

## Outside Counsel

# The Business Case for Dispute Prevention Processes

**D**ispute prevention processes are structures designed to prevent conflicts from escalating into disputes and delaying the completion and fulfillment of a contract, which negatively impacts all its stakeholders. To date, such initiatives have proven to be very effective in construction projects. This article makes the case for scaling the use of dispute prevention processes well beyond the realm of construction. Outlined below are some of the key benefits and challenges of dispute prevention processes for business owners, investors, and employees. These benefits of dispute prevention—triggered much earlier than traditional dispute resolution processes—should be deployed by businesses in broader commercial contexts to mitigate the risk that early disagreements grow into

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impediments to project completion, litigation and costly damages.

Generally, the term “dispute” connotes demand letters, recriminations, arbitration and even litigation. Disputes are presaged typically by disagreements, and processes for dispute resolution become necessary after one side, or the other, believes that damages will ensue. These damages may be monetary or the infringement of a right created by the contract in question. The goal of dispute *prevention* is to intervene before there are *any damages*.

The core idea of “dispute prevention” is to avoid business disruption and litigation costs that flow from

the initiation of legal proceedings. The authors’ collective experience as arbitrators, adjudicators, mediators and business executives has led us to believe that numerous worthwhile projects (including potentially life-saving collaborative research) have collapsed because processes were not in place to support the constituents to continue their valuable work; instead, the parties engaged in litigation and other dispute resolution practices, ending any chance to achieve the initial, promised goal in a timely manner, if at all.

Dispute prevention processes provide a needed resource for those situations when business dealings hit unexpected speed bumps. They provide guide rails throughout the life of a project that allow the parties to keep the business venture moving forward. They ensure that disagreements do not escalate into disputes that become lawsuits or arbitration claims. They are the business professionals’ tools to avoid the cost and burden of traditional dispute resolution.

Historically, dispute prevention processes have proven to be very effective

in construction projects where the parties agree to engage a third party throughout the life of the project. The third party frequently consists of a Disputes Board comprised of one or more professionals with experience in the construction industry and as neutrals (arbitrators or mediators). These professionals may have experience as arbitrators, mediators or special masters, but that is not their role when it comes to dispute prevention. Rather, their primary role, and objective, as dispute prevention neutrals is not to resolve disputes but rather to assist their clients in preventing their occurrence in the first place. They are therefore generally retained at the early stages of a project to be on stand-by, ready to assist the various stakeholders when needed, as the project proceeds through its lifecycle. The establishment, role, and responsibilities of the Disputes Board are spelled out and memorialized at the outset by written agreement among the parties. The Disputes Board's mandate can range from attending regular project progress meetings, to foreseeing potential sources of conflict, to intervening in the event a conflict arises. The prior written agreement spells out the scope of the intervention and method for resolution of the conflict. The objective is to prevent conflicts from escalating, and risking delays that could hinder completion of the construction project and negatively impact the stakeholders. Given the time-sensitive nature of most construction matters and the inter-dependencies among their

stakeholders, dispute prevention has proven to be a project-saving tool for project participants and a significant cost-saving one for all constituents.

In many businesses outside the construction industry, the benefits of dispute prevention neutrals are readily apparent. However, they rarely are used in general, commercial contracts, even when disputes are foreseeable, such as when ongoing collaboration is contemplated. It is time for dispute prevention processes to gain traction in the commercial world, beyond construction contracts. Recently, the pharmaceutical sector has begun to

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adopt aspects of dispute prevention to mitigate the risk of supply chain disruption. Similarly, pharmaceutical early-stage development collaborations would be a natural fit for the insertion of a dispute prevention neutral into the collaboration agreement, to get involved as soon as a disagreement arises between companies. Bespoke dispute prevention clauses could be drafted for the pharmaceutical industry in its contracts as part of the dispute resolution escalation process that is often contemplated in these arrangements. Effective use of neutral dispute prevention professionals could prevent

the breakdown of collaborations, to the benefit of the stakeholders as well as the eventual health and medical sector.

Another natural fit for dispute prevention processes are family business groups, which historically have experienced the core elements that can lead to conflict: multiple parties with interdependencies and different needs, all with interests in one or more joint business enterprises. Similarly, start-ups and young companies may also have significant short and long-term interdependencies amongst their stakeholders. With fragile infrastructure, and no time to lose in the race for growth, they would also benefit from the use of dispute prevention processes to help their founders, investors, employees and other stakeholders mitigate the risk of interpersonal conflict that could hinder growth or lead to their demise. When disagreements are not addressed early, they can become disputes that lead to failure of the enterprise and loss of investment dollars and business reputation.

The value of dispute prevention processes should be considered from a cost-benefit perspective to determine their overall impact on a business undertaking. Stakeholders may be hesitant to build in to the project financials their potential cost in the absence of an actual dispute. However, the expense associated with dispute prevention processes is generally nominal relative to the size of the projects, and the importance of the relationships, they aim to secure. In weighing the cost-benefit ratio, the

risk of a dispute occurring must be considered, and take into account the disruption or loss of a potentially valuable collaboration as well as the cost of counsel, if the dispute is allowed to gain a head of steam. Once a disagreement or conflict evolves into a dispute, there is no choice but to retain counsel to defend the business interests, and the business interests are often irreparably damaged by the nature of legal filings. To alleviate cost concerns, the dispute prevention provision can be written to avoid an unnecessarily burdensome structure. For example, by having only one dispute prevention neutral, rather than three, and providing for hourly rate compensation, costs are contained. With that approach, the number of hours needed is low, unless and until a significant conflict arises that requires more time from the neutral to defuse. In sum, the objection to incorporating a dispute prevention process based on economics could be rather shortsighted if one were to consider it from a pure financial perspective: The investment—represented by the cost of retaining the dispute prevention neutral(s) for the duration of the collaboration—is minimal, given the risk/cost avoidance of an unresolved dispute and the return represented by the timely completion of a project or similar multi-party goal.

Another concern about dispute prevention methods is that an outsider would be positioned to learn about the collaboration and areas of potential friction. Dispute prevention can

only be effective if there is a neutral who is placed “inside” the business enterprise; however, the amount of intrusion should not be of concern, if the construction industry experience is considered. An effective neutral will be able to demonstrate that the benefits of dispute prevention outweigh any concern over outside intrusion.

Perhaps the biggest challenge to establishing dispute prevention processes outside of the construction arena is the fact that they are new and unfamiliar to most business people. Currently, parties’ corporate counsel and advisors are unaccustomed to including such clauses when drafting contracts. Dispute prevention clauses are new to most businesses and their advisors. But just as mediation was a “new” concept several decades ago, so too will this process for dispute prevention prove itself to be valuable, and will become the new normal in future years.

Dispute prevention processes require buy-in from the business thought leaders who oversee the business collaborations, projects and relationships with their counterparts. Greater awareness of their existence, potential uses and benefits by companies and their business advisors is essential so that they can be considered at the outset of a business arrangement. Equipped with the basic elements of dispute prevention structures, business executives leading the initiative can evaluate their risk avoidance benefit, functioning, and added value. At the same time, corporate lawyers drafting transactional documents will become increasingly

familiar with the various structures to consider when including a dispute prevention structure in deal documentation. Working together, corporate lawyers and their clients will draft a dispute prevention structure that is tailored to the specifics of their deal. As dispute prevention processes grow in use outside the construction industry, it is hoped that such increased awareness will be coupled with greater tools that both business decision-makers and corporate counsel can apply when they decide to establish a dispute prevention structure. As the opportunity cost of unresolved disputes, in terms of business disruption, lost profitable ventures, and litigation, becomes increasingly steep, the time is ripe to consider the implementation of dispute prevention processes more broadly—as an effective tool, akin to an insurance policy, to mitigate the downside financial risk of any contractual undertaking involving interdependent parties and time sensitive goals.