Final Offer Arbitration (FOA)

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Final Offer Arbitration

(“*baseball*”, “*last best offer*”, “*pendulum*” arbitration)

- In Conventional Arbitration, if arbitrators are expected to “**split the baby**”, parties will have an incentive to make extreme offers (“**chilling effect**” on negotiations).
  - In August 1963, US Congress had ordered compulsory arbitration to terminate labor railroad disputes and avoid strikes.
  - This is why in 1966 Carl Stevens originally proposed FOA (“one-or-the-other principle”) for wage bargaining
- In FOA, arbitrators must necessarily **select one of the offers** submitted by the parties
  - Lack of flexibility of arbitrators will encourage parties to submit reasonable final offers, to maximize chances of success.
  - Preliminary exchange of offers may **encourage parties to settle**.
  - Even if an award is necessary, dispute resolution is **fast** and **low cost**.
  - While FOA typically applies to pure monetary disputes, “*package-based*” FOA is occasionally used (e.g. bargaining in New Zealand police)

FOA in practice

- Labor & commercial negotiations
  - "*FOA challenge*" (Bazerman & Kahneman, "*How to make the other party play fair*", HBR, 2016)
    = Open negotiation with a reasonable offer + Propose final price to be determined under FOA
  - In 2015 **ICDR** approved its **FOA Supplementary Rules**
- Imposition by regulatory authorities, to force parties to negotiate a fair price
  - Canadian Transportation Agency, for rates disputes between carriers and shippers
  - Canadian Radio-Television and Telecommunications Commission, to decide disputes on rates for "Canadian programs"
  - Australia´s "**News media and digital platforms mandatory bargaining code**" (2021)
    - The bill (an amendment to the Competition and Consumer Act) was designed to correct imbalance in negotiating power between digital platforms and news publishers
    - As a result, News Corp reached agreements with Google (April 2020) and Facebook (February 2021).

FOA in practice (II)

- BEPS Agreement and Double Taxation Treaties
  - OECD recommends inclusion of FOA provision to sort out **bilateral disputes between national tax authorities** on how to avoid double taxation of taxpayers in cross-border transactions (e.g. transfer pricing)
  - FOA already foreseen in some bilateral Double Taxation Treaties (e.g. US-Spain DTT)

- FOA has also been suggested or used to determine
  - Royalties for Standards Essential **Patents** (SEP), when licensing is mandatory
  - In the US
    - Emergency care: fees charged to hospitals by out-of-network emergency doctors (e.g. New York city)
    - Drug prices charged by big pharma to health insurance companies

FOA Supplementary Rules (ICDR, 2015)

- Parties will **exchange at least 2 settlement offers** prior to the arbitration hearing
  - Such offers will not be shared with the arbitration tribunal
- At least 2 weeks before hearing, parties will simultaneously submit their **final offers** to the tribunal and their counterparties
  - Each offer will contain a **single monetary amount**, covering all claims, set offs or counterclaims (excluding pre- and post-award interest and arbitration costs)
  - Only the parties may see the final offers at that time
  - The tribunal shall **not open the final offers until the end of the hearing**
  - Absent agreement, offers cannot be changed once submitted to the tribunal
- After considering the evidence submitted in the hearing, the tribunal shall choose one of the final offers
  - The tribunal will only add any interest or arbitration costs, pursuant to the arbitration rules, applicable law or agreement
  - The award shall be **reasoned**, stating the rationale for its selection of one party's final offer

“News media and digital platforms mandatory bargaining code” (Australia, 2021)

- Australian Communications and Media Authority (ACMA) to keep a **register** of “bargaining code arbitrators”
- Object: **remuneration** to be paid by a digital platform to a news business for making available news content
- Procedure:
  - **News business may give notice to ACMA that arbitration should start** if a) unsuccessful bargaining for 3 months and b) the bargaining parties have agreed to arbitration about terms for resolving the “remuneration issue”.
  - If the parties cannot agree on the panel of arbitrators, appointments to be made by ACMA from its roster
  - Expedited discovery process
  - Final offers cannot be more than **30 pages** in length
    - Each party may make a 20-page submission about the other party’s final offer
    - ACMA itself may give to the panel a submission about both final offers
  - “The panel must accept one of the final offers unless the panel considers that each final offer is **not in the public interest** because it is highly likely to result in serious detriment to
    a) The provision of covered news content in Australia; or
    b) Australian consumers.

    The panel must consider the **bargaining power imbalance** between Australia news business and the designated digital platform corporation”.

Tentative conclusions

- If the “objective value” of the claim is ambiguous, FOA may disadvantage the party which
    - Is more risk averse (it will make offers below its subjective valuation, to ensure success)
    - Resorts to FOA less frequently (it will have fewer opportunities to make up for cases lost)

  To address those difficulties, academics have suggested a number of FOA variations (“amended FOA”, “combined FOA”…)

- FOA may be suitable for some pure **quantum disputes** between **well-informed parties**
    - In the absence of legal changes (like in Australia), this will require that both parties accept FOA and ICDR-inspired rules.