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Mediation as Condition Precedent to Binding Dispute Resolution

Contract clauses requiring mediation as a condition precedent to binding dispute resolution, if not properly fulfilled, can lead to delay and expense for a party seeking arbitration or access to the courts. Counsel must understand the potential options available when a party fails to comply with the mediation condition precedent and the importance of properly drafting these clauses.

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Mediating a dispute can provide significant commercial benefits, and parties to a contract often include dispute resolution clauses that require mediation before the commencement of arbitration or litigation proceedings. It is well-recognized that mediation can be a valid contractual condition precedent to binding dispute resolution. A party that fails to comply with a mediation condition precedent can face substantial risks, such as disallowance of an award of attorneys' fees and costs to which it would otherwise be entitled or dismissal of an action. It is critical for these clauses to be well-drafted to protect the contracting parties' interests and avoid unwanted consequences.

This article provides an overview of the key legal issues related to contractual mediation condition precedent clauses, including:

- The enforceability of mediation condition precedent clauses.

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- When courts permit the case to proceed despite a party's refusal to mediate.
- The options available for the non-breaching party when a party refuses to mediate.
- Practical tips for drafting an agreement containing a mediation condition precedent clause.

ENFORCEABILITY OF MEDIATION CONDITION PRECEDENT CLAUSES

A clause calling for mediation before binding dispute resolution is enforceable, meaning that contracting parties must submit to mediation before pursuing arbitration or litigation if required by the contract. An unfulfilled mediation condition precedent can prevent the breaching party from compelling arbitration or proceeding with litigation, and the non-breaching party may rely on various legal doctrines and procedural options to enforce the clause.

MEDIATION AS A CONDITION PRECEDENT TO ARBITRATION

Courts in many jurisdictions have held that a contractual clause providing for mediation as a condition precedent to arbitration is enforceable (see, for example, *Golden State Foods Corp. v. Columbia/Okura LLC*, 2014 WL 2931127, at *5-6 (C.D. Cal. June 26, 2014) (quoting Cal. Civ. Code § 1436, which defines the term condition precedent, and explaining that parties must use plain, unambiguous language when providing for a contractual condition precedent)).

Federal circuit courts that have addressed the issue have emphasized that the Federal Arbitration Act's (FAA's) policy in favor of arbitration does not operate without regard to the wishes of the contracting parties (see, for example, *Perdue Farms, Inc. v. Design Build Contracting Corp.*, 263 F. App'x 380, 383-84 (4th Cir. 2008) (affirming the district court's denial of a motion to dismiss or stay proceedings pending arbitration and to compel arbitration, holding that an unfulfilled condition precedent to arbitration rendered the arbitration clause unenforceable); *HIM Portland, LLC v. DeVito Builders, Inc.*, 317 F.3d 41, 44 (1st Cir. 2003); *Kemiron Atl., Inc. v. Aguakem Int'l, Inc.*, 290 F.3d 1287, 1291 (11th Cir. 2002); see also *Begley v. Fullana-Morales*, 546 F. Supp. 3d 103, 105-07 & n.3 (D.P.R. 2021); *R&F, LLC v. Brooke Corp.*, 2008 WL 294517, at *2-3 (D. Kan. Jan. 31, 2008); *In re Pisces Foods, L.L.C.*, 228 S.W.3d 349, 351-54 (Tex. App. 2007); for more on the FAA, search Understanding the Federal Arbitration Act on Practical Law).

Determining whether mediation was requested and rejected is a factual issue to be decided on a case-by-case basis. For example, in *MB America, Inc. v. Alaska Pacific Leasing Co.*, the court concluded that merely advising the adversary of the terms of a mediation clause and, in attempting to resolve the dispute, stating that "hopefully [mediation] will not be necessary" was not a sufficient request to mediate. The court cautioned that a party must convey a clear request to mediate and receive the equivalent of a clear response. (367 P.3d 1286, 1290-91 (Nev. 2016).)

MEDIATION AS A CONDITION PRECEDENT TO LITIGATION

Courts have also upheld the enforceability of clauses requiring non-binding dispute resolution before litigation. For example, *DeValk Lincoln Mercury, Inc. v. Ford Motor Co.* involved an automobile dealership agreement requiring the dealer to submit any claims arising from termination of the dealership agreement to a policy board within 15 days after termination and made the submission a condition precedent to the dealer's "right to pursue any other remedy available under [the] agreement or otherwise available under law." The court upheld summary judgment in favor of the defendant because the dealer failed to submit the claims to the policy board within the time provided. (811 F.2d 326, 335-36 (7th Cir. 1987); see also *AMF, Inc. v. Brunswick Corp.*, 621 F. Supp. 456, 460-61 (E.D.N.Y. 1985); *MB Am., Inc.*, 367 P.3d at 1288-89.)

A court may deny remedies, such as attorneys' fees, to plaintiffs who have failed to satisfy a mediation condition precedent.

A court may deny remedies, such as attorneys' fees, to plaintiffs who have failed to satisfy a mediation condition precedent (see, for example, *Lange v. Schilling*, 163 Cal. App. 4th 1412, 1417-18 (2008) (where an agreement required the plaintiff to attempt mediation before commencing litigation, rejecting the plaintiff's assertion that his failure to seek mediation should be excused because he was unable to locate the defendants until he hired an investigator after filing the complaint, and concluding that the plaintiff "could have readily complied with the requirements ... simply by hiring the investigator, learning sellers' whereabouts, and mailing an offer of mediation to them *before* filing his complaint")).

WHEN COURTS PERMIT THE CASE TO PROCEED DESPITE A PARTY'S REFUSAL TO MEDIATE

Where an agreement contains a mediation condition precedent to arbitration or litigation, refusal to mediate may sometimes be:

- Deemed a waiver of the condition precedent by the breaching party, thereby allowing the other party to proceed with arbitration or litigation.
- Equated to an unsuccessful effort to mediate, meaning the condition precedent is satisfied and the other party may proceed with arbitration or litigation.

WAIVER OF THE CONDITION PRECEDENT

There is some authority for the proposition that a mediation condition precedent clause can be waived, allowing the other party to proceed with arbitration or litigation. This proposition

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is also supported by substantial analogous authority that waiver of an arbitration clause, often by litigation conduct, can allow the other party to move directly to litigation.

For example, in *DeValk*, the plaintiffs, who were owners and managers of an automobile dealership, asserted that even if the relevant mediation clause (which required the submission of claims related to the settlement of accounts to a policy board within one year after termination or nonrenewal of the dealership agreement has become effective) operated as a condition precedent to litigation, the defendant waived the requirements of that clause by its conduct. The defendant continued negotiations with the plaintiffs following the final date on which an appeal to the policy board could be taken and did not insist on strict performance of the clause. (811 F.2d at 335-37.)

A court may equate a party's refusal to mediate to an unsuccessful effort to mediate, meaning the mediation condition precedent is satisfied and the other party may proceed with arbitration or litigation.

The plaintiffs pointed to the law of arbitration clauses as a "closely analogous area." In addressing the issue, the Seventh Circuit examined a state court case holding that an insurer "may waive the compulsory arbitration provision of its insurance policy by its conduct" and that "[s]uch waivers ... may be implied by the acts, omissions, or conduct of the insurer or its agents." However, although the Seventh Circuit determined in *DeValk* that the defendant's conduct after expiration of the time for submitting an appeal to the policy board may possibly constitute a waiver, it rejected the plaintiffs' waiver argument because the relevant agreement contained an enforceable anti-waiver clause. (*DeValk*, 811 F.2d at 337 (quoting *Bielski v. Wolverine Ins. Co.*, 150 N.W.2d 788, 790 (Mich. 1967)).)

Additionally, although one court ultimately rejected this approach (see below *Unsuccessful Effort to Mediate*), a party could legitimately argue that where the other party omitted the mediation step and proceeded straight to arbitration, the omission constituted a waiver of the mediation condition precedent and therefore rendered ineffective the right to arbitrate, allowing the party to compel litigation of the dispute.

Another scenario that may give rise to a waiver of a mediation condition precent is where a party to an agreement containing a mediation condition precedent to arbitration engages in litigation conduct. A court may find that the party waived the right to arbitrate by engaging in litigation conduct inconsistent with an intent to arbitrate, making the other party's compliance with the mediation condition precedent no longer necessary. However, in a significant opinion rendered on May 23, 2022, the US Supreme Court held in a 9-0 decision in *Morgan v. Sundance, Inc.* that a waiver of the contractual right to arbitration cannot be conditioned on a showing of prejudice (142 S. Ct. 1708, 1713 (2022)). Therefore, earlier cases that inquired into whether the party opposing arbitration suffered prejudice as a result of the other party's litigation conduct are no longer authoritative in determining whether the right to arbitrate has been waived.

UNSUCCESSFUL EFFORT TO MEDIATE

A court may equate a party's refusal to mediate to an unsuccessful effort to mediate, meaning the mediation condition precedent is satisfied and the other party may proceed with arbitration or litigation. For example, in *Gerber v. Riordan*, the court disagreed with the plaintiff's argument that the defendants waived their rights under the relevant agreement by refusing to mediate in accordance with the court's prior orders. The agreement provided that "[a]ll disputes arising out of this Agreement shall be submitted to mediation" and if "mediation is not successful in resolving the entire dispute, any outstanding issues shall be submitted to final and binding arbitration." The plaintiff seemed to argue that, because the defendant refused to mediate, the entire dispute resolution clause was no longer effective and he could forgo arbitration and proceed directly to litigation. The court held that the defendant's refusal to mediate simply meant, within the context created by the agreement at issue, that mediation had not been successful. Therefore, under the agreement, arbitration was the next step. (535 F. Supp. 2d 860, 861-62 (N.D. Ohio 2008).)

OPTIONS FOR THE NON-BREACHING PARTY

In the face of an unfulfilled mediation condition precedent, the non-breaching party may attempt to bring a motion to compel specific performance of the mediation clause. Although some states, such as California, do not have a statute specifically addressing motions to compel mediation, support for this approach can be found in cases in which courts ordered mediation where the parties agreed to mediate as a condition precedent to arbitration (see, for example, *Barr v. Frannet, LLC*, 2008 WL 59295, at *3 (N.D. Tex. Jan. 3, 2008); *Mann v. Brooke Franchise Corp.*, 2007 WL 3379723, at *1 (D. Kan. Aug. 20, 2007)).

As one court noted in the arbitration context, compelling arbitration "is in essence a suit in equity to compel specific performance of a contract" (*Wagner Constr. Co. v. Pac. Mech. Corp.*, 41 Cal.4th 19, 29 (2007)). There arguably is no reason to conclude that the same logic would not equally apply where a party seeks to compel contractually required mediation, though the appropriate procedure for doing so may differ from what is required to bring a motion to compel arbitration (for example, a party might bring an action for specific performance rather than a petition to compel arbitration under Section 4 of the FAA).

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Moreover, courts have recognized the essential role mediation plays in judicial proceedings, which is akin in some ways to arbitration, and which may provide further support for the proposition that courts may compel mediation (see, for example, *Advanced Bodycare Sols., LLC v. Thione Int'l, Inc.*, 524 F.3d 1235, 1240-41 (11th Cir. 2008) (recognizing that agreements to mediate "might be specifically enforceable in contract or under other law" but also acknowledging authority that does not support the view that the arbitration scheme is an appropriate mechanism for analyzing mediation agreements)).

Search Hybrid, Multi-Tiered and Carve-Out Dispute Resolution Clauses for more on the enforcement of mediation provisions.

Additionally, where a mediation condition precedent is not satisfied, the non-breaching party may consider bringing a motion to either:

- Dismiss the claim.
- Stay the arbitration or litigation pending mediation (possibly combined with a motion to compel mediation).

(See, for example, *N-Tron Corp. v. Rockwell Automation, Inc.*, 2010 WL 653760, at *7-8 & n.16 (S.D. Ala. Feb. 18, 2010); *SEMCO, L.L.C. v. Ellicott Mach. Corp. Int'l*, 1999 WL 493278, at *2-3 (E.D. La. July 9, 1999); *Matter of Lakeland Fire Dist. v. E. Area Gen. Contractors, Inc.*, 16 A.D.3d 417, 417-18 (2d Dep't 2005).)

Search Compelling and Staying Arbitration in the US Toolkit for a collection of resources to help counsel submit an application to a US federal or state court requesting an order to compel or stay arbitration.

Mediation Toolkit

The Mediation Toolkit available on Practical Law offers a collection of resources to assist counsel with the mediation process. It features a range of continuously maintained resources, including:

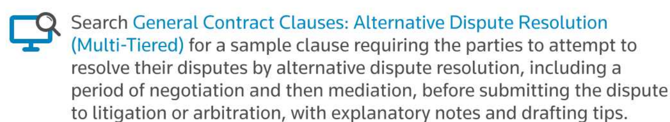
- Complex US Mediation: Key Issues and Considerations
- Considerations for Conducting an Effective Mediation: The Mediator's Perspective
- US Mediation Agreement
- How to Prepare a Client for Mediation
- Questions for In-House Counsel to Ask Litigation Counsel About Mediation (US) Checklist
- Challenging Mediation Confidentiality and Mediation Privilege in the US
- Considerations for Having the Mediator Serve as Arbitrator in the US
- Virtual Mediation: Key Issues and Considerations
- US Mediation Statement
- Using Mediation Better: Understanding the Apex Conversation

DRAFTING TIPS

Given the significant role that mediation can play in the dispute resolution process, it is critical for parties that want to provide for mandatory mediation as a condition precedent to arbitration or litigation to properly draft the relevant clause.

When drafting a mediation condition precedent clause in a commercial contract, the parties should:

- Consider to whom within their respective organizations the dispute should be referred, because negotiations are most likely to be successful when the individuals in question:
  - are familiar with and have responsibility for the products or services that are the subject of the dispute; and
  - have sufficient authority within the organization to make the decisions necessary to resolve or escalate the matter or dispute.
- Set a reasonable time limit within which mediation must commence and conclude. In *Sor Technology, LLC v. MWR Life, LLC*, for example, the court rejected the plaintiff's argument that it could not fulfill its obligation to mediate prior to filing suit because the defendants "stonewalled and sabotaged [its] repeated mediation efforts." The court noted that the relevant agreement provided for a 30-day window to complete mediation once the parties referred the matter to the mediator, which the parties had not done in that case. Noting that the agreement contained no other provision that would require the mediation to start within a specific time, the court refused to "impose a time limit the [p]arties never agreed upon in their contract." The court dismissed the plaintiff's complaint without prejudice so that it may refile its claims once it fulfilled the mediation condition precedent. (2019 WL 4060350, at *3 (S.D. Cal. Aug. 28, 2019).) As this case demonstrates, specifying a reasonable outside time limit for the mediation process to occur can help shield a party from the adverse consequences of an uncooperative opposing party.
- Clearly state the scope, application, and terms of the mediation condition precedent.
- Consider whether:
  - the clause should apply to all disputes or whether any carve-outs are needed;
  - the clause should apply when a claim arises under a separate contract between the same parties related to a similar subject; and
  - the provisions relating to the timing of negotiations and mediation are realistic.
- Consider including terms tolling the running of any statute of limitations for the disputed claim during the pre-suit negotiation or meditation process.



Search General Contract Clauses: Alternative Dispute Resolution (Multi-Tiered) for a sample clause requiring the parties to attempt to resolve their disputes by alternative dispute resolution, including a period of negotiation and then mediation, before submitting the dispute to litigation or arbitration, with explanatory notes and drafting tips.

Search Escalation Clause Incorporating Provision for Arbitration for a boilerplate arbitration clause providing for escalation of a dispute through alternative dispute resolution procedures comprised of a meeting of party representatives, followed by mediation and culminating in arbitration, with explanatory notes and drafting tips.

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