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HONG KONG MEDIATION LECTURE

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The Benefits and Technical Challenges of Combining Mediation with Arbitration as Complementary Processes (Beyond Oranges)

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What an honor to participate in history-making in Hong Kong!

In thinking about the events of this week—these marvelous programs—and now this inaugural lecture, I am reminded of a friend of mine we lost entirely too soon. I am talking about David Caron, perhaps known to many of you. A fellow California-based law professor, he later also spent several years as the Dean of Kings College, London's law faculty before returning to the Iran-US Claims Tribunal.

During his remarkable life, David had leadership posts in many professional and academic organizations. Putting aside his drive, lovely demeanor and fine intellect, his success in leading these organizations reflected his understanding of the importance of community building, a principle which he applied whether it was for the 100 year old American Society of International Law or for the somewhat younger Institute of Transnational Arbitration.

It strikes me that this event tonight is at least in part an opportunity to grow our community—the mediation community in Hong Kong (and beyond). That so many of you have come tonight, and in many cases from far away, is already indeed promising.

One of the challenges in presenting remarks to a wonderfully diverse group such as this is that there are inevitably people who could easily replace me before the microphone and, indeed, do a better job, while there will be others who are rather new to the topic.

That mix is not so different from my LLM classes, in which I find mid-career lawyers from blue-chip law-firms next to smart enthusiastic recently-qualified lawyers.

The point is: ultimately you have asked a teacher to make remarks, so I hope I will be forgiven for doing what I do in the classroom, which is to aim for somewhere in the middle, while throwing the advanced students some brain-teasers and the new entrants to the field the occasional life line.

The topic I have been asked to address is:

"The Benefits and Technical Challenges of Combining Mediation with Arbitration as Complementary Processes"

And, I am going to add the subtitle "Beyond Oranges".

Here I should warn you that—in the spirit of building two way communication in our community--I am going to ask you at the end of my prepared remarks to vote on a question of process design. So ready yourselves!

I actually teach four courses per year at Pepperdine's Straus Institute, but technically, they are all straight international arbitration topics. My hope is someday to teach a course called "international disputes process design"—and I have gone so far as to outline a catalog description for such a course, should I ever be consulted about what courses to add to what is already a very rich curriculum.

Regardless, I always manage to work into the class-room the notion that even with its somewhat settled structure, arbitration remains reasonably flexible and especially with the parties' consent there is a great deal one can do to innovate using other techniques--especially mediation.

I am to some extent the victim of an English education, as my British friends like to say, and so I am entitled to use the adage I learned from them: That is: "there are horses for courses"—I assume that refers to horse racing and the fact that some horses are good at one distance, others at different length course, some can jump, some not so much, some are better on a muddy track—and so on.

A quick trip to the internet teaches us that there are many ways to classify horses and more types than you might have imagined—and, so it is with dispute resolution techniques.

In the classroom I generally like to go from general to specific so that when, as inevitably happens, we find ourselves in the weeds, we can find our way back to basics.

In talking international dispute resolution techniques, I thus start with a flow chart with three branches or categories- category one is the "adjudicative" branch and category two is the "collaborative branch" –and then-- in the middle of the flow chart-- I have a branch called hybrid methods (essentially a third category).

As you will probably have guessed, the adjudicative branch consists in litigation and arbitration. Both rely on third party decision makers. These are processes that –when taken to their intended conclusion--produce a particular kind of finality: a determination by a third party empowered to create "preclusive effects' that is to say: to produce outcomes that are *res judicata*.

The collaborative branch of the flow chart is exemplified by negotiation and mediation. These are, by contrast to adjudication, techniques that –if all goes well--end the dispute by settlement, but in and of themselves can go no further. They have in common that the process and outcome is to a great extent voluntary, and to that extent within the control of the parties.

Whereas, litigation and arbitration, contemplate that although the parties may have a certain level of autonomy to shape the process (especially in arbitration) ultimately the result is imposed on them by the empowered third party—be that the judge or the arbitrator.

With adjudication, of course, there is a corresponding measure of risk, as you generally do not really know the outcome until it is announced.

Some of you were in Los Angeles a few weeks ago when I gave my version of the well-traveled story of the oranges.

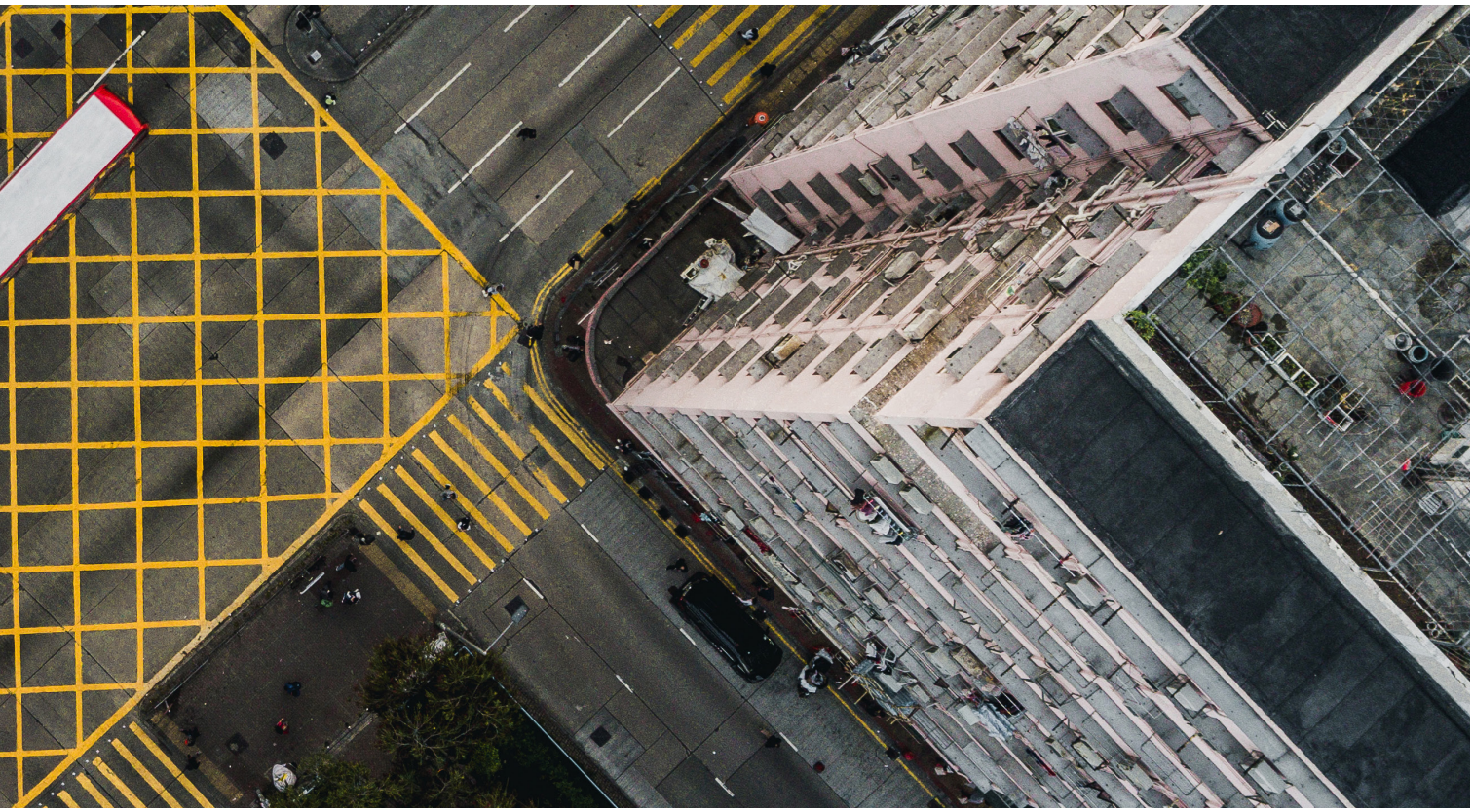
My students know that I permit myself to re-use a hypothetical provided I add a flair, or a new dimension, and I intend to do that here (hence "beyond oranges").

So, imagine a dispute over a commercial quantity of oranges. For the time being they are well cared for in a refrigerated warehouse. Two disputants both claim the right to dispose of the oranges.

There is no contract clause between them dictating the method of resolving the dispute; indeed, between them there is no contract at all.

One party claims it has a superior right to the oranges because that party—whom we'll call the buyer (Dundee Ltd.)—entered into what it regards as a valid international sale of goods contract with the grower.

The other party (a diversified conglomerate involved in myriad activities) claims a superior right to the oranges because the grower of the oranges borrowed money from it and pledged the oranges as collateral. The loan was not repaid.



Option One: Let's assume the parties decided to arbitrate. The value of these organic oranges, by the way, is about 1 million US dollars. Not a huge case in terms of amount in controversy, but you may add as many zeros as you like provided that we agree that at some point a larger case may require us to adjust the design of our disputes architecture.[1]

With the help of an institution, a sole arbitrator is empaneled, and after the usual administrative matters, the tribunal sets as a preliminary matter the question of governing law or laws. Note that the Grower is based in Country A, the putative buyer (Dundee, Ltd) is based in Country B and the lender/creditor is based in Country C. The loan was negotiated in country D and the alleged Sale of Goods contract was negotiated on a yacht in international waters. (You'll appreciate I am trying to construct a difficult governing law scenario).

The purported sale-of-goods contract is silent on governing law, and even if the grower and putative buyer (Dundee) designated the proper law of contract, that designation might not govern the agreement between the grower and the lender/pledgee.

Obviously, it would be helpful to the parties for pleading purposes to know what law or laws the tribunal will ultimately consult, and so the question is set out as a preliminary matter for separate briefing and argument.

After there has been expended three months and $100K each in legal and expert fees, and $25K in tribunal fees, the arbitrator issues its ruling on governing laws, and invites the parties to begin briefing the merits based on that determination.

Legal teams on both sides advise their clients to budget another $75-150 thousand dollars to get through that next briefing phase. And, both sides launch a search for foreign law experts with whom to consult, and ultimately sponsor before the tribunal.

Now the arbitral method would certainly be able to reach a result eventually, presumably in the form of an award of declaratory relief. There would be a winner and a corresponding loser.

Assuming the award is not set aside in a court at the seat of arbitration, the award would in turn benefit from a global treaty regime that should facilitate its recognition in most countries of the world. (I'm referring –of course—to the New York Convention).

That Convention requires national courts to give effect to both written agreements to arbitrate and to foreign arbitral awards. Those twin obligations have helped make arbitration first among equals for international commercial disputes.

But, let us turn back the clock, and change from arbitration to Option 2: Mediation. Assume that rather than a sole arbitrator, a sole mediator is appointed to deal with the oranges dispute.

1. There is a chain in the United States, and perhaps also in your jurisdiction, called "Whole Foods Markets". The standard joke is, given the pricing of the premium groceries they sell, the name should be changed to "Whole Pay-Check Markets". So, it is entirely possible that my hypothetical $1 million (US) for these oranges is indeed too low.

Being well versed in private international law, that mediator quickly realizes that the governing law and third party issues will generate great unpredictability of outcome if entrusted to a court or arbitral tribunal.

But this is mediation. The legal back-drop is secondary. As the text book says, the question is one of interests, not legal rights. And so the mediator sets out to understand the dispute—not as an arbitrator would, but with the mindset of a mediator.

Very early in the process—perhaps in ex parte meetings known as a caucuses—she asks each party why they want the oranges.

It turns out: the lender has an affiliate company that will pay well for the right to take the juice from these high quality oranges.

The other party—Dundee—in turn, is Scotland's premiere maker of thick-cut marmalade. It will only use the oranges' peels. (In fact, for it, the juice actually is a bit of a nuisance).

And so, as usually happens in the oranges hypothetical, the classic win-win deal quickly presents itself: Each party shall have the parts of the oranges its desires according to a detailed agreement on shared custody that they work out rather quickly with the help of the mediator; one will own the juice, the other: the peels.

Notice that was an outcome the parties engineered and controlled —it was not one the mediator was empowered to impose on them. She only guided the process and proposed a solution; then, she helped structure the sharing arrangement.

By the way, legal fees in total were 25 thousand US dollars, and the mediator billed for two days' time—around $15,000.

Sadly, no private international law professors were employed as experts. (The choice and content of governing law, after all, were not controlling, but—no doubt—the potential complexity that those issues presented was a factor used by the mediator in promoting settlement).

The widely-traveled story of the oranges is designed to show how one might be able to find a win-win solution using mediation. But, the example as it stands remains an exercise in merely distributing a fixed pie, albeit in an ingenious way.

Consider the flair I mentioned (and the beyond oranges element). That is, let's expand the proverbial pie. Thus, assume that both parties still harbored doubts about settlement. (After all, the lawyers on both sides had told their respective clients that each had a really good case). So, the mediator reengages.

She asks the both of them how they planned to transport the oranges if they won possession. Dundee Ltd said it would hire refrigerated trucks. Knowing its affiliates intentions, in turn, the lender proudly announced that its affiliate had its own fleet of refrigerated trucks, and because it was not the busy season that company would have plenty of trucks to get the oranges to the juice extraction facility.

So the proposal: the mediator invites them to recall that despite their lawyers respective assessments of the merits, they could not be certain to win the oranges. They could however control whether by cooperation they might improve the bottom line of each of them.

And so it is agreed, after juicing, the peels will be transported to Dundee in the affiliate company's refrigerated trucks. That affiliate of the lender will charge Dundee Ltd for use of the trucks, but not as much as Dundee would have paid a third party transport company. Without much added deal complexity, we have expanded the pie, and not merely distributed it!

Many of you know quite a bit about mediation so you will have realized that in my oranges hypothetical case I conveniently skipped over one of the principal obstacles with respect to mediation, that is: how to introduce the mediation notion and then actually convene the parties, when each may fear signaling weakness or suggesting to the counter-party a lack of confidence.

My smart beautiful wife is of Dutch extraction. Her mother, who recently passed at age 99, served in the Dutch Resistance and taught her daughter that the direct way is usually best (here the word "blunt" –comes to mind). So my wife's approach might be say to the other side: "We are going to mediate. It will be good for both of us, except not at your offices; there might be "bugs".

Since we are talking about a metaphor for my marriage and also making a point about the importance of good communication in mediation, as in marriage, let me develop this side story: To my surprise the direct method worked (she is usually right) and a successful mediation ended the dispute. But as the story goes, during the mediation, one party summoned the courage to say to the other "you know, I must I confess I was somewhat offended when you suggested that our side might have planted listening devices in the break-out rooms at our offices for purposes of this mediation".

In the mediation I have in mind, several more confusing exchanges would follow that. One side would have remembered –verbatim-- what had been said. At some point—there would be a breakthrough—and that party would inform the other that: "I said nothing whatever about

listening devices—the idea never entered my mind--by 'bugs' I, of course, meant spiders, ants and other pests that are attracted to the kind of messiness one finds in your offices."

In the end the misunderstanding did not side-track the mediation (or the marriage), because, the mediator, being well-suited to addressing cross-cultural disputes, would have detected that one party says 'bugs' and the other hears 'listening devices'. Disaster averted!

Back to the problem of convening the parties: A partial remedy to the dilemma of how to successfully invite mediation—at least in contract disputes—is simply to have language calling for mediation in the contract—to perform a "triggering" function.

For triggering, the standard "step" clause serves well. It, after all, can't be a sign of weakness if long before the dispute arose, we agreed to mediate before moving to more binding processes.

Another aid to convening the parties in mediation is present when one or both companies have published policies preferring ADR, in which case the lawyers can exercise "strength from weakness" by saying something like "although we think this is for us a very solid case, our board has determined that mediation preserves business relationships and lowers costs for all concerned. Besides, as emphasized on the company web site, they believe avoiding adjudication is good for the planet because it saves all that paper."

In the context of investor-State disputes, appropriate treaty language might trigger the mediation conversation, as might encouragement from the relevant administering institution and from the tribunal itself.

To return to my simple classroom flow chart, the branch devoted to hybrids is between the other two—that is between the adjudicative mode of arbitration and the collaborative approach of mediation. It is wedged between the other two to suggest the possibility that one might be able to borrow the best of both techniques.

Many of you will have encountered the above-mentioned step clauses in contracts. You know the ones; they call for the parties to solve their disputes by attempting first good faith negotiation, followed if necessary by third-party assisted negotiation (which I call mediation) followed if necessary by arbitration.

Sometimes the word "binding" precedes arbitration in the clause just to signify that when you enter that arbitration stage, one has moved from collaborative to adjudicative (that is something final rather than some kind of advisory process producing a non-binding best-guess at the outcome in court).

Ignoring the negotiation stage, we might call this "standard med-arb" (that is: mediation followed by binding arbitration).

This combination has several positive attributes: it gives the parties a chance to avoid imposed results, using a method that is more likely to preserve the commercial relationship and, if successful, will end the dispute rather economically.

Mediation will hold the same promise of win-win and expanded pie solutions that we illustrated with the oranges, and—simply by virtue of the process—will help the parties better understand their dispute, including its strengths and weaknesses. For this enlightenment to occur early in the process is no doubt beneficial.

Unless measures are taken to improve on this result, however, mediation ends in a settlement agreement that is, perhaps at best, enforceable as a contract and thus subject to contract defenses.

In some legal systems it may be possible by following certain formalities to give it added weight. In a California, in 1989, we added to the UNCITRAL Model Arbitration Law a chapter on Conciliation (which terminologically we do not distinguish from "mediation").

One of the provisions in that chapter likens a mediated agreement embodied in a particular way to an arbitration award:

Specifically, § 1297.401 of the California Code of Civil Procedures states:

> If the conciliation succeeds in settling the dispute, and the result of the conciliation is reduced to writing and signed by the conciliator or conciliators and the parties or their representatives, the written agreement shall be treated as an arbitral award rendered by an arbitral tribunal duly constituted in and pursuant to the laws of this state, and shall have the same force and effect as a final award in arbitration. (end quote)

Within California, this magical transformation will likely be respected—essentially making a mediated settlement an arbitral award on agreed terms. Revisiting this section with international enforcement in mind, however, made me wonder if it was fair to call it the California "conciliation chimera."

So I looked up the definitions of "chimera". Indeed one was good fit: "A thing that is hoped or wished for but in fact is illusory or impossible to achieve." Synonyms are said to include: "illusion, fantasy, delusion, dream, and figment of the imagination·"

At least in terms of global enforcement, it may indeed be a "chimera" we are talking about. It will of course be up to the various New York Convention States as to whether the agreement in question would be considered an arbitral award.

But, notice that the above provision does not require that the conciliation take place during a pending arbitration. That fact might suggest to the outside world a technical problem—namely that one needs a dispute submitted to arbitration before one can have an arbitral award—so that simply calling it an award may not be enough to earn it predictable enforcement under the New York Convention.

If not qualifying for New York Convention enforcement, it would fare no better than a mediated settlement agreement.

But, would that be so bad?

We now have the Singapore Convention. As many of you know, Article 3(1) is perhaps the essence of the convention: it provides:

> "Each [State] Party to the Convention shall enforce a[n] [international] settlement agreement in accordance with its rules of procedure and under conditions laid down in this Convention"

Just to be clear "settlement agreement" is defined as:

> "[a]n agreement resulting from mediation and concluded in writing by parties to resolve a commercial dispute".

The Convention goes on to define what makes a settlement agreement "international" and also—in terms broadly analogous to the New York Convention—identifies permitted defenses to enforcement.

The Convention has many signatories, (some of you might have been in Singapore for the big event in August) but for it to rival the New York Convention the key will be over time to convert signatures into ratifications.

Many of you will have anticipated my next point, which is —contrary to the above hypothetical— if there was an ongoing arbitration when the mediated settlement was reached, the tribunal will generally be empowered to embody that settlement in an award on agreed terms if requested by the parties, such that the California chimera procedure would be unnecessary.

The concept of an award on agreed terms is more well-known procedure than California's chimera procedure, and thus the outcome will presumably have a better chance of global enforcement as a New York Convention award.

Returning to the standard med-then-arb process, let me argue for a friendly amendment. The problem is that if one ends the mediation phase and moves on to arbitration alone, one may miss opportunities for the mediator to seize on settlement possibilities created by the normal momentum and attitudinal shifts that take place as the parties come to more fully to understand their dispute and its weaknesses, especially in light of mounting costs.

I, therefore, favor "shadow" mediation—also called "concurrent" mediation. The model I like starts with the usual initial attempt at mediation, but rather than there being an end to the mediation phase when the arbitration begins, the mediator or mediators merely draw back for time to allow the arbitration to launch. They then reengage later at set junctures throughout the arbitration.

Let me add some detail to this skeleton. Concurrent mediation will work best when there is cooperation between the two types of neutrals. Mediators will be best equipped if they are privy to all the parties' submissions and communications with the arbitrators, and if they are entitled to attend all meetings among the tribunal and the disputants.

The various ways in which parallel mediation will be accommodated by the tribunal can be laid out in an early procedural order, and might include, for example, that the hearing schedule will include open days or half-days, to be determined closer to the hearing time, during which breaks the mediators can meet with the parties.

At the same time, the two processes are fully separate—the mediators and the arbitrators do not interact in any way that involves the mediators in arbitral decision-making on the merits.

On the other hand, when the tribunal asks the parties to cooperate in some fashion to, for example: agree on stipulated facts, or to fashion a protective order, or to work harder on identifying a common bundle of key documents, or to narrow the scope of documentary exchanges, the mediator may well be able to help with that collaboration.

Again, that is not in any way helping the arbitral tribunal with deciding the merits, and equally, the mediators ought not to be thought by the parties to have some inside knowledge as to what the tribunal is thinking on the merits. They should be positioned to say "you heard what I heard" and "you know what I know" perhaps followed by "I do of course have some educated guesses, but let's make it so it does not matter what the tribunal might have ultimately decided."

By the way, I am aware in Asia and elsewhere, one finds med-arb that involves "double hatting" in which the same neutral plays both roles. Perhaps we can explore this during question time. For now let me underscore that the model I am discussing contemplates that the arbitrators and mediators will be different neutrals, for reasons we can discuss when we move to questions.

To return to my model, let me add a word about mediator qualifications: given what I just said about the possibility that the mediators might have educated guesses about the outcome if it were left to the arbitral tribunal to decide, it would be helpful if the mediator was familiar with the international arbitration process; and, in my ideal world the mediator would be as well-qualified as the arbitrators to decide the dispute.

That is, an ability to authoritatively point out defects in the parties' respective substantive cases promotes settlement.

Also, in a particularly high profile case—perhaps with a State on one side--the prestige and authoritativeness of the mediator may be especially important because that can provide cover for the parties who may worry about answering to various internal and external constituencies.

That is: it may be useful to the participant teams to be able to say: "Famous jurists A&B—our mediators—both said: First, our case's outcome could not be confidently predicted (including who would pay costs); and second, that an award we do not control will potentially have x, y, z negative consequences; and third, on the world stage we look as if we were forthright by having famous jurists A&B investigate our case, and fourth both sides look like winners in this deal, and fifth, although we cannot control the international press, by proper packaging and the sponsorship of a deal by A&B we can improve the chances that we will be treated fairly in the media and by the several constituencies to whom we must answer."

One of course need not have a State party involved to imagine a dispute with multiple constituencies and interests intersecting. Consider, again, the oranges hypothetical. Then add the fact that there is a warehouse that has patiently held the oranges but wants now to be paid and it now threatens to sell the oranges. There is also an NGO that alleges that international labor laws have been violated because there were children involved in the picking of these premium oranges. Here the question is, does the shadow mediation model work? I would confidently say yes.

Just to be clear, I see no problem if the shadow mediation involves parties over whom the arbitral tribunal itself does not have jurisdiction. The architecture is flexible enough to accommodate such scenarios, perhaps by including an additional mediator (that is to use "team" or "co-mediation" alongside an arbitration that advances apace). Those additional parties may be part of a single settlement agreement, or, more likely, may be included in side agreements so that the main two-party dispute can be embodied in an award on agreed terms.

Returning to investor-State disputes, I foresee a model in which the investor/claimant on the one hand and the host-State respondent on the other would each appoint a mediator to form a two mediator team. That team would shadow a sole arbitrator who moves forward with speed and agility and not characteristic of three-arbitrator tribunals.

So now, as promised (or "threatened", if you prefer) a community growing exercise in which you vote.

Here is the background: I am working on a treaty election that States might make available in their BITs in addition to the standard ICSID and ad hoc claimant choices. Its detailed mechanics would be elaborated upon perhaps in an Appendix to the treaty (an idea I like because States could simply agree to add it to an existing investment treaty without much re-engineering of the existing treaty text).

By electing to activate the Appendix, the claimant could launch a procedure in which there is sole arbitrator and two co-mediators; the latter would shadow the arbitration in the manner I described above.

But, here is the question. Should the co-mediators both be selected by an institution, or should the mediation team be formed by each party selecting one mediator? Bear in mind that under either model, both mediators would be required to be independent and impartial.

Before we vote, let me add that I have come to assume that party appointment might add legitimacy to the process and be consistent with general notions of party autonomy but would suffer the possible defect that the mediators will not be chosen principally based on their style compatibility and complementarity.

By contrast, presumably an institution would give greater weight to appointing mediators that have complementary subject matter knowledge and skill sets, so as to generate the greatest scope for inventiveness and synergism.

Epilogue

I declare this exercise a success! Most of you voted, and my visual scan of your uplifted hands indicates that –by a ratio of 3 to 1--most of you favor party-appointment of mediators.

And, to summarize some of the reasons given, the party appointment majority believes that party appointment of team mediators will add both to their control of the process and their comfort with it.

I'll note in closing that I have encountered resistance to the idea that there be only one arbitrator. The vast majority of investor-State arbitrations have involved three arbitrators. And one can appreciate the reasons for having three.

Nevertheless, to the extent that the current system is attacked for being slow, an arbitral tribunal with only one calendar to accommodate is bound to improve on the existing average duration of investor-State disputes. And, to be honest, I am confident that quite often it will not matter because the dispute will end in a mediated settlement before the tribunal has to render its award.

It remains for me to thank Secretary Cheng, Madam Joubin Bret, and Herbert Smith Freehills for the hospitality and the forward-looking outlook in embracing process design. Also, thank you for being here tonight, and for the free advice!