Department of Justice

STATEMENT

OF

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BEFORE

THE

COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON IMPROVEMENTS IN JUDICIAL MACHINERY
UNITED STATES SENATE

CONCERNING

ARBITRATION

ON

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It is a pleasure to appear before the Subcommittee on Improvements in Judicial Machinery to urge careful and prompt consideration of S.2253. This bill provides for an experiment in certain federal district courts with mandatory but non-binding arbitration of selected cases.

This proposal for court-annexed arbitration is a key element in the program of the Department of Justice to assure access to effective justice for all citizens and to improve the operations of our judicial system. In that effort over the past year we have worked very closely with this Subcommittee. We have been grateful for the counsel and cooperation you and your staff have provided us. As a result of our joint efforts, including the work of the Kastenmeier Subcommittee in the House, a number of measures are moving forward which will have a salutary impact on the administration of justice in the federal courts.

We have reached the point in our judicial system where simply adding more judges will not necessarily enable us to insure adequate access to effective justice for the variety and volume of disputes with which the federal courts are faced.

It is difficult to state with certainty what the cumulative effect would be of various court reform measures now pending in the Congress. We do not know whether or in what form they will be enacted. Each measure is directed at a particular part of the judicial process, and each would produce its own particular benefits.

Expanding the role of magistrates will relieve district court judges of tasks that do not require their attention. Diversity jurisdiction reform will clear the way for more federal judicial time to be given to federal law questions. The measure now before you to experiment with court annexed arbitration for some types of disputes is complementary to these other measures.

The consequence of clogged federal courts and mounting backlogs is not only an overworked federal judiciary but also litigants frustrated with unconscionable delay and great expense in their efforts to obtain the resolution of their legal disputes. This bill seeks to broaden access for the American people to their justice system and to provide mechanisms that will permit the expeditious resolution of disputes at a reasonable cost.

A large measure of actions filed in federal district courts are resolved by settlement before any trial. However, many settlements take place only after substantial preparation expenses have been incurred, often including voluminous discovery. In addition, some of the trials that are held could be avoided by having a neutral third party consider the evidence and provide an informed decision on the merits, with some inducement to the litigants to accept that decision as the judgment in the case.

This proposal for court-annexed arbitration has been designed with these twin goals in mind: (1) speeding up the resolution of cases that are now settled and (2) resolving more quickly and less expensively many of the cases that now go to trial.

The Successful State Experiences

Compulsory non-binding arbitration of civil court cases has been utilized by several states with good results. In Pennsylvania, a court-annexed arbitration system has been in effect for over 25 years. New York and Ohio have utilized arbitration since 1970; Michigan and Arizona, since 1971. California adopted a statute providing for compulsory non-binding arbitration that became effective in 1976, after a successful program of voluntary arbitration. In addition, arbitration procedures for particular kinds of cases, such as medical malpractice and uninsured motorist insurance disputes, have been utilized in several states.

Thus the use of arbitration at the state level is gradually expanding. In Pennsylvania, the original jurisdictional ceiling was $1000. It was raised to $2000, then $3000, and, in 1971, after considerable study, to $10,000. Moreover, I am aware of no state that has chosen to discontinue arbitration after trying it out.

The State systems generally involve referral of money damage cases to volunteer lawyer arbitrators. The maximum value of claims that may be referred varies from $3,000 to $10,000.

The arbitrators are paid fees ranging from $30 in Ohio to $150 in California per case. They hear the evidence under relaxed rules of admissibility and render an award. There is generally a trial de novo available in the trial court, but with financial disincentives placed upon such a demand. Some States impose their disincentives on any party requesting a trial de novo, others only if the party does not improve its position at the trial de novo. The State plans have generally fared well against court challenges, beginning with the decision upholding the constitutionality of the first program in Pennsylvania. Smith, 381 Pa. 223, 112 A.2d 625, appeal dismissed sub nom. Application of Smith v. Wissler, 350 U.S. 858 (1955).

Appeal rates for trials de novo have ranged from 5 to no more than 15 percent of all cases arbitrated. This means that from 85 to 95% of cases referred to arbitration terminate there. Because of the difference in magnitude between the State cases and the cases encompassed in our arbitration proposal, we recognize that direct comparisons are difficult to make. However, the success that the State systems have had clearly indicates that this experiment is one worth trying in the federal courts. We have examined the particular procedures of the different State programs to determine what procedures would work best in the Federal system.

My own interest in the use of arbitration was heightened by my service as chairman of the Pound Conference Follow-up Task Force. In May of 1976, a distinguished group of lawyers, judges, and academicians gathered together in Minneapolis under the auspices of the Judicial Conference of the United States, the Conference of Chief Justices, and the American Bar Association. The conference marked the 50th anniversary of Roscoe Pound's seminal address entitled "The Cause of Popular Dissatisfaction with the Administration of Justice." At the conclusion of the conference, the Task Force was appointed to formulate recommendations based on the deliberations of and the material presented at the Conference. One of the main recommendations of the Task Force report was that arbitration procedures should be tried in the Federal courts. Consequently, when I became Attorney General, I directed the Office for Improvements in the Administration of Justice to develop legislation that would put this idea into effect.

The Proposed Statutory Plan

S.2253 would authorize an experiment with court-annexed arbitration for specified categories of cases in five to eight district courts for a three-year period. The legislation would also authorize any additional district court in the country to adopt the statutory experiment at the option of the judges. The Federal Judicial Center would evaluate the program and report to the Congress.

The bill sets forth specific categories of cases which would automatically be referred to arbitration before trial. These cases were identified on the basis of three criteria. The first criterion is that the cases involve claims for money damages only. In such cases, often the only dispute is over the amount of money owed by one party to the other. In contrast, pleas for equitable relief would probably mean increased complexity and could require the continuing supervision of the court. Such cases would be inappropriate for arbitration.

The second criterion is that cases referred to arbitration be limited to those in which the claim does not exceed $50,000. In cases with claims in the hundreds of thousands or millions of dollars, the cost of a subsequent trial and of any disincentives for demanding such a trial are very small, relative to the claim itself. It is our belief,based upon the experience in the states that, where large amounts are involved in the suit, the likelihood of one litigant or another requesting a trial de novo is greatly increased. In addition, cases involving hundreds of thousands of dollars or more could very well be of such complexity that they would require an arbitration proceeding of greater length than the speedy proceedings intended to be produced by the bill. As a result, suits over $50,000 are not mandatorily referred, but the parties to a money damage lawsuit of any amount may consent to arbitration under the procedures set forth in the bill.

The final criterion is that the cases present predominantly factual issues, rather than complex legal questions, constitutional claims, or novel issues of law which may establish important precedents. These matters are the province of the federal judiciary. With cases involving arbitration, referral under the bill is to occur only after the disposition of pretrial motions, which will allow for the pre-arbitration resolution by the district court judge of many legal issues.

By applying the foregoing three criteria to the federal civil docket, we have concluded that money damage tort and contract cases are the groups of cases that are most suitable for arbitration. With respect to cases in which the United States is not a party, the language in the bill as now drafted covers most of these cases. However, we have more closely examined this issue since transmitting the statute to the Congress, and we believe now that Section 644 (a)(2)(B)(ii) should be amended to make it simpler and more comprehensive. Our amended version reads:

> "(ii) jurisdiction is based in whole or in part on section 1331, 1332, or 1333 of this title, and the action is based on a negotiable instrument or contract or is for personal injury or property damage, except that an action brought pursuant to section 130 of the Truth-in-Lending Act (16 U.S.C. 1640) shall not be referred."

Under this amended provision all tort and contract cases under $50,000 are covered. These are matters that most commonly

turn on questions of fact. They are cases that attorneys experienced in litigating before the federal courts could, with reasonable facility, determine the award a trial would produce. Thus, the arbitration process should present the parties in these cases with a result closely approximating what they could expect should they go to trial in the district court.

Cases arising under the truth-in-lending statute have not been included. This is a new, complex area of the law, involving voluminous regulations and still in need of published legal precedents. The computation of the amount of damages is automatic under a formula in the statute and would leave the arbitrator without discretion. Also, the losing party pays attorney's fees which are better set by a judge.

We have provided a separate category for cases in which the United States is a party. Many of these cases are treated differently from those involving private parties. For example, actions against the federal government arising out of contracts to which the government is a party must be initially tried before the United States Court of Claims. Others go through administrative proceedings not unlike arbitration before reaching the federal district court. For instance, the Federal Tort Claims Act requires that an administrative claim be filed and disposed of by the relevant agency as a predicate to a district court action. We do not believe that the parties to such actions should be required to go through an additional similar procedure.

We have been examining all money damages cases in which the United States is a party and are in the process of preparing a list of U.S. party cases to be arbitrated. The principle under which we are proceeding is that a category of cases should be referred to arbitration if it meets the criteria set forth above unless there is a compelling reason not to refer it.

It is preferable to reserve United States party cases to regulation in order to maintain administrative flexibility. Statutory designation is best with cases in which the United States is not a party. The categories are simple and straightforward. Moreover, there is no obvious individual or agency to make prompt and informed decisions on the addition or subtraction of non-government cases from the group to be referred.

Number of Cases Affected

It is difficult to predict precisely how many cases will be referred to arbitration under the legislation. I can, however, provide an impression of the magnitude of caseload that will be involved.

Nationally, 23,494 cases founded in tort and 19,928 cases founded in contract, in which the United States was not a party, were filed in the year ending June 30, 1977. This was out of a total of 130,567 civil filings that year.

Statistics provided by the Administrative Office of the United States Courts show that 7,396 of the 23,494 tort actions involved claims under $50,000. However, the amount of the claim

was not reported in an additional 4,724 cases. If those are prorated among the cases where demand was reported, the number of cases under $50,000 rises to 9,257.

There were 9,007 contract cases under $50,000, out of a total of 19,928; 5,310 were unreported, resulting in an estimated total of 12,279 contract cases under $50,000. If, under the legislation, the Chief Justice were to select eight districts to participate, and together they processed ten percent of the federal district court caseload, then there would be on the order of 925 tort and 1,228 contract cases arbitrated in each year in those experimental districts. This would be enough to provide meaningful information on how well the process worked. As we develop the list of cases in which the United States is a party that are to be referred to arbitration, we will be able to provide some estimates on the expected volume of these cases. The numbers of United States cases, however, will undoubtedly be substantially below the foregoing private party totals, because the overall case totals in this category are initially well below those for private party cases.

I would like to add here that approximately 65% of the tort and 69% of the contract actions under $50,000 filed each year are filed under diversity jurisdiction. Elimination or reduction of diversity jurisdiction by the Congress would substantially reduce the number of these cases referred to arbitration.

How Court-Annexed Arbitration Will Work Under S. 2253

The bill provides that the arbitration is to be conducted by attorneys who are experienced members of the Bar of the particular district court. To be certified as an arbitrator, an attorney must have been a member of the Bar of any state for at least five years and be currently admitted to practice before the certifying court. In addition, the attorney must be determined by the certifying court to be competent to perform the duties of an arbitrator. The Chief Judge will certify as many arbitrators as he determines to be necessary to implement the program. Thus, in each district a panel of attorneys experienced with federal court litigation will be maintained. It should be large enough so that no individual arbitrator will be called upon to serve more than two or three times a year.

Arbitrators are to be paid a fee to be set by the district court not to exceed $50 per case plus expenses, which may not include expenses for the procurement of office space. Service as arbitrators would be an excellent pro bono publico activity for the Bar. Lawyers are officers of the court and have an obligation to contribute to improving the administration of justice. It would be unfortunate if fees for arbitrators were set at such a level that it could be viewed as a program to enrich the legal profession. In addition, the modest fee will encourage arbitrators to dispose of cases expeditiously.

The proposed statute sets forth general procedures to be followed in all districts for cases submitted to arbitration. Cases are to be referred to arbitration by the clerk of the court immediately after the twentieth day following the close of pleadings, unless discovery or pretrial motions are filed with the court during the twenty-day period.

If pretrial motions are filed, referral is made immediately upon the disposition of those motions. If discovery is commenced, up to 120 days is allowed for its completion. The case is then referred to arbitration.

These time periods were established in order to allow opportunity for the resolution of the case on the pleadings or by summary judgement or on other legal grounds and to allow the parties to conduct such discovery as can be completed within 120 days. Limited discovery may frequently be necessary in order that the parties are well enough prepared to be able to have a meaningful and fair arbitration proceeding.

Upon referral to arbitration, the parties have seven days to select their own arbitrators and to decide whether to have a single arbitrator in place of a panel of three. If they do not notify the clerk that they have selected their own arbitrators or that they want a single arbitrator, a panel of three arbitrators is selected at random by the clerk from the list maintained by the district court.

The arbitration hearing must commence within thirty days of the referral of the action to arbitration. At the hearing

witnesses may be subpoenaed and the Federal Rules of Evidence are to be non-binding guides, except that privileged material may not be introduced. It is intended that these relaxed rules would permit the admission of some hearsay evidence, particularly in documentary form. For example, a written report might be introduced instead of having an expert witness testify in person.

Upon conclusion of the hearing, the arbitrators are to render an award promptly. This award becomes the judgment of the court in the case unless a party demands a trial de novo within twenty days. Where such a demand does occur, the case is placed on the civil docket of the court and treated in all respects as if it had never been referred to arbitration. No matters relating to the arbitration proceeding may be admitted in the trial de novo without the consent of both parties except for the use of testimony from the arbitration hearing for impeachment purposes.

It is our hope that the rate of demands for trials de novo will be relatively low, i.e., no higher than the 5 and 15 percent experienced in the states. There has been no state experience with cases at the $50,000 level. It is instructive, however, to note that in Pennsylvania the appeal rate of approximately ten percent did not rise, when the jurisdictional amount for the state's program was raised from $3,000 to $10,000.

Disincentives to demanding a trial de novo are included. Unless the party demanding a trial de novo obtains from the trial a judgment more favorable to him than the

arbitration award, he would be assessed the costs of the arbitration proceedings, including the arbitrator's fees, and interest on the amount of the arbitration award from the time it was filed.

By allowing for a trial de novo, the right of parties to a federal court trial is preserved. The disincentives to appeal are included to cause the parties to consider more carefully whether the arbitration award constitutes a satisfactory resolution of the case. Congress has a degree of discretion in determining the manner in which the Seventh Amendment right to jury trial and the due process right to access to the federal courts are implemented (c.f. Capitol Traction Co. v. Hof, 174 U.S. 1 at 23,1899). Congress can establish a program such as this to expedite case disposition and to reduce the cost of federal litigation. It is also reasonable to provide for the allocation of the costs of the arbitration proceedings in a manner designed both to promote the purposes of the program (i.e., acceptance of the arbitrator's awards) and to allocate fairly the costs of the proceedings among the parties.

Local Rule Pilot Districts

Last summer the Office for Improvements in the Administration of Justice conducted a survey of the Chief Judges of the United States District Courts to get their views about how to improve access to justice, especially for civil cases. Two-thirds of the Chief Judges participated. They gave a warm endorsement to the concept of court-annexed arbitration: an overwhelming majority

thought it would reduce costs and delay for litigants and increase the overall efficiency of the judiciary.

Based on that reception, the Department of Justice has worked with the federal judiciary to provide a pilot project in court-annexed arbitration. Three federal district courts are now testing the arbitration process with local court rules modeled after the proposed legislation: the District of Connecticut, the Eastern District of Pennsylvania, and the Northern District of California.

While these local rule plans are modeled on the bill, there are interesting variations in procedures and in the types of cases submitted to arbitration in each of the districts. These variations sho ld provide valuable experience in refining the details of the bill. The Federal Judicial Center is evaluating the local rule experiments. The Administrative Office of the Courts has been very cooperative in assisting with the implementation of court-annexed arbitration in the pilot districts.

Operating under local rule is not a satisfactory long-term arrangement. If we are to have reliable information on how effective this program is and for what types of cases it is most useful, we need the three-year, thoroughly evaluated experiment that the statute would provide, as well as the larger, more systematically selected set of districts. And we need to be able to operate without the cons raints under which local rule programs must operate. For example, there are limitations under the current local rules experiment on disincentives to appeal that may be

utilized and there are restrictions on arrangements for compensation of arbitrators. While the pilot projects can operate for the moment under local rule, it would be far preferable to proceed for any substantial period with the explicit approval of the Congress. The types of cases to be arbitrated and the procedures to be employed should ultimately be established on a uniform national basis by the legislative branch. In short, the local rule pilot districts are providing a valuable warm-up for the main event, which should commence as soon as possible.

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