Einstein's lessons in mediation

When two companies could not agree a price for a trade mark sale, they decided to hold an arbitration followed by a mediation. Those involved explain how this unusual process worked

Einstein once explained his greatest theory in terms all of us can understand: "When you are out with a nice girl, an hour seems like a second; when you are standing on a red-hot coal, a second seems like an hour – that's relativity". Many relativities are connected to opposites. Too often we reject things that are opposite to traditional beliefs and practices as being unsuitable, contradictory, oxymorons, and un-doable. It is human nature to hate oxymorons. Their relativities are out of balance.

Anecdotal evidence is an oxymoron. So is truthful propaganda. Groucho Marx claimed that military intelligence is also one, though Napoleon would have disagreed; we even buy oxymorons – have you ever seen a label that says "pure 100% orange juice from concentrate"? Einstein himself famously claimed that it was not possible simultaneously to prevent, and to prepare for, war, only to be proved wrong by the advent of nuclear weapons. Life is full of oxymorons. But strip away the superficial reaction and maybe they are not so self-contradictory in reality. So let's pose another oxymoron: can you have an arbitration-mediation, an Arb-Med? Not a printing error, this – an arbitration followed by a mediation.

People who train as facilitative mediators learn that arbitrators are judges – they make decisions on behalf of argumentative parties who then have to live with the result imposed upon them. Mediators, however, never get judgmental, they merely aid the parties, and any decisions are taken by the parties, not by the mediator. Based on those archetypal characterizations, it appears contradictory for an arbitrator to act as a mediator, and many would claim that it is an oxymoron for a mediator to arbitrate.

Therefore, they don't do it. Neutrals get asked to act as one, or as the other, but not as both! How can you trust a neutral person with your deepest secrets, your real bottom line, your hidden agendas, if that person can impose a decision? It makes no sense.

Another of Einstein's remarks was "If at first an idea is not absurd, there is no hope for it". So, let's not be so hasty and dismissive of the idea of a single neutral being both an arbitrator and a mediator on the same day with the same parties.

Mediators are taught to hypothesize, to search for options for mutual gain. They often ask questions beginning "What if..." as a means to provoke the listener into thinking outside the box.

Einstein would urge us to ask: "What if the neutral was asked to wear two hats, to be an arbitrator and a mediator, but not at the same time? First to be an arbitrator, make a decision, seal the decision in an envelope without telling the result to the parties, and then become a mediator? What if the parties agreed in advance that they would open the envelope, and be bound by its contents, only if the mediation were to fail to result in an agreed outcome?"

A real scenario

PMEC is a small, independent, successful business selling upmarket casual clothing and accessories for men originally themed on 1950s aviator gear – the kind of wardrobe you would expect to catch the eye of the new breed of Hollywood actors.

BAT is a tobacco company that for decades had owned a series of clothing trade marks that were licensed to PMEC. BAT had no interest in continuing to own the trade marks, and was happy to sell them to PMEC, who preferred to own its own brand names rather than operate under a licence agreement. It was a common situation – a willing buyer, a willing seller, and a simple deal.

Negotiations went well until the discussion, inevitably, turned to value. PMEC had one idea about what it was willing to spend to buy the brand rights, and BAT had another idea about what it was willing to accept in order to sell those brand rights. The two figures were dramatically different. So it was agreed that each would instruct an independent professional firm expert in valuing brands to arrive at a fair price. It was also agreed that the parties would then exchange their valuation reports and meet again to finalize the value.

The parties did not have a dispute about anything. Nor was either even contemplating a conflict with the other. Both just wanted to do a deal but could not agree on the key issue – money.

When the valuation reports arrived, and were exchanged, it emerged that the expectations of each party were very different. Two prominent professional firms had arrived at very different valuation results based on the same facts.

Bob Bulder, MD of PMEC:

"I run my own business and own a high percentage of the shares. We are in the fashion business – it is cyclical, decisions have to be made many months ahead, it is risky, we have to be highly entrepreneurial and for me control is everything. Although we have never had a problem with BAT owning many of the brand names we use on our clothing lines, nevertheless we have always been uncomfortable not actually owning them ourselves. It's rather like the difference between owning the freehold of your home and owning the leasehold. I would rather own the freehold.

For me, buying these trade marks was about the cost of feeling comfortable. BAT was not threatening to take the

rights away, or anything like that, and although I was prepared to pay something for the rights, I had my limits. I also had options. I could have re-branded over time. Or I could have merged with another company and used their brand rights. Or I could have put up with the discomfort and continued to license the rights from BAT. We don't have a lot of capital, and are nowhere near as cash-rich as BAT. Because I had options, I had worked out the upsides and downsides of each one. I knew exactly how much I could spend to buy these trade marks, but obviously, if I could get them for less then I would."

Michael Leathes, Head of IP at BAT:

"My company had gradually sold off its non-core rights and focused on what it knows best: being a tobacco business. Owning and maintaining these clothing brands was a throw-back to the past. We wanted to divest them, but not to give them away. There was really only one buyer – PMEC. They had built a business using these brands and it would have been irresponsible of a company like BAT to threaten to sell the brand rights to a third party just to intimidate PMEC into paying more. So I didn't do it.

On the other hand, the trade marks in question were certainly not worthless, and the company's shareholders had the right to expect that I would sell them for a fair value. I had an independent valuation in my hands, and I had shared it with Bob, but it was far above the valuation he had in his hands."

At a lunch to try and bridge the gap, the two parties discussed the valuation reports each had commissioned. PMEC viewed the BAT valuation report as completely unacceptable and, worse, unaffordable. BAT viewed the PMEC valuation report as equally unacceptable, almost as a give-away. They discussed a principle – was BAT willing to accept a price below its valuation, and was PMEC willing and able to pay a price above that indicated in its valuation? With affirmative responses on both sides, the next question was: is it possible to agree high and low parameters – a range within which the agreed valuation would fall? Further discussion resulted in BAT conceding that, despite its independent valuation, it would accept a price of no more than €x and PMEC conceded that despite its independent valuation, it was willing to pay at least €y. Although this was progress – the parties now had a narrower range within which to find the right number – there was still a large, apparently unbridgeable, gap.

The options

The most obvious way forward was to arbitrate the valuation issue and both parties would then live by that result. However, both rejected the idea. BAT feared that it would lead to an unacceptably low result and PMEC feared that it would lead to an impossibly high outcome.

Baseball (or final offer) arbitration was an alternative, and it was considered. A neutral person would be invited to read each side's valuations, hear the parties' representations, and then each party would make an offer at which to close the deal. The neutral could then decide which offer was more reasonable, and that would be the offer that closes the deal. The neutral would have no power to suggest or determine any other solution. This was how the salaries of Major League Baseball players were settled. It might have worked here because the technique automatically encourages each party to put forward its best offer to encourage that offer to be the one chosen by the neutral. So the process automatically encourages gap-closing.

A variation on the theme was night baseball, so called because it operates like baseball arbitration with the difference that the parties do not disclose their offers to the neutral but seal them in envelopes; the neutral then makes a decision which is disclosed to the parties, the envelopes are opened, and whichever party's offer is closest to the neutral's decision is the one that prevails.

Mediation was also considered. However, the risk remained that maybe no deal would have emerged, and one party felt this could have wasted time and cost.

The way forward that was eventually chosen was a blend of arbitration and mediation – an Arb-Med. The parties agreed that they would ask a neutral person to wear two hats, but not simultaneously. The process chosen was simple – the neutral would spend a morning acting as an arbitrator, and would arrive at a fair and appropriate valuation over lunch but would not disclose that amount to the parties. Instead, the neutral would place the decision in an envelope, place the envelope on the meeting room table, then become a mediator. If, by the end of the afternoon, the parties, with the neutral mediator's help, could not arrive at an agreed outcome, the envelope would be opened and the parties would accept the valuation figure that it contained.

This would not have worked the other way around – as Med-Arb – where the neutral begins as a mediator, then, if the parties fail to agree an outcome, becomes an arbitrator and renders a decision that binds the parties. Neither of the parties would have revealed their own private circumstances to a mediator who later might metamorphose into an arbitrator with the power to *impose* a decision on the parties.

The merit in the Arb-Med process over the other options was that an outcome was always guaranteed at the end of the day, but the parties had ample opportunity to control that outcome themselves by arriving at an amicable arrangement.

Selecting a neutral

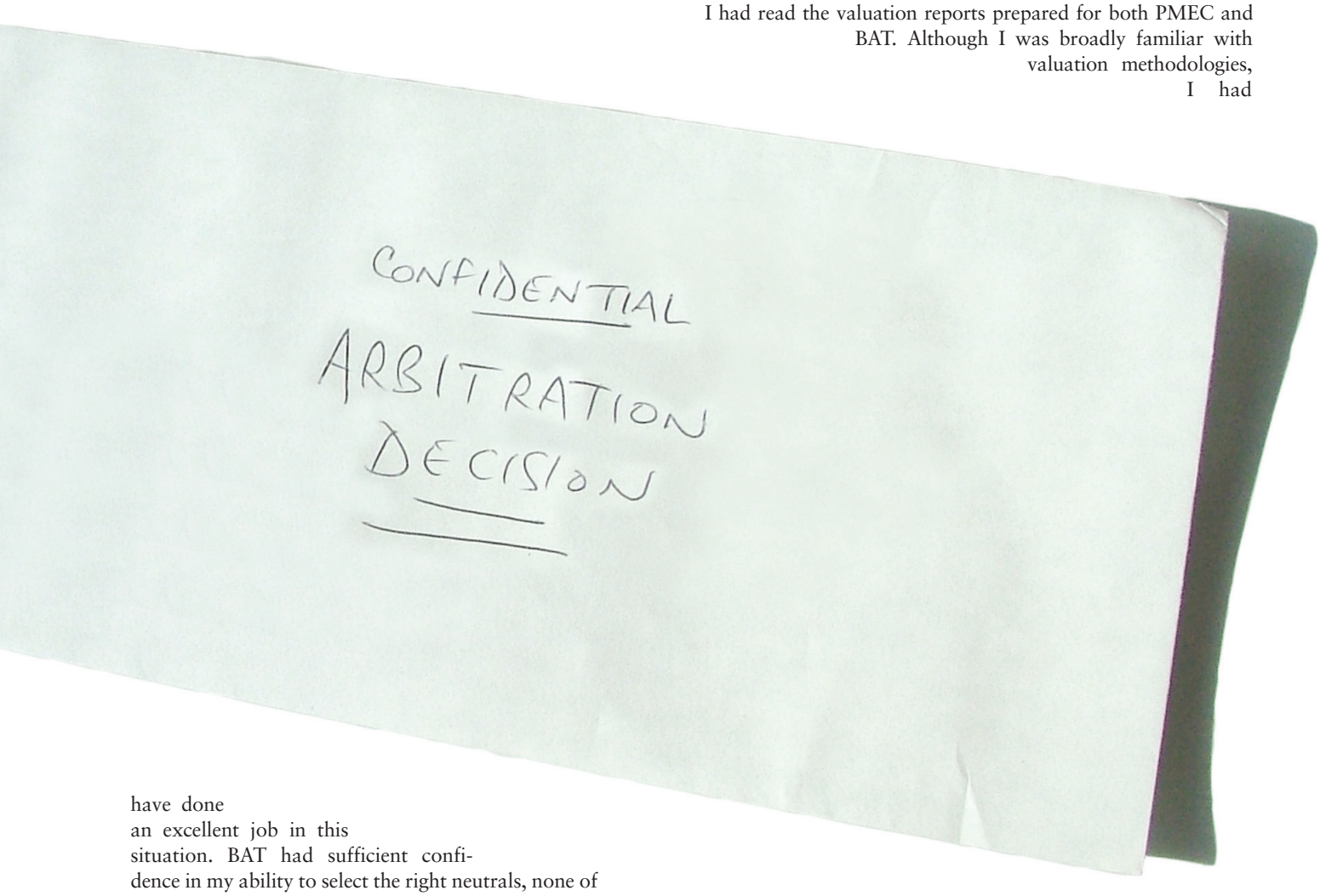
Having agreed on the process for determining the valuation of the intellectual property assets, the next vital ingredient was to identify the neutral. It had to be someone able to act as both an arbitrator on valuations, and also as a mediator. It had to be someone in The Netherlands as the Arb-Med would take place in Amsterdam. The parties agreed to ask ACBMediation, a member of the MEDAL alliance (comprising leading mediation bodies in five countries), to propose three suitable neutrals. Both parties trusted ACBMediation to narrow down the choice to neutrals with the right skills and quality. On receipt of a list of three people proposed by ACB, BAT invited PMEC to choose whichever one it liked and that choice would be acceptable to BAT.

Manon Schonewille, Director, ACB Mediation, Den Haag:

"Mediation bodies can play a vital role in convening the parties in a common frame of mind – even if they disagree on matters of substance. After consulting with PMEC and BAT regarding the process to be followed and

the profile of the mediator, I considered who among my excellent panel of neutrals was specifically suitable to guide this Arb-Med situation. They wanted a neutral with skills as an arbitrator and as a mediator who was flexible enough to play both roles in one day perfectly. The requested profile was for a business-wise, hands-on mediator. I have a number of professionals on my panel who have such skills. And they needed a neutral who could quickly get to grips with the esoteric area of intellectual property valuation principles as it relates to the fashion industry.

I put forward three members of my panel. All could have done an excellent job in this situation. BAT had sufficient confidence in my ability to select the right neutrals, none of whom they knew personally by the way, that they were able to let PMEC choose among the three resumés I sent to the parties.



This incredibly important convening role of mediation bodies is often underestimated. A provider like ACBMediation can speed up a negotiation process tremendously by helping the parties to narrow down the selection based on their own requirements, checking to ensure there are no conflicts of interest or scheduling constraints, and if necessary being there to inter-mediate if the parties need help agreeing on a choice of mediator. It can usually all be done on the phone and by email. I merely set the stage for the performance to begin."

The Arb-Med process

As in all mediations, the parties need to sign a mediation agreement which deals with such matters as the sharing of the costs, confidentiality, privileged nature of the discussions and so on. In an Arb-Med, the mediation agreement also needs an "envelope clause". This is a provision which explains that the result of the arbitration phase of the process will not be disclosed immediately to the parties but placed in a sealed envelope, to be opened, and to bind the parties, only if the mediation phase fails to produce a negotiated agreement, or, even if the mediation does result in an agreement, if the parties all agree that the envelope should be opened.

Willem Kervers, mediator:

"This was the first time I had conducted an Arb-Med. The arbitration phase went smoothly enough. Prior to the day chosen for the mediation, I had read the valuation reports prepared for both PMEC and BAT. Although I was broadly familiar with valuation methodologies, I had also asked the parties in advance if they would share the cost of allowing me access to a valuation expert, someone who had the expertise to answer my questions on valuation technicalities on an objective and impartial basis.

I was aided in this case by the fact that the parties had already agreed parameters within which any valuation for these assets would fall. But the gulf between the two was considerable, and the task before me was challenging. However, with the help of the expert, who I consulted while the parties took a lunch break (leaving me with sandwiches, which in the Netherlands are excellent!), I did arrive at a valuation based on the parties' presentations during the morning session and the facts explained to me."

After lunch the parties returned to the meeting room to see a sealed envelope sitting prominently on the table for all to see. It was a bright day, but even the rays of the afternoon sunshine

striking the table did not enable anyone to see what was inside. Curiosity pervaded the atmosphere.

Willem Kervers, mediator:

"I began the afternoon session by emphasizing that I had removed my arbitrator hat. I had done my evaluative job. The output of my arbitrator mode was in that envelope. I explained that my role had now changed radically; my goal in the afternoon was to assist the parties to arrive at a negotiated agreement to avoid opening the envelope – an act which would most likely have pleased one party but not both. I considered it vital that the parties considered me differently, even subconsciously. Because of my role in the morning session as an arbitrator, I had to ensure they grasped the distinction. It was a bit easier than I expected, because it was the parties, not ACB or myself, that had suggested an Arb-Med, but all the same, the effort had to be expended."

Had I negotiated a better deal than would have been possible if I had let someone else decide?

The mediator held several private sessions with each party, and after two hours had moved them both on to common ground. The gap was closed by exchanging terms that represented value as well as by understanding what each needed to reach a mutual agreement. Heads of agreement were signed and initialled. The deal was done.

Bob Bulder, MD of PMEC:

"At the end of this experience, after we shook hands and celebrated the conclusion of the terms on which the brand rights would be transferred to us, I was curious to know what was inside the envelope. Had I negotiated a better deal than would have been possible if I had let someone else decide? So I asked Michael whether he would agree to open the envelope. But he declined. That was fine with me – I suppose it was just my entrepreneurialism and inquisitiveness coming to the surface!"

The envelope represented the potential worst alternative to a negotiated agreement

Michael Leathes, Head of IP at BAT:

"I could understand why Bob wanted to know what the envelope contained. So did I, actually, and for similar reasons. But I declined for a further reason. We had shaken hands. Both of us were happy with the outcome. If we opened the envelope, that situation would most likely change. One of us would suddenly have become unhappy. If the number in the envelope was higher than what we had agreed, then obviously I would be unhappy. If the number was lower, Bob would have been unhappy. To come away from that negotiation with Bob unhappy would also have made me unhappy, despite being better off, because he's a friend. I explained this to Bob. He understood my rationale. It's not about turning a blind eye. Some things are just better not knowing."

And so this deal concluded satisfactorily. The parties never opened the envelope. A huge gap in perceptions of value had been bridged by the mediator finding non-monetary issues which could be thrown into the pot of consideration and which enabled both parties to get what they needed. The arbitration could not have achieved this because judicial decisions are purely one-dimensional.

Manon Schonewille, Director, ACB Mediation, Den Haag:

"In any negotiation, whether in a dispute context or as a straightforward deal, there are dynamics and undercurrents that seal the deal. In this case, the deal sealer was the power of the envelope. Here we had two parties who wanted to do a deal but had different ideas about its value. Because Willem had made a decision, the parties knew they would end the day with a result. But would it have been palatable to both? The envelope represented the potential worst alternative to a negotiated agreement. It served as a constant reminder, a permanent reality check. It influenced both parties to listen more carefully to the other, to be more inventive in seeking solutions, because opening that envelope could leave them worse off. It was psychology at work. The relativity between best and worse case scenarios, and the relative position of the unknown realistic outcome contained in the envelope all played a vital role. Einstein would have been proud of those who took part."

The last word should rest with the Arb-Mediator. Was the result in that envelope much different from what the parties ended up agreeing?

Willem Kervers, mediator:

"Maybe. Maybe not. It may be a big question, but it is also the wrong question. The right question is – did the parties do a good deal? The answer here was Yes. They were pleased. It was also a multi-faceted deal and they worked it out together. It was much better for them than whatever one-dimensional number I had written in the envelope. This deal pleased them both. Outcomes don't come better than that."

Michael Leathes is head of intellectual property, British American Tobacco, London. Bob Bulder is managing director, PMEC BV, Amsterdam. Willem Kervers is a mediator in Rotterdam. Manon Schonewille is managing director, ACBMediation, Den Haag