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Final Offer Arbitration: A Model for Dispute Resolution in Domestic and International Disputes

NAME: Elissa M. Meth

During the last thirty years, a new form of arbitration has emerged in the United States. Called final offer, or last-best offer, arbitration, the dispute resolution procedure limits an arbitrator to choosing the final offer made by one of the parties. n1 It is designed to motivate each party to negotiate in good faith [*385] and genuinely attempt to compromise in order to create a final offer that an arbitrator will select as most reasonable. n2 The theory predicts that good faith bargaining and the risk of losing will facilitate settlements. n3

Various private and public sector disputants in the United States have adopted final offer arbitration ("FOA") to resolve contract-based disagreements. The most publicized use is by Major League Baseball ("Baseball"), which adopted FOA, or salary arbitration, as a means to set salaries for veteran players. n4 Currently, several states also use FOA to settle disputes with unionized public employees. n5 In 1994, the IRS and Apple [*386] Computer chose FOA to resolve a $ 114 million tax disagreement. n6

Although those who have used FOA have found it to be an effective process, few outside of Baseball and public sector collective bargaining relationships have adopted it. n7 International arbitrants have ignored it altogether. n8 As a dispute resolution procedure that encourages settlement, preserves relationships and is time and cost effective, FOA could be ideal for many disputants. This note explains the advantages and disadvantages of FOA, offers guidance to domestic and international disputants who wish to implement it and describes disputes that can readily benefit from it.

I. AN OVERVIEW OF FINAL OFFER ARBITRATION

FOA is a form of interest arbitration that developed in the United States as an alternative to the strike. n9 Interest arbitration replaces the strike, which is the cost of disagreement in traditional collective bargaining relationships, with the risk that a third party will implement a settlement. n10 The risk can be avoided only if the parties agree to a settlement prior to the arbitration deadline. n11

[*387] A. *Final Offer Arbitration v. Conventional Arbitration*

The attributes of FOA are best understood in contrast to conventional arbitration. In conventional arbitration, a bargaining impasse is submitted to an arbitrator who selects either party's position on one or all of the pending issues, compromises between the parties' positions or awards a unique solution. n12 It is criticized because of the deterrent, or "chilling effect" it is purported to have on the parties' incentives to bargain in good faith. n13 The theory of the chilling effect predicts that the availability of interest arbitration as a dispute resolution procedure decreases the parties' willingness to engage in serious negotiations. n14 Because an impasse will be submitted to an arbitrator, one or both parties have an incentive to refuse to bargain prior to the arbitration if they

believe they will receive a better outcome from arbitration than from negotiation. n15 Disputants may also perceive the conventional arbitration process as likely to result in some form of compromise on their final offers; this perception causes them to undervalue the risks of the arbitration hearing, posture during negotiations and assume extreme positions designed to influence the arbitrator's decision. n16 The parties may also conclude that any change in their initial bargaining position will reduce the likelihood of obtaining a favorable award. n17

Because FOA prohibits arbitrators from compromising between final offers, it imposes a higher cost than conventional arbitration: the risk that a third party will endorse an adversary's final offer. n18 The possibility of losing entirely in the arbitration counteracts the chilling effect. n19 It also acts as a [*388] psychological, economic, and political incentive for the parties to reach their own agreement. n20 For these reasons, the FOA hearing has been referred to as "the hydrogen bomb poised above the bargaining table whose very terror should assure its non-use." n21

B. *Final Offer Arbitration Facilitates Bargaining and Settlement*

In addition to increasing the risk of submitting a dispute to an arbitration hearing, FOA arbitration facilitates settlement in many other ways. First, FOA encourages good faith bargaining by motivating parties to develop and exchange their most reasonable positions prior to the arbitrator's decision. n22 "Reasonable" in the context of FOA refers to an offer that is defensible based on the factors that the arbitrator may consider. n23 FOA does seem to encourage reasonable offers; each side knows that the arbitrator is unable to compromise, so each side is wary of making unreasonable offers that increase the chance that its opponent will win at the hearing. n24 Final offers in salary arbitration tend to be reasonable because they may be figures never proposed during preceding [*389] negotiations and they are exchanged simultaneously; n25 therefore, it is impossible for

the parties to assess each other's offer and base a counteroffer upon it. n26 Each party must independently determine a defensible value of a player and hope that its determination is more reasonable than the one reached by the other side. n27

Second, each party's final offer communicates previously concealed information that may be hampering the negotiation process; this information includes risk preferences and knowledge of facts relevant to the arbiter's decision. n28 As each party learns more about the other through the disclosure of final offers, the likelihood of finding a settlement increases.

Third, inherent in final offer arbitration are distributive and interest-based settlement incentives.

1. *Distributive incentives to settle*

When the only dispute between parties is a numeric value, FOA's reasonable final offers provide a midpoint and a range of numbers on which to focus negotiations. n29 Each side can asses the likelihood that the arbitrator will value the disputed item as worth more or less than the midpoint. n30 This analysis helps the parties predict which offer the arbitrator will choose. The offer that is closer to the prediction of the arbitrator's value of the item is likely to win the arbitration; the parties then settle accordingly. n31

In Baseball, this midpoint analysis promotes settlement. n32 Close final offers usually settle because a compromise number is easy to reach. n33 Final offers [*390] which are far apart often settle as well because each side fears that the arbitrator will choose the other's offer. n34 Salary disputes in Baseball tend to settle at or near the midpoint, but whichever party has a more defensible number in relation to the midpoint generally receives a more favorable settlement. n35 Settlements fail to be reached only when one side makes what the other perceives to be an indefensible offer. n36

2. *Interest based incentives to settle*

In addition to distributive settlement incentives, FOA contains interest based settlement incentives. One is uncertainty. Since the parties will ultimately be uncertain about the arbitration outcome, they will prefer the security of an agreement. n37

Variables specific to the parties in certain relationships may also encourage settlement. In Baseball, for example, players continue to play for their clubs after the arbitration. Therefore it is beneficial for teams to avoid hearings, which might require them to insult players and present arguments that harp on a player's physical or mental defects, or demean his past contributions to the club, playing record or public appeal. n38 Players may wish to avoid the hearing to secure benefits that are available only if they settle. These include, but are not limited to, bonuses, guaranteed contracts, no trade clauses, single occupancy rooms on road trips and requiring the team to pay for hotel charges [*391] initially instead of reimbursing the player. n39 If any of these benefits are important to a player, he will have an incentive to settle. Finally, the option of multi-year contracts encourage settlement. Players whose salaries are determined by an arbitration hearing receive only one-year contracts. n40 If either side desires a multi-year contract, it must settle. Multi-year contracts also give the parties a greater period of time over which to spread salary discrepancies and more flexibility to do so. n41 Finally, a club might be willing to offer more money, or a player to play for less, if in return, the club is guaranteed to have the player's services, or the player receives job security, for an extended period of time. n42

C. *High Percentages of Parties Using FOA Settle*

In practice, participants to FOA avoid arbitration hearings in great numbers. n43 Ninety percent of disputes that enter the Baseball salary arbitration process settle before the hearing. n44 Few studies have been conducted recently on the success of public sector FOA, but assessments of FOA

that occurred during the 1970s indicated that parties reached negotiated agreements in high numbers and avoided strikes. n45 In the early years of the Wisconsin FOA [*392] program, for example, arbitrators resolved only 9 of 173 negotiations. n46 In the 1980s, approximately two-thirds of the cases in New Jersey, in which arbitration was initiated, ended in voluntary settlements; in the other third of the cases, in which awards were rendered, half were actually formal or informal consent awards. n47

D. *Success in FOA Arbitration Without Settlement*

Although FOA's goal is settlement, the procedure may be successful even when an arbitrator imposes a solution. In some circumstances, political pressures or a difference of information or opinion may necessitate a finding by a third party. n48 If the parties in such situations narrow their disagreement prior to the hearing, either by reducing the number of disputed issues or the range within disputed issues or both, the process is still considered a success. n49

It may also be that parties faced with close final offers would be satisfied with either outcome, but their own proposal offers them an option that is slightly better than their opponent's. In such a case, the parties may not settle, but each will be satisfied with the neutral's choice, regardless of what it is. In such a case, FOA is successful because it creates a result acceptable to both parties.

Finally, FOA is successful if it saves the parties time and money over conventional arbitration or litigation. When the IRS and Apple Computer chose FOA, they did so because each preferred the expertise of arbitrators and [*393] neither wanted to endure what could have resulted in a ten-year litigation. n50 After the arbitrator issued an award, both parties endorsed the process because they had narrowed their differences prior to the submission of final offers, the time period between the arbitration proceedings and the decision was short compared to the projected time for

litigation and the process was much less expensive than litigation would have been. n51 The parties also appreciated the confidential nature of FOA and the lack of voluminous briefs. n52 Baseball's salary arbitration saves time and money over conventional negotiations by providing structure to salary negotiations and imposing strict timing requirements for filing, n53 submission of final offers, n54 the hearing, n55 and the arbitrator's decision. n56 Because the arbitrator does not issue a written decision, further costs are eliminated. n57

II. FORMS OF FOA

FOA has many variations, which parties may combine to meet their needs. n58 Parties can specify the FOA system to which they agree at the outset of their [*394] relationship or they can create a system when a dispute arises. n59 If parties wait until a disagreement occurs to design a system, a resolution will be delayed while they create the arbitration process; in addition, tensions arising from the substantive dispute may impede the creation of the procedure. If the parties can overcome these challenges and create a FOA system at the time the dispute arises, however, they will benefit from a FOA procedure that is tailored to solve their particular dispute.

Whenever it is that the parties choose to create their dispute resolution system, they will have many choices to make. The first decision involves whether to invoke "issue-by-issue" or "package" FOA. This choice is relevant only when there is more than one issue in dispute. n60

A. *Issue-By-Issue Final Offer Arbitration*

In issue-by-issue FOA, the arbitrator chooses a final offer on each issue independently. n61 Under this method, the arbitrator has flexibility to create a balanced award; as the number of issues in dispute increases, however, the characteristics of issue-by-issue FOA begin to mirror conventional arbitration. For example, if there are many issues in dispute, an arbitrator can balance the

number decided in favor of each party; this potential dilutes the high settlement pressure FOA should impose on parties due to the neutral's inability to compromise. n62

B. *Package Final Offer Arbitration*

The package system more closely reflects the goals of FOA. Under it, the arbitrator chooses one party's entire offer, n63 eliminating much of the discretion [*395] that arbitrators wield in both conventional arbitration and issue-by-issue FOA. n64 The lack of discretion is replaced by high party risk: one party will have its entire offer rejected by the arbitrator. n65 This risk maximizes each party's incentive to reach a negotiated settlement. n66 It also prevents neutrals from imposing their view of desirable compromises upon the parties, a freedom they enjoy under issue-by-issue FOA, conventional arbitration and litigation. n67 Finally, package FOA seems to impose such high pressure on arbitrants that they are encouraged to settle at least some issues before the arbitration hearing. n68

C. *Other Procedural Variations*

After the parties choose between issue-by-issue and package FOA, they can select other procedural variations designed to resolve both single and multi-issue disputes. n69

1. *Concealed final offers*

One option involves concealing the final offers. n70 Under this method, the arbitrator reviews the evidence and then makes a decision, unseen by the parties, before the parties reveal their proposals. n71 The final offer that is closest to the arbitrator's decision is implemented. n72 This approach encourages reasonable offers. The arbitrator will form a decision based on the factors, without influence by the parties' final offers. Since the closest final offer wins, outrageous and extreme

final offers are discouraged. A problem with this approach for non-numeric issues is that the closest final offer might be unclear.

[*396] 2. *Dual final offers*

Another option allows each party to submit two final offers. n73 This approach provides all involved with more information about each party's preferences, and increases the probability that one of the offers will be attractive enough to induce the other to settle. n74 Data on dual final offer FOA suggests that the increase of information due to the multiple offers facilitates settlements. n75

3. *Independent fact-finders*

Hiring an independent fact finder is an option chosen by several public sector FOA systems. n76 There are two roles a fact finder might fulfill: evaluating the proposals of each party or making a recommendation that the arbitrator considers along with the parties' final offers. n77 Either way, the fact finder identifies a possible settlement area. n78 Fact-finding appears to reduce the number of issues that parties submit to the arbitrator by facilitating resolution of a significant number of them. n79 When Massachusetts used this approach, it appeared that the issues narrowed as disputes moved through fact-finding to FOA; n80 the presence of fact-finding also seemed to lower the propensity of the parties to proceed to the arbitration hearing. n81

The fact-finder option, however, has flaws. One researcher has found a strong tendency for arbitrators to choose the final offer of the party whose position was endorsed by the fact-finder, especially if the other party did not [*397] modify its position after the fact finding occurred. n82 If the fact-finder's recommendation rested between the two final offers, the researcher found that the arbitrator tended to choose the fact finder's recommendation. n83 Other research suggests that reliance on the fact-finder causes FOA to assume characteristics similar to conventional arbitration:

the parties amend their final offers based on the fact-finder's report, which was often a unique solution. n84 Because of the tendency of arbitrators to choose the fact-finder's proposal or some variation of it, and of the parties to amend their final offers based on the fact-finder's proposal, fact-finders may introduce the chilling effect to FOA. Another disadvantage of the fact-finder option is that parties who deem the fact-finder's report to be acceptable may assume the arbitrator will choose or be influenced by the report; that party will then be motivated to refuse to bargain after final offers are submitted. n85 In this scenario, the fact-finder will, by designing a proposal acceptable to one party but not the other, create a situation in which one party faces two acceptable final offers while the other faces only one; the first party's perceived risk of proceeding to the arbitration hearing will decrease, thereby diluting the structural benefits of FOA. n86

4. *Combining various forms of ADR*

A fourth option for complex disputes is to resolve different issues through different forms of alternative dispute resolution, including FOA. This approach can include resolving economic issues through FOA and non-economic issues through conventional arbitration. n87 It can also include FOA as the last step in a process preceded by negotiation, mediation and fact-finding. n88 Finally, parties can create a system that gives disputants a choice between numerous arbitration procedures, some of which are variations of FOA and others of which are [*398] variations of conventional arbitration. n89 Combining other forms of ADR with FOA will not impede the goals of FOA, but it may add time and monetary cost to the dispute resolution procedure.

5. *Negotiation after submission of final offers*

All final offer systems should encourage the parties to continue to negotiate after the final offers are submitted and prior to the issuance of the award by the arbitrator. n90 A negotiated settlement, or the narrowing of disagreement, is the goal of FOA, and the final offers allow parties to learn

about each other's preferences and to create new proposals based on the information. n91 FOA systems should encourage parties to apply any new information they learn to settlement discussions. Thus far, all FOA systems allow parties to continue to negotiate after the final offers are made, and this is a key feature of the system that future agreements should retain. n92

6. *Confidentiality*

Arbitration proceedings, documents and even the existence of the dispute itself can be kept confidential. n93 If confidentiality is important to the parties, they should include provisions in the arbitration agreement that specify publicity constraints.

7. *Costs*

When disputants create a FOA system, they should determine in advance who will bear its costs. In Baseball, the cost of salary arbitration is split [*399] between the player and the club. n94 Assigning the costs to the loser, if the dispute proceeds to the hearing, is another option which may increase the risk of losing and make the creation of reasonable offers and settlements even more attractive to the parties.

III. THE ARBITRATOR

In addition to creating the basic design of the system, parties to FOA agreements must discuss the structure of the arbitration panel. FOA allows disputants to define the neutral's role and to choose the identity and number of arbitrators who will preside. Parties, therefore, may decide where, when and in what forum the dispute will be arbitrated, choose arbitrators with expertise in relevant areas and dictate the criteria that arbitrators can consider. n95

A. *The Arbitration Panel*

Most FOA schemes involve either a one-arbitrator or a three-arbitrator panel. n96 If the parties choose one arbitrator, the arbitrator should be neutral, and if the parties prefer, someone with expertise in the area of the dispute. If the parties designate a three-arbitrator panel, they can choose arbitrators with expertise relevant to the dispute, or one representative of each side and a neutral third arbitrator who acts as the chairman and makes the ultimate decision. In international commercial arbitration, there is a general custom to appoint three-person tribunals, except when the amount in controversy fails to justify the cost. n97 Three-arbitrator panels in FOA retain commonly identified benefits of three-arbitrator panels in other arbitration contexts. Three arbitrators can combine their expertise, improving the likelihood that the panel will identify and comprehend important points and convey that understanding to the parties. n98 When choosing a three-arbitrator panel, disputants should consider that they may involve a significant increase over a one-arbitrator panel in monetary cost and the time required to render a decision. n99

If the parties choose a three-arbitrator panel, each arbitrator should be neutral as to the dispute. If two of the three arbitrators are partisan, they will essentially be party representatives. In this scenario, the panel will mimic a [*400] one-arbitrator panel because the representatives will act as advocates who try to sway the true neutral. n100 To avoid the risk that one of the party-appointed arbitrators will act as counsel to its appointing party while the other arbitrator acts as a neutral, parties should, when they create the panel, define the roles of its members. n101 Otherwise, one party may have an advocate on the panel while the other does not. n102 This balance could affect the outcome of the arbitration. n103 Therefore, if each FOA party appoints an arbitrator to the panel, the agreement should specify whether those appointees are to act as party representatives or as neutrals.

The FOA systems in the United States have had a variety of arbitration panels. Three arbitrators presided over the final offer arbitration between IRS and Apple Computer; they each had expertise in different areas relevant to the dispute. n104 The FOA system in Eugene, Oregon used a three-member panel: one representative of each side and a neutral chairperson. n105 A single arbitrator renders a decision in New Jersey. n106 The structure of the arbitration panel in Major League Baseball has changed gradually over the course of the Agreement from a one-arbitrator panel in 1997 to a three-arbitrator panel in 2000 and 2001. n107 These changes have been the result of a collective bargaining compromise; n108 the clubs favored a three-arbitrator panel n109 whereas the players preferred a single arbitrator. n110 The players favored single-arbitrator panels because they are less expensive than three arbitrators. n111 The clubs considered a single arbitrator to be untrustworthy since he or she would be [*401] motivated to arbitrate in a way that fosters job security; n112 a three-arbitrator panel, however, voting confidentially, would ensure neutral decisions uninfluenced by employment concerns. n113 The clubs were also concerned that a single arbitrator might rule unreasonably or fail to understand the intricacies of Major League Baseball or one side's argument. n114 The clubs decided that a three-arbitrator panel would alleviate these concerns because two reasonable arbitrators can overrule an unreasonable one and an arbitrator who understands the arguments can explain them to the other two. n115

B. *Selection of the Panel*

As in other forms of arbitration, the parties should create a procedure for selecting the members of the arbitration panel. n116 When individual members of a three-arbitrator panel are selected, each party will generally choose one arbitrator, with those two, or an independent authority, choosing the third. n117 Each arbitrator may also be chosen from a designated pool of eligible neutrals.

Arbitrators in New Jersey, for example, are chosen for three-year terms from a list generated by a private company. n118 Baseball arbitrators are selected from a list of potential arbitrators furnished by the American Arbitration Association. n119 The Major League Baseball Players' Association (MLBPA), representing the Players, and the Players' Relations Committee (PRC), representing the clubs, each strike a name from the list until the requisite number of arbitrators remain; then the MLBPA and the PRC jointly assign individual arbitrators to particular cases. n120 Apple and the IRS chose arbitrators pursuant to a seven page arrangement in their agreement. n121 After the arbitration, both sides reported that they would have benefitted from a [*402] streamlined process with fewer proposed arbitrators and relaxed selection criteria. n122

The considerations that are important in choosing arbitrators for international FOA are the same as the considerations that are important in choosing arbitrators in any international commercial arbitration context: the arbitrator's nationality, restrictions or qualifications for arbitrators in the agreement, the applicable law of the parties' dispute, requisite industry or technical expertise and the language of the arbitration. n123 The arbitrators should also satisfy any requirements of independence and impartiality required by the governing law of the arbitration. n124

C. *Requiring a Decision*

Parties should require the arbitration panel to reach a decision. n125 It is possible that the arbitrators will deem neither final offer acceptable and refuse to decide. n126 Such a situation could result in no award, and much wasted time, money and effort. n127 Requiring the panel to reach a decision would eliminate this potential problem. n128

D. *Weighting the Factors*

If the parties feel that the arbitrators should weigh some factors more heavily than others, they should so state in the agreement. n129 According to one study, 15 of 22 arbitrators with considerable experience in interest arbitration stated that statutory criteria had no effect on their decision. n130 One explanation is that the statutes did not provide the arbitrators with the weight of the factors; therefore, the arbitrators had extensive latitude to create awards according to their own sense of propriety or equity. n131 In Baseball, the collective bargaining agreement does not apportion a weight among the salary arbitration factors, so [*403] arbitrators have much discretion to apportion it themselves. n132 Weighting the factors could be an answer to some of this system's criticisms. Similarly, New Jersey authorizes consideration of finances, but critics argue that arbitrators do not account for the public's ability to pay enough; n133 specifying the weight an arbitrator must give to the ability to pay factor is a potential solution to this problem.

The parties' ability to weight the factors is a benefit of FOA over litigation. If the parties were to litigate their dispute, they would not, without a legal basis, be able to dictate which factors a judge could consider or how much weight the judge could give each one. Therefore the judge's resolution of the matter would be harder to predict than an arbitrator's, and the parties would have a more difficult time structuring their negotiations around a likely outcome.

E. *Reasoned Decisions*

The parties can control whether the arbitrator will issue a reasoned explanation of the decision. When arbitrators provide such decisions, they include considerable detail about how the application of the statutory criteria led to the decision on each issue. n134 In salary arbitration, there are no reasoned decisions, but some commentators believe this should be changed. n135 Other FOA sys-

tems, for example New Jersey, require such reasoning. n136 Reasoned decisions raise the monetary cost of FOA, but they ensure that the arbitrator applies the specified criteria appropriately.

A potential problem with requiring a reasoned decision is the plight facing arbitrators who believe a fair settlement is exactly in the middle of the two final offers. Such an arbitrator may have difficulty justifying one final offer over the other. If the arbitrator picks one final offer arbitrarily, then there might be sufficient grounds for a court to refuse to enforce the award. n137 Thus far, no parties have complained about the outcome of a FOA procedure on this basis.

[*404] F. *Simultaneous Announcement of Decisions*

In Baseball, arbitration decisions are publicized throughout the arbitration season. n138 One commentator has suggested that all salary arbitration awards should instead be announced simultaneously, thereby prohibiting arbitrators that decide cases late in the arbitration season from attempting to even the number of awards decided in favor of each side. n139 It would also prevent early decisions from influencing late ones. n140 If parties plan to send a large number of disputes to FOA in a short amount of time, they may want to consider simultaneous announcement of decisions as an option; if parties are implementing FOA to settle only one dispute, this option is inapplicable.

IV. FACTORS THE ARBITRATOR MAY CONSIDER

Researchers have concluded that arbitrators arbitrate in such a way that they will bolster their demand as arbitrators; to remain in demand, they objectively relate their awards to the arbitration criteria outlined by the parties. n141 Therefore, it is important for the parties to determine in advance the factors the arbitrator may consider when making a decision. Common criteria include: comparability, ability to pay, productivity, variations in job content or hazards, historical trends,

equity and forces within the marketplace. n142 Baseball has chosen to list ten factors specific to its industry that arbitrators may and [*405] may not consider. n143 Because comparability and ability to pay are controversial factors, they are discussed separately.

A. *Comparability Criteria*

Comparability criteria generally apply to employment disputes, but can be extended to other areas as well. In the employment context, comparability criteria authorizes arbitrators to compare wages, salaries, hours and working conditions of employees involved in the arbitration proceeding with the wages, salaries, hours and working conditions of employees who perform comparable duties in jurisdictions similar to those involved in the dispute. n144 Its theory is that employees who have similar responsibilities in similar communities should receive similar salaries. n145

Comparability has been criticized as leading to an unending spiral of wage increases n146 and for its reliance on data that are unclear, ambiguous and easily manipulated. n147 It also limits arbitrator discretion and prohibits innovation. n148 At the same time, the parties are prevented from proposing innovative final offers because the absence of a comparable solution elsewhere discourages the arbitrator from choosing the creation. n149 Some feel these constraints on [*406] arbitrator discretion and party creativity are appropriate because novel solutions should only result from negotiation or legislation, not by unilateral proposal by a party or an arbitrator. n150

Comparability criteria can be relevant in disputes over commodities other than labor and in disagreements over non-employment-related contract terms, for example, in the price of materials. If the parties are concerned about unusual proposals, they should include comparability criteria as a factor arbitrators should consider.

B. *Ability to Pay*

Ability to pay is another controversial FOA factor. If the arbitrator omits this factor from consideration, a solution unrealistic to a certain budget might result. Baseball prohibits salary arbitrators from considering the financial position of the player or the club; n151 this prohibition tends to be one of the main objections that Baseball owners have to salary arbitration. n152 Parties to FOA in other contexts allow arbitrators to consider ability to pay. n153

In labor relationships, employees have questioned whether an ability to pay factor is fair. n154 They argue that the price of no other commodity that an employer purchases, besides employee labor, is based on the employer's financial resources. n155 Since salaries won through arbitration are imposed instead of contracted for freely, however, the possibility that an award could [*407] place a party in financial trouble is inherent in the process. Therefore, parties should allow arbitrators to consider the financial viability of final offers. n156

Another problem with an ability-to-pay factor is that it often only reveals speculative information. n157 One solution to speculative "ability to pay" language in arbitration clauses is a specification which allows arbitrators to compare similar cost schedules in the same industry. For example, if competitors in the same market and the same industry have lower costs for a disputed item than a FOA party, the competitors will be able to offer a lower price; if the cost of the item to the FOA party is forced to rise because of an arbitral award, the ability of the arbitral pair to compete in the market could suffer. n158 Therefore, the costs to competitors of similar inputs should be a factor that the arbitrators may consider. To decide which competitors are similar, arbitrators should be authorized to consider geographic proximity, size, operations, unionization status and other relevant factors agreeable to the parties. n159 Finally, to avoid accounting disagreements, parties should agree on the method that will sufficiently demonstrate a party's ability to pay. n160

V. CRITICISMS OF FOA

Those considering FOA as a dispute resolution procedure should be aware of the common criticisms of the system: n161

A. *Narcotic Effect*

As with any form of arbitration, FOA has a potential "narcotic effect." n162 This phenomenon teaches parties who have previously used arbitration to rely on it to resolve future impasses and to refrain from resolving disputes without it. n163 Research shows the existence of a narcotic effect in FOA; when FOA is [*408] available to disputants, they implement it more often than those who use conventional arbitration. n164

In FOA, however, the narcotic effect is not disadvantageous. That those who use FOA declare impasses much more often than arbitrators implement awards demonstrates that FOA arbitrants use the process to facilitate negotiations. n165 Although FOA disputants may invoke arbitration more often than their conventional arbitration counterparts, they reach the arbitration hearing less often and submit fewer issues to the arbitrator. n166 Most cases settle between the date the arbitration is initiated and the date the arbitrator's decision is expected; only a small percentage are resolved by an arbitrator. n167

B. *Parties Must Understand FOA for it to Work*

Research indicates that FOA is most effective when the parties fully understand the nuances of the process. n168 They then try harder to settle and feel more positive about their opponent. n169

Experience seems to teach parties the skills necessary to effectively use FOA. n170 One study suggests that among arbitrators, patterns of deciding cases develop. n171 Therefore, even if a sin-

gle industry uses different arbitrators, the behavior of previous arbitrators predicts the behavior of future ones. n172 The study also suggested that as parties became more familiar with one another, they revealed more information during FOA, which helps each side achieve a more optimal solution. n173 It seems that salary arbitrants have learned to use [*409] FOA to their advantage. During the 1999 salary arbitration season, the clubs pushed for earlier and more advantageous settlements than in years past; they appeared to reach their objectives. n174

C. *Concerns About Package FOA*

Commentators criticize package FOA for several reasons. They argue that the system allows parties to include outrageous offers for a small percentage of issues in otherwise completely moderate and reasonable final offer packages. n175 They also complain that it is possible for the packages to be neither balanced nor reasonable, n176 yet the arbitrator must choose one nonetheless, potentially inflicting injustice on one party. n177 This possibility becomes more likely in package FOA as the number of issues in dispute rises. n178 Finally, critics assert that any portion of these situations could combine to force an arbitrator to select between two unreasonable offers. n179 The possibility that parties will maintain unreasonable positions is unlikely, however, because FOA rewards the more reasonable party and punishes the more extreme. n180

[*410] D. *Gamesmanship*

FOA has been criticized for encouraging "gamesmanship" or prompting the parties to focus on predicting the arbitrator's mindset instead of resolving the issues. n181 Even if this is true, FOA is still likely to encourage reasonable final offers that facilitate settlement.

E. *Baseball Might be an Anomaly*

Parties contemplating FOA should realize that they might not obtain Baseball's ninety percent settlement rate. The yearly repetition of the salary arbitration process probably contributes to the high settlement rate since it provides the parties with the opportunity to learn about and form expectations concerning the merits of, and their likelihood of success in, the process. n182

FOA might also be less effective for parties whose association will end after the arbitration. The parties to salary arbitration must continue to work together, so they have an incentive to make reasonable offers that will preserve their relationship. n183 Parties who will part after the arbitration might be motivated to make an unreasonable offer and hope that the arbitrator will choose it, providing them with a windfall. Although this type of behavior may discourage non-parties to the arbitration from arbitrating with the unreasonable party in the future, the unreasonable party will suffer no repercussion from the arbitration at issue since the relationship will end with the arbitration.

The absence of non-economic factors that encourage settlement might also contribute to a lower settlement rate outside of the Baseball context. The lure of multi-year, guaranteed contracts with bonuses and other perks is a strong incentive for many players and clubs to forego the salary arbitration hearing. n184 In other contexts, the absence of non-economic variables that are important to one or both parties might impede settlement.

VI. USING FOA IN DOMESTIC AND INTERNATIONAL DISPUTES

FOA is an ideal alternative dispute resolution procedure for many types of disputes. n185 Although this note has focused on a few disagreements in the [*411] United States that have found the process useful, there are numerous other kinds of disputes, both domestic and international, n186 that could also benefit from it. To illustrate, this section discusses selective types of disagreements, which for the reasons indicated, can benefit from FOA. n187

A. *Pricing Disputes*

When parties agree that a dispute is solely over the value of an item, rather than whether any money is owed, FOA is perfectly orchestrated to facilitate settlement. n188 Because of the risk of losing, parties that invoke FOA to solve a pricing dispute will have an incentive to propose reasonable prices. n189 Once they exchange their proposals, they can continue to negotiate. The midpoint analysis will help them (1) realistically assess the potential for the arbitrator to choose their proposed price; and (2) focus negotiations on the range of reasonable prices between the proposals. n190 If the final offers are close, a compromise number will be easy to reach. If the final offers are far apart, the high risk of proceeding to the arbitration hearing will encourage settlement. n191

[*412] FOA offers advantages over both litigation and conventional arbitration for pricing disputes. First, FOA is a simple process. As such, it is quicker and cheaper than litigation, and its associated appeals process, and conventional arbitration. Therefore, it will save participants money and limit the time during which the price is unreflective of the market in which they are operating. Second, FOA, unlike litigation and conventional arbitration, neutralizes the chilling effect by discouraging extreme pricing positions. n192 Therefore, the final offers are likely to be much closer together than in either conventional arbitration or litigation, in which the parties expect the neutral to split the difference. With close final offers, settlement is more likely. Third, FOA final offers represent prices the parties actually think are reasonable, as opposed to litigation and conventional arbitration demands, which often represent windfall positions. n193 Since the parties are likely to be more expert in their affairs than the arbitrator, reasonable prices created by them will provide the neutral with more guidance than the extreme demands generated in conventional arbitration and litigation. Fourth, parties with pricing disputes often continue to work together after the arbitration;

the lower antagonism associated with FOA as opposed to conventional arbitration and litigation will facilitate a return to a positive working relationship. n194 Fifth, parties who submit pricing disputes to FOA will have more control over the outcome since they will have notice of the neutral's options prior to the decision. In litigation and conventional arbitration, the parties make demands, but these often do not reflect what the neutral ultimately decides; since the range of decisions a neutral can make is vast, parties may overestimate their potential to prevail. In FOA, parties are more realistically able to assess their likelihood of winning the arbitration. Accordingly, they can weigh their risk and determine if settlement is more attractive then the probability that the neutral will choose their opponent's solution.

For parties with pricing disputes, FOA provides an additional advantage over litigation: flexibility. A court is constrained to apply the terms of a contract as they were originally executed. Since anticipating pricing disputes is not always possible, the contract may not account for such a dispute. Parties to FOA can create a FOA procedure either at the formation of the contract or when a pricing dispute arises. They can also authorize an arbitrator to evaluate whatever factors they deem important at the time of the arbitration and weight the factors when their import becomes clear. n195 This flexibility will allow the [*413] parties to use FOA to solve their dispute when litigation may be unhelpful. For all of these reasons, parties with pricing disputes may fare better in FOA that in either litigation or conventional arbitration.

Following are examples of pricing disputes that could benefit from FOA:

1. *Long-term contracts*

Increasingly common are long-term contracts for the provision of commodities like oil, coal, metal and uranium. n196 It is difficult to predict how these and associated markets will develop, so the long-term contracts often feature adjustment clauses that account for fluctuations in labor,

transportation and material costs, commodity indexes, import and export duties, insurance premiums and other factors that the parties believe might cause either an increase or decrease in the price of the commodity. n197 The clauses sometimes lead to disputes because it is difficult to measure the influence of many of these factors on price; the effect may be speculative or hard to differentiate from the contribution of other factors. n198 In these situations, the parties do not dispute that a price change is warranted. Their dispute focuses solely on the value of the price change.

In the absence of settlement, a FOA award may be better for both parties than a conventional arbitration or litigation award. For example, an increase in labor costs in a particular country might make it more expensive to produce materials there. A manufacturer/seller from that country and a buyer from another country may agree that a new price is required, but disagree as to an appropriate new value. When the dispute arises, the parties can design their arbitration system and designate changing labor costs as a factor the arbitrator can consider. This change may have been unforeseen at the time of contracting. If the parties choose litigation, the court may refuse to intervene unless the original contract provided for a revised price due to labor cost changes. Even if a court did agree to settle the dispute, the parties, who are from different countries, might encounter trouble enforcing a judicial decree.

Assuming a neutral is inclined to impose a new price, the parties would expect the neutral in litigation and conventional arbitration to compromise between their positions, so they would have incentive to assume extreme positions. The buyer, for example, would have an incentive to make an offer that is close, if not equal to, the original contract price. The seller would have [*414] an incentive to exaggerate the effect of the increased labor costs and argue that the price should rise substantially. From the final offers, the neutral would learn little about the price the parties actually thought was warranted and would probably compromise between the offers. If the parties imple-

mented FOA, the process would encourage them to calculate a reasonable price adjustment due to the labor cost changes. Their resulting reasonable proposals would facilitate settlement. Furthermore, if the parties choose litigation or conventional arbitration, it will be difficult for them to predict the neutral's decision and settle accordingly. FOA's midpoint analysis, however, would help them realistically assess their potential to win and the attractiveness of settlement. Finally, the lower antagonism associated with FOA will inflict less harm on the parties' continuing working relationship than would litigation and conventional arbitration.

2. *Construction cases*

Pricing disputes arising out of construction contracts are also amenable to FOA. Parties to these contracts sometimes disagree over fees for items and services outside of the original contract specifications, including claims for extensions of time, unanticipated work, additional expenses and disruption costs. n199 The parties may agree that the contractor is entitled to fees for which the contract does not account but disagree as to how much is owed. n200 For the same reasons that FOA may be a better option than litigation or conventional arbitration for pricing disputes arising out of long-term contracts, it can be a better option for pricing disputes arising out of construction contracts.

For example, in conventional arbitration or litigation, the incentive to assume extreme positions may encourage a contractor to claim that disruptions and delays caused millions of dollars in extra fees, while the contractee claims extra costs of only a few hundred thousand dollars or no extra costs at all. Presumably, an appropriate outcome is somewhere in the middle of the two proposals. Such a situation may force a conventional arbitrator or judge to speculate as to the appropriate award since the cause of the increased costs may be unclear. FOA would encourage the parties to realistically assess the value of the cost change and propose reasonable price adjustment. The neu-

tral would learn much more about an appropriate price from these FOA proposals than it would from conventional arbitration or litigation demands because they reflect the considered proposals that the parties themselves think are reasonable. The parties, after analyzing the final offers and predicting the potential for the arbitrator to choose each, may be able to settle. If they are unable to settle, the [*415] reasonable offers would facilitate a less adversarial arbitration and the award would likely be more acceptable; the parties would have had notice of the two possible awards and made a decision that both final offers were preferable to a settlement.

3. *Other pricing disputes*

Whenever parties agree that a fee is owed but disagree as to the appropriate value, FOA can facilitate settlement. Such disputes arise in countless types of situations and scenarios, including contract buyout cases, currency conversion disputes and disagreements over interest rates and royalties. This note discusses only a few examples of pricing disputes amenable to FOA, but the array is limited only by the imagination of contracting parties.

B. *Bifurcated Cases*

Increasingly, cases in which parties dispute both liability and damages are resolved in a bifurcated format, with liability determined first and damages later. n201 In such cases, damages can be awarded through FOA. Often, liability will be based on legality, whereas damages will be based on facts. Bifurcating these cases and using FOA in the second stage will allow parties to focus on the legal issues in the liability phase without confusion by factual issues that go to damages. Once liability is assessed, the parties can submit the damages dispute to FOA. Even if the damages are speculative, FOA will encourage the parties to make the most reasonable demands possible, thereby

facilitating settlement and offering the neutral as much help as possible if the neutral ultimately has to impose a solution.

FOA would be better than litigation or conventional arbitration of damages disputes for the same reasons it is advantageous in pricing disputes. n202 In addition, the two-stage process will increase the effectiveness of FOA. Research shows that the effectiveness of FOA increases as the parties learn more information about the neutral and the other party. n203 During the liability phase, the neutral and the parties will begin to build a working relationship and provide insight into their preferences and positions. The information exchange and the interactions between the parties during this phase will facilitate [*416] reasonable final offers that lead to settlement in the damages phase. The parties can rely on the information they learn during phase one when they create their final offers in the damages phase. In addition, the interactions between the parties during phase one will provide an opportunity for the parties to become familiar with each other and build trust. Some commentators believe that the repetition of salary arbitration and the working relationships it creates contribute to the 90% settlement rate. n204 Although parties to a two-phase bifurcated proceeding will not recreate the frequent repetition of salary arbitration, the two phases will, on a smaller scale, increase the effectiveness of FOA and facilitate settlement of damages claims.

Arbitrating instead of litigating a bifurcated proceeding gives the parties the option of using FOA arbitration in phase two. In court, FOA is not an option for a judge. Therefore, bifurcated judicial proceedings which determine liability and damages in different stages use, as a predicate in the damages phase, demands that are likely to represent extreme positions. Settlement discussions based on these demands are likely to be victims of the chilling effect. If the parties choose to combine conventional arbitration and FOA, they will benefit from a litigation-type proceeding for liability, but gain the benefits of FOA at the damages stage.

Examples of types of cases and specific cases that could have been bifurcated and submitted to FOA at the damages stage follow:

1. *Frustration and impracticability*

Circumstances sometimes arise causing courts in America and Europe to find that as a consequence of events unforeseen at the time of contracting, a contract's purposes are frustrated or performance is impracticable. n205 The courts then either excuse performance or adjust the terms of the contract. n206 If the contract is terminated, one of the parties may seek reimbursement for losses due to nonperformance. The losses are likely to be speculative, and FOA can facilitate an acceptable solution for both parties. Because FOA can be implemented after the unforeseen events occur, the parties can authorize the [*417] FOA arbitrator to consider the unforeseen circumstances as factors. A judge would not be able to consider these factors if they had not been addressed in the original contract.

An example of a frustration case which could have been bifurcated and FOA implemented at the damages phase occurred between a claimant, a French contractor, and a defendant, the Ministry of Finance of an African country. n207 The claimant agreed to construct, complete and maintain certain building, mechanical and electrical works for the airport in the defendant's country. n208 At the same time, the claimant was excavating a canal, located 300 km from the airport, for the Ministry of Irrigation of the defendant's county. n209 The claimant was subjected to a terrorist attack at the canal site, and its employees were taken hostage. n210 To secure release of the hostages and for the safety of other employees, the claimant ceased work at the canal site, but left a skeleton crew there for minor maintenance work. n211 After subsequent terrorist attacks, the claimant completely evacuated the canal site. n212 Work at the airport initially continued uninterrupted, but after the claimant fully evacuated the canal site, it concluded that the airport could become a target.

n213 The contractor accordingly ceased work at the airport and evacuated the airport camp except for a minimum number of employees who maintained custody of the equipment and tools. n214 The French Embassy then received threats of violence if the airport work resumed. n215

The claimant filed for arbitration, alleging frustration or impossibility. n216 It requested compensation for increased costs and losses; the defendant disputed the contractor's claims and moved for damages for breach of contract. n217 The arbitrators issued a partial award in which they determined that the claimant was entitled to suspend work due to frustration; they deferred decision on relief. n218 The arbitrators also determined that the defendant was not entitled to recover damages or to obtain other relief against the claimant. n219

[*418] At the damages stage, FOA may have been a better alternative than conventional arbitration. The arbitrators had already determined liability, so the sole remaining issue was the value of damages. Since the value of future losses due solely to the frustration was speculative and the final offers by the parties were likely to represent extreme positions, a conventional arbitrator would have had to speculate as to an appropriate outcome. To influence that determination, the parties would have been motivated to assume extreme positions. In FOA, the parties would have had incentive to propose a reasonable value of damages. Since the parties know more information about their dispute than any neutral could, their reasonable FOA final offers likely would have represented solutions better for them than any created by a third party. By neutralizing the chilling effect in this manner, FOA could have facilitated negotiations, helped the parties settle or contributed to a better arbitration decision.

2. *Breach of contract*

An example of a breach of contract case that could have benefitted from FOA in the damages stage concerned failure to perform allegations. The claimant was a purchaser from a West African

country that provided telecommunications services in that country. The defendant was a supplier from the United States who manufactured telecommunications equipment. n220 The parties negotiated a contract for sale, delivery and installation of some of the defendant's equipment. n221 Due to technical problems, the defendant installed the equipment late; after installation, it failed to operate normally. n222 Both parties attempted to repair the equipment locally, but they eventually determined that it was inappropriate for the site. n223 The claimant then revoked its acceptance of the defendant's equipment and covered by purchasing other equipment from another manufacturer. n224

The parties attempted to negotiate a settlement, but resorted to ICC conventional arbitration after they reached an impasse. n225 The claimant requested repayment of the contract price, the cost of cover (the difference between the contract price for the original equipment and the substitute), and [*419] incidental and consequential damages. n226 The defendant requested that the arbitrators reject the claimant's claims and counter-claimed for the costs of the repairs. n227

The arbitration panel determined that the claimant was entitled to revoke acceptance of the equipment. It then granted the claimant's claims for repayment of the contract price and incidental damages, granted in part the claimant's claim for cost of cover and rejected the claimant's claim for consequential damages. n228 The arbitrators rejected the defendant's counterclaims in full. n229

If the parties had used package FOA at the damages phase, they may have settled their claims without third-party intervention. Assuming that the arbitrators correctly assessed the facts and liability, this indicates that the claimant had overestimated the value of the defendant's liability and the defendant had grossly underestimated its liability. Package FOA would have motivated the parties to parse the issues submitted to arbitration. n230 To create the most reasonable offer, the claimant would have had an incentive to forego some of the claims for which its arguments were

weakest, like for consequential damages. The defendant would have been motivated to acknowledge that it was liable for some damages and make a final offer accordingly. The parties thus would have settled more issues themselves, giving them more control over the ultimate outcome. Further, the final offers likely would have been closer together than the final offers under the conventional arbitration format and settlement more likely. If the parties had not compromised when they created final offers, for example, if they had assumed the same positions they did in the actual case, they would have faced a high risk that the arbitrator would choose the other side's offer. This would have provided great motivation for the parties to settle before the hearing. By encouraging the parties to parse the issues and propose reasonable final offers, and by imposing a high risk of losing at the arbitration, FOA could have facilitated a better outcome than conventional arbitration or litigation. Even if the parties had not settled, their voluntary compromises would have made each final offer a more acceptable solution than the final offers made in the conventional arbitration format.

[*420] 3. *Construction cases*

Unlike the scenario in which parties to a construction contract agree that extra fees are owed, but disagree as to the new value, some parties to construction disputes disagree on whether extra fees are owed at all. In these cases, the neutral must first decide whether fees are owed; conventional arbitration can be used at the liability phase and FOA at the damages stage.

A specific example of a construction dispute that could have been bifurcated and the damages dispute submitted to FOA occurred between a claimant, a European contractor, and a defendant, the Ministry of Public Works of a Middle Eastern country that hired the claimant to construct a highway. n231 The claimant eventually submitted claims to arbitration for extensions of time, extra works, additional expenses, delay, disruption costs and miscellaneous other cost items. n232 The defendant asserted that some claims were inadmissible and all others were precluded by the con-

tract. n233 With a minor exception, the arbitrators found that the defendant was liable for all of the claimant's claims. n234

Assuming that the arbitrators correctly interpreted the contract, then the facts of the case lead to the conclusion that the claimant had a much stronger argument than the defendant as to entitlement for additional fees. Had the parties opted for bifurcated FOA, the arbitrators could have decided in phase one that the defendant was liable. In phase two, the defendant would have had an incentive to make the claimant a reasonable monetary offer. Once the defendant made a reasonable offer, the parties may have been able to settle. That the defendant claimed it owed nothing likely impeded settlement negotiations during the dispute. The defendant also probably anticipated, due to the conventional arbitration format, that it would win at least some of its arguments and that the arbitrator would compromise on damages. With package FOA, the defendant would have known that if the arbitrator decided the issues, it would either lose or win them all. Since the defendant's arguments were apparently much weaker than the claimant's, the defendant would have had an incentive to compromise and propose a final offer that would have facilitated settlement. The negotiated settlement would likely have been a better outcome for both parties.

[*421] 4. *Other bifurcated cases*

Like the array of pricing disputes amenable to FOA, bifurcated cases about any subject, whose second phase will resolve a numerical dispute, are amenable to FOA. Examples of bifurcated proceedings that can benefit from FOA, like those of pricing disputes, are too numerous to list. n235

VII. CONCLUSION

FOA is a dispute resolution procedure that can help parties with a large variety of numerical disputes reach solutions without third-party intervention. Despite its advantages over litigation and conventional arbitration, however, FOA has yet to be widely embraced. If parties with either inter-

national or domestic disputes disagree over a numerical value and desire a dispute resolution procedure that promotes settlement and provides cost and time efficiency, they should seriously consider final offer arbitration.

Legal Topics:

For related research and practice materials, see the following legal topics:
Civil ProcedureAlternative Dispute ResolutionArbitrationsGeneral OverviewCopyright LawFormalitiesArbitration Royalty PanelsInternational Trade LawDispute ResolutionArbitration

FOOTNOTES:

n1 Tom Arnold, *Vocabulary of ADR Procedures*, 51 (Oct.) DISP. RESOL. J. 74, 77 (1996). The process was first proposed by Carl Stevens in 1966. *See* Carl Stevens, *Is Compulsory Arbitration Compatible with Bargaining*?, 5 INDUSTRIAL RELATIONS 38 (February 1996). For descriptions of modern implementations of the system, *see* Major League Baseball Agreement, Article VI F(5) (1997) [hereinafter Agreement]. *See also* SPORTS LAW, § 5.05[4][c]; John J. Gallagher and Margaret H. Spurlin, *Interest Arbitration Under the Railway Labor Act*, SA31 ALI-ABA 459, 474 (1996); Joseph R. Grodin, *Either or Arbitration for Public Employee Disputes*, 11 INDUS. REL. 260 (May 1972); and Gary Long and Peter Feuille, *Final-Offer Arbitration: "Sudden Death" in Eugene*, 27 INDUS. & LABOR. REL. REV. 186, 192 (1974).

n2 *See* Gallagher and Spurlin, *supra* note 1 at 474. *See also* Arnold, *supra* note 1 at 77.

n3 *See infra* at text accompanying notes 9-47.

n4 Baseball players and owners created salary arbitration during collective bargaining in reaction to Baseball's history of reserve clauses and collusion. Baseball team owners proposed salary arbitration in an effort to retain control over the players' services instead of allowing them to become free agents. The players agreed to salary arbitration because they wanted some influence over their salaries pre-free agency. They also wanted a system that would ensure that the owners paid them a fair wage. Interview with John Westoff, attorney for the Major League Baseball Players' Relation Committee (August 19, 1998). For a more in-depth discussion of Baseball's history of reserve clauses and collusion, *see* Jonathan M. Conti, *The Effect of Salary Arbitration on Major League Baseball*, 5 SPORTS L. J. 221, 223-28, 232 (1998). *See also* Thomas Hopkins, *Arbitration, A Major League Effect on Players' Salaries*, 2 SETON HALL J. SPORT L. 301, 302-11, 314 (1992); Frederick Donegan, *Examining the Role of Arbitration in Professional Baseball*, 1 SPORTS L. J. 183, 184-88, 197-98; (1994); and Jack F. Williams and Jack A. Chambless, *Title VII and the Reserve Clause: A Statistical Analysis of Salary Discrimination in Major League Baseball*, 52 U. MIAMI. L. REV. 461, 472-77 (1998).

Players are eligible for salary arbitration only if they have between three and six years of experience in Baseball. *See* Agreement, *supra* note, 1 Art. VI F(1). Players with at least two but less than three years of Baseball experience who have accumulated at least eighty-six days of service during the immediately preceding season and who rank in the top seventeen

percent in total service in the class of players who have at least two but less than three years of Baseball experience are also eligible for salary arbitration. *See id.*

n5 *See* CONN. GEN. STAT. ANN. § 22a-285g (West 1999); D.C. CODE § 1-618.2 (1981); IOWA CODE ANN. § 20.22 (West 1999); ME. REV. STAT. ANN. tit. 13 § 1958-B(5)(A) (West 1998); Minn. Stat. Ann. § 179A.16 (Subd. 14)(West 1998); N.J. STAT. ANN. § 34:13A-16c (West 1999); OKLA. STAT. ANN. tit. § 51-108(4) (West 1999); PA. STAT. ANN. § 11-1122-A, 23-A, 24-A, 25-A (West 1999); WASH. REV. CODE. ANN. § 35.21.779, 47.64.240 (West 1999) and WIS. STAT. ANN. § 111.77(4)(b), 289.33 (West 1988). *See also* Paul Gordon, *Submitting "Fair Value" to Final Offer Arbitration*, 63 U. COL. L. REV. 751, 758 (1992); Michael Finch and Trevor Nagel, *Collective Bargaining in the Public Schools: Reassessing Labor Policy in an Era of Reform,* 1984 WIS. L. REV 1573, 1628 n. 214; and Arvid Anderson, *Presenting an Interest Arbitration Case: An Arbitrator's View*, 3 LAB. LAW. 745 (1987).

n6 The IRS and Apple chose FOA to resolve a dispute arising out of the IRS' belief that Apple was shifting income out of the country by overpaying for parts manufactured at its Singapore subsidiary. *See* Jay A. Soled, *Transfer Tax Valuation Issues, The Game Theory, and Final Offer Arbitration: A Modest Proposal for Reform*, 39 ARIZ. L. REV. 283, 305-06 (1997).

n7 There have been proposals to adopt FOA in other contexts, for example, in bankruptcy disputes, *see* Mary Bedikian, *Bankruptcy Practitioners: Alternative Dispute Resolution*

(ADR) for Bankruptcy Claims. 780 PLI/COMM 353, 362 (Nov.-Dec. 1998), and fair value disputes between stockholders and companies. *See generally*, Gordon, *supra* note 5. FOA has also been endorsed as an ADR method that attorneys should suggest to their clients. *See* Robert Fitzpatrick, *Shouldn't We Make Full Disclosure to Our Clients of ADR Options?* SD34 ALI-ABA 29, 45-46 (1998). The FCC has a FOA system in place, but it is unclear whether the agency has used it. *See* 1060 PLI/CORPORATION 321.

n8 There are no reported cases of international final offer arbitration.

n9 Interest arbitration is a collective bargaining procedure designed to avoid strikes while resolving labor disputes over the terms of a contract. By contrast, rights arbitration interprets the terms to which the parties previously agreed. *See* Paul L. Burgess & Daniel R. Marburger, *Do Negotiated and Arbitrated Salaries Differ Under Final-Offer Arbitration*? 46 IND. and LAB. REL. REV. 548 (1993). *See also* Anderson, *supra* note 5 at 757. Interest arbitration is also different from grievance arbitration, which interprets or applies an existing contract. *See* Philip E. Garber, *Compulsory Arbitration in the Public Sector: A Proposed Alternative*, 26 ARB. J. 226, 228 (1971).

n10 *See* Burgess & Marburger *supra* note 9. For discussion of the history of strikes, *see* R. Theodore Clark, Jr., *Public Employee Strikes: Some Proposed Solutions*, 2 LAB.L.J. 111 (1972).

n11 *See* Burgess & Marburger *supra* note 9. To value final offer arbitration as a process, one must assume that bargaining is good, and impasses or strikes are bad. *See* Peter Feuille, *Final-Offer Arbitration and Negotiating Incentives*, 32 ARB. J. 203, 204 (Sept. 1977). West-off interview, *supra* note 4.

n12 *See* Jeffrey Chicoine, *A Critical Review of Collective Bargaining Dispute Resolution Under the PECBA and Alternative Models*, 13 LERC MONOGRAPH SER. 53, 67 (1994); and Long *supra* note 1 at 188.

n13 *See* Chicoine, *supra* note 12 at 67. *See also* Long *supra* note 1 at 189; Gallagher and Spurlin, *supra* note 1 at 473; and Joan Weitzman and John M. Stochaj, ATTITUDES OF ARBITRATORS TOWARD FINAL-OFFER ARBITRATION IN NEW JERSEY, 35 ARB 25, 27 (1980).

n14 *See* JAMES L. STERN & JOYCE M. NAJITA, LBR. ARB. UNDER FIRE 118 (1997). *See also* Chicoine, *supra* note 12 at 67.

n15 *See* Chicoine, *supra* note 12 at 67.

n16 *See* Long *supra* note 1 at 189. *See also* Conti, *supra* note 4 at 231; Chicoine, *supra* note 12 at 67; Donegan, *supra* note 4 at 191-92; Gallagher & Spurlin, *supra* note 1 at 473; and Stern & Najita *supra* note 14 at 118. Research suggests that judges, like arbitrators, are

likely to compromise between the valuation estimates of the parties, thereby discouraging negotiation between litigants. *See* Soled, *supra* note 6 at 289-91 and 289 & n.40.

n17 *See* Stern & Najita *supra* note 14 at 118.

n18 *See* Long *supra* note 1 at 188; Weitzman & Stochaj, *supra* note 13 to 27.

n19 *See* Long *supra* note 1 at 202 (1974). *See also* Howard G. Foster, *Final Offer Selection in National Emergency Disputes*, 27 ARB. J. 85, 89 (1972); and Paul I. Perlman, Note, *Final Offer Arbitration: A Pre-Trial Settlement Device*, 16 HARV. J. LEG. 513, 516-25 (1979).

n20 *See* Stevens, *supra* note 1 at 46; and Long *supra* note 1 at 190. Some believe FOA also provides public sector unions with an effective means to compel serious, as opposed to surface, bargaining in the absence of the right to strike. *See* Lawrence T. Holden Jr., *Final Offer Arbitration in Massachusetts*, 31 ARB. J. 26, 28 (1976). *See also* Conti, *supra* note 4 at 232-33.

n21 *See* Holden, *supra* note 20 at 28. Research suggests that FOA, as compared to conventional arbitration, effectively increases the probability of negotiated settlements by requiring the parties to bargain in the context of a high risk "strikelike" impasse resolution procedure. *See* Long *supra* note 1 at 203. *See also* Robert J. Martin, *Fixing the Fiscal Police and Firetrap: A Critique of New Jersey's Compulsory Interest Arbitration Act*, 18 SETON HALL

LEGIS. J. 59, 73 (1993); Gordon, *supra* note 5 at 772. *See also* Amy Farmer & Paul Pecorino, *Bargaining with Informative Offers: An Analysis of Final-Offer Arbitration*, 27 J. LEGAL STUD. 430 (1998). *But see* Charles M. Rehmus, *Is a "Final Offer" Ever Final?,"* 79 MONTHLY LBR. REV. 43 (Sept. 1974) (arguing that final offer arbitration is not better than conventional arbitration at ending stalemates, but that those who were able to settle under conventional arbitration continue to do so, and those who could not, go to the arbitrator); and Holden, *supra* note 20 at 28. For an explanation of how game theory encourages settlement in final offer arbitrations, *see* Soled, *supra* note 6 at 304. For a comparison of the costs of disagreement under compulsory arbitration and conventional negotiation, *see* Long *supra* note 1 at 188-90.

n22 *See* Fizel, *Play Ball, Baseball Arbitration After 20 Years*, 49-J. DISP. RESOL. J. 42, 46 (1994). *See also* Donegan, *supra* note 4 at 191-92.

n23 Interview with David Cohen, General Counsel, New York Mets (August 18, 1998); interview with Michael Weiner, Assistant General Counsel, Major League Baseball Players' Association (August 20, 1998); and Westoff interview, *supra* note 4. These factors will differ depending on the arbitration agreement between the parties. *See e.g. infra* at text accompanying notes 141-55.

n24 Cohen and Weiner interviews, *supra* note 23. *See also* Conti, *supra* note 4 at 234; Fizel, *supra* note 22 at 44; Arnold, *supra* note 1 at 77; and Robert G. Howlett, *Interest Arbitration in the Public Sector*, 60 CHI-KENT L. REV. 815, 830 (1984).

n25 Cohen and Weiner interviews, *supra* note 23. *See also* SPORTS LAW *supra* note 1 at § 5.05[4][c] & n.87; and Hopkins, *supra* note 4 at 310. On the same day each year, all players and clubs participating in a salary arbitration submit their "final offer" by exchanging the offers with each other. There is no requirement in the Agreement that the offers be filed on the same day, but generally, all final offers are filed on the last possible day. This practice is customary because the clubs and players want to file their final offers after collecting as much information about other settlements as possible. Cohen and Weiner interviews, *supra* note 23.

n26 Cohen and Weiner interviews, *supra* note 23.

n27 *Id.*

n28 *See* Farmer & Pecorino, *supra* note 21 at 415, 416, 430.

n29 Weiner interview, *supra* note 23.

n30 Cohen and Weiner interviews, *supra* note 23.

n31 Cohen interview *supra* note 23. When the parties assess their position's relation to the midpoint and its likelihood of success at the arbitration, they consider the same factors that the arbitrator can consider. *Id.*

n32 Cohen and Weiner interviews *supra* note 23. Brian Cashman, the General Manager of the New York Yankees, agrees that the midpoint is an important factor to consider during post-final offer salary arbitration negotiations. *See* Ronald Blum, *Jeter Agent Says Next Move is Yanks',* AP ONLINE, February 17, 1999, available in LEXIS, News Library, Curnws file.

n33 Cohen and Weiner interviews, *supra* note 23.

n34 Cohen interview *supra* note 23.

n35 Weiner interview, *supra* note 23.

n36 Cohen interview, *supra* note 23.

n37 *See* Stevens, *supra* note 1 at 46. *See also*, Long *supra* note 1 at 190.

n38 Cohen interview, *supra* note 23 and Westoff interview *supra* note 4. FOA, however, can be adversarial. *See* C. Raymond Grebey Jr., *Another Look at Baseball's Salary Arbitration*, 38 ARB. J. 24, 30 (1983); and James B. Dworkin, *Salary Arbitration in Baseball: An Impartial Assessment After Ten Years*, 41 ARB. J. 63 (1986). Some players have been offended by treatment they received from their clubs during salary arbitration. *See* Williams & Chambless, *supra* note 4 at 484-85. The New York Daily News reported that the New York Yankees jeopardized their relationship with All-Star outfielder Bernie Williams when they insisted on setting his salary through arbitration. The 1999 salary arbitration between the

Yankees and Derek Jeter may have had the same result. *See* Peter Botte, *Jeter is Shocked by Table Manners/Gets Earful in Arbitration*, NEW YORK DAILY NEWS, February 16, 1999 at 25; and Ken Davidoff, *Posada First to Feel Pinch as Yankees Tighten Purse*, THE RECORD (Bergen County, NJ), March 3, 1999 at S02. *See also* Peter Botte, *Yank Dollars Irk Posada Catcher at 350g*, NEW YORK DAILY NEWS, March 3, 1999 at 60; Blum *supra* note 32; and Ronald Blum, *Jeter Beats Yankees in Arbitration*, AP Online, February 16, 1999 available in LEXIS, News Library, Curnws File. Even so, conventional arbitration and litigation, the alternatives to final offer arbitration, are much more destructive to working relationships than final offer arbitration. *See* Gordon, *supra* note 5 at 780. *See also* Michael Pryles, *Assessing Dispute Resolution Procedures*, 7 AM. REV. INT'L ARB. 267, 273 (1996). For further discussion about FOA and its effect on the relationship between the parties, *see* Long, *supra* note 1 at 190.

n39 *See* Cohen and Weiner interviews, *supra* note 23 and Westoff interview, *supra* note 4.

n40 *See* Cohen and Weiner interviews, *supra* note 23.

n41 *See* Weiner interview, *supra* note 23.

n42 *See id.*

n43 *See* Fizel *supra* note 22 at 44.

n44 *See* Fizel, *supra* note 22 at 46. In 1996, 76 players filed for arbitration, 10 went to a hearing. In 1997, 80 players filed, 5 went to a hearing. In 1998, 81 players filed, 8 went to a hearing. Statistics provided by the Major League Baseball Players' Association, notes on file with author. In 1999, 62 players filed, 11 went to a hearing. *See* Steve Repsher, *Roundup*, THE WASHINGTON TIMES, 5D, 16 Jan. 1999. *See also*, Hal Bodley, *Average Salary Increased $ 1.25M for 38 in Arbitration*, USA TODAY, 4C, 22 Feb. 1999. For statistics from previous years, see Fizel, *supra* note 22 at 44; Conti, *supra* note 4 at 232-33; and Donegan, *supra* note 4 at 192-93. This note went to publication before the 2000 arbitration season.

n45 Prior to the enactment of Michigan's final offer statute, 40% of public sector employment cases submitted to an arbitrator settled before the arbitrator announced an award. *See* Gordon, *supra* note 5 at 772. *See also* Howlett, *supra* note 24 at 827-28. During a comparable period after Michigan enacted FOA, 70% settled before an arbitrator announced an award. *See* Gordon, *supra* note 5 at 772. A number of cities used FOA during the 1970s with similar results. *See e.g.* Fred Witney, *Final Offer Arbitration: The Indianapolis Experience*, 96 MONTHLY LBR. REV. 20, 23 (May 1973). In New Jersey, from the implementation of FOA through 1980, there were no police or firefighter strikes, and the rate of voluntary settlement was high. *See* Martin, *supra* note 21 at 62.

n46 *See* James L. Stern, *Final Offer Arbitration-Initial Experience in Wisconsin*, 97 MONTHLY LBR. REV. 40, 41 (Sept. 1974).

n47 *See* Richard A. Lester, *Analysis of Experience Under New Jersey's Flexible Arbitration System*, 44 ARB. J. 14, 19 (June 1989). *See also* Weitzman & Stochaj *supra* note 13 at 27-28.

n48 *See* Feuille *supra* note 11 at 219. One arbitrator has stated that although avoiding arbitration is the goal of FOA, "the world is evil, and there are times when a final-offer award must be issued." *See* Harold Newman, *Interest Arbitration: Impressions as a PERB Chairman*, 37 ARB.. J. 7 (Dec. 1982).

n49 FOA appears to reduce the number of issues submitted to arbitration. *See* Howlett, *supra* note 24 at 831. The Eugene, Oregon experience with FOA suggests that the process is effective at narrowing the area of disagreement around many monetary and nonmonetary issues. *See* Long *supra* note 1 at 203. The Eugene experience also suggests, however, that FOA might be less effective at bridging gaps between party positions on issues that require a yes or no answer. *See* Long *supra* note 1 at 203. For a discussion of the convergence of final offers in Baseball, see B. Jay Coleman, Kenneth M. Jennings & Frank McLaughlin, *Convergence or Divergence in Final-Offer Arbitration in Professional Baseball*, 32 INDUSTRIAL RELATIONS 238 (1993); and Conti, *supra* note 4 at 233-34. *See also* Fizel *supra* note 22 at 44-45 (concluding that final offers in salary arbitration have failed to converge or diverge because of inflation, increased team attendance and increased television revenue).

n50 *See* Soled, *supra* note 6 at 306 & n.104. The IRS also preferred final-offer arbitration because it wanted to test the viability of FOA under the Tax Court's Rule 124 in a transfer

pricing dispute; Rule 124 allows the IRS and taxpayers to choose arbitration to settle disputes. *See id.* at 310 & n.104.

n51 *See* Soled, *supra* note 6 at 306. *See also* Richard Sansing, *Voluntary Binding Arbitration as an Alternative to Tax Court Litigation*, NATIONAL TAX JOURNAL, 6 January 1997; and *After Successful Use of Baseball Arbitration, Apple, IRS Both Declare Themselves Winners*, 11 ALTERNATIVES TO HIGH COST LITIG. 163, 163-64 (Dec. 1993) (hereinafter "Apple, IRS Both Declare Themselves Winners").

n52 *See* James P. Fuller, *Intercompany Pricing Under Section 482 in the Context of Joint Venture Operations*, 444 PLI/TAX 841, June 1999. *See also* Sansing, *supra* note 51; and *Apple, IRS Both Declare Themselves Winners* at 163-64, *supra* note 51.

n53 *See* Agreement, *supra* note 1 at VI F(5). *See also* SPORTS LAW *supra* note 1 at § 5.05[4][c].

n54 *See* Agreement, *supra* note 1 at VI F(3)(a) and (b). *See also* SPORTS LAW *supra* note 1 at § 5.05[4][c].

n55 Approximately one month after the final offers have been submitted, a hearing will take place. *See* Agreement, *supra* note 1 at VI F(3)(a), (b) and (5). *See also* SPORTS LAW, *supra* note 1 at § 5.05[4][c].

n56 The arbitrator has 24 hours to make a decision after the hearing. *See* Agreement, *supra* note 1 at VI F(5). *See also* SPORTS LAW, *supra* note 1 at § 5.05[4][c]. At least one commentator believes that Baseball should relax the time constraint on the arbitrator. *See* Conti, *supra* note 4 at 244-45.

n57 *See* Agreement Art. VI F(5) *supra* note 1.

n58 *See* GARY B. BORN, INT'L COMM. ARB. IN THE UNITED STATES, COMMENTARY & MATERIALS 2, 43 (1994). *See also* Martin Hunter, Jan Paulsson, Nigel Rawling & Alan Redfern, THE FRESHFIELDS GUIDE TO ARB. AND ADR, CLAUSES IN INT'L CONTRACTS 26-27 (1993).

n59 *See* Born *supra* note 58 at 61. One commentator has suggested that it is difficult to anticipate international disputes which might be appropriate for FOA. *See* James T. Peter, *Med-Arb in International Arbitration*, 8 AM. REV. INT'L ARB. 83, 101 (1997).

n60 If there is only one issue in dispute, as in salary arbitration (where only the numerical value of a player's one-year salary is at issue), there is no difference between issue-by-issue and package final offer arbitration.

n61 *See* Garber, *supra* note 9 at 232. *See also* Richard Kirschner, *Labor Management Relations in the Public Sector: An Introductory Overview of Organizing Activities, Bargaining*

Units, Scope of Bargaining, and Dispute Resolution Techniques, SD09 ALI-ABA 271, 296 (1998); and Conti, *supra* note 4 at 230.

n62 *See* Stern & Najita *supra* note 14 at 118.

n63 *See* Kirschner, *supra* note 61 at 296. *See also* Conti, *supra* note 4 at 230 and Charles M. Rehmus, *Varieties of Final Offer Arbitration*, 37 ARB. J. 4, 5 (Dec. 1982).

n64 *See* Chicoine, *supra* note 12 at 68. *See also* Conti, *supra* note 4 at 230; Garber, *supra* note 9 at 232; Stern & Najita *supra* note 14 at 118; Witney, *supra* note 45 at 23 (criticizing FOA because the most reasonable final offer might fail to meet the needs of the parties or it might be inequitable or undesirable); and Stern, *supra* note 46 at 42.

n65 *See* Chicoine, *supra* note 12 at 68. *See also* Conti, *supra* note 4 at 230.

n66 Feuille "*Final Offer Arbitration and the Chilling Effect*" in D. LEWIN, FEUILLE & KOCHAN, EDS. PUBLIC SECTOR LBR. RELATIONS: ANALYSIS AND READINGS 299 & 301 (1977).

n67 *See* Howlett, *supra* note 24 at 830. *See also* Soled, *supra* note 6 at 289-91 and 289 & n. 40.

n68 *See id.*

N69 *See* BORN *supra* note 58 at 2.

n70 *See* Pryles, *supra* note 38 at 271.

n71 *See id. See also* Arnold, *supra* note 1 at 77.

n72 *See* Pryles, *supra* note 38 at 271.

n73 *See* Long *supra* note 1 at 198. This option is only relevant if the dispute concerns at least some non-numeric issues. For example, it would not work for salary arbitration in which the only issue is the monetary value of a one-year salary.

n74 *See id.*

n75 *See* Rehmus, *supra* note 63 at 5.

n76 *See E.g.* IOWA CODE ANN. § 20.22 (West 1999); PA. STAT. ANN. § 11-1123-A (West 1999); and WIS. STAT. ANN. § 111.77(4)(b) (West 1999).

n77 *See* Daniel G. Gallagher, *Interest Arbitration Under the Iowa Public Employment Relations Act,* 33 ARB. J. 30, 32 (1978). *See also* Rehmus, *supra* note 63 at 6. Although dis-

putants in New Jersey have the option of a fact-finder, they have not implemented fact-finding as an option. *See* Lester, *supra* note 47 at 15.

n78 *See* Gallagher, *supra* note 77 at 35.

n79 *See* Daniel G. Gallagher & Richard Pegnetter, *Impasse Resolution Under the Iowa Multistep Procedure*, 32 INDUS. AND LBR. REL. REV. 327, 338 (1979).

n80 *See* Holden, *supra* note 20 at 32. Massachusetts no longer compels its government to submit to mandatory binding final offer arbitration. MASS. GEN. LAWS ANN. ch. 150E § 1, NOTES OF DECISIONS 2 (West 1999). After determining that the Commonwealth could not be bound by mandatory arbitration, Massachusetts limited its alternative dispute resolution to voluntary procedures. *See* 1980-81 Mass. Op. Atty. Gen. 128. The change was not influenced by an opinion about final offer arbitration as a process. Phone interview with former Massachusetts Attorney General Francis Bellotti, September 28, 1999.

n81 *See* Gallagher and Pegnetter, *supra* note 79 at 338.

n82 *See* Gallagher, *supra* note 77 at 34.

n83 *See id.*

n84 *See* Feuille, *supra* note 11 at 212. Research found that 70% of settlements in Iowa that involved a fact-finder were based on the fact-finder's recommendation. Similar statistics were gathered in Massachusetts. *See* Rehmus, *supra* note 63 at 6.

n85 *See* Gallagher, *supra* note 77 at 31.

n86 *See id.*

n87 *See E.g.*, MICH. COMP. LAWS. ANN. § 423.238 (West 1978). *See also* Martin, *supra* note 21 at 66-67.

n88 *See e.g.* Holden, *supra* note 20 at 27. *See also e.gs.* Stern, *supra* note 46 at 40; and Long *supra* note 1 at 191-9 and 192 & n.21. Wisconsin has used a system which combines FOA with other alternative dispute resolution procedures. After either party requested arbitration, the Wisconsin Employment Relations Commission investigated the dispute to determine whether an impasse had been reached. *See* Stern, *supra* note 46 at 40. During the investigation, the Commission conducted an intensive mediation effort and would order arbitration only if it concluded that mediation failed. *See id.* If the Commission approved arbitration, the parties could request conventional arbitration, but the default was FOA. *See id.*

n89 New Jersey's Employer-Employee Relations Act, for example, suggests six arbitration formats among which the parties can choose: 1. conventional arbitration of all unsettled issues; 2. package FOA in which the arbitrator chooses between the last offer of the employer

as a single package and the last offer of the employees' representative as a single package; 3. issue-by-issue FOA in which the arbitrator chooses, for each issue, between the last offers of the employer and the employees' representative; 4. package FOA in which the arbitrator chooses one package of final offers as proposed by a fact-finder, the employer or the employees' representative; 5. issue-by-issue FOA in which the arbitrator chooses, for each issue, among a fact-finder's recommendation, the employer's last offer and the employees' representative's last offer; and 6. a hybrid approach in which the parties submit economic issues to package FOA and non-economic issues to issue-by-issue FOA. N.J. STAT. ANN. §§ 34: 13A-16c(1) to (6) (West 1999).

n90 *See* Garber, *supra* note 9 at 237.

n91 *See* Farmer & Pecorino, *supra* note 21 at 430.

n92 *See e.g.* Martin, *supra* note 21 at 79. *See also* James W. Mastriani, *Interest Arbitration for Protective Services in New Jersey, New Jersey Public Employer-Employee Relations No. 6* (New Jersey Institute of Management and Labor Relations, Rutgers University, 1977) *cited* in Weitzman and Stochaj, *supra* note 13 at 27; and Long *supra* note 1 at 192.

n93 *See* Pryles, *supra* note 38 at 273.

n94 *See* Agreement *supra* note 1 at VI F (11).

n95 *See* HUNTER, et, al., *supra* note 58 at 26-27.

n96 *See infra* this section.

n97 *See* BORN *supra* note 58 at 60.

n98 *See* BORN *supra* note 58 at 60. *See also* Garber, *supra* note 9 at 235; and Witney, *supra* note 45 at 24.

n99 *See* Garber, *supra* note 9 at 235. *See also* Witney, *supra* note 45 at 24.

n100 *See* Garber, *supra* note 9 at 235. *See also* Tom Arnold, *Suggested Form of Contract to Arbitrate a Patent or Other Commercial Dispute, Annotated*, C976 ALI-ABA 229, 232 (1994).

n101 *See* Garber, *supra* note 9 at 235. *See also* Arnold, *supra* note 100 at 232.

n102 *See id.*

n103 *See id.*

n104 The arbitrators were a retired federal judge, an economist and an industry expert. *See Apple, IRS Both Declare Themselves Winners* at 163-64, *supra* note 51.

n105 *See* Long *supra* note 1 at 192.

n106 N.J. STAT. ANN. §§ 34:13A-16e (West 1999).

n107 *See* Agreement *supra* note 1 at Art. VI F (7). Under the present agreement, the structure of the arbitration panel changes each year. In 1997, one arbitrator settled each dispute unless a request was made for a three-arbitrator panel. In 1998, a single arbitrator settled half of the disputes, and a three-arbitrator panel settled the other fifty percent. In 1999, seventy-five percent of the arbitrations went to a three-arbitrator panel and twenty-five percent went to one arbitrator. In 2000 and 2001, one hundred percent of the arbitrations will be decided by three-arbitrator panels. *See* Agreement *supra* note 1 at Art. VI F (7).

n108 Cohen interview, *supra* note 23.

n109 *Id.*

n110 Weiner interview, *supra* note 23.

n111 *Id.*

n112 Arbitrators are chosen from a jointly agreed upon list of arbitrators that often does not change from year to year. Cohen interview *supra* note 23. *See also* Agreement *supra* note

1 at Art. VI F (7). An arbitrator whose decisions are disfavored by either the players or the clubs is likely to be stricken from the list in the following year. Cohen interview, *supra* note 23. The clubs felt that being an arbitrator for Major League Baseball is a prestigious job, and they were concerned that for job preservation, a single arbitrator would decide an even amount of cases for each side, regardless of the merits. *Id.*

n113 Cohen interview, *supra* note 23.

n114 Westoff interview, *supra* note 4.

n115 *Id.*

n116 *See* BORN *supra* note 58 at 61.

n117 *See id. See also* HUNTER, et. al., *supra* note 58 at 26-27.

n118 N.J. STAT. ANN. §§ 34:13A-16e (West 1999). *See also* Weitzman & Stochaj, *supra* note 13 at 26 (1980).

n119 *See* Agreement at VI F(7).

n120 *See id. See also* Fizel, *supra* note 22 at 43.

n121 *See Apple, IRS Both Declare Themselves Winners* at 164, *supra* note 51.

n122 *See id.*

n123 *See* BORN *supra* note 58 at 62.

n124 *See generally id.* at 63-66.

n125 *See* Witney, *supra* note 45 at 23-24.

n126 *See id.* at 24.

n127 *See id.*

n128 *See id.*

n129 *See* Stern & Najita *supra* note 14 at 125.

n130 *See id.*

n131 *See* Gregory G. Dell'Omo, *Wage Disputes in Interest Arbitration: Arbitrators Weigh the Criteria*, 44 ARB. J. 11, *cited* in Stern & Najita *supra* note 14 at 118.

n132 *See* John P. Gillard, Jr., *An Analysis of Salary Arbitration in Baseball: Could a Failure to Change the System be Strike Three for Small-Market Franchises?*, 3 SPORTS LAW. J. 125, 135 (1996). *See also* Hopkins, *supra* note 4 at 332.

n133 *See* Martin, *supra* note 21 at 62, 91-93.

n134 *See* Lester, *supra* note 47 at 20.

n135 *See* Agreement, *supra* note 1 at Art. VI F (5). *See also* Conti, *supra* note 4 at 244-45; Gillard *supra* note 132 at 136; and Hokins, *supra* note at 333.

n136 *See* N.J. STAT. ANN. § 34:13A-16(f)(5) (West 1999).

n137 Courts review arbitration awards under an arbitrary and capricious standard. *See e.g.* Brown v. Rauscher Pierce Raefnes Inc., 994 F. 2d 775, 781 (11th Cir. 1993); and Randall v. Lodge No, 1076, 648 F. 2d 462, 465 (7th Cir. 1981). If a reviewing court determines that an arbitrator imposed an award on an arbitrary basis, the court will likely overturn the award.

n138 Salary arbitration hearings occur throughout the month of February, and decisions are announced within 24 hours of the hearing. *See* SPORTS LAW, *supra* note 1 at § 5.05[4][c]. *See also* Agreement, *supra* note 1 at Art. VI F (5).

n139 *See* Conti, *supra* note 4 at 244-45.

n140 *See id.*

n141 *See* Burgess & Marburger *supra* note 9 at 549.

n142 *See* Martin, *supra* note 21 at 68. *See also* Tim Bornstein, *Interest Arbitration in Public Employment: An Arbitrator View of the Process*, 83 LBR. J. 77, 83 (1978).

n143 A salary arbitrator may consider: the player's contribution to his team during the past season, special qualities of leadership and public appeal, the length and consistency of his career contribution, his compensation history, comparative salaries, the existence of any physical or mental defects on the part of the player, the recent performance record of the team (including but not limited to its league standing) and attendance as an indication of public appeal. *See* Agreement, *supra* note 1 at Art. VI. F(12). *See also* SPORTS LAW, *supra* note 1 at § 5.05[4][c]. The salaries of players in comparable positions, skill and seniority generally get the most attention at the hearings. *See* Labor Law and Collective Bargaining at 274. Arbitrators are not permitted to consider the club's or player's financial position, the press or similar commentary except for annual player awards, offers made by either side prior to the arbitration, the costs to the parties of their representatives, attorneys, etc., salaries in other sports or occupations or the requirements of Major League Baseball's Luxury Tax system. *See* Agreement, *supra* note 1 at Art. VI F(12)(b)(i)-(v) and (14). *See also* Williams & Chambless, *supra* note 4 at 480.

n144 *See* Martin, *supra* note 21 at 69. *See also e.g.s* N.j. STAT. ANN. §§ 34:13A-16(g) (West 1999); and Agreement, *supra* note 1 at Art. VI. F(12) and SPORTS LAW, *supra* note 1 at § 5.05[4][c] & n.90.

n145 *See* Martin, *supra* note 21 at 69. *See also* Michael Fox, *Criteria for Public Sector Interest Arbitration in New York City: The Triumph of Ability to Pay and the End of Interest Arbitration*, 46 ALB. L. REV. 97, 101 (1981).

n146 *See* Monroe Berkowitz, *Arbitration of Public-Sector Interest Disputes: Economics, Politics and Equity*, 1976 PROCEEDINGS NAT'L ACAD. OF ARB. 160, 167.

n147 *See* Arnold M. Zack, Comment, 1971 PROCEEDINGS NAT'L ACAD. OF ARB. 189.

n148 *See* Charles C. Mulcahy and Marion E. Mulcahy, *Innovation as the Key to a Redesigned and Cost Effective Local Government*, 78 MARQ. L. REV. 549, 571-72 (1995).

n149 *See id.*

n150 *See* Gallagher & Spurlin, *supra* note 1 at 475.

n151 *See* Agreement note 1 at Art. VI. F(12)(b).

n152 *See* Gillard, *supra* note 132 at 134-35. The owners complain that salaries for players have undergone massive increases since FOA began and even players who lose at the arbitration receive a pay raise. *See* Conti, *supra* note 4 at 222, 234-35. *See also* Williams and Chambless, *supra* note 4 at 480; and Fizel, *supra* note 22 at 42. Indeed, throughout the history of salary arbitration, only nine players have received salary decreases as a result of the system. Fizel, *supra* note 22 at 45. The reasons for this outcome, however, might relate to the unique labor market of baseball players. Before they are eligible for arbitration, players are bound to play for their team at whatever price the team decides to pay them. When they become arbitration-eligible, they are compensated based on a competitive labor market. Therefore, much of the salary increase can be attributed to the move from the monopsonistic labor market of pre-arbitration eligible players to the competitive labor market of the arbitration eligible players. Statistics show that even with the large increases in salary due to arbitration, players are still paid below their market value when their salaries are set through the salary arbitration system. *See* Fizel, *supra* note 22 at 44-45, 46-47. *See also* Conti, *supra* note 4 at 235-42; and Hopkins, *supra* note 4 at 316-17.

n153 *See e.g.* Stern *supra* note 46 at 40; and Long *supra* note 1 at 192.

n154 *See* Martin, *supra* note 21 at 70.

n155 *See id.* at 70 & n.64. *See also* Fox *supra* note 145 at 103; and HARRY EDWARDS et. al., LBR. RELATIONS LAW IN THE PUBLIC SECTOR, CASES AND MATERIALS 755 (4th ed. 1991).

n156 Including this factor in the FOA analysis could lead to disputes over the computation of ability to pay. If one party desires this factor enough, however, the parties should be able to agree on a computation.

n157 *See* Fox *supra* note 145 at 101. *See also* Martin, *supra* note 21 at 70.

n158 *See* Gallagher & Spurlin, *supra* note 1 at 469.

n159 *See id.*

n160 One party might distrust the other's claims of financial inability. This has been true in baseball. *See* Williams & Chambless, *supra* note 4 at 484. To avoid this complication, the parties should agree on the type of accounting acceptable to all.

n161 For a more in-depth analysis of the most common objections to final offer arbitration, *see generally*, Nels E. Nelson, *Final-Offer Arbitration: Some Problems*, 30 ARB. J. 50 (1975). *See also* Martin *supra* note 21 at 61; and Feuille *supra* note 11 at 204.

n162 *See* Stern & Najita *supra* note 14 at 118.

n163 *See id.*

n164 *See* Feuille, *supra* note 11 at 219.

n165 *See id.* at 216.

n166 *See supra* at text accompanying notes 43-51.

n167 *See id. See also supra* at text accompanying notes 43-47.

n168 Angelo S. DeNisi & James B. Dworkin, *Final-Offer Arbitration and the Naive Negotiator*, 35 INDUS. AND LBR. REL. REV. 78, 79 (1981). For the DeNisi & Dworkin study, full understanding of the process entailed more than familiarity with the rules; it included review of a detailed, videotaped demonstration of negotiations, the arbitration and participant reactions. *See id.* at 80-81.

n169 *See id.* at 87.

n170 *See id. See also* Lester, *supra* note 47 at 21.

n171 *See* DeNisi & Dworkin *supra* note 168 at 238.

n172 *See id.* When arbitrators make decisions, they reveal previously concealed information such as their idea of a fair wage, wage comparability and the ability of the employer to

pay. *See id.* at 240. *See also* Craig A. Olson & Barbara L. Rau, *Learning From Interest Arbitration: The Next Round,* 50 INDUS. and LAB. REL. REV. 237, 241 (1997).

n173 *See* DeNisi & Dworkin, *supra* note 168 at 240.

n174 *See* Associated Press, *Players Get Record Pay Raises*, THE LAS VEGAS REV., February 23, 1999, at 5. Of the thirty-seven players in 1998 who avoided a hearing and agreed to a one-year contract, twenty-two settled below the midpoint, seven settled at the midpoint and eight players settled above the midpoint. In 1999, there were nineteen players who avoided a hearing and agreed to a one-year contract. Twelve settled below the midpoint, seven settled at the midpoint and none settled above the midpoint. Settlements in 1999 also came earlier than they had in the past with twenty-four of the sixty-two arbitration eligible players settling before numbers were exchanged. *See id.*

n175 *See* Howlett, *supra* note 24 at 830. *See also* Garber, *supra* note 9 at 232; and Chicoine, *supra* note 12 at 68. At least one researcher found that parties are unlikely to include extraneous issues in final offer packages. *See* Howlett, *supra* note 24 at 830.

n176 *See* Chicoine, *supra* note 12 at 68. *See also* Howlett, *supra* note 24 at 831; and Peter, *supra* note 58 at 101.

n177 *See* Rehmus, *supra* note 63 at 435. *See also* Martin, *supra* note 21 at 72; Clark, *supra* note 10 at 120; and Weitzman & Stochaj *supra* note 13 at 27.

n178 *See* Peter *supra* note 58 at 101.

n179 *See* Clark, *supra* note 10 at 120. *See also* Martin, *supra* note 21 at 73

n180 *See* Martin, *supra* note 21 at 73; Howlett, *supra* note 24 at 830; and *supra* this note at text accompanying notes 18-24. Clark suggests that a neutral fact-finder making recommendations prior to the submission of final offers would reduce the potential for unreasonable offers. *See supra* note 10 at 120. For reasons why a fact-finder might be undesirable, see *supra* at text accompanying notes 82-86.

n181 *See* Weitzman & Stochaj *supra* note 13 at 27.

n182 *See generally*, Olson & Rau, *supra* note 172.

n183 *See infra* note 37.

n184 Weiner interview, *supra* note 23. *See also supra* at text accompanying notes 40-42.

n185 For a general discussion of the merits of alternative dispute resolution, *see generally* Tom Arnold, *Why ADR?*, 493 PLI/PAT 245.

n186 The examples in this note demonstrate that FOA is compatible with the law and culture of dispute resolution in the United States. If parties in countries other than the United States wish to implement FOA for a domestic dispute, they should familiarize themselves with the law and culture of alternative dispute resolution in the country that will enforce their contract to ensure that FOA is a suitable option.

FOA is compatible with the rules governing international arbitrations. Two major sets of rules governing international arbitration, written by the ICC and UNCITRAL, do not dictate the kind of award that international arbitrators may create. *See* ICC RULES OF ARB. and UNCITRAL ARB. RULES *in* DOMINIQUE HASCHER, COLLECTION OF PROCEDURAL DECISIONS IN ICC ARBITRATION 1993-1996, 230, 274 (1997). Therefore, the parties are free to place restrictions on the arbitrator's decision, like a requirement that the arbitrator choose between the final offers. One commentator, James Peter, has suggested that FOA's main function is to induce concessions. *See* Peter, *supra* note 58 at 101. He asserts that because international arbitrators are bound by the law, international arbitrants do not assume extreme positions in expectation of a compromise by an arbitrator; therefore, he concludes that the "the main incentive to agreeing to [FOA] in international arbitration loses weight." Peter, *supra* note 58 at 101. Peter does not offer empirical support for his assertion that international arbitrants do not assume extreme positions, and regardless of the arbitrator's duty to apply the law, the conventional arbitration format provides parties with an incentive to posture during bargaining and assume extreme positions. Even if Peter is correct, international disputants can benefit from FOA's timing and cost efficiencies, so they have much incentive to consider it.

n187 The examples that follow are based on disputes between international parties, but they exemplify disagreements that can occur between domestic parties as well.

n188 Since the only issue is price, issue-by-issue and package arbitration are the same.

n189 *See supra* text accompanying notes 22-27.

n190 *See supra* text accompanying notes 30-36.

n191 *See supra* text accompanying notes 18-21.

n192 *See supra* text accompanying notes 12-21.

n193 *See supra* text accompanying notes 12-17.

n194 *See supra* note 38.

n195 *See supra* text accompanying notes 129-133 and 141-160.

n196 Interview with Professor Hans Smit, January 19, 1999. Professor Smit is an international law and arbitration professor at Columbia Law School and Editor-in-Chief of *The American Review of International Arbitration*.

n197 *See generally*, W.E. Shipley, *"Escalator" Price Adjustment Clauses*, 63 A.L.R. 2d 1337 (1959).

n198 Smit interview, *supra* note 196.

n199 Smit interview, *supra* note 196.

n200 *Id.*

n201 *See e.g.* Lewis v. Intermedics Intraocular, 1998 WL 139988, *3 (E.D.La. 1998); Longo v. F.W. Woolworth Co., 1997 WL 642993, * 1 & n. 2 (E.D.Pa. 1997); Burger v. Mays, 176 F.R.D. 153, 155 & n.1 (E.D. Pa. 1997); John Cheeseman Trucking, Inc. v. Dougan, 805 S.W.2d 69, 70 (Ark. 1991); Shpritzman v. Strong, 670 N.Y.S.2d 50 (N.Y. 1998); Moody v. Dykes, 496 S.E.2d 907, 909 (Ga. 1998).

n202 *See supra* text accompanying notes 188-194.

n203 *See supra* text accompanying notes 170-174.

n204 *See* DeNisi & Dworkin *supra* note 168 at 238.

n205 *See generally*, Hans Smit, *Frustration of Contract: A Comparative Attempt at Consolidation*, 58 COL. L. REV. 287 (1958). *See also* Burlington N. and Santa Fe Ry. Co., v.

Kansas City S. Ry. Co., 45 F. Supp. 2d 847, (D. Kan. 1999); Bank of Am. Nat'l Trust and Sav. Assoc. v. Envases Venezolanos, 740 F. Supp. 260, 266 (S.D.N.Y 1990); and Howard v. Nicholson, 556 S.W. 2d 447, 481-82 (Mo. Ct. App. 1977). *See also* E. ALLEN FARNSWORTH, CONTRACTS 700-37 (2d ed. 1990).

n206 *Id.*

n207 *See* SIGVARD JARVIN, YVES DERAINS & JEAN-JAQUES ARNALDEZ, COLLECTION OF ICC ARBITAL AWARDS 1986-1990 101 (1994).

n208 *See id.*

n209 *See id.*

n210 *See id.* at 102.

n211 *See id.*

n212 *See id.* at 103.

n213 *See id.* at 104.

n214 *See id.*

n215 *See id.* at 104-105.

n216 *See id.* at 106.

n217 *See id.*

n218 *See id.*

n219 *See id.*

n220 *See id.* at 27.

n221 *See id.* at 27-28.

n222 *See id.*

n223 *See id.*

n224 *See id.*

n225 *See id.*

n226 *See id.*

n227 *See id.*

n228 *See id.*

n229 *See id.*

n230 Had they used issue-by-issue FOA arbitration, the outcome likely would have been the same as under conventional arbitration because the parties' incentive to parse the issues would have been absent.

n231 *See id.* at 189.

n232 *See id.* at 191.

n233 *See id.*

n234 *See id.* The tribunal did find for the defendant on one ground. *See id.* at 198.

n235 Additional illustrative examples include damages claims arising from intellectual property disputes over copyrights, patents and trademarks. Phase one would determine if a

copyright, patent or trademark is held by one party and was infringed by the other and if so, phase two could determine the damages owed.

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