

# Unpacking the Standing Neutral:

A Cost Effective and Common-Sense  
Approach for Preventing Conflict

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# UNPACKING THE STANDING NEUTRAL

## EXECUTIVE SUMMARY

*"All complex contracts will be incomplete. There will be errors, omissions, and the like."*

*Oliver Williamson, 2009 Nobel Laureate in Economic Sciences*

Let's face it. You need not be a Nobel-prize winning economist to know that contracts are inherently incomplete. No lawyer has yet crafted the perfect contract that will anticipate every eventuality. Problems and unexpected events are always around the corner.

Long-term contractual relationships are especially vulnerable to the damage caused by friction in relationships, particularly when this friction turns into a formal dispute. In far too many relationships the parties do not perceive a need to engage in conventional conflict resolution until they begin to experience real pain. By that time, they have blamed each other for their troubles. Unfortunately, this usually means that the parties' relationship has reached a breaking point, which can lead to calling on their respective lawyers who are not typically incentivized or instinctively inclined to resolve conflicts constructively in the way best suited to the preservation of the relationship. And if typical negotiations fail, the next step is calling in a mediator, and perhaps eventually ending up in arbitration or the court system.

To avoid these harmful escalations of conflict in business relationships, this paper argues for the proactive use of a "Standing Neutral" – a trusted, independent expert advisor (or a panel of three advisors) – chosen by the contracting parties at the onset of the relationship with the clear goal to maintain a healthy relationship. A Standing Neutral process can best be described as a proactive, quick, informal, flexible, adaptable, non-adversarial, neutral, expert, preferably nonbinding, process for preventing and achieving the earliest possible solution to problems and preventing potential disputes.

This white paper includes five parts. It will help you understand the why, what and how of using a Standing Neutral for preventing and managing conflicts.

- Part 1 **explains why** the time is ripe to consider collaborative approaches for resolving conflicts
- Part 2 shares **research** which supports using a Standing Neutral, suggesting that such preventive conflict resolution techniques are not simply a new fad, but perhaps one of the best-kept secrets that should be widely unlocked and adopted for widespread use
- Part 3 highlights the **what and how** of using a Standing Neutral
- Part 4 shares **examples** of the Standing Neutral concept **in practice**
- Part 5 explores the **costs and benefits** of using a Standing Neutral

In addition, we provide a comprehensive Appendix on how to design a dispute prevention, de-escalation and resolution system.

The bottom line? It is YOUR bottom line. Using a Standing Neutral is the most effective and efficient way to govern and improve today's modern commercial relationships.



## UNPACKING THE STANDING NEUTRAL

### PART 1: WHY THE NEED FOR A STANDING NEUTRAL?

*"An ounce of prevention is worth a pound of cure." "A stitch in time saves nine."  
"Fortune favors the prepared mind." "Blessed are the peacemakers."*

Those common-sense maxims have been around for decades, if not hundreds of years. However, these age-old adages are rarely considered when managing contractual conflicts.

Contracts can be similar to buying a new pair of shoes; it is often great at first - but sometimes friction occurs. Small misalignments are like the rub from that brand-new pair of shoes which can be unpleasant and turn into a blister. Left unchecked what starts as friction or misaligned interests can turn into a full-blown dispute – or worse – end up in court. While the vast majority of conflicts avoid litigation, the time and cost associated with traditional lawyer-led negotiation, mediation, and arbitration can be protracted and expensive. Even if the issue does not go to a formal dispute, the friction causes lost opportunity, value leakage and transaction costs: what Oliver Williamson calls Transaction Cost Economics.

The simple fact is that friction should be expected in any complex contract. Why? In the words of Nobel Laureate Oliver Williamson: "all complex contracts will be incomplete. There will be errors, omissions, and the like."<sup>1</sup> The very nature of complex contracts means it is impossible to predict every 'what if' scenario given today's global and dynamic business environment.

Another Nobel Laureate – Oliver Hart – echoes Williamson's sentiments regarding incomplete contracts. Hart's latest research with John Moore suggests you really should not blame 'the other guy' for what may seem like opportunistic behaviors. Rather it stems from what Hart calls *shading*.<sup>2</sup> Shading is not opportunistic behavior, but *retaliating behavior* in which a party stops cooperating, ceases to be proactive, or makes counter moves because of disappointment. Shading happens when a party doesn't get the outcome it expects from the deal and feels the other party is to blame for it or does not act reasonably by helping to mitigate the losses.

To provide another example, consider the all too contentious "scope-creep" debate. A supplier projects its business case based on the information shared during a competitive bid process. Let's assume the supplier estimates it will make a 15% profit margin. If demand is lower than expected or there is extra work not anticipated (e.g., scope-creep), the supplier will have lower than expected profit. This disappointment will cause the supplier to justify asking for approval for scope changes. And if the buying organization makes it difficult to get a contract changes through, the supplier may be tempted to reduce service levels or replace the expensive A-team with the less costly C-team. In short – each party's action leads to the other party's reaction, creating the negative tit-for-tat cycle. One disappointment leads to another, and the vicious cycle begins. This problem is so systemic in large and complex deals it is sometimes called the *death spiral* because once the cycle starts it often ends with an incumbent supplier losing the work to a competitor during the next bid cycle. Sadly, the root cause is often not opportunism, but disappointment based on the expectations that the parties have.

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The concept of shading makes sense, especially with complex deals. In complex deals, a contract will always be incomplete, with gaps, errors or omissions opening the door for shading behavior after the contract is signed. Traditional contracts rarely contain proactive alignment mechanisms to avoid disappointments.

In far too many situations, the need to begin a process for dealing with disputes isn't recognized until after those disappointments have led to real pain and frustration. Much like how we get lulled into thinking our new pair of shoes will magically get better with time as they get "worn in," most contracting parties resist using formal dispute resolution processes until it is often too late, and the damage is done.

The reality is that many issues do not resolve themselves easily and they drag on. However, most issues can be prevented, or at least resolved, while they are still small. To avoid these harmful escalations of conflict in business relationships, this paper argues for using the more preventive and proactive approach of a Standing Neutral to collaboratively resolve any differences in "real-time" when any issues or misalignment is still small.

### ***What is a Standing Neutral?***

A Standing Neutral is an innovative and promising improvement on traditional Alternative Dispute Resolution (ADR) techniques. A Standing Neutral process uses a highly qualified and respected expert, pre-selected - or "standing" - neutral who helps parties resolve issues throughout the life of a relationship. The classic Standing Neutral plays a facilitation role to help the parties see each other's perspectives and, when appropriate, provides a non-binding recommendation. Some parties use variations such as a Standing Mediator or even a Standing Arbitrator. Others have found that using a Standing Neutral upfront in the actual design and creation of a contract can lead to significant value and a more fair, balanced, "win-win" contract.<sup>3</sup> An approach to the Standing Neutral concept is to engage the neutral early on, facilitating proactive and constructive dialogues and day-to-day discussions, with the aim to provide continuous alignment and prevent issues altogether.

Organizations adopting Standing Neutrals proactively acknowledge the reality that no relationship is perfect, and no contract can cover every eventuality. Errors, omissions and ambiguities can cause misinterpretation. Small things such as "does this idea count for gainsharing?" or interpretation of performance data "did the supplier score 3 or 4 on the scorecard?" cause frustration – especially for suppliers who may feel they do not have a voice. In addition, complex contracts operating in dynamic environments require frequent adjustments.

The time is ripe for commercial relationships to benefit from demonstrated successful experience with the Standing Neutral method. While there are many ADR techniques (see Appendix 1), we focus the rest of this paper on the Standing Neutral because it is probably the least widely understood yet most useful of all the ADR techniques. One reason it is often misunderstood is because it differs from the "legal" ADR approaches, which are traditionally adversarial by nature. Instead, the Standing Neutral uses a more proactive and broader business focus designed to keep the parties in strategic partnerships such as joint ventures, long-term business arrangements, and outsourcing arrangements in continual alignment of interest and out of conflict.



### PART 2: RESEARCH SUPPORTING THE STANDING NEUTRAL

Alternative dispute resolution techniques, and the use of third parties in relationships, are not new. But what is new is the emerging emphasis on shifting away from reactive dispute resolution to proactive prevention processes. Part 2 looks at the research supporting the Standing Neutral concept – what we believe is the highest potential proactive prevention approach.

#### The Rise of Alternative Dispute Resolution for Solving Conflicts

Judicial (court) systems for resolving disputes have been in effect throughout civilized history. And almost as long as courts have been used, individuals and organizations have sought simpler, more efficient and more cost-effective means to deal with disputes – processes known today as Alternative Dispute Resolution (ADR) techniques. While modern ADR methods have only been in place for 40 years, one could argue the roots of ADR date all the way back to a decree issued by the Chinese Emperor, Kang-Hsi (1654-1722). Emperor Kang-Hsi made the following decree in response to complaints from citizens about the corruption and tyranny of the Chinese courts:<sup>4</sup>

"The Emperor, considering the immense population of the Empire, the great division of territorial property and the notoriously litigious character of the Chinese, is of opinion that lawsuits would tend to increase to a frightful extent if people were not afraid of the tribunals and if they felt confident of always finding in them ready and perfect justice. As man is apt to delude himself concerning his own interests, contests would then be interminable, and the half of the Empire would not suffice to settle the lawsuits of the other half. I desire, therefore, that those who have recourse to the courts should be treated without any pity and in such a manner that they shall be disgusted with law and tremble to appear before a magistrate. In this manner, the evil will be cut up by the roots; the good citizens who may have difficulties among themselves will settle them like brothers by referring to the arbitration of some old man or the mayor of the commune. As for those who are troublesome, obstinate and quarrelsome, let them be ruined in the law courts; that is the justice that is due to them."

Michael McManus and Briana Silverstein document the history of ADR in "Brief History of Alternative Dispute Resolution in the United States."<sup>5</sup> Their research revealed that formal ADR techniques date as far back as the Norman Conquest which allowed for a local and highly respected layperson to conduct informal, quasi-adjudicatory settings in their communities rather than use a more formal King's court.

The concept of using alternatives to court was expanded more formally in the early trade guilds that sought to enforce standards of quality, performance and marketplace behavior. Many of those systems continue today in commercial markets such as the diamond market and the textile industry.<sup>6</sup>

Pilgrims brought the concept of ADR to the United States "preferring to use their own mediation process to deal with community conflicts." When disagreements occurred, members of the community would hear claims, determine fault, assess damages, and ensure that the parties reconciled with one another.<sup>7</sup> Mediation was formally institutionalized in the U.S. in 1898 when Congress, following initiatives begun a few years





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earlier in Massachusetts and New York, authorized mediation for collective bargaining disputes.<sup>8</sup> In 1925 Congress passed the Federal Arbitration Act, which included express authorization for courts to enforce arbitration awards.<sup>9</sup>

The modern terms "Alternative Dispute Resolution," and "ADR," were coined as a result of the first Pound Conference in 1976 (inspired by Harvard law professor Roscoe Pound)," which promoted the use of mediation and arbitration as adjuncts to the traditional legal system.<sup>10</sup> The Pound Conference marked the beginning of a formal movement that encouraged the business world to actively embrace out-of-court processes for managing conflict. The movement attempted to move the dispute resolution process farther "upstream," closer to the origins and sources of disputes.

The 1980s were a decade of increased interest and use of ADR. In 1983 the Center for Public Resources (now more aptly named the International Institute for Conflict Prevention and Resolution, or CPR) was established as a think tank for the improvement of ADR processes. In a 1984 address to the American Bar Association, then-Supreme Court Chief Justice Warren Burger advocated for lawyers to increase their use of ADR. He acknowledged that while trials may be the only way to resolve some disputes, the legal system is too adversarial, painful, destructive, and inefficient to effectively manage all disputes.<sup>11</sup>

### The Advent of Proactive Prevention Practices

Even before ADR was taking hold, the business attorney Louis M. Brown argued that new ideas and innovative processes for the *anticipation of conflict* and *dispute prevention* were needed. He called this "preventive law".<sup>12</sup> Brown's work sparked an interest in the formal study of preventive conflict approaches – most notably in the construction industry, which is notorious for costly disputes which can have a dire impact on the timeliness and success of a project.

One of the earliest known preventive practices dates to the late 1800s when the American Institute of Architects established a system for resolving construction project disputes between project owners and contractors, which designated the architect as the initial judge of the contractor's performance. In case of dispute over the architect's decision, the process called for a prompt appeal to an *ad-hoc*, one-issue arbitration before an expert construction industry arbitrator. Typically, there was usually no shortage of qualified individuals who could serve as arbitrators on short notice.

The American Institute of Architects system emphasized timeliness, which was crucial for fast-moving construction projects where delays can be costly and have a significant negative impact. Further, the easy availability of an immediate decision in arbitration encouraged architects to act fairly and with integrity, usually resulting in mutual acceptance of the architect's decision without an appeal, thus avoiding and preventing any dispute.

The practice of using preventive techniques in the construction industry was expanded in 1975 when a group of innovative construction practitioners conceived the idea of a "dispute review board" of geological engineers to immediately solve difficult rock and soil problems on a major tunneling construction project.<sup>13</sup> By the mid-1980s, owners and contractors on major civil engineering projects further expanded on the concept by



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developing long-term "trusting" alliances to achieve greater efficiency and cost savings, processes which they called "strategic partnering," which later evolved into "project-specific partnering."<sup>14</sup> During the same period, other advances also emerged such as using "financial incentives to encourage cooperation"<sup>15</sup> and the concept of realistically allocating risks on construction projects to achieve maximum efficiency.<sup>16</sup>

A common characteristic of these contractual preventive processes - in contrast to conventional ADR "resolution" processes – is that they proactively address problems and potential disputes before they morph into intractable disputes, rather than reactively deal with disputes after they have occurred.

The 1990s initiated a more formal study into preventive techniques. The Construction Industry Institute (CII) led the pack with significant research between 1991 and 1994, which validated the utility of prevention processes. The CII added to the body of knowledge by suggesting the use of a "disputes potential index" to identify potential sources of trouble on construction projects.<sup>17</sup> The CII also demonstrated that the Dispute Review Board concept could be expanded to multi-disciplinary projects such as high-rise office buildings and not just projects involving single technical disciplines.<sup>18</sup>

A key part of CII's research contribution was the formal recognition of a critical distinction between "preventive" techniques and "resolution" techniques in dispute resolution. This distinction was known as the "continental divide of dispute resolution" and is the point where parties lose control, and the process moves from proactive *prevention* to reactive *resolution* which "is neither timely nor cheap and is seldom satisfactory."<sup>19</sup> The terms are defined as:

- "Preventive" techniques: processes that enable the parties (and persons in privity with the parties) to keep control of their disagreement and avoid conventional dispute resolution
- "Resolution" techniques: processes through which "outsiders" or "strangers" to the disagreement seek to resolve a dispute

During the same timeframe, the American Arbitration Association<sup>20</sup> and the Center for Public Resources<sup>21</sup> also advanced the understanding of preventive approaches when they classified these approaches into a spectrum or continuum of progressive dispute prevention processes which could be combined into graduated processes or "systems" to provide contracting parties a full range of dispute prevention and resolution alternatives.<sup>22</sup>

This early work in effect moved the dispute resolution process even further "upstream," embracing proactive processes that anticipate, deal with and prevent problems and potential disputes at the source before they must be subjected to traditional, expensive, time-consuming and potentially relationship-damaging dispute resolution.

One of the most recent preventive techniques is the use of data analytics to search for early warning indicators. The idea emerged in 2012 when data analytics experts began to analyze electronic data files (e.g., documents, emails, texts) to detect patterns that might indicate a potential risk. If a risk is detected, the suspected data can be analyzed and addressed before a potential problem develops into a serious concern. For example, if a potentially risky problem appears in yesterday's emails, inside counsel may decide to conduct an internal investigation today to confirm or deny the "early warning." If confirmed, and since the text at issue has been surfaced in near real-





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time, risks can be addressed internally before they develop into real problems, disputes, or litigation.<sup>23,24</sup>

While the construction industry was having early successes with preventing practices, other industries were still stuck in "resolution" – which was growing more complicated and costlier. A 1994 *Harvard Business Review* article critiqued ADR in the aptly titled article "Alternative Dispute Resolution: Why It Doesn't Work and Why It Does," stating: "The bad news is that ADR as currently practiced too often mutates into a private judicial system that looks and costs like the litigation it's supposed to prevent."<sup>25</sup> Cornell Law School reports this has only worsened over the years.<sup>26</sup>

The good news is there is increased interest from the academic and business communities in expanding "preventive" ADR techniques outside of the construction industry. This movement is led by visionaries such as:

- Thomas D. Barton, Coordinator of The National Center for Preventive Law at the California Western School of Law
- Helena Haapio, Assistant Professor of Business Law at the University of Vaasa and as International Contract Counsel at Lexpert Ltd based in Helsinki, Finland <sup>27</sup>
- Tim Cummins, President and CEO of the International Association for Contract and Commercial Management (IACCM) <sup>28</sup>
- Bernard Mayer, Professor of Dispute Resolution, The Werner Institute, Creighton University<sup>29</sup>
- James P. Groton, a "recovering lawyer" who has practiced dispute prevention throughout his career <sup>30</sup>
- Kate Vitasek, Faculty and Lead Researcher for the University of Tennessee's work on Vested Outsourcing <sup>31</sup>

While arbitration and mediation are still the most well-known and used ADR techniques today, the concept of ADR has grown to mean any method of resolving disputes without resorting to litigation in a courtroom.<sup>32</sup> In addition, utilizing preventive processes has expanded beyond the construction industry to many other kinds of business relationships.<sup>33</sup>

Recognition of the value of preventive practices got a boost when the International Mediation Institute (IMI) organized a follow up to the original Pound Conference in 2016/2017 to evaluate the state of dispute resolution 40 years after the first Pound Conference of 1976.<sup>34</sup> The series of conferences (known as the Global Pound Conferences) were held in 29 cities around the world and brought together thousands of users, providers and advisors to discuss the future direction of ADR. During the event, delegates were asked to vote on which dispute resolution processes should be prioritized to improve dispute resolution. In the overall cumulative voting, the delegates - by a substantial margin - voted for "pre-dispute or pre-escalation processes to prevent disputes," overall other dispute resolution processes.

### Expanded Use of Neutral Third-Parties

Organizations – especially organizations wishing to procure goods and services – have long used outside third-parties such as advisory, consulting and legal service providers to help them select and source suppliers. In the early 1990s, researchers began to explore the concept of using third-parties as "bridge builders" in relationships.<sup>35</sup> In 1991 Brown



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noted third-parties play the role of "central actor among diverse constituencies" who can be an effective conduit for "ideas and innovations, a source of information, a broker of resources, a negotiator of deals, a conceptualizer of strategies, and a mediator of conflict."<sup>36</sup>

Neutral third-parties have been shown to provide value in a variety of capacities, including:

- Research by LG. Zucker (1986) into trust theory suggests that people engage in self-monitoring and demonstrate more trusting behaviors in a relationship when there is a shared link to a third-party<sup>37</sup>
- J.S. Coleman, who in 1990 argued that when a mutual third-party is connecting two parties, the neutral third-party could exert sanctions that will restrain the parties from behaving opportunistically towards each other<sup>38</sup>
- "Bridging organizations" whose role is to facilitate multi-sector partnerships (F. Westley and H. Vredenburg 1991)<sup>39</sup>
- "Boundary spanners" in networks (R. S. Burt 1992)<sup>40</sup>
- "Go-betweeners" in alliances (B. Noteboom 2004)<sup>41</sup>
- "Intermediaries" for improving innovation (J. Howells 2006)<sup>42</sup>
- Building and repairing trust (Noteboom 2004, McEvily and Zaheer 2004, Mesquita 2007)<sup>43</sup>
- Preventing opportunistic behavior (Coleman 1990) and reducing the negative effect of power disparity (Noteboom 2004)<sup>44</sup>
- Henry Adobor and Ronald S. McMullen found the use of a credible neutral third-party exerts indirect influence by inspiring self-monitoring with no direct sanctions<sup>45</sup>
- Gillian Hadfield, who advocated in 2017 for a shift to third-party regulation to create lower-cost approaches to "ensure that not only poor-country suppliers, but also the global corporations that buy from them, are bound to rules"<sup>46</sup>

Research in a *Journal of Purchasing and Supply Management* article titled "Strategic Purchasing and Supplier Partnerships – The Role of a Third-party Organization" shows a third-party can play a "significant and positive role in the development of interfirm relationships."<sup>47</sup>

### The Advent of the Standing Neutral

As noted previously, the first Dispute Review Board (DRB) was established in 1975. The DRB was a trusted three-party panel of independent expert advisors chosen by contracting parties to be immediately available to help resolve disputes that arise between them during their contractual relationship. By 1991 the process had been used successfully on over 100 projects requiring expertise in only a single technology, such as tunnels (geotechnical engineering), dams (civil engineering), other massive civil engineering projects, and a few commercial projects. By that time the DRB and was recognized as a superior process for keeping the peace on a construction project. The first use of the term "Standing Neutral" to characterize a Dispute Review Board appears to have been in a 1991 CPR Publication "Preventing and Resolving Construction Disputes."<sup>48</sup>

Unlike a neutral used on an *ad-hoc* basis for dispute resolution in mediation or arbitration, a Standing Neutral is a readily-available "fast response" technique, designed to prevent any issues from escalating into adversarial disputes that might otherwise go to mediation,

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arbitration or litigation. A key feature is that the neutral is "standing." - meaning it is integrated into the parties' continuing governance structure. Another key concept is that the Standing Neutral supports the relationship itself and both parties equally; the goal is to ensure the success of the relationship.

### A Look Ahead

There is little formal research into the use of Standing Neutrals outside of the construction industry; this is a major reason the University of Tennessee has developed this comprehensive white paper.

The remainder of this paper demonstrates the unique advantages of the Standing Neutral and how to put a Standing Neutral into practice.

Part 3 explores the basics - the what and how - of a Standing Neutral. Part 4 shows how the Standing Neutral process can be tailored to meet the specific needs of different business relationships, illustrating real-world examples of using a Standing Neutral in practice. Part 5 provides evidence of the costs and benefits of adopting the Standing Neutral process.

We conclude with a call to action for individuals and organizations to incorporate Standing Neutrals into their business relationship - especially for the most strategic and complex deals - to prevent potential misalignment of interests that can easily result in shading behaviors that erode trust and can eventually lead to full-blown conflicts.



### PART 3. THE WHAT AND HOW OF A STANDING NEUTRAL

There are several variations of a Standing Neutral. Part 3 focuses on the "classic" Standing Neutral, while Part 4 explains how the process can be modified to meet the needs of a particular relationship and provides examples of how progressive organizations are evolving the concept of the Standing Neutral to provide even more value.

#### The Role of the Classic Standing Neutral

The role of a Standing Neutral has also been referred to variously as a "Referee," or "Wise-Person," or "Dispute Review Board" or "The Glue." The primary role of a "classic" Standing Neutral is to serve as a "real-time" dispute-resolver throughout a relationship. Because the neutral is "standing" he or she can act immediately to resolve any potential or actual disputes which the parties cannot resolve themselves. There are several variations of a classic Standing Neutral, but almost all involve these typical steps:

##### **Selection**

At the outset of their relationship, parties select one or three persons in whom they have trust and confidence to serve as their dispute-resolver (the Standing Neutral) throughout their relationship. A single Standing Neutral should always be entirely independent. In most cases where there is a multi-member Standing Neutral, each party nominates one member, and the two nominated neutrals will select a third member; in such cases, it is typically required that every panel member be acceptable to both parties and that all panel members be independent and impartial, with no special allegiance to the nominating party. As part of the selection process, the parties formalize an agreement with the Standing Neutral which includes determining the Standing Neutral's responsibilities and authority.

##### **Briefing**

The parties brief the Standing Neutral regarding the nature, scope and purpose of the relationship or venture. As part of the briefing, the Standing Neutral is usually equipped with a basic set of contract materials and supporting documents.

##### **Continuing Involvement**

The Standing Neutral is usually part of ongoing governance, to be available on short notice and meet regularly with the parties for a basic review of the progress of the relationship, even if there are no issues. Sometimes the Standing Neutral is merely available on an ad-hoc basis, with the contracting parties calling in the Standing Neutral, whenever necessary, to give an advisory opinion.

##### **Dispute Resolution/Admissibility of Recommendation**

If the parties have a dispute they cannot resolve themselves after receiving the advice of the Standing Neutral, they may use the Standing Neutral for formal dispute resolution. Depending on the wishes of the parties, the Standing Neutral is given authority to act on issues and disputes by rendering either a nonbinding evaluation or recommendation or a binding decision. If the Standing Neutral is empowered to make only a recommendation, either party may challenge the Standing Neutral's recommendation. However, the recommendation will typically be admissible as evidence in any subsequent arbitration or litigation.

##### **Costs**

The parties equally absorb the cost and expenses of the Standing Neutral.



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### Three Critical Elements of the Standing Neutral Process

There are three critical elements essential to the success of the Standing Neutral technique:

- Early mutual selection
- Continuous involvement by the neutral
- Prompt action on any issues.

Each element is discussed below in more detail. We then explain why the elements – when combined - work so well. We will also explain how the Standing Neutral services as a valuable dispute prevention function.

#### Early Mutual Selection

Using a Standing Neutral begins when the parties mutually agree and designate a single neutral (or a board of three neutrals such as a Dispute Board in the construction industry). The parties should jointly select a Standing Neutral where each has high confidence in the neutral's integrity and expertise. A Standing Neutral is typically an expert in the industry in which the parties are involved (e.g., construction, facilities management, IT services).

The Standing Neutral should be jointly selected by the parties *early* in the relationship. If the Standing Neutral plays a role as a deal architect, he or she should be selected *prior* to the parties starting their contracting process. If the Standing Neutral is used primarily in the issue resolution process as part of ongoing governance, the Standing Neutral should be selected *during* the contracting process and before the contract is signed. This allows for the Standing Neutral to be embedded as part of the ongoing governance mechanisms.

By establishing a Standing Neutral from the inception of the relationship, the Standing Neutral becomes part of the team and helps to create a collaborative atmosphere. Many view a Standing Neutral as a "mutual friend," "referee," or "sensible sounding board" because their advice is respected and accepted more readily than if the parties brought in a third-party stranger (mediator or arbitrator) after there is a formal dispute.

Pre-selecting a Standing Neutral at the onset of the contract avoids many problems associated with the kind of adversarial jockeying and delays associated with trying to find a suitable mediator or arbitrator after controversy arises.

#### Continuous Involvement

Once the Standing Neutral is selected, he or she is briefed on the relationship and furnished with the necessary documents describing the relationship.

The role of a Standing Neutral will vary based on his or her entry point into the relationship. For example, the University of Tennessee's popular Vested outsourcing methodology for developing highly collaborative win-win outsourcing relationships embeds a neutral third-party "deal architect" as a coach as part of the contract development. The Standing Neutral as a coach provides an objective view on facts and issues which helps the parties ensure they get to a fair and balanced contract.



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Organizations that embed a Standing Neutral as part of ongoing governance (e.g., such as in the construction industry's Dispute Review Board) will rely on the Standing Neutral to help the parties immediately address and resolve issues and concerns that arise in the relationship and to prevent the problems from escalating into full-fledged disputes. This continuous and swift involvement ensures problems are resolved while they are small, avoiding the need for more costly mediation, arbitration or litigation. The ready availability of the Standing Neutral and his/her familiarity with the relationship make it possible to obtain a prompt resolution of any disputes.

One of the key differences between a Standing Neutral and a mediator or arbitrator is that the Standing Neutral has ongoing involvement with the parties during the life of the contract (or project, as in the construction industry). The parties routinely provide the Standing Neutral with periodic progress reports as the relationship progresses and, when possible, invite the Standing Neutral to meet occasionally with the parties absent any immediate dispute. For example, in construction projects, Dispute Boards are often part of the project administration. Likewise, in an outsourcing relationship, a Standing Neutral can be embedded into formal governance mechanisms such as Quarterly Business Reviews.

Because a Standing Neutral has more of a "hands-on" approach, he or she can almost always earn trust quickly as being fair and impartial. In addition, the continuous involvement of the Standing Neutral generates a feel for the dynamics and progress of the relationship. Also, they can coach each party about the potential opportunistic behaviors that can easily start a downward spiral of tit-for-tat negative actions.

A key benefit of having a Standing Neutral embedded in the relationship is that it significantly increases the speed with which he/she can offer advice and render decisions if needed. Also, the Standing Neutral will hear every dispute that occurs during the history of the relationship, which promotes more candid discussions. This enables the Standing Neutral to shift the focus from that of a "judge" to one of a "coach."

Last, the ongoing nature of the relationship with the Standing Neutral becomes a powerful inherent incentive for the parties to "self-monitor" behaviors and avoid opportunism and shading<sup>49</sup> behavior much the way a referee works in a sport to curb bad behaviors. Thus, the Standing Neutral can influence, during the contract period, positive actions that improve contract performance.

### Real-Time and Prompt Action on Issues/Concerns/Disputes

A key objective of a Standing Neutral process is to preserve cooperative relationships between the contracting parties. The classic Standing Neutral emphasizes "keeping the peace" in a relationship while modern Standing Neutrals focus on a more proactive continual alignment of interests. A good Standing Neutral process is a "fast response/dose of reality" technique emphasizing "real-time" resolution.

The Standing Neutral is expected to be available on relatively short notice to consult with the parties and to discuss issues while misalignment and problems are still new and likely still small. The Standing Neutral has an uncanny ability to help the parties resolve any misalignment because they are a trusted "part of the team." The Standing Neutral reviews an issue while it is in the earliest stage and helps the parties identify ways forward in an





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informal capacity before issues become disputes. The Standing Neutral's early involvement creates valuable opportunities for the parties to avoid conflicts through proactive communication. Also, the participation of lawyers as advocates for parties is discouraged to preserve the informality of the process and to help keep the process as non-adversarial as possible.\* This offers a significant advantage over traditional mediation, arbitration or reconciliation techniques.

Usually, if the parties cannot reach a resolution, the Standing Neutral will render an impartial recommendation (not a compromise proposal) when issues arise.<sup>50,51</sup> If the Standing Neutral is called on to make a recommendation, recommendations are often regarding matters of entitlement only, leaving the discussion of amounts up to the parties after they have received the advice. Typically, the recommendations of the Standing Neutral are non-binding and parties can choose a more formal dispute resolution process such as arbitration or litigation if the Standing Neutral's recommendation is not accepted. However, sometimes the parties give the Standing Neutral the authority to act as an arbitrator to make binding decisions. The downside to asking for a binding decision is this will likely encourage the participation of lawyers serving in an adversarial capacity, changing somewhat the nature of the process.

Experience has shown that when an issue is referred to the Standing Neutral, the Neutral's decisions have generally been accepted by both parties with no attempt to seek relief from any other tribunal. This result is enhanced where there is a contract stipulation stating that if any subsequent arbitration or litigation occurs, the decisions of the Standing Neutral will be admissible in evidence in a future formal arbitration or litigation.

### Why the Standing Neutral Process Works So Well

When parties combine the three elements above into a Standing Neutral process they are, in essence, establishing the "rules" of how they will use the Standing Neutral to prevent or resolve issues early. A well-designed Standing Neutral process embeds its customized rules as foundational components of the parties' ongoing governance.

Standing Neutrals have had a remarkable record of success wherever they have been used. In the vast majority of cases, the parties never look to the Standing Neutral to make any recommendations or decisions. And in the small minority of cases where the Standing Neutral actually makes a recommendation, 95% of the recommendations are accepted by the parties without resort to mediation, arbitration or litigation.<sup>52</sup>

The establishment of a Standing Neutral—which appears at first to be merely an efficient technique for quickly resolving disputes—creates a dynamic situation in which the participants in the business enterprise change their relationship and their attitudes toward each other. The changes usually are an evolution, rather than a conscious effort. For example, at first it is common for contracting parties to feel they are simply choosing an expert neutral for resolving conflicts between them promptly. However, as the Standing Neutral interacts with the parties during ongoing governance forums, the parties develop a greater sense of confidence in the Standing Neutral's ability to quickly alleviate friction in the relationship. When this happens, the parties shift their view of the Standing Neutral from "dispute-resolver" to one of a "mutual friend" or a "sensible sounding board."

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\* Lawyers are often Standing Neutrals. However, when acting in the capacity of a Standing Neutral they do not formally represent either party in a formal legal capacity, but rather as a neutral advisory role



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Simply put, the mere act of appointing a Standing Neutral can be like a magic bullet for reducing or even eliminating friction between parties to a contract. Research supporting this dates to 1933 when Elton Mayo researched the "Hawthorne Effect," which states the mere act of watching can affect behaviors.<sup>53</sup> Since then several researchers have shown the impact of using outsiders. For example, Adobor and McMullen found "the sheer presence of a third-party fosters 'self-monitoring' of behaviors" and Dan Ariely has shown that the presence of others causes people to behave more honestly and reign in unethical behavior such as cheating.<sup>54</sup> These effects are amplified when the third-party observer is knowledgeable in the subject matter of the agreement and in the nature of the agreement.

Why does the presence of a Standing Neutral have such a powerful impact? The evaluative, but typically non-binding, nature of the Standing Neutral provides a helpful "dose of reality" to the parties and encourages them to be more objective in their dealings with each other. When differences of opinion do arise, the parties' continuous access to the Standing Neutral allows them to quickly use the Standing Neutral as an objective sounding board, obtaining a recommended course of action minimally disruptive to the business relationship. This encourages teamwork and leads to improved performance by all parties. The contracting parties become inherently incentivized to concentrate on "fixing the problem" rather than "fixing the blame," and use their mutual knowledge to solve the problem rather than relinquishing control to the Neutral. A side benefit is when the parties construct their own solutions to problems, they often increase their trust and confidence in each other's abilities which ultimately strengthens the relationship.

For these reasons, the Standing Neutral serves as not only a standby "real-time" dispute *resolution* process, but also as a remarkably successful *prevention* process offering these benefits:

### **Improved Attitudes and Performance**

A well designed and executed Standing Neutral process significantly increases contracting parties' certainty that problems will be resolved promptly and fairly. This encourages the parties to seek a mutual solution to their problems without even involving the neutral, which ultimately improves attitudes and performance because:

- It requires the parties to identify issues early and deal with them promptly
- It encourages the parties to communicate with each other
- It encourages the parties to evaluate their positions on issues realistically
- It encourages straightforward dealing and discourages game-playing and posturing
- It improves relationships between the parties

### **High-Quality Dispute Decision**

If the Standing Neutral makes a recommendation or decision, its quality is superior, because:

- It resolves the issues/disputes speedily
- It is made by a person who was voluntarily selected by the parties and has already been pre-qualified as an expert
- Pre-selection of the neutral before an issue arises saves the time and difficulty often associated with selecting a neutral after a dispute has arisen
- The neutral has the benefit of familiarity, continuity, and accumulated experience of the relationship
- The issue is resolved while facts are still fresh



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- The parties are more likely to accept a recommendation or decision as fair because they have confidence in the expertise, knowledge and integrity of the neutral
- If the neutral makes a binding decision rather than merely a recommendation, it is final, and thus there is no uncertainty about the outcome

### Low-Cost Decision

A Standing Neutral is an extremely cost-effective way to prevent and resolve disputes because:

- The issue is resolved before it becomes unmanageable
- The disruptive effects of delayed decisions are avoided
- The substantial expenses, risks and uncertainties a mediation, arbitration or lawsuit are avoided

### Key Steps to Engage a Standing Neutral

Incorporating a Standing Neutral typically involves these steps:

- Start by checking any country or state-specific guidelines that might limit a Standing Neutral to act a third-party neutral. For example, the State of Washington has guidelines for lawyers wishing to work as third-party neutrals (see Appendix 3).
- Next, the parties to a long-term business contract perform research and compile a shortlist of experts in the field. In considering candidates, they should focus on the individual's expertise, neutrality and integrity. Experience as a Standing Neutral should not be a necessary requirement. Nor does the Standing Neutral have to be a lawyer.<sup>†</sup>
- As part of the selection process, the parties inform the neutral of the purpose and scope of their deal and the contractual relationship. A key part of the selection process is ensuring the potential candidate has no conflicts of interest and that the candidate can support the expected timeline and/or cadence of any regularly scheduled governance meetings he or she is expected to participate in.
- Once the Standing Neutral is selected, the parties brief the Standing Neutral and provide all the documents relevant to the parties' relationship.
- The parties and the Standing Neutral then sign an agreement. It is critical to note the costs of the Standing Neutral is split evenly between the parties so that each is equally invested in the relationship. When using a Standing Neutral as part of ongoing governance, we recommend that the role of a Standing Neutral be formally embedded into the parties' contract.
- If the Standing Neutral can no longer fulfill his or her role, the parties will choose a replacement Standing Neutral with the existing Standing Neutral often formally briefing the new person. This should be accomplished without biasing the new Standing Neutral during the transition.

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<sup>†</sup> Some countries or states have specific laws regulating a lawyer's ability to act as a neutral. See for example Appendix 3 with the guidelines from the State of Washington

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### Sample Standing Neutral Agreement Terms

A typical Standing Neutral agreement for ongoing governance support should do the following:

- Define the compensation model by which the Standing Neutral will be paid
- Outline the Standing Neutral's purpose, role and authority
- Establish the ongoing commitment of the Standing Neutral, including which meetings the Standing Neutral should regularly attend and the availability expectations for ad-hoc needs
- May also provide for the frequency and manner in which the parties are to periodically update the Standing Neutral on the progress of the project/relationship, such as periodic management reports and any incident reports
- Can require that the Standing Neutral's advice and decisions are admissible evidence in any subsequent arbitration or litigation
- Should also specify whether the neutral is empowered to issue binding decisions (not typical)



### PART 4. VARIATIONS AND EXAMPLES IN ACTION

Part 4 serves three purposes. First, it highlights the evolution of how Standing Neutrals are being used. Second, we explain typical variations in practice, emphasizing there is not a "one size fits all" way to design a Standing Neutral process. Third, we offer real examples of how organizations are successfully incorporating a Standing Neutral into their relationship.

#### Evolution of the Standing Neutral Concept

As mentioned previously, the use of a Standing Neutral has evolved over time. For example, in the construction industry where the concept originated, there are now Dispute Adjudication Boards (DABs). These are empowered to make binding interim decisions requiring immediate compliance to avoid delays in a construction project, which can be appealed only following completion of construction. Using DABs has been incorporated into the World Bank construction contract forms.<sup>55</sup>

In the United Kingdom there is a statutory process, incorporated by law into most construction contracts, whereby a single neutral adjudicator can be called in to make a quick adjudication on disputed issues, which is binding until completing construction. While the statute does not require that the adjudicator be "standing," parties sometimes choose the adjudicator in advance essentially enabling the adjudicator to be a Standing Neutral who makes a binding decision. This process has been described as a "pay now, litigate later" process, or a "quick fix" solution to a construction claim, on the assumption that anything that goes awry with the adjudication process can be cured following construction in subsequent litigation or arbitration.<sup>56</sup>

The role of the Standing Neutral has also expanded outside of the construction industry. Standing Neutrals are now found in outsourcing agreements, the financial services industry, franchise agreements, outsourcing agreements, long-term construction projects, and operational and maintenance contracts.

The role of Standing Neutral is also expanding to go further "upstream". For example, being included as part of the contract development (e.g., as in the University of Tennessee's Vested outsourcing methodology) playing the role of "coach" or "deal architect" at the inception of the relationship to ensure a fair and balanced agreement that optimally meets both parties' needs.

The next section describes the key decision factors parties need to mutually agree upon when designing a Standing Neutral role for their relationship.

#### Variations of the Standing Neutral Process

There is not a "one size fits all" Standing Neutral process. It is versatile and can be easily modified to meet the unique needs of the parties and their situation. When the parties are designing their Standing Neutral process, they will need to consider these factors discussed on the following page.<sup>57</sup>

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### **Number**

A Standing Neutral process typically either involves one or three members (i.e., Dispute Review Boards commonly used in the construction industry). The number is typically a factor of the experience and budget. In some cases, a single Standing Neutral may not have the appropriate skills needed for the parties' unique situation.

### **Degree of Neutral's Involvement**

A key decision factor is to determine the level of involvement. Do you want your Standing Neutral to be part of pre-contract signing or only as part of the post-contract performance?

At a minimum, your Standing Neutral should be integrated as part of ongoing governance – but you will need to determine their level of involvement. Will they have fairly close and continuous involvement at all governance levels? Or will they have only occasional contact such as attending Quarterly Business Reviews or simply to serve in a standby role?

Parties that want their Standing Neutral to be part of pre-contract signing should also determine the level of involvement. For example, will the Standing Neutral simply play a facilitative and coaching role, or will they be more involved such as providing joint project management through the contracting process or perhaps even assist in contract drafting?

### **Dispute Resolution Role**

Another key decision factor is to determine the Standing Neutral's role in resolving disputes if they do arise. The functions range from serving a strictly facilitative role (such as acting as a Standing Mediator) to an expert advisory role (such as rendering a professional advisory opinion on a technical matter). In some cases, the Standing Neutral plays an even broader role such as rendering non-binding or even legally binding decisions.

### **Facilitative or Adjudicative Role**

If the Standing Neutral is given the authority to make decisions, the parties should determine the level of authority. For example, will the Standing Neutral have the authority to make binding or non-binding decisions? Whether the Standing Neutral should have a facilitative or adjudicative role depends upon the speed and certainty that the parties seek. In the construction industry, where the parties need an objective reality check to resolve a problem so construction can proceed without delay or uncertainty, and an adjudicative role is preferred. However, other business relationships may not require the speed or certainty and may prefer a facilitative role.

### **Fact-Finding Latitude**

In cases where the Standing Neutral's role is to make a decision or recommendation, whether non-binding or binding, the neutral may be given any of a wide range of possible degrees of latitude in making his or her determination, such as the ability to hire outside experts, or make a personal investigation, as distinguished from merely receiving information and evidence produced by the parties. Or the parties could agree to frame the issues to be determined by the neutral in a “baseball arbitration” format, where the neutral must choose between two alternative proposals made by two parties.



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### Examples in Practice

In this section, we provide examples of 12 variations of how parties are using Standing Neutrals in practice. **Figure 1** summarizes each example to show how they vary across a continuum ranging from preventive in nature to a formal dispute resolution.

**Figure 1: Summary of Standing Neutral Examples**

Pre-Contract Signing	During Contract Performance			
Prevention (pre-contract signing)	Problem Solving	Dispute Control	Facilitated Resolution	Formal Dispute Resolution
	1. Dispute Board (common in the construction industry)			1 Dispute Adjudication Board
	Single Standing Neutral			
		2. Standing Expert (Microsoft Outsourcing)		
	3. Standing Mediator (South Korea Ombudsman Office)			
				4. Standing Arbitrator (Toyota)
5. Deal Architect/Partnering Facilitator (Telia/Veolia)				
6. Branding & Licensing Example				
		7. Franchise Wise-Persons Committee		
	8. Outsource Agreement Embedded Governance			
		9. Real Estate Development Standing Arbitrators		
9. Labor Services Deal Architect				
	11. Non-Profit NGO Wise-Persons Committee			
	12. Outside Director Role			

Each example is discussed in more detail.

### Most Common Variations

The International Institute for Conflict Prevention and Resolution outlines the six most common variations of a Neutral including the Dispute Review Board, Single Standing Neutral, Standing Expert, Standing Mediator, Standing Arbitrator and Partnering Facilitator/Deal Architect.<sup>‡58</sup> Each is discussed below.

<sup>‡</sup> For a more comprehensive discussion see the International Institute for Conflict Prevention and Resolution article “How and Why the Standing Neutral Dispute Prevention and Resolution Technique Can Be Applied.” See endnote citation for complete reference.



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## 1. Dispute Board/Dispute Adjudication Board

The Dispute Board (also called a Dispute Review Board or Dispute Adjudication Board) was first used in 1975 in the construction industry.<sup>59</sup> A Dispute Board is typically a neutral three-member board appointed at the beginning of a business relationship and continuing in place throughout the relationship. The Dispute Board regularly visits with the parties and between visits receives updates so the board can stay abreast of developments during the business relationship.

If disputes arise, the Dispute Board “hears” the matter in an informal process. It then gives the parties detailed, but nonbinding, findings and recommendations they can accept or reject, or use as the basis for further negotiations. Some Dispute Boards, which also are known as Dispute Adjudication Boards, issue “temporarily binding” determinations that the parties are bound to honor immediately, subject to the right to arbitrate or litigate later if they so choose.

The main driver of Dispute Boards has been for World Bank-funded projects. The first use of a Dispute Board outside of the United States was Honduras (for the El Cajon Hydroelectric Project). The number of very large international projects using Dispute Boards has risen dramatically since the mid-1990s, including

- Channel Tunnel Project, where a standing five-member DAB was used
- Hong Kong Airport Project, where a seven-member DAB was used
- Ertan Hydroelectric Power Project in China, where a three-member DRB was used.<sup>60</sup>

Dispute Boards and single Standing Neutral can be classified as the “classic” Standing Neutral because the focus is limited to problem-solving and de-escalation ADR techniques versus more problem prevention techniques.

A single individual Standing Neutral is an efficient substitute for a multi-person Dispute Board and has been used effectively outside of the construction industry in a similar nature to how Dispute Review Boards are used. The Dispute Review Board Foundation suggests a single Standing Neutral be used for construction projects under \$10 million in costs while projects larger than \$10 million in construction costs should use the standard three-member dispute board.<sup>61</sup>

The authors’ experience is that non-construction related relationships tend to use a single Standing Neutral.

## 2. Standing Expert

If the parties foresee a potential need during their relationship to seek an expert determination on disputed matters, they can appoint a Standing Expert who can be called upon to render an expert opinion whenever necessary. Standing Experts are technical experts – typically without legal training. They are most useful in relationships where complex technical, accounting, cost, or quality standards could be at issue.

Standing Experts differ from Dispute Boards and single Standing Neutrals because - while they may be “standing” - they typically are only brought in when a dispute arises around a technical issue that needs a formal opinion.



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A good example of a Standing Expert comes from Microsoft. When Microsoft first outsourced its facilities management services to Grubb & Ellis, it created a scorecard to measure Grubb & Ellis's performance. A portion of Grubb & Ellis' compensation was based on performance as defined by the scorecard. Initially, there was a significant gap in expectations and performance as measured by Microsoft versus Grubb & Ellis. For example, Microsoft believed Grubb & Ellis score on a particular item was a "3" while Grubb & Ellis perceived their performance to be a "5". The parties brought in a Standing Expert with experience in facilities management to review Grubb & Ellis' performance and help the parties determine the actual performance level. Microsoft would then use the Standing Expert's score to calculate Grubb & Ellis' incentive payouts. Over the first two years, the Microsoft and Grubb & Ellis perception gaps on performance decreased by 91.5 percent, resulting in tight alignment between the two companies on what performance meant.<sup>62</sup>

It is possible for the Standing Neutral to also play the role of a Standing Expert if qualified to do so.

### 3. Standing Mediator

If desired, the Standing Neutral can be asked to be a mediator rather than an objective fact finder. While this approach can work, it can also be argued that the objective approach of a fact-driven neutral is preferable to the "bargaining" context of mediation. However, the concept behind a Standing Mediator has worked for institutions such as the United Nations. The United Nations Secretary-General often acts as a mediator in international conflicts. Ombudsmen within government agencies or universities or businesses also can serve in the role of mediator (or funnel the disputes to other mediators) and can move quickly to intervene before the conflict worsens. South Korea, for example, has created an ombudsman office in its investment promotion agency that is accountable directly to the Prime Minister. The purpose is to help foreign investors navigate any issues that might arise while doing business in Korea.

### 4. Standing Arbitrator

Some labor contracts, particularly in industries such as basic steel, have employed umpires, or continuing arbitrators, known sometimes as "permanent" arbitrators. Here the neutral is given the power to render binding decisions, thus acting as an arbitrator.

Most Standing Arbitrator arrangements use the arbitrator in the same quasi-judicial capacity as many ad-hoc arbitrators. But a few are encouraged to also act as a mediator before arbitration (which the authors prefer). For example, some have expectations that the neutral will apply a larger view to help the parties avoid repetitive cases.

Toyota Motor Sales, USA and its dealers provide a good Standing Arbitrator example. They use Private Adjudication Center, Inc. to administer a program for resolving disagreements both quickly and inexpensively. The program – which consists of nine neutrals geographically distributed throughout the United States – are on call to resolve disagreements between Toyota and their dealers in the operating regions. Under the program, if a dealer does not agree with Toyota Motor Sales about sales credits, they have seven days to work with their regional office to sort out the disagreement. If they fail to gain agreement, the regional office forwards background information on the disagreement on the eighth calendar day, triggering the involvement of the appropriate Neutral. The process is informal and inexpensive; disputing parties may participate in an arbitration hearing in person, by conference call, or by submission of documents with most



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participating by conference call eliminating travel expense. Each side presents its case within a half-hour period and both the neutral arbitrator and the parties may ask questions. The arbitrator has one week to issue the opinion. Attorneys may not assist disputants in hearings and the arbitrator's decision is binding for Toyota Motor Sales, but not for the dealers.<sup>63</sup>

When the Standing Neutral is given authority as an arbitrator – which typically involves making a binding decision - it can raise the adversarial level of the relationship and can encourage the active participation by adversarial lawyers. In the Toyota example, they mitigate this concern because attorneys are not present – and only Toyota Motor Sales was bound by the decision (not the dealers – who are viewed as the weaker party). Giving more control to the weaker party (dealer) builds the dealers' confidence that the process is fair.

### **5. Partnering Facilitator/Deal Architect**

Organizations involved in highly complex and strategic relationships (e.g., outsourcing relationships) where there can be a risk of creating a contract with misaligned interests or perverse incentives are turning to Standing Neutrals and other neutral parties to help craft their agreement. The University of Tennessee has done significant work to train neutrals through its Certified Deal Architect (CDA) program since 2011.<sup>64</sup> The role of the Certified Deal Architect is to objectively facilitate the parties in crafting a win-win outsourcing agreement best both party's needs.

A good example of a corporation using a neutral party as a coach during the contracting and initial transition process of a large outsourcing deal is the Swedish Telcom Telia.<sup>65</sup> Telia has used the UT Vested® methodology for five of their most complex outsourcing deals, engaging a Certified Deal Architect at Cirio (a Swedish law firm). The cost was split evenly between and the service providers.

When Telia set out to craft a deal with Veolia for facilities management across 16,000+ network sites, the complexity of the deal led them to expand the role of the neutral party to include not just a Certified Deal Architect from Cirio law firm, but also neutrals from EY Advisory to provide support services for a comprehensive project management role which would serve both parties. Together, Cirio law firm and EY's management consultants played the role of a neutral "coach" from concept to creation of the actual agreement. Telia's Andreas Sahlen, Head of Estate Management and Real Estate Law, has commented on the effectiveness of using a Standing Neutral during the contract development phase of a complex contract. "Playing the role of a neutral facilitator was a key part of the CDAs role. It was a good way to build trust and spur innovation."

Telia's Ingrid Wallgren (procurement leader on the deal) noted, "The really good part was that our CDA coach was not sitting on one side. They were on both sides, both supplier and buyer. So, they were really good at handling the facilitator role and not taking one perspective in the different discussions we had. They managed to drive the discussions from both sides very well. And that was good for us."



### Other Innovative Examples

While the above examples represent the most common approaches, there are many other innovative examples of how organizations are effectively using Standing Neutrals in practice.

#### 6. Branding and Licensing Agreement Example

This example involves two parties engaged in a long-term branding and licensing agreement. The example shows how two parties incorporated a Standing Neutral from pre-contracting signing all the way through formal dispute resolution.<sup>66</sup>

In this example, the parties engaged a well-known IP attorney as their Standing Neutral for both pre and post-contract support (a conflict of interest check was performed before formally engaging the attorney). Pre-contract, the Standing Neutral was chartered to review the overall contract language pertaining to IP between the parties to ensure the parties allocated risks realistically. The Standing Neutral was also asked to help the parties embed governance mechanisms into the agreement outlining a formal process for managing issues and concerns, with the goal to prevent disputes. With the Standing Neutral's help, the parties agreed to a formal governance structure with a clear and timely path for managing disagreements. For example, there were formal definitions of what an issue, concern and dispute meant and how a disagreement would flow through each step. As part of the process, the parties embedded a step-negotiation process to facilitate the timely resolution of issues at the lowest possible level with protocols for how and when a disagreement would be escalated to the next level (e.g., from issue to concern or from concern to dispute). Each step was time-bound to encourage timely resolution.

If the parties' governance mechanisms failed to resolve a disagreement, they agreed that the Standing Neutral would act as both a mediator and an arbitrator as needed. First, the Standing Neutral would act as a mediator. If the parties could not come to a solution after a set time frame, the Standing Neutral was given the authority as an arbitrator to make a binding decision. The Standing Neutral was also chartered to provide contract language changes if needed.

The cost of the Standing Neutral was split evenly. The parties never had an issue escalate to a dispute and the Standing Neutral was never called on by the parties to provide a decision or participate in any revision of the contract.

#### 7. Franchise Agreement Example

In a franchise system, the interests of the franchisor and its franchisees must be aligned for the franchise system to be effective. The concept of a Standing Neutral has been adopted successfully for dealing with friction in franchise systems under the term of a "Wise-Persons' Committee" as shown in this Canadian franchise example.

A Wise-Persons' Committee is a permanent (rather than *ad-hoc*) committee whose members are individuals who:

- Have high credibility within the franchise network (that's why they are called "Wise-Persons")
- Are very familiar with the franchise network and can thus recognize where its best interests lie



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- Are not actively involved in the network
- Have no personal interest in the decisions and actions of the franchisor or franchisees or in the substance or outcomes of their recommendations, except for the sole objective of seeing the network succeed while continuing to adhere to its mission and values

Most often, the members of a Wise-Persons' Committee are former franchisees who have achieved success, former franchisor's executives who have gained considerable credibility both among franchisees and with the franchisor, and/or experienced individuals who are, or have been, close to the franchise network.

The members of the Wise-Persons' Committee are appointed by a joint decision of the franchisor and of its franchisees (and not by the franchisor alone). Franchisees must acknowledge that the individuals appointed to the committee are not dependent on the franchisor and have nothing to gain by favoring the franchisor or any other member of the network. A credible and active Wise-Persons' Committee represents the collective consciousness of the franchise network, buttressing its mission and values and its common interests. This is therefore a mechanism that, when properly organized, will afford very useful opportunities, in particular for ironing out problems, differences and disagreements within the network.

The primary role of a Wise-Persons' Committee is to provide, within a short time frame, the opinion of individuals recognized as "wise" and "neutral" to all members of the franchise network (franchisor's executives, franchisees, immediate partners, etc.), on any decision or action (whether by one or more franchisees or by the franchisor) that:

- Creates a problem
- Seems to violate the "relational contract" between the franchisor and its franchisees or the mission and values of the franchise network
- Does not seem primarily in the interests of the franchise network as a whole

A franchisor or one or more franchisees can submit any dispute that arises within the franchise network that the parties cannot resolve themselves. The Wise-Persons' Committee makes recommendations on the reasonable avenues to find a resolution in the best interests of the network. The result of the deliberations of a Wise-Persons' Committee almost always takes the form of recommendations rather than decisions. However, because those recommendations are ordinarily communicated to all the franchisees and to the franchisor, they carry definite weight within the network. If the committee members also have influence over the parties to a dispute (from their expertise and/or reputation within the network), they can also act as conciliators to facilitate a fair, and mutually acceptable, settlement.

Even when no specific situation is put to the Wise-Persons' Committee, it meets regularly to keep up to date on developments within the franchise network and on the opportunities, issues, and challenges that arise along its way. The Committee will thus be prepared to act quickly when necessary, and its recommendations will be correspondingly better and more relevant.





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The experience of the committee members and the fact that they have no stake in the outcome mean they bring a different perspective and can often see the forest rather than just the trees. They are often in a better position to see the longer-term consequences of a dispute for the network and to recommend fresh options for resolving it.

### **8. Outsourcing Agreement Example**

Outsourcing agreements – especially ones that are complex and integrated in nature – are good candidates for a Standing Neutral. This example is from a sole source strategic facilities management outsourcing agreement spanning nearly 70 facility management services in nearly 200 assets.<sup>67</sup> The buying organization initially engaged SIREAS, LLC a global real estate advisory firm to provide consulting for the bid process to help them select a supplier to consolidate the services of over 200 suppliers through the solution design, partner selection, contract negotiation and execution to transition.

SIREAS was initially engaged to represent the buying organization during the bid process. However, through the process, the supplier found value with SIREAS's expertise and integrity and that SIREAS understood the intent of the relationship. Both parties agreed to have SIREAS act as a Standing Neutral during the transition phase, with the cost split 50/50.

The value of using a Standing Neutral provided an almost immediate return on investment (ROI) as the parties got through the common transition issues fairly and expeditiously. For example, in the first quarter, it became apparent that one particular key performance indicator (KPI) outlined in the contract was driving inappropriate behaviors on both sides of the table. Major organizational changes within the client had introduced new players who came from different organizations and were not familiar with the “intent” of the deal and more particularly of the rationale behind the particular KPI. Independently, each party began conversations with the Standing Neutral to express concern (for different reasons) about what was happening with the KPI and the impact it was having on performance and the supplier's fee. After gathering the relevant information, SIREAS brought both parties to the table and facilitated a discussion. The teams were reminded of the original intent of the KPI. They were informed of the challenges each side was facing and the behaviors occurring as each side attempted to resolve their concerns independently. Within a short timeframe, the parties agreed with SIREAS' recommendation to suspend the KPI until the challenges with data collection and reporting could be addressed. Training sessions were delivered for the new players to reinforce the intent of the deal, delineate the desired outcomes, address the appropriate supplier management/client management behavior and define the appropriate action plan to replace the KPI. What normally would have been a negative cycle was resolved equitably and amicably addressing each party's needs.

The success of using a Standing Neutral during the transition phase prompted the companies to expand the use of the Standing Neutral for the full duration of the agreement (five years with multiple extension options). Both parties felt this made sense when considering the complexity and the dollar value of the deal. As such, the Standing Neutral role was permanently embedded into the formal governance structure and escalation processes to provide ongoing advice and guidance relative to effective performance measurement strategies, management of the governance platform, and onboarding training for new managers joining the relationship from either party.

### **9. Real Estate Development Example**

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This next example involves a real estate developer and a hotel chain.<sup>68</sup> The developer would design and build a novel experiment between a luxury hotel and condominiums. The hotel chain would own and operate the hotel once the project was complete.<sup>69</sup> The parties used two specially-designed types of Standing Neutrals to deal with different aspects of the relationship, which included the employment of various “real-time” ADR features, including binding “baseball” arbitration.<sup>§</sup>

The developer wanted to secure all of its financing and commence construction of the project. The buildings that would house the retail and residential portions of the complex had been designed, but unfortunately two signature elements needed for the complex – a luxury hotel and associated condominiums – were not yet designed. The cost and time of completion of every element of the project had to be specified before closing the financing of the entire project. The agreement was essential to both the developer and the hotel chain for two reasons: 1) to specify a firm date of completion of the hotel and condominiums; and, 2) to make sure any unresolved detail of design or construction would not delay the project.

The developer and hotel chain used a creative approach for deploying two Standing Neutrals to enforce compliance with what was essentially an “agreement to agree,” and to make sure that no disputes would delay the delivery date or disrupt the project. The first Standing Neutral was designated as the “Condominium Arbitrator” and the second as the “Development Arbitrator”. These Standing Neutrals would serve similar – but different – functions. However, in both cases the Standing Neutral was empowered as a Standing Arbitrator to ensure timely resolution of any issues.

Having the Condominium Arbitrator made sure that the parties would negotiate and record a Condominium Declaration to define the condominium portion of the overall project so advance sales of condominiums could take place (an essential element in the cash flow financing of the project). The parties selected a Standing Neutral who was a law professor and an expert in condominium law. The parties agreed that if they disagreed about any term and conditions of the Declaration they would present their respective positions and proposed language to the Condominium Arbitrator who would promptly make a binding decision on which party’s language would be used. The Standing Neutral served until the parties completed negotiations and decided on the Condominium Declaration.

The parties successfully negotiated the Condominium Declaration in a timely manner with no disputes, and the Condominium Arbitrator was discharged.

The purpose of having the Development Arbitrator was to make sure that no unresolved disputes would interfere with the achievement of the project’s critical delivery date. For the Development Arbitrator role, the parties chose a construction lawyer familiar with the type of design and construction involved in the hotel project and who was also a well-known expert in dispute prevention and resolution systems. The Development Arbitrator assisted in drafting the contractual Development Arbitrator contract language and served for the entire duration of the project.

The Development Arbitrator portion of the contract required that if the parties disagreed over any element of design or construction of the hotel, they would immediately call on

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<sup>§</sup> See Appendix 1 for an overview of the various types of ADR methods including baseball arbitration



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the Development Arbitrator. The Development Arbitrator would then meet with the parties within five days in a short mediation session to see whether the disagreement could be resolved in real-time. If a real-time resolution didn't happen, the Arbitrator scheduled a hearing to be held within 21 days where the parties presented evidence supporting their respective positions. The Arbitrator then had two days to make a final and binding decision, not subject to appeal. The speed of the arbitration process was enhanced by a requirement that the parties present the dispute to the Development Arbitrator in a "baseball arbitration" or "final offer" format, thus calling for an "up or down" decision on the issue in dispute: "Which party is correct – the Developer or the Hotel Chain?" The process guaranteed that no dispute could go unresolved for over 27 days.

A key part of the process was to keep the Development Arbitrator in the loop during the entire process, ensuring prompt action if necessary. To do this the parties provided the Development Arbitrator with monthly reports and access to the project through a webcam. During the two and a half years it took to complete the design and construction of the building, the Development Arbitrator was on call if there were any disputes.

The results were spectacular, with no disputes for the Development Arbitrator to settle through the formal arbitration process the parties had defined. Throughout the project, the construction schedule was maintained. While the parties occasionally disagreed, they resolved all issues themselves because the process helped them stay on track -

Incorporating the Standing Neutrals helped the parties completed the highly complex and risky project within budget and ahead of schedule. Since no disputes had to be referred to either Standing Neutral, the total overall cost of the two Standing Neutral processes on this massive project was less than .001% of the project costs.

### **10. Labor Services Agreement**

The Vancouver Island Health Authority (Island Health) and Hospitalist case study shows how two parties can leverage a Standing Neutral as a deal architect to help them develop a labor services contract.<sup>70</sup> Between 2000 and 2014 Island Health and the Hospitalists had gone through contentious contract negotiations four times. When their fourth contract expired on June 30, 2014, neither side was optimistic about how negotiations would proceed. An April 2015 *TimesColonist* summing up the situation with the headline, "One year later, no sign of deal for Greater Victoria Hospitalists."

The parties recognized the critical need to build a new relationship and changed personnel in the fall of 2015 to get the relationship back on track. But the relationship was so broken that contract negotiations went into a standstill; neither side knew how to proceed. Simply put, both sides were stuck.

Both parties agreed to send key leaders and stakeholders, including 12 Island Health Administrators and nine Hospitalists, to a three-day "Alignment Workshop" on May 30, 2016, facilitated by a Standing Neutral from The Forefront Group (a Vested Center of Excellence). The parties went on to use the Vested methodology to co-create a win-win agreement – something neither party thought possible before bringing in the Standing Neutral. Participants of the process comment on the effectiveness in a well-documented case study later featured in Harvard Business Review.<sup>71 72</sup>

- ### Wordle After Vested (October 2018)



The last example is from Emmaus International.<sup>73,74</sup> Emmaus International is a solidarity-based non-profit organization acting against poverty and exclusion. It brings together 350 associations in 37 countries, spread over four continents. All member organizations share the same goal: acting against the causes of poverty and as vehicles for social transformation.

- Ensure that the bodies of Emmaus International are true to the spirit of the founding tenets of the organization
- Develop opinions and proposals for resolving disputes between the regional organizations, between one or several national and regional organizations and the Board, disputes within national or regional organizations

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meeting, the Wise-Persons' Committee composed of one member per Region. Its members are natural persons who do not belong to the Board." Any Emmaus International member group can put forward candidates.

The Wise-Persons' Committee is convened by its president who sets the agenda at least one month in advance. The Committee exercises its duties independently of the Board or the Executive Committee. It addresses its recommendations and justified opinions in writing to the Board and can, at the Board's request, make oral presentations.

The Wise-Persons' Committee can have a case submitted to it by the Board, Executive Committee, a regional organization or national organization. The submission must be made in writing with the parties concerned copied in and must detail the initiatives already undertaken without success by the different parties. Once the Committee has received a case, it sends an official confirmation of receipt to the submitting party. The Wise-Persons' Committee can request all necessary paperwork to help them make a recommendation. All the members of Emmaus International have a duty to provide their assistance when called upon. From that point onwards, the Committee must issue its opinions and/or recommendations within five months.

The Committee's decision is based on a majority by its members, with the president of the committee having the deciding vote if a tie occurs. In the event of an opinion about aims and objectives, the submission addressed to the Wise-Persons' Committee should be justified by an explicit reference in writing.

### **12. Outside Director**

Standing Neutrals can also help with problems of corporate governance. An example of such a person could be the dean or experienced faculty member of a local business school who serves as an outside director. The outside director should be paid a director's fee, furnished with the key management reports provided to other directors, and is expected to attend all board meetings, ask questions, participate in discussions, and get a good perspective on the affairs of the company. However, the outside director has a vote only in the case of a disagreement among the "inside" directors, in which case the outside director has the deciding vote.

A good application of using an outside director as a Standing Neutral is when stock ownership is equally divided between two stakeholders. In this case, an outside director can act as a Standing Neutral for resolving deadlocks between equal owners. The Standing Neutral can also be employed in drafting the corporate charter and by-laws that might avoid the later paralysis of a deadlock.

Another application is where half of the shareholders are engaged in management and the other shareholders are not. In this case the firm could establish a five-person Board of Directors, two of whom represent the evenly matched "insiders" and three of whom are highly respected independent "outside" directors. They all function as a real board, and each director has a vote. The advantage of this arrangement is that when two inside directors disagree, it takes the votes of at least two of the three outside directors to carry the vote.

A third example is in a business where there are two stockholders with a great disparity in ownership interests and there is a concern that the majority stockholder will ride



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roughshod over the minority stockholder to the detriment of the company. Here the by-laws could provide for a five-person board of directors; two of whom are appointed by the majority stockholder, one of whom is appointed by the minority stockholder, and two more “outside directors” who are jointly by both stockholders. Under this system, if a disagreement occurs, the majority needs the vote of only one independent director, while the minority needs the vote of both independent directors. This process works well because the independent outside director(s) can control the outcome, creating an incentive for all directors to exercise good judgment and to act reasonably for the best interests of the company.<sup>75</sup>





### PART 5: COSTS/BENEFITS OF USING A STANDING NEUTRAL

As Louis M. Brown – known as the father of preventive law – aptly noted, “It usually costs less to avoid getting into trouble than to pay for getting out of trouble.”<sup>76</sup>

Section 5 gets to the heart of Brown’s advice by focusing on the costs and benefits of using a Standing Neutral.

#### A Hard Look at The Hard Cost of Disputes

While you may never end up in a formal dispute, if you do, it is likely to be costly. How costly can disputes be? Professor Gillian Hadfield compiled some of the best data and estimates about the cost of disputes in her book *Rules for the Flat World*.<sup>77,78</sup> Below are some highlights:

- 2013 National Center for State Courts study (employment lawsuits) – the median cost of an employment lawsuit is \$90,000<sup>79</sup>
- 2012 American Intellectual Property Law (IP patent suits – combined cost of the parties)
  - \$700,000 for cases less than \$1 million
  - \$6 million for cases between \$1 million and \$25 million
  - \$11 million for a case worth over \$ 25 million.
- Kip Viscusi’s Vanderbilt University study (personal injury): 75% of award fees goes to legal fees and costs.

Hadfield cites the high hourly rates of lawyers as just one factor that makes the legal system costly; the time to work through legal processes and costs associated with the “discovery” process is also a significant burden.

Let’s first look at the time involved. According to data from the World Bank’s Doing Business project, the time required to enforce a contract (from the moment the plaintiff sues until payment is made) ranges from about five months in Singapore and seven in New Zealand (best cases) to over four years in Guatemala, Afghanistan, and Suriname (worst cases).<sup>80</sup>

A second cost factor includes the “discovery” process – most commonly used in the United States. Hadfield points to several studies that quantify the high cost of discovery processes, but one that sticks out is an estimate Microsoft provided in a 2011 letter to a federal judicial committee investigating discovery costs, stating that for every page of evidence used in an average case, the company had produced 1,000 pages, manually reviewed 4,500 pages, collected and processed 90,000 pages, and preserved 340,000.

While litigation is expensive, the International Association for Contract and Commercial Management reports that very few contracts actually go to trial. Iva Bozovic and Gillian Hadfield’s research shows contracting professionals report “it is common knowledge that litigation is almost always an empty threat; outside of bet-the-company type settings, it costs too much in legal fees and reputational damage, it takes too long and/or it is too unpredictable.”<sup>81</sup>

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Research shows using ADR techniques reduces costs associated with managing and resolving disputes. Many studies have explored the effectiveness of ADR in reducing the costs of dispute resolution relative to litigation.<sup>82</sup> Estimates of cost savings vary substantially from study to study, depending on the type of ADR process evaluated, the type of cases, the type of intervention, and the local conditions. The World Bank's Doing Business project estimates of the total costs incurred by firms that use an ADR process range from 3 to 50 percent of the costs incurred by firms that go through a court litigation process.<sup>83</sup> The authors' experience is that a Standing Neutral falls in the lowest range.

**Figure 2** illustrates the relative transaction costs of different dispute resolution methods.<sup>84</sup>

**Figure 2: Relative Transaction Costs of Different Methods of Dispute Resolution**

Judicial Proceedings	\$
Arbitration	\$
Mini-Trial	\$\$\$\$\$\$\$\$\$\$\$\$
Mediation	\$\$\$\$\$
Expert Advisory Opinion	\$\$\$
Standing Neutral	\$

While ADR techniques such as arbitration and mediation are more cost-effective than litigation, each step on the road to dispute resolution involves incremental transaction costs. What might start with bringing in an expert advisor on-board can often lead to a mediator that can then progress to an arbitration situation. Kenneth P. Kelsey, Director Commercial Operations for ABB Daimler-Benz Transportation (North America), explains why disputes drag on when not settled quickly:<sup>85</sup>

One reason is that too many organizations are led by far-sighted members of top management and corporate counsels that cannot resist the urge to “protect” their companies at all costs. This can be worsened if an outside legal counsel is happy to put up a healthy fight for their clients in the name of “protecting” their clients at all costs rather than get a swift and fair resolution of issues to preserve peace between business partners. And when this happens, emotions can take over. As emotions soar, pride can prevent a realistic and early resolution of conflict. Finger-pointing and blame kicks in and what is often a difference of opinion sets up a series of “he said/she said” disagreements and each party hunkers down to prove they are “right.” When this happens, disagreements can turn into full-blown disputes that are costly and can cause problems well beyond the costs involved.

Let's look at a real example of how a contract dispute for a City and their local Firefighters Union fell into this trap.

- April 2014: issue raised at the monthly Labor Union staff meeting
- April 2014 – Nov 2014: issue continues to be discussed at monthly meetings with no resolution; parties suggest the issue be addressed through a formal bargaining process as part of the contract renewal
- Nov 2014: City and labor union begin formal contract negotiations



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- July 2015: after failed negotiations, City brings in a labor union expert as a consultant to facilitate discussions with the union
- August 2015: Firefighters Union brings in an expert advisor to help them determine how they will negotiate
- October 2015: City dismissed expert on their side because of no progress
- Nov 2015: Firefighters Union expert advisor suggests mediation, citing the parties are “too far apart”
- Nov 2015: City and Firefighters Union each hire outside counsel to represent them in the mediation
- Jan 2016: Firefighters Union dismisses their expert advisor (can’t afford the advisor and a lawyer)
- Feb 2016: mediation begins
- Nov 2016: mediator suggests arbitration after failed the mediation
- Jan 2017: disgruntled parties sign contract because neither likes going to arbitration
- Jan 2017 to present: Firefighters Union keeps their attorney on retainer, citing lack of trust with the City

The entire resolution process took 44 months and did not get resolved!

Our experience shows it is far too easy for organizations such as the City and Firefighters Union to get sucked into a negative tit-for-tat cycle that spins out of control, adding various costs and time throughout the protracted conflict resolution cycle. These costs include not only direct costs for lawyers, accountants and claims consultants. There are also hidden costs involving inefficiencies, delays, loss of quality, and indirect costs for salaries of the in-house personnel.

Let’s revisit the case of the City and Firefighters Union. Both parties had hard costs associated with expert advisors (on each side) and outside counsel (on each side). Besides the hard costs, the City and the Firefighters Union lost manpower throughout the long and arduous process who spent countless hours in contract negotiations instead of performing duty-related work. In addition, the City bore hard costs associated with paying overtime to backfill the firefighters while they were pulled out of duty during contract negotiating days.

One of the most significant hidden costs is that associated with lost trust in a valuable business relationship as the parties grow tense about an unsettled outcome. These costs add up to what Nobel Laureate Oliver Williamson calls “transaction cost economics.”<sup>86</sup>

### Empirical Evidence of the Benefits of a Standing Neutral

So, are there really benefits of using a Standing Neutral? The answer is an unequivocal YES.

Since the first Dispute Review Board (the classic example of a Standing Neutral) was created in 1975, thousands of construction projects have used Standing Neutrals. While there is limited research outside of the construction industry, the Dispute Review Board Foundation (DRBF) offers significant empirical evidence supporting the benefits of using a Standing Neutral. The



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DRBF has gathered information about dispute boards since 1982; its records show that 1996, the process has been employed on over 2,700 projects, aggregating some \$275 billion in construction costs.<sup>87</sup> The Foundation reports:

- 58% of the projects that used Dispute Review Boards were “dispute free,” with no disputes submitted to the DRB.
- 98.7% of the disputes submitted to a DRB for hearing resulted in settlement of the dispute with no subsequent arbitration or litigation.
- In the handful of cases where a party challenged a DRB decision in arbitration or litigation, most were either not pursued to a conclusion or failed.

Cheryl Chern’s comprehensive research has led to a book, “Chern on Dispute Boards,” now in its third edition. According to Chern, Dispute Boards result in even the most strenuous dispute being resolved with a between a 95% to 99% success rate for preventing costly arbitration and litigation.<sup>88</sup>

The Standing Neutral process, while significantly more streamlined and cost-effective than mediation or arbitration, does have costs. For example, there are initial costs involved in selecting, appointing, and briefing the Standing Neutral. The largest costs are the ongoing costs of periodically keeping the neutral informed about the relationship. However, the costs are relatively minimal when compared to the potential costs of resolving a dispute in litigation, arbitration, or even mediation.

According to the DRBF records, Dispute Boards are remarkably inexpensive, even though most are three-member panels rather than a single neutral. Costs include an hourly rate commensurate with the experience of the neutrals used, plus out-of-pocket expenses. According to two examples cited by the Foundation in its 2019 Manual, total costs for a three-member DB can range from about .01% of final construction contract cost for a \$250 million project to about .24% for a \$600 million project, depending on size, scope and location of the project, along with the number and severity of disputes.<sup>89</sup> In general, “the carrying costs of a dispute board are small, usually in the range of 0.05% to 0.15% of project costs...The cost of a DB will deliver a positive return on investment as a result of faster project project-delivery times, the minimization of cost overruns, the prevention of most disputes and a much lower cost of resolution for unavoidable disputes.”<sup>90</sup>

Perhaps the greatest source of cost savings from using a Standing Neutral is the beneficial side effect of reducing – and perhaps eliminating – disputes. As shown in Part 2, the sheer presence of a neutral third-party promotes “self-monitoring” behaviors that prevent the gamesmanship that can often spiral into a series of negative tit-for-tat reactions that lessen trust such as seen in the City and Firefighters Union.



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### Non-Cost Benefits of Using a Standing Neutral

The following outlines many of the common-sense non-cost benefits from using a Standing Neutral.

#### **Reduced Time to Resolve Issues**

Common sense indicates the longer it takes to resolve a disagreement, the more emotionally attached an organization gets to their “position.” And the longer the issue goes on, the greater the costs – especially for those issues that turn into a formal dispute or litigation. As such, the primary benefit of deploying a Standing Neutral is a significant reduction in the time to resolve an issue. How?

The Standing Neutral is “standing.” He/she is integrated into the ongoing governance of the relationship. This gives them an advantage over a mediator or arbitrator who typically has a very challenging role. When a mediator or arbitrator is brought in, he/she faces a situation where the parties may be emotionally charged as the result of protracted, unsuccessful negotiations before the mediator got involved. By the time the parties get to mediation or arbitration, they are almost always entrenched in their positions. In mediation, one of the first objectives of a mediator has to be to 'de-energize' the situation and focus the parties on the real problem and real solutions; not who is at fault. Also, an ad-hoc mediator does not have the history with the parties, which adds to the cost to get up to speed.

#### **Improved Clarity and Alignment**

A Standing Neutral can improve clarity and alignment – especially when used during the pre-contract phase of a relationship. Let's take the case of Telia – the Swedish Telcom who used a Standing Neutral for implementing a Vested outsourcing agreement with their supplier Veolia. The outsourcing agreement was vast – spanning multiple facilities and maintenance services in over 16,000 locations across the Nordics. The Standing Neutral helped the parties to fairly define the scope and baseline of the agreement and clearly articulate the desired outcomes, objectives and measures included in the actual contract.

Sebastian Hamlund, Business Developer for Veolia, was thankful for the education and coaching provided by their neutral Certified Deal Architect, Cirio law firm's Erik Linnarsson. “Erik helped both Telia and Veolia define how we are going to behave in this future contract. That made us really secure. We began to see how we would measure success and how we as a supplier could become successful under a Vested model.”

Using a Standing Neutral also provides an objective view and coaching with tough discussions like pricing. Hamlund credits their coaching sessions with Cirio and EY for helping them make the mindset shift.

“The pricing model was where Telia and Veolia made the leap from a conventional, transactional “price” approach to a pricing model with incentives. The education differed greatly from the old way of doing things, particularly regarding pricing. Cirio and EY were really, really great in helping to keep us stay focused on how Vested grows the pie and shares the pie mindset as we set out to create the pricing model. Usually when we get a new contract we focus a lot on the ‘how’ and ‘price’ – trying to translate the customer's work into how we are going to make money, and what we are going to do to make up the money if we end up on the short end of the stick in pricing negotiations. Vested was

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different. Erik reminded us of our commitments and how we needed to behave and that made us really secure.”<sup>91</sup>

### Improved Collaboration and Trust

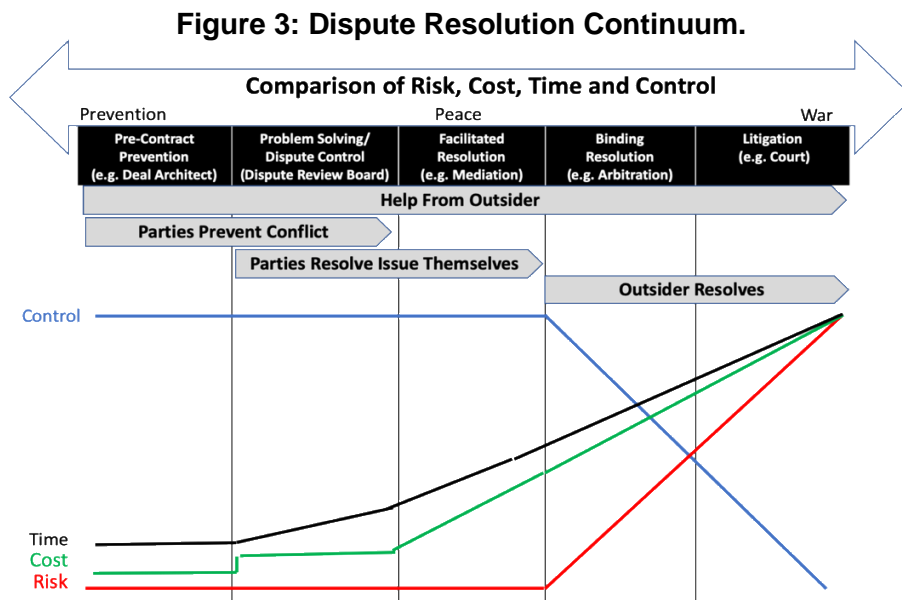
The third benefit is hard to quantify: the value of increased collaboration and trust due to more proactive and preventive communications. Using a Standing Neutral helps preserve cooperative relationships between the contracting parties. A Standing Neutral is used very early when parties are in misalignment. The highly collaborative nature allows the parties to construct their own solutions to problems, strengthening their relationship and creating trust and confidence. In short, it helps teach the organizations how to use transparency and fact-based problem-solving versus more conventional negotiation approaches when looking at differences in opinion.

A case in point is in the Island Health and the Hospitalist example featured in Part 4 – Examples in Action. Using a Standing Neutral increased trust levels between the parties by over 84%. In addition, it helped the parties get to what most thought was impossible – a win-win agreement especially given the fact the parties were at a virtual standstill in contract negotiations.

It is critical to also highlight what is set out above: the appointment of the Standing Neutral typically implies that the costs of the Standing Neutral(s) are split evenly between the parties, so each party is equally invested in the relationship and thereby improves trust in the neutral(s).

### Dispute Resolution Continuum: Comparison of Cost, Risk, Control, Time

**Figure 1** (see Part 4) introduced examples of how contracting parties are using different types of Standing Neutrals across a continuum ranging from preventive in nature to one that is more formal and binding. In **Figure 3** (below) we expand on the notion of the continuum showing how cost, risk, time and control of a dispute increase along the continuum. Each is discussed in more detail below, showing how an emphasis on prevention and facilitated early resolution can generate significant benefits.







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**Control and Risk** - Arbitration is often characterized as a "split the baby" kind of dispute resolution process and as such, it is not uncommon for each party to be dissatisfied with the outcome.<sup>92</sup> A benefit of using a Standing Neutral or mediation is the parties themselves arrive at the solution; therefore, there is a high probability that the solution will be carried out as agreed. In that respect both have the same benefit of high control and low risk.

**Costs** – The cost of using a Standing Neutral or a mediator is typically split between the parties. The authors' experience shows that the total cost of dispute resolution is less when using a Standing Neutral versus a mediation. Why? Mediation often involves a costly discovery process, but a Standing Neutral doesn't require discovery because the Standing Neutral is already familiar with the facts. Also, mediation nearly always involves lawyers (like in the Firefighter's example) while the Standing Neutral process is a party-driven process that discourages the use of lawyers

Many perceive the cost of a Standing Neutral is higher than that of a mediator because the cost of using a Standing Neutral is incurred as part of ongoing governance support throughout the life of the relationship while a mediator is only brought in once there is a dispute. Because typical fees for Standing Neutral and mediator are about the same, it gives the illusion that the cost of using mediation is less because the parties "only pay for what you use." However, the authors' experience shows this is not true, because using a mediator greatly increases the time and other costs associated to get to a resolution. While mediation has proven effective in resolving otherwise intractable disputes, it usually occurs only after the parties have expended considerable resources attempting to resolve the dispute. Further, getting to the installation of a mediator and getting on their schedule can take significant time. In addition, a mediator not involved in an ongoing nature with the parties lacks relational knowledge and familiarity and almost always has costs associated with "ramp up" time. Last, the mediation process is often adversarial and includes lawyers, which can drag out the mediation process, such as the case of the City and the Firefighters Union dispute.

**Time** - Because a Standing Neutral is embedded in the relationship (or on standby) the time to resolve disagreements is greatly reduced. Also, the non-adversarial nature (e.g., a Standing Neutral is viewed as "mutual friend" or "referee" or "the glue"), means the parties gain alignment before a disagreement turns into a dispute that goes to a mediator. As mentioned previously, research shows embedding a neutral in the relationship enables "self-monitoring" and often prevents disputes.

### Funding Your Standing Neutral

It is important to reiterate a Standing Neutral is a *jointly* funded resource. This ensures the Standing Neutral works on behalf of the parties equally in helping the parties prevent any issues and resolve ones that have resolved. Often the cost of a Standing Neutral can be budgeted for – especially when using modern Standing Neutrals formally embedded into an ongoing governance forum such as in an outsourcing agreement or a project administration for a construction project.

The cost of a Standing Neutral varies based on their role, frequency of use, and the number of neutrals used (e.g., a single neutral is less expensive than a panel of three

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neutrals). Standing Neutrals are typically paid an hourly rate commensurate with their expertise.

When using a Standing Neutral post-contract signing, the key is to include the Standing Neutral early enough he/she provides timely and effective issue mitigation and resolution. While there is not a “right” answer for how frequent or early to embed a Standing Neutral, most organizations find using a single Standing Neutral can be effective when placed at the mid-tier governance framework (not the lowest level). For example, in an outsourcing agreement the Standing Neutral would likely not join weekly operational meetings, but would attend more strategic governance forums such as a quarterly business review or perhaps monthly management reviews.

When using a Standing Neutral pre-contract signing (such as when using a Deal Architect to assist with the design and contracting of a strategic partnership), the cost of a Standing Neutral is typically commensurate with the size of the deal and level of support the parties need. The larger, more complex and risky a potential deal, the more parties should expect to pay a Deal Architect. Faculty leading the University of Tennessee’s Certified Deal Architect (CDA) program suggest that organizations consider using a neutral CDA on any complex deal or when the parties are seeking to create a Vested relationship for the first time.



### CONCLUSION: THE MAKING OF A MOVEMENT

While Louis Brown is credited as the founding father of “preventive law,” his early work inspired a growing cadre of followers who have researched and expanded on every facet of the concept of preventing disputes. Today there is a clear and unmistakable evolving trend toward incorporating proactive approaches for preventing and managing disputes into all business relationships. This recent trend is aptly termed “the Prevention Movement.”

The use of a Standing Neutral in business relationships – especially a modern Standing Neutral who focuses on helping the parties stay in continual alignment – proves the adage “An ounce of prevention is worth a pound of cure.”

While there are skeptics, the Prevention Movement is taking hold as evidenced at the 2017-2018 Global Pound Conferences held worldwide. During the conference major stakeholders in the dispute resolution field (users of dispute resolution services, their advisors and lawyers, providers of both adjudicatory and non-adjudicatory services, and the researchers and educators who influence the users of dispute resolution services) revealed the following consensus:

- Dispute resolution should be conceived and practiced earlier in the trajectory of risks that can develop into conflict, escalating from differences of opinion to arguments, aggression, and finally disputes that have to be dealt with through formal dispute resolution efforts
- Pre-dispute or pre-escalation techniques are the most promising and valuable methods for improving the future of dispute resolution and should prevent disputes
- Where possible, risks should be understood and addressed in advance so problems never arise
- Where efforts to prevent problems fail, steps should be initiated to de-escalated, contain, or provide “real-time” resolution of conflicts so the costs, hostilities and delays of formal dispute resolution can be avoided.

The conclusions from the Global Pound Conferences demonstrate that the Prevention Movement is no longer just an aspiration of a few visionaries, but one seen as needed in today’s modern economy.

Our goal for this white paper was to provide a comprehensive overview of the why, what and how of using a Standing Neutral. We hope the examples we have shared inspire how a Standing Neutral can be incorporated into all facets of a business relationship – ranging from pre-contract signing all the way through formal dispute resolution techniques much more effective than traditional mediation and arbitration.

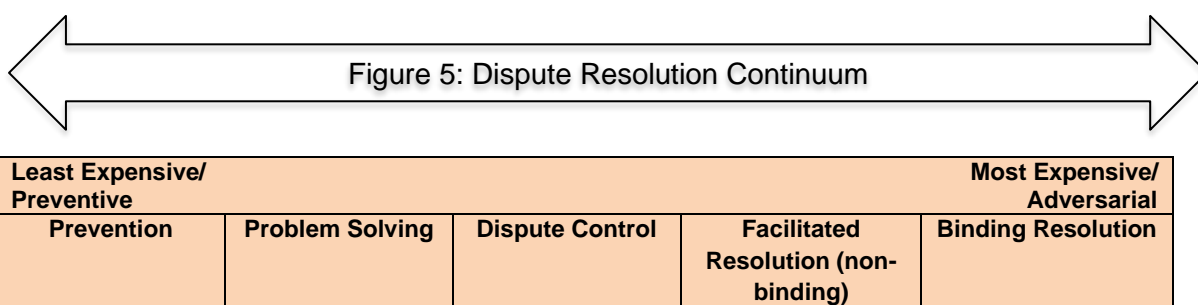
We challenge you to join the Prevention Movement and incorporate a Standing Neutral into your strategic relationships. To learn more, read on in the Appendix for a deeper dive.



## APPENDIX 1: DESIGNING A DISPUTE PREVENTION, DE-ESCALATION AND RESOLUTION SYSTEM

Designing a dispute prevention, de-escalation and resolution system should be the backbone of every relationship's prevention effort. In fact, the authors view it as so essential we recommend your system is formally embedded (such as shared in the NCR example in Part 4) which requires all of its commercial contracts to include a clause specifying ADR as the first, preferred method of settlement should a disagreement arise.

There are many ADR techniques and approaches for preventing, controlling and resolving disputes; ADR methods fall along a continuum ranging from preventive in nature to formal dispute resolution techniques such as arbitration or mediation. Within the continuum, there are five categories (**Figure 5**).



This Appendix summarizes the most popular methods for each category – from least adversarial and costly to most adversarial and costly. Use this Appendix to help you design your dispute prevention, de-escalation and resolution system.

### Characteristics of a Good System

Since problems and potential disputes can occur in many different ways and times during a relationship, no one size of dispute resolution mechanism fits all problems and disputes. We suggest three design characteristics.

First, a good dispute prevention, de-escalation and resolution system anticipates the problems and disputes most likely to occur and designs a system of techniques, controls, filters, and dispute resolution devices that will ensure that all disputes are promptly and realistically dealt with by the parties and resolved quickly in the most efficient possible manner.

Second, a good system uses a “stepped” approach, with parties agreeing on a series of techniques that:

- Establishes a cooperative relationship which will help to prevent problems from arising
- Sets up processes that will de-escalate disagreements
- Provides real-time techniques designed to resolve any disputes immediately
- Provides for a neutral-assisted form of consensual dispute resolution such as mediation if these techniques do not resolve all disputes

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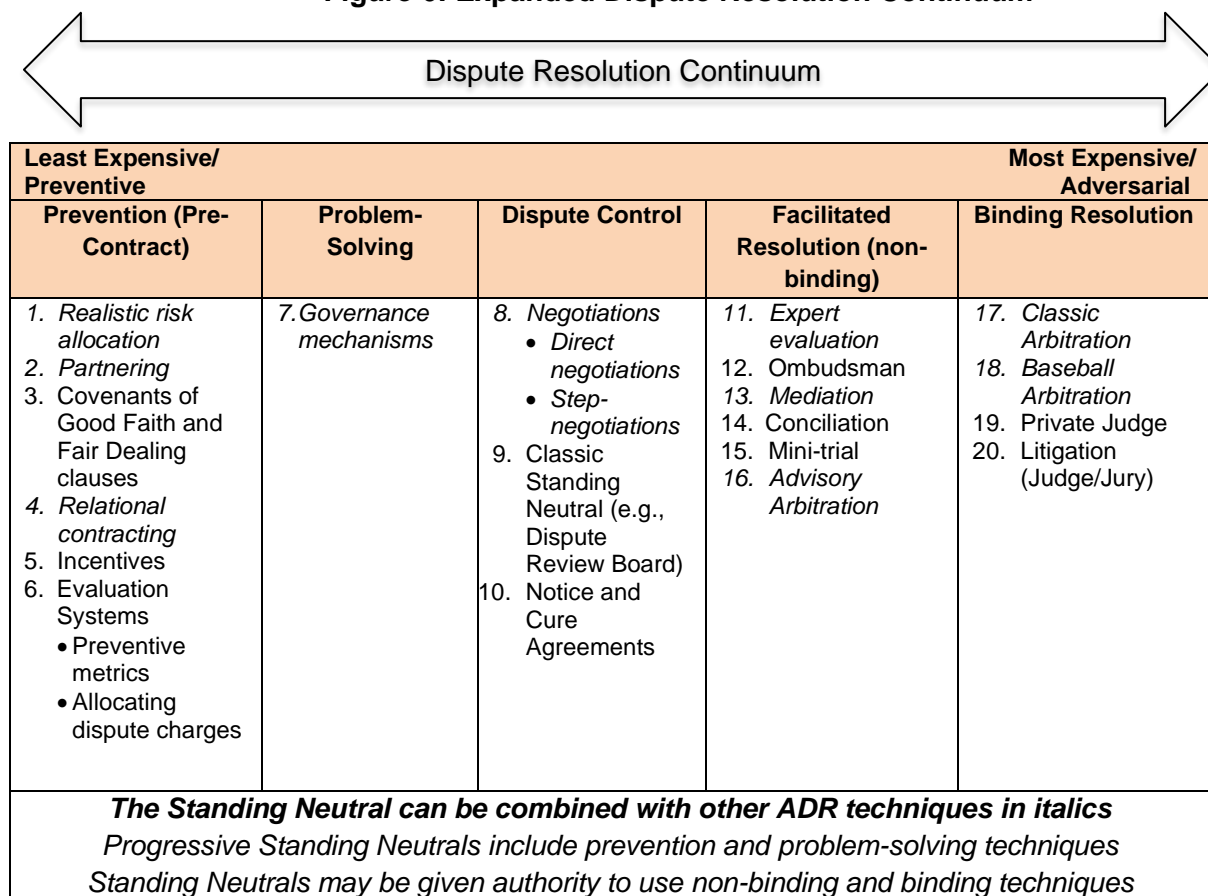
- Includes a backstop method of achieving final and binding resolution, such as arbitration before expert arbitrators

Third, a good system should be agreed on at the beginning of the relationship and is ideally formally embedded into a contract through including ADR clauses and processes, often in a formal Contract Schedule. Formally incorporating a dispute prevention, de-escalation and resolution system acknowledges the reality that problems and disputes will occur and enables the parties to agree on the most effective techniques for their relationship before there are any issues.

### Types of ADR Techniques

As mentioned previously, ADR techniques fall into five categories ranging from preventive in nature to formal dispute resolution techniques such as mediation and arbitration. **Figure 6** below shares an expanded dispute resolution continuum. The first 19 items are all considered forms of ADR. Preventive techniques are the lowest cost and most effective techniques and should be a key part of any dispute prevention and resolution system. Each item is profiled as part of this Appendix.

**Figure 6: Expanded Dispute Resolution Continuum**





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The elements of a Standing Neutral (early mutual selection, continuous involvement, and real-time and prompt action) can be combined with many of the ADR techniques such as the Standing Mediator, and a Standing Arbitrator explained in Part 4. Regardless of which preventive conflict resolutions tools are used, one thing is certain; the parties should agree on which tools they will use, and how they will use them, **before** any disagreements or formal disputes arise. This way the parties have agreed on *how* they will de-escalate when and if they need to. Ideally, contracting parties determine this *during* the contracting process itself.

Each ADR method is profiled in this Appendix.

### Prevention Techniques

Problem prevention techniques are implemented during the planning stages of a business relationship to proactively structure the relationship in ways that avoid many problems. Many problem prevention techniques build trust through transparent and collaborative approaches designed to lay a strong foundation for a healthy and aligned relationship.

#### 1. Realistic Risk Allocation

Realistic risk allocation helps prevent problems by assigning each potential risk of the business relationship to the party best able to manage, control or insure against the particular risk.

Realistic risk allocation is a common sense, business-focused approach for mitigating risks. Unfortunately, this fundamental principle of good business management and dispute prevention practice is not widely recognized or understood. Procurement professionals and lawyers are often encouraged to “shift risk” – especially in supplier relationships – in the pursuit of getting the “best possible deal.” This can create problems of a magnitude far greater than any temporary benefit of “winning” during contracting negotiations.

When parties do not allocate risk appropriately, it can create undue stress and impose an ill-placed risk to a party not equipped to handle the risk. It can increase costs, sow the seeds of countless potential disputes, create distrust and resentment, and establish adversarial relationships that likely will interfere with the success of the business enterprise.

In multiple-party relationships such as construction projects, realistic assignments of risk are important to the maintenance of healthy relationships and to control costs. In the classic multi-party example of a construction project, an owner’s use of superior bargaining power to shift risks unrealistically to another party typically creates a chain reaction of cost inflation, resentment, downstream risk-shifting, defensive and retaliatory tactics, and misunderstandings caused by different perceptions as to the enforceability of some risk-shifting provisions. The result is usually adversarial relationships, disputes and claims, which could have been avoided by intelligent sharing of risks.

Usually it will be obvious that certain risks logically should be assigned to a particular party. However, in other cases either party can handle other risks equally well or some risks might not be effectively handled or even insured against by either party. In those cases, the assignment of those risks must be dealt with through bargaining, likely reflected in the economic terms of the deal.





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Standing Neutrals engaged as Deal Architects (such as in the Telia example in Part 4) often incorporate realistic risk allocation into the contracting process.

### 2. Partnering

Partnering is a team-building effort in which the parties purposefully establish cooperative working relationships. Partnering is effective in both long-term relationships and project-specific relationships. Standing Neutrals engaged as Deal Architects (such as in the Telia example in Part 4) often incorporate partnering contracting process.

The goal of partnering is to create a collaborative environment and foster trust early in the relationship. Common partnering techniques involve creating common goals and seeking to understand the parties' individual expectations and values. The expected benefits from partnering activities include improved efficiencies and cost effectiveness, increased opportunity for innovation, and continual improvement of quality products and services.

Partnering ideally is instituted at the beginning of the relationship and often includes holding a retreat among key personnel involved in the project/relationship. Partnering activities work best when the parties bring in an independent facilitator who uses facilitative teaming to initiate open communications and help the parties develop non-adversarial processes for resolving potential problems, in much the way the Standing Neutral did in the branding and IP relationship example in Part 4.

While partnering is ideally done at the onset of a relationship, partnering can occur at any time in a relationship. The Vested outsourcing methodology is an excellent partnering methodology designed specifically to help parties lay the foundation for strong and healthy relationships. The Vested methodology embeds most of the preventive ADR techniques into the contract and governance structures intending to keep long-term outsourcing relationships operating at the least possible friction and transaction costs between the buyer and service provider.

### 3. Covenants of Good Faith and Fair Dealing clauses

Covenants of Good Faith and Fair Dealing clauses obligate contracting parties to deal with each other honestly, fairly, and in good faith with the intent to not destroy the right of the other party or parties to receive the benefits of the contract. The laws of many jurisdictions impose an implied obligation of good faith and fair dealing in every contract. However, parties can formally and explicitly include good faith provisions in their contract. Doing so increases the parties' obligation to make fair decisions – even if it may contrast with the stated letter of the contract.

For example, below is a sample clause:

*The parties, with a positive commitment to honesty and integrity, agree to these mutual duties:*

- 1) Each party will act in good faith and engage in fair dealing*
- 2) Each will assist in the other's performance*
- 3) Each will avoid hindering the other's performance*
- 4) Each will fulfill its obligations diligently*
- 5) Each will cooperate in the common endeavor of the contract*



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Good faith clauses can also be unique clauses targeted at setting specific direction to those who may find themselves in a dispute. For example, below is a sample good faith negotiation clause.

*The parties will attempt in good faith to promptly resolve any controversy or claim arising out of or relating to this agreement by negotiation between representatives of the parties with the authority to settle the controversy.*

Explicitly including good faith and fair dealing clauses are important in long-term business relationships where the contract as stated may not be in step with the changing business conditions. Of course, parties should always document their decision-making and alternatives considered, communicate with the affected parties and explain the reasons for the considered decision. This is an important exercise because it provides a sounding board for the decision.<sup>93</sup>

### 4. Relational Contracting

Relational contracting is similar in intent to having good faith and fair dealings clauses; however, it is much more in-depth. For example, a relational contract obligates the parties to rational behavior by establishing *relationship* rules, not just the business and legal aspects of the contract. IACCM and the University of Tennessee are strong advocates for relational contracting practices and offer an excellent white paper *Unpacking Relational Contracting: The Practitioner's Go-To Guide for Understanding Relational Contracts*.<sup>94</sup>

Unlike the simple good faith clauses noted above, a good relational contract embeds a formal “Statement of Intent” into the contract that includes a jointly developed shared vision, guiding principles and citing the intended behaviors desired as part of the relationship. Relational contracts are ideal for long-term contracts operating in a dynamic environment where the contract requirements specified on day one of the contract will likely not be the exact needs in the future. The parties are obligated to “live into their intentions” to fill in any gaps, errors or omissions in the agreement. A well-designed relational contract incorporates relational governance mechanisms into the formal agreement to obligate the parties to effectively manage the relationship proactively (see governance techniques outlined previously).

Relational contracts always recognize the inevitability and need for change by including a specific “changes control” clause and a process to fairly address changes that need to take place.

### 5. Incentives

Incentives that encourage cooperation can be a useful tool to align interests between two contracting parties. Well-conceived positive incentive programs align goals, can encourage superior performance, and discourage conflict. Incentives can take many forms. In one construction industry example, the leader of a multi-party enterprise established a bonus pool that, upon attainment of specific goals, shared incentives among the organizations with whom the leader contracts. Under such a system the bonus is payable only if these participants as a group meet the assigned goals; the bonus is paid either to everyone or to no one. This device provides a powerful incentive for the participants to work cooperatively with each other, and reduces conflicts that might occur in a common enterprise when every participant might otherwise be motivated solely by their limited perception of their short-term interests, rather than the success of the

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enterprise as a whole. Well thought out incentives encourage participants to subordinate individual interests to legitimate needs and success, ultimately to benefit all project participants.

The University of Tennessee's Vested methodology includes the use of monetary and non-monetary incentives to align interests in long term complex contracts. For example, **Figure 7** shows how Intel incentivizes DHL with both a gainshare (shared % of savings) and automatic contract extensions for good performance.<sup>95</sup>

Desired Outcome	Standard / Measure	Incentives
Increase Cost Savings	Annual target of (%)	% of Savings
Improve Delivery Performance	Maintain adjusted average annual OTD goal (98%) and raw OTD goal (96%). Improve CDD by 2%.	Automatic contract extension if target met & saving goal was achieved
Reduce Shipment Damage	Maintain outbound DPM annual average of 1,388. Improve severe inbound damage to <0.9% average in last quarter of year.	
Maintain Safety Scores	Determine goal based upon new safety measurement criteria. Measure for 1 quarter then determine target.	
Maintain Intel Customer Satisfaction Score	Maintain score of <1% per month and 2.0 flexibility points from SRC. Team to adjust goals after Q1.	

**Figure 7: Incentive Framework for an Outsourced Logistics Contract**

### 6. Evaluation Systems

Evaluation methods can measure the effectiveness of the various types of ADR, to help educate an organization on how to best use ADR techniques. We outline two evaluation methods below:

*Measuring lawsuits prevented vs lawsuits won* drives the preventive thinking for those responsible for managing and mitigating contracting risk. NCR, AT&T, US WEST, BankAmerica and Chevron have all changed their evaluation systems to being preventive, evaluating lawyers, contract managers, and paralegals not merely on lawsuits won or lost but also on disputes avoided, costs saved, and the crafting of solutions that preserve or even enhance existing relationships. The legal departments in these organizations use quantified measures and objectives to reduce systematically the number of lawsuits pending, the time and money spent on each conflict, and financial exposure. Because of this attention, NCR closes over 60% of filed cases within a year after they are opened.<sup>96</sup>

*Allocating dispute charges* to the budget of the department that generated the dispute is an effective technique for educating organizations and individuals about the true costs of



the dispute. When individuals understand transaction costs, they often make decisions such as seeing the merit of investing in preventive techniques such as a Standing Neutral.

### Problem-Solving Techniques

Problem-solving tools help parties deal constructively with problems that can arise, but have not arisen yet. There are many forms of problem-solving techniques – both contractual and operational. Some of the more popular are profiled below.

#### 7. Governance Mechanisms

Governance mechanisms are one of the most powerful tools in the preventive law toolkit. Governance mechanisms outline how the parties should manage all aspects of the relationship. Governance mechanisms fall into four broad categories:

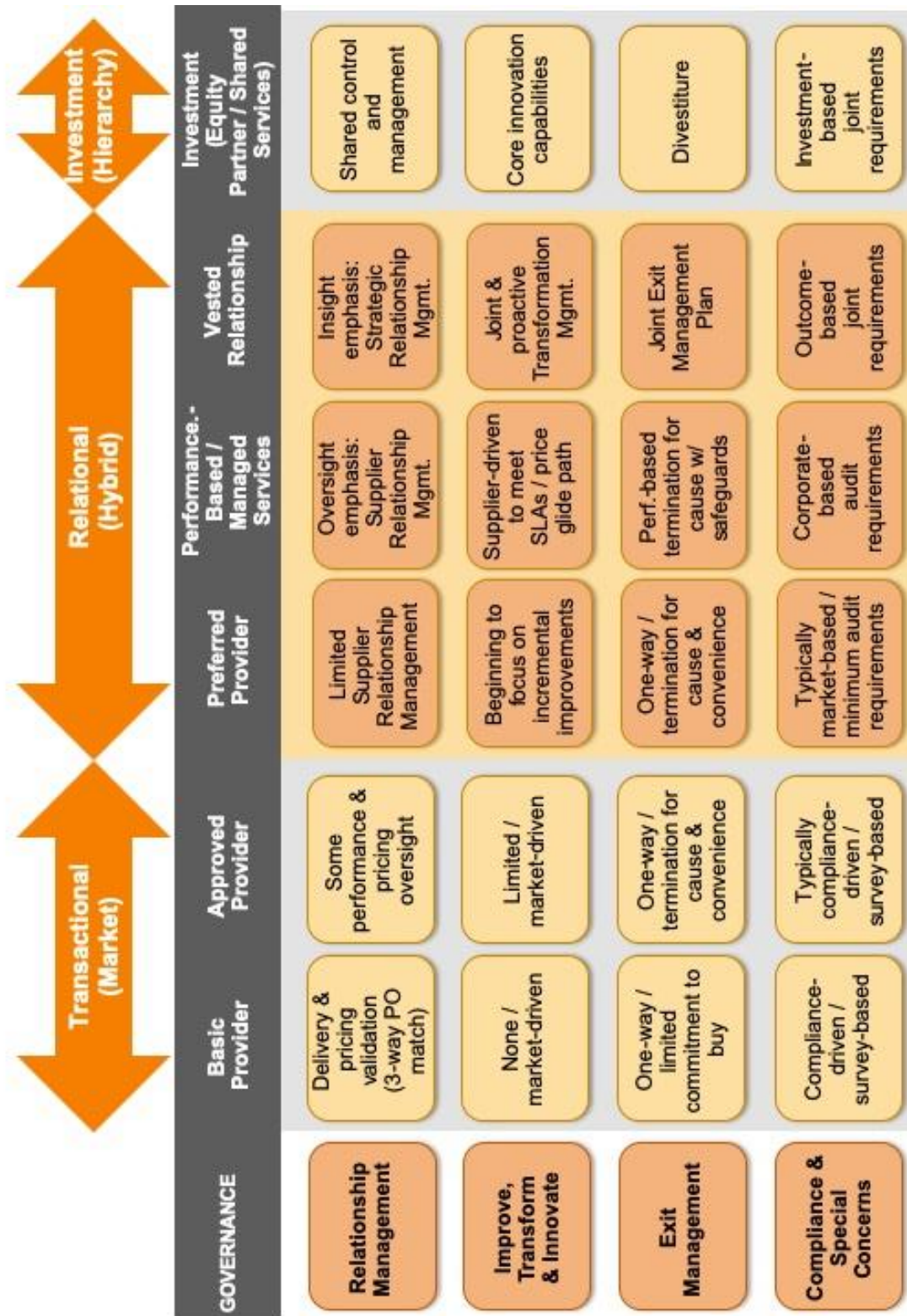
- 1) How to manage the relationship
- 2) How to manage change (both contractual change management, continuous improvement, and larger-scale transformation/innovation)
- 3) How to manage a potential exit
- 4) How to manage compliance and regulatory concerns

Governance mechanisms should vary based on the nature of the business relationship. For example, simple transactional agreements should have basic governance provisions while a large and complex outsourcing relationship should have sophisticated governance mechanisms such as a formal tiered governance structure with peer-to-peer (two-in-a-Box relationships) across separate functional roles. Larger deals may have one or more full-time individuals dedicated to managing the business. The book *Strategic Sourcing in the New Economy* provides high-level guidance on how the mindset of governance should evolve across different sourcing business models.<sup>97</sup> (see **Figure 8**)



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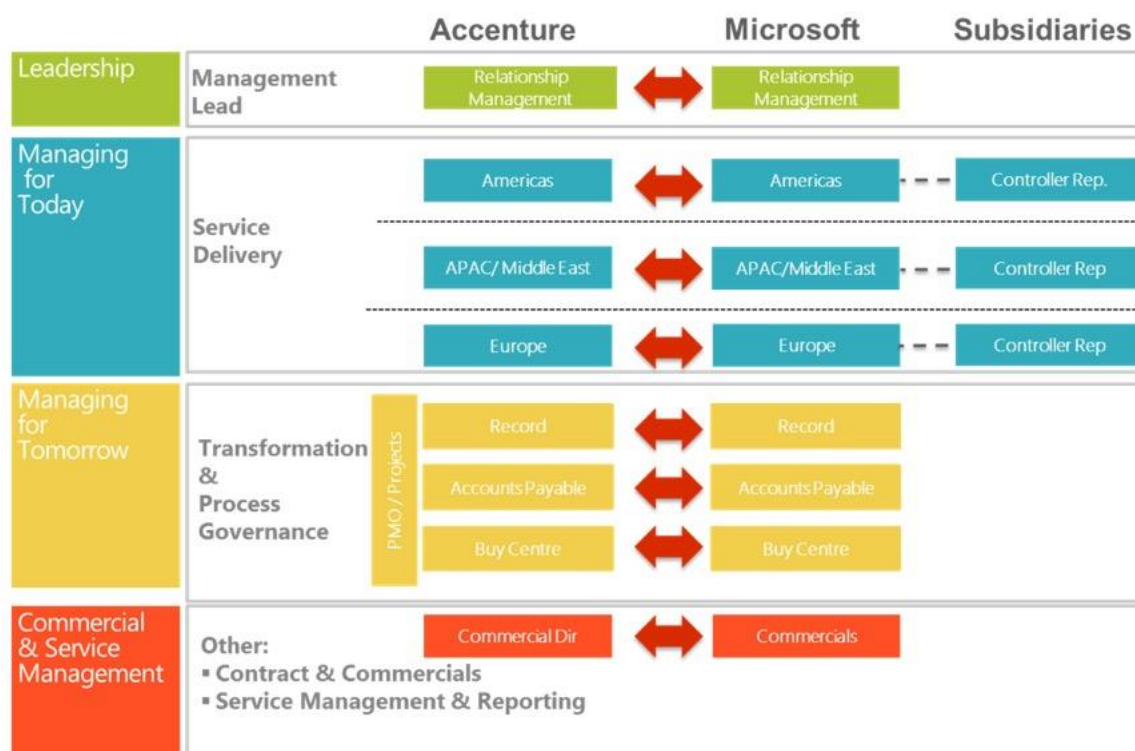
Figure 8: Suggested Governance Mechanisms for Each Sourcing Business Model



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A good example of a governance structure for a large successful outsourcing agreement is Microsoft–Accenture with 16 full-time people managing their back-office finance/operational outsourcing relationship – which spans 116 subsidiaries.<sup>98</sup> (see Figure 9)

**Figure 9: Microsoft–Accenture Governance Structure**



Standing Neutrals playing the role of pre-contract Deal Architect often help the parties incorporate notice and cure agreements into their contract.

### 8. Negotiation

Negotiation is the most common technique and is almost always attempted first to resolve a dispute. The main advantage of this form of dispute settlement is that it allows the parties to control the process and the solution themselves. There are hundreds (if not thousands) of books on negotiating. Negotiations strategies range from adversarial to win-win, with book titles sharing how to *Start with No*, *Getting to Yes*, and *Getting to We*. We advocate for transparent, win-win negotiation philosophies – especially with large, complex and strategic long-term relationships.

*Step-Negotiation* is a form of negotiation. It is an excellent negotiation practice where individuals at the lowest level in each organization are encouraged to solve issues promptly when they arrive. If these individuals cannot resolve a problem at their level promptly, their immediate superiors, who are not as closely identified with the problem, are then asked to confer and try to resolve the problem; if *they* fail, the problem is then escalated to higher management in each organization. Because of an intermediate





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manager's interest in keeping potentially messy problems from bothering higher management, and in demonstrating to higher management the manager's ability to solve problems, there is a built-in incentive to resolve disputes before they ever have to go to the highest management level.

The most effective step-negotiations processes have pre-agreed timeframes to encourage a speedy resolution. Without a timeframe, step-negotiations processes often stall because the lower-level individuals “churn” in their efforts for fear of being seen as a failure in their ability to solve problems. When lower levels churn in a step-negotiation process, the result is almost always increased friction (e.g., the blister on the foot getting infected). The Toyota example shared previously used a step-negotiation coupled with a timeframe. In large or complex outsourcing contracts, a good practice is to have a three-tier governance structure and to use a “two-in-a-box” (peer-to-peer) approach where the tier that first has the disagreement seeks to resolve it.

### 9. Classic Standing Neutral

The conventional approach for a Standing Neutral focuses on dispute control post-contract signing – most commonly helping parties “keep the peace” on a “real-time” basis during the course of a contract such as with a Dispute Review Board. However, the role of Standing Neutral can vary widely as shown in Part 4.

A key part of the Standing Neutral process is for the parties to determine the

- Number of Standing Neutrals (one or three as in Dispute Resolution Boards)
- Role (which range from serving as a strictly facilitative role to an adjudicative role such as a Standing Arbitrator)
- Neutral's fact-finding latitude
- Whether the Standing Neutral's recommendation should be binding or non-binding

Based on the decisions above, there are many variations of how a Standing Neutral works in practice. For example, the Standing Neutral role can be expanded beyond the traditional dispute control to support parties with prevention, problem-solving and formal dispute resolution. The most common variations include the Standing Mediator and Standing Arbitrator. Most recently, organizations have been using a Standing Neutral in the role of a Deal Architect during pre-contract signing. When this is done the Standing Neutral often incorporates pre-contract ADR techniques.

### 10. Notice and Cure Agreements

Notice and cure agreements are contract clauses designed to call attention to possible contract violations and provide an opportunity to correct them. The notice should outline the process for how each party is informed of a potential breach and the offending party typically has a fixed amount of time to cure (or fix) the problem causing the breach. Well thought out notice and cure agreements give the parties “rules” and “instructions” for formally communicating perceived breach of contract issues.

Standing Neutrals playing the role of pre-contract Deal Architect often help the parties incorporate notice and cure agreements into their contract.



### Facilitated Resolution Techniques (Non-Binding)

#### 11. Expert Evaluation

Expert evaluation is a process in which the parties use an expert who provides a balanced and unbiased evaluation of the dispute and offers an opinion and/or recommendation. An expert evaluator is a professional in the specific field (e.g., construction, facilities management, IT) and may or may not be an attorney. If an attorney, they may provide an opinion about the likely outcome of a trial.

Standing Neutrals may also provide expert evaluation. The real estate development example in Part 4 is an example of how the Standing Neutral was both an expert and an attorney.

#### 12. Ombudsman

An ombudsman is a person (or office) chartered to investigate disputes. An ombudsman often issues nonbinding reports, with recommendations addressing problems or future improvements deemed desirable. Both the Army Materiel Command (AMC) and NASA use an ombudsman to resolve problems as part of the acquisition process. The ombudsman investigates reported complaints or requests for assistance from business/industry, and ensures that proper action is taken. Working directly for the commander, the ombudsman can cut through organizational "red tape" and improve the command problem-solving process.<sup>99</sup>

NCR and AT&T use an ombudsman to analyze each dispute at the outset to assess objectively the financial exposure posed by the claim. The written analysis, distributed to management, includes an ADR plan and suggestions on how to strengthen the relationship with the opponent. If the case can be handled through ADR at or below the calculated risk-exposure level, the company will resolve it without litigation. The overall aim is to resolve the contention efficiently with little expenditure of time and money.<sup>100</sup>

#### 13. Mediation

The American Bar Association (ABA) defines mediation as:<sup>101</sup>

"A private process where a neutral third person called a mediator helps the parties discuss and try to resolve the dispute. The parties have the opportunity to describe the issues, discuss their interests, understandings, and feelings; provide each other with information and explore ideas for the resolution of the dispute. While courts can mandate that certain cases go to mediation, the process remains voluntary in that the parties are not required to come to agreement. The mediator does not have the power to make a decision for the parties, but can help the parties find a mutually acceptable resolution. The only people who can resolve the dispute in mediation are the parties themselves."

The ABA augments the definition, by explaining "There are a number of different ways that a mediation can proceed. Most mediations start with the parties together in a joint session. The mediator will describe how the process works, will explain the mediator's role and will help establish ground rules and an agenda for the session. Generally, parties then make opening statements. Some mediators conduct the entire process in a joint session. However, other mediators will move two separate sessions, shuttling back and forth



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between the parties. If the parties reach an agreement, the mediator may help reduce the agreement to a written contract, which will then be enforceable in court.”<sup>102</sup>

The original intent of mediation was to allow the parties to have an economical way for disputing parties to work together to come up with a solution rather than turning the problem over to the legal departments. However, in practice parties typically bring in their lawyers such as with the City and the Firefighters Union example shared in Part 5. The American Bar Association states: “As practiced today, mediation typically is a lawyer-driven process, involving extensive participation by opposing attorneys, and may well involve discovery. mediation, like arbitration, incurs substantial transaction costs for both parties.”

A Standing Neutral can – if the parties agree - play the role of mediator in helping the parties come to a solution.

### **14. Conciliation**

Conciliation often gets confused with mediation and arbitration, but in most jurisdictions, the terms rarely are considered as interchangeable.

Conciliation differs from mediation in that in mediation the mediator works with the parties to help them come up with an agreement mutually acceptable. In conciliation, however, the conciliator meets with the parties separately, who present their sides. The conciliator may ask the parties to make concessions to get to a resolution. Ultimately the conciliator drafts a resolution he or she considers and beneficial to both parties, but the proposed resolution is non-binding and the parties may accept or reject it as they wish.<sup>103</sup>

A Standing Neutral could be given the authority to act as a conciliator.

### **15. Mini-trial**

A mini-trial is really not a trial at all. Rather, it is a settlement process. The American Bar Association (ABA) defines the mini-trial<sup>104</sup> as:

A private, consensual process where the attorneys for each party make a brief presentation of the case as if at a trial. The presentations are observed by a neutral advisor and by representatives (usually high-level business executives) from each side with the authority to settle the dispute. At the end of the presentations, the representatives attempt to settle the dispute. If the representatives fail to settle the dispute, the neutral advisor, at the request of the parties, may serve as a mediator or may issue a non-binding opinion as to the likely outcome in court.

### **16. Advisory Arbitration**

Advisory arbitration is a form of arbitration but is non-binding. See 17 below (Arbitration) for a definition of arbitration.

Standing Neutrals can perform the role of Advisory Arbitration if given the authority.



### Binding Resolution Techniques

Binding resolution is the costliest type of ADR, with only a formal court process exceeding these costs.

Standing Neutrals may be given authority to act as an arbitrator, such as in the real estate development and IP examples shared in Part 4. We recommend that Standing Neutrals not be asked to issue binding arbitration decisions unless the context of the deal (such as where “time is of the essence” as in the case of the Real Estate Development example).

#### 17. Arbitration

The American Bar Association (ABA) defines arbitration<sup>105</sup> as:

“A private process where disputing parties agree in writing that one or several individuals can make a decision about the dispute after receiving evidence and hearing arguments. Arbitration is different from mediation because the neutral arbitrator has the authority to make a decision about the dispute. The arbitration process is similar to a trial, in that the parties make opening statements and present evidence to the arbitrator. It is usually conducted under the procedural rules of an established dispute resolution organization such as the American Arbitration Association, CPR, JAMS, or a similar international organization. Compared to traditional trials, arbitration can usually be completed more quickly and is less formal. For example, often the parties do not have to follow state or federal rules of evidence and, if the parties agree, the arbitrator is not required to apply the governing law. After the hearing, the arbitrator issues an award. Some awards simply announce the decision (a “bare-bones” award), and others give reasons (a “reasoned” award). Awards are not public records. The arbitration process may, if agreed, be either binding or non-binding. When arbitration is binding, the decision is final, can be enforced by a court, and can only be appealed on very narrow grounds. When arbitration is non-binding, the arbitrator’s award is advisory and can be final only if accepted by the parties.”

Arbitrators must be formally trained or certified as arbitrators. Arbitrators come from a wide variety of educational and professional backgrounds. While many have a legal background or are practicing attorneys, many others have backgrounds in accounting, insurance, finance, health care, construction or other fields. A few states require that arbitrators be experienced attorneys. The American Arbitration Association requires arbitrators to have at least ten years of professional experience and appropriate education and training in arbitration to be added to the AAA National Roster of Arbitrators.<sup>106</sup>

In addition, many view arbitration as it is currently practiced as looking and costing like the litigation it is supposed to prevent noting, “procedures now typically include a lot of excess baggage in the form of motions, briefs, discovery, depositions, judges, lawyers, court reporters, expert witnesses, publicity, and damage awards beyond reason (and beyond contractual limits).”<sup>107</sup> The ABA states arbitration “incurs substantial transaction costs for both parties, in the form of lawyers’ and arbitrators’ fees, costs of discovery, and experts’ fees. These are “sunk” costs for each party, ordinarily not recoverable from the other party.”<sup>108</sup> The criticism is especially sharp for court-annexed arbitration, which judges in



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federal jurisdictions often mandate after contestants have begun to litigate. A Harvard Business Review article says:

“Not surprisingly, the parties tend to pursue the case as they began it—with a lot of hostility and all the expensive paraphernalia of a lawsuit—despite the judge’s admonition to arbitrate. What’s more, if either party objects to the arbitration decision, it can take the case back to the judge. Despite the drawbacks—high legal costs, lost time, lack of finality—some 65% of cases facilitated by the American Arbitration Association are court-annexed ADR.”<sup>109</sup>

Standing Neutrals may be given authority to act as an arbitrator, such as in the real estate development and IP examples shared in Part 4.

### 18. Baseball Arbitration

Baseball arbitration is a type of arbitration in which the disputing parties submit a proposed award to the arbitrator, and the arbitrator picks only one party’s request. Baseball arbitration got its name because it has become popular for resolving salary disputes between baseball players and team owners.

In baseball arbitration, the player or his representative and the Major League Baseball club each submit a salary figure. These figures are given to a three-person panel of professional arbitrators. The process provides each party one hour to present its case to the panel followed by 30 minutes for rebuttal. After each side has presented its case, the panel decides which salary figure to award. It is an all-or-nothing proposition in which the panel will either choose the proposed figure from the player or by the team. There is no middle ground or compromise.

Baseball arbitration limits an arbitrator’s discretion in arriving at a decision. A key benefit of baseball arbitration is an inherent incentive for each side to offer a reasonable proposal to the arbitrator hoping his/her award will be accepted. The rationale is that unreasonable offers will likely result in the unreasonable party losing.

Although the process itself is easy to understand, critics view it as ripe with danger because “the player is required to be in attendance and listen as the team tries to minimize that player’s accomplishments and value to the team. At the end of the process, that same team tells the player how important he is to its success in the upcoming season. It is a hard message to deliver at least with a straight face.”<sup>110</sup>

Baseball arbitration is increasingly used in commercial disputes such as the real estate development example shared in Part 4. The arbitrators can either be a panel (as in baseball) or an individual as in the real estate development example. Because the arbitrator can only choose between the parties’ offers, it is sometimes called an “either/or” arbitration or a “final offer” arbitration.

### 19. Private Judge

The American Bar Association (ABA) defines a private judging<sup>111</sup> as

“A process where the disputing parties agree to retain a neutral person as a private judge. The private judge, who is often a former judge with expertise in the area of the dispute, hears the case and makes a decision in a manner similar to

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a judge. Depending on court rules, the decision of the private judge may be appealable in the public courts.”

Private judges were first introduced in the United States in the late 1970s in New York. The parties’ attorneys select the private judge, and the cost is split between the disputing parties. Private judges typically hear domestic relationship cases, breach of contract cases and a variety of civil cases. They would not hear criminal cases such as murder or a case that requires a jury.

The benefits of using a private judge are primarily speed, picking the judge, and privacy. There is also a benefit for the taxpayers because the disputing parties pay for the cost.

### 20. Litigation

Litigation is not an ADR technique and is the most expensive and adversarial dispute resolution technique. The American Bar Association (ABA) defines litigation<sup>112</sup> as:

“Litigation is a process for handling disputes in the court system. Litigation is a *contested action*, where someone else, such as a judge may make the final decisions for the parties unless the parties settle before trial. Settlement can happen at any point during the process. During the litigation process, there may be a series of hearings and temporary orders (e.g. temporary custody and support), culminating in the final orders. Final orders regarding the real issues in the case (e.g. custody, support, division of assets) are usually entered only after there has been a trial with witnesses.”





### APPENDIX 2: SAMPLE LANGUAGE FOR SELECTING STANDING NEUTRAL SERVICES

The parties will, either in their contract or immediately after entering into their contractual relationship, designate a Standing Neutral who will be available to the parties to assist and recommend to the parties the resolution of any disagreements or dispute which may arise between the parties during the course of the relationship.

**Appointment.** The neutral will be selected mutually by the parties. The neutral should be experienced with the kind of business involved in the parties' relationship, and should have no conflicts of interest with either of the parties.

**Briefing of the Neutral.** The parties will initially brief the neutral about the nature, scope and purposes of their business relationship and equip the neutral with copies of basic contract documents. In order to keep the neutral posted on the progress of the business relationship, the parties will furnish the neutral periodically with routine management reports, and may occasionally invite the neutral to meet with the parties, with the frequency of meetings dependent on the nature and progress of the business venture.

**Dispute resolution.** Any disputes arising between the parties preferably should be resolved by the parties themselves, but if the parties cannot resolve a dispute, they will promptly submit it to the neutral for resolution.

**Conduct of hearing and recommendation.** As soon as a dispute is submitted to the neutral, the neutral will set an early date for a hearing at which each party will be given an opportunity to present evidence. The proceedings should be informal, although the parties can keep a formal record if desired. The parties may have representatives at the hearing. The neutral may ask questions of the parties and witnesses, but should not during the hearing express any opinion concerning the merits of any facet of the matter under consideration. After the hearing the neutral will deliberate and promptly issue a written reasoned recommendation on the dispute.

**Acceptance or rejection of recommendation.**

Within two weeks of receiving the recommendation, each party will respond by either accepting or rejecting the neutral's recommendation. Failure to respond means that the party accepts the recommendation. If the dispute remains unresolved, either party may appeal back to the neutral, or resort to other methods of settlement, including arbitration (if agreed upon by the parties as their binding method of dispute resolution) or litigation. If a party resorts to arbitration or litigation, all records submitted to the neutral and the written recommendation will be admissible as evidence in the proceeding.

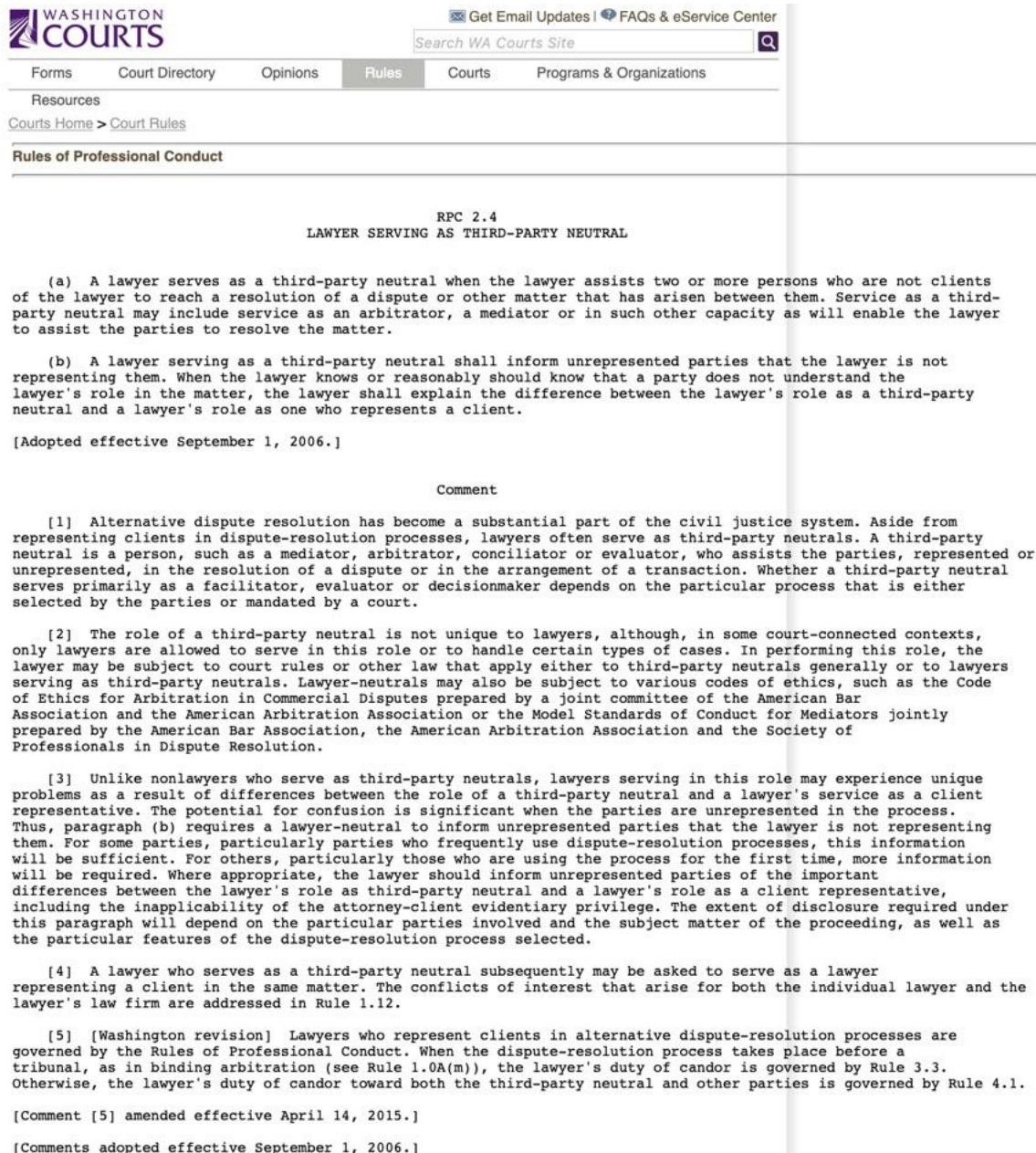
**Fees and expenses.** The neutral shall be compensated at his or her customary hourly rate of compensation, and the neutral's compensation and other reasonable costs shall be shared equally by the parties.

**Succession.** If the neutral becomes unable to serve, or if the parties mutually agree to terminate the services of the neutral, then the parties will choose a successor Standing Neutral.

## UNPACKING THE STANDING NEUTRAL

### APPENDIX 3: GUIDELINES FOR LAWYERS SERVING AS THIRD-PARTY NEUTRALS

*This Appendix shows that different jurisdictions can have different laws regarding using a lawyer as a Standing Neutral. Please check local laws as you design your preventive system.*



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RPC 2.4  
LAWYER SERVING AS THIRD-PARTY NEUTRAL

(a) A lawyer serves as a third-party neutral when the lawyer assists two or more persons who are not clients of the lawyer to reach a resolution of a dispute or other matter that has arisen between them. Service as a third-party neutral may include service as an arbitrator, a mediator or in such other capacity as will enable the lawyer to assist the parties to resolve the matter.

(b) A lawyer serving as a third-party neutral shall inform unrepresented parties that the lawyer is not representing them. When the lawyer knows or reasonably should know that a party does not understand the lawyer's role in the matter, the lawyer shall explain the difference between the lawyer's role as a third-party neutral and a lawyer's role as one who represents a client.

[Adopted effective September 1, 2006.]

Comment

[1] Alternative dispute resolution has become a substantial part of the civil justice system. Aside from representing clients in dispute-resolution processes, lawyers often serve as third-party neutrals. A third-party neutral is a person, such as a mediator, arbitrator, conciliator or evaluator, who assists the parties, represented or unrepresented, in the resolution of a dispute or in the arrangement of a transaction. Whether a third-party neutral serves primarily as a facilitator, evaluator or decisionmaker depends on the particular process that is either selected by the parties or mandated by a court.

[2] The role of a third-party neutral is not unique to lawyers, although, in some court-connected contexts, only lawyers are allowed to serve in this role or to handle certain types of cases. In performing this role, the lawyer may be subject to court rules or other law that apply either to third-party neutrals generally or to lawyers serving as third-party neutrals. Lawyer-neutrals may also be subject to various codes of ethics, such as the Code of Ethics for Arbitration in Commercial Disputes prepared by a joint committee of the American Bar Association and the American Arbitration Association or the Model Standards of Conduct for Mediators jointly prepared by the American Bar Association, the American Arbitration Association and the Society of Professionals in Dispute Resolution.

[3] Unlike nonlawyers who serve as third-party neutrals, lawyers serving in this role may experience unique problems as a result of differences between the role of a third-party neutral and a lawyer's service as a client representative. The potential for confusion is significant when the parties are unrepresented in the process. Thus, paragraph (b) requires a lawyer-neutral to inform unrepresented parties that the lawyer is not representing them. For some parties, particularly parties who frequently use dispute-resolution processes, this information will be sufficient. For others, particularly those who are using the process for the first time, more information will be required. Where appropriate, the lawyer should inform unrepresented parties of the important differences between the lawyer's role as third-party neutral and a lawyer's role as a client representative, including the inapplicability of the attorney-client evidentiary privilege. The extent of disclosure required under this paragraph will depend on the particular parties involved and the subject matter of the proceeding, as well as the particular features of the dispute-resolution process selected.

[4] A lawyer who serves as a third-party neutral subsequently may be asked to serve as a lawyer representing a client in the same matter. The conflicts of interest that arise for both the individual lawyer and the lawyer's law firm are addressed in Rule 1.12.

[5] [Washington revision] Lawyers who represent clients in alternative dispute-resolution processes are governed by the Rules of Professional Conduct. When the dispute-resolution process takes place before a tribunal, as in binding arbitration (see Rule 1.0A(m)), the lawyer's duty of candor is governed by Rule 3.3. Otherwise, the lawyer's duty of candor toward both the third-party neutral and other parties is governed by Rule 4.1.

[Comment [5] amended effective April 14, 2015.]

[Comments adopted effective September 1, 2006.]



### APPENDIX 4: BARRIERS TO ADOPTING A STANDING NEUTRAL

Despite the growing trend toward preventive law techniques many organizations resist investing to incorporate a Standing Neutral into complex contracts. This Appendix outlines common barriers cited for not using a Standing Neutral and offers suggestions for overcoming each barrier.

***Legal Counsel Do Not Support Using a Standing Neutral.*** Richard Susskind's book *The End of Lawyers?* uses the metaphor of a lawyer watching his or her client walking precariously along the edge of a cliff. The lawyer, instead of erecting a barricade or warning lights at the top of the cliff, simply parks an ambulance at the bottom of the cliff.<sup>113</sup>

Lawyers were originally antagonistic and at best cynical about the Alternative Dispute Resolution movement in the late 1980s and early 1990s, saying that the initials "ADR" stood for "Alarming Drop in Revenues." Continuing lawyer antagonism to the prevention objectives of ADR is illustrated by the voting at the Global Pound Conferences (GPC). In response to the question "Which stakeholders are likely to be the most resistant to change in commercial dispute resolution practice? the overwhelming verdict among the GPC delegates (even including the lawyer delegates) was "External lawyers."<sup>114</sup>

Ironically, now that many retirement-age lawyers are going into the "resolution" business, their livelihood depends even more upon an unending flow of intractable disputes, so they are even more opposed to prevention than they might formerly have been.

*Overcoming the barrier:* One of the best approaches to getting legal counsel to support the use of a Standing Neutral is to remind them it is their professional obligation help keep their clients out of disputes and litigation; and that a part of that obligation is to keep themselves informed about the kinds of prevention practices that can help to meet that obligation. One way is to start by sharing this white paper or talking to someone who is an expert or has used a Standing Neutral effectively. If you would like to speak to someone who has used a Standing Neutral please contact the University of Tennessee's lead researcher, Kate Vitasek at [kvitasek@utk.edu](mailto:kvitasek@utk.edu)

Another approach is to focus the parties on the purpose of the relationship in the first place, which is to achieve the specific outcomes identified. Remind the teams, including the attorneys, that the best way to achieve those goals is to maintain a healthy relationship. The more quickly potential disputes are alleviated or eliminated the more likely the relationship will stay healthy.

***Not Wanting to Spoil the Euphoria.*** Some people may fear that addressing the subject of dispute resolution during the early stages of a relationship is akin to suggesting to a happily engaged couple they should sign a pre-nuptial agreement.

*Overcoming the barrier:* Don't wait until after you have signed a new deal to think about your dispute resolution processes. Instead, embed it as a task in your overall contracting process that simply must be addressed. For example, the Vested methodology simply treats completing preventive practices as deliverables that must be completed as part of the contracting process – similar to how the team must develop a Statement of Work or a Pricing Model for the relationship.



## UNPACKING THE STANDING NEUTRAL

***A Sense There Won't be Future Problems.*** It is human nature to ignore issues and hope they go away (i.e., the small blister on your foot). Sometimes this strategy can work, but often it does not. In addition, far too many business people don't think in terms of conflict systems. One of the biggest reasons for disputes in large complex contracts such as an outsourcing agreement is because problems do not become apparent until the managers have moved to other positions (and thus avoided responsibility). A good relationship may have prevented a formal dispute, but when, for example, a "new sheriff" comes to town the party with a complaint may not feel obligated to continue to bite their tongue. Also, if the parties have not put in preventive techniques such as sound governance or a Statement of Intent, there is often a sense that no one affirmatively has responsibility for managing conflict generally.

*Overcoming the barrier:* Have team members complete a "what if..." exercise "what if a new sheriff comes in and demands the supplier to cut cost by 20%?" or "what if XX happens, how will you deal with it fairly?" Augment this exercise by having team members share real war stories of what has happened on other deals/relationships. Then look at the existing processes for managing disputes. What would happen if one of these "what if's" or war stories happened to your deal and all you had was your existing dispute process versus embedded practices for more collaborative and early resolution?

***Traditional Resistance to Change.*** One lawyer nicely summed up the reason his company has not adopted the practice of Standing Neutrals: "People get set in their ways. Teaching an old dog new tricks is very tough. Change is upsetting the apple cart and people don't want to hear it." So, while including a Standing Neutral may seem like a no-brainer at first blush, proponents often face significant barriers that make it difficult to adopt and sustain this innovation. Common reasons cited for not wanting to change include: 1) inside counsel and middle-level employees feel they handle disputes effectively and resent efforts to reduce their autonomy; 2) outside counsel worry about interference with their professional responsibility to produce the best legal results and their ability to generate substantial revenue that generally flows from existing "litigation as usual" practices; 3) a company culture of fighting the good battle to prove they are right; 4) doing something different seems risky and brings on criticism if the new idea does not work well and 5) there is a concern, often on the supplier side, that the Standing Neutral may get "in-between" or block them from building a deep connection with their client.

*Overcoming the barrier:* The good news is the success of both traditional ADR and the newer prevention and de-escalation processes such as Standing Neutrals have become better known, so resistance is diminishing. We suggest the best approach is through education on the why, what and how of using a Standing Neutral. Sharing this white paper or talking is a great first step.

In addition, people rarely change unless the pain to change is less than their current pain. In this case, try piloting the concept on the rebound of a bad deal. For example, let's say you have a bad supplier relationship and you will bid to find a new supplier. Use this opportunity to "pilot" the concept. Other good ways to get buy-in is putting in preventive techniques such as measuring dispute prevention versus disputes and charging the cost of disputes to the department(s) involved. This fact-based data will open the eyes of individuals to the hidden cost of traditional approaches. See these ideas and others in Appendix 1.





## UNPACKING THE STANDING NEUTRAL

***A Perception that Multi-level Dispute Resolution Slows Down the Process.*** Some people may feel that specifying more than one level of dispute prevention and resolution, such as partnering or a Standing Neutral before resorting to mediation or arbitration, imposes an unnecessary delay. As such, many contracts simply have a straight path to either arbitration or litigation. However, common sense points to the fact the earlier an issue is addressed, the more likely it can be resolved amicably.

*Overcoming the barrier:* Analyze a recent issue that went to mediation and arbitration. Dissect the path the issue took, how long each step took, and how much it cost. Most issues take a path similar to the City and Firefighters Union example and lead to a long drawn out process with significant hidden costs. Mapping out one or two disputes should be eye-opening on why it would be better to embed a Standing Neutral who can speed the process with an early recommendation while the issue is small.

***The Perception that a Powerful Party Will Benefit from An Inefficient Method of Resolving Disputes.*** Sadly, organizations that have power often use (and abuse) their power. One way this is manifested in disputes is when the powerful party draws out the weaker party hoping the weaker party will give in (especially due to the cost of resolving the dispute). Using power to influence an outcome typically stems from the buy-side in a buyer-supplier relationship, but not always. For example, Mondelez International issued a letter to all suppliers that (regardless of their contract) they would be moving to a 120-day payment term.<sup>115</sup> Most suppliers – especially small and mid-size companies - simply can't fight back. When a buyer knowingly (or perhaps does not know) they are using their influence negatively, it will probably lead to negative tit-for-tat behavior from the supplier – most often in passive-aggressive behaviors. This is worse after a contract is signed – especially for large or complex contracts such as outsourcing agreements hard and costly to unwind.

*Overcoming the barrier:* This barrier is the hardest to overcome. Organizations and individuals who maintain that power-based approaches are preferable are unlikely to change. Our view? Refuse to work with these organizations or individuals. And if you must, factor in the risk so you will be compensated for their bad behavior and the hassles you will have.

## UNPACKING THE STANDING NEUTRAL



### ABOUT THE AUTHORS



**Kate Vitasek** is an international authority for her award-winning research and Vested® business model for highly collaborative relationships. Vitasek, a Faculty member at the University of Tennessee, has been lauded by *World Trade Magazine* as one of the “Fabulous 50+1” most influential people affecting global commerce. Her work has led to 7 books including *Vested: How P&G, McDonald’s and Microsoft Are Redefining Winning in Business Relationships* and *Getting to We: Negotiating Agreements for Highly Collaborative Relationships*.

Vitasek is known for her practical and research-based advice for driving transformation and innovation through highly collaborative and strategic partnerships. She has appeared on Bloomberg, CNN International, NPR, and Fox Business News.



**James P. Groton** is a retired partner of the Atlanta law firm of Sutherland, Asbill and Brennan (now known as Eversheds-Sutherland LLC), where he headed its Construction and Dispute Prevention and Resolution practice groups. Groton has conducted research and written extensively on processes used in the construction industry and other relationship-based businesses to prevent and de-escalate disputes (see [www.jimgroton.com](http://www.jimgroton.com)).

In his work for the Global Pound Conference (see [www.jimgroton.com](http://www.jimgroton.com)) he advocated for broader use of these processes. He holds degrees from Princeton University and the University of Virginia Law School.



**Dan Bumblauskas** is an associate professor and the Hamilton/ESP International fellow for supply chain and logistics management at the University of Northern Iowa. He also serves as Vice President of PFC Services, Inc., a consultancy based out of Marietta, Georgia; a visiting professor at the University of Washington Foster School of Business; and holds a courtesy appointment at the University of Missouri Trulakse College of Business. Dan has published over 40 scholarly journal articles and conference proceedings in various business management and engineering outlets.

Dan holds multiple degrees from Iowa State University and Harvard University.





### ABOUT THE CONTRIBUTORS

This white paper was made possible by the several organizations that both participated in our research and shared examples and research data supporting the use of a Standing Neutral. The University of Tennessee would like to thank the following organizations, with special recognition for several individual contributors who have reviewed this white paper for accuracy and shared their experiences regarding the use of the Standing Neutral.

**FASKEN** – A Canadian national law firm. Special thanks to attorney and mediator **Jean H. Gagnon** who pioneered franchise law in Quebec and Canada and is one of the founders of the Quebec Franchise Council.

**SIREAS, LLC** – A U.S. based advisory firm specializing in outsourced facilities management and governance. Special thanks to SIREAS' executive chairman **Michele Flynn** who is a visionary and expert in the fields of outsourcing, facilities management, real estate and governance.

**CI-Advisory** – an Australian consulting firm specializing in supply chain relationships and supply chain risk management. Special thanks to founder **Andrew Downard** who holds a Ph.D. in supply chain management focused on collaborative and trust-based approaches.

**Cirio** – a progressive law firm in Sweden that is a leading authority on relational contracting practices. Special thanks to **Erik Linnarsson** (Partner) and **Erik Engstrom (Associate)** who have been pioneers in bringing preventive techniques to their clients.

**EY** – with a special thanks to **Magnus Kuchler** (Partner) and **Amanda Lundell** (Manager) of the **Nordics Outsourcing Advisory Practice**. Under their leadership, EY is bringing a practical and applied approach for how advisory firms can apply the art, science and practice of Standing Neutrals in practice in outsourcing deals.

**Commercial Officers Group** – Special thanks to **Jim Bergman** who tirelessly promotes thought leadership in contracting and commercial practices.

## UNPACKING THE STANDING NEUTRAL

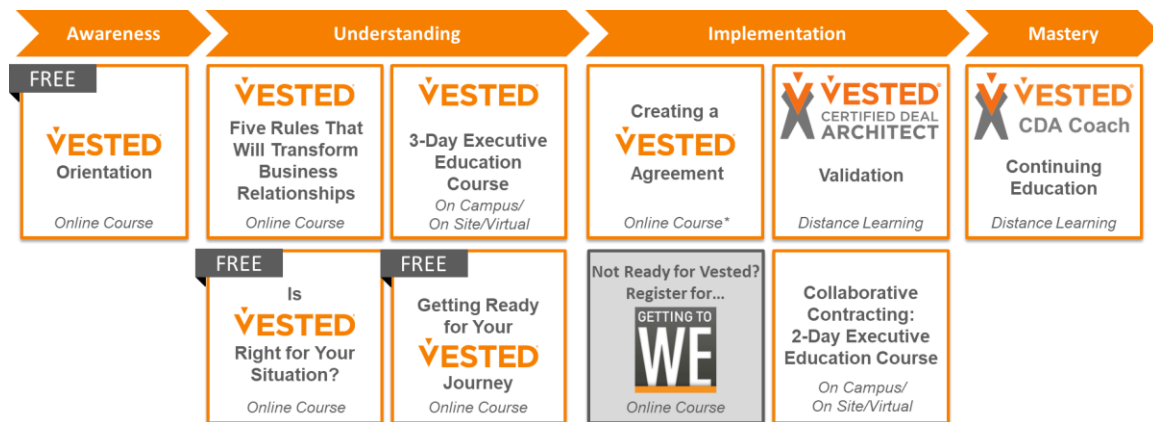
### FOR MORE INFORMATION

*The University of Tennessee* is highly regarded for its Graduate and Executive Education programs. Ranked #1 in the world in supply chain management research, researchers have authored seven books on the Vested business model and its application in strategic sourcing.



We encourage you to read the books on Vested, which can be found at most online book retailers (e.g., Amazon, Barnes and Noble) or at [www.vestedway.com/books](http://www.vestedway.com/books).

For those wanting to dig deeper, UT offers a blend of onsite and online courses including a capstone course where individuals get a chance to put the Vested theory in practice. Course content is designed to align to where you are in your journey ranging from Awareness to Mastery. For additional information, visit the University of Tennessee's website dedicated to the Vested business model at <http://www.vestedway.com/>; you can learn more about our Executive Education courses in the Certified Deal Architect program. You can also visit our research library and download case studies, white paper and resources. For more information, contact [kvitasek@utk.edu](mailto:kvitasek@utk.edu).



\* Prerequisites for *Creating a Vested Agreement* class are:

*Five Rules, Is Vested Right?, Getting Ready, and the Vested 3-Day Executive Education Course*



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## ENDNOTES

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- <sup>10</sup> The Global Pound Conference series was inspired by Harvard law professor Roscoe Pound and the name of a 1976 conference named for him; it was an impetus for the growth in the popularity of arbitration and mediation in the USA. See "Global Pound Conference," at [https://en.wikipedia.org/wiki/Global\\_Pound\\_Conference](https://en.wikipedia.org/wiki/Global_Pound_Conference)
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- <sup>28</sup> Cummins writes extensively on collaborative and relational contracting in his *Commitment Matters* blog for IACCM. See <https://blog.iaccm.com/commitment-matters-tim-cummins-blog>
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- <sup>48</sup>James P. Groton, "Jobsite Dispute Resolution," *Preventing and Resolving Construction Disputes* (Chapter 6) *CPR Institute* 1991. Links: <https://onlinelibrary.wiley.com/doi/abs/10.1002/alt.3810091208> and [https://www.cpradr.org/resource-center/toolkits/construction-briefing-dispute-resolution-boards-other/\\_res/id=Attachments/index=0/CPR-Dispute-Review-Boards-and-Other-Standing-Neutrals-Constructiontitle.pdf](https://www.cpradr.org/resource-center/toolkits/construction-briefing-dispute-resolution-boards-other/_res/id=Attachments/index=0/CPR-Dispute-Review-Boards-and-Other-Standing-Neutrals-Constructiontitle.pdf)
- <sup>49</sup>The concept of shading was developed by Nobel Laureate Oliver Hart. Shading is not opportunistic behavior, but rather *retaliating behavior* in which a party stops cooperating, ceases to be proactive, or makes countermoves because of disappointment. Shading happens when a party doesn't get the outcome they expect from the deal and feels the other party is to blame for it or does not act reasonably by helping to mitigate the losses. In short – each party's action leads to the other party's reaction, creating the negative tit-for-tat cycle. One disappointment leads to another and the cycle begins. The concept of shading makes sense, especially with complex deals. In complex deals, a contract will always be incomplete with gaps, errors or omissions opening the door for shading behavior after the contract is signed. Traditional contracts simply do not contain mechanisms to avoid disappointments.
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- <sup>51</sup>R. Hafer, "Dispute Review Boards and Other Standing Neutrals: Achieving 'Real Time' Resolution and Prevention Disputes," *CPR Dispute Prevention Briefing: Construction*. (2010). Available online at [https://www.cpradr.org/resource-center/toolkits/construction-briefing-dispute-resolution-boards-other/\\_res/id=Attachments/index=0/CPR-Dispute-Review-Boards-and-Other-Standing-Neutrals-Constructiontitle.pdf](https://www.cpradr.org/resource-center/toolkits/construction-briefing-dispute-resolution-boards-other/_res/id=Attachments/index=0/CPR-Dispute-Review-Boards-and-Other-Standing-Neutrals-Constructiontitle.pdf)
- <sup>52</sup>Dispute Resolution Board Foundation (DRBF) *Dispute Review Board Manual* (2007) Available online at [http://www.drb.org/manual\\_access.htm](http://www.drb.org/manual_access.htm).
- <sup>53</sup>See Elton Mayo, "The Hawthorne Experiment. Western Electric Company (1933)" Chapter 3 in *Classics of Organization Theory*, 2016, p.134-141. Available at: <https://www.cengage.co.uk/books/9781285870274/> 1





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- <sup>57</sup> This section is taken from the work of Jim Groton, one of the authors. For a more comprehensive discussion see the article written by him in J.P. Groton "The Standing Neutral: A Real Time Resolution Procedure That Also Can Prevent Disputes," *CPR Alternatives to the High Cost of Litigation* (2009) 27(11): 177-185. (The newsletter for the International Institute for Conflict Resolution and Prevention)
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- <sup>60</sup> Ibid.
- <sup>61</sup> See the Dispute Resolution Board Foundation FAQ at: <https://www.drb.org/concept/faq/>
- <sup>62</sup> Chris Owens and Michele Flynn, "Locking in the Benefits of Outsourcing: Innovation, Cost Reduction, and Continuous Improvement at Microsoft," *Leader*, September 2005, 2–5.
- <sup>63</sup> Rene Stemple Ellis, Geeetha Ravindra, Neil Vidmar and Thomas Davis, "The Reversal Arbitration Board: An ADR Model for Resolving Intra-Corporate Disputes," *Journal of Dispute Resolution* 1994 v4 93-110. Available at: [https://scholarship.law.duke.edu/faculty\\_scholarship/1541/](https://scholarship.law.duke.edu/faculty_scholarship/1541/)
- <sup>64</sup> UT's CDA program is modeled after a typical journeyman approach where individuals must apply their knowledge in practice. Besides the knowledge gained in the UT on-site and on-site courses, CDA candidates must also complete the [UT Validation capstone course](https://www.vestedway.com/certified-deal-architect-program/) that involves delivering a Vested agreement. See <https://www.vestedway.com/certified-deal-architect-program/>
- <sup>65</sup> Kate Vitasek and William DiBenedetto, "Telia and Veolia: From Supplier to Strategic Partner," *University of Tennessee* case study, Jan. 2019. Available at: [https://www.vestedway.com/wp-content/uploads/2019/01/Telia\\_Veolia-case-study\\_short-version-PDF-Jan-30-2019-do-not-distribute.pdf](https://www.vestedway.com/wp-content/uploads/2019/01/Telia_Veolia-case-study_short-version-PDF-Jan-30-2019-do-not-distribute.pdf)
- <sup>66</sup> Kate Vitasek, one of the authors, was directly involved in this example
- <sup>67</sup> Interview with Michele Flynn (Executive Chairman, SIREAS), June 20, 2019.
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- <sup>69</sup> This discussion is adapted from "A Real Example of the Use of Two Standing Neutrals to Bind a Business Relationship," a paper by James P. Groton.
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- <sup>75</sup> For additional elements of prevention practices tailored specifically for corporate governance, see IFC 2011; O’Neal 1978 in the list of references
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- <sup>82</sup> This survey is representative of existing studies while not attempting to include them all. For other surveys of mostly U.S. literature, see Bingham and others (2009), Menkel-Meadow (forthcoming), and Ward (2007). Many studies are based on nonrandom assignment of cases to ADR, which leaves a concern that firms that chose to use ADR could differ in some unobservable ways from firms that did not and thus that the outcomes may be attributable at least in part to these differences rather than to the effectiveness of ADR.
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## UNPACKING THE STANDING NEUTRAL

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