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Arbitration in the United States Today - A Multifaceted Response to the Economics of Dispute Resolution

*Clifford L. Whitehill**

I. LAWYER'S RESPONSIBILITY TO USE AND INFORM CLIENTS OF ADR

There is a growing recognition among members of the U.S. legal community that resolving disputes is not the exclusive domain of the court system. The rapid growth of the alternative dispute resolution (ADR) movement over the last fifteen years attests to this.

ADR is a term which refers broadly to alternatives to court adjudication of disputes: negotiation, mediation, arbitration, and various hybrids. There is nothing new about many of these processes. Negotiation is what lawyers do most of the time. What is new is the recognition that such processes work to achieve much better results when they follow what are now well developed patterns and forms.

Arbitration practice can be traced back to the late 1700s in New York. Mediation has been part of American culture since the early days of this country when Jewish and Chinese communities preferred it to an alien legal system. It is reported that George Washington had an arbitration clause in his will to settle disputes among his heirs, and that Abraham Lincoln arbitrated a boundary dispute between two farmers when he practiced law.

ADR developed as a movement within the legal infrastructure as a direct consequence of or response to the litigation explosion of the early 1970s. It has flourished through the work of court reformers, legal scholars, and cultural anthropologists.

The majority of private lawyers have reacted more with inertia than with resistance, seeing no reason why they should alter long-standing habits by incorporating ADR into their practice. Not surprisingly, our unique allowance in the United States of the lawyer's contingent fees often motivates the lawyer to prefer trial, thereby getting a chance to tap into a large verdict.

Although a growing number of lawyers know what the acronym ADR means, relatively few have ever considered its use. Indeed, most practicing lawyers still do not know the difference between mediation and arbitration, how summary jury trials, mini-trials and other ADR

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procedures are conducted, or why and when to use them. One reason for this indifference is that corporate clients, despite their enthusiasm for ADR, rarely ask outside counsel to consider or use ADR. Concerns about appearing "wimpish" inhibit many lawyers from even mentioning ADR to clients.

Why should a lawyer practice ADR? To propose that law firms develop expertise in ADR and integrate it into their practice is simply a recognition that ADR is increasingly required to properly service clients. Escalating litigation costs, over-crowded court dockets, growing client awareness, and the mounting sophistication of a relatively small number of ADR practitioners in devising and implementing ADR mechanisms all point to the need. In addition, the movement by courts and legislators to mandate ADR as an adjunct to, or substitute for, litigation adds momentum. The single most important reason for developing law firm expertise in ADR is that ADR can generate a better resolution of certain disputes more expeditiously and less costly than litigation can.

Client interest in ADR is based, at least in part, on disenchantment with the legal profession's performance as cost-effective dispute resolvers. Although most filed lawsuits are settled without adjudication, the problem, according to many clients, is that compromise comes too late, is too expensive and is too stressful. Because of this, litigation often fails to produce a favorable result even for the "prevailing" party.

In-house counsel at many companies have become more sophisticated in the use of ADR procedures and other cost-effective mechanisms than outside counsel. Corporate clients are increasingly seeking alternative forms for the resolution of disputes and are designing and implementing ADR procedures without the help of outside counsel.

There are several reasons why the private bar has been resistant to ADR. First, the culture of the law is a litigator's culture, a culture of "winners" and "losers." Traditionally, lawyers have been trained in law school to litigate.

The law of inertia dictates that it is difficult to change the way lawyers think about dispute resolution. Concerted efforts need to be made to sensitize lawyers "to skills, attitudes and actions that are productive to agreement rather than contention." Lawyers should be able to provide counseling in the full range of ADR procedures and trained to consider doing so not just once, but at various stages of a dispute's evolution.

Resistance to ADR by some attorneys and commentators has also been grounded in concerns about a possible diminution in professional responsibility, a lowering of ethical standards as a result of perceived tensions between a lawyer's so-called "conciliatory" role as ADR adviser, and his canonical responsibilities to zealously advocate the interests of his client. However, attorneys have long advised clients to negotiate and settle disputes when of the opinion that doing so is in the clients best interests.

Indeed, the aggressive pursuit of such seemingly conciliatory courses of action in appropriate cases is often the hallmark of zealous advocacy. Clearly, the same is true of pursuing ADR options.

Both the ABA Model Rules of Professional Conduct and the Model Code of Professional Responsibility sanction such courses of action and fully support efforts by the bar to counsel clients about ADR options. ABA Model Rule of Professional Conduct 1.2(a) calls upon the lawyer to "consult with the client as to the means by which [the client's objectives] are to be pursued." Ethical Consideration 7-8, contained in the Model Code of Professional Responsibility, instructs the lawyer to ensure that a client's decisions are made only after the client has been informed of relevant legal and non-legal considerations and of the possible effect of "each legal alternative." Ultimately, "the decision whether to forego legally available objectives or methods because of non-legal factors is for the client and not for the lawyer."

Many lawyers are uncomfortable with involving a client with what they perceive as strategy. But if the mission is to help clients find the best way to handle a dispute, not merely by litigation, but also by a variety of other available techniques, why should it not be part of the explicit professional obligation to canvass those options with clients? How would we feel about a doctor who suggested surgery without exploring other possible choices?

Perhaps a number of lawyers are not fulfilling this responsibility because of the nagging thought that to do so may hurt them financially, again raising the question of the widespread use of contingent fee arrangements.

Some attorneys insist that their clients want to win rather than settle or mediate, but it is the client who should make that decision after being fully informed of all the available options. We might be surprised by the choices some clients will make when they are candidly told the expected final costs versus the benefits of a lawsuit.

How might an obligation to discuss ADR alternatives with a client be implemented? There are a number of possible approaches. Attorneys could hand out a brochure that describes the most common alternatives and discuss these options with their clients. As part of an attorney's pre-trial submissions, he could be required to certify compliance with the obligation to discuss ADR. Such an approach is about to be initiated in Jackson County, Missouri.

ADR is not a panacea and is not appropriate for every dispute. But integrating ADR into a firm's practice will lead to better settlements of disputes by sensitizing outside counsel to their critical role as problem solvers, and to the many factors that should be considered in determining what dispute handling mechanisms will best serve a client's interests. At my company, General Mills, we solve the problem in advance by requiring all written contracts to contain an ADR provision.

II. STATE COURT USAGE OF ADR

Since its creation in 1986, the Conference of State Court Administrators (COSCA) Committee on Alternative Dispute Resolution has monitored both the development of court-connected ADR programs and research into ADR's effects on dispute resolution. Based on the information gathered in these pursuits, the ADR committee has recommended that courts explore the use of alternative processes that are organized to permit appropriate court supervision and evaluation, and designed and managed to promote faster, less expensive, and better ways to resolve disputes. At the ADR committee's request, the American Bar Association has reflected this perspective in its treatment of ADR in its Standards Relating to Court Organization.

In a recent report to the COSCA membership, the ADR committee presented its position on the court's responsibilities in instituting ADR programs and discussed some of the issues that the ADR movement raises for the administration of justice. The report included the ADR standards, incorporated in the American Bar Association Standards Relating to Court Organization, and a bibliography of further sources of information. The report is an educational resource for COSCA members and others contemplating the institution of court-annexed or court-referred ADR programs.¹

Over the past several years, more and more state courts have embraced the ADR strategy known as the "settlement week." Now, Texas has taken a step that will transform the trend into a tradition. There, a state law requires all its larger courts to hold two settlement weeks each year. The Texas statute institutionalizes on a grand scale an ADR practice that heretofore has been used primarily on an ad hoc, court-by-court basis.

During settlement weeks, the courts close, and local lawyers, judges, and parties strive to mediate settlements to long-pending cases. In the state courts that have tried the technique to date, the results have been impressive, with settlements reached in large numbers of cases, and with the local legal community eager to make the "week" an annual event.

The Texas law takes the "week" to an even higher level. This was dramatized in the last week of September 1990, when 150 state courts in a dozen counties closed and local lawyers, judges, and disputants mediated well over 2,000 pending lawsuits. Lawyers with the required training served as mediators in these efforts.

According to Jim Hutcheson, general counsel of the Texas Office of Court Administration in Austin, the statute, which took effect on August 28, 1989, specifically mandates two settlement weeks per year in all

¹ A copy of the report can be obtained from the CPSCA ADR Committee, National Center for State Courts, 300 Newport Avenue, Williamsburg, Virginia 23187-8798.

Texas counties with a population of 150,000 or more. Mr. Hutcheson estimates there are fifteen counties of such size in the state.

The law says the two "weeks" can be held either during law week in May, during the state judiciary's judicial-conference in September, or during any other weeks the particular court designates. Most courts find the May and September dates the most convenient.

III. FEDERAL COURT USAGE OF ADR

The U.S. District Court for the Northern District of California has sponsored six special procedures to facilitate dispute resolution. Some of these, such as early neutral evaluation, court-annexed arbitration, and reference to a special master, are court ordered in certain categories of cases and initiated by the parties in others. Other procedures, including non-binding summary jury trials, bench or mini-trials, and trials before a U.S. Magistrate are strictly voluntary.

ADR options are offered by other federal courts, including the U.S. District Courts in Michigan, Massachusetts, and the District of Columbia. Judges in the U.S. District Court for the Western District of Michigan are permitted by local rule to order cases into nonbinding mediation, arbitration, summary jury trials, and mini-hearings. The Michigan court's Local Rules prescribe detailed procedures for each of these ADR processes.

In Washington, D.C., the U.S. District Court recently initiated experimental early neutral evaluation and mediation programs, and the Court of Appeals has adopted a mandatory mediation program. Cases in the Court of Appeals are selected for mediation by the Court's Chief Staff Counsel. By contrast, participation in the district court's ADR programs is strictly voluntary. Ten other federal district courts have court-annexed arbitration programs in which cases below a threshold amount - some as high as \$150,000 - are automatically referred to arbitration.

IV. FEDERAL AGENCY USAGE OF ADR

There is a green light for United States government agencies to use ADR. Following a decade in which a handful of federal agencies pioneered the practice of ADR in the public sector, Congress has enacted a landmark law that authorizes and promotes ADR use throughout the national government. The Administrative Dispute Resolution Act of 1990 (P.L. 101-552) (ADR Act) is aimed at bringing a variety of alternative methods of dispute resolution to the thousands of cases in which the federal government is a party. For example, in 1989, 55,000 of the 220,000 lawsuits filed in federal courts featured the national government as one of the disputants. That daunting statistic does not include the tens of thousands of cases involving the government that are handled administratively.

The ADR Act does not mandate the use of ADR. In all instances,

the government and the private parties must both consent to it. But the law requires every federal agency to adopt an ADR policy, explicitly authorizes agencies to use ADR, and greatly facilitates and promotes its use through a host of amendments to the Administrative Procedures Act and other statutes. The new law, which carries a five year sunset provision, was introduced by Senator Charles E. Grassley of Iowa in May 1989 (S. 971). The House bill, H.R. 2497, was sponsored by Representative Dan Glickman of Kansas.

A major player in the new law is the Administrative Conference of the States (ACUS). ACUS, an advisory group charged with helping federal agencies improve their procedures, has championed greater federal use of ADR since the mid-1980s. The group took a leading role in drafting this specific statute. Under the terms of the law, ACUS will advise agencies about their ADR policies, set standards for neutrals who will preside over ADR proceedings, collect data on agency ADR use, and perform other tasks.

Signed by President Bush on November 15, 1990, the new law is one of three major pieces of ADR legislation enacted by the 101st Congress. The second, the Civil Justice Reform Act, sets an ambitious plan for using ADR and case management techniques in the federal courts. The third, the Negotiated Rulemaking Act, establishes guidelines for a popular ADR process for drafting administrative rules and regulations.

In the introductory section of the Administrative Dispute Resolution Act, Congress observes that the private sector has made great and profitable use of ADR, and declares that government agencies should seek the same benefits. However, a Senate report on the bill observes that "up to now there has been no government-wide emphasis on the use of ADR techniques." The Act provides first, that its terms apply to nearly all federal disputes, including those based on "formal and informal adjudications," "rulemakings," "enforcement actions," "licenses or permits," "contract administration," and "litigation brought by or against the agency." The law gives similarly broad scope to the types of ADR it allows, including "settlement negotiations, conciliation, facilitation, mediation, factfinding, minitrials, and arbitration, or any combination thereof." The Act then directs all federal agencies to adopt a policy on use. To do so under the terms of the statute, an agency must consult with ACUS and must examine the kinds of disputes on the agency caseload. Furthermore, the law gives several specific commands to encourage the development of a serious, actively deployed ADR policy.

The statute goes on to declare that every agency "shall designate a senior official to be the dispute resolution specialist." This specialist is responsible for ensuring agency compliance with the law and for effectuating the ADR policy the agency develops.

The Act also requires all agencies to provide training on a regular basis both to the appointed ADR specialist and to all other employees involved in formulating and implementing the ADR policy. Further, it

directs every agency to review its standard contracts and grants agreements with an eye toward possible amendments to those forms in order to "authorize and encourage the use of dispute resolution."

After giving these detailed instructions to federal agencies, the ADR law next provides the agencies with implicit authority to use ADR on a consensual basis. This grant of authority clarifies a confused area. Many observers have argued that some federal agencies are not permitted to use ADR, or certain types of ADR, for various reasons. In addition to the full and express grant of power, the new law dispels such confusion with other provisions, including the arbitration procedures described below.

While the new law encourages agencies to use ADR in a wide range of possible disputes, it also sets out several factors or circumstances that may indicate the inadvisability of ADR in a particular case. For example, the law states that ADR may be inappropriate if the matter is of great "precedential value," or if it "significantly affects persons or organizations who are not parties to the proceeding," or if "a full public record of the proceeding is important."

As noted above, the new law allows parties to agree to either non-binding or binding ADR procedures. The latter, raises special issues and the new statute consequently devotes several sections to these issues. To assure the consensual nature of the arbitration, the law forbids agencies from making an agreement to arbitrate a precondition for entering a contract or obtaining a benefit.

The law also provides that an award becomes final thirty days after issuance. However, at any time before that, the head of the agency involved can vacate the award or terminate the proceeding if an award has not yet been rendered. Thus, technically, the arbitration is nonbinding on the government. The primary purpose of this provision is to answer a variety of constitutional and statutory arguments forwarded by the Justice Department about the bill.

V. ADR OF EMPLOYMENT DISPUTES

It is customary today to find well developed grievance and arbitration procedures employed by companies for union employees. Faced with an unprecedented volume of litigation by former employees claiming that employment terminations were unlawful, employers have begun to use alternative dispute resolution mechanisms, including similar grievance and arbitration procedures, in an attempt to promote practices designed to further sound relations between management and employees not represented by a union. Just as the arbitration remedy promotes industrial peace in a unionized company through a private contractual system of dispute resolution, so too in a nonunion company can a binding arbitration system be a stabilizing force in the workplace.

The question of exclusivity and finality of private arbitration agreements is supported by federal and state law policy favoring arbitration of

disputes. The Federal Arbitration Act (FAA) flatly declares that an arbitration provision "shall be valid, irrevocable and enforceable. . . ." The Supreme Court stated in *Southland Corporation v. Keating* that "[i]n enacting Section 2 of the FAA, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration." The FAA's policy favoring arbitration is carried out by a rigorous enforcement of arbitration agreements through orders compelling arbitration and orders staying litigation, and by limiting the scope of judicial review of arbitration awards.

In two recent decisions interpreting the FAA, the Supreme Court has held that state laws which would operate to defeat enforcement of arbitration agreements by allowing a judicial forum for claims subject to arbitration are preempted by the FAA. In *Perry v. Thomas*, the Court held that California Labor Code Section 229, which specifically provides for a judicial forum for the collection of unpaid wages despite any arbitration agreement, was preempted by the FAA. Thus the employee's state court suit against his employer for breach of contract, conversion, conspiracy and breach of fiduciary duty arising out of a commissions dispute was subject to the arbitration agreement in the plaintiff's employment contract.

Similarly, the Supreme Court held a few years earlier, in *Southland Corporation v. Keating*, that a provision of the California franchise investment law that purported to require judicial resolution of claims, notwithstanding an agreement to arbitrate, was preempted by the FAA. Therefore, the federal law in favor of agreements to arbitrate should preempt state law wrongful discharge actions based on federal laws when the parties have agreed to arbitrate in a nonunion setting.

To fall within the ambit of the FAA, an arbitration system in a nonunion setting must meet two threshold requirements. First, there must be a written agreement to arbitrate. Second, the arbitration agreement must be in a contract involving commerce. Congress enacted the FAA pursuant to its authority under the commerce clause of the Constitution. The United States Supreme Court has routinely held that Congress' powers pursuant to the commerce clause extend to transactions and activities having only the slightest relationship to interstate commerce. Therefore, most suits by employees will fall within the commerce test.

The system of industrial self-government envisioned by federal law is in danger of being bypassed in favor of state law actions for wrongful or retaliatory discharge. Some state laws provide generous remedies for tortious discharge, such as punitive damages that employees would ordinarily not obtain through grievance and arbitration procedures under collective bargaining agreements. Employees will have more incentive to pursue state remedies leading to the further undermining of the exclusivity and finality of private arbitration of labor disputes under the FAA.

Faced with an unprecedented number of lawsuits for wrongful or

retaliatory discharge, there is a clear need for state courts to adopt the federal policy in favor of agreements to arbitrate employee/employer disputes. The grievance and arbitration system remedy has traditionally promoted stability in industrial relations and should not be undermined by creative pleading to avoid federal jurisdictional requirements.

There can be no doubt that ADR can offer significant benefits to both the employer and employee. At the very least, ADR gives the employer the opportunity for first review of an employee dispute. An employee dispute which is presented to an employer's internal ADR system may be the employer's last chance to resolve the matter without resorting to costly litigation.

In general, an internal ADR system will prove to be a cheaper and faster method of resolving employee disputes. Moreover, an internal ADR system will allow the employer to identify an employee complaint that is truly meritorious. The employer will also be able to identify and address serious management problems before they can generate additional litigation.

In conclusion, the ADR process used in a nonunion setting has not been widely accepted by employers or employees. Employers do not understand the benefits of ADR and, consequently, do not feel the need for a formal dispute resolution system. Those employers may be concerned that easy access to such a system may cause more employees to dispute their termination. Employers mistakenly would rather maintain status quo management control over employee disputes. Employees, in contrast, tend to view the ADR process as a mere extension of management. To overcome these misconceptions and to make ADR a success, efforts must be made by the employer to institutionalize the ADR process. Employees must be convinced that the ADR system will provide merit-oriented decisionmaking. Only then will ADR's significant economic and legal benefits be realized by both the employee and employer, benefits that are now being enjoyed in many other areas of commerce.

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