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Final-offer arbitration

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Hybrid processes in ADR

Final-offer arbitration

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Different models of arbitration have both advantages and disadvantages. The disadvantages relate to expense, time, undue formality and the tendency of arbitrators to 'split the difference' between claims made. Final-offer arbitration is a response to the disadvantages of conventional arbitration as an effective method of solving disputes.

The model

In final-offer arbitration, the arbitrator chooses one of the unalterable offers put forth by each party, based upon the elements of either party's final proposals made during the collective bargaining process.¹ Since the offer made by each party is meant to be their most reasonable offer, incentive is given to the parties to make concessions and generate offers which are the most attractive to *both* parties, so as to persuade the arbitrator to pick their offer.² The incentive to make concessions is based on the uncertainty over which side's offer will be picked and this forces both sides to stay away from extreme positions.³ Once compromises are made, the chances of resolving a dispute are increased.

Prior to arbitration, parties might be required to go through negotiation or mediation in order to encourage them to settle as many of the issues as possible themselves. Arbitration affects the negotiation process and its outcome in two ways. By having an arbitrator choose only one of the offers made, both parties will attempt to generate an offer which the arbitrator will deem to be the *most reasonable*; this process will push the parties towards a settlement since each party will try to move its position closer towards the solution which has the most objective support.⁴

If, on the other hand, the parties' positions are conflicting, then neither party will want to move as this will be seen as a less advantageous result than that which could be gained through arbitration.⁵ If the parties do not make any concessions, then arbitration will be a substitute for bargaining.⁶

Strengths

One of the main strengths of final-offer arbitration is that it is more likely that compromise and settlement will take place since an extreme offer will not be chosen by the arbitrator.⁷ This means that both sides will take a position which is more in line with the other party's position. The losing party may not be awarded anything it proposed.

Another significant advantage is that final-offer arbitration does not impose the 'chilling effect' upon the incentive to bargain, a defect of the conventional arbitration process.⁸ The chilling effect arises when either party believes that it will gain a better outcome from the arbitrator than it will through negotiating

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so it does not negotiate with skill, disclosure or creativity and leaves the decision up to the arbitrator.⁹ This effect leaves the parties with little incentive to bargain with some degree of honesty, disclosure and skill.

Further, in conventional arbitration, and especially in labour disputes, since arbitrators tend to simply 'split the difference', the cost of having the arbitrator do so is still less than a strike would cost.¹⁰ In final-offer arbitration, parties are encouraged to negotiate a settlement, come to a more reasonable position and have an increased incentive to avoid arbitration.¹¹ What drives the parties to do this is the fear that the arbitrator will choose the other side's offer. Because of this, final-offer arbitration pushes each side towards agreement in a way that conventional arbitration does not.¹²

Weaknesses

The main weakness of final-offer arbitration is that the decision may not be the most equitable or may not necessarily meet the needs of the parties.¹³ In package selection, if either or both sides mistakenly or deliberately make offers which include terms that are inequitable to the other side, the arbitrator is left with no choice but to choose the best of the inequitable options.¹⁴ Parties may deliberately include such terms into an otherwise equitable offer in order to gain ground with respect to an issue to which the other side would normally never agree.¹⁵ If both parties participate in such behaviour, then one party will 'be rewarded for its misjudgment or deviousness while the other suffers a severe penalty'.¹⁶

Because arbitration is final and binding on both sides, the side whose offer was not chosen will often suffer great losses, greater than if the arbitrator simply 'split the difference'. The award will favour one side and be less equitable to the other.¹⁷

For inexperienced negotiators, since they may not understand the risks of using final-offer arbitration, they will not have the incentive to compromise in negotiations.¹⁸ Even if they understand the risk, they may believe that their position is more in line with predicted market or court outcomes and will therefore still not compromise.¹⁹ They would then suffer self-inflicted martyrdom.

Diagnostic suitability of final-offer arbitration

The ability of final-offer arbitration to lessen the differences with regard to issues of dispute between two parties depends, to a certain extent, on the type of dispute.²⁰ It has been suggested that disputes regarding wage rates, historical patterns or relationship issues are more likely to generate resolutions which are, at a minimum, tolerable whereas disputes regarding job or income security generate a very different result since they deal with rights and union structures rather than pure economic disagreements.²¹

Final-offer arbitration in the United States is used primarily in disputes involving public employees where strikes cannot occur due to inordinate economic loss or danger to public health and safety.²² Examples of such areas of employment are police and firefighters. If such employees were to strike, the public would be helpless if

ADR Bulletin new ownership

From the beginning of 2008 the **ADR Bulletin** will be produced by the **Dispute Resolution Centre at Bond University**. The chairman of the Bulletin Board will be John Wade, the business manager, Cheryl Hensel, the general editor, Laurence Boule, and the executive assistant, Yvette Zegenhagen. There will continue to be an independent Editorial Panel. Further aspects of this new venture will be announced in the next issue. Please direct enquiries to adrbulletin@bond.edu.au.



a situation arose where their services were needed. As a result, clauses are often written into such employment contracts which state that final-offer arbitration, where the decision is binding and final, must be used to settle any disputes.

Final-offer arbitration is also used to resolve disputes involving professional sports players where the player is contractually tied to an organisation and cannot be voluntarily employed elsewhere until his or her contract is completed.²³ Salary arbitration has been used in the United States since 1974 between the Major League Baseball Players Association and club owners.²⁴ An arbitrator chooses either the player's final demand or the club's final offer as the player's compensation for next year; they are not allowed to compromise between the two offers.²⁵ Arbitrators base their decision on the following criteria: player performance during the past year, length and consistency of the player's career, salaries of comparable players and the team's on-field success and attendance; team profitability and market size cannot be considered.²⁶

It has also been suggested that final-offer arbitration be used to settle tort cases in order to relieve court congestion.²⁷ The plaintiff submits his or her lowest demand and the defendant submits his or her highest offer to the arbitrator (who then picks an amount based on an assessment of pre-arbitration bargaining between the parties) and the offer that is closest to the arbitrator's figure becomes the award.²⁸ This rewards parties who participate in the bargaining process and make reasonable offers instead of penalising those who do not attempt to settle.²⁹ Commentators state, however, that this process would only be effective if made compulsory and would only apply to cases that had more than two possible outcomes.³⁰

Conclusion

While not a perfect solution to the perils of conventional arbitration, final-offer arbitration intends to

restrict the conventional process so as to put more of the decision-making power in the hands of the parties. As a theoretical model, final-offer arbitration seems attractive in some kinds of disputes. So why has it remained so apparently unknown in Australia? ●

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(1975) 14(3) *Industrial Relations* 302 at 304.

10. Above note 9.
11. Above note 8 at 576.
12. Above note 9 at 305.
13. Above note 1 at 23.
14. Clifford Donn, 'Games final-offer arbitrators might play' (1977) 16(3) *Industrial Relations* 306 at 309.
15. Above note 14 at 309–10.
16. Above note 14 at 310.
17. Charles Feigenbaum, 'Final offer arbitration: better theory than practice' (1975) 14(3) *Industrial Relations* 311 at 312.
18. David Lipsky and Thomas Barocci, 'Public employees in Massachusetts and final-offer arbitration' (1978) *Monthly Labor Review* 34 at 35.

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Endnotes

1. Fred Whitney, 'Final-offer arbitration: the Indianapolis experience' (1973) *Monthly Labor Review* 20 at 21–22.
2. Howard Foster, 'Final offer selection in national emergency disputes' (1972) 27 *Arbitration Journal* 85 at 90–91.
3. Above note 2 at 90.
4. Above note 2 at 93.
5. Above note 2.
6. Above note 2 at 92.
7. Paul Staudohar, 'Results of final-offer arbitration of bargaining disputes' (1975) 18(1) *California Management Review* 57 at 57.
8. Peter Feuille, 'The public administrator and final offer arbitration' (1974) *Public Administration Review* 575 at 576.
9. Peter Feuille, 'Final offer arbitration and the chilling effect' (1975) 14(3) *Industrial Relations* 302 at 304.
10. Above note 9.
11. Above note 8 at 576.
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14. Clifford Donn, 'Games final-offer arbitrators might play' (1977) 16(3) *Industrial Relations* 306 at 309.
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17. Charles Feigenbaum, 'Final offer arbitration: better theory than practice' (1975) 14(3) *Industrial Relations* 311 at 312.
18. David Lipsky and Thomas Barocci, 'Public employees in Massachusetts and final-offer arbitration' (1978) *Monthly Labor Review* 34 at 35.
19. Above note 18.
20. Above note 2 at 95.
21. Above note 2.
22. Above note 7 at 61.
23. Above note 7.
24. Above note 7 at 60.
25. James R Chelius and James B Dworkin, 'An economic analysis of final-offer arbitration as a conflict resolution device' (1980) 24(2) *The Journal of Conflict Resolution* 293 at 296.
26. John L Fizek, 'Play ball: baseball arbitration after 20 years' (1994) *Dispute Resolution Journal* 42 at 43.
27. Charles W Adams, 'Final offer arbitration: time for serious consideration by the courts' (1987) *Nebraska Law Review* 213 at 216–217.
28. Above note 27 at 217.
29. Above note 27.
30. Above note 27.



ADR DEVELOPMENTS

- On 21 February 2008 the **Supreme Court of Western Australia issued a practice direction on the Supreme Court Mediation Program**. The direction, which outlines various conditions of the process including where mediations are to be held, confidentiality and representation, makes some interesting directives. Mediations must be attended in person and teleconferences will be considered non-compliance. Additionally, practitioners are instructed to discuss various matters in regard to mediation with their clients including possible outcomes at trial, costs incurred up to the date of the mediation conference, costs likely to be incurred in taking the matter to trial, costs likely to be recovered if the party wins and if they lost, the interests of the parties and possible solutions to the dispute. The practice directive can be found by following the links on the Supreme Court of Western Australia website at www.supremecourt.wa.gov.au.
- The latest *International Comparative Legal Guide to International Arbitration* was released at the end of 2007. The guide provides a comprehensive worldwide legal analysis of the laws and regulations of international arbitration written by leading international arbitration lawyers. It is divided into two main sections, the first being six general chapters on key international arbitration issues, particularly from the perspective of a multi-jurisdictional transaction. The second section comprises 58 country question and answer chapters which are further divided into five regional sections. For a complete overview of this report go to: www.researchandmarkets.com/product/e4eb74/the_international_comparative_legal_guide_to.
- The 'Online guide to mediation', an award-winning ADR weblog, has changed location after three years and is now available at <http://mediationchannel.com>. The blog offers information, news and commentary, as well as the occasional offbeat story on mediation, negotiation, law and conflict management. The blog was one of the first to deal exclusively with ADR and

since its inception, the number of ADR blogs has grown exponentially. For more on ADR blogs visit, the 'World directory of ADR blogs' at <http://adrblogs.com> where you can search for blogs by categories, countries and regions.

- On 5 March this year **The United Nations announced the launch of its new Standby Team of Mediation Experts** at a press conference at its headquarters in New York. The launch was by the Under-Secretary-General for Political Affairs, B Lynn Pascoe. This initiative comes amid a broader effort by Secretary-General Ban Ki-moon to build up United Nations capacity for preventative diplomacy by strengthening its Department of Political Affairs.

Two of the six experts who initially comprise the Standby Team have already been dispatched to Kenya to assist in the ongoing African-led mediation efforts to resolve the political crisis there. Other team members were in New York for briefings before taking up their assignments in the field.

The Standby Team was chosen from hundreds of candidates, through a process that included an open invitation for nominations from United Nations Member States.

The founding Team members are Joyce Neu (United States), Team Leader; Jeffrey Mapendere (Zimbabwe), Security Arrangements (from ceasefires to the demobilisation, disarmament and reintegration of combatants); Patrick Gavigan (United States/Ireland), Transitional Justice and Human Rights; John McGarry (Canada), Power-Sharing; and Andrew Ladley (New Zealand), Constitution-making.

The Mediation Support Standby Team will be supervised by the Department of Political Affairs and can be deployed either as a group or separately, depending on need. Their services are being offered to current United Nations envoys, political and peacekeeping missions in the field, as well as to regional organisations with which the United Nations works closely in conflict mediation. For more information see www.un.org/News/Press/docs//2008/pa1.doc.htm.