AMERICAN BANKRUPTCY INSTITUTE

2019 Southwest Bankruptcy Conference

Alternative Dispute Resolution Provisions in Bankruptcy

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CONCURRENT SESSION

2019

THERE IS A PLACE FOR MEDIATION IN BANKRUPTCY COURT

Mediation has become more popular in both State and Federal Courts, but appears to be not so much in demand in Bankruptcy Court. A variety of reasons may explain why this is the case. Without question, many Bankruptcy Court disputes do not lend themselves to mediation because of their simplicity, expediency, and in many instances, the parties may not be in a position to bear the cost of the mediation process. Presumably, in other situations, attorneys' unfamiliarity or discomfort with the process may come into play and, additionally, some practitioners may not realize how effective mediation can be in many instances. Finally, because of the unusual nature of work in this area, many highly trained and qualified mediators are simply not familiar with discrete bankruptcy issues, which can easily impact on a mediator's effectiveness.

Notwithstanding all of the obstacles just described, mediation definitely has a place in the bankruptcy world, can be successful, save the parties money, and minimize adversaries' time, psychological investment and, in many cases, brain damage.

I will provide some historical perspective on development of this area in the Arizona Bankruptcy Court system.

HOW IT ALL STARTED

In the early 1990s, I volunteered on what I believe was a Bankruptcy Section committee specifically formed to investigate the drafting of mediation guidelines for the Bankruptcy Courts. The savings and loan collapse of 1990/91 had triggered a dramatic downturn in the economy and, in particular, in Arizona, because of the large numbers of these institutions which dominated our financial marketplace. As the RTC intervened, the number of bankruptcy cases skyrocketed and the Bankruptcy Court dockets became, in many instances, overwhelmingly crowded. Many forward thinking individuals in the bankruptcy field recognized the benefit of alternative dispute resolution and, in particular, mediation, which had rarely been considered prior to the early 1990s.

That committee researched other districts' progress in this area and even though I do not believe it succeeded in drafting and implementing mediation standards which were eventually adopted by the local courts, it set the groundwork for what we have today, which includes a pool of certified bankruptcy mediators, both compensated and uncompensated, a much higher level of sophistication among our bankruptcy judges to conduct mediations, and professional mediators now very sophisticated in this area.

Because of a personal interest I have always had in mediation and a deeply engrained belief that a large percentage of disputes could be resolved by the intervention of an impartial third party expert, I actively began seeking out the assistance of bankruptcy judges to mediate matters over twenty (20) years ago.

In the mid-1990s, our sitting judges were receptive to the idea to a varying degree, but many of them recognized they were lacking training and sophistication in that area.

Nevertheless, I engaged in a methodical and deliberate campaign to engage all of the different judges in this process and I believe I succeeded in compelling every single one of them to intervene in that capacity, with the exception of Judge Ollason in Tucson.[*] During the course of the mediations that I engaged in during the 90s and through the beginning of the century, I concluded the following.

a. It was very cost effective for most participants;
b. The success rate of it was higher than I even thought, probably 70 to 80%;
c. The judges sincerely seemed to enjoy it;
d. Most of the lawyers involved enthusiastically participated, but did not fully understand the process;
e. Additional training for the judges would be helpful, though the judges were doing a fine job without that training; and
f. A more formal structure for the process would benefit everyone.

At the same time, I quickly learned the difference between evaluative mediation versus what I call facilitative mediation in that some judges tried to direct the parties towards what they believed would be the ultimate result if the matter proceeded to Court, whereas other judges were only concerned with trying to facilitate a settlement regardless of how the matter would ultimately be resolved through formal proceedings.

So, what is mediation and when is it appropriate?

The following is the verbiage I provide any client who may at any juncture want to consider mediation.

MEDIATION

> Mediation is a procedure in which the parties to litigation voluntarily agree to meet with a third party, the mediator, in hopes of settling the outstanding disputes between the parties. The purpose of mediation is to achieve a settlement relatively quickly and inexpensively and to bring a dispute to a final close. Mediation requires the active participation of all parties involved and requires that those parties are willing to listen to a third party and consider what he or she may recommend.
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> To increase the chances that the implementation of mediation would be successful, a number of attorneys underwent an extensive mediation program and were certified as mediators after completing an application process. However, mediation does not require that you select a certified mediator, though if you select one that is not certified, it is a good idea to at least make sure that the person selected is generally

[*] There was no nefarious reason for omitting Judge Ollason. It simply resulted from my not knowing Judge Ollason that well and a perception that he was heavily debtor biased.

familiar with the mediation process to increase the chances that a settlement is reached during the mediation hearing.

To encourage the free exchange of information and to create an atmosphere conducive to settlement, what takes place as part of the mediation process is not otherwise admissible in the underlying case. And, during the course of the mediation proceeding itself, if a party does not want a communication with the mediator to be disseminated to the other side, the mediator is bound to not disclose that information.

Because you do not want the mediation process to be rushed, you need to put aside a full day for mediation. The mediator will normally begin with a joint meeting of all parties and then separate the parties so he can speak individually with each side. During the course of the day, he will go back and forth while he becomes educated and begins to formulate a settlement strategy. Periodically, he may bring the parties together again to talk and there may even be times in which the mediator speaks to one side's counsel outside of the client's hearing or directly to a client without the attorney being present. However, whatever process the mediator utilizes requires the consent of the parties and their counsel.

In advance of the mediation hearing, the mediator normally wants each side to submit a mediation brief. A properly drafted brief will provide the mediator with the tools necessary to formulate a strategy, but the mediation brief should not be a compilation of the entire case. Instead, the brief should focus on how the mediator can achieve a settlement since it is not the mediator's goal to decide who is right or wrong, but rather to find a resolution palatable to all involved.

The timing of the mediation is crucial to its success. Engaging in mediation too early in the case can be a total waste of time if the parties are not aware of the basic components of each side's position. Additionally, it is oftentimes difficult to convince a party to settle early in the case because commonly parties may be firmly entrenched since nothing has occurred to convince that settlement may be a better approach. Therefore, it is normally better to engage in mediation once all the parties have had a chance to become better educated about the respective claims and defenses.

You do not want to wait too long to mediate because if you do, the parties may even become more entrenched than at the beginning and will have spent so much time and money in litigating that they no longer have an interest nor can financially justify a compromise through mediation. For example, if a party is being sued for $100,000.00, and each side has already spent $30,000.00 or $40,000.00 in legal fees and costs at the time the matter is presented to a mediator, there may not be a solution available that would make the plaintiff happy which the defendant could even afford

or justify. It therefore becomes important for the parties to proceed with mediation at a point in which the time and money spent is not so great that a compromise is not practical.

What does mediation cost? The parties split the cost of the mediator and you need to assume that a mediator will charge somewhere around $6,000.00 - $7,000.00 to prepare for and conduct a one-day mediation. From past experience, you need to assume that it will take four to five hours for you and your counsel to prepare for mediation and prepare the appropriate mediation brief. Therefore, you need to anticipate that your legal fees for preparing for and attending the mediation will probably be about $7,000.00. Though these numbers are obviously estimates, you need to anticipate that between the mediator's services and your own attorney's time, you are looking at somewhere around $10,000.00 - $10,500.00. Though this is a serious number, it is inconsequential if mediation will settle a six-figure dispute in which each side can easily spend $50,000.00 - $100,000.00 in legal fees and costs.

I am a fan of mediation for many reasons. Even before mediation was becoming popular in Bankruptcy Court, I had been having difficult litigation cases referred to other bankruptcy judges for mediation because such a practice had been common in State Court where I practiced extensively in the 1980s. Between the early 1990s and a few years ago, I was able to settle five of my more difficult bankruptcy litigation cases through mediation conducted by other bankruptcy judges. On each occasion, I was and still am convinced that the result achieved was the most economical and equitable one possible.

Coincidentally, I was on a State Bar committee that began this process in 1990, but for political reasons, was never able to procure approval of mediation rules and procedures. But, as a believer in the process, I was a member of the first certification class and am now a certified bankruptcy mediator.

Finally, if the parties select the proper mediator and time it right, mediation is successful 80%-90% of the time. It works for the simple reason that a trained and impartial third party is in the best position to evaluate a dispute and has no reason to recommend a specific resolution except for a sincere belief that such a resolution is in everyone's best interest.

This verbiage has evolved over the years and has encouraged clients to consider mediation and provided enough background so that the client could make a knowing and intelligent decision. It also addresses from the onset the important questions of; a) cost; b) the process itself; and c) its success rate. What the introduction does not do is address a number of discrete issues which need to be determined on a case-by-case basis.

I will begin with the initial issue of when you should mediate.

WHEN DO YOU MEDIATE?

When a Court strong-arms parties into mediation, the mediation's timing is probably outside the control of the adversaries. However, especially in bankruptcy matters, the judges oftentimes look to the parties for guidance as to when the timing is right, which allows the parties a fair amount of discretion as to when mediation is scheduled.

As a practical matter, since mediation is voluntary, the client and the client's counsel need the cooperation of the other side, but interestingly enough, persuading opposing parties to mediate has normally not been that difficult. And, when an invitation is summarily rebuked, this in itself is highly educational in that litigation strategy needs to focus on preparing for trial since a vociferous refusal of mediation sends a rather strong signal of the other side's intent and desires.

Since the overall goal of mediation is to save money, how far does the litigation have to progress for mediation to be most cost effective?

Over the years, I have discovered something which many experienced lawyers vehemently disagree with; you normally do not need to engage in extensive discovery before mediating. They do not need to do so because in most cases, discovery simply confirms a party's respective position for evidentiary purposes and rarely results in any type of dispositive finding. The pendency of time-consuming and all expensive discovery actually helps facilitate a settlement, whereas once it is completed, that cost more often than not hampers the settlement process.

If you believe that in most cases the earlier the mediation, the better, one may ascribe to the view that mediation should be attempted even before litigation ensues. That philosophy is the reason why many agreements now mandate mediation even before formal proceedings are commenced.

In certain instances, initiating mediation may be premature. Once the Complaint is filed and the issues are joined, waiting for at least initial disclosure is probably advantageous in many cases. In other situations, at least some exchange of information and at least one round of negotiations can be extremely helpful to educate parties about the other side's position and expectations.

Interestingly enough, even when mediation fails in part because it was too early, an astute litigator can still be educated about how the adversary views the case and the mediator's perspective on the strengths and weaknesses of each side's positions.

Separate and apart from the timing of the mediation relative to the age of the case, a party needs to consider certain psychological and practical factors as well. I never want my client to walk into mediation after losing an important Motion or facing damaging

discovery or when for whatever reason, a client is not 100% mentally prepared. Most of the time the other side welcomes the chance to mediate when the case is not going well for it.

SELECTING A MEDIATOR

I devote substantial attention to considering which mediator to use depending upon a number of factors, including the issue being addressed, the amount involved, the personalities of the parties, who the opposing counsel is, and different mediation styles. Sometimes I'm accused of mulling over this decision too much, although in most cases, it is probably worth it.

Since I have mediated so many cases over the years, I have familiarized myself with the varying styles utilized and have come to the following conclusions.

The first factor to take into account when selecting a mediator is whether the mediator uses an evaluation approach versus more of a facilitative one. Without question, when I have the facts and/or the law in my favor, I want the former. When I need a mediator who will not be concentrating on the respective strengths and weaknesses of my client's case, I pick a mediator who will use his/her skills to find a way to bring the parties together regardless of the respective strengths of each side's case.

I am often surprised that when my adversary is choosing the mediator, this basic style concern is not taken into account. I almost always try to consider and prioritize this concern.

Sometimes, you need a mediator who can be an absolute "hammer." No one was better than Gary Birnbaum at this rather discrete skill. His confidence, bravado and borderline obnoxiousness made him unbelievably effective in most cases. In many instances, I personally loved this approach since I have always believed that even a mediocre settlement is normally better than proceeding to trial. The only time it can backfire is when; a) a mediator of this type decides your case would lose and will not listen; or b) a client is so intimidated that the client wants to fold notwithstanding your advice.

Some of the mediators prepare far more carefully and meticulously than others. Your clients will pay the price for this approach, but regardless of the relative strengths of my client's case, I would rather have a mediator over-prepared than not. In simpler cases or ones in which an in depth understanding is not necessary, an over-prepared mediator can actually be problematic, but this is the exception. You need to take this into account from the onset.

Some mediators are brilliant at being able to incorporate detailed financial data into the analysis. If you have a case where this can be crucial, you would want to pick a mediator who will review the numbers in advance and be comfortable working with them during the mediation sessions.

Some mediators are warm and fuzzy and do an excellent job in setting a very soothing atmosphere to encourage reconciliation. Before you go this route, think about the parties involved and whether this important skill is totally superfluous in your case.

I really appreciate it when the mediator quickly recognizes whether the case may not settle, but decides to use the mediation process to create an atmosphere in which settlement may be possible later on, or occasionally, advises your client that the client's position is strong, the other side is being unreasonable and do not be afraid to continue the litigation under the circumstances. A mediator can be very beneficial in such situations even without a settlement.

You want a mediator who is astute enough to recognize the dynamics of the situation. If one side is stubborn, the mediator needs to find a way of discouraging the side from being so. If one side is being overly aggressive, the worst thing you can do is encourage that conduct continuing. Or, if a party is adopting totally unreasonable positions, demonstrating to the party the error of his/her ways can be invaluable in settling the case.

Should you consider an ex-bankruptcy Judge or another standing bankruptcy Judge? No easy answer exists since some judges appear to have had mediation training, some are highly effective independent of formal training or not, and others are frankly ineffective.

So, I recommend if a Judge is an option, consider this alternative, especially since the cost is right, free, but conduct research first. I probably have utilized every bankruptcy Judge, either retired or not, with two or three exceptions, and can tell you that certain are exemplary in some cases, while other are not.

I try to avoid becoming embroiled in a squabble over the selection of the mediator. I do so by asking the other side to simply forward to me three or four names of acceptable mediators. Almost without exception, I have discovered that at least one of the names will be fine.

I love this approach for the simple reason that it is much easier to settle the case if your adversary has selected the mediator for very obvious reasons. Remember, most lawyers select mediators based on what they perceive to be "success" with an individual, which by its very nature means that opposing counsel be more inclined to listen to the mediator's recommendations.

I will now review some mediation strategies.

MEDIATION STRATEGIES

Now that you have picked the appropriate time and the perfect mediator, the lawyer's work is far from over.

Drafting the Mediation Memorandum can be as crucial as any aspect of the procedure. Most mediators will grant the parties a fair amount of leniency as to the length of the Brief. Its length can be a very important strategic determination since in certain cases, a short Brief can be far more effective, whereas in more complex or unusual situations, a more detailed Brief may be necessary.

Think about whether you want confidential Briefs, either in lieu of exchanged Briefs or in addition to the primary briefing. I have always preferred at least a short confidential Brief to educate the mediator as to certain aspects of the dispute without inciting the other side. I have never had a mediator object vociferously to a confidential Brief, especially because sometimes it provides the mediator with crucial information which can actually facilitate a settlement.

For example, if a party believes that the adversary is being driven by personal, non-business reasons, alerting the mediator of this background can be invaluable. Not surprisingly, this suggestion can be very offensive to certain individuals or entities, so including it in an exchanged Brief can be very detrimental. Along the same lines, if an attorney believes that the other side is acting irrationally, the inclusion in a confidential Brief can be far less confrontational.

When I was a young, naïve lawyer, I believed that clients should walk into a mediation with a totally open mind and without any preconceived notions. I wanted the whole process to be as "fresh" as possible.

Now, I follow a diametrically opposed approach. Besides sending the letter, which I included earlier in this outline, I educate the client about the specific mediator selected, his/her style and actually try to walk the client through an actual mediation session, but in a condensed fashion. For example, I warn the client not to expect any real progress during the morning and, based upon the mediator selected and the adversary, sometimes tell the client not to expect to see any serious negotiation movement until the very end of the day. You would be amazed how much easier and more productive the session is once clients understand exactly what to expect.

The client and I agree in advance as to how much the client would volunteer without my direct input. Some clients want a chance to talk at great length to the mediator, whereas others are simply not comfortable. Never assume this going in.

I warn the client about the extent of the confidentiality of the process. Most importantly, I explain to the client that even though any offer made during the mediation cannot be used for any other purpose, once you offer a number at mediation, the other side will use that figure as a starting point going forward regardless of what occurs. If the client is not used to negotiating, this last aspect of the process will be very surprising to the client.

I point out to the client that even the most experienced mediators still have a tough time divorcing themselves from his or her personal biases and predilections. In most instances, if you are likeable and the mediator knows you are totally credible, the mediator will not be able to ignore this perception.

I ask the client to dress comfortably, but professionally, because I want to show the mediator respect. Even though oftentimes certain mediators will emphasize the need to be as comfortable and informal as possible, I always wear a suit. I may be very informal in break-out sessions with the mediator when only my client is present, but if joint sessions are utilized, never communicate in an informal manner with the mediator or put the mediator in a compromising position. Regardless of how well the mediator may know you, and sometimes you know the mediator very well, the mediator wants to maintain pure impartiality and you can help facilitate this.

As already mentioned, if the mediation is not going to succeed, I decide as early as possible what I can gain from the mediation and make sure to achieve what I can. Recently, I had a mediator tell my client and me that the other side was being totally unreasonable and that if the adversary would not change his position that we should go forward in litigation. Even though the client trusted me, this simply corroborated what I told the client and made her more comfortable suing.

You need to reduce any settlement to writing at the mediation regardless of how late it may be and how brief the settlement document may be. Even a hand-written agreement is better than an oral understanding. Even if it requires you to stay around an extra half an hour to an hour while you work on the wording of the settlement, do it. One reason why I always define the length of the mediation going in is to make sure at the eleventh hour, the parties do not part ways because of a scheduling conflict.

Finally, and once again this may seem obvious, you need to make sure that your client understands the financial obligation of the mediation and that the mediator needs to be paid. Do not put the mediator in the position of having to chase your client, which is unprofessional and is totally inappropriate on your end. If you are unsure that your client will pay, then make sure the client pays in advance even though there is nothing wrong with you reviewing the mediator's bills. I will not question most mediators' bills, and, if necessary, will explain it to the client so the client is also comfortable with it.

Finally, it is important to consider how a mediation can go awry.

MEDIATION PITFALLS

You can avoid almost all of the mediation minefields that may arise, but occasionally one will pop up unexpectedly.

If the mediator appears to be unprepared, spend the time early in educating the mediator. Do not try to focus on settling the case until the mediator has a full grasp of the background.

Sometimes the mediator will advise you very early that the other side does not appear to want to be reasonable or does not fully understand the process. In that case, I always grant the mediator permission to spend as much time as necessary early in the process to ascertain whether the other side's attitude can be changed. The mediator needs to differentiate posturing from the other side's inability to grasp the reality of the situation.

Occasionally, your own client will go sideways on you during the mediation process. This will sometimes prompt me to talk to the mediator privately to advise the mediator what may be prompting the client to state certain things and take certain positions. Since I always warn the client that I may have private sessions with the mediator, the client should be comfortable with this process.

Similarly, if a client feels like the mediator is picking on him/her, I will take the mediator aside privately and let the mediator know that the mediator's effectiveness is being impacted by my client's perception of what is going on.

Finally, and this happens very rarely, if my intuition tells me that for whatever reason the mediation may be counterproductive, which is extremely rare, I will as professionally as possible stop the mediation process.

I will elaborate on confidentiality.

CONFIDENTIALITY OF MEDIATION

A fundamental and crucial aspect of mediation is the confidentiality of the process. Mediation is intended to encourage an open and free exchange of information and concerns, and confidentiality helps advance those principles.

Confidentiality exists on two different levels during the mediation process. The entire procedure itself is confidential, which means that unless a binding settlement is reached or the parties agree to waive confidentiality, nothing that occurs during the mediation is admissible during any legal proceedings or otherwise can be used by a party for any purpose. Secondarily, during the course of the mediation, communications of a party with the mediator are otherwise confidential unless that party specifically agrees that any such discussions can be disseminated to the other side.

Though in 2011, one Ninth Circuit case suggests that in certain instances mediation may not be unconditionally confidential, a party can assume that whatever happens in mediation is absolutely confidential, no "ifs, ands or butts." *See Facebook, Inc. v. Pacific Northwest Software, Inc.,*640 F.3d 1034 (9th Cir. 2011).

It is important that a practitioner fully appreciate what this means. Without an adversary's consent, regardless of what may have happened in the mediation, a party cannot utilize anything that occurred in mediation for any purpose whatsoever. This is

even the case if ultimately it is determined that a party adopted an unreasonable position in mediation, lost the case and is now seeking legal fees. The prevailing party should not be able to argue that the opposition took an unreasonable position during mediation, resulting in some of the fees being incurred, because doing so would defeat the very purpose of mediation. Please note that this is totally different than if during the course of ordinary negotiations a party was advancing an unsupportable position. In that case, the successful party could utilize such negotiations to bolster an attorney fee claim.

Arizona case law has not only consistently upheld the confidentiality of mediation, but also has prevented a party from suing an attorney for malpractice because of a position that may have been argued during the mediation. See the case of *Grubaugh vs. Hon Blomo, County of Maricopa, et al.*, 238 Ariz. 264, 359 P.3d 1008 (App. 2015). Though at first glance, immunizing a lawyer from malpractice in such circumstances may appear to be extending the confidentiality concept unnecessarily too broad, extending confidentiality to that extent protects a lawyer who speaks candidly because of the protections of the mediation process. If a lawyer needs to fear that a client could sue him/her because of what that lawyer may have said or done during the mediation itself, lawyers could very well be stifled in their presentations. Furthermore, disgruntled clients who ultimately lose a case after not settling in mediation could then point the finger at their lawyers. Of course, this has the net result of basically immunizing a sloppy or irresponsible lawyer who totally misuses the mediation process, but a client needs to understand that reality is one of the consequences of mediation.

One cannot stress enough the reality that even though any offer made during mediation cannot be used for any other purpose during the course of the litigation, once an offer is uttered to the other side, that party will necessarily assume such an offer is the new baseline amount or offer for future negotiations. This is not precarious if that party is really presenting a final offer at the mediation and is willing to proceed to trial, but if such a party wants to engage in serious negotiations going forward, that party will need to accept that whatever was offered at the mediation is now the starting point for further discussions.

Similarly, educating the mediator of your bottom line position at the beginning of the mediation itself is also very risky unless you are dealing with a very experienced and skilled mediator. You want to be candid and forthright with the mediator, but remember that the mediator's goal in almost all instances is to see the case settled and not be overly concerned if the result is similar to what a judge would determine. If a mediator receives the impression that your client is extremely flexible and pliable and wants to settle regardless of the cost of doing so, it is almost impossible for even the best mediator to not utilize that knowledge to force a settlement.

SUMMARY

I sincerely believe that almost any dispute can be resolved at mediation if the other side is rational, you pick the correct mediator, and you and your client are properly prepared. Since in almost all instances, it is in your client's best interest to settle the case

if possible, it is incumbent upon you as counsel to do everything possible to ensure a satisfactory result at the mediation.