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Part 1 – ABI Model Local Mediation Rule
Part 2 - Lehman Brothers Claim Facility

IIAMA International and MWI Mediation Training Program
Cambridge, Massachusetts
September 21-25, 2015

Introduction

I am particularly excited and honored to participate in this program and share some of my experiences and thoughts with you. Latin America, particularly Brazil, is one of the more frequent regions generating involvement in cross-border insolvency cases that are filed in the US.

BRAZIL, along with a few other Latin American countries, is a member state of the United Nations Commission on International Trade Law, commonly known as UNCITRAL, which has produced a model law on cross-border insolvency, adopted in the US as Chapter 15 of the Bankruptcy Code. My work in this area involves this law in significant respects. My partners at CBInsolvency are well known in this area, and some of you may have met them – Daniel Glosband from the firm Goodwin Procter here in Boston and Judge Leif Clark from Texas, a well-known recently retired bankruptcy judge.

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Mediation and other forms of Alternative Dispute Resolution have become an integral and substantial part of the legal landscape affecting bankruptcy practice as much as other practice areas such as litigation, employment law, labor law, and marital dissolution.

Early in my career in the 80's, I developed a keen interest in mediation, and became an advocate for its use in bankruptcy cases in the US. I have seen it develop over this time from a small community-based practice, with lawyers volunteering in a district to serve as a mediator in small matters that could not sustain any significant expenditure on legal costs, to today, where the largest bankruptcy proceedings use mediation to resolve multi-million dollar disputes as well as to achieve consensual plans of reorganization. For the past 5 years, I have served as one of 4 court-appointed mediators to assist in the resolution of complex, multi-party derivative contract disputes in the Lehman Brothers bankruptcy case in New York City. MWI has served as my Case Manager for this engagement, and has served in that role for me in other insolvency engagements as well, including Circuit City, Enron and Dura Automotive.

My talk with you today will provide a brief history of how the use of mediation has developed in one of the nation's most specialized courts, the courts of bankruptcy. There is at least one bankruptcy court in each state, and the largest states have several in different cities. Each of these courts may have more than one judge. Here in Massachusetts, we have one bankruptcy court, with 3 divisions – Boston, Worcester and Springfield, and there are a total of 5 judges, with three in Boston. By contrast, New York has 4 courts, each with some divisions, and a total of 20 judges when I last counted. All of These courts are part of the federal judicial system, as opposed to the state, and they are administered through a centralized system based in Washington DC. However, each court is authorized to promulgate its own local rules. It is in these local rules that we find the mediation procedures in use today around the country.

Today we are going to take a closer look at the provisions of a local rule for using

mediation in a bankruptcy case, and we will also look at the specific ADR Procedural Order entered in the Lehman bankruptcy case governing the specific use of mediation in that case. The local rule we will be looking at is a recently published model rule drafted by the American Bankruptcy Institute, the premiere educational and networking organization for all things bankruptcy here in the US. I was the founding chair of the ABI's Mediation Committee in 1996, and I helped to draft the Model Local Rule. So I am a good person to speak to you about it, but one drawback is I may not remember these things that well. So I have these notes. However, another drawback is that I may not be able to read them that well. And so it goes.

Audience Participation

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It is important to note at the outset that there are basically two kinds of mediation that can go on in bankruptcy cases as a result of the nature of the relief bankruptcy affords. I will be speaking about business or company bankruptcies, but the principles also apply to individual bankruptcies. When a company or person files for bankruptcy or has a bankruptcy filed against it which is accepted, all of the company's or person's assets, liabilities and affairs are subject to the jurisdiction of the court. There may be several legal disputes that are ongoing or may arise in the context of the bankruptcy, and each dispute may be the subject of a specific action in the bankruptcy court overseeing the bankruptcy case. In the Lehman bankruptcy case, there were hundreds of disputes and depending on what matters you would include, such as specific creditor claims that were filed and were disputed, hundreds of thousands of discrete disputes. Any of these could potentially be the subject of mediation. I will talk a little more about that in a few minutes.

The other type of mediation that has been more recently developed into the practice is the mediation of the company's plan of reorganization to conclude its bankruptcy case. In

our bankruptcy system, the person or company is given the right to choose between attempting to reorganize or simply liquidate its assets and distribute funds to creditors. I understand the system is similar in Brazil. Of course, creditors have a substantial say in what happens in any case. It is that right held by the creditors that gives rise to the opportunity to use mediation to achieve a consensually based plan, and save a lot of time and costs that would otherwise be expended by the parties if they were unable to negotiate an agreed-upon plan to begin with.

In either type of mediation, the specific dispute within a case mediation and the more global plan mediation, the mediation is generally authorized by the presiding judge pursuant to an existing local rule of the court. In most of the bankruptcy courts, the mediation rule was developed by the court working with the local bar of attorneys. Often, the development of a rule was the culmination of the experiences of practitioners who began to using mediation on an ad hoc basis in their cases. In still other places, mediation was initiated in cases at the suggestion of certain judges who were progressive in their judicial function, or who at least had too big a caseload!

In the late 80's and early 90's, there was very limited use of mediation in bankruptcy cases. In 1994, out of the ninety bankruptcy courts in the US, there were 9 bankruptcy courts with mediation rules, 9 considering the adoption of a rule, and 7 with frequent ad hoc ADR use. Over the next decade and into the early 2000's, mediation became more widely accepted. By 1998, at least twenty-eight bankruptcy courts (or approximately 30% of the courts) had local rules, and it really reached a tipping point as we approached 2010, particularly with the financial crisis of 2008 and the filing of the Lehman case, which has been the largest and most complex insolvency case in bankruptcy history by a wide margin.

At the present time, approximately fifty of the ninety bankruptcy courts in the United States are using mediation pursuant to local bankruptcy rules, general orders, or

guidelines.[1] Several more are at some stage of consideration regarding the implementation of an ADR program, and still others have been noted for frequent ad hoc use of ADR or an existing federal district court mediation rule.[2] These numbers are continually changing and increasing.[3] The proliferation of mediation programs in our bankruptcy courts mirrors the development of ADR in the judicial system generally. The Alternative Dispute Resolution Act of 1998 and prior federal legislation has resulted in the development of ADR programs in the nation's federal district courts.[4]

So let's now take a look at a typical bankruptcy court local rule, the Model Mediation Rule from the ABI, and see how one of our courts has implemented mediation in its jurisdiction.

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[1] Jacob A. Esher, Am. Bankr. Inst., *Compendium Of Bankruptcy Court Local Rules On ADR* (21st Annual Winter Leadership Conference 2009).

[2] *See* Robert J. Niemic, *Bankruptcy Courts With Court-Annexed ADR Procedures* (Working paper, Federal Judicial Center, on file with the author); Jacob A. Esher, *Compendium of Bankruptcy Court Local Rules on ADR (American Bankruptcy Institute, Winter Conference Materials 2009)*.

[3] The Federal Judicial Center's preliminary report in 1994 indicated 9 bankruptcy courts with mediation programs, 9 considering such a program, and 7 with frequent ad hoc ADR use. Robert J. Niemic & Jeffrey Reich, *ADR in Bankruptcy Courts: Summary of Local Bankruptcy Rules & General Orders on ADR* (Federal Judicial Center 1994) (unpublished draft on file with the author). By 1998, at least twenty-eight bankruptcy courts (or approximately 30%) had local rules, general orders, or guidelines in place that governed judicial referral of bankruptcy matters to mediation. Robert J. Niemic, *Mediation in Bankruptcy: The Federal Judicial Center Survey of Mediation Participants* at 5 (Federal Judicial Center 1998). By the summer of 2008, only forty of the nation's bankruptcy courts did not have a local rule concerning ADR. Jacob A. Esher, *Compendium of Bankruptcy Court Local Rules on ADR (American Bankruptcy Institute, Winter Conference Materials 2009)*.

[4] 28 U.S.C. §§651-658 (2000); Judicial Improvements & Access to Justice Act, 28 U.S.C. §§651-658 (1988); Civil Justice Reform Act, 28 U.S.C. §471 (1990). For a comprehensive and detailed work on Federal District Court ADR programs and results, *see* Elizabeth Plapinger & Donna Stienstra, ADR & Settlement In The Federal District Courts (1996), a sourcebook for judges and lawyers, a joint project of the Federal Judicial Center & the CPR Institute for Dispute Resolution.

ABI Model Local Rule

American Bankruptcy Institute - Bankruptcy Court Local Mediation Rule (Rule 9019)

Slide 1.

a) Types of Matters Subject to Mediation - this model rule says any dispute can be referred to mediation, within the court's discretion. While some matters may not be suitable to mediation for public policy reasons, that is a case-by-case exception typically.
b) Effects of Mediation on Pending Matters – this rule provides the case continues on unaffected unless otherwise ordered; often, litigation may be suspended or time frames extended to allow for mediation to take place where necessary or appropriate, again at the court's discretion

Slide 2.

The Rule provides general guidelines for how the mediation will be conducted, who should attend, what should be submitted, and scheduling – generally all in the discretion of the mediator, but with notice to the parties of what is or has occurred should there be separate meetings with parties, which is common in bankruptcy mediation. The rule also provides that the mediator may report to the court should a party fail to comply with the rules.

(c) The Mediation Conference –Informal Mediation Discussions
    i. Time and Place of Mediation Conference
    ii. Submission Materials
    iii. Attendance at Mediation Conference
        i. Persons required to attend
        ii. Persons allowed to attend
        iii. Failure to attend
    iv. Mediation Conference Procedures
    v. Settlement Prior to Mediation Conference

Slide 3.

Maintaining The Confidentiality of mediation is of paramount importance, so the Rule has extensive provisions regarding this

ii. Confidentiality of Mediation Proceedings
    i. Protection of Information Disclosed at Mediation
    ii. Discovery from Mediator
    iii. Protection of Proprietary Information
    iv. Preservation of Privileges
    v. Recommendations by Mediator

Slide 4.
The rule provides general procedures for concluding the mediation, dealing with any required filings and reporting the results to the court; it also says the agreement reached in mediation may not be disclosed to the court unless it was intended to be and is in fact binding on the parties

(f) Post-Mediation Procedures
  (i) Filings by the Parties
  (ii) Mediator's Certificate of Completion
  (iii) If the Agreement in Principle is not completed

Slide 5.
The Rule provides procedures for or terminating the mediation, and provides that mediators have the same immunity from liability for their actions as a mediator as a judge would have for court proceedings, except for actual fraud or other willful misconduct.

(g) Withdrawal from Mediation
(h) Termination of Mediation
(i) Applicability of Rules to a Particular Mediation
(j) Immunity

Any questions on the Rule and what we have talked about at so far?

Now we will look at how mediation has been used in specific cases, particularly in the Lehman Brothers case, for which I served as a mediator during the past 5 years. Lehman used mediation in what is often referred to as a "Claim Resolution Facility" or an "ADR Procedure" or "Protocol".

Use of Mediation in Claim Facilities

The use of claim resolution facilities, which use structured negotiation and mediation to resolve large numbers of disputed matters in substantial insolvency cases in the US, was developed in the 1990's in the context of significant Chapter 11 cases and has become a standard feature in cases involving hundreds or thousands of disputed creditor claims and recovery actions.

A claim resolution facility is a custom-designed alternative dispute resolution program

using structured negotiation, mediation and, sometimes, arbitration to resolve disputed claims in insolvency cases. The program, the terms and implementation of which must be approved by the bankruptcy court after notice and hearing, is typically drafted, proposed and administered by attorneys representing the Chapter 11 debtor business or its representative.

The facility enhances prospects of reaching a negotiated settlement by promoting the exchange of necessary information and providing a procedure for the exchange of a settlement offer and a counteroffer. If the structured negotiation provisions do not yield a quick settlement, the facility will provide for mediation to commence with mediators previously approved by the court based on recommendations usually made by the debtor or its representative. If mediation is not successful, some facilities may then provide for arbitration.

Since these procedures are not governed by formal rules of evidence and procedure, there can be a significant saving of time and cost for all parties. The success of the early facilities has made them a mainstay in today's practice. In one of the first uses of a facility in the 1990s, the procedure implemented in the Greyhound Bus Chapter 11 case involved more than 3,000 claimants.[5] The procedure was subsequently used successfully in many other cases involving substantial numbers of disputed claims.[6]

Experience demonstrates that voluntary settlements occur in the great majority of matters where facilities are used, with the majority of the settlements occurring even prior to the mediation stage. A recent example is in the Lehman Brothers liquidating Chapter 11 cases in the Southern District of New York, where structured negotiation and mediation was used to manage and resolve hundreds of disputes arising from early

[5] *Eagle Bus Mfg., Inc. v. Rogers,* 62 F.3d 730, 734 n. 6, 27 BCD 982, 983-84 (5th Cir. 1995).
[6] *See In re Kmart Corporation, et. al,* Case No. 02-B02474 (SPS) (Bankr. D. Del. 2002); *In re Harnischfeger Industries, Inc.,* Case No. 99-2171 (PJW) (Bankr. D. Del. 2000); *In re Venture Stores, Inc.,* Case No. 98-101-RRM (Bankr. D. Del. 1998); *In re Rich's Department Stores, Inc.,* Case No. 96-11793-JNF (Bankr. D. Mass. 1998).

termination of derivative contracts due to the bankruptcy filings.[7] A June 2015 status report states that over $2.9 billion was collected by the Lehman Estate in 410 ADR matters resolved with 527 counterparties. Of the 235 disputes that went through mediation and were concluded as of the time of the report, 219 were settled and only 16 failed to reach settlement.[8] A similar facility has been used to manage and seek resolution of numerous clawback actions in the Madoff SIPA liquidation case, although public reporting of the results has not been provided.[9]

So let's take a look at how a claims facility is put together and how it works, using the Lehman Claim Facility, or ADR Procedure, as a guide.

The Lehman Claim Facility

REFER TO POWER POINT SLIDES

ADR Procedures Order – Lehman Brothers

Slide 1:
The Order first incorporates the Court's Standing Order, which in the Southern District of New York takes the place of a local rule and has the same effect as a local rule. It is often procedurally easier for a court to issue a standing order instead of a local rule, so this is not uncommon. The NY Standing Order is similar to the Model Rule in most important respects. The rest of these initial provisions are about how the mediation is to be enabled in these particular disputes.

1. Standing Mediation Order
2. Derivatives ADR Counterparties
3. Derivatives ADR Disputes
    a) When Debtors shall not implement ADR Procedures
    b) Must make commercially reasonable efforts

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[7] *In re Lehman Bros. Holdings Inc.*, No. 08-13555 (SCC) (Bankr. S.D.N.Y. 2008). The author is one of the court-appointed mediators in this case.
[8] Id., Letter to Honorable Judge Shelley C. Chapman Regarding Sixty-Seventh ADR Status Report (9 June 2015, ECF No. 49939).
[9] Order (1) Establishing Litigation Case Management Procedures for Avoidance Actions and (2) Amending the February 16, 2010, Protective Order, In re Bernard L. Madoff, SIPC v. Bernard L. Madoff Investment Securities LLC, Adv. Pro. No. 08-01789 (SMB), Dkt. No. 3141, 10 November 2010 (Bankr. S.D.N.Y. 2008).

c) Indenture Trustees subject to Order
d) Delivery of notice

Slide 2:
These are more enabling procedures – please note that his procedure was a mandatory one, in which the court has ordered that the Debtor here, Lehman Brothers, was allowed to compel parties to attend mediation of their dispute in New York, but only after notice and an opportunity to settle the matter prior to mediation, as set forth in the next slide.

4. Settlement of Disputes During the Derivatives ADR Procedures
    (a) Any settlement discussions, the contents of papers submitted for mediation, and all discussions in mediation shall remain confidential and shall not be discovering as evidence in subsequent litigation
    (b) Participation Mandatory
5. No Substitute for Claims Procedures
6. Debtor's Rights

Slide 3:
Here, the procedure is as I described for a claims facility generally, with a notice, demand, counteroffer and settlement conference stage preceding a mediation. As I mentioned, out of the 410 matters that got to this stage, about half were settled prior to mediation.

- Notice/Response Stage
    - Exchange settlement offers and attempt to resolve dispute
    - Debtor provides notice containing sufficient information, and Counterparty must respond in writing within 30 days
        - Agree to or deny settlement demands
        - Failure to respond
    - Requesting the initial settlement conference

Slide 4:
These procedures are general and are quite similar to the types of provisions in the local rule, with the exception that this procedure specified all mediations to occur in New York City regardless of where the disputing party was located. This was not that shocking since disputes in bankruptcy cases are resolved by the court handling the case, which here was in New York in any event.

- Mediation Stage
    - Choice of mediator
    - Powers of Mediator
    - Mediation Sites
    - Mediation Briefs
    - Appearance at Mediations
    - End of Mediation

Slide 5:
These provisions are also similar to the Local rule. In this facility, it was specified that the Debtor would pay all the costs and fees of the mediation, including the mediators' fees, but each party would pay for their own expenses and professional fees for their own

professionals to attend the mediation. That is a very common economic arrangement in bankruptcy cases, although some procedures require that the disputant also contribute to the mediator's fees and costs, usually at a pre-set amount per case.

- Other Provisions
  - Deadlines
  - Sanctions for Parties
  - Confidentiality
  - Jury Trial, Arbitration and Exclusive Foreign Forum Selection Rights Unaffected
  - Fees

Any questions on this?

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