

Compelling Mediation in the Context of Med-Arb Agreements

It is obvious to all who work in the alternative dispute resolution (ADR) field that the most important federal statute—the Federal Arbitration Act (FAA)—does not define its key term: “arbitration.” A recent case, *Advanced Bodycare v. Thione*,¹ invited the 11th Circuit to explore which types of ADR processes are considered “arbitration” for purpose of the FAA. The question itself is not a novel one, as several appellate courts have struggled with this issue at one time or another. What is novel is the narrow test the 11th Circuit developed to determine which ADR processes qualify as arbitration, thus making the contract providing for that process subject to the FAA. This gives significant rights to a party who desires to enforce the agreement by seeking a stay of litigation and an order compelling a reluctant party to arbitrate.

What does “arbitration” mean in the context of the Federal Arbitration Act? With no statutory definition to guide them, courts have struggled with this question. This article looks at a recent 11th Circuit decision on the issue and discusses its troubling consequences for parties who desire to enforce agreements to use the process known as Med-Arb.

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Under the 11th Circuit's narrow test, an agreement to mediate, as well as an agreement to mediate or arbitrate, falls outside of the scope of the FAA. This holding seems uncontroversial in view of the facts in *Thione*. But its logical extension portends troubling developments for broad-based ADR, particularly for contractually mandated, two-step ADR mechanisms that combine mediation and arbitration in sequence (a process commonly referred to as med-arb).

This article endeavors to assess how the landscape of current arbitration law may be altered by the 11th Circuit's decision in *Thione* and how its teachings might apply to the growing use of step mediation/arbitration clauses. We argue that although the FAA may be inapplicable to a contract containing only a mediation agreement, where the final stage of a step clause is binding

impasse in mediation will block an end to the dispute since a binding arbitration decision will follow if the parties are unable to reach a settlement agreement.

The fact that the parties have agreed in advance to accept an arbitrator's decision as final and binding has led some commentators to refer to med-arb as "mediation with muscle" or "mediation with a bite."³

The last few years have seen an expansion in the use of med-arb.⁴ The contours of today's med-arb have developed primarily in the context of labor, international and corporate disputes.⁵ Parties have been lured by med-arb's ability to encourage settlement because the parties would rather reach their own agreement than have an arbitrator impose a decision on them. And if the parties do settle during mediation, their settle-

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arbitration, *Thione's* holding should not apply so that the FAA's remedies remain available to the parties throughout the process, including during the mediation phase.

The Two-Step Mediation/Arbitration Clause

There are many forms of med-arb. Many think it is a hybrid process in which the mediator becomes the arbitrator if the dispute does not settle in mediation and it becomes necessary to arbitrate.² Others view med-arb as separate sequential processes in which there are two neutrals: one serving as the mediator and the other serving as the arbitrator if it is necessary to conduct an arbitration proceeding.

A variation on the latter process, known as comed-arb, allows the mediator and the arbitrator to jointly conduct a fact-finding hearing at the outset of the dispute. The hearing is followed by mediation, and then arbitration if the mediation does not succeed. For purposes of this article, med-arb refers simply to any process in which mediation takes place as a condition precedent to binding arbitration.

Why Med-Arb?

Med-Arb agreements allow parties to combine the benefits of two ADR processes—mediation and arbitration—and, as a result, guarantee that a final and binding award will be issued in the event that a settlement is not achieved in mediation. Med-arb eliminates the possibility that

ment agreement becomes the final award, which is binding and enforceable as law.⁶

The finality med-arb brings to disputes is arguably its most appealing attribute. And as suggested above, the threat of an arbitration award gives parties a greater incentive to settle than in mediation alone. In most situations, it is in the best interest of the parties to amicably resolve their disputes during the mediation step and avoid the cost of arbitration and losing control over the outcome of their case.

"Arbitration" under the FAA

Since the FAA and its legislative history fall short of providing any direct indicators of the meaning of the term "arbitration," it has fallen to the courts to establish the parameters of that term. A variety of legal tests have been put forward, one of which is the "classic" arbitration model described by the 1st Circuit in *Fit Tech v. Bally Total Fitness*. The 1st Circuit ruled that classic arbitration involves at least these four "common incidents": (i) an independent adjudicator, (ii) who applies substantive legal standards, (iii) provides an opportunity for the parties to be heard, and (iv) renders a final, binding decision or award after the hearing.⁷

The 5th and 10th Circuits appear to subscribe to this model. In *General Motors Corp. v. Pamela Equities Corp.*, the 5th Circuit stated, "Arbitration is the reference of a particular dispute to an impartial third person chosen by the parties to a dispute

who agree, in advance, to abide by the arbitrator's award issued after a hearing at which both parties have an opportunity to be heard."⁸ In *Salt Lake Tribune Publishing Co. v. Management Planning*, the 10th Circuit held that classic arbitration was characterized by "empower[ing] a third party to render a decision settling [the] dispute."⁹

By contrast, the 4th, 8th, and 9th Circuits have enforced under the FAA written dispute resolution provisions that do not call for a binding award. An example is *United States v. Bankers Insurance Co.*, wherein the 4th Circuit opined that "[a]lthough non-binding arbitration may turn out to be a futile exercise ... this fact does not, as a legal matter, preclude a non-binding arbitration from being enforced [under the FAA]."¹⁰

The 9th Circuit agreed with this rationale in *Wolsey v. Foodmaker, Inc.*, in which it said, "Arbitration need not be binding in order to fall within the scope of [the FAA]."¹¹

Citing these 4th and 9th Circuit cases as persuasive precedents, the 8th Circuit, in *Dow Corning Corp. v. Safety National Casualty Corp.*, said that while binding arbitration is the norm under the FAA, there was no express language in the FAA that limited the statute to binding arbitration agreements.¹²

District court interpretations of the term "arbitration" under the FAA have been just as varied. The court in *AMF Inc. v. Brunswick Corp.* recognized the disparity in the decisions of other courts, acknowledging that arbitration is "a term that eludes easy definition."¹³ Of the precedent from the early 20th century, the court observed, "[A]t no time have the courts insisted on a rigid or formalistic approach to a definition of arbitration." Thus, it was content to find that "no magic words such as 'arbitrate' or 'binding arbitration' or 'final dispute resolution' [were] needed to obtain the benefits of the [FAA]."¹⁴

The contract at issue in *AMF* stated that in the event a controversy arose with respect to a particular aspect of the parties' agreement, an "advisory third party" would be commissioned to render an "advisory opinion" that would not bind the parties. Giving no weight to the absence of the word "arbitration" in the parties' contract, the court framed the issue using language from Section 2 of the FAA: Was "a controversy" likely to be "settled" by the ADR process set forth in the parties' agreement? The court answered the question in the affirmative, finding that a non-binding process that ultimately results in a factual determination that could affect the rights of the parties is sufficient to "settle" their "controversy," even though they might want to continue to resolve related disputes in another forum.

The fact that the ADR process the parties agreed to use "may not end all controversy between the parties for all time is no reason not to enforce the agreement," the court said.

Thus, construed broadly, the *AMF* decision could lead to the conclusion that any ADR process likely to settle a dispute "in the light of reasonable commercial expectations" would be sufficient to invoke the remedies in the FAA.¹⁵ As a district court decision, the ruling is not binding precedent. However, the reasoning in *AMF* has been cited and followed by several circuit courts.¹⁶

Other district courts have broadly interpreted the term "arbitration" to embrace mediation, a process that is procedurally distinct from arbitration. For example, in *Fisher v. GE Medical Systems*, the district court in the Middle District of Tennessee concluded that "arbitration in the FAA is a broad term that encompasses many forms of dispute resolution," including mediation.¹⁷ After noting that "federal policy favors arbitration in a broad sense," the court found that "mediation surely falls under the preference for non-judicial dispute resolution." Thus, it held that an agreement to mediate before filing a lawsuit was subject to the FAA and, as a result, the court had authority to compel the parties to mediate.

In *Cecala v. Moore*, a district court in the Northern District of Illinois went so far as to say that an agreement to mediate all disputes "arising out of" or "relating to" a contract was properly categorized as a "generic arbitration clause" for purposes of a state arbitration statute.¹⁸ The court used the terms "arbitration" and "mediation" interchangeably, and did not draw any attention to the procedural distinctions between the two processes. It went on to enforce a mediation agreement under the FAA and then stayed judicial proceedings pending mediation.

Another district court, in *Ellis v. American Environmental Waste Management*, following *AMF*, enforced a mediation provision under the FAA, reasoning that it "manifest[ed] the parties' intent to provide an alternative method to 'settle' controversies arising under [their agreement]."¹⁹ The court also held that the intent of the mediation provision fit "within the [FAA's] definition of arbitration."

One commentator aptly noted that a logical extension of the *Ellis* decision would make the FAA applicable to "virtually any ADR process."²⁰

What this conflicting body of judicial decisions teaches us is that courts do not agree on a single definition of the term "arbitration." It is with this

awareness that we turn to the 11th Circuit's *Thione* decision.

A Close Look at *Thione*

Prior to this case, the 11th Circuit had not addressed the types of ADR processes that qualify as "arbitration" under the FAA. *Thione* was, therefore, a case of first impression.²¹

The case involved a licensing agreement that gave the plaintiff exclusive rights to market and distribute the defendant's nutritional supplements and a related testing kit. The licensing agreement contained an ADR clause stating that if a dispute were to arise under the agreement that was not resolved privately within 60 days, the dispute would be submitted to either "non-binding arbitration or mediation with a mutually agreed upon, independent arbitrator or mediator."

Over the course of the parties' commercial relationship, the defendant allegedly sent *Thione* many defective testing kits and failed to adequately cure this breach of contract. In derogation of the ADR clause in the licensing agreement, *Thione* filed a breach of contract case in state court in Florida. After removing the case to federal court on diversity grounds, the defendant filed a motion to stay the suit pending arbitration pursuant to Section 3 of the FAA. The district court denied the stay on the ground that the parties' agreement failed to require the parties to arbitrate the dispute through a final decision.²² The district court reasoned that since the agreement created "an option for the aggrieved party to call for either non-binding arbitration or mediation, the parties had made arbitration the prerogative—not the obligation—of the aggrieved party."

On appeal, the 11th Circuit framed the issue as whether a contract under which disputes were to be submitted to either "non-binding arbitration or mediation" was an agreement "to settle by arbitration a controversy" in accordance with Section 2 of the FAA, thereby making the dispute

"referable to arbitration" under Section 3 and making entry of a stay of litigation mandatory. Section 3's stay remedy, the court noted, would be unavailable to an aggrieved party if the ADR procedure failed to constitute "FAA arbitration."

The 11th Circuit acknowledged that "there are few clear rules in delineating the bounds of FAA arbitration" and that several district courts had ruled that mediation agreements are enforceable under the FAA, primarily based on the principle that doubts about arbitrability are to be resolved in favor of arbitration. However, the 11th Circuit was persuaded by the 1st Circuit's reasoning in *Fit Tech*. This case suggested that the true test for deciding whether a particular dispute resolution process constitutes "FAA arbitration" is to look for the four "common incidents" of "classic arbitration."

Although the 11th Circuit stated that the presence or absence of any one common incident would not always be determinative, it held that one common incident controlled the result in *Thione*: a process that results in a final and binding award. The 11th Circuit held as follows. Where a dispute resolution process "does not produce some type of award that can be meaningfully confirmed, modified, or vacated by a court upon proper motion, it is not arbitration within the scope of the FAA." The court explained that the FAA "clearly presumes that arbitration will result in an 'award' declaring the rights and duties of the parties," and "much of arbitration law is predicated on the existence of an award."

The court went on to explicitly state that because mediation does not resolve a dispute, that process is not within the FAA's scope. It reasoned that allowing a party to compel mediation under the FAA could increase the time and cost spent in litigation, thus running afoul of the purpose of the FAA. Furthermore, the court said that when a contract gives the parties an option to mediate or arbitrate, that agreement also is not

The 11th Circuit relied on the 1st Circuit, which previously ruled that "classic arbitration" involves at least these four "common incidents": (i) an independent adjudicator, (ii) who applies substantive legal standards, (iii) provides an opportunity for the parties to be heard, and (iv) renders a final, binding decision or award after the hearing.

“an agreement to settle by arbitration a controversy” and therefore is not enforceable under the FAA.

Thus, the existence of the option to mediate was enough to preclude enforceability of the arbitration agreement under the FAA, despite the existence of the option to arbitrate.²³

Since the ADR clause in *Thione* allowed the parties to choose between alternatives that included a non-binding process, the 11th Circuit found that the clause was not capable of enforcement under the FAA.²⁴

Thione holds that processes that deviate from classic arbitration do not fall under the scope of the FAA. This holding was based on the 11th Circuit’s concern that the FAA not be indiscriminately applied. For this reason the court applied a simple test for “FAA arbitration”: Will an award ensue?

Furthermore, the court said that when a contract gives parties an option to mediate or arbitrate, that agreement also is not “an agreement to settle by arbitration a controversy” and therefore is not enforceable under the FAA.

Med-Arb and *Thione*

Significantly, *Thione* is silent with respect to whether a court could grant remedies under Section 3 of the FAA when the parties have agreed to mediate *and* arbitrate, if necessary. The 11th Circuit simply did not address whether these remedies could be applied to mediation when that process is a predicate to classic arbitration. Thus, if the parties entered into a med-arb agreement, could a district court grant a mandatory stay of litigation and enter an order compelling mediation? If not, when could those remedies be invoked?

In some jurisdictions, where a party has refused to mediate under a med-arb clause, district courts have liberally granted motions to stay litigation pending mediation, and if necessary, arbitration, under the FAA.²⁵ However, the 1st and 11th Circuits have taken a more cautious approach, reasoning that since mediation is a “condition precedent” to arbitration, the arbitration provision of the med-arb clause is not triggered, and the FAA cannot be invoked until one party requests mediation.²⁶

However, in both scenarios courts have stayed litigation in support of med-arb agreements. Many courts have also granted motions to compel mediation under a med-arb agreement, reasoning that the mediation is part of the arbitra-

tion process. But in the 11th Circuit, the *Thione* decision calls into question the availability of these FAA remedies to support the mediation step of a med-arb agreement.

We believe these remedies should be available for the following reasons. First, med-arb agreements make arbitration the final step of a two-step ADR process in order to avoid litigation in court. Thus, they are designed “to settle by arbitration a controversy” under Section 2 of the FAA. In our view, any dispute triggering the med-arb clause should be “referable to arbitration” under Section 3 of the FAA if a party fails to comply with the med-arb clause, such as by failing to mediate.

Second, while a mediation clause standing alone will not result in an adjudication of a dispute, med-arb guarantees an end to the dispute through a mediated settlement agreement that

can be enforced as an award, or an adjudication in arbitration if the parties do not reach a mutually acceptable settlement. With such finality assured, remedies under Section 3 and Section 4 of the FAA should be applicable to med-arb agreements.

While there are avenues to compel mediation outside of the FAA,²⁷ we believe the federal courts should embrace the growing support of med-arb by, among other things, finding that these agreements are enforceable in their entirety under the FAA.

Conclusion

There is a fundamental distinction between an ADR agreement that allows parties to either mediate or arbitrate disputes, and a classic med-arb agreement, which calls for mediation as a condition precedent to binding arbitration. While a med-arb agreement was not before the 11th Circuit in *Thione*, we caution against applying that court’s reasoning to med-arb agreements. We agree that the FAA may be inapplicable to agreements to mediate. But med-arb agreements are different because they are intended to bring the dispute to an end, one way or another. We hope that a future decision by the 11th Circuit will expand the classic arbitration model to include the med-arb process. ■

ENDNOTES

¹ No. 07-12309, 2008 U.S. App. LEXIS 8584 (11th Cir. April 21, 2008).

² Some believe that where the same neutral serves as the mediator and arbitrator, the differences between mediation and arbitration are artificial. See generally Carllose de Vera, "Arbitrating Harmony: 'Med-Arb' and the Confluence of Culture and Rule of Law in the Resolution of International Commercial Disputes in China," 18 *Colum. J. Asian. L.* 149, 155-156 (2004). A med-arb agreement can be drafted in a way that allows the parties to opt-out from using the mediator as the arbitrator in the second stage upon timely notice.

³ See Karen L. Henry, "Med-Arb: An Alternative to Interest Arbitration in the Resolution of Contract Negotiation Disputes," 3 *Ohio St. J. Disp. Resol.* 385, 390 (1988). See also Sherry Landry, "Med-Arb: Mediation with a Bite and An Effective ADR Model," 63 *Def. Couns. J.* 263 (1996).

⁴ Even a decade ago, as much as 40% of *Fortune* 1000 companies were participating in med-arb. See David Lipsky & Ronald Seeber, "The Appropriate Resolution of Corporate Disputes: A Report on the Growing Use of ADR by U.S. Corporations," (Martin and Laurie Scheinman Institute on *Conflict Resolution*), available at <http://digitalcommons.ilr.cornell.edu/icrpubs/4>.

⁵ John T. Blankenship, "Developing Your ADR Attitude: Med-Arb, a Template for Adaptive ADR," 42 *Tenn. B. J.* 28, 32-33 (2006).

⁶ This is yet another benefit of the Med-Arb process. A settlement agreement resulting from a "pure" mediation is generally enforceable as a contract but courts are unlikely to give that agreement the same deference as an arbitral award. Mediated settlements in the context of Med-Arb are different, however, since the mediation and arbitration processes are intertwined, and the mediated settlement can be recorded in the arbitral award and become binding and enforceable.

⁷ 374 F.3d 1, 7 (1st Cir. 2004).

⁸ 146 F.3d 242, 246 (5th Cir. 1998).

⁹ 390 F.3d 684, 689 (10th Cir. 2004).

¹⁰ 245 F.3d 315, 322 (4th Cir. 2001).

¹¹ 144 F.3d 1205, 1209 (9th Cir. 1998).

¹² 335 F.3d 742, 747 (8th Cir. 2003).

¹³ 621 F. Supp. 456, 459 (E.D.N.Y. 1985).

¹⁴ For this proposition, the decision in the *AMF* case cited *City of Omaha v. Omaha Water Co.*, 218 U.S. 180, 194 (1910) ("a plain case of the submission of a dispute or difference which had to

be adjusted ... was in fact arbitration, though the arbitrators were called "appraisers"). It later refers to *Wood v. Lucy Duff-Gordon*, 222 N.Y. 88 (1917), in which Judge Cardozo granted equitable relief in a contract action, stating: "The law has outgrown its primitive stage of formalism when the precise word was the sovereign talisman, and every slip was fatal. It takes a broader view today ... The whole writing may be 'instinct with an obligation,' imperfectly expressed...")

¹⁵ See also Thomas J. Stipanowich, "The Arbitration Penumbra: Arbitration Law and the Rapidly Changing Landscape of Dispute Resolution," 8 *Nev. L.J.* 427, 440 (Fall 2007).

¹⁶ See *Fit Tech*, *supra* n. 7. See also *Harrison v. Nissan Motor Corp.*, 111 F.3d 343, 349 (3rd Cir. 1997); and *Wosley Ltd. v. Foodmaker, Inc.*, 144 F.3d 1205, 1208 (9th Cir. 1998).

¹⁷ 276 F. Supp. 2d 891, 893 (M.D. Tenn. 2003),

¹⁸ 982 F. Supp. 609, 613 (N.D. Ill. 1997).

¹⁹ 1998 WL 903495 *2 (E.D.N.Y. 1998).

²⁰ Thomas Stipanowich, "The Arbitration Penumbra," 8 *Nev. L.J.* 427 n. 110.

²¹ No. 07-12309, 2008 U.S. App. LEXIS 8584 (11th Cir. Apr. 21, 2008).

²² See *Advanced Bodycare Solutions LLC v. Thione Int'l, Inc.*, 514 F. Supp. 2d 1326 (S.D. Fla. 2007), *aff'd*, see citation *supra* n. 1.

²³ Even though the alternative to mediation was non-binding arbitration, the 11th Circuit's own language implies that its decision would be no different had the alternative been binding arbitration. The court stated, "When an aggrieved party has an unconditional right to choose between two or more dispute resolution procedures, and one of them is not FAA arbitration, the contract is not one 'to settle by arbitration a controversy.'" It further said, "[A] dispute resolution clause that may be satisfied by arbitration or mediation, at the aggrieved party's option, is not 'an agreement to settle by arbitration a controversy' and thus is not enforceable under the FAA ..."

²⁴ While the 11th Circuit held "that the mandatory remedies of the FAA may not be invoked to compel mediation," it acknowledged that stays in aid of mediation were not *per se* impermissible. The court recognized that "district courts have inherent, discretionary authority to issue stays in many circumstances, and granting a stay to permit mediation (or to require it) will often be appropriate ..."

²⁵ See, e.g., *Design Benefit Plans, Inc. v. Emright*, 940 F. Supp. 200 (N.D. Ill.

1996) (granting a party's motion to compel mediation/arbitration and stay proceedings pursuant to FAA §§ 3 and 4). See also *Woodlands Christian Acad. v. Logan*, 1998 Tex. App. LEXIS 3185, at 8-9 (Tex. App. 1998) (citing arbitration precedents relating to enforcement of multi-step process involving mediation followed by binding arbitration).

²⁶ See, e.g. *HIM Portland LLC v. Devito Builders, Inc.*, 317 F.3d 41, 44 (1st Cir. 2003); see also *Kemiron Atlantic Inc. v. Aguakem Int'l Inc.*, 290 F.3d 1287, 1291 (11th Cir. 2002).

²⁷ Some jurisdictions have codified rules for the enforcement of mediation agreements. See, e.g., the Texas Alternative Dispute Resolution Procedures Act, Tex. Civ. Prac. & Rem. Code Ann. § 154.001-154.073. In the international context, special statutes now allow for enforcement of mediation agreements. See, e.g., the UNCITRAL Model Law on International Commercial Conciliation (2002); see also the California International Arbitration and Conciliation Act, Cal. Civ. Proc. Code § 1297.11-1297.432.

Absent legislation, most courts have the inherent power to order mediation *sua sponte* when doing so may expedite resolution of a case. See, e.g., *U.S. Fidelity & Guaranty Corp. v. Bangor Area Joint School Auth.*, 355 F. Supp. 913, 917-918 (E.D.P.A. 1973) (quoting *Merritt-Chapman & Scott Corp. v. Pennsylvania Turnpike Comm'n*, 387 F.2d 768, 773 (3rd Cir. 1967), as follows: "[S]uch a remedy is one which is within the inherent power of a court and does not require statutory authority.... The power to stay proceedings is 'incidental to the power inherent in every court to control the disposition of the causes on its docket.'")

The ability to enforce contracts to mediate also may be seen as incidental to a court's authority to order parties to participate in mediation. See Stipanowich, *supra* n. 20, at 448, citing Elizabeth Plapinger & Donna Stienstra, *ADR and Settlement in the Federal District Courts: A Sourcebook for Judges and Lawyers* 66 (1996), for the proposition that most federal mediation programs authorize judges to order parties to mediation even without their consent. Stipanowich says this authority has been established by several rules of court. Here he cites *Vitakis-Valchbine v. Valchbine*, 793 So. 2d 1094, 1098 (Fla. Dist. Ct. App. 2001), and *Fuchs v. Martin*, 845 N.E.2d 1038 (Ind. 2006).

Finally, a mediation agreement may be specifically enforced as a contract.