawyers and membership on rosters of arbitrators with similar qualifications prepared by a service provider are deemed to have these credentials. For example, the American Arbitration Association has established a National Roster for Commercial Finance Disputes of qualified arbitrators for such disputes.

Some arbitration practitioners have suggested that the chairperson of an arbitration panel should be an attorney, and, if possible, an attorney admitted in the jurisdiction of the forum where the arbitration will be conducted. This

²⁸ Awards may be vacated if they result from arbitrators that violate the 'evident partiality' standard of the Federal Arbitration Act (Title 9, U.S. Code §10) or §23 of the Revised Uniform Arbitration Act (2000). Arbitrators are required to disclose potential conflicts and much litigation has ensued over the level of disclosure required and degree of partiality to vacate an award. See, for example, *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145, 85 S. Ct. 337, 21 L.Ed.2d 301 (1968) and the many resulting cases.

draft does not require such a designation, particularly since the forum of the arbitration may not be apparent at the time that the arbitrators are selected. This issue has been left for discussion in the formulation of the final Model Rules.

Joint Committee Revision Notes

The consensus of the joint Committees was to move to the Commentary the examples of minimum qualifications for arbitrators to achieve the “demonstrated knowledge and experience” standard for arbitrators under these Model Rules. The provision requiring arbitrators to be ‘neutral’ was thought by the Committee to be redundant with the Base Rules and was deleted. The Committee also recognized that an experienced commercial finance arbitrator may not have the most experience or qualifications to rule on evidentiary matters or other hearing details, so it is only required that an experienced commercial finance arbitrator be a member of a multi-arbitrator panel, not necessarily the Chair. The provision for appeal from the designation of arbitrators was added at the request of the Committee, however, such matters should be left to the Base Rules, and there is a serious question as to whether this provision is necessary in these Model Rules.

7.0 Number of Arbitrators:

Unless otherwise provided in the Arbitration Agreement, all claims shall be determined by one (1) arbitrator; however, if the Statements of Amount in Demand indicate that the good faith estimate of the monetary amount of the claim of any party exceeds five million dollars (\$5,000,000.00) (or such other amount as may be specified by the parties in the Arbitration Agreement), upon the written request of any party received by the Service Provider prior to the appointment of an Arbitrator, the Commercial Finance Dispute shall be determined by a panel of three (3) arbitrators.

Commentary

These model rules adopt a threshold standard of \$5 million before the expense of three (3) arbitrators is required and selection of three arbitrators must be requested by one of the parties. This limit was selected to avoid burdening relatively small cases with additional costs. Of course, these limits can be modified in specific arbitration proceedings by agreement of the parties or, in advance for specific transactions, in the Arbitration Agreement.

Joint Committee Revision Notes

The joint Committees had considerable discussion over the ‘trigger’ amount for a three (3) arbitrator panel. The consensus was to leave this amount as a ‘place holder’ for further discussion, and with the express statement that the

parties are free to modify this trigger amount in their Arbitration Agreement. The reference to ‘neutral’ arbitrators was also deleted pursuant to the Committee comment in the Note to Section 6.0.

8.0 Power of Arbitrators to Determine Jurisdiction:

In addition to any authority of the Arbitrator under the Base Rules, the Arbitrator shall have the power to rule on all issues, claims, defenses, questions of conflicts of law, questions of arbitrability and objections relating to the existence, scope and validity of the Finance Agreements, contract, transaction or relationship of the parties to the arbitration. Without limiting the foregoing, the Arbitrator shall have the power to rule on all issues, questions of arbitrability and proper parties to the arbitration proceeding, including, without limitation, objections relating to jurisdiction, contract law and enforceability of the Arbitration Agreement.²⁹ The Arbitrator may rule on such matters either as preliminary matter or in the final Award.

Commentary

These Model Rules attempt to give the arbitrator the greatest permissible breadth of authority to determine questions of existence, scope and validity of the Financing Agreements and the Arbitration Agreement. The omission of any particular legal theory or issues in the list does not imply that they are excluded. For example, a determination of unconscionability is not listed but matters of unconscionability of a contract or clause may be determined by an arbitrator in a particular case under applicable law – such as, for example, Section 2-302 of the Uniform Commercial Code relating to a contract for the sale of goods.

Joint Committee Revision Notes

The joint Committees were of the opinion that under applicable law in the United States the question of the ‘unconscionability’ of an arbitration clause or other Arbitration Agreement itself would not be a matter to be determined by an arbitrator, but was part of the determination by a court relating to the effectiveness of an Arbitration Agreement, so the reference was deleted. An arbitrator may, however, determine unconscionability in the context of the effectiveness of a specific contract or term under specific applicable statutory law, so a comment was added to make this clear.

²⁹ If a challenge is brought to the enforceability of an agreement of which an arbitration clause is a part, as opposed to a challenge specifically to the arbitration clause itself, the enforceability issue is for the arbitrator to decide. *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 315 (1967) (under the Federal Arbitration Act – and incorporated into §6 of the Revised Uniform Arbitration Act (2000)). The court, however, must decide challenges to the arbitration clause itself or whether or not the particular controversy is subject to an arbitration clause. §6 Revised Uniform Arbitration Act (2000).

9.0 Conformity to Law:

9.1 Required Application of Substantive Law: The Arbitrator shall give effect to the applicable substantive law applied to the facts that it shall find and may grant any legal, equitable or other remedy or relief provided by law in deciding a Commercial Finance Dispute.

Commentary

A number of arbitration rules, such those of the AAA and JAMS, only require the arbitrator to grant relief that the arbitrator deems ‘just and equitable’. In Commercial Financial Disputes, however, most disputes are governed by an extensive and well-litigated code (for example, the Uniform Commercial Code) on which lenders and borrowers have relied in entering into their transaction. These Model Rules require the Arbitrator to give effect to the applicable substantive law to determine the Commercial Finance Dispute and a right of appeal for matters of substantive law has been provided in Section 17.0.

9.2 Effect of Statutes of Limitations: The Arbitrator shall give effect to statutes of limitation in determining any Commercial Finance Dispute and may dismiss the arbitration proceeding on the basis that the Commercial Finance Dispute is barred. For purposes of determining the application of any statute of limitations, the receipt of the written notice of an arbitration claim by the Service Provider shall be the equivalent of the commencement of an action or proceeding in court. Notwithstanding the foregoing sentence, in the event of any earlier commencement of an action or proceeding in a court of competent jurisdiction on such Commercial Finance Dispute prior to an order of such court to proceed with the arbitration of the Commercial Finance Dispute, the date of commencement of such earlier action or proceeding shall be used in such arbitration to determine any statute of limitations issue.

9.3 Conformity to Privilege Rules: Although the Base Rules may not require strict conformity to the rules of evidence, the Arbitrator shall give effect to applicable law relating to privileges and work product.

10.0 Provisional and Self-Help Remedies:³⁰

10.1 Self-Help and Interim Remedies Generally Permitted: Unless otherwise expressly provided in the Arbitration Agreement, stayed by the Arbitrator pursuant to these Model Rules or enjoined by a court, any party to the arbitration of a Commercial Finance Dispute under these Model Rules may, at any time or from time to time: (a) exercise self-help

³⁰ Courts are divided over whether a provisional remedy such as an injunction may issue under the Federal Arbitration Act. Section 8 of the Revised Uniform Arbitration Act (2000) specifically permits the court or the arbitrator to issue such interim remedies. The Revised Uniform Arbitration Act, however, does not expressly authorize an arbitrator to issue a stay to restrain a party from exercising a self-help or interim remedy – such matters are best addressed by a court.

remedies, if permitted by applicable law, including, but not limited to, setoff, or recoupment, repossession or collection of collateral or the protection and preservation or liquidation and realization of collateral; (b) exercise any judicial or power of sale rights to realize upon any collateral; and (c) institute and maintain an action for judicial relief in a court of law to obtain an interim remedy (such as, but not limited to, injunctive relief, writ of possession, attachment, appointment of a receiver or other provisional or supplementary remedies) prior to the issuance of an Award by the Arbitrator. The institution or maintenance of an action for judicial relief, or other pursuit of the self-help or interim remedies as provided herein, shall not constitute a waiver of the right or obligation of the plaintiff seeking such remedies, or of any other party, to submit the Commercial Finance Dispute to arbitration pursuant to the Arbitration Agreement. The result of any such self-help or interim remedy or the application of any proceeds from such remedy may be considered by the Arbitrator in its Award.

Joint Committee Revision Notes

The joint Committees felt that the Arbitrator should not have the authority to issue an order to a party not to proceed with a self-help or interim remedy. The Committees felt that this was a matter best determined by a Court and a reference to this fact was added to a footnote.

10.2 Determination by Arbitrator of Provisional Remedy: Unless otherwise provided in the Arbitration Agreement, the Arbitrator may, upon the written request of a party to the arbitration, take whatever interim measures and grant whatever interim or provisional remedy, including requiring a bond or other security, as the Arbitrator may deem appropriate; provided that such interim measures are permitted under the Base Rules and under the law governing the arbitration proceeding and, if different, the jurisdiction where the provisional remedy would be implemented.

11.0 Consolidation of Arbitration Cases:

Intentionally Omitted.³¹

Joint Committee Revision Notes

After considerable discussion the joint Committees felt that the matter of consolidation, whether substantive consolidation of claims or merely for purposes of trial, is unsettled and is a matter that should be addressed by the Base Rules and applicable law, not in these Model Rules.

³¹ Consolidation is permitted under §10 of the Revised Uniform Arbitration Act (2000) if the conditions set forth therein are satisfied.

12.0 Punitive Damages:

Unless otherwise expressly provided in the Arbitration Agreement, the Arbitrator may not award punitive damages or other exemplary relief unless such an award is expressly authorized by statute applicable to the Commercial Finance Dispute for a civil action in court involving the same claims and facts and the facts found by the Arbitrator justify the award under said statute.

Commentary

Some arbitration rules, such as the AAA Commercial Financial Disputes Arbitration Rules, attempt to restrict the ability of the arbitrator to award punitive or exemplary damages. Although the United States Supreme Court has permitted the arbitration of antitrust and RICO cases notwithstanding a limitation on punitive damages, the court took a ‘wait and see’ attitude to determine whether or not arbitration would impermissibly impair the rights of the parties in particular cases.³² In addition, provisions of the Uniform Commercial Code, which will govern most Commercial Finance Disputes, expressly authorize the awarding of statutory fines, penalties or damages in commercial cases under particular circumstances.³³ The lesson is to avoid the issue by allowing the arbitrator to grant relief expressly permitted by statute. To obtain punitive or exemplary relief in an arbitration award under these Model Rules both the relief must be granted by statute and the facts found by the arbitrator must justify the relief if the case had been brought in a court applying the same substantive law.

Joint Committee Revision Notes

The joint Committees wished to make clear that these Model Rules do not authorize punitive or exemplary relief unless it is authorized by the substantive statutory law applicable to the case if it had been brought in court.

13.0 Class Actions:

Intentionally Omitted.

³² See, for example, *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 107 S. Ct. 2332, 96 L.Ed.2d 185 (1987) (RICO claim and claim under §10b of Securities Act may be arbitrated), *Pacificare Health Systems, Inc. v. Book*, 538 U.S. 401, 123 S. Ct. 1531, 155 L.Ed.2d 578 (2003) (allowing RICO case to be arbitrated despite argument that arbitration clause limited award of treble damages) and *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 105 S. Ct. 3346, 87 L.Ed.2d 444 (1985) (permitted arbitration of case arising under antitrust laws).

³³ See, for example, UCC §9-625 (permitting award of consequential damages resulting from inability to obtain financing as the result of secured party’s misconduct and imposing a statutory fines of \$500 for secured party’s failure to take certain actions).

Joint Committee Revision Notes

After considerable discussion the joint Committees felt that the matter of class actions is unsettled and is a matter that should be addressed, in the same manner as for consolidation of actions, by the Base Rules and applicable law, not in these Model Rules.

14.0 Effect of Mediation:

Unless expressly and clearly stated otherwise in the Arbitration Agreement, and notwithstanding the exercise of any right of negotiation or mediation pursuant to the Base Rules, the Loan Documents or the Arbitration Agreement, any party to a Commercial Finance Dispute may commence an arbitration proceeding pursuant to the Base Rules and these Model Rules at any time, regardless of whether or not said negotiation or mediation has been completed or terminated, and completion or termination of said negotiations or mediation shall not be a condition precedent to the commencement of an arbitration proceeding under the Base Rules and these Model Rules.³⁴ Determination as to whether any such express condition exists in the Arbitration Agreement and whether any such condition has been fulfilled is a matter for determination by the arbitrator in an arbitration proceeding under these Model Rules and the arbitrator shall have jurisdiction and authority both to make such determination and to fashion a remedy, such as a limited stay of the arbitration proceeding, if the arbitrator determines that such a condition exists and has not been fulfilled.

Commentary

These Model Rules require an arbitration clause to be very clear as to whether any negotiation, mediation or other condition precedent in the agreement bars the filing an arbitration case. Unless such intent is clear these Model Rules will allow the filing and determination of the arbitration case. These Model Rules also make clear that the arbitrator has the jurisdiction to determine whether any such condition precedent exists and has been satisfied and to fashion a remedy to avoid waste and potential for delay if the arbitrator finds that any such condition has not been satisfied. A stay of the arbitration proceeding until fulfillment of any such condition is provided as an example of one potential remedy – to avoid the delay inherent in commencing a new arbitration proceeding, selection of arbitrator and other waste if the Commercial Finance Dispute is not resolved when the condition for continuation of the arbitration proceeding is ultimately satisfied.

³⁴ This provision is intended to limit the problems noted in recent cases caused by unclear drafting.

Joint Committee Revision Notes

The joint Committees wished to make very clear that the arbitrator under these Model Rules has the jurisdiction to determine whether any conditions to commencement or continuation of the arbitration proceeding exist and that the arbitrator would have the authority to fashion an appropriate remedy, such as a stay of the arbitration proceeding until fulfillment of any such condition that the arbitrator may find has not been satisfied.

15.0 Award Requirements:

15.1 Statement of Facts and Conclusions of Law Required: In the event the Arbitration Agreement provides for an appeal under Section 17 of these Model Rules, the Award by the Arbitrator shall include a written statement of the findings of material and relevant facts found by the Arbitrator and a statement of the application of the applicable substantive law to said facts that support the Award. If the Arbitration Agreement does not provide for an appeal under Section 17 of these Model Rules the Award by the Arbitrator shall be in form and content as required by the Base Rules.

Commentary

Unless required by an arbitration agreement, reasoned awards are generally not required in arbitration matters. To permit an effective appeal of matters of law allowed under these Model Rules in Section 17.0 if the parties ‘opt-in’ to the appeal provisions in the Arbitration Agreement, however, the Award should include a statement of the facts found by the arbitrator and the application of the applicable substantive law to the facts found. No appeal is permitted within the arbitration proceeding under these Model Rules for matters of fact determined by the arbitrator; however to correct any error that the appeal panel may find in the arbitrator’s interpretation or application of the substantive law an appeal panel will have to know what those facts are, in order to apply the correct law to the facts of the dispute found by the arbitrator. Since the appeal provisions of these Model Rules are not applicable unless the parties have agreed to them in the Arbitration Agreement, unless the parties have elected for the appeal provisions to be effective the requirement of statements of fact and conclusions of law will not be required and the form of the Award will be the same as the requirements for such Awards under the Base Rules.

Joint Committee Revision Notes

The Committees felt strongly that the appeal provisions and the additional requirements under these Model Rules to support such appeals should not be applicable until and unless the parties expressly agreed to ‘opt-in’ to the appeal provisions in the Arbitration Agreement. The draft of the Model

Rules has been revised to make the additional requirements inapplicable unless the parties so ‘opt-in’.

15.2 Timing of Award: Unless otherwise agreed by all of the parties to the arbitration proceeding or specified by law, the Arbitrator shall make the award promptly, no later than thirty (30) days after the arbitration hearing is closed, subject to any provisions in the Base Rules for reopening and reclosing of hearings.

15.3 Power of Arbitrators in Award: Notwithstanding anything to the contrary set forth in the Base Rules, except as may be expressly set forth in the Arbitration Agreement or in these Model Rules, the Arbitrator may grant any remedy or relief that the Arbitrator finds is in accordance with the applicable substantive law governing the Commercial Finance Dispute, including, without limitation, damages, injunctive relief and specific performance. The Arbitrator may also award and apportion fees, expenses and compensation related to the Award and attorney’s fees and costs as provided in the Base Rules, the Finance Agreements, the Arbitration Agreement and under the applicable substantive law governing the Commercial Finance Dispute.

Commentary

Some arbitration rules, such as the AAA Commercial Financial Disputes Arbitration Rules, attempt to restrict the ability of the arbitrator to award specific performance or injunctive relief. However, provisions of the Uniform Commercial Code, which will govern many Commercial Finance Disputes, expressly authorize the awarding of specific performance and injunctive relief in commercial cases under particular circumstances.³⁵

16.0 Confidentiality of Awards:

Unless otherwise expressly stated in the Arbitration Agreement or otherwise agreed by all parties to the arbitration proceeding, confidentiality of Awards shall be as provided in the Base Rules. If Awards are not to be confidential the Service Provider may publish or distribute written Awards under these Model Rules or may provide copies of such Awards to publishers of case decisions for publication. Notwithstanding that any Awards are not to be confidential the Service Provider may redact the names of the parties, or other references that might identify the parties, in such Awards, however, unless otherwise provided in the Arbitration Agreement, the Service Provider shall not be required to redact such names or references.

³⁵ See, for example, UCC §2A-507A (specific performance permitted for delivery of unique leased goods or “in other proper circumstances”); UCC §5-111(a) (allowing specific performance against an issuer of a letter of credit for a non-monetary obligation); UCC §9-601(a)(1) (permitting a secured party to obtain a judgment or enforce the security agreement by “any available judicial procedure”); UCC §9-625(a) (permitting a court to order or restrain collection, enforcement or disposition of collateral in event of secured party’s misconduct) and UCC §9-627(c) (making collection, enforcement, disposition or acceptance of collateral approved in a judicial proceeding commercially reasonable).

Commentary

Some arbitration rules provide that arbitration proceedings and awards are confidential and may not be disclosed by the parties, the service provider or the arbitrator unless necessary for enforcement of the award or if disclosure is required by law. This provision makes clear that, in the absence of an agreement to the contrary by the parties, confidentiality of arbitration awards shall be governed by the Base Rules. Of course, the parties are free to waive confidentiality in particular transactions by including an “opt-out” of the confidentiality provisions in the arbitration agreement. Whether or not the parties decide to waive confidentiality, however, the Service Providers may redact the names or other references that might identify the parties in accordance with their usual procedures, but are not required to do so unless expressly set forth in the Arbitration Agreement.

Joint Committee Revision Notes

The Exposure Draft of the Supplementary Arbitration Rules provided that awards would not be confidential. The Exposure Draft provided that unless the parties “opt in” to confidentiality, awards would not be confidential and may be disclosed to reporting companies. The theory for this change was that publication of the reasoned awards required pursuant to these Model Rules would assist in the development of commercial law and is customary for commercial disputes. The non-confidentiality of the award under the Exposure Draft of the Model Rules, however, was a matter of substantial controversy in the joint Committees. The arbitrator and service company representatives that participated in the Committees felt that this is a major change and felt that this should be revised to require confidentiality of awards unless the parties expressly agree to “opt out” of confidentiality – to conform to the treatment under most Base Rules. The Committee ultimately provided for a return to the usual confidentiality rules in this Final Draft.

17.0 Appeal of Legal Matters:³⁶

If expressly stated in the Arbitration Agreement, the following appeal provisions in Sections 17.1 through 17.7 of these Model Rules shall be applicable to Awards rendered

³⁶ The question of whether parties may contract for expanded judicial review or modify the standards for judicial review under the Federal Arbitration Act was considered by the Supreme Court in the case of *Hall Street Associates, LLC v. Mattel, Inc.*, 552 U.S. 576, 128 S. Ct. 1396 (2008). In *Hall* the Supreme Court found that the parties could not alter, by contract, the standards for judicial review of an arbitration award once the arbitration was over. These Model Rules create a limited right of appeal within the arbitration forum and before an Award becomes final and subject to the rights of review by a court of the underlying arbitrator decision and of any revision by the appeal panel under the court’s normal review standards. Therefore, this Supreme Court decision should not affect the appeal rights in these Model Rules or later review or enforcement of the final Award by a court.

pursuant to these Model Rules. If the appeal provisions in this Section 17 of these Model Rules are not authorized by the parties in the Arbitration Agreement, the Award of the Arbitrator shall be governed in accordance with the provisions of the Base Rules.

17.1 Delayed Effectiveness of Award and Appeal; Appeal Deadline: An Award by an Arbitrator pursuant to these Model Rules shall not be final and may not be enforced by any party to the arbitration proceeding until the expiration of fifteen (15) days after the Award has been sent to the parties; provided that if said expiration date falls on a weekend or holiday that is not a business day of the Service Provider, the deadline date shall be extended to the end of the next following business day of the Service Provider (the “**Appeal Deadline**”). If, prior to the Appeal Deadline, the Service Provider receives a notice of appeal satisfying the requirements of Section 17.2 the Service Provider shall notify the other parties and the Arbitrator of such appeal. Upon receipt of such timely notice of appeal and notification thereof to the parties the Award shall not become final for purposes of judicial enforcement or modification under the Base Rules until or unless the Award is affirmed or modified by the Appeal Panel pursuant to Section 17.5 or all appeals are dismissed pursuant to Section 17.3. By filing or defending any appeal pursuant to these Model Rules a party does not waive any right to claim that the Award should be vacated pursuant to applicable statutory law.

Commentary

These Model Rules do not provide for an automatic appeal process that is unless the parties expressly authorize them in the Arbitration Agreement. If the parties elect not to ‘opt in’ to these appeal provisions a number of the provisions of these Model Rules that support the appeal right (such as the delayed effectiveness of the Award and the enhanced requirements for Awards) are no longer necessary. Therefore, these other sections provide that these additional requirements will not be applicable unless the parties expressly adopt these appeal provisions. As part of this appeal right an Award by an arbitrator under these Model Rules will not be final and may not be enforced for a period of fifteen (15) days after it is sent to the parties. If a notice of appeal is received the Award does not become final until it is affirmed or a modified Award is entered at the conclusion of the appeal process. These Model Rules also make clear that by participating in an appeal a party does not lose the right to later claim that an Award should be vacated for misconduct under governing statute – this is due to the fact that the appeal rights under these Model Rules are limited to matters of applicable law and do not reach issues of misconduct in the proceeding that would cause a court to vacate an Award.

Joint Committee Revision Notes

Considerable discussion occurred over these appeal provisions. Experienced arbitrator members of the Committees expressed their strong opinions that these appeal procedures: (a) delay the finality of the arbitration process; (b) require arbitrators to research the applicable law and additional

arguments -- unless they are expressly permitted to rely upon the arguments presented to them by the parties; (c) increase the costs of the arbitration, since a transcript will likely be required by arbitrators in order to render a reasoned opinion; (d) provide a standard that a court might try to second-guess under a “manifest disregard of the law” theory (although this theory under the FAA is now suspect after the case of Hall Street Associates, LLC v. Mattel, Inc., 552 U.S. 576, 128 S. Ct. 1396 (2008)); (e) allow mischief since the losing party will always appeal to delay the Award against it. These experienced arbitrator members of the Committee felt that these appeal procedures should not automatically be applicable unless the parties expressly “opt-in” to them. After considerable discussion the Committees determined that the provisions of the earlier draft Model Rules, which provided that the appeal provisions would be mandatory unless the parties “opt-out”, should be revised to not require the appeal provisions to be applicable unless they are expressly authorized in the Arbitration Agreement. The Committee felt that the requirement that the parties “opt-in” to the appeal provisions should be provided in the exposure draft for comment and that the Committees should consider deleting or revising them only after comments are received from the commercial finance industry. A sentence was also added to this section at the suggestion of the Committees to make clear that by participating in an appeal a party does not lose the right to later claim that an Award should be vacated for misconduct under the governing statute. Commentary has been added to this section to explain these concepts and revisions have been made to this and other sections to address some of the concerns of the experienced arbitrator members of the Committees. Since there was no comment from the commercial finance industry to the Exposure Draft seeking a return to the mandatory appeal process unless the parties “opt-out”, the final draft retained the requirement that the parties expressly “opt-in” to make the appeal provisions applicable.

17.2 Notice of Appeal and Cross-Appeal: Any party to an arbitration proceeding under these Model Rules may appeal a final Award provided that the party delivers a written notice of appeal to the Service Provider prior to the Appeal Deadline, which notice of appeal shall specify: (a) those matters of applicable substantive law that the appellant claims are in error, with a brief statement of the basis for the appeal of such matters; and/or (b) those matters regarding the application of applicable substantive law to the facts found by the Arbitrator that the appellant claims are in error, with a brief statement of the appeal of such matters. Upon receipt of a timely notice of appeal pursuant to this Section 17.2 the Service Provider shall notify, and shall provide a copy of such notice of appeal to, the Arbitrator and the other parties to the arbitration. Within seven (7) days after the Service Provider sends the notice to the parties of the appeal, any other parties to the arbitration proceeding may deliver a notice of cross-appeal to the Service Provider, which notice of cross-appeal shall specify (a) those matters of applicable substantive law that the cross-appellant claims are in error, with a brief statement of the basis for the appeal of such matters; and/or (b) those matters regarding the application of applicable substantive law to the facts found by the Arbitrator that the cross-appellant claims are in error, with a brief statement of the appeal of such matters. Upon receipt

of a timely notice of cross-appeal pursuant to this Section 17.2 the Service Provider shall notify, and shall provide a copy of such notice of cross-appeal to, the Arbitrator and the other parties to the arbitration. In the event that any notice of appeal or notice of cross-appeal is not received by the Service Provider strictly within the time limits required by Section 17.1 or this Section 17.2, or does not satisfy the minimum requirements for a notice of appeal or a notice of cross-appeal pursuant to this Section 17.2, the Service Provider may reject said appeal or cross-appeal, shall notify the party filing said notice, the other parties and the Arbitrator of the rejection and the Award or appeal thereof shall proceed as if said appeal or cross-appeal had not been filed.

17.3 Appeal Panel and Procedure: The appeal panel shall consist of three (3) arbitrators, all of whom shall be impartial, independent and shall have the demonstrated knowledge and experience in commercial finance transactions required of a single arbitrator or the chairperson of the arbitration panel under Section 6.0 of these Model Rules. The Service Provider shall consult with the parties on recommendations for appointments to the appeal panel. If the parties to the arbitration proceeding do not agree as to the selection of the members of the appeal panel within seven (7) days after the Service Provider provides a list of candidates, the Service Provider shall appoint the appeal panel and shall notify the parties of the candidates selected and identify the chairperson of the appeal panel. The chairperson of the appeal panel shall set, and shall notify the parties of, a briefing schedule and of page and format limitations for briefs and other submissions applicable to the appeal. The appeal panel may conduct oral argument if requested by all of the parties to the arbitration or if the appeal panel determines that oral arguments would be helpful in complex or unusual cases and shall notify the parties of the date, time and place that such oral argument will be held. In the event that a party taking an appeal or a cross-appeal fails to submit briefs or other submissions, to pay any required deposits for appeal costs, or to attend any required oral argument, the appeal panel may dismiss the appeal or cross-appeal and proceed as if such appeal or cross appeal had not been filed. If such dismissal of an appeal or cross-appeal resolves all pending appeals, the Award shall become final for purposes of judicial enforcement or modification under the Base Rules immediately upon notification by the Service Provider to the parties of such dismissal.

Joint Committee Revision Notes

The members of the Committees felt that it was important to give the appeal panel the right to dismiss pending appeals for failure of a party bringing an appeal or cross-appeal to comply with briefing or argument schedules, to reduce the possibility of mischief and delay. The original Award would then become final and effective if all pending appeals have been dismissed.

17.4 Record and Standards for Review on Appeal: The record on appeal shall consist only of the Award, any exhibits that had been entered into the record by the Arbitrator and the transcript of any stenographic record made the official record of the arbitration proceedings under the Base Rules. The Arbitrator shall send to the Service Provider any such Exhibits or transcript within ten (10) days after receiving a notice of any appeal under these Model Rules. The sole standard for review is to determine whether the Arbitrator in its Award either: (a) made a material error in the substantive law applicable to the Commercial Financial

Dispute as presented by the parties or in determining the Award, which error resulted in a adverse decision to the party taking the appeal or cross-appeal; or (b) made a material error in the application of the applicable substantive law as presented by the parties to the facts as found by the Arbitrator, which error resulted in an adverse decision to the party taking the appeal or cross-appeal. No evidence will be taken or considered by the appeal panel and the facts as found by the Arbitrator shall be deemed to be correct on appeal.

Commentary

The standard for review under these Model Rules is whether the Arbitrator, in determining the Award, made a material error either in the substantive law applicable to the dispute or in the application of the applicable substantive law to the facts as found by the Arbitrator – which material error resulted in a decision adverse to the party taking the appeal or cross appeal. The correct substantive law applicable to the transaction, however, must have been presented by one or more of the parties to the Arbitrator to be considered on appeal. In no event should the appeal panel entertain a new argument or issue of law that was not presented to the Arbitrator below. The appeal panel also may not review or revise any facts found by the Arbitrator or find any additional facts – findings of fact may only be found by the trial Arbitrator.

Joint Committee Revision Notes

The members of the Committees felt that it was important to require that all issues on appeal have first been presented to and considered by the Arbitrator in the initial Award. Therefore a requirement has been added that any appeal must be limited to the substantive law that was presented by the parties to the trial Arbitrator.

17.5 Final Award on Appeal – Affirmed or Modified Award: The appeal panel may affirm, vacate or modify an Award and shall render its decision within thirty (30) days after the later of the receipt of the final briefs by the parties or the conclusion of oral argument. In the event that the decision of the appeal panel is not filed with the Service Provider within said thirty (30) day period the Award shall be deemed to have been affirmed and shall be final for purposes of enforcement or judicial review. Unless otherwise agreed by all of the parties, the appeal panel shall issue a brief written decision. The appeal panel will make its decision by majority vote and the Service Provider will send a copy of the appeal panel decision to the parties. The appeal panel may also draft and file a supplementary or modified Award incorporating the costs of the appeal. In the event that the appeal panel affirms the Award, the Award shall be final for purposes of enforcement or judicial review. In the event that the appeal panel modifies an Award to correct errors of applicable substantive law and the application of applicable substantive law to the facts found by the Arbitrator, the appeal panel shall issue a revised Award in the form required of the Arbitrator in Section 15.1 of these Model Rules, with the statement of material and relevant facts being those found by the Arbitrator and a corrected statement of the applicable substantive law and the application of the

applicable substantive law to said facts as determined by the appeal panel, and the modified Award shall then be final for purposes of enforcement or judicial review.

17.6 Vacating of Award; Additional Proceedings: In the event that the appeal panel finds that additional facts are required to be found to determine a Commercial Financial Dispute as the result of it finding a material error by the Arbitrator in applicable substantive law, the appeal panel shall vacate the Award. If the appeal panel vacates an Award, unless otherwise agreed by all of the parties to the arbitration proceeding, the Commercial Finance Dispute will be remanded to the original Arbitrator, with any unavailable Arbitrator or member of a panel being appointed pursuant to the Base Rules and these Model Rules. Unless otherwise agreed by all of the parties to the arbitration proceeding, in a further arbitration proceeding subsequent to an appeal panel vacating an Award the facts to be found by an Arbitrator in the subsequent arbitration proceeding will be limited to the additional facts required to determine the Commercial Finance Dispute pursuant to the applicable substantive law found by the appeal panel – in which case, the facts found by the Arbitrator in the original Award shall be assumed to be correct in the subsequent arbitration hearing and the Arbitrator shall conduct the arbitration hearing and issue a subsequent Award pursuant to the Base Rules and these Model Rules. Any Award on such subsequent arbitration shall be subject to appeal pursuant to these Model Rules.

Commentary

Since the appeal panel may not review or revise any facts found by the Arbitrator or find any additional facts, if the appeal panel finds that additional facts are necessary to determine the matter under the applicable substantive law the matter must be remanded to the trial Arbitrator to conduct an additional hearing to determine the required additional facts. Unless the parties agree otherwise, or the original Arbitrator is not available, the matter is to be remanded to the original trial Arbitrator to determine the additional facts.

Joint Committee Revision Notes

The original draft of the Model Rules provided that unless all of the parties agreed otherwise any remand by an appeal panel to find additional facts would have to be to an entirely new Arbitrator for a new trial and determination of all of the facts and issues. The members of the Committees felt strongly that this rule would involve a substantial waste of time and resources and was not necessary. Consequently, the provision was redrafted to have any vacated matter referred back to the original trial Arbitrator to determine just the additional facts required to decide the matter under the applicable substantive law found by the appeal panel to be applicable to decide the matter. The Arbitrator would only be required to find the additional facts necessary to decide the matter and the findings of fact in the original Award would remain effective.

17.7 Costs of Appeal: Unless otherwise provided in the Arbitration Agreement, the costs of any appeal shall be established and paid by the parties as set forth in the Base Rules. In the event that neither the Arbitration Agreement nor the Base Rules provide a rule for payment of the costs for an appeal the costs of the appeal, including, without limitation, the fees and costs of the Service Provider and the members of the appeal panel, shall be paid by the appellant and any cross-appellants and the Service Provider may, from time to time, require the appellant and any cross-appellants to pay deposits for the costs of the appeal. In a modified or supplementary Award the appeal panel may assess the fees, expenses and compensation relating to the appeal among the parties in such amounts as the appeal panel determines is appropriate.

Joint Committee Revision Notes

The original draft of the Model Rules provided that, unless the parties agreed otherwise or the Base Rules have a different rule, the costs of any appeal would be equally divided between the appellant and any cross-appellant. The members of the Committees felt that this was not workable and that the Service Provider should have the ability to require payment of deposits as a condition of any appeal or cross-appeal and that the appeal panel should be able to assess the costs of appeal among the parties. This discussion led to the addition of authority, in Section 17.5, for the appeal panel to enter a modified or supplementary Award relating to these fees and the ability, in Section 17.3, for the appeal panel to dismiss any appeal or cross-appeal if the required deposits are not paid.

18.0 Modification of Model Rules if No Appeal:

In the event in the Arbitration Agreement of the parties does not authorize the appeal provisions in Section 17 of these Model Rules, Sections 17.1 through 17.7 of these Model Rules shall be inapplicable to any arbitration proceeding relating to any Commercial Finance Dispute governed by said Arbitration Agreement.

**SAMPLE ARBITRATION CLAUSES
USING MODEL SUPPLEMENTARY ARBITRATION RULES
FOR COMMERCIAL FINANCE TRANSACTIONS**

The following sample provisions are provided for illustration of the use of the Model Rules. These provisions are intended as a part of other agreements including identification of the parties, substantive governing law and other provisions not included in the following provisions. Two forms are shown. The first adopting all of the default settings in the Model Rules and the other providing a simple form to vary some of the Model Rules parameters while leaving its overall structure intact. Of course, these clauses are provided only for illustration and should not be used without advice of counsel knowledgeable in the law of the jurisdiction governing these arbitration agreements and their effect – for example, waivers of jury trial in some jurisdiction may have to, or should, be separately stated and be conspicuous and the selection of governing law for the arbitration proceeding may not be effective relating to the particular transaction.

Sample Form 1: Simple adoption of Model Rules.

The parties agree that controversies or claims between or among the parties relating to this agreement or documents related thereto or contemplated therein, or the conduct of the parties with respect to transaction contemplated therein, shall be determined by arbitration administered by _____ [*specify the name of the administering agency, to be the “Service Provider” under the Model Rules*] pursuant to the _____ [*specify arbitration rules to be the “Base Rules” under the Model Rules*]³⁷ and the Model Supplementary Arbitration Rules For Commercial Finance Transactions available from the Business Law Section of the American Bar Association at <http://ABA-Finance-Arb.org>.³⁸ Judgment upon the award rendered by the arbitrator(s) may be entered in any court having jurisdiction thereof. The arbitration shall be conducted in the English language in _____ [*specify location if desired, otherwise the Base Rules control*].

[*Alternative choice of law provision, if not otherwise provided in the underlying agreement.*] This arbitration agreement, and any arbitration proceedings or award rendered pursuant to this arbitration agreement, shall be governed by the law of the State of _____.

³⁷ Examples include, (a) the American Arbitration Association pursuant to its Commercial Arbitration Rules (including the Optional Rules for Emergency Measures of Protection); (b) the American Arbitration Association pursuant to its Commercial Financial Disputes Arbitration Rules; (c) the National Arbitration Forum pursuant to its Code of Procedure; (c) JAMS pursuant to its Comprehensive Arbitration Rules and Procedures; (d) International Institute for Conflict Prevention and Resolution (“CPR”) pursuant to the International Institute for Conflict Prevention and Resolution Rules for Non-Administered Arbitration; or (e) UNCITRAL Arbitration Rules with the American Arbitration Association as the appointing authority.

³⁸ Reference to where the final Model Rules will be published will be added and corrected as the form is completed for use.

Sample Form 2: Adoption and Modification of Parameters of Model Rules.

The parties agree that controversies or claims between or among the parties relating to this agreement or documents related thereto or contemplated therein, or the conduct of the parties with respect to transaction contemplated therein, shall be determined by arbitration administered by _____ [*specify the name of the administering agency, to be the “Service Provider” under the Model Rules*] pursuant to the _____ [*specify arbitration rules to be the “Base Rules” under the Model Rules*]³⁹ (the “Base Rules”) and the Model Supplementary Arbitration Rules For Commercial Finance Transactions (the “Model Rules”) available from the Business Law Section of the American Bar Association at <http://ABA-Finance-Arb.org>.⁴⁰ Judgment upon the award rendered by the arbitrator(s) may be entered in any court having jurisdiction thereof. The arbitration shall be conducted in the English language in _____ [*specify location if desired, otherwise the Base Rules control*].

Notwithstanding, any inconsistent provisions of the Model Rules and the Base Rules, the parties agree to the following revisions to the Model Rules: [*Select and modify any of the following clauses as desired*]

- **Limitation on Commercial Finance Disputes Subject to Arbitration:** The term “Commercial Finance Disputes” as used in the Model Rules shall be limited to the following: [*insert desired limitation – however, note issues of unconscionability, overreaching and question whether the arbitration fails to provide a sufficient remedy.*]
- **Optional Identification of Finance Agreements** The term “Finance Agreements” shall mean, without limitation, the following: [*insert description of loan documents, if desired -- note that the arbitration clause will only be effective for parties that are executing the arbitration agreement, so mere identification of a document in the arbitration agreement will not bind a party that did not sign the arbitration agreement.*]
- **Small Matter “Opt Out” of Arbitration:** Notwithstanding the provisions of Section 5.0 of the Model Rules, [the dollar amount set forth in Section 5.0 the Model Rules shall be \$_____ (*insert amount for limit on de-minimus ‘opt- out’ of arbitration, if different from \$100,000*)] or [the parties may not terminate the arbitration agreement pursuant to Section 5.0 of the Model Rules.]
- **Number of Arbitrators:** Notwithstanding the provisions of Section 7.0 of the Model Rules, [all claims shall be determined by _____ () arbitrator(s)] or [if the Statements of Amount in Demand indicate that the good faith estimate of the monetary amount of the claim of any party exceeds _____ dollars (\$ _____), upon the written request of any party received by the Service Provider before the appointment of

³⁹ See, for example, the suggestions in footnote 37.

⁴⁰ See the comment in footnote 38.

an Arbitrator, the Commercial Finance Dispute shall be determined by a panel of three (3) arbitrators].

- **Restriction on Provisional and Self-Help Remedies:** Notwithstanding the provisions of Section 10.0 of the Model Rules, the parties may not exercise any self-help remedies or any judicial or power of sale rights or institute and maintain any action to obtain an interim remedy relating to the Commercial Finance Dispute prior to the issuance of an Award by the Arbitrator.
- **No Punitive Damages:** Notwithstanding the provisions of Section 12.0 of the Model Rules, the Arbitrator shall not have the authority to award punitive or exemplary damages, whether or not provided by statute, in addition to compensatory damages and each party hereby irrevocably waives any right to recover any such damages with respect to any Commercial Finance Dispute determined by arbitration.
- **No Confidentiality of Award:** Notwithstanding the provisions of Section 16.0 of the Model Rules, any Awards in the arbitration proceedings shall not be confidential and may be disclosed by the Service Provider or the Arbitrator as well as the parties.
- **Right of Appeal:** The provisions of Section 17 of the Model Rules, providing for a right of appeal from an Award, shall be applicable to Awards rendered pursuant to this agreement.

[Alternative choice of law provision, if not otherwise provided in the underlying agreement.] This arbitration agreement, and any arbitration proceedings or award rendered pursuant to this arbitration agreement, shall be governed by the law of the State of _____.

Unless otherwise defined in this agreement, capitalized terms used in this [section of this] agreement shall have the meanings ascribed to them in the Model Rules.