THE BUREAU OF NATIONAL AFFAIRS, INC.

June 22, 1990

Karen Siegel
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Administrative Office of the U.S. Courts
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Washington, D.C. 20544

Dear ~~Ms. Siegel~~ Karen:

I thought that you might like to have the ADRR issue with the article to which you contributed.

Please accept BNA's sincere thanks for your help in making this publication useful and interesting.

I hope that you will continue to let me know about further developments that may be of interest to ADRR's readers.

Thanks again,

Sophie

Sophie C. Eilperin
Managing Editor
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Resolution Report
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Karen Segal
FYI
CC

BNA's *Alternative* DISPUTE RESOLUTION REPORT

June 7, 1990
Volume 4, Number 12

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New Developments

Sen. Biden Revamps Civil Justice Reform Bill to address objections by U.S. Judicial Conference. Original bill required every district court to develop case management plan and to offer litigants ADR options; new bill gives courts more flexibility and contemplates inclusion of ADR in several pilot delay-reduction programs. (Page 187)

'ADR Is Catching On,' Justice Official Says. Assistant Attorney General Stuart M. Gerson indicates that U.S. Department of Justice is willing to mediate its long-standing dispute with software manufacturer, but manufacturer calls DOJ's position 'hypocritical.' (Page 188)

Arbitrators' Power to Award Interest would be clarified by new rule proposed by New York Stock Exchange. Rule would also allow arbitrators to consolidate proceedings and discipline NYSE members who fail to pay awards. (Page 189)

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BNA's Alternative Dispute Resolution Report

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NEW DEVELOPMENTS

Federal Courts

Biden Revamps Civil Justice Bill To Address Judiciary's Opposition

Guidelines, rather than requirements, characterize new civil justice reform bill, which would require each federal district court to develop and implement plan to reduce expense and delay in civil justice; U.S. Judicial Conference adopts 14-point program which parallels some aspects of new bill.

Bowing to opposition from the federal judiciary, Sens. Joseph R. Biden Jr. (D-Del) and Strom Thurmond (R-SC) revamped a civil justice reform bill introduced in January and unveiled a new version May 17 that would create 77 new judgeships, establish a pilot case management system and set guidelines to avoid case delays.

"When it comes to what the district courts are required to do under this legislation, we've given the districts more flexibility than they would have had under the original bill," Biden, who is chairman of the Senate Judiciary Committee, said in urging support for reforms to reduce delays and the expense of civil litigation.

The original bill (S 2027) would have required each district court to develop a case management plan that included a system to track cases based on their complexity, and to offer litigants ADR options (4 ADRR 76). The revised version (S 2648) would establish four-year demonstration programs in five district courts: two of these programs would use case tracking systems, and three would employ delay-reduction mechanisms, including alternative dispute resolution. The new bill would also require each federal district court to implement a "civil justice expense and delay reduction plan" developed within that district or adopted from a model plan developed by the Judicial Conference of the United States, the judiciary's governing body.

"We've set out what we want them to do in terms of core principles and guidelines, rather than more specific requirements," Biden said.

The new bill, which includes a fiscal 1990 authorization of $20 million for the demonstration and civil justice plan programs, also restores the role of magistrates in the pretrial process.

More Judgeships

Responding to the judiciary's call for more judgeships to reduce caseloads, Biden and Thurmond, the ranking Republican on the Judiciary Committee, would create 77 new judgeships—66 in the district courts and 11 in the circuit courts—with the 20 district courts most overloaded with drug cases each getting at least one additional judge. Biden originally sought to propose adding judges to the federal court system as a separate measure.

Biden noted in his floor statement that he and Sens. Howell Heflin (D-Ala) and Charles E. Grassley (R-Iowa) expect to add to the bill "noncontroversial recommendations" for court reform made by the Judicial Conference's Federal Courts Study Committee in April.

Biden said the committee will hold a hearing on S 2648 June 12, with the intention of moving the bill out of committee "shortly after that hearing." The committee last met to debate S 2027 on March 6, when it heard from the Judicial Conference that the original bill was "extraordinarily intrusive into the internal workings of the judicial branch" (4 ADRR 99).

The executive committee of the Judicial Conference met May 18 and took the first opportunity to study the new bill, worked out by Biden's staff and officials of the Judicial Conference during the last several weeks, conference spokesman David Sellers said. The committee members declined to immediately comment on the measure, but Sellers said that after "a lot of give and take . . . we're certainly getting closer."

Biden said the bill is "aimed at making the civil justice system more accessible, more prompt in the resolution of disputes, and less expensive."

Defending the need for legislation, Thurmond said "it is appropriate to consider procedural changes which will reduce the costs and delays confronted by those who seek to resolve their disputes through the civil litigation system," adding that additional judgeships also are critical to address the problems.

Pilot Programs, ADR

As proposed, four-year pilot programs using a tracking system to separate the simple cases that can be handled quickly from those that are more complex would be set up in the U.S. district courts in the Western District of Michigan and the Northern District of Ohio.

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The district courts in the Northern District of California, the Northern District of West Virginia, and the Western District of Missouri would establish trial programs to reduce costs and delays using methods—including alternative dispute resolution—they select in consultation with the Judicial Conference.

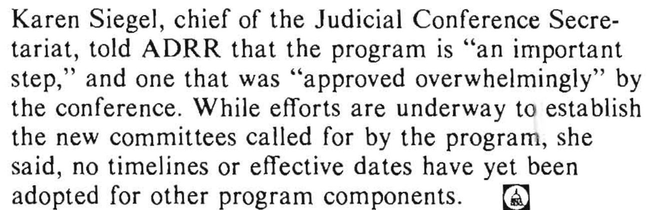
Each district court would establish its own civil justice expense and delay reduction plan after considering recommendations of an expert advisory panel set up in that district. Those plans must include provisions such as differential treatment of cases by complexity; early case planning by a judicial officer; "early, firm trial dates" within 18 months of the filing of the complaint, unless the judicial officer believes that deadline cannot be met; and conferences where necessary to explore settlement, discovery schedules, and other delay- and expense-reduction alternatives.

Judicial Conference Acts

Whatever may be the future of the Biden bill, a 14-point program approved April 27 by the U.S. Judicial Conference calls for a number of activities that parallel those contemplated by the bill. Among the provisions of the "Program to Address the Problems of Cost and Delay in Civil Litigation and to Improve Case Management" are that:

- The chief judge of each federal district court shall appoint an "advisory group of lawyers and representative clients" to help that court assess its docket conditions and to recommend measures to reduce cost and delay and improve case management practices. Each district court is to implement the recommendations that it finds "feasible and constructive."
- The reports and recommendations of each advisory group, and a copy of the measures implemented by each district court, are to be forwarded to the Judicial Conference. If the conference is not satisfied with the way a district court has responded to its docket conditions or to the advisory group's report, it may request that court to take further action.
- The Judicial Conference will create a committee on Case Management and Dispute Resolution. This committee will develop a document explaining the "wide range of different measures that courts might consider adopting in response to cost and delay problems," including alternative dispute resolution programs. It will also develop at least two model plans for civil expense and delay reduction. After the reports, recommendations, and implementation measures are received from each district court, the committee will develop a comprehensive report describing current conditions and trends.
- Each district court is to reconvene its advisory group every three years, in order to evaluate its programs, reassess its conditions, and recommend adjustments to existing programs or practices.
- The Judicial Conference will add "substantial new training programs for judicial officers and appropriate court staff in case management techniques."

Karen Siegel, chief of the Judicial Conference Secretariat, told ADRR that the program is "an important step," and one that was "approved overwhelmingly" by the conference. While efforts are underway to establish the new committees called for by the program, she said, no timelines or effective dates have yet been adopted for other program components.



Federal Agencies

'This Alternative Dispute Resolution Is Catching On,' Justice Official Says

Assistant Attorney General Stuart M. Gerson, head of Civil Division of Department of Justice, indicates DOJ's willingness to mediate its lengthy and contentious dispute with software manufacturer, under auspices of mediation program of U.S. Court of Appeals for District of Columbia; opponent, which has prevailed before bankruptcy and district courts, calls DOJ's interest in mediation "hypocritical."

Stuart M. Gerson, Assistant Attorney General, Civil Division, U.S. Department of Justice, May 11 endorsed the concept of mediation as a way for "bringing a fresh view to a dispute" between the Justice Department and a software manufacturer. At a press briefing which included discussion of a lengthy and contentious series of legal actions between DOJ and Inslaw Inc., Gerson acknowledged the "all-consuming nature" of the case for the plaintiff. He said, however, that "there is no case that can't settle," and that the department is taking a "cooperative stance" with regard to the mediation program of the U.S. Court of Appeals for the District of Columbia Circuit.

Inslaw claims that the Justice Department copied its litigation support system without authorization, drove it into bankruptcy, and covered up allegations of conflict of interest. Inslaw's president has stated publicly that it refuses to mediate the appeal.

Suggested Mediation

Gerson made his remarks in response to a reporter who asked whether the DOJ-Inslaw dispute, which started soon after the parties entered into a contract in 1982, would be mediated. Gerson stated that he had heard that Inslaw might not be interested in mediation, but said that DOJ is "open to all kinds of things to resolve that case or any other case." "My own view is that there is no case that can't settle," he added.

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Gerson said that DOJ did not suggest mediation in this case, but that it acted in response to the mediation program of the U.S. Court of Appeals for the District of Columbia Circuit. "We were asked if we were willing to participate in it. We said we were."

Gerson added that "this alternative dispute resolution is catching on." When a reporter asked whether the court had hired a special master or an arbitrator, Gerson explained that a mediator "acts as facilitator or a go-between, doesn't make a decision, but works with the parties, evaluates various arguments and possibilities, and attempts, if possible, to fashion a remedy that the parties themselves will come up with." He then remarked, "Whether that will work in this case I haven't any idea."

Gerson stated that "if you strip away a lot of the invective that's been hurled around in this case, it's a commercial dispute" that might "be susceptible to some form of mediation process" where "private lawyers of great experience and prestige . . . could bring a fresh view to the dispute."

In spite of the heated nature of the controversy, Gerson said, "[y]ou still have something that involves money. Can we look at that as an item in our inventory of cases? We can. And that's the kind of thinking that we try to apply to all of our civil cases."

Case Management Software

The litigation arose from Inslaw's contract to develop a litigation support system for DOJ. However, the parties' relationship deteriorated during contract performance. Inslaw attributed many of the problems to the fact that DOJ's contract administrator—who formerly worked as its general counsel—was biased against the company.

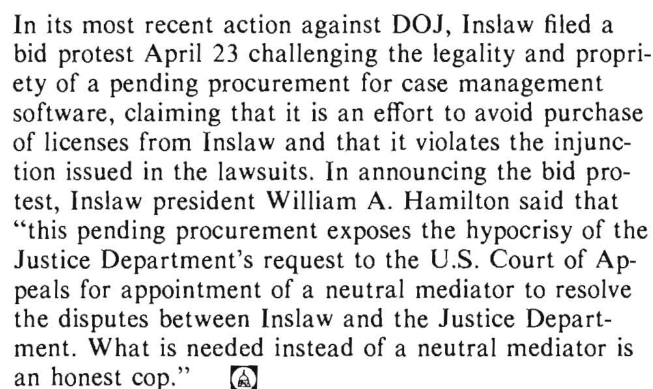
Shortly before completing the contract, Inslaw filed for reorganization under Chapter 11 of the federal bankruptcy laws. Meanwhile, DOJ began using the disputed software to implement the system in offices not covered by the contract. Inslaw filed a claim against DOJ for $2.9 million in licensing fees, maintaining that the software had been copied without its authorization.

The bankruptcy court found that the contract administrator intensely disliked Inslaw and its chief executive. The bankruptcy judge concluded that DOJ had converted Inslaw's enhanced system by "trickery and deceit," and was intending to use the system in a fashion not contemplated by the contract. The court issued a declaratory judgment finding Inslaw to be the sole owner of the proprietary improvements, and concluding that DOJ had wrongfully exercised control over the software in violation of the bankruptcy code's automatic stay. The court further ordered DOJ to compensate Inslaw under the terms of the licensing agreement, enjoined certain officials involved in administering the contract from further participation in the litigation, and awarded attorneys' fees and costs to the contractor.

The government appealed to the U.S. District Court for the District of Columbia, which affirmed the bankruptcy court's decision. (*United States v. Inslaw Inc.*, DC DC, No. 88-528, 11/22/89). A further appeal is now pending before the U.S. Court of Appeals for the District of Columbia Circuit.

Inslaw Refuses Mediation

The Inslaw litigation has led to hearings by the House Judiciary Committee, which is investigating the Justice Department's computer procurement practices. Inslaw has also brought suit asking for a new investigation by DOJ of the administration of the contract, claiming that two earlier ones were biased.



In its most recent action against DOJ, Inslaw filed a bid protest April 23 challenging the legality and propriety of a pending procurement for case management software, claiming that it is an effort to avoid purchase of licenses from Inslaw and that it violates the injunction issued in the lawsuits. In announcing the bid protest, Inslaw president William A. Hamilton said that "this pending procurement exposes the hypocrisy of the Justice Department's request to the U.S. Court of Appeals for appointment of a neutral mediator to resolve the disputes between Inslaw and the Justice Department. What is needed instead of a neutral mediator is an honest cop."

Securities

NYSE Proposes Changes to Clarify Arbitrators' Power to Award Interest

New rule would give arbitrators explicit authority to award interest and to determine its amount, as well as to consolidate actions and to discipline New York Stock Exchange members who fail to pay awards.

The New York Stock Exchange May 7 proposed rule changes that would clarify the authority of its arbitrators to impose interest on arbitration awards (Release No. 34-28000, 5/7/90).

The proposed changes also would clarify that the Director of Arbitration may appoint a public—as opposed to an industry—arbitrator to decide customer claims under $10,000. The proposals further would spell out the authority of arbitrators to consolidate actions and to dismiss cases after repeated adjournments.

The Securities and Exchange Commission, which must approve the proposed rule changes, is seeking comments on them. The NYSE's proposed rule changes are based on proposals developed by the Securities Industry Conference on Arbitration, the SEC noted.

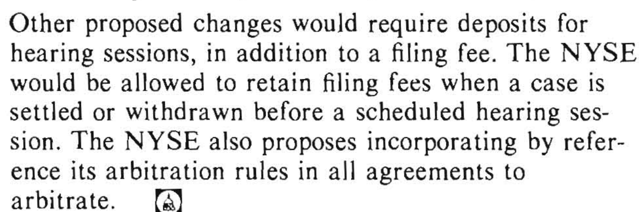
Explicit Authority

The NYSE proposal would give arbitrators explicit authority to award interest and to determine the rate of interest "with discretion." The NYSE contends that interest on awards would encourage prompt payment and increase public confidence in arbitration proceedings. Awards would bear interest from the date of award and would have to be paid within 30 days, according to the proposal.

The proposed rule changes also would codify the current exchange practice of appointing a public arbitrator to decide customer claims under $10,000 and to preside over pre-hearing conferences. The proposal further would clarify the NYSE's arbitration director's authority to determine the time and place for hearings, to consolidate actions, and to discipline an exchange member for failing to pay an arbitration award, according to the commission. The NYSE notes that it currently relies on its implicit authority to discipline members who do not pay awards.

In addition, the proposed changes would increase the fee for adjournments and would grant arbitrators express authority to dismiss cases without prejudice in the event of repeated adjournments, the SEC noted.

Other proposed changes would require deposits for hearing sessions, in addition to a filing fee. The NYSE would be allowed to retain filing fees when a case is settled or withdrawn before a scheduled hearing session. The NYSE also proposes incorporating by reference its arbitration rules in all agreements to arbitrate.



Employment

NASD Arbitrators Award $38.2 Million To Fired Executive in Contract Dispute

Multi-million dollar award is culmination of 22 days of arbitration hearings, 40 witnesses, 1200 exhibits, and 700 pages of post-hearing briefs.

A former public finance executive of Prescott, Ball and Turben Inc., a securities firm, was awarded $38.2 million by National Association of Securities Dealers arbitrators in an employee contract dispute (*Prescott, Ball & Turben Inc. and Kanuth*, Case No. 88-1919, NASD, 5/2/90).

Arbitrators agreed with Robert Kanuth that he was discharged improperly from his position at PBT, a subsidiary of Kemper Financial Companies Inc. In addition to damages for breach of contract, the three-person panel awarded Kanuth punitive damages and damages for defamation and intentional infliction of emotional distress. The award includes $1.77 million in salary; $31.4 million in incentive compensation; $3 million for emotional distress; $1 million for defamation; and $1 million in punitive damages.

Acquisition and Contract

The dispute centered on PBT's decision to acquire Cranston Securities Co. from Kanuth and others for approximately $11.3 million. In connection with the acquisition, Prescott and Kanuth entered into an employment contract under which Kanuth was named chief executive officer of the Cranston/Prescott division of PBT. The five-year contract contained a provision that allowed Kanuth to be terminated only if he engaged in "gross misconduct," the arbitrators noted.

In May 1988, after a series of disagreements and disputes between Kanuth and various Prescott executives, Kanuth filed suit in the U.S. District Court for the District of Columbia seeking relief for alleged breaches of his employment contract. He also sought damages for fraudulent inducement with respect to the transaction by which Prescott acquired the stock of Cranston securities. In June, Prescott's board of directors voted to terminate Kanuth's employment.

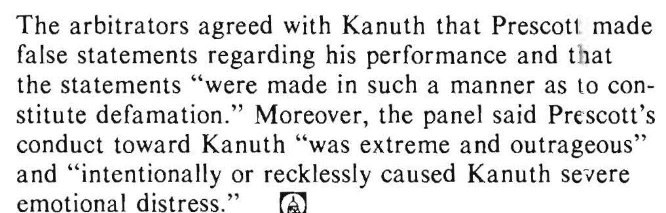
The firm then commenced an arbitration proceeding before the NASD, charging that Kanuth fraudulently induced it to acquire Cranston Securities stock, breached his fiduciary duty to Prescott, and committed corporate waste. On Prescott's motion, the court action was stayed and referred to arbitration, where NASD consolidated Kanuth's complaint with Prescott's action.

Improper Dismissal

The arbitration hearing was extremely lengthy, the arbitrators noted. Testimony was received from 40 witnesses and comprised nearly 7,000 pages of written transcript. The hearings required 22 days, and there were approximately 1,200 exhibits. There also were 700 pages of post-trial briefs submitted by both sides.

The arbitrators held that Prescott failed to prove its claims against Kanuth and therefore that Prescott acted improperly in terminating his employment in June 1988.

The arbitrators agreed with Kanuth that Prescott made false statements regarding his performance and that the statements "were made in such a manner as to constitute defamation." Moreover, the panel said Prescott's conduct toward Kanuth "was extreme and outrageous" and "intentionally or recklessly caused Kanuth severe emotional distress."



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COURT DECISIONS

Supreme Court

Court Won't Decide If FAA Preempts State's Securities Arbitration Rule

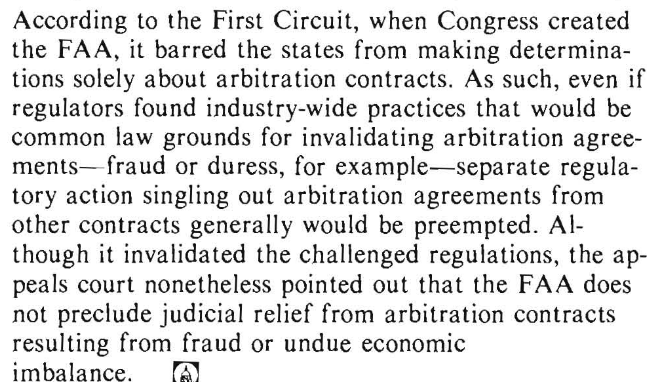
Denial of review leaves in effect First Circuit's ruling that Federal Arbitration Act preempts Massachusetts regulations which prohibit securities broker-dealers from including mandatory arbitration clauses in customer agreements.

The U.S. Supreme Court May 29 declined to review a controversial federal appeals court decision that Massachusetts rules barring broker-dealers from including mandatory arbitration clauses in customer agreements are preempted by the Federal Arbitration Act. (*Connolly v. Securities Industry Association*, US SupCt, No. 89-894, 5/29/90)

Massachusetts adopted the rules in response to the Supreme Court's 1987 decision in *Shearson/American Express Inc. v. McMahon*, which held that predispute arbitration agreements are enforceable as to 1934 Securities Exchange Act claims (107 SCt 2332, 1 ADRR 83, 107). The day after the regulations were unveiled, the Securities Industry Association challenged them as unconstitutional.

The district court concurred in SIA's view that the regulations impermissibly treated arbitration agreements differently than other contracts, and it barred their implementation (3 ADRR 25). The U.S. Court of Appeals for the First Circuit—terming the rules "patently inhospitable to arbitration"—affirmed (3 ADRR 339).

According to the First Circuit, when Congress created the FAA, it barred the states from making determinations solely about arbitration contracts. As such, even if regulators found industry-wide practices that would be common law grounds for invalidating arbitration agreements—fraud or duress, for example—separate regulatory action singling out arbitration agreements from other contracts generally would be preempted. Although it invalidated the challenged regulations, the appeals court nonetheless pointed out that the FAA does not preclude judicial relief from arbitration contracts resulting from fraud or undue economic imbalance.



Supreme Court

Arbitrator's Reinstatement of Mechanic Won't Be Subject of High Court Review

Justices decline opportunity to resolve differences among federal circuits in application of Misco principles to cases challenging arbitral awards on public policy grounds.

The U.S. Supreme Court declined May 21 to review an arbitration award reinstating a mechanic who was fired for failing to properly tighten the lug bolts on a customer's car tires, despite the employer's contention that consideration of the case would give the justices an opportunity to clarify the public policy exception to the finality of arbitration awards. (*Stead Motors of Walnut Creek v. Automotive Machinists Lodge No. 1173, IAM,* US SupCt, No. 89-1238, 5/21/90)

Stead Motors of Walnut Creek, an automotive services company near San Francisco, asked the Court to review a decision by the en banc U.S. Court of Appeals for the Ninth Circuit rejecting the company's contention that reinstatement of the mechanic would violate the public policy favoring the safety of the traveling public (3 ADRR 409). According to the company, resolution of the case would have remedied a split in the circuits resulting from various readings of the Supreme Court's 1987 decision in *Paperworkers v. Misco*, 108 SCt 364 (1 ADRR 329).

The company argued that the mechanic, Gale Rocks, had exhibited an indifference to the consequences of his actions since the incident with the lug bolts was a repeat offense. The arbitrator, however, ruled that after a 120-day suspension, Rocks must be reinstated.

A three-judge panel in 1988 ordered the award vacated because it was contrary to the state's paramount concern with public safety on the highways (2 ADRR 163). The full Ninth Circuit reversed, however, citing the rule of judicial deference to arbitration awards. To fall within the exception to that rule, a public policy must be more than merely general considerations of supposed public interests, the court said.

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Seeking review, Stead Motors argued that the case both factually and procedurally offered the Supreme Court a "unique opportunity to resolve the conflict among the circuits by refining the general principles enunciated in *Misco*," which, it said, failed to establish "rules of general applicability to cases challenging arbitral awards on public policy grounds."

Six federal appeals courts have expanded on the principles of *Misco* "in markedly different ways" when considering challenges to arbitrators' reinstatement awards in discharge cases involving "workers guilty of dubious acts," the company said. "Without further guidance from this Court, similar cases in different jurisdictions will breed dissimilar rulings."

Rocks' union, Automotive Machinists Lodge No. 1173, a division of the International Association of Machinists, contended that Stead Motors failed to address the issue central to the decision by the full Ninth Circuit—whether or not there is a "sufficiently explicit and dominant California public policy expressed in state statutory laws and precedents to merit invocation of the public policy doctrine at all."

This issue, the union said, does not merit the court's attention since the Ninth Circuit's conclusion "involves no circuit conflict or conflict with this Court's cases but, instead, concerns a mixed question of law and fact resolved entirely by reference to State law and the particular facts of this case."

Securities

AMEX Provision on AAA Arbitration Superseded by Agreement, CA 2 Says

Broker-customer agreement requiring arbitration of disputes before one of several designated arbitration forums may supersede provision in American Stock Exchange constitution allowing customer to elect arbitration by American Arbitration Association.

A provision in the American Stock Exchange constitution giving customers the right to arbitrate disputes before the American Arbitration Association—the "AMEX window"—is superseded by a more specific customer-broker agreement, the U.S. Court of Appeals for the Second Circuit ruled May 7. (*Merrill Lynch, Pierce, Fenner & Smith Inc. v. Georgiadis*, CA 2, No. 89-9151, 5/7/90)

Therefore, Judge William Timbers said, a customer alleging that he lost $2 million after being fraudulently induced to trade in options by Merrill Lynch, Pierce, Fenner & Smith Inc. must arbitrate his claims before the New York Stock Exchange in accordance with his customer agreement.

Customer Agreement

A long-term investor with Merrill Lynch began to trade in options in 1980 and signed a "Standard Options Agreement." This agreement provided that any dispute between the parties "shall be settled by arbitration only before the National Association of Securities Dealers, Incorporated, or the New York Stock Exchange, or an Exchange located in the United States upon which listed options transactions are executed."

In 1989, the investor filed a demand for arbitration with the American Arbitration Association, rather than one of the arbitration forums specifically designated in his customer agreement. He alleged that after 25 years of investing conservatively in blue chip stocks and bonds, he fraudulently was induced to trade in put and call options and lost all of his more than $2 million portfolio in the market crash of October 1987. He alleged that Merrill Lynch and the broker who handled his account breached various statutory and common law duties.

AMEX Window

In his demand for arbitration, the investor invoked the AMEX Window provision of the AMEX constitution, Section 2, Article VIII. This provision states that: "if any of the parties to a controversy is a customer, the customer may elect to arbitrate before the American Arbitration Association in the City of New York, unless the customer has expressly agreed, in writing, to submit only to the arbitration procedure of the Exchange."

Merrill Lynch then commenced an action in New York state court to compel the investor to arbitrate his claims before the NYSE in accordance with the customer agreement. Because the investor failed to elect one of the specified arbitration forums provided in his customer agreement, the court noted, Merrill Lynch was authorized under the agreement to make the election on his behalf, and did so by electing the NYSE.

The investor removed the action to federal district court. In October 1989, the district court granted Merrill Lynch's motion to compel him to arbitrate before the NYSE and to enjoin the AAA from arbitrating his claims. The district court found that the AMEX Window provision was overridden by the more specific customer agreement.

Parties' Intent

The Second Circuit affirmed, saying: "Our task is to enforce the intent of the parties regarding arbitration absent a showing of some circumstance that would provide grounds for revocation of the customer agree-

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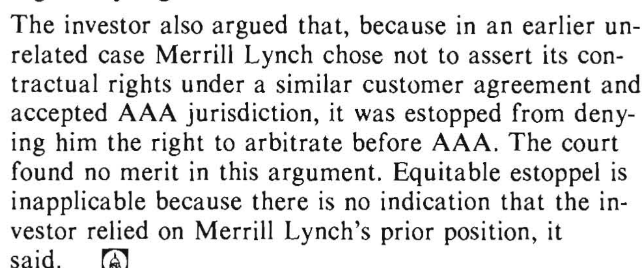
ment." The language of the customer agreement plainly requires that disputes between the parties be settled by arbitration "only before" one of several designated arbitration forums, the court concluded. Further, the investor made no allegation of fraud or overreaching on the part of Merrill Lynch that would vitiate the validity of the agreement, the court said.

"[T]he arbitration provision of the AMEX Constitution may be superseded by a more specific customer agreement of the parties," the court held. The court noted that the Securities and Exchange Commission has issued a release prohibiting arbitration agreements that limit customers to a single self-regulatory organization arbitration forum. That is not the case here, the court said, because the investor had a choice of several self-regulatory organization forums.



The investor also argued that, because in an earlier unrelated case Merrill Lynch chose not to assert its contractual rights under a similar customer agreement and accepted AAA jurisdiction, it was estopped from denying him the right to arbitrate before AAA. The court found no merit in this argument. Equitable estoppel is inapplicable because there is no indication that the investor relied on Merrill Lynch's prior position, it said.

Securities

AMEX Window Requires Customers to Arbitrate In New York, CA 2 Rules

Provision of American Stock Exchange constitution allowing customer to elect arbitration of securities claims "before the American Arbitration Association in the City of New York" is forum selection clause that requires customers electing AAA arbitration to arbitrate in New York City.

The terms of the American Stock Exchange constitution providing customers with the right to arbitrate disputes before the American Arbitration Association mandate that such arbitrations take place in New York City, the U.S. Court of Appeals for the Second Circuit ruled May 7. (*PaineWebber Inc. v. Rutherford*, CA 2, No. 89-9035, 5/7/90)

Accordingly, Judge William Timbers found, a couple pursuing claims against PaineWebber is not entitled to arbitration before the AAA in Orlando, Fla.

Inflated Stock Allegations

The case arose from claims by a large number of customers against PaineWebber Inc., alleging that employees of PaineWebber touted a certain stock in order to inflate its value, induced customers to buy shares, and then sold their own shares before the price collapsed.

A number of the claimants had not signed pre-dispute agreements with PaineWebber. Their right to arbitration was governed by the AMEX Window, Section 2, Article VIII, of the AMEX constitution. They filed their complaint in the AAA's Miami office, and included a demand for arbitration before the AAA in Orlando.

PaineWebber filed suit in New York state court, seeking to block the requested arbitration. The claimants then removed the action to the U.S. District Court for Southern New York. That court held that the claimants had to submit their claim to the AAA in New York or forego arbitration. This appeal followed.

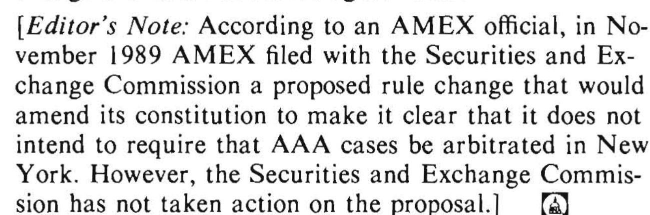
Forum Selection

The appeals court affirmed.

It noted that the terms of the AMEX Window provision state that the arbitration is to be "before the American Arbitration Association in the City of New York." The claimants argued that this phrase is merely a reference to the headquarters of the AAA, rather than a forum selection clause, but the court disagreed. "The argument that 'in the City of New York' is descriptive is undermined by the fact that, at all relevant times, there was only one American Arbitration Association," the court said. "The geographic reference is superfluous if not a forum selection clause."

In essence, the court said, the claimants invited it to read the phrase "*in* the City of New York" as "*of* the City of New York." Because it "must give effect to the agreement by its terms, if possible," the court declined that invitation.

The court acknowledged that its holding conflicts with the views of AMEX and the AAA. Both organizations would permit arbitration nationally, absent a contractual provision to the contrary, the court noted. However, the court said, it "cannot alter the unambiguous terms of the AMEX Window simply because the alternative construction may be thought to be fairer to the [claimants]." If AMEX finds this construction unacceptable, the court concluded, it is "of course free to change the terms of future agreements."



[*Editor's Note:* According to an AMEX official, in November 1989 AMEX filed with the Securities and Exchange Commission a proposed rule change that would amend its constitution to make it clear that it does not intend to require that AAA cases be arbitrated in New York. However, the Securities and Exchange Commission has not taken action on the proposal.]

NEW LAWS and BILLS

New Bills

CONNECTICUT

Arbitration of Construction Disputes
H 5836 (Committee on Government Administration)
4/6 Substitute Bill Recommended

Allows state agencies and their design and construction contractors to use any recognized alternative dispute resolution entity they can mutually agree upon, rather than mandating use of American Arbitration Association construction industry rules as current law requires.

FLORIDA

Arbitration of Uninsured Motorist Insurance Claims
H 3197 (Geller)
4/3 Introduced

Requires all uninsured or underinsured motorist insurance policies to include provision for binding arbitration which may be exercised only at option of insured.

HAWAII

ADR Roundtables
SR 76, SCR 87 (Matsuura)
3/14 Introduced

Requests judiciary's Center for Alternative Dispute Resolution to convene and moderate series of roundtable discussions to strengthen and expand ADR use in courts; parties invited should include representatives of courts, bar associations, plaintiff and defense bars, insurance council, and American Arbitration Association; recommendations are to be completed by 1991 legislative session.

MISSOURI

Mediation of Custody Disputes
H 1372 (Kasten)
1/11 Introduced

Authorizes courts to order mediation of child custody or visitation disputes, except in cases of domestic violence; directs that in appointing mediator, court shall consider parties' wishes and mediator's expertise, educational qualifications and training; requires mediator to inform parties about process and ensure that parties consider best interest of child; provides for termination of mediation if it may harm parties or child or if parties are unable to participate meaningfully; states that costs of mediation are to be taxed to parties.

NEW JERSEY

Court-Ordered Arbitration of Tort Claims
H 1707 (J. Smith)
1/22 Introduced

Raises, from $15,000 to $20,000, ceiling for mandatory court-ordered arbitration of certain tort claims arising out of accidents.

Construction Contract Arbitration
H 2523 (Zangari)
1/16 Introduced

Requires construction contracts entered into by state transportation department to contain arbitration clauses.

Attorney's Fees Arbitration
H 2682 (Moore)
1/24 Introduced

Pertains to disputes regarding attorney's fees and costs; requires that if arbitration panel consists of three members, client may opt that one member be nonlawyer and second member be attorney whose area of practice includes area in which disputing attorney provided or was to have provided service; requires that if arbitration panel consists of one person, client may opt that arbitrator be such attorney.

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NEW MEXICO

Disputes Between Foster Parents and State
S Memorial 5 (Garcia)
1/16 Introduced

Requests state human services department to investigate and propose alternative dispute resolution process between foster parents and department.

Educational Mediation Programs
H Memorial 26 (Huerta)
1/26 Introduced

Requests state public education department to determine which school districts use mediation programs offered by New Mexico Center for Dispute Resolution and to determine programs' effectiveness.

NEW YORK

Motor Vehicle Dispute Arbitration
S 7315 (Levy)
3/6 Introduced

Authorizes suspension or revocation of motor vehicle dealer's registration in event dealer fails to pay arbitration award.

OKLAHOMA

Workers' Compensation Claim Mediation.
H 2091 (Hunter)
2/9 Introduced

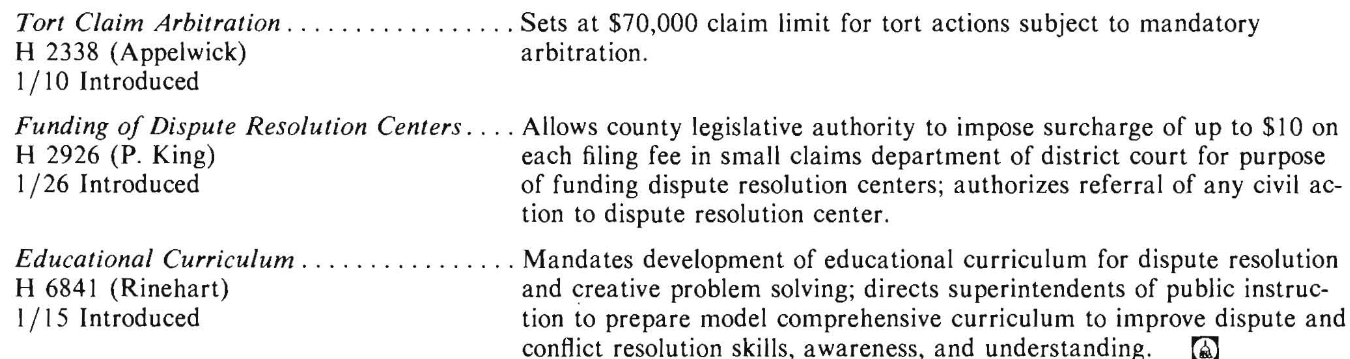
Allows workers' compensation claimant to request mediation in lieu of formal judicial hearing to resolve controverted issues.

UTAH

Public ADR Providers
H 294 (White)
1/18 Introduced

Provides for licensing of public ADR providers who serve in mediation or arbitration processes ordered by public entities and in which parties have no choice of process or ADR provider; makes it misdemeanor for any person to serve as public ADR provider without license; allows exemption from licensing requirements for arbitrators and mediators appointed by Federal Mediation and Conciliation Service, members of Utah State Bar, and other agencies or persons that licensing board finds to be competent and exempted; requires that applicants for licensure have a bachelor's degree or some equivalent combination of education and training, complete 30 quarter hours or equivalent college-level work relating to ADR, and complete 15 hours of internship, as approved by licensing board.

WASHINGTON



Tort Claim Arbitration
H 2338 (Appelwick)
1/10 Introduced

Sets at $70,000 claim limit for tort actions subject to mandatory arbitration.

Funding of Dispute Resolution Centers
H 2926 (P. King)
1/26 Introduced

Allows county legislative authority to impose surcharge of up to $10 on each filing fee in small claims department of district court for purpose of funding dispute resolution centers; authorizes referral of any civil action to dispute resolution center.

Educational Curriculum
H 6841 (Rinehart)
1/15 Introduced

Mandates development of educational curriculum for dispute resolution and creative problem solving; directs superintendents of public instruction to prepare model comprehensive curriculum to improve dispute and conflict resolution skills, awareness, and understanding.

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RESOURCES

Publications

CPR Guide Explains How Companies Can Incorporate ADR Into Daily Use

The corporate general counsel's role in implementing the routine use of ADR "cannot be overemphasized," according to a new publication by the New York City based Center for Public Resources Inc., "Mainstreaming: Corporate Strategies for Systematic ADR Use." The guide profiles 11 companies that have reshaped their legal departments to include routine use of ADR. The book is available for $80 from CPR Legal Program, 366 Madison Ave., New York, NY 10017, 212-949-6490, Fax: 212-949-8859.

Case Histories

The companies profiled in the guide were enthusiastic about their success rates and the savings they have achieved. Travelers Company noted that more than 85 percent of the cases it has submitted to mediation have been settled. General Mills Inc. said it believes—although it hasn't done a formal cost analysis—that it saves, on the average, hundreds of thousands of dollars by using ADR.

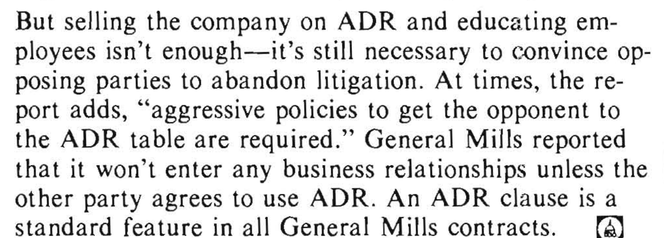
The initial step in creating a successful ADR program, according to the guide, must be "visible express commitment by top management." This can take the form of a policy statement pledging the company to pursue ADR. But the next step—implementing an ADR program—is harder. The report suggests that "[p]rogrammatic ADR adoption requires vigilant oversight and creative law department management by a pivotal player: the general counsel."

Approaches vary. For example, Amoco Corp. gives its attorneys full discretion in determining the appropriate use of ADR. Aetna Life & Casualty Co., in contrast, has built a presumption favoring ADR into its computerized docket control system. An ADR code must be entered for all disputes, showing either what stage of ADR the dispute is in or explaining why ADR wasn't used.

Although the general counsel will likely have primary responsibility for implementing an ADR program, he or she may find it helpful to delegate some oversight to an ADR "point person" or team, the report says. The report also suggests that it may be useful to hire an outside ADR specialist or consultant to help tailor an ADR system to the company's needs.

Education should stress potential ADR benefits and should include training in how to analyze a case for potential ADR application and descriptions of the different ADR processes. But training must reach beyond the law department to encompass top management, corporate managers who will likely participate in the ADR process, staff users of ADR, and outside counsel. The training methods for each group will differ.

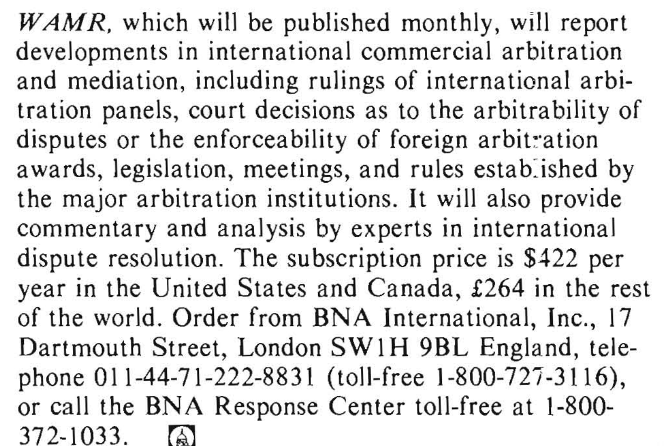
For example, the report says, "training" for the chief executive officer may consist mainly of sensitizing him or her to ADR's potential benefits, while staff who will use ADR may require much more specific training. Travelers commissioned a detailed interactive video computer program providing an in-depth focus on early negotiation skills for claims personnel, the report notes.



But selling the company on ADR and educating employees isn't enough—it's still necessary to convince opposing parties to abandon litigation. At times, the report adds, "aggressive policies to get the opponent to the ADR table are required." General Mills reported that it won't enter any business relationships unless the other party agrees to use ADR. An ADR clause is a standard feature in all General Mills contracts.

BNA Launches New Publication On International Commercial ADR

International commercial dispute resolution is the subject of a new publication—*World Arbitration and Mediation Report*—now available from BNA International Inc., a subsidiary of The Bureau of National Affairs, Inc.



WAMR, which will be published monthly, will report developments in international commercial arbitration and mediation, including rulings of international arbitration panels, court decisions as to the arbitrability of disputes or the enforceability of foreign arbitration awards, legislation, meetings, and rules established by the major arbitration institutions. It will also provide commentary and analysis by experts in international dispute resolution. The subscription price is $422 per year in the United States and Canada, £264 in the rest of the world. Order from BNA International, Inc., 17 Dartmouth Street, London SW1H 9BL England, telephone 011-44-71-222-8831 (toll-free 1-800-727-3116), or call the BNA Response Center toll-free at 1-800-372-1033.

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Note, *Mandatory mediation and summary jury trial: guidelines for ensuring fair and effective processes*, 103 Harvard Law Review 1086 (March 1990).

Rennie, Sandra M., *Kindling the environmental ADR flame: use of mediation and arbitration in federal planning, permitting, and enforcement*, 19 Environmental Law Reporter 10479 (November 1989).

Riskin, Leonard L.; Westbrook, James E., *Integrating dispute resolution into standard first-year courses: the Missouri plan*, 39 Journal of Legal Education 509 (December 1989).

Rowe, Thomas D., Jr., *Background paper (American Law Institute study on paths to a 'better way': litigation, alternatives, and accommodation)*, 1989 Duke Law Journal 824 (September 1989).

Schiffer, Richard A., *The use of mediation in resolving disputes in electronic data interchange*, 6 Computer Law & Practice 55 (November-December 1989).

Shell, G. Richard, *ERISA and other federal employment statutes: when is commercial arbitration an "adequate substitute" for the courts?* 68 Texas Law Review 509 (February 1990).

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Tarte, Lee, *Clergy arbitrator liability: a potential pitfall of alternative dispute resolution in the church*, 32 Catholic Lawyer 310 (Fall 1988).

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PRACTICE and PERSPECTIVE

Agricultural Mediation

Farm Mediation Service Director and Mediator Discuss Use of Process in New Rural Disputes

A recently enacted Iowa law continues until 1993 the Iowa Farm Mediation Service, which was originally established to resolve farmer-creditor disputes; the law also extends use of mediation to rural disputes that do not necessarily involve farmers and creditors. The article that follows, based on interviews with Micheal Thompson, FMS director, and Bob Hemshoot, FMS attorney and mediator, discusses the role of mediation in rural communities, and the reasons why the process would be helpful in resolving newly emerging agricultural contract and environmental disputes.

SOLON, Iowa—(By a BNA Special Correspondent)—The Iowa Farm Mediation Service turned the 'sunset' of their program into the sunrise on a whole new approach to farm mediation. The Iowa mediation program was initiated five years ago, making it one of the first of its kind in the United States. The Iowa legislature at that time established a sunset date of July 1, 1990 for the mediation service. According to FMS director Micheal Thompson, it was originally thought that the service would be temporary, as a measure to ease the 'farm crisis' of bankruptcies and foreclosures. But it is now apparent that even though the number of bankruptcies has slowed somewhat, there are still problems within the farm community which require the skills of mediation.

"There was a recognition on our part that problems in rural America are not limited to just farmer-creditor problems," Thompson explained. "When you are a community, being in court may be the worst thing for you. You are concerned that the court experience will not only destroy individuals, but the whole relationship which is needed to maintain rural ties and rural fiber.

"Rural fiber is made up of people working together," he continued. "What happened with the farm crisis is that the social fabric was shaken and in some cases ripped. Mediation is helping to restore that fabric."

In May, Iowa governor Terry Branstad signed into law House File 2404, an act which extends the life of FMS to July 1, 1993. More importantly, the amending law greatly expands the situations which call for or permit mediation by farm parties.

"The independence and isolation of farm residents poses special obstacles in dispute resolution."

In addition to mandatory mediation for financially distressed farmers, the new statute authorizes voluntary mediation for care and feeding contracts, farmer nuisance suits and conservation disputes. Each of these areas has special importance for farm communities, particularly those in the Midwest and Iowa.

New Law

The legislative findings and declarative portion of the act explain the unique status of farmers which makes mediation particularly appropriate for handling their disputes. It states: "The general assembly . . . finds that the independence and isolation of farm residents poses special obstacles in dispute resolution. Legal proceedings may be a costly, time-consuming, and inefficient means of settling disputes in which a farm resident is a party. Disputes may be better resolved in an informal setting where understanding and accommodation may replace a formal and adversarial proceeding. Therefore the general assembly declares that farm mediation should be expanded to include more disputes between farm residents and opposing parties."

Voluntary mediation can be requested by either the farmer or another party in the dispute. FMS will evaluate voluntary mediation applications and if there is a decision to mediate, a mediator will meet with the farmer and other party. The act also establishes fees of $25 per hour per party, except where a party can demonstrate financial hardship.

Mandatory mediation is required prior to the farmer or other party initiating a civil proceeding in a financial dispute. A filing party cannot begin a civil proceeding until that person receives a mediation release, or the court determines that:
- the time delay required for the mediation would cause the person to suffer irreparable harm; or
- the dispute involves a claim which has been brought as a class action.

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Care and Feeding Contracts

Mediation of care and feeding contracts involves a controversial farm practice which has recently gained popularity. Farmers agree to raise livestock which belong to another person, in exchange for a portion of any profit from the animal sales. The most common arrangement brings together an economically desperate farmer and a large agribusiness.

According to Bob Hemshoot, an attorney for FMS and a legal professor at the University of Northern Iowa who has handled over 100 farm mediation cases, the situation is ripe for abuse: "The feeder (of the livestock) is at a terrific disadvantage when the owners of the livestock 'suggest' that the farmer make improvements in their facility. The farmer has watched his capital assets decline in value and his ability to generate income go away during the 80s. Now he is willing to feed someone else's animals just to generate income.

"But he must borrow money to build those better facilities so that he can have cash flow from contract feeding. The banker loans the money, then suddenly the contractor pulls out of the deal, and the farmer is unable to service his debt. Now there is a bad loan on top of everything."

Hemshoot is not sure why so many contractors withdraw from such agreements, but it happens frequently. It has led to very ugly situations in the Midwest, including animals starving and cases of assault. In Minnesota, he pointed out, the legislature passed a law that will make the contractor a guarantor in situations where over $100,000 worth of improvements are made to satisfy the requirements of the contractor.

Hemshoot is concerned that this will alter the farmer-contractor relationship, perhaps negatively, even though it provides protection to banks who lend. "Whenever you have a new piece of legislation like this which changes basic contractual relationships in a substantial way, nobody can accurately predict exactly what effect that will have."

Nuisance Claims

Nuisance claims are becoming more prevalent. In the context of a farm dispute, a nuisance is defined as "an action injurious to health, indecent, or offensive to the senses, or an obstruction to the free use of property, so as essentially to interfere with the comfortable enjoyment of life and property."

Nuisance suits can involve farm neighbors or nonfarm persons living adjacent to farmers. The classic dispute over fences still exists, but today mediators are more likely to see disputes which center around 'quality of life' issues. Hemshoot said a dispute which is growing more common is over the 'smelly' neighbor. The smell may come from a livestock confinement operation which produces manure, or from organic farming methods which 'spread' that smell. With more people fleeing into the country for the good life, the chances of urban senses being shocked by such farm practices grows. But there is no really satisfactory way to resolve these issues through the courts.

"Today mediators are more likely to see disputes which center around 'quality of life' issues."

"There has been a long history of trying to use common law remedies to deal with disputes and the courts traditionally can't do it," Hemshoot said. "There are two results available to the court. One is an injunction, which basically puts the farmer out of business. The other is money damages. But how many dollars do you award for a certain amount of stink? And then a year later what do you do—come back to court for more dollars because of the stink? The thing to do is to try and work together, to understand each other's needs."

Environmental Issues

Nuisance claims often involve farmers dealing with new social relationships. Mediation essentially permits the kind of dialogue which should have happened of its own accord, but did not. A different kind of learning experience is now beginning to affect the farm community and is following the same pattern of ignorance fumbling towards enlightenment. This is in the area of conservation disputes.

The 1985 Farm Bill requires farmers to file conservation compliance plans with the U.S. Department of Agriculture by the end of 1990. In many cases, the costs of implementing conservation compliance plans may make it hard for farmers to continue in business. Other environmentally-oriented rules are about to be written into the 1990 Farm Bill. Farmers are likely to find themselves literally breaking the law with increasing frequency.

Conflicts are growing between environmentalists and farmers. Regulatory agencies are being pressured to clamp down on farmers who cause soil erosion or contaminate our water supplies with their agrichemicals. Both Hemshoot and Thompson said that it may be necessary to protect farmers from punishment in some cases, while they learn what they need to know about conservation, and to avoid dividing farm and nonfarm communities.

"Our biggest problem with the environment is that I don't think people have really been educated as to what they can do," Thompson said. "People have been asked to create environmental plans for conservation, and they made those plans,

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but a lot of those plans aren't implementable. Just because you write a plan doesn't mean you can do it on your farm. The present environmental direction will make it very hard for farmers who are heavily in debt to stay in the business.

"Mediators can act in this case like the practical pig," Thompson said. "You have to show people the logical implications of any kind of activity." [*Editor's Note:* In the children's story of "The Three Little Pigs," the practical pig was the one who took the time to build his house of brick, while his brothers built theirs of straw and wood. The two pigs who built their houses hurriedly saw them easily destroyed by the wolf, and had to seek refuge with the practical pig and his better thought-out solution.]

"Getting closer to environmentalists doesn't mean you won't have conflicts with them," Thompson continued. But you do have a process available to deal with that conflict so it doesn't get out of hand."

Thompson emphasized that as the rural communities become more fragile, the need to avoid disputes grows. "A right and a wrong often create more problems in a community than a court resolution is worth," he said.

"Mediators can act in this case like the practical pig. You have to show people the logical implications of any activity."

On the other hand, the process of mediation itself is a means to explore new territory. Recently the FMS helped to facilitate a meeting between environmentalists and farmers in Southwestern Iowa who were reviewing the new environmental laws. The farmers were on the way to being in violation of some of these laws, and the environmentalists were poised for action. The two groups had not known each other before the meeting, but an informal setting gave the farmers a chance to explain their problems and the environmentalists a chance to work with them in considering workable options.

Mediation, in the absence of any legal action, brought the farm and environmental communities together. Thompson hopes that mediation can be made mandatory before any environmental regulations are finally imposed on farmers. To date, this is still being debated at the federal and state levels.

FMS presently handles about 1500 to 2000 cases a year, down from a high of nearly 5,000 cases when Iowa was losing about 3,000 farmers annually in the mid-80s. Thompson said that a factor affecting this decrease was the cumulative understanding gained between the farming and the financial communities because of so many mediations. Now, that process is being broadened into all aspects of rural life, in hopes of similar positive results.

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