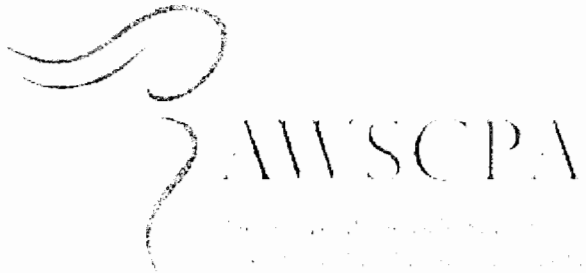
ARBITRATION & MEDIATION: ROLES & OPTIONS FOR THE CPA



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I. Introduction

Our long-evolving Anglo-American system of jurisprudence has worked well for hundreds of years and is one of the greatest socio-political inventions ever devised. However, the civil justice system has shown an emerging institutional weakness over the last several decades caused by the modern convergence of three principal factors: (1) the increased burdens on courts and judges created by the sheer volume of the "litigation explosion"; (2) the increased complexity of the law and lawsuits involving highly technical issues, voluminous documents, and expert testimony far beyond the ken of the average juror; and (3) the increased costs and delays associated with developing a civil case in light of the first two factors, as exacerbated by the legal profession's concern with avoiding professional malpractice by overdoing the job.

Consider that the minimum requirements for civil jurors in Texas as prescribed by Section 62.101, *et seq.*, of the Texas Government Code are basically (1) being at least eighteen years of age, (2) being qualified to vote (although not necessarily registering to vote), (3) being able to read and write, and (4) not being a convicted felon. This is certainly not the description of a person business would call upon to make decisions of major proportion concerning the resolution of a commercial dispute.

Fortunately, private dispute resolution mechanisms are becoming increasingly available and popular as alternatives to pursuing a dispute through the civil justice system. While some controversies between business parties need traditional, formal litigation procedures, many commercial disputes can be resolved privately through non-binding mediation or binding arbitration, in ways that save time, money, and relationships.

II. The Law of Alternative Dispute Resolution ("ADR")

A. Texas ADR Act

In 1987, the Texas Legislature enacted the Texas ADR Act (Chapter 154, Tex. Civ. Prac. & Rem. Code). This Act provides procedures for Court referral of pending litigation to any one of five ADR processes: (1) mediation, (2) mini-trial, (3) moderated settlement conference, (4) summary jury trial, and (5) arbitration. Mediation and arbitration have definitely stepped to the forefront as the preferred vehicles. The Act also specifies minimum qualifications of the impartial third-parties who convene ADR proceedings: at least 40 classroom hours of training in dispute resolution techniques.

B. Texas General Arbitration Act

Chapter 171, Tex. Civ. Prac. & Rem. Code, declares that a written agreement to submit any existing controversy to arbitration or a provision in a written contract to submit to arbitration any controversy thereafter arising between the parties is valid, enforceable, and irrevocable,

with the following exceptions: (1) unconscionable contracts; (2) collective bargaining agreements between employers and labor unions; (3) contracts of individuals involving $50,000 or less, unless both the parties and their attorneys sign the written agreement; (4) personal injury claims, except when counsel for both parties sign; and (5) workers' compensation claims. Arbitration awards are favored by Courts as a means of disposing of disputes, and thus every reasonable presumption will be indulged to uphold them. The Act sets up procedures for "confirming" arbitration awards (*i.e.* having Courts rubber-stamp them into judgments), vacating awards, as well as enjoining or compelling arbitration.

C. Employer/Employee Arbitration Statute

A separate statute, *i.e.* Chapter 102, Tex. Labor Code, sets up the mechanisms for arbitration of employer/employee disputes.

D. International Commercial Dispute Arbitration

A separate statute, *i.e.* Chapter 172, Tex. Civ. Prac. & Rem. Code, sets up the mechanisms for arbitration of international commercial disputes.

E. Federal Arbitration Act

The Federal Arbitration Act at 9 U.S.C. Sections 1-15 encourages private agreements for binding arbitration in transactions involving maritime, interstate, or international commerce, in a manner similar to the Texas General Arbitration Act, except that consumer transactions are not exempted as they are under the Texas $50,000 rule.

F. Common Law: Arbitration, Accord and Satisfaction, Compromise and Settlement

At common law, arbitration was once discouraged because it was perceived as "ousting the Court of jurisdiction." However, the modern view is to encourage arbitration at common law and create presumptions in favor of it because it keeps cases out of Court and promotes repose. Indeed, compromise and settlement are given every possible opportunity of succeeding by rules of law such as Rule 408, Tex. R. Evid., which provides that except in limited circumstances, evidence of furnishing or offering or promising to furnish, or accepting or offering or promising to accept, a valuable consideration in compromising or attempting to compromise a claim disputed as to validity or amount, is not admissible in Court to prove liability for, or invalidity of, the claim or its amount. Evidence of conduct or statements made in compromise negotiations is likewise not admissible.

The common law has consistently recognized that the existence and resolution of a dispute is sufficient consideration to support an agreement on different terms - *i.e.* an "accord." The performance of the accord (*i.e.* "satisfaction") completes the effect of the settlement transaction as a discharge of the originally disputed obligation. Thus, for example, if a creditor claiming he is owed $10,000 agrees to accept a compromise payment of $8,000 instead, then the accord and satisfaction disposes of the original debt. This again supports settlement processes by lending a stamp of finality to the result.

III. ADR Procedures

A. Binding Arbitration

Binding arbitration is the traditional private dispute resolution forum recognized by the Texas and federal arbitration acts. By committing contractually to arbitration, either before or after the dispute arises, the parties agree to be bound by the result of the arbitrator's award. Since the Courts will generally rubber-stamp such awards by converting them into judgments, except in limited and unusual circumstances (*i.e.* fraud on the part of the arbitrator), the arbitration is the "court" of first and last resort. However, because the parties define their forum, they may also select their arbitrator or panel of arbitrators. This means that a "jury" may be selected which has expertise or experience in the arena in which the problem arises. They may also schedule the proceeding at their convenience and may limit the expense involved in preparation and presentation of their respective positions.

B. Non-Binding Arbitration

Non-binding arbitration is a forum in which each party and counsel for the party present the position of the party before an impartial third-party, who renders a specific award. However, if the parties do not stipulate in advance that the award will be binding, then the award is not binding and serves only as a basis for the parties' further settlement negotiations.

C. Mediation

Mediation is a forum in which an impartial person, the mediator, facilitates communication between parties to promote reconciliation, settlement, or understanding among them.

D. Moderated Settlement Conference

A moderated settlement conference is a forum for case evaluation and realistic settlement negotiations. Each party and counsel for the party present the position of the party before a panel of impartial third-parties, usually attorneys. The panel may issue an advisory opinion regarding the liability or damages of the parties or both, but the advisory opinion is not binding on the parties.

E. Mini-Trial

In a mini-trial, pursuant to agreement, each party and counsel for the party present the position of the party either before selected representatives for each party, or before an impartial third-party, to define the issues and develop a basis for realistic settlement negotiations. The impartial third-party may issue an advisory opinion regarding the merits of the case, but that advisory opinion is not binding upon the parties unless the parties agree that it is binding.

F. Summary Jury Trial

In a summary jury trial, each party and counsel for the party present the position of the party before one or more panels of six or more jurors, to define the issues and develop a basis for realistic settlement negotiations. The jury (whose deliberations may be videotaped for subsequent review and evaluation by the participants) may issue an advisory opinion regarding either liability or damages or both, but that advisory opinion is not binding upon the parties.

IV. Confidentiality of ADR Processes

A. Unless expressly authorized by the disclosing party, the impartial third party conducting the ADR procedure may not disclose to either party information given in confidence by the other and shall at all times maintain confidentiality with respect to communications relating to the subject matter of the dispute.

B. Unless the parties agree otherwise, all matters, including the conduct and demeanor of the parties and their counsel during the settlement process, are confidential and may never be disclosed to anyone, including any appointing Court.

C. A communication relating to the subject matter of any civil or criminal dispute made by a participant in an alternative dispute resolution procedure, whether before or after the institution of formal judicial proceedings, is confidential, is not subject to disclosure, and may not be used as evidence against the participant in any judicial or administrative proceeding.

D. Any record made at an alternative dispute resolution procedure is confidential, and the participants or the third party facilitating the procedure may not be required to testify in any proceedings relating to or arising out of the matter in dispute or be subject to process requiring disclosure of confidential information or data relating to or arising out of the matter in dispute.

V. Documentation: Setting the Stage for ADR

A. Pre-Dispute Arbitration Clauses

Any controversy or claim arising out of or relating to any aspect of this contract (or agreement or engagement letter), or the performance or non-performance of this contract (or agreement or engagement letter), shall be settled by binding arbitration by submission to Wells & Cuellar Commercial Mediation and Arbitration Services, which shall conduct such arbitration at 440 Louisiana, Suite 718, Houston, Texas 77002. Judgment upon the award rendered may be entered in any court having competent jurisdiction.

1. Enforceability Under Texas General Arbitration Act

Prior to January 1, 1966, in Texas, only when an arbitration agreement involved an existing dispute and was filed with the Court would it be mandatorily enforceable. Any other arbitration agreement, except one viable under the Federal Arbitration Act, could be breached by either party at any time prior to rendition of an award. As of January 1, 1966, the Texas Legislature enacted the Texas General Arbitration Act, which applies both to agreements to arbitrate existing disputes as well as those to arbitrate future disputes.

2. Enforceability Under Texas Common Law

Passage of the Texas General Arbitration Act did not obviate the Texas common law regarding enforceability of arbitration agreements. Instead, the Act has been held to provide an alternative basis for enforcement. Before 1977, Texas common law allowed either party to an arbitration agreement to refuse to submit to arbitration any time prior to rendition of an award. But in 1977, the Texas Supreme Court, in the case of *Lacy vs. City of Lubbock*, 559 S.W.2d 348 (Tex. 1977), changed the common law rule to permit specific enforcement of arbitration agreements, recognizing that "[i]n addition to alleviating some measure of the burden on the courts, arbitration in a commercial context is a valuable tool which provides business people, and all citizens, with greater flexibility, efficiency, and privacy."

3. Enforceability Under Federal Arbitration Act

The Federal Arbitration Act provides yet another alternative basis for upholding an arbitration agreement, provided interstate commerce is involved. Interstate commerce is given a very broad interpretation and the actual nexus to interstate commerce may be fairly minimal or attenuated.

B. Post-Dispute Agreements to Arbitrate

We agree to submit to Wells & Cuellar Commercial Mediation and Arbitration Services for arbitration at 440 Louisiana, Suite 718, Houston, Texas 77002, the dispute involving (explain briefly), and further agree that a judgment upon the arbitration award may be entered in any court having jurisdiction.

C. Pre-Dispute Mediation Clauses

Any controversy or claim arising out of or relating to any aspect of this contract (or agreement or engagement letter), or the performance or non-performance of this contract (or agreement or engagement letter), shall first attempt to be resolved by submission to mediation by Wells & Cuellar Commercial Mediation and Arbitration Services, which shall conduct such mediation at 440 Louisiana, Suite 718, Houston, Texas 77002. The parties agree to attend and participate in good faith in such mediation.

D. Post-Dispute Agreements to Mediate

See the attached "Request for Submission to Mediation" form.

V. Roles for CPAs

A. Party or Party Representative

CPAs may themselves be parties to ADR and enjoy its benefits personally, or they may be among the representatives of a party such as their professional firm or their client.

B. Consultant to Party

In a manner analogous to the consulting role that CPAs can play in litigation support, CPAs can serve as consultants to parties who may choose to resolve their disputes by ADR.

C. Expert Witness

In binding arbitration proceedings, a "trial" of disputed issues of fact and law is conducted during which evidence is presented to and evaluated by the fact-finder/arbitrator. Therefore, the same need for expert witnesses that exists in the Courtroom also exists in the arbitration room. In the same way that CPAs can provide expert analysis, financial modelling, evaluations, and testimony in litigation, they can provide these same services in arbitration.

Since mediation is not a process of submission of evidence for evaluation by a third-party fact-finder, there is no role for "testimony" *per se*. However, mediation is a process of presentation of positions aimed at persuading the opposing party and at having a salutary impact upon the negotiation process channelled through the mediator. Therefore, in certain cases, a CPA's summary and presentation of the financial or quantitative aspects of a party's position may greatly facilitate the purposes of this non-binding ADR process.

D. Consultant to Mediator

The mediator's skills may be in the realms of the law, negotiation techniques, or human interaction, but not in the realms of finance and accounting. In certain cases where the issues are complex or technical, it may make sense for the mediator to be assisted by a CPA-consultant. In such a case, the CPA's client is the mediator, and the CPA's relationship to the dispute would be as an arm of the mediator; however, the CPA's fees may be passed through to and shared between the parties (like the mediator's fees), if the parties so agree.

E. Mediator

There is nothing about the concept of mediation, or the requirements for mediators set forth in the Texas ADR Act, which necessitates a law license. Indeed, practicing as a mediator is not practicing law, and many qualified mediators are not attorneys. While many disputes otherwise destined for litigation, or which are referred out of the litigation process, should probably be mediated

by lawyers who are familiar with the legal implications of a party's position, this is not invariably the case. CPAs who train and obtain certification can serve as mediators in any case where their experience and expertise is appropriate to address all ramifications of the process and the resolution of the dispute by settlement.

F. Co-Mediator

An interesting hybrid accommodation of the two previously mentioned roles is the concept of co-mediation. Section 154.051(c) of the Texas ADR Act provides that the Court may appoint more than one mediator; indeed the parties in a voluntary mediation always have the option to call upon a team of two or more mediators. A very effective team of joint mediators in certain types of business disputes might be one consisting of both a lawyer and a CPA working together, both in the role of mediator. Not only could the lawyer and CPA consult with one another to cover a broader range of expertise, but the process might also be more focused and efficient where disputed issues have both legal and accounting (or tax) implications.

G. Arbitrator

Likewise, arbitrators need not be attorneys. In many disputes, a CPA-arbitrator, either as a member of a panel or as an individual arbitrator, might be in the best position to effectively render a binding decision for the parties.

VI. Options for CPAs

A. Client vs. Third-Party: Litigate, Arbitrate, or Mediate?

When your clients make you aware of disputed transactions in which the prospect of a lawsuit is "brewing," you can help to make them aware of the pros and cons of proceeding with litigation or invoking some form of ADR.

B. Administrative Agency Issues: Litigate, Arbitrate, or Mediate?

Increasingly, administrative agencies such as the IRS, the EEOC, the EPA, and the SEC are using ADR processes in areas where litigation has been the traditional remedy. When mediation is attempted as an early step, the traditional administrative and litigation remedies are still available in the event the mediation fails.

C. Fee Disputes: Litigate, Arbitrate, or Mediate?

Many CPAs are unwilling to sue clients for fees, particularly when the fees to be recovered are less than $10,000, because of the costs associated with suing, the distraction in time lost from other productive professional work, and the risk of a malpractice counterclaim. However, use of ADR to resolve fee disputes ameliorates the cost, the time investment, and the malpractice risk, as well as keeping the dispute private. In many such cases CPAs would do themselves a favor to initiate a request for submission to mediation. This is even more feasible where an agreement to mediate and/or arbitrate has been incorporated into the initial engagement letter. Keep in mind that in

consumer transactions, the Texas General Arbitration Act does not favor arbitration where the consideration involved is less than $50,000. However, the same limitation does not apply to mediation. CAVEAT: Your professional liability carrier (if any)must be consulted and involved in any decision to include ADR clauses in engagement letters, or to channel covered disputes through an ADR process. Do not jeopardize your coverage by failing to clear the issue with your insurer!

D. Professional Liability Issues: Litigate, Arbitrate, or Mediate?

By the same token, when the specter of a professional liability claim is raised by a client, many CPAs will merely put their head in the sand and wait in fear until the client hires a lawyer and files a malpractice suit. A more pro-active approach which may make sense in many cases is to submit such a dispute to ADR. Consider a client's threats as a signal that ADR may need to be suggested; or better yet, incorporate the agreement to mediate and/or arbitrate into the initial engagement letter. Remember that in transactions with individuals, the Texas General Arbitration Act does not favor arbitration where the consideration involved is less than $50,000. However, the same limitation does not apply to mediation. CAVEAT: Your professional liability carrier (if any) must be consulted and involved in any decision to include ADR clauses in engagement letters, or to channel covered disputes through an ADR process. Do not jeopardize your coverage by failing to clear the issue with your insurer!

VII. Conclusion: A Case Study

Consider a case where Tom Fall of the CPA firm of Fall, Winter & Summer, P.C., has done $10,000 worth of tax and consulting work for Joe Client, but has not been paid. Apparently Joe, a sharp businessman, is not paying the bill submitted by the firm because he does not believe that Tom gave him sound professional advice concerning the tax treatment of certain investments, which investments coincidentally also have performed poorly. When Tom pressed Joe to pay the delinquent receivable, Joe responded with the threat of a malpractice suit. Unfortunately, there was no agreement to mediate in the engagement letter signed by the client. No lawsuit has yet been filed.

1. Coordination with Insurer (if any)

2. Request for Submission to Mediation

3. Contact of Client by Mediation Service

4. Agreement to Mediate

5. Mediator's Opening of the Mediation

6. Presentation of CPA's Position

7. Presentation of Client's Position

8. Controlled Dialogue and Exchange of Information

9. Separate Caucusing with the Parties

10. Generating Options for Potential Solutions and/or Compromises

11. Shuttle Diplomacy and Negotiations

12. Settlement Agreement

13. Documentation and Finality

In spite of the flaws in the judicial system, ADR is not a panacea. Some disputes will need to be litigated. This brief outline is not intended to be exhaustively comprehensive of a complex and constantly evolving subject. However, at least now you hopefully have a fundamental framework of understanding as to the dispute resolution options to be considered and the roles that the CPA might undertake.

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REQUEST FOR SUBMISSION TO MEDIATION

Mediation is a private, non-binding forum in which an impartial person, the Mediator, facilitates communication between parties to promote reconciliation, settlement, or understanding among them.

****

To Be Completed By Initiating Party:

Initiating Party _____
Party Representative/Employee _____
Address _____
Telephone No. _____ FAX No. _____
Attorney, If Any _____
Address _____
Telephone No. _____ FAX No. _____

Nature of Dispute from Initiating Party's Viewpoint: _____
_____
_____

Please provide five proposed dates for the mediation procedure: _____
_____

Responding Party _____
Party Representative/Employee _____
Address _____
Telephone No. _____ FAX No. _____
Attorney, If Any _____
Address _____
Telephone No. _____ FAX No. _____

Initiating Party should fax or mail this Request to:
Wells & Cuellar
Mediation and Commercial Arbitration Services
440 Louisiana, Suite 718
Houston, Texas 77002
(713) 222-1281
FAX (713) 237-0570

Our 2005 fee for services initiated by this form is $700 for a session lasting up to 4 hours, $1,400 for a session lasting between 4 and 8 hours, and $175/hr. for additional time. Such fees are to be split equally between the parties, unless otherwise agreed.

****

To Be Completed By Responding Party:

Is any of the above information concerning Responding Party incorrect or incomplete? _____
If so, please indicate the changes needed here or above: _____
_____

Nature of Dispute from Responding Party's Viewpoint: _____
_____
_____

Does Responding Party agree to submit the dispute to mediation? _____
If so, please provide five proposed dates for the procedure or select two proposed above: _____
_____

Responding Party should fax or mail this form back to:
Wells & Cuellar

Useful ADR Websites

- www.wellscuellar.com

  (News and Case Summary,
  Dispute Resolution & Arbitration)

- www.adr.org

  (American Arbitration Association, Rules/Procedures,
  Dispute Resolution Rules for Professional Accounting
  and Related Services Disputes)

- www.arbitration-forum.com

  (National Arbitration Forum)

- www.txmca.org

  (Texas Mediator Credentialing Association)

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Speaker and Seminar Trainer

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  Brent is an experienced commercial litigator, mediator, and arbitrator.

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  Brent is board certified in Consumer and Commercial Law by the Texas Board of Legal Specialization.

- **CREDITORS' RIGHTS AND DEBT COLLECTION**
  Brent is certified in Creditors' Rights Law by the American Board of Certification.

- **AND MORE**
  Brent has spoken on topics as diverse as Covenants Not To Compete, Expert Witness Techniques, and the Uniform Commercial Code. Let him design a program tailored to the needs of your particular company, civic organization, or professional group.

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