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Med-Arb — Can You Afford the Risk?

By James J. Vlastic

Med-Arb is a dispute resolution process in which, once the parties have failed to reach a negotiated settlement in the mediation stage of the process, the mediator becomes an arbitrator to render a binding decision. This process of med-arb poses risks for the parties that do not present themselves when the mediator and arbitrator are different persons. These risks are the focus of this article.

Traditional mediation is generally understood to be a voluntary, non-binding dispute resolution process in which an independent and unbiased mediator is enlisted to facilitate a negotiated resolution between the adverse parties.¹ The mediator often meets with the parties in separate caucus sessions in which the mediator explores each party's interests, seeking grounds to resolve the dispute based on the parties' interests, rather than by strict enforcement of either party's legal rights. Traditional arbitration, on the other hand, is a process whereby an independent, unbiased third party (or third parties) sits in judgment of legal rights and remedies to which the claimant is entitled against the defendant. The arbitration award is based upon legally relevant evidence presented in hearings in which both parties are present.

Is the Mediation Session in Med-Arb Voluntary?

In traditional mediation, binding resolution is not reached until each party agrees to the proposed result. Either party can terminate the session at any time without affecting their existing legal rights and available remedies. Many mediators would argue that it is never appropriate for a mediator to coerce a party to resolve a dispute. The parties to med-arb choose, however, to relinquish their ability to decide when and whether to resolve their dispute in their own best interests. They delegate instead to a third party, the med-arbitrator, the decision over what they should give up in the interest of a final resolution. Should the parties fail to resolve the case at the mediation stage of the process, the med-arbitrator, in the end, practices the ultimate coercion, by simply ordering the resolution that he/she believes to be fair, after the parties have refused to agree to it. Some would suggest that even a settlement achieved during the mediation phase of med-arb is therefore, in some

measure, coerced because it is achieved in the face of the ultimate coercion of the impending med-arbitrator's award. One commentator has observed that, "the arbitrator — consciously or not — puts his ego behind the settlement that he has crafted: and if a party says "no" and the arbitral decision comes down against them, they will be very often convinced of the fact that this was because the arbitrator resented their not accepting the settlement, and I do not think it is proper for an arbitrator to put parties in that position."² The fact that a med-arb award may not be subject to challenge in court, if supported by appropriate contractual provisions and waivers, does not eliminate this potentially coercive aspect of the process.

Disclosure of Interests or Weaknesses May Be Hampered in Med-Arb

It has been observed that "[a]dvocates and parties would be forewarned to consider judiciously what information to present to a neutral who would ultimately give an opinion which may have a decisive impact on further negotiations."³ Will a party freely admit weakness in their case during the mediation phase to a med-arbitrator, who they know will later make a binding decision? Does heightened reluctance to admit weakness during the mediation phase of the process reduce the likelihood that the mediator will be able to guide the parties to a mutually acceptable negotiated resolution? In the pure mediation context, a party is arguably motivated to identify interests and weaknesses that can be useful to the mediator in brokering a mutually satisfactory resolution of the dispute, because the mediator lacks power to eventually bind that party to any result that the mediator determines to be "fair", and the party retains the power to terminate the negotiation at any time. Not so, perhaps, in med-arb.

Med-Arb Circumvents Traditional Due Process Protections

Inherent in med-arb is the due process concern that information communicated confidentially at caucus to the med-arbitrator is not known to the opposing party, and is not subject to response or clarification by the

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opposing party. This is directly contrary to traditional due process rules governing fair hearings of disputes on the merits, which forbid ex parte communications with the decision maker. This lack of transparency is particularly problematic in that the med-arbitrator hears ex parte communications as to the parties' interests, beyond evidence legally relevant to their rights.

“There are no safeguards against how the arbitrator interprets what he has been told and how it would or might affect his perception of the dispute, the parties or the witnesses, and the weight he would have to give to their evidence, in light of the information he has acquired. It is still very much discouraged in international commercial arbitration disputes, to mandate that the arbitrators act both as conciliators (mediators) and arbitrators in the same dispute.”⁴

Parties agreeing to med-arb need to understand that they have relinquished the protections of due process arbitration, which can be achieved only by the introduction of a new, and unbiased arbitrator who is not burdened with ex parte communications from the parties about the facts and their interests, that are not subject to disclosure to or dispute by their adversary.

The med-arbitrator not only hears information ex parte, but hears a type of information related to parties' interests that, at best, distracts from his/her ability to render a fair and unbiased decision on the factual and legal merits of the parties' dispute, without being influenced by extraneous factors. Parties agreeing to med-arb risk both the loss of neutrality of the med-arbitrator, and the loss of due process through these ex parte communications with the arbitrator.

“The process of mediation, as it has been developed in the Western hemisphere of the world, presupposes that the mediator would hold separate meetings with the parties. At these caucuses, the mediator might become seized of information regarding the parties which might not be known to each other. The mediator would know the parties' bargaining threshold and what the parties would be happy to accept in settlement of the dispute. This material aspect of the mediation process offends one of the cardinal principles of arbitration. The arbitrator must not have ex parte communications with either party but must promptly disclose the same to the other party, and other members of the arbitral tribunal (if any). This is to protect the transparency of the arbitral process. This is also to protect the arbitrator(s) from being influenced in his or their judgment, by extraneous matters or facts not put in evidence before the arbitral tribunal, and possibly not known to the other party.”⁵

Med-Arb intentionally introduces the med-arbitrator, during the mediation, to legally irrelevant information. This cannot help but impact the arbitrator's decision making process subliminally, if not in an acknowledged way.

“[I]f the med arbitrator engages in caucuses, he may invite the parties to discuss extraneous matters, for example, emotional issues which may not be understood as strictly relevant for resolution purposes, but these issues may be relevant for settlement purposes. It is difficult to believe that the med-arbitrator will remain unaffected as an arbitrator, after becoming privy to private, perhaps intimate, emotional, personal and other “legally” irrelevant information or compromise positions.”⁶

This confidential and legally irrelevant “interest” information, while typically disclosed to a mediator, would never be disclosed to a traditional arbitrator, so there would be no need for the arbitrator to “put it out of his head”.⁷ Some observers suggest that mediation might be conducted without caucus in a med-arb proceeding, thus curing the problem of lack of transparency. This may work, but mediation without caucus does not cure the problem of intentional communication of legally irrelevant information focused on the parties' interests, rather than on the facts and the law that are, or should be, determinative of the rights of the parties in arbitration.

Med-Arb Transforms “Rights” Arbitration Into “Interests” Arbitration

The arbitrator in traditional arbitration is vested with the authority to impose a resolution on the parties, but only in accordance with the due process protections, and based upon the parties' legal rights, no matter how much those rights may diverge from their interests. In traditional arbitration, the power to bind the parties to a resolution is relinquished to the arbitrator under rules that seek to obtain a decision derived from a transparent due process hearing on the factual and legal merits of the dispute. The traditional mediator focuses, and attempts to persuade the parties to focus, on the parties' interests, rather than on their legal rights and remedies, which are the traditional focus of arbitration. The mediator typically endeavors to learn the threshold of an acceptable settlement for each of the parties. The mediator, however, lacks the power to dictate the resolution of the dispute in accordance with what he/she perceives to be the interests of the parties. As the mediator becomes an arbitrator in med-arb, he/she becomes possessed of the inherent power, albeit not the express authority, to “decide” the dispute in the range of the parties' interests, rather than strictly in accordance with the factual and legal merits of each party's position. This is not usually what the parties have contracted for in arbitration. By the time that they reach the arbitration phase of med-arb, this is also a result that they were unwilling to achieve through facilitated negotiation. Nonetheless, the power to bind the parties to a resolution is passed to the med-arbitrator who will, in caucus, acquire information to which one party is not privy, leading to a decision based, at least in part, on the parties' interests. The shift from mediation to arbitration involves the parties relinquishing the power to decide their own dispute in favor of a third party mandate. The traditional arbitration award is based primarily on the arbitrator's judgment of the parties' rights. The parties agreeing to med-arb effectively abdicate the goal that the med-arbitrator will decide their dispute without bias or consideration of their interests, and based exclusively on the factual and legal merits of the case. The parties

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typically, nonetheless, contract with the med-arbitrator for just such a decision on the merits. What they receive is not true due process arbitration, despite its label. The med-arbitrator's judgment is likely to be based on the med-arbitrator's perception of their interests, in part as disclosed in caucus.

Take for example a case where Party A benefits from a legally binding contract that would be enforced by summary disposition in litigation. Party B has an entirely sympathetic and fair position in the dispute, entitling it to most of the relief that it seeks. An arbitration award should be 100% for Party A. However, a mediated resolution should be 50% or more in favor Party B. It is highly unlikely that a med-arbitrator after meeting in caucus with both parties, and understanding their respective interests, will return an arbitration award 100% for Party A, notwithstanding Party A's entitlement to that award on the merits. This is because the process will have shifted from "rights" arbitration to "interests" arbitration.⁸ Party A, upon agreeing to med-arb, had better understand that its legal rights are unlikely to be enforced in the med-arb award. The selection of the med-arb process, in large part, selects the result.

Med-arb should not be used if the parties desire or expect to receive a decision based exclusively on the factual and legal merits of the dispute. What they will receive, instead, is a binding resolution in arbitration, crafted by a third party according to his/her perception of each party's interests. The med-arbitrator having failed to persuade the parties to settle according to terms that he/she thinks to be fair, simply orders his/her chosen result at the end of the proceeding.

Conclusion

Parties contracting for med-arb should appreciate that they will receive neither a resolution in mediation born entirely of uncoerced,

facilitated negotiation around their interests, nor an arbitral decision based exclusively on their legal rights and remedies as established by legally relevant facts. Instead, they will relinquish their rights to agree to a negotiated result that they believe to be fair by delegating to a third party med-arbitrator the power to order what he/she perceives to be the "fair" result, based upon his/her evaluation of the parties' interests. In situations where the importance of resolving the dispute outweighs each party's need for an acceptable result, med-arb may be a useful process. Parties in need of a subjectively fair result, based upon either the merits of their claim, or their own perception of their interests, should approach the suggestion to engage in the med-arb process with extreme caution. ❄️

1. James T. Peter, Note & Comment: Med-Arb in International Arbitration, 8 Am. Rev. Int'l Arb. 83 (1997).
2. Peter, *supra*, p. 97.
3. Lela P. Love and Kimerlee K. Kovach, An Eclectic Array of Processes, Rather than One Eclectic Process, 2000 J. Disp. Resol. 295, at 297.
4. Emilia Onyema, The Use of Med-Arb in International Commercial Dispute Resolution, 12 Am. Rev. Int'l Arb. 411, 415 (2001).
5. Onyema, *supra*, p. 416.
6. Peter, *supra*, p. 91.
7. Carlos DeVera, Arbitrating Harmony: 'Med-Arb' and Confluence of Culture in Rule of Law in the Resolution of International Commercial Disputes in China, 18 Colum. J. Asian L. 149 (Fall, 2004).
8. DeVera, *supra* p. 156.