MEDIATION OF INSURANCE MATTERS

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I. The Vanishing Trial and The Emergence of ADR

In December 2003, the American Bar Association noted that the percentage of filed civil cases going to trial had fallen from 11% in 1962 to 1.8% in 2002. In state court, the number of jury trials has declined by more than 25%, with less than 1% of such cases filed actually being tried over a 25 year period. With these figures in mind, it is important to understand that many of these litigated cases, including claims against insurers and their insureds are being settled through various forms of alternative dispute resolution ("ADR"), such as negotiation, mediation and arbitration. While reducing our reliance on trials to resolve civil disputes, ADR has served to address a broad category of disputes in the insurance context. This broad category of disputes includes both third-party claims against insureds and inter-insurer disputes as well. The reason that private litigants are turning to ADR is straight forward: the process saves time and money, and results in forms of settlement not otherwise available in litigation.

II. Description of ADR Techniques

ADR is a term that covers a range of methods which are designed to resolve disputes short of trial. Of course, ADR does not replace the trial system. Some cases will always need to be tried to a jury or before a court. ADR supplements and complements the court system by making other processes available to resolve disputes in a cost effective and time efficient manner and without the "I win you lose" outcome of litigation.

As has been mentioned, a number of methods of ADR are available. The first and most familiar is negotiation. However, negotiation is actually only the first step in attempting to resolve a dispute. The process of negotiation encompasses all of the efforts by the parties to settle their differences without the intervention of a neutral third-party. The negotiation process is voluntary and nonbinding.

Arbitration is more like litigation; it involves a decision by a neutral party by which the disputants have agreed to be bound. It can be elaborated that often, it will involve some form of discovery and testimony by witnesses at the arbitration hearing itself.

Mediation lies between negotiation and arbitration. It involves an impartial and neutral third-party in the process. The mediator will assist the parties in attempting to reach a voluntary agreement to the dispute. The mediator is not a Judge; therefore, he or she will not find for one side or the other. What the mediator does is listen to both sides and try to find common ground. The mediator does not assess blame or dictate a settlement; he or she has no authority to render binding decisions. The parties retain control over the process and make their own decisions about what type of settlement will be reached, if any.

In "facilitative" mediation, the mediator usually deals with the parties or their attorneys, jointly or in separate "caucuses." In facilitative mediation, the mediator generally does not express an opinion on the merits of the case or its settlement value. Rather he or she helps the parties define the issues, overcome barriers to communication, and explore alternative methods of resolving their

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dispute. In "evaluative" mediation, the mediator has a somewhat different charge in that he or she may recommend a specific settlement or a particular resolution of the dispute.

The advantages of mediation generally are said to be as follows: (i) mediation is relatively inexpensive as compared to litigating a case to its conclusion; (ii) generally speaking, the mediation proceeding is confidential in nature; (iii) mediation reduces the emotional barriers to communication and helps parties focus on their interests; (iv) the parties control the process and decide the outcome as opposed to having the decision rendered for them either by a Court or other trier of fact; and (v) as a result, mediation is more likely than litigation to result in a solution satisfactory to both parties.

The disadvantages of mediation are sometimes considered to be as follows: (i) in the absence of Court direction, the attendance and participation of parties cannot be compelled; thus the parties must agree to participate; (ii) the results are not binding and must be effectuated in a written settlement agreement; and, (iii) whether mediation is successful may depend on the skill of the mediator.

Mediation should be considered in almost any situation where negotiations have reached a stalemate. To be effective, it is only necessary that the parties have sufficient information on which to base their discussions, and that they have a good faith desire, incentive and authority to resolve the dispute.

A mediator is sometimes able to break an impasse by proposing settlement options. Disputing parties may be more receptive to a neutral's proposals than to proposals from the other party. Each can explore the neutral's proposal without compromising a position previously taken.

Mediation also is helpful when there is a likelihood that the parties will continue to deal with each other in the future. This can include disputes between employees and employers, landlord and tenant, customers and suppliers, neighborhood disputes and issues between insurers and insureds. In these type of cases, the parties have an incentive to address their underlying problems and come to mutual decisions. This is more constructive to an ongoing relationship than the hostility that may result from litigation.

III. Statutory Support of ADR

A. Federal Support of ADR

The Federal Government's support for ADR in civil disputes is expressed both in statutes and administrative guidelines. For example, the Administrative Dispute Resolution Act of 1996 (the "ADRA") gives federal agencies authority to use ADR in a number of types of disputes, and exempts mediation from disclosure under the Freedom of Information Act. Under the ADRA, federal agencies must adopt a policy for implementation of ADR. See 5 U.S.C. §574(a), (b).

A later Alternative Dispute Resolution Act, that of 1998, requires each federal district court to develop ADR procedures for use in civil actions. While this Act encourages use of all forms of ADR, it does not mandate a uniform set of procedures. Instead, district courts are free to fashion their own programs. See 28 U.S.C. §651. Here in New York, both the Eastern and Southern Districts have established ADR Programs. Recently, the Western District has implemented a pilot program which will operate from January 1, 2006 to December 31, 2006.

Presidential Executive Order 12998 requires government litigation counsel to be trained in ADR techniques and encourages them to be utilized in civil disputes to which any federal agency is a party. 61 Fed. Reg. 4729 §1(c)(2).

The Department of Justice has also implemented policies for using ADR. The methods include arbitration, mediation, early neutral evaluation, neutral expert evaluation, mini-trials and summary jury trials. See 61 Fed. Reg. 36896. The Internal Revenue Service Restructuring and Reform Act of 1998 (26 USC §7123) directs the IRS to make both arbitration and mediation more widely available. The procedures include fast track mediation to help taxpayers resolve disputes involving audits, trust fund recovery penalties and other collection actions. See IRS Pub. 3605 (Rev. 12-2001.

B. New York State Support of ADR

At the State level here in New York, there are a number of court-annexed mediation programs, including rules applicable to those programs. Only a few will be discussed here. First, the Commercial Division for Supreme Court, New York County has authorized Justices to direct parties to participate in ADR. Under the Rules, the Justices direct ADR (which usually takes the form of mediation) at the earliest practical moment. Generally speaking, the Order of Reference will stay all proceedings, including discovery and motions, for a period of 45 days from the date the identity of the Neutral is confirmed. The confirmation date usually commences a 30 day time period in which the mandatory mediation is conducted. Further mediation sessions can be conducted after the initial session, so long as it is within the 45 day period. These mediation sessions must be attended by the party in person or, in the case of a corporation, by a representative who is both in possession of all pertinent facts and authorized to settle without consultation. This may involve more than one person. The Rules provide for complete confidentiality. The mediators serve on a pro bono panel.

Second, the Commercial Division for the Supreme Court, Westchester County has recently instituted a Pilot ADR Program. Under the Rules, it is the policy of the Court to encourage the resolution of disputes and the early settlement of claims. Like the Program in New York County, the first session must be conducted within 30 days of the confirmation date, and proceedings are stayed for a period of 45 days. The Rules also provide for complete confidentiality. Any person designated to serve as a Neutral shall be immune from suit. The Neutrals in the ADR Program receive fees. Court-annexed ADR Programs throughout the State can be researched at www.nycourts.gov.

As discussed below, on December 29, 2005, the Commercial Division Rules in New York were amended to provide that certain actions in Westchester County with a monetary threshold of over $100,000 will be heard in the Commercial Division. Among others, these will include actions involving breach of contract arising out of business dealings, employment agreements not including claims involving principally alleged discriminatory practices, environmental insurance coverage, commercial insurance, U.C.C. cases and transactions with commercial banks and other financial institutions. The Commercial Division Rules became effective on January 17, 2006. Hence, these types of suits involving municipalities should be subject to the Commercial Division's Pilot ADR Program.

Third, some Appellate Court Programs in New York have also been instituted. The First Department utilizes a "Pre-Argument Conference Program." In my own experience, I have participated as counsel in a mediation where a First Department's Special Master reached out to invite non-parties to the appeal. The Second Department has instituted a Civil Action Management Program.

Fourth, the New York State Legislature has passed legislation to enable the creation of Community Dispute Resolution Centers ("CDRCs") to resolve neighborhood and interpersonal disputes. The goal is to offer a "quick, inexpensive and voluntary resolution of disagreements, while at the same time serving the overall public interest by permitting the criminal justice community to concentrate its resources on more serious criminal matters." McKinney's Session Laws of New York at 2630. In Westchester, the CDRC is Westchester Mediation Center ("WMC"). WMC is principally involved with local neighborhood disputes. It has established mediation programs in a number of Westchester Town and City Courts. Each County in the State has established their own Community Dispute Resolution Center.

Finally, although not applicable to insurance mediation, the recently issued Matrimonial Commission Report to Chief Judge Kaye recommended a number of sweeping changes to the disposition of matrimonial cases in New York. The Report concludes that ADR, particularly mediation, should be expanded in matrimonial cases, particularly those involving children.

C. Insurance Industry Support of ADR

In 1995, the AIDA Reinsurance and Insurance Arbitration Society, ARIAS U.S., a not-for-profit corporation, was formed for the purpose of promoting the improvement of the insurance and reinsurance arbitral process. In that regard, the Society has conducted training and contractor programs and has developed model arbitration clauses and guidelines for arbitration. More recently, ARIAS has begun to offer a roster of mediators, well-versed in insurance and reinsurance matters. Access to this information can be obtained at www.arias-us.org.

The Institute for Conflict Prevention and Resolution ("CPR") was founded in 1979. CPR is dedicated to the identification and application of appropriate alternative solutions to disputes. CPR has been a proponent of insurance related mediation for over twenty years. It maintains an active Insurance Committee and established a Corporate Insurance Coverage Committee in 2005. In June 2006, a group of CPR members issued the Reinsurance Industry Dispute Resolution Protocol which calls for alternative dispute resolution in the area of reinsurance. CPR maintains a list of neutrals. Information can be accessed at cpradr.org.

IV. Types of Insurance Disputes In Which To Use ADR

A principal form of ADR used by insurance companies is mediation. Of course, many insurance and reinsurance disputes are arbitrated; however, we will focus on mediation in this section. As previously mentioned, mediation is helpful in disputes involving ongoing relationships which are often the case with insurers and insureds. Since mediation encourages the parties to work together, it is conducive to maintaining relationships rather than destroying them. Accordingly, any coverage dispute between an insured and insurer should be considered as a candidate for mediation.

As for third-party actions, employment cases, including discrimination and sexual harassment cases, are particularly suited for mediation. Cases where the parties need to vent their emotions are suitable as these emotions can be defused in the conciliatory atmosphere of mediation. Creative solutions may also be devised in employment cases that are not available in litigation, such as rehiring, reassignment, or rescission of termination, so that a new job may be easier to procure. Alternatively, the claimant may be willing to settle for a letter of reference, or a public apology by the alleged harasser – something no jury will ever award.

Suits involving breach of contract for good or services, suppliers, vendors, environmental and commercial insurance and dealings with financial institutions are suitable for mediation. These suits would also be subject to Westchester Supreme Court's Commercial ADR Program.

Mediation is also a good way to bring nonmonetary solutions to the settlement table in certain categories of cases. This could involve defamation cases where an apology or retraction from the opposing party often will facilitate settlement. Other claims common to public and commercial institutions include section 1983 claims, claims of false arrest, personal injury claims and other business disputes.

Mediation has been widely used in labor relations for years. Mediation of labor grievances, workplace disputes and wrongful termination claims is now widely practiced. Finally, mediation can be useful in resolving disputes with multiple parties and issues, such as environmental, land use and community disputes. Creative and flexible ways to address these interests can be explored, looking forward in a constructive manner.

V. Confidentiality of Mediation Communications

As a general proposition, Section 849-a(6) of the New York Judiciary Laws, which established CDRCs, provides, in pertinent part, as follows:

> Except as otherwise expressly provided in this article, all memoranda, work products, or case files of a mediator are confidential and not subject to disclosure in any judicial or administrative proceeding. Any communication relating to the subject matter of the resolution made during the resolution process by any participant, mediator, or any other person present at the dispute resolution shall be a confidential communication.

In the context of the CDRC Program, the statutory confidentiality provisions of Judiciary Law section 849-a (6) cannot be waived by the parties. The leading case in this area is People v. Snyder, 129 Misc.2d 1137, 492 N.Y.S. 2d 890 (Sup. Ct. Erie Cy. 1985). There, the District Attorney subpoenaed all records pertaining to a mediation in which a defendant in a criminal trial had participated. The Court found that the grant of the subpoena would subvert the Legislature's clear intention to guarantee the confidentiality of CRDC records . The Court noted that the statute as drafted did not permit waiver of confidentiality.

While section 849-b(6) applies only to CDRCs, the rule of confidentiality has been expanded into other areas and situations. For example, in Bauerle v. Baulere, 616 N.Y.S.2d 275 (4th Dep't 1994), the Appellate Division held that the a lawyer who undertakes to act as mediator may not thereafter act as counsel for one of the parties to the dispute even though the mediation was not pursued after the initial meeting. The Court held that "disclosures that are relevant to the subject of mediation or litigation made in the context of mediation are deemed confidential even though the adversary party is present."

Similarly, in Bernard v. Galen Group, Inc., 901 F.Supp. 778 (S.D.N.Y. 1995), the Court awarded sanctions against counsel for disclosing the dollar amounts of settlement offers made at a Court-ordered mediation. The mediation occurred in a copyright case referred to mediation under the the Southern District's ADR Program.

No statutory privilege exists to protect confidentiality in mediation within the jurisdiction of New York State. Interestingly, however, the Matrimonial Commission Report also recommended a Court Rule or statutory amendment to provide for confidentiality in mediation in all cases, except for abuse cases. Furthermore, it should be noted that mediators will generally require the parties to execute a mediation agreement, which will usually require confidentiality.

VI. Helpful Tips For Mediating The Litigated Case

As attorneys, we are all aware of what factors contribute to a good result at trial, or what makes one a good or great trial attorney. But the same understanding must now be gained as to mediation, particularly in view of its continued growth. When should an insurer seek mediation? What can insurers do to achieve the best result possible? What makes for a better mediation? What role should the underwriter play in the mediation process? With these questions in mind, set forth below are some tips for participating in a successful mediation.

A. Mediate Early

Often, mediation does not take place until after costly and time-consuming discovery in a civil action. If mediation does not take place early, it may be a lost opportunity. Insurers should consider pre-action mediation. In this regard, consideration should be given to an early and detailed exchange of views on any dispute and an early, overall resolution to avoid litigation costs. Where agreeable, exchange mediation briefs that detail liability and damages. Information sharing and information gathering is key to the identification of common ground.

One question that comes to mind in this context is the nature of the lawyer's obligation to discuss or suggest mediation to the client. A number of jurisdictions require a lawyer to discuss ADR with the client. For example, in Texas "counsel shall discuss the appropriateness of ADR in the litigation with their clients and with opposing counsel." S.D. Tex. L.R. 20(A)(1). California requires that counsel "shall advise" clients regarding the availability of ADR options. See Sacramento Super. & Municipal Ct. L.R. App. A.

Insofar as New York is concerned, as mentioned above, on December 29, 2005 the Commercial Division Rules were amended to provide that counsel "shall consult" about the use of ADR prior the preliminary or compliance conference. These Rules went into effect on January 17, 2006. In a commercial action all parties "shall be obligated to attempt in good faith to achieve early resolution of their dispute by use of appropriate forms of non-binding Alternative Dispute Resolution."

B. Mediator Selection

It is always important to ask for the mediator's qualifications, experience and training. While one party may prefer the appointment of a retired Judge, it may be useful to consider use of other ADR professionals. It is true that in order to settle a claim, one party may only need to hear the settlement value of a claim as estimated by a retired Judge. However, in some cases it may be appropriate to consider a mediator with subject matter expertise. A mediator with knowledge of a particular subject matter and training in the process may be helpful in assisting the parties to achieve a resolution.

C. Prepare for Mediation as Though it is Trial

It is just as important to prepare for mediation as it is to prepare for trial. Careful review of the facts is key. No stone should be left unturned. The insurer should know jury verdicts in similar cases, court decisions and other objective criteria by which to evaluate damages and settlement possibilities. It is equally important to prepare the claims handler or underwriters for the mediation. Counsel should consider what may be the best and worst case alternatives to a negotiated settlement so that a reasonable settlement can be determined.

The client should be advised that the process of mediation is not fact-finding, but a mechanism to assist the parties in finding a joint solution. The mediator is not a Judge, he or she will not find in favor of one side or the other. It is also important to set aside sufficient time for the mediation. In the case of a complex matter, this means at least one day. This will allow the mediator and the parties to focus their entire attention on resolution of the dispute.

D. Presentation at Mediation

The presenting party, usually counsel, must have total command of the facts and law. Counsel should be prepared to educate the other side and must display a complete, crystal clear understanding of the applicable legal principles. This will enhance credibility with the mediator as well as the opposing side. No exaggerations of fact or overstatements should be made, lest credibility be lost during the negotiation process. Do not hesitate to use experts to assist the mediator in understanding the technical issues in a case. These experts can include accountants or other damages experts, who should clearly set forth in detail the position on damages. In certain cases, counsel should consider bringing the client to the mediation. This could be the claims handler or underwriter. The client may be helpful in explaining the position to the mediator. Finally, confidentiality should be reviewed throughout the mediation in terms of what information disclosed to the mediator can be revealed to the other side.

It is useful for a representative of the insurance carrier of the insured to attend the mediation. In some jurisdictions other than New York, such attendance may be required. In instances where an insurance representative does not attend, counsel should be provided with the requisite authority, and the representative should be available by telephone. Where insurance coverage issues are involved, the mediation may be of a nature where those coverage issues as well as the principle settlement are negotiated. The mediation will proceed more smoothly if those coverage issues are discussed and addressed in advance. An open dialogue with the insurance carrier should always be pursued because its funds are often involved in false arrest, malicious prosecution, wrongful termination and other garden-variety personal injury claims against municipalities.

E. Finalization of Mediated Settlement

The success of a mediation is measured by whether the parties have reached common ground and effectuated their settlement. Where a settlement is reached, it is incumbent that it be properly documented immediately. Therefore, it is good practice to prepare a Memorandum of Understanding at the conclusion of a successful mediation, which should be executed by the authorized parties. This means having those parties either present at the mediation or available by facsimile. Only then

can one be sure that the effort undertaken to settle will be fully binding, not subject to second-guessing or reevaluation.

CONCLUSION

Insurers should avail themselves of opportunities to resolve disputes in both duty to defend claims and in inter-insurer coverage disputes. In particular, mediation of the litigated case is an effective, cost-saving measure and should be considered in all cases. Where appropriate, insurers should give consideration to mediating the inter-insurer coverage disputes as well.

The Legislature can do more to enhance the development of ADR in general and mediation in particular. The Legislature should consider amending the CPLR to provide for confidentiality in mediation of all litigated cases, not just CDRC cases, in a manner consistent with case law. This will provide further incentive for parties to mediate. The Legislature could also require attorneys to discuss ADR options with their clients or, at the very least, with opposing counsel before a preliminary Court conference. Finally, the practicing bar should be leaders in fostering cooperation and establishing mechanisms to allow mediation to flourish in New York.