Telling Stories: How Alternative Dispute Resolution Could Have Saved Costs and a Business Relationship

by Joan D. Hogarth

Joan D. Hogarth is an experienced neutral with substantive legal experience in health care and in assisting seniors to navigate the legal landscape. Hogarth has arbitrated over 250 consumer and securities cases and approximately 55 mediations to include Storm Sandy cases. She may be reached at jayhogarth12@gmail.com.

It is worthwhile for alternative dispute resolution (ADR) professionals to explore how ADR can effectively and efficiently resolve issues and save the relationship. For example, when two business partners and friends became so embroiled in a complex weave of lawsuits that a judge would characterize them as "bitterly litigated cases," alternatives to litigation may well have mitigated the toll on the parties' business relationship. We begin in 2005, when one of the parties invested in property in what was once a "seedy" part of New York City—the Bowery. After carefully considering his options, the investor decided on developing a hotel complex, including residential units on the top three floors and the roof. Lacking any experience in this area, the party brought in a boutique hotel expert to design and operate the project. A dispute arose around 2011 when one party alleged that the other was blocking the exercise of a right agreed to at the inception of the project. A series of lawsuits, motions, and court appearances followed; seven years later, the matter remains in the New York Supreme Court with no scheduled hearing date.

The story I am about to tell was gleaned from news articles, podcasts, and publicly available court documents.[1] It demonstrates the costs in time, money, and relationships in a business dispute that was strictly about money with no stated desire to set legal precedents in contract law or civil procedure. It may have begun with a simple lawsuit, but today there have been more than half-a-dozen lawsuits filed directly or derivatively connected to the underlying issues of contract interpretation and breach. I highlight some of the major elements of ADR that are implicated in the case; for example, pre-dispute ADR clauses, willingness of parties to participate in ADR, confidentiality, cost savings, speedier resolution, and more importantly, salvaging an otherwise good business relationship.

The Story

In the early 2000s, Gerald Rosengarten purchased adjoining properties in the Bowery with the expectation to take advantage of gentrification taking place in the vicinities. He contemplated many uses and eventually settled on a hotel project. Recognizing his limitations, he invited Richard Born, a famous hotelier known for inventing the boutique hotel concept. Born brought in his experts. The partners were to focus on design and operation of the hotel—The Bowery.

In 2005, Rosengarten and John Ruha formed Ruandro LLC, with each owning 50 percent interest in the company. The only asset of Ruandro was the sublease to three floors and the roof of The Bowery Hotel. To participate in Ruandro, Ruha borrowed $2 million from Rosengarten and pledged his 50 percent interest as security in the event of a default. The default would essentially turn the management and decision-making of Ruandro over to Rosengarten.

The Bowery Hotel was managed by Three on Third LLC (TOT), in which Rosengarten and Ruha were members. TOT was part of the project because it is known for its excellence in hospitality operations. There were other partners in TOT, most important for this story, the aforementioned Born. Rosengarten had a 12 percent equity stake in TOT and would be paid a percentage of the profits from the hotel operations. He, through Ruandro, also owned the sublease for the top three floors and roof of the hotel and the roof and the rights to convert such property into condominiums for sale, if and when the land (the ground lease) was bought by the company. With the death of the land owner and the land now available for sale, Rosengarten/TOT could fulfill a condition precedent to Rosengarten's rights to convert the top floors into condominiums for sale. Rosengarten alleges that Born undermined the agreement, and instead of purchasing the land through TOT, he circumvented the agreement and purchased it directly thereby blocking the conversion. A series of related disputes followed: the defaulted $2 million loan to Ruha, a $50 million lawsuit against Born for allegedly blocking Rosengarten from exercising his rights to convert the apartments, a $1.5 million lawsuit representing the unpaid profits from

Rosengarten's 12 percent stake in TOT, interpleaders and motions to dismiss the $50 million lawsuit, and other shareholder derivative lawsuits.

Suitable ADR Processes

Business disputes are well-suited for ADR and the Ruandro case is no exception because of the complexities and interrelation of the disputes, the ongoing delays, costs of discovery, and the costs associated with legal fees for the five law firms and counting that have been involved, as well as broken business relationships. In fact, it's an ideal case for ADR.

Negotiation

Negotiation, as an ADR tool, could have been used. From all accounts, it may have been attempted over "Scotch," per Born. For the negotiation to advance, there has to be a high degree of willingness and some level of trust of the parties. The parties willingly come together to arrive at an agreement with which they can live. The process and outcome are confidential.

Mediation

If negotiation fails to produce a desired result, the next ADR process that could be successful would be mediation. Mediation is a facilitated negotiation where a trained and skilled third-party neutral serves as the "interpreter" of interests, feelings, and objectives in the negotiation. A California court describes mediation as:

> … [being] particularly useful when parties have a relationship they want to preserve. So when family members, neighbors, or business partners have a dispute, mediation may be the ADR process to use. Mediation is also effective when emotions are getting in the way of resolution.[2]

The outcome of the mediation session—or sessions—frequently is a creative, confidential agreement arrived at by the parties. The mediator might open and close the session, which includes decision-makers for all parties, with a joint meeting that allows the parties to summarize their position, and in the end, to come to an agreement. Like the negotiation, mediation is confidential and it is the most conducive for preserving relationships since the parties control the negotiations and ultimate agreement; the sessions also allow high emotions to be tempered. Mediation may include the exchange of information. The mediator facilitates the discussion of issues and the exploration of possible solutions in joint sessions and, where useful, in caucuses with each party. Mediation is a particularly attractive ADR process because it easily can be tailored to the needs and characteristics of the parties and the demands of the subject matter. The parties discussed herein may have been ripe for mediation very early in the process and could have used mediation at any time.

Early Neutral Evaluation

Mediation is usually voluntary, and parties may continue to take the path of litigation because they feel they will win. This is where another ADR process could be helpful. In early neutral evaluation, the parties present the merits of their case and answer questions of a highly qualified evaluator who will provide a nonbinding decision and a range of awards. The evaluator is an expert who is able to identify the hot spots, the risks, and the likelihood of success. Oftentimes, hearing what a case is worth and understanding the possible pitfalls and the associated risks, parties who may have taken intractable positions are then able to rethink their positions. The evaluator's decision is nonbinding and the session is confidential.

Arbitration

Finally, the parties could be directed to arbitration. Arbitration is much like litigation in that a "private judge" listens to the arguments, reviews evidence, and unilaterally makes a decision. Arbitration is consensual, and, if included in an agreement, one party cannot unilaterally withdraw from the process. The parties, for the most part, are bound by the decision and have no right of appeal, even though, under very limited circumstances, they may attempt to vacate an arbitral award.

Where ADR Could Have Saved Costs and Business Relationships

Agreements

Prior to the dispute and in the contract formation, it would have been a best practice to include a provision for dispute resolution. Despite its absence from the agreement, the parties are still free to engage in ADR with a post-dispute agreement. The parties must be willing. In the Ruandro case, the talk by one party of having a business discussion over scotch and the talk by the other that he wanted the case to be settled without going to trial are indicators to broach the discussion of ADR. In this case, parties were soon taking positions from which it was hard to retreat—one party declaring that the contract was complex and memories as to what was agreed to could have faded over the following 10 years. This roadblock to early dispute resolution can be reduced by including a dispute resolution clause that does not just reference courts, venue, and choice of law for litigation purposes. Advocates should offer these clauses as part of their counsel at contract formation.

Relationships

The Ruandro case cried out for a functional working relationship. ADR can help keep principals involved in the dispute resolution process while their lawyers help them work through goals, risks, and rewards presented by the issues, as well as alternative paths to a final resolution. The ADR practitioner can facilitate the interactions between disputants and optimize outcomes for all parties. In the Ruandro case, the relationship between the parties became bitter and personal as the principals retreated from the actual dispute resolution process.

Of course, there may come a point at which positions become intractable and civil discussion is impossible, when litigation, then, is the only recourse. Even in those cases, ADR may offer arbitration as a reasonable, most cost- and time-effective alternative to formal judicial proceedings.

Confidentiality and Privacy

Because ADR is not a part of the judicial process, the proceedings or sessions or information produced under discovery are confidential. In an open court there are transcripts, orders, and motions—all available to the public. When a judge scolds the parties, it becomes headline.[3] When the judge characterizes a party's behavior as "inexcusable" and "unacceptable," it becomes part of the story.[4] In ADR, the process, the terms, and the agreement are all among the parties and the neutral who is duty-bound to keep it confidential.

Time

The Ruandro dispute began in 2011. Lawsuits were filed in 2014. Today the case is still making its way through the court. Getting a case through the court system is a very lengthy process. Closely associated with the time are the opportunities lost. For seven years, Rosengarten has not been able to exercise his rights. That is an opportunity lost. Then there's the time spent in court—there have been at least 74 court appearances since the lawsuit was filed in 2014. All this time contributes to increased costs.

Discovery

In this case, arguments over discovery orders have been costly. Months and months of back and forth have not produced results. Discovery is one of the main drivers of cost in litigation next to attorney's fees. Ideally, in ADR, discovery can be limited by the parties' rules or the neutral. In this case, one party produced over 500,000 pages, many of which were nonresponsive to the discovery requests and even included junk mail. Had the parties used ADR, discovery would have been limited.

Costs

There are costs associated with the running of the clock, with attorney's fees, and court costs. And, as mentioned prior, the lost opportunity to convert and sell the condominiums as Rosengarten wanted and then to pursue other business opportunities.

Conclusion

More than five years after the dispute first began, two friends and partners continue to litigate. As of this writing, at least six lawsuits have been filed and five law firms have been engaged. Seventy-four court appearances later, one New York Supreme Court judge declared these to be "bitterly litigated cases."[5] While the Ruandro case may illustrate the extreme, it can serve as a warning of just where business disputes can go. ADR offers many possibilities for more useful outcomes. If the parties do not know about ADR, advocates should have ADR in their tool bag, and counsel should have their clients consider ADR both before and after disputes arise. Attorneys representing clients in any situation in which conflict may arise or has already arisen should consider: placing ADR clauses into agreements, counseling clients on the advantages and disadvantages of ADR, and sharing the successful and meaningful process of ADR. ⊙

If you have stories of the successful use of alternative dispute resolution to resolve commercial disputes or relationships, contact us at fedbaradr@gmail.com or join the Section by visiting the FBA's home page and signing up.

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Endnotes

[1]Sources for the illustrative case are: *This Week in Crain's New York*, Crain's N.Y. Bus. (Aug. 4, 2014), http://www.podtrac.com/pts/redirect.mp3/www.crainsnewyork.com/assets/mp3/CN9579782.mp3; Andrew J. Hawkins, *Inventor of the Leisure Suit Sues Inventor of the Boutique Hotels*, Crain's N.Y. Bus. (Aug. 4, 2014, 12:01 AM), http://www.crainsnewyork.com/article/20140804/REAL_ESTATE/308039997/inventor-of-leisure-suit-sues-inventor-of-boutique-hotel; Tess Hofmann, *Bowery Hotel Co-Owner Stuck in Legal Battle With Partner,* Real Deal (May 19, 2015, 12:00 PM), https://therealdeal.com/2015/05/19/bowery-hotel-co-owner-stuck-in-legal-battle-with-partner; Andrew J. Hawkins, *Judge Slaps Down Posh Bowery Hotel Owner For His Legal Shenanigans*, Crain's N.Y. Bus. (July 29, 2015, 12:01 AM), http://www.crainsnewyork.com/article/20150729/BLOGS04/150729872/judge-slaps-down-posh-hotel-owner-for-his-legal-shenanigans; *Ruandro LLC. v. Three on Third LLC*, Admin. Order, Index #155505/14; *Rosengarten v. Born,* Index #651147/14, New York Civil Supreme Court; *Ruandro LLC v. Born*, 2016 N.Y. Misc. Lexis 2047.

[2]This is the definition used by the Superior Court of California. Mediation: Alternative Dispute Resolution (ADR), Super. Ct. Cal., http://www.monterey.courts.ca.gov/ADR/Mediation.aspx (last visited Sept. 25, 2017).

[3]Hawkins, *Judge Slaps Down Posh Bowery Hotel Owner For His Legal Shenanigans*, *supra* note 1.

[4]*Id.*

[5]*Ruandro LLC v. Born*, Slip. Op. 31008(U), No. 651148/2014 (N.Y. Sup. Ct. May 19, 2016), *available at* http://www.courts.state.ny.us/REPORTER/pdfs/2016/2016_31008.pdf.

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