

How to Best Mediate and Arbitrate Cases Involving Changes to Senior Management

By **Mark E. Segall**

As a mediator and arbitrator at JAMS, I frequently face the difficult task of mediating and arbitrating cases involving senior-level executives. The purpose of this article is to explore how best to address the issues that arise in cases of this type. In addressing this topic, I bring to bear my nine years of experience as a JAMS mediator and arbitrator, and my prior experience as head of litigation worldwide at JPMorgan Chase. Among other things, I supervised all employment litigation in that capacity and evaluated risk and settlement and litigation strategy in cases of this type.

Cases involving C-suite executives pose a particular challenge because of their unique set of circumstances. The individuals involved are at the very top of their professions but suddenly find themselves either out of a job or demoted.

If a senior executive is discharged, he or she may be seen as incompetent or, even worse, having engaged in conduct that is so egregious as to justify being discharged for cause, the economic consequences of

which include forfeiting millions of dollars in severance and/or stock rights. Depending on the terms of the employment agreement, actions that would warrant a discharge for “cause” may require finding conduct that is criminal or an act involving fraud or willful misconduct. Discharges for certain categories of “cause” require 30 days’ notice and an opportunity to cure, but once a company decides to discharge a senior executive, rarely, if ever, does the company follow such provisions. If a senior executive is demoted or forced out, he or she may feel, sometimes with justification, like a victim of discrimination or retaliation. If he or she chooses to leave voluntarily, he or she may be subject to a debilitating non-compete provision or restrictive covenant, or even allegations that he or she misappropriated confidential information obtained during employment. If a company must announce an immediate change in leadership, there is an urgent need to make peace before making any public announcement. The allegations made in these disputes can be ugly and expensive to litigate. And they raise the risk to reputation that can make obtaining a comparable



position extremely difficult. This poses particularly thorny issues for a mediator to overcome and for an arbitrator to determine.

Considerations for the Mediator

When a senior executive is discharged, emotions usually run high on both sides. The senior executive has likely been a success throughout his or her career. This is probably the first time that he or she has been accused of being incompetent or having engaged in wrongdoing.

The senior executive needs to vent. He or she needs an opportunity to present his or her case before a neutral, which is why the initial *ex parte* session with the mediator is often quite long. The executive needs to tell the

mediator about his or her career, including what he or she thinks went wrong at the company. Hearing the entire story directly from the executive and not just from his or her lawyer establishes trust and builds rapport.

At the same time, the mediator has to make clear just how difficult the challenges to recovery may be. The senior executive must understand the risk that one or more claims may not succeed. Asking questions will provide clarity on how long the litigation or arbitration may last, how much it might cost and how the trier of fact may not deliver a favorable decision. The executive needs to understand the extent to which attacks, even if they are illegitimate, will be made on his or her performance and character. At the same time, fighting this battle for years will pose obstacles both practical and emotional to moving on to the next stage of the executive's professional life.

For the company, the reverse is true. The mediator needs to hear the full story about the senior executive's alleged failures of performance and/or misconduct. The company will be convinced that it made the right decision and that it needs to move forward with different leadership. Hearing the company's position in great detail also establishes trust and builds rapport.

As he or she did with the senior executive, the mediator needs to make clear to the company just how difficult it may be to defend its case. If the company claims there will be a success-

ful dispositive motion at an early stage, the mediator needs to ask the company's lawyers to be realistic with their client about their chances of winning that motion. For the company, the allegations may also be ugly. Depending on whether the forum for the case is public, there may be adverse publicity. Here, too, there are the attorneys' fees (even for a successful defense), not to mention the risk of not prevailing and the amount of time spent in preparation and testimony, which could have been better spent planning the best way forward. If a foreign company is involved, it needs to understand the particular risks in proceeding with arbitration or litigation in the United States.

Both sides need to be realistic about the upsides and downsides of their cases, especially when determining best- and worst-case damages calculations. Where appropriate, it may be helpful to indicate to the parties how I might react to an argument through the eyes of an arbitrator. If an individual has credibility issues, I will discuss that with his or her lawyer. Conversely, if the executive, as he or she often does, will make a very good impression, I will convey that to the other side. Each side should ask their lawyers what is the least/most they would recommend accepting/paying. Both sides need to evaluate the exposure, if any, that may exist from any counterclaims that may be asserted and take that into account.

Even if the parties reach a deal on economic terms, they must

then have difficult discussions concerning the public statements each side will make concerning the senior executive's departure. If the executive will remain with the company for a period of time following the settlement, there has to be agreement concerning his or her duties and responsibilities during that period. If the executive is free to pursue a new opportunity, there has to be agreement on whether there will be restrictions on what types of business he or she can pursue and how long these restrictions may last. While it may be easy for both parties to agree not to disparage each other, it may be much harder to restrict the executive from hiring employees who once worked for the company.

Considerations for the Arbitrator

The arbitration of these types of cases requires careful consideration of the language of the governing contracts, if any, and a thorough exposition of the relevant facts. The language itself often is in the employment agreement and relevant sale documents, and is the standard against which the conduct at issue needs to be judged. As noted above, the standards differ depending on what was negotiated. On the other hand, if it is an at-will employment situation, with no employment contract, then the laws on discrimination and/or retaliation become the standard against which the conduct must be judged.

These cases are very fact intensive. It is not unusual for the transcript to

be between 1,500 and 2,000 pages, with extensive pre-hearing and post-hearing briefing. The story of what happened is often quite complicated. The determinations that are made often turn, in large measure, on the credibility of the senior executive, those who made the decision to discharge and the other fact witnesses. The arbitrator must determine whether the executive really acted improperly within the meaning of the contract or whether there was no more than a significant disagreement on matters of style, approach and business direction. When a company is acquired by a foreign company or private equity firm, the differences in culture, values and/or approach are sometimes so fundamental that a senior executive (or executives) can no longer remain with the successor company. But this alone will not trigger the cause provisions of the relevant agreements. In instances of genuine disagreement, the portions of the employment agreement requiring 30 days' notice and an opportunity to cure may be triggered, but once a company decides to make a management change, those responsible rarely want to invoke those provisions; instead, they will probably move straight to discharge. In fact, of all the cases I have mediated and arbitrated in this area, I cannot recall a single one in which the notice provisions of the employment agreement were invoked by a company. There also may be counterclaims asserted against the executive for breach of fiduciary duty or fraud. If the conduct is sufficiently egregious,

there may even be a claim to recover past compensation on the grounds that the executive was a "faithless servant," as defined by relevant case law.

These cases often involve difficult questions concerning what a senior executive can do upon departure and when. Has there been a restriction on the scope of competition or the use of confidential information? Can he or she use his or her track record with the prior employer when seeking a new job? In the case of a trader, a question often arises concerning who owns the trading models.

Questions of damages can sometimes be simple, such as where the amount of severance is specified in the contract, but they also be quite difficult if, for example, the right to future bonuses depends on proof of profit levels had the executive not been terminated or not engaged in competitive behavior that was forbidden by the contract. The question of whether damages are unduly speculative is often one for the arbitrator to consider.

When a company initiates a lawsuit against a former employee, the employee often claims that he or she is entitled to upfront advancement of legal fees. This often is a subject of a request for emergency relief at the outset of an arbitration. Whatever decision the arbitrator makes initially can be revisited if he or she determines that the employee engaged in willful misconduct or fraud (the exact standard to apply depends on the

language of the indemnification clauses at issue).

Path to Resolution

In both mediation and arbitration, cases involving senior executives involve difficult issues of both fact and law. Strong personalities and highly successful executives are usually involved in complex situations. The mediator must work through all that to get to a resolution. In cases where mediation has not been successful, then it is up to whoever is chosen as the arbitrator to hear all the evidence and reach a decision that is unlikely to bring complete satisfaction to either party but may still confer the advantages of efficiency, confidentiality and choice of adjudicator.

Mark E. Segall, former head of litigation for JPMorgan Chase & Co., is a mediator and arbitrator with JAMS.

