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Add ADR to your business contracts before disputes arise

Many legal conflicts arise between people or between institutions whose interactions are episodic, or unplanned-personal injury, for example, or disputes between competitors who are not linked by privity of contract. In such instances alternative dispute resolution can only be chosen after the dispute has arisen.

However, in many business relationships the majority of interactions that give rise to disputes are created or governed by contracts entered into in advance. It is possible for dispute resolution and conflict management also to be planned for in advance.

Guest Column

William C. Barrett III

Needless to say, the best time to agree on a sensible way to resolve a contractual dispute is when the parties are negotiating their business agreement and before any dispute has arisen. In the atmosphere of businesslike cooperation that typically prevails at that juncture, agreeing on rational, fair dispute resolution procedures can be a relatively simple task. Once a dispute has erupted, it can be much more difficult for parties to agree when they are adversely positioned.

As many litigating attorneys will attest, presenting an ADR solution to a furious client is not in the best interest of the firm and, hence, the attorney. Dana D. McDaniel, an intellectual property litigator for Williams, Mullen, Christian & Dobbins in Richmond, states that, "When a client engages an attorney, he or she is typically looking for aggressive representation and results. I think many lawyers hesitate to suggest mediation-no matter how appropriate-as a first-line solution for fear that the client will perceive the lawyer as not being aggressive." This understanding among litigators, known as avoiding the "weak knee" appearance, is common.

However, when contracts carry ADR clauses, a proactive and planned-for mechanism guides the parties in resolving breaches and provides a cure for non-conformance. ADR users testify that it is far easier to get agreement to use ADR processes at the point of entering agreements rather than after disputes break out.

This accord is accomplished through the use of an ADR clause inserted in the body of a contract. In essence, the clause stipulates that the parties shall first attempt to solve their problems with alternatives to litigation. The rest of this article will address aspects of drafting good ADR clauses.

Drafting ADR Clauses

The literature on drafting ADR provisions is scant. Virginia form books offer minimal treatment of arbitration and none on mediation.

However, the following guidelines should help corporate counsel and law firms in beginning a comprehensive ADR systems design for their companies and clients. A sample dispute resolution clause is provided as a sidebar below.

As with other contract provisions, specificity can be important in mapping out dispute resolution in a contract. An attorney should provide answers to questions, such as: Who and how the process is initiated? What events will trigger it? and Which resolution procedures will be used?

But these ADR provisions will require some sophisticated considerations. The specification of particular disputes must be done precisely, especially in threshold amounts or underinclusive language. Here is a drafting tip: The 9th U.S. Circuit Court of Appeals recently ruled that the phrase "arising out of may not be as broad as it sounds in triggering contract clauses. Carl G. Love of Cushman Darby & Cushman in Washington suggests appending the phrase "or relating to" to the phrase "arising out of."

Multi-Step Provisions

One of the most promising of the new clause designs is the "multi-step" or escalated ADR clause. Attorneys may need to overcome the parties' objections to pre-dispute clauses being added to contracts. Using a variety of ADR approaches can make these clauses more palatable.

For years the only ADR clause used was for mandatory and binding arbitration. The ADR movement still uses binding arbitration, but it is consistently being relegated to "last place" status.

Instead, contracts can begin with clauses that do not contain binding or final determination results, and leave parties in control of the process and the outcome, giving management on all sides the most comfort. These clauses can contain evaluative options such as neutral factfinding and evaluations but should not be binding.

Two-, three-, or four-step resolution begins within the usual decisionmaking structure of the contracting parties and escalates outward. For example, the first step would establish negotiations between line managers before escalating to executives. Next, unresolved matters would be submitted to mediation and then to mini-trial. A third step would provide for binding or non-binding arbitration.

Rules for conducting dispute resolutions are already available from the American Arbitration Association, the CPR Institute for Dispute Resolution (New York) and some private ADR providers. These can be incorporated by reference, after the attorneys have selected a set of rules that best fit the needs of the parties to

William C. Barrett 111 is a principal in Barrett-Framme Mediation in Richmond. He also is a Virginia Supreme Court Certified Mediator, a Certified Public Accountant, and a Certified Tax Professional.

the contract.

Clauses from CPR were used in the writing of this article.

As for selecting the neutrals who will help resolve a dispute, a departure from the typical arrangement may be warranted. Often disputes will be resolved by a three-member panel, with each side selecting a neutral and the two neutrals selecting their third colleague. Problems can arise if the procedure is drafted too strictly. Typically, in arbitration clauses, if a party misses the deadline for choice, the arbitration will commence with only one party's neutral making the third-person selection. The sessions commence with only two neutrals, each chosen by one side.

It is better to provide that if one party fails to name a facilitator within the agreed time, a disinterested third party will be called upon instead to name a neutral.

Cooling off

An ADR clause should take into account legitimate concerns that one party or the other will win a "race to the courthouse" if non-binding ADR is unsuccessful and if the parties are not committed to engage in binding arbitration as the final step. Providing for a "cooling off' period is an aid in many ways, not least among them is the possibility of bringing parties back together after re-thinking cloudy or volatile issues. Also, clauses should provide for provisional relief or for tolling a statute of limitations.

Confidentiality also requires some attention. Most consensual proceedings are facilitated settlement negotiations and as such are entitled to the protection accorded by Rule 408 of the Federal Rules of Evidence and the Code of Virginia.

Neutrals in commercial cases facilitate, mediate, arbitrate, etc., by contract. Their protection against being drawn into administrative proceedings as witnesses or having dispute documents discovered is by the same contract. The Code of Virginia §§ 8.01576.1 et seq. protects in court-referred mediation proceedings, but can be binding on 376 (VLW 095-6-066).

Discovery

Since ADR is about win-win solutions to disputes, and *not* about winning a dispute, much of the discovery process can be streamlined. Both neutral and expert factfinding enables the parties to assess their respective positions and to facilitate resolution.

Language that instructs the parties to "permit the neutral(s) to facilitate such discovery as shall be determined appropriate in the circumstance(s)..." will help in the exchange of relevant documents and information in both nonbinding and binding ADR.

Sample dispute clause

10. **Mediation /Arbitration**

10.1 In order to expedite the prompt resolution of any dispute, controversy or claim (hereafter referred to as "dispute") which may arise under this agreement, the parties mutually agree that the procedure set forth below will be utilized by each prior to any party instituting any legal proceedings against any other party:
(a) In the event a dispute shall arise between the parties under this agreement the aggrieved party shall provide the other party(s) with a written notice (pursuant to the notice provision of this agreement) setting forth the nature of the problem and parties or contact persons identified in 10.3 below as the dispute resolution representative. The party's representative will be of such senior management as to have authority to settle the dispute (and will not have direct responsibility for administration of this agreement).
(b) The dispute resolution representative shall immediately attempt to resolve the dispute by communication within their own firm and with the authorized representative of the other fi rm(s). (c) If the parties are not able to effectuate a resolution of the dispute within 15 days of receipt of written notice, either party shall submit the issue to mediation under the Rules of Submission of (a named mediator) or through another mediator or dispute resolution firm acceptable to both parties.
(d) The mediation process described in (c) above shall commence within 15 days of failure to reach agreement by direct discussion (a maximum of 30 days from receipt of written notice of the dispute pursuant to (a) above). This time limit may be extended by mutual agreement of the parties.
(e) Mediation of the dispute shall be conducted promptly with the full cooperation of the parties and shall be completed within 15 days of commencement unless (i) the mediator shall declare the parties at an impasse, (ii) the time period is extended by the mediator, or (iii) the parties mutually agree to extend the time period for mediation.
10.2 In the event the parties are unable to resolve their differences by the process outlined in 10.1 above, they shall:
(a) Submit to arbitration through {a named mediator), the American Arbitration Association. CPR Institute for Dispute Resolution, or another arbitrator acceptable to both parties by (a sole arbitrator or three arbitrators, of whom each party shall appoint one). The arbitration shall be governed by the United States Arbitration Act, 9 U.S.C § l -16, and judgment upon the award rendered by the Arbirtrator(s) may be entered by any court having jurisdiction thereof.
(b) The place of the arbitration shall be (specify location or that location decided by agreement). (c) The Arbitrator(s) (are/are not) empowered to award damages in excess of actual damages, including punitive damages.
10.3 The procedures specified in this Article 10 shall be the sole and exclusive procedures for the resolution of disputes between the parties arising out of or relating to this agreement; provided, however,
(a) That a party may seek a preliminary injunction or other preliminary judicial relief if in its judgment such action is necessary to avoid irreparable damage.
(b) Despite such action the parties will continue to participate in good faith in the procedures specified in this Article 10.
(c) All deadlines specified in this Article 10 may be extended by mutual agreement.
(d) All applicable statutes of limitations shall be tolled while the procedures specified in Article 10 are pending. The parties will take such action, if any, required to effectuate such tolling.
10.4 The designated dispute representatives for each party are set forth below:
For ABC Company: {The Managing Director (Name?)} For XYZ Company: (Vice President - Sales (Name?))