EVIDENT PARTIALITY OF ARBITRATORS IN LAW FIRMS

By

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I. Introduction

In the last decade, there have been a growing number of challenges to arbitration decisions, some derived from one statutory basis for vacating an award, "evident partiality" of an arbitrator.[1] The purpose of this article is to examine selected case law focused on a particular fact situation: a member of a law firm being appointed as an arbitrator.

The law firm context presents particular difficulties because lawyers are required to zealously advocate the interests of their client and the representation (and conflicts) of one member of a firm are attributed to the others. Therefore, a member of a law firm might be conflicted from acting as an arbitrator in a dispute due to the representation of an affiliate of a party to the arbitration by a partner in a distant office of which the prospective arbitrator is completely unaware. The conflict check process is complicated by difficulties in checking party affiliates and prospective witnesses.

II. Standards and Guidelines for Evident Partiality

Two different standards for evident partiality emerged from *Commonwealth Coatings Corp. v. Continental Casualty Co.* 393 U.S. 89 (1968) which involved the failure of an arbitrator to reveal that one of the parties to the arbitration was a regular customer. For a plurality, Justice Black wrote

> It is true that arbitrators cannot sever all their ties with the business world, since they are not expected to get all their income from their work deciding cases, but we should, if anything, be even more scrupulous to safeguard the impartiality of arbitrators than judges, since

> the former have completely free rein to decide the law as well as the facts and are not subject to appellate review. We can perceive of no way in which the effectiveness of the arbitration process will be hampered by the *simple requirement that arbitrators disclose to the parties any dealings that might create an impression of possible bias.*

Id. at 148-9 (emphasis added).

Justice While concurred in the *Commonwealth Coatings* decision commenting that arbitrators are not automatically disqualified by a business relationship is disclosed to the parties. He further wrote:

> The Court today does not decide that arbitrators are to be held to the standards of judicial decorum . . . . It is often because they are men of affairs, not apart from the marketplace, that they are effective in the adjudicatory function.
> . . . .
> Of course, an arbitrator's business relationships may be diverse indeed, involving more or less remote commercial connections with great numbers of people. He cannot be expected to provide the parties with his complete and unexpurgated business biography. But it is enough for present purposes to hold, as the Court does, that where the arbitrator has a substantial interest in a firm which has done more than a trivial business with a party, that fact must be disclosed.

Id. at 150 – 2 (concurring opinion).

In reviewing this case law, subsequent courts have blended the opinions of Justices Black and White and articulated the evident partiality standard in various ways. In *Positive Software Solutions, Inc. v. New Century Mortg. Corp.,* 476 F.3d 278, 283 (5th Cir. 2007) the court stated the issue as whether the nondisclosure involves a "significant compromising relationship." In *Applied Indus. Materials Corp. v. Ovalar Makine Ticaret*

Ve Sanayi, A.S., 492 F.3d 132, 137 (2nd Cir. 2007) the court stated the issue was whether "a reasonable person would have to conclude that an arbitrator was partial to one party to the arbitration." For a very similar articulation of the issue, *see Kaplan v. First Options of Chicago, Inc.*, 19 F.3d 1503, 1523 n. 30 (3rd Cir. 1994). The court in *Woods v Saturn Distribution Corp.,* 78 F.3d 424, 427 (9th Cir. 1996) described the issue as whether the non-disclosed information creates a "reasonable impression of bias."

Several courts have identified factors useful in application of the evident partiality test. *See Scandinavian Reinsurance Co. Ltd. v. St. Paul Fire and Marine Ins. Co.*, 668 F.3d 60, 74 (2nd Cir. 2012) describing factors adopted in the Fourth Circuit:

> (1) the extent and character of the personal interest, pecuniary or otherwise, of the arbitrator in the proceedings; (2) the directness of the relationship between the arbitrator and the party he is alleged to favor; (3) the connection of that relationship to the arbitrator; and (4) the proximity in time between the relationship and the arbitration proceeding.

See also, the standards used by district courts in the Second Circuit described in note 18. *Id.*

III. ARIAS-US Code of Conduct

One point of reference to these issues is the ARIAS-US Code of Conduct. Canon IV provides, in part:

> 1. Before accepting an arbitration appointment, candidates should make a reasonable effort to identify and disclose any direct or indirect financial or personal interest in the outcome of the proceeding or any existing or past financial, business, professional, family or social relationship that others could reasonably believe would be likely to affect their judgment, including any relationship with persons they are told will be potential witnesses.
>
> . . . .
>
> 3. The duty to disclose all past and present interests or relationships is a continuing obligation throughout the proceeding. . . .

IV. Selected Case Law on Evident Partiality of Arbitrators in Law Firms

A. <u>No Evident Partiality Found</u>

The party arbitrator for the reinsurer failed initially to disclose that four years earlier while working in a law firm, he represented a subsidiary of the reinsurer in a dispute that was settled and billed 380 hours on the matter. The cedent moved to vacate an

adverse order based on alleged evident partiality based on the non-disclosure. In the course of its decision, the court observed:

> Parties are free to choose for themselves to what lengths they will go in quest of impartiality. . . . The more experience the panel has, and the smaller the number of repeat players, the more likely it is that the panel will contain some actual or potential friends, counselors, or business rivals of the parties. Yet all participants may think the expertise-impartiality tradeoff worthwhile; the Arbitration Act does not fasten on every industry model of the disinterested generalist judge. . . . To the extent that an agreement entitles parties to select interested (even beholden) arbitrators, §10(a)(2) [of the Federal Arbitration Act] has no role to play.2

The court ruled that there was no evident partiality citing the following factors: (a) the arbitrator's former law firm did not represent a party in the current arbitration and nobody connected with the firm was a material witness; and (b) the work the arbitrator did for the reinsurer's subsidiary was unrelated to the current dispute.3 The court ruled that failure to disclose this connection did not turn the non-disclosure into evident partiality. 4

Another tangential law firm connection was involved in *NGC Network Asia, Llc. V. Pac Pacific Group International, 2012 U.S. Dist. Lexis 14970 (S.D.N.Y.).* Pursuant to AAA

procedures, a Los Angles partner in Arent Fox was selected as the arbitrator. Shortly thereafter, the partner informed the parties that his Washington DC office had worked for the National Geographic Society which was a parent of National Geographic Television that sold programming to NGC International that, in turn, provided it to NGC, a party to the arbitration. The court rejected the claim that the partner was evidently partial:

> Thus, the question for the Court is whether a reasonable person would have to conclude that [the arbitrator], whose firm never represented NGC, but has represented an entity [the National Geographic Society] that is a non-controlling (27%) indirect owner of NGC, exhibited evident partiality. The answer is plainly "No."5

B. Evident Partiality Found

Thomas Kinkade Co. v. Lighthouse Galleries, Llc., 2010 U.S. Dist. 10757 (E.D. Mich.) involved an arbitration that lasted nearly seven years. In the fifth year of the arbitration, the umpire informed counsel that: (a) a partner in his law firm had been retained as a defense expert in a malpractice action against one of the other arbitrators; and (b) another partner in his law firm had been asked to represent a defendant in the arbitration in an unrelated NASD arbitration. This plus a series of one-sided decisions

and irregularities caused the plaintiffs to seek vacature for evident partiality. The court granted the motion ruling:

> Taken together the aforementioned issues cast a dark shadow over the parties' arbitration proceeding. It is not just that Defendants benefited from a single error of law; time and again irregularities in the proceeding favored Defendants. Given [the umpire's] mid-arbitration disclosures, these circumstances cannot be blamed on coincidence alone and a reasonable person would have to conclude that [the umpire] was partial to Defendants. Therefore, the arbitration award must be vacated. 6

Another finding of evident partiality was made in *Amoco v. Occidental Petroleum Corp*., 343 S.W.3d 837 (Ct. App. Tex. 2011). After disclosures but before the hearing, a party arbitrator left his firm and became "of counsel" at another firm which represented parties related to those in the arbitration and attempted block the testimony in the arbitration of an officer of a related party in the arbitration. The arbitrator did not disclose these relationships. The court found evident partiality:

> We recognize that evident partiality is generally proved by an arbitrator's nondisclosure of his own potential conflicts,

> whereas here [the arbitrator's] evident partiality was proved by his nondisclosure of *his firm's* potential conflicts. Nonetheless, the fact that a reasonable person could conclude the circumstances *might* have affected [the arbitrator's] impartiality triggered his duty to disclose.[7]

IV. Commentary

The above case law suggests that any current or very recent representation of a party, or a related entity, by the arbitrator or a member of the arbitrator's law firm will be regarded by a court as evident partiality. However, the odds of a court so finding decreases with an increase in the time and distance between the representation at issue and the arbitration.

ENDNOTES

[1] Federal Arbitration Act 9 U.S.C.A §10 (a)(2).
[2] 307 F.3d 617 at 620.
[3] *Id.* at 621.
[4] *Id.* at 623.
[5] 2012 U.S. Dist. Lexis 14970 *9-10.
[6] 2010 U.S. Dist. Lexis 6443 *28-8.
[7] 343 S.W.2d 837 at 850 (emphasis in the original).