Chapter 2: Diagnostic Phase

1. Key Elements of an ADR Diagnostic

Before deciding whether to begin a mediation project in a country, and what the project should look like, a detailed analysis must be conducted of the country’s needs and its legal and business environments. The following questions must be addressed in this assessment phase:

1. What are the problems with the resolution of commercial disputes in the country?
2. Can these problems at least partly be ameliorated by introducing mediation or other ADR methods?
3. Are there appropriate preconditions to start a mediation project in the country, and if yes:
4. What is the detailed plan of action?
5. What are the obstacles to implementation and what is the plan to overcome those obstacles?

There are a few factors that should be carefully assessed when deciding whether to begin a mediation project in a country: existing laws, practice and culture of dispute resolution, perceived need of mediation, ADR experience, key stakeholders, NGOs and international organizations, and sustainable financing. These factors, which can be modified according to the country’s specific features, are:

- **Existing laws and regulations** creating a legal environment for resolving commercial disputes. Does the country comply with international standards?

- **Practice of dispute resolution in civil cases**: functioning of (commercial) courts and other legal institutions and professionals associations (e.g. bailiffs, attorneys); number of procedures needed for contract enforcement; time needed for enforcement; court fees and legal fees; access to justice; geographical access to the courts; corruption; other strength and weaknesses, etc.

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13 There are many more possible problems that can and should be assessed, depending on the circumstances. Also note that answers to these and other questions may differ depending on the regional differences between the parts of the country (and cities).
- **Culture (of dispute resolution).** Litigious-ness; social acceptance of the settlement; rate of settlement within and outside of courts; trust in the court system and judiciary; perceived and real corruption; approach to legal and judicial reform; economical and social background; legal and cultural background of the region, etc.

- **ADR experience.** Existence of traditional or modern alternative methods; successful and unsuccessful attempts of introducing ADR; public awareness of ADR and particularly mediation; former ADR trainings; the pool of trained and trainable mediators.

- **Perceived need to introduce mediation** and identification of areas where it would be particularly helpful. When do the parties give up on court proceedings and why, what disputes are perceived appropriate for mediation? Is the country obliged/pressured to modify its system (by international organizations, neighboring countries, etc.)?

- **Key stakeholders and political support.** Key groups and individuals holding stakes in ADR and their declared and potential support for the project, particularly. Judiciary, Ministry of Justice, small and medium enterprises (SMEs), bar associations, and business organizations. What are their strengths, weaknesses, successes; key opponents; areas requiring capacity building?

- **NGOs and international organizations interested or involved in ADR.** Past, present, and future projects with ADR component. Areas of common interests, possible financial contributions or projects involving economy of scale (e.g. common mediation trainings).

- **Sustainable financing.** Available sources; restrictions and goals of donors; financial needs of the project, etc. The duration of the project is not likely to be shorter than three years.

Generally, mediation is most needed and should work best where transactional costs of litigation and other court procedures are particularly high. “High transactional costs of litigation” can be understood broadly, as any obstacle to efficient resolution of dispute, whether dilatory, monetary or other costs that raise the expense of resolving a dispute for a party. Mediation should also be introduced where the level of settlement is particularly low. Although such low settlement level may mean a culture that is adverse to mediation, even gradual change in this type of culture will be an important achievement.

An important exception to that rule is where the court system is so inefficient and the justice is delayed to the point that it poses no or little threat to the parties. The consequences of delayed justice take away incentives to settle for many
parties. This phenomenon of no “shadow of the law (court) “is described later in this chapter.

Assessment of the above issues should be made through analysis of legal documents, statistical data and, most importantly – interviews with and polls of key stakeholders (particularly judges, bar members, potential mediators, legal experts, and SMEs).

2. Limitations of Mediation

Project managers have to understand when mediation is appropriate and when it is not. The right conditions have to be in place in the country for a mediation project to be successful and to achieve the intended objectives. Unlike a judge, a mediator cannot force the parties that are in dispute to resolve their dispute through mediation (as mediation is a non-binding procedure). The parties need to have the right incentives to choose mediation over litigation or arbitration. This is something that is often ignored and is the main cause of many failed mediation projects.\(^\text{14}\)

Box 1: No Incentives for Parties, No Mediation

The following is an illustration of what could happen when the right incentives for the parties in dispute are not in place:

“The dispute was between a Turkish manufacturer and a Palestinian buyer that paid in advance using a letter of credit. When the buyer received the goods, it found that they were defective and called the manufacturer to complain. The manufacturer said that the goods were fine when they left its plant, so the damage was not its problem. The Palestinian buyer then requested mediation at the recently established mediation center in Ramallah. But the Turkish firm ignored repeated requests to visit Ramallah to mediate the dispute. The administrator of the ADR program concluded that the problem was lack of awareness of the program’s benefits—that if the Turkish company had better understood the advantages, it would have come. In reality, the failure here was one of case selection. The Turkish firm had no interest in any other outcome. It had already received its money from the buyer. Why would it risk going to Ramallah, where the best outcome would be a decision that it could keep the money?”\(^\text{15}\)

The absence of these incentives along with other prerequisites and conditions will jeopardize the success of the project. Under such circumstances, it is not advisable to engage in a reform project. The experience of the WBG in implementing ADR projects confirms that creating the right incentives for the party is critical for the success of the project.

There are a number of ADR projects in which the WBG participated that have shown meager results (see table 2 below). The common explanation in most of these projects is that they failed because there were no incentives for the parties to resolve their disputes, or the parties were not aware of the incentives. In other words, in these countries, most of the parties referred to mediation did not have or

\(^{14}\) See “Alternative Dispute Resolution – when it works, when it doesn’t”, PREM notes, WB 2005, Richard Messick, with subsequent changes by L. Rozdeiczer, and Alejandro Alvarez de la Campa.

\(^{15}\) Extract from “Alternative Dispute Resolution – when it works, when it doesn’t”, PREM notes, WB 2005.
did not see enough incentives to attempt to mediate their disputes with other companies. Usually, the way to mitigate these problems is to establish an appropriate mechanism for case selection (the case involving the Turkish manufacturer and a Palestinian buyer would not have been selected for mediation if these mechanisms were in place), introducing awareness about the benefits of mediation or other ADR mechanisms and other incentives described in Chapter 4 of the manual. In other successful WBG projects (as we will show later in the manual) the parties had the incentive to mediate and the appropriate cases were referred by the courts to mediation/arbitration. Further in the manual, in Chapter 4, it is explained how to establish the right incentives and methodology to select appropriate cases for mediation.

Table 2: Results of mediation and arbitration projects in Albania, Ecuador, the West Bank and Gaza and an arbitration project in Sri Lanka

<table>
<thead>
<tr>
<th>Country</th>
<th>Months program in effect</th>
<th>Cases submitted</th>
<th>Cases resolved (% of total)</th>
<th>Cases pending</th>
</tr>
</thead>
<tbody>
<tr>
<td>Albania</td>
<td>16</td>
<td>8</td>
<td>0 (0%)</td>
<td>1</td>
</tr>
<tr>
<td>Ecuador</td>
<td>10</td>
<td>888</td>
<td>214 (24%)</td>
<td>0</td>
</tr>
<tr>
<td>West Bank and Gaza</td>
<td>12</td>
<td>13</td>
<td>3 (23%)</td>
<td>6</td>
</tr>
<tr>
<td>Sri Lanka</td>
<td>60</td>
<td>317</td>
<td>84 (26%)</td>
<td>N/A</td>
</tr>
</tbody>
</table>

Source: World Bank

It must be noted that one of the key differences between mediation and arbitration is the way in which parties enter the process. While mediation is usually a voluntary process, most parties go to arbitration because they had committed to it through the arbitration clause in the contract establishing the transaction that was a ground for the dispute (i.e. before the dispute arose). If there is an enforceable arbitration clause, the parties do not have a choice in participating in the arbitration proceedings, and later are bound by the arbitration award.

SMEs should also be encouraged to include mediation clauses in their contracts. Parties to such agreements will be obliged to meet for mediation and attempt to mediate (in some jurisdictions there is also a requirement to mediate “in good faith”). Since mediation is a non-binding process, parties still can decide whether they want to settle and cannot be forced to do it. It is not clear whether mediation clauses are enforceable and how the sanctions for non-compliance will vary under different jurisdictions\(^\text{16}\). For examples of Mediation Clauses and Corporate Pledges, see Appendix C.

The lack of incentives is possibly the most common reason for failed ADR projects – the lack of demand for mediation. The biggest problem in most countries is a low perceived demand for mediation services and the small number of appropriate cases going to mediation. Thus, in designing and executing the project, more attention and resources should be directed to creating greater incentives to participate in mediation, selecting appropriate cases, and informing parties of potential benefits and limited risks of mediation.

3. Which Problems Can Be Ameliorated by Introducing Mediation or Other ADR Mechanisms?

Mediation is a good tool to, at least partly, achieve the following objectives:

- Reduce court backlogs.\(^{17}\)
- Reduce time necessary for contract enforcement.\(^{18}\)
- Reduce costs of dispute resolution (e.g. by limiting court and legal fees).\(^{19}\)
- Increase number of in-court settlements (facilitated by judges or mediators).
- Reduce formality and complexity of the existing processes.
- Reach geographically dispersed population.
- Teach judges some elements of case management.
- Increase satisfaction with dispute resolution.


\(^{18}\) Although mediation itself is not an enforcement mechanism and mediators alone do not possess powers of compelling the disputants to enforce a contract there are different ways in which mediation can shorten the time necessary to enforce a contract. Successful mediation can drastically shorten the time necessary for reaching a solution (mediation usually is resolved in one session). Mediation out of court system can resolve the conflict at a very early stage (before the case is brought to the court).

\(^{19}\) The subject of cost savings for various ADR procedures is a complex one, and the results vary significantly depending on the types of cases and court settings, as well as the sophistication of the research. In addition, a distinction must be drawn between cost savings to the disputants and savings to the legal system. In general, there has been no persuasive evidence of the latter, but some evidence of the former. See McEwen, Note on Mediation Research, in Goldberg, Sander, Rogers and Cole at 162-164. Compare Kokkali James et al (1996) An Evaluation of Mediation and Early Neutral Evaluation Under the Civil Justice Reform Act Santa Monica, CA: RAND, with Ontario study (Han, Robert and Bar, Carl (2001) Evaluation of the Ontario Mandatory Mediation Program (Rule 24.1): Executive Summary and Recommendations Ontario, Canada: Queen's Printer.). See also AAA survey p. 19 – 20 (91% of corporate counsel surveyed believed that mediation saves money, 71% thought so about arbitration) and Brett, Barsness and Goldberg 12 Neg Journal 3 1996 at p. 263) who conclude that mediation is far less expensive than arbitration. Litigation costs in civil law countries are generally lower than in civil countries – see description of mediation in Germany in Appendix E, page 68.
- Effectively handle complex multiparty disputes.
- Effectively handle disputes where sophisticated expertise is needed.
- Increase access of disadvantaged groups.\(^{20}\)
- Support case management and create models for further court reform.
- Reduce high level of tension in business communities\(^{21}\) and promote long-lasting relationship between business partners.
- Modify the “culture of dispute resolution” based on adversarial proceedings and the assumption of the zero-sum game, and hostile mindset.
- Respond to the concerns of equity and relationship.
- Bypass discredited and/or corrupted courts, and assist in eliminating corruption.

When considering the introduction of commercial mediation, it is important for the project manager to consult extensively with firms in the country about the main reasons they should go to mediation instead of litigation. Firms will be the main beneficiaries of commercial mediation and therefore are the best positioned to determine which problems can be solved by introducing mediation. An interesting perspective on this is that of American firms in choosing mediation over litigation (see Appendix D).

Mediation may be an efficient tool in eliminating corruption. By avoiding litigation, parties have a choice to bypass the courts. For example, it has been observed that mediation projects (including but not limited to commercial court systems) in a few Latin American countries, such as Argentina, Bolivia, Ecuador, Nicaragua, and Peru,\(^{22}\) could directly have a positive impact in the serious problems of systemic corruption in the judicial system, violence, and an inability to communicate peacefully within society at large.

Another form of mediation that has proven to be successful in reducing corruption is that of the ombudsman.\(^{23}\) The meaning of “Ombudsman” differs depending on the jurisdictions. In the United States, it is a form of mediation. This notion is differently understood in Europe, where ombudsmen are often found around indus-

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\(^{20}\) This particularly concerns illiterate and/or poor population who cannot afford to navigate conventional legal channels. In this case, however, there is a danger that these groups may receive a “second class” justice and be in fact forced to settle on less advantageous terms. See Grillo, T. (1991). “The Mediation Alternative: Process Dangers for Women.” *Yale L.J.* 100.

\(^{21}\) This may be particularly significant in post conflict regions where ADR models can emphasize the importance of reconciliation and relationships over retribution and “winning” in dispute resolution.

\(^{22}\) See Moyer, T. J. and Emily Stewart Haynes (2003). “Mediation as a Catalyst for Judicial Reform in Latin America.” *Ohio St. J. on Disp. Resol* 18. Part IV of this paper provides descriptions of actual mediation programs in place in Argentina, Bolivia, Ecuador, Nicaragua, and Peru.

try sector consumer *adjudication*, or public authority adjudication, for example, over financial or health services, or pensions or government administration - sometimes legally binding on the organization or created by statute. Some such ombudsmen use mediation as part of their preliminary handling of such cases.

However, a note of caution is necessary because mediation is not always useful in eliminating corruption. Parties are normally not compelled to mediate and to settle. A party may refuse to settle and try to “benefit” from the corrupted court system. Therefore, both parties must want to avoid the corrupted system and choose mediation as an alternative.

One crucial goal of any mediation project that is often overlooked is raising the awareness and capacity of judges to facilitate settlement and judicial management. One of the results of the project should be an increase in the rate of in-court settlement facilitated by the judge (not by mediators). Through proper training and better understanding of mediations, judges should be capable of not only effectively choosing cases for mediation but also settling more cases during court proceedings. The institutionalized ADR-judicial mediation, where sitting judges act as mediators in programs closely integrated with the traditional adjudicative system mechanism is probably most developed in Quebec. This model is particularly important and interesting. Unlike the various experiments with pilot projects or limited initiatives in mediation that other jurisdictions have tried, the Quebec justice system now integrates adjudicative and mediational justice at every level and in virtually every area of law, including family matters, civil and commercial law, administrative matters, and, recently, criminal law.

Some of the objectives that mediation is not likely to achieve include:

- strengthening the rule of law,
- setting precedent and establishing legal framework,
- promoting consistent application of law,
- addressing power imbalances between the parties,
- addressing discrimination or human rights problems,
- forcing parties to participate in ADR or court proceedings, and
- causing punitive or deterrent results.

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Weak “shadow of the court”

The effectiveness of mediation projects can be seriously limited by an inefficient court system that produces particularly long delays in making enforceable decisions. Frequently, one of the most important incentives for the parties to mediate is to avoid court decisions. When a potential court decision is postponed many months and often years, at least one of the parties (usually a debtor) has no incentive (no threat) to pursue mediation. If this party can successfully use dilatory tactics or rely on court's inaction, such party will not be willing to settle in mediation. In other words, the disputants realize that they mediate “in the shadow of the court,” meaning that the court is an alternative (or a threat) in case they don’t reach settlement in mediation. Therefore, mediation may not be effective when the court system is so inefficient that it does not provide a credible threat of a court resolution in a foreseeable future.

However, there are ways to minimize the risks of failure under these circumstances, if the project manager still thinks that introducing mediation makes sense. Because one of the main goals of the project is to speed up enforcement of contracts (e.g. through clearing of the court dockets) one should not argue that the mere existence of the problems to be corrected should prevent the project from taking place.\textsuperscript{26} The goal of the project is not to channel all or even most cases to mediation, but to select a relatively small percentage of cases that are suited for this procedure and help parties achieve settlement. Once the mediation starts working and clearing out the dockets, the shadow of the court will likely become stronger and more parties (threatened with foreseeable court decision) will likely agree to mediate.

The lack of court threat may be also present when there is high corruption in courts (e.g. case of Albania). But high corruption in a country should not automatically hold up a mediation project. Even though the corruption may be widespread, it is probably not equally present and accepted in all courts. Therefore, finding a less corrupted court or president of the court, who is willing to monitor the flow of cases and fight corruption might be a good argument for starting a pilot project there. Also, corruption is not likely to concern all cases, and those corruption-free cases may be more likely to settle. In case of corruption, mediation may start up other court reforms including closer monitoring of cases, and case management that can battle corruption more effectively. As proved by successful reduction of corruption in Latin American countries, mediation may be a useful tool in achieving this objective.\textsuperscript{27}

\textsuperscript{26} As shown in most research mediation can successfully limit costs and delay of the contract enforcement.

\textsuperscript{27} See Moyer, T. J. and Emily Stewart Haynes (2003). “Mediation as a Catalyst for Judicial Reform in Latin America.” Ohio St. J on Disp. Resol. 18.
If mediation, in theory, seems to be the right solution for improving some of the problems with commercial dispute resolution, one has to see if the conditions are in place for starting a mediation project.

4. Preconditions/Prerequisites for Beginning the Project

As soon as it has been determined that mediation, in theory, could rectify some of the problems with the resolution of commercial disputes in a country, the project manager should decide whether there are necessary conditions to begin a mediation project. Potential preconditions to the project can result from any of the problems identified in the assessment. However, at this stage, it is crucial to decide at the inception of the project which of many difficult conditions in a country make it hard to succeed or too risky to try. In other words – what are the prerequisites for beginning a mediation project?

Out of the many potential obstacles, there are a few conditions necessary for a mediation project to begin. If the following conditions are present, the project has a fairly high probability of succeeding:

- Private sector demand for alternative ways of resolving disputes. Incentives for the parties to choose ADR over litigation.

- High transaction costs” of resolving commercial disputes through courts and/or perceived need for mediation.

- Support of the critical group of key stakeholders, most importantly the judiciary and particularly the president of the pilot court (or other key stakeholder group if there is a plan to establish a “private” mediation center\(^28\)).

- Possibility of securing financial resources for at least three years to implement the project.

- Possibility of establishing enforcement mechanisms for ADR and realistic chances of passing and enforcing laws on mediation in a reasonable time. (This will be the case where there is no law directly regulating mediation and local stakeholders in the country, particularly the judiciary and the Ministry of Justice believe that a law introducing mediation is necessary).

If any of these preconditions are not viable, then chances for project success will decrease. There are, of course, ways to make these conditions a reality, but the project manager should know that they are the most critical elements for a project to be successful and that most of the energy at the beginning of the project has to focus on these conditions.

\(^28\)The establishment of a mediation center will be discussed later in the manual. Since in this manual we argue that beginning with a court-connected mediation center is usually the best option, at this point we presume the need of judicial support.