



Resolving Construction Disputes Through Baseball Arbitration

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“Baseball is a game where you gotta have fun. You do that by winning.” —Dave Bristol, manager for the Reds, Brewers, Braves, and Giants

“It doesn’t matter if you win or lose, it’s how you play the game.”
—People Who Lose

Winning certainly matters. But as parties to construction disputes know, winning can often come at quite a cost. That is undoubtedly why arbitration has become so popular in resolving construction disputes. It is rare for a large project to end without a controversy, and the timely and efficient resolution of those controversies may matter almost as much as the winning itself. Arbitration has well known advantages over litigation. Yet arbitration still often involves complex issues and exaggerated claims. But, in at least certain kinds of construction arbitrations, there may be a method to streamline the process.

Final-offer arbitration—more commonly known as “baseball arbitration”—could offer significant savings of both time and cost. In a traditional arbitration, the arbitrator has discretion to issue any award that the arbitrator finds to be just and equitable. The arbitrator usually explains his or her decision on each issue in the arbitration and calculates the award precisely. By

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contrast, in baseball arbitration, the arbitrator's choice is typically limited to only one of the specific awards requested by a party. The arbitrator has no discretion to independently calculate the award, but must select one of the competing proposals. In a two-party case, for example, the award may only be the *exact* amount requested by the plaintiff or the *exact* amount requested by the defendant—nothing higher, lower, or in-between.

Baseball arbitration is slowly becoming more popular as a process for resolving certain construction disputes. It works best for two-party disputes where the controversy is limited to money. And there are many, many controversies in this country every year that fit this profile and are, therefore, well suited for baseball arbitration. Baseball arbitration is recognized as having at least three advantages over more traditional arbitration:

- the risk of an adverse ruling is contained,
- the process strongly encourages settlement, and
- it simplifies and streamlines the award process.

Baseball arbitration acquired its colloquial name because it is the method by which some Major League Baseball players resolve their salary disputes. The players request a certain salary and their team requests another, typically lower, salary. Then there is a hearing before an arbitrator to determine which number is more fair. But the authority of the arbitrator is strictly limited to a binary choice. After the hearing, the arbitrator picks either one of the two numbers and that becomes the player's salary for the next season.

The key to baseball arbitration, and perhaps its most interesting facet, is that it necessarily encourages the parties to be reasonable. In fact, the cost of being unreasonable can be devastating. Since the arbitrator may only choose from the exact numbers that were provided by the parties, there is a risk that an unreasonable request, even by the party with the best case, may nevertheless result in the arbitrator choosing the *other* party's suggested award. The party with the best case can *lose* simply because its requested award was too high or too low.

For instance, suppose a general contractor sues an owner for alleged non-payment of \$1 million worth of very legitimate change orders but has also asserted an additional \$9 million of meritless delay damages. Traditional arbitration litigants will often advance their most extreme position. In the above example, the owner might be expected to offer zero and seek a defense award while the plaintiff will demand the full \$10 million. What is the perceived advantage of being unreasonable? Litigants often expect that an arbitrator will “split the baby” based on the parties’ demands. This fear has been studied and debunked, yet it persists. Regardless, in baseball arbitration precisely the opposite is true. Extreme positions are risky. Consider how this example might play out in the context of baseball arbitration.

Say the contractor requests an award of \$8.5 million and the owner requests an award of just \$250,000. Here, the contractor’s request would include almost all of its meritless delay claim. The arbitrator may feel compelled to select the \$250,000 award—just 25% of what the arbitrator may otherwise feel is the fair value of the total case—because the arbitrator regards this to be the more reasonable of the two requests. In this case, the contractor’s unreasonable demand may lead to the rejection of its suggested award.

On the other hand, if the contractor requests a more reasonable award, say \$1.5 million, and it is the owner that requests an unreasonable award, say \$100,000, the arbitrator may instead feel compelled to select the \$1.5 million award, a number 50% higher than he or she otherwise would have found to be proper. In this case, the owner’s unreasonable position (virtually ignoring the legitimate change orders) may lead to the rejection of its position. Both parties, as it turns out, have a tremendous incentive to ask for a reasonable award.

These hypothetical scenarios suggest one of the key benefits of baseball arbitration. If the parties appropriately weigh the value of the claims and request reasonable arbitration awards, they may find that they are not all that far apart from each other. And that tends to play out in practice. It is common for parties to settle baseball arbitration cases without need for a hearing, after the requested awards are exchanged. In this way, baseball

arbitration could be thought of as a useful ADR double-play: A formal arbitration that has a built-in propensity to encourage settlement.

Using again the above hypothetical: say the owner's suggested award is \$850,000 and the general contractor suggests an award of \$1.2 million. The parties' \$10 million dispute is now reduced to a \$350,000 difference. More than 96% of the controversy is now resolved simply by adhering to the baseball arbitration process. With so much less at stake, it would only be natural for the disputants to view settlement with favor and as within reach. And the research has borne out that final-offer arbitration succeeds in encouraging settlement.

Construction cases are often complex disputes made up of many smaller claims. It is not uncommon for a single construction case to be comprised of a dozen or more smaller, constituent claims. In traditional arbitration, the arbitrator must adjudicate the liability and damages issues on each and every claim. With baseball arbitration, however, the arbitrator need only decide as between the competing proposed awards. There may be no need for an exhaustive claim-by-claim analysis of liability and damages in baseball arbitration, especially when it is apparent that one of the two requested awards is excessively high or low.

There is nothing to suggest that baseball arbitration awards are subject to challenge any more than traditional awards. In *U.S. Steel Mining v. Wilson Downhole*,¹ for example, the court enforced an award entered in a baseball arbitration despite the arbitrator admitting in his decision that he "would have arrived at a lesser and different amount" were he allowed to do so. Other courts, in other parts of the county, have similarly confirmed baseball arbitration awards.²

Baseball arbitration does not necessarily suit every construction controversy. It works best when the dispute involves competing claims for money between two parties. However, it may not work so well for controversies involving several parties, each pointing the finger at the others, where an

¹2006 WL 2869535, *2 (W.D. Pa. Oct 5, 2006).

²See, e.g., *Rain CII Carbon, LLC v. ConocoPhillips Company*, 674 F.3d 469 (5th Cir. 2012); *MCI Telecommunications Corp. v. Michigan Bell Telephone Co.*, 79 F. Supp. 2d 768 (E.D. Mich. 1999).

allocation of fault among the parties may be required. Similarly, baseball arbitration may not be well suited for controversies involving injunctive relief, specific performance claims, or requested declaratory relief. Consider the following.

What happens if the owner withholds contract balance on the general contractor on several grounds including that the electrical subcontractor's work was defective? Suppose the general contractor does not pay the electrical subcontractor (because the owner did not pay it). The electrical subcontractor has a claim against the general contractor and the general contractor has a claim against the owner. Can this case go to baseball arbitration? It would seem that sorting out who is at fault among these three competing interests is exactly what traditional arbitration does best. And what if the subcontractor asserts a wildly excessive claim against the general contractor? If the case goes to baseball arbitration, the contractor is in a pickle. If it seeks an award of the electrical contractor's total (unreasonable) claim, it risks the arbitrator picking the owner's number. Yet the unreasonable demand was not issued by the general contractor. It would merely be passing the demand through. Would the general contractor be better off if it asked for *less* than the electrical contractor demanded? That, too, seems unfair. If the general contractor "wins" the arbitration, it may still be on the hook for any difference between the award and the electrical contractor's demand. The general contractor would be punished for being the reasonable one, which is precisely the opposite of what baseball arbitration is designed to do. Although these issues can be addressed, the point is that these situations are not well suited for baseball arbitration. While traditional arbitration is flexible enough to accommodate this kind of scenario, the rigidity of baseball arbitration, which is otherwise its strength, may not be.

In drafting a baseball arbitration provision, you will want to consider the following:

- Can "final" offers be revised or amended? And if so, when?

- When will the proposed awards be revealed to the arbitrator and other parties? Or will they be kept sealed until after the arbitrator has rendered a decision (so-called “night baseball”)?
- Will the arbitrator’s decision be reasoned? Or will it be a simple selection of one of the suggested awards?
- Will there be a single aggregated award? Or will it be done claim-by-claim?
- How are claims of subcontractors and suppliers to be handled? Do standard form subcontracts and purchase orders contain a pass-through provision or liquidating agreement limiting claims to what the general contractor may recover in a baseball arbitration?

Baseball arbitration may not be right for every construction dispute. But at least for two-party construction disputes, it offers unique advantages. Even if it was not originally included in the construction contract, it certainly makes sense to consider baseball arbitration as a *post*-dispute resolution tool. If “how you play the game matters,” baseball arbitration may be the winning strategy.