Ex Parte Communications in Arbitrations

and Their Consequences

By

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I. Introduction

Arbitration panels commonly adopt rules pertaining to *ex parte* communications concerning: (a) the time periods within which counsel may communicate with their party arbitrators; (b) counsel copying opposing counsel and party arbitrators on communications with the umpire; (c) party arbitrators copying the opposing party arbitrator on communications with the umpire; and (d) the umpire copying both party arbitrators on internal panel communications and both counsel and both party arbitrators on external communications. A common version of such rules has been codified in the ARIAS Code of Conduct, Cannon V. Notwithstanding some recent, well-publicized cases involving *ex parte* communications, the consequences of such communications are not well understood. The purpose of this article is to explore selected case law dealing with the consequences of *ex parte* communications.

II. Case Law under the Federal Arbitration Act and State Clones

The Federal Arbitration Act ("FAA") governs arbitration of issues involving interstate commerce. However, many states have enacted their own versions of arbitration laws that, typically, are very similar to the FAA. As a result, cases based on state law are relevant even if the insurance transaction involved is interstate commerce.

A. Cases in Which the Court Declined to Vacate an Order

There are many such cases. One case involving a reinsurance dispute is *Mutual Fire, Marine & Inland Ins. Co. v. Norad Reinsurance Co.*, 868 F.2d 52 (3rd Cir. 1989). During the course of the hearing, it became evident that one or more of the panelists tried (unsuccessfully) to track down one of the individuals involved in the dispute. Losing counsel argued that this was an *ex parte* investigation by the panel that constituted misbehavior by which that counsel's client was prejudiced pursuant to § 10 (c) of the FAA. The court noted that losing counsel had the burden of proof that prejudicial *ex parte* communications took place. The court ruled that counsel had not met this burden of proof:

> Even if we assume, as appellants contend, that the evidence they proffered establishes that the arbitrators engaged in some form of *ex parte* contacts, we nevertheless conclude that the arbitrators' award can stand because the appellants have failed to carry their burden of showing how these contracts prejudiced them. The mere assertion by appellants that the arbitrators used information obtained *ex parte* in order to render their decision . . . is not enough, in our view, to establish the requisite prejudice necessary for this court to vacate the arbitrator's (*sic*) award.[1]

Remmey v. PaineWebber, Inc., 32 F.3d 143 (4th Cir. 1994) involved an umpire with a joking and informal matter. Testimony suggested that the umpire might have had an *ex parte* discussion with one of the counsel about seating in a crowded hearing room. The court found that the losing side did not prove that such a conversation actually took place or that even if it did, that the losing side was prejudiced thereby:

> [A]ppellant has failed to show that any remarks regarding seating would have prejudiced her case. Failure to make such a showing bars vacature of the arbitral award because "the party seeking a vacation of an award on the basis of *ex parte* conduct must demonstrate that the conduct influenced the outcome of the arbitration." Indeed, the decision of who sits where during a proceeding is a classic discretionary call for a presiding offer. {Appellant's] attempt to elevate this innocuous matter into a basis for overturning the entire arbitral result is indicative of a scatter-shot attack on an adverse decision.[2]

A somewhat bizarre case on *ex parte* communications is *Global Gold Mining LLC v. Calder Res., Inc.*, 941 F. Supp. 374 (S.D.N.Y. 2013). The losing party claimed it was prejudiced by its *ex parte* conversation with the sole arbitrator on the basis that the conversation gave the losing party a false impression of where it stood in the arbitration and, as result, such party made certain tactical decisions that did not result in a favorable order. Ignoring the irony of the situation, the court ruled that there was no prejudice to the losing party since: (a) the arbitrator's comments, if they in fact were made, were merely a present assessment that could change as the case developed; and (b) that there was no assurance of that different tactics would have produced a more favorable result.

Heartland Surgical Specialty Hosp., LLC v. Reed, 48 Kan. App. 237 (Ct. App. Kan. 2012) involved an arbitration between a hospital and a physician over a non-compete. The attorney for the physician had an 18 minute *ex parte* phone call with the single arbitrator who thereafter dismissed all but one of the hospital's claims without a hearing. The hospital sought to vacate the arbitrator's ruling on *ex parte* and other bases relying on Kansas arbitration statute "K.S.A. 5-412(a) and (b) which require the court to vacate the court an arbitration award where '(1) The award was procured by corruption, fraud or other undue means; [or] (2) There was evident partiality by an arbitrator appointed as a neutral or corruption in any of the arbitrators or misconduct prejudicing the rights of any party."'[3] The court declined to vacate:

> It goes without saying that the arbitrator and [the physician's] counsel should not have engaged in any *ex parte* communications about what pleadings were to be filed or about

> any other similar subjects. [The hospital] argues then that there should be a strong presumption of prejudice sufficient to vacate the award. However, we are aware of no such presumption in Kansas law. Rather, when a party files a motion to vacate an arbitration award on grounds of improper *ex parte* communication, the party must advance proof that any *ex parte* communication "affected or played a part in the decision rendered by the arbitrators."
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> . . . Based on the relevant facts from the record, which are undisputed, we fail to see that any *ex parte* communication affected the arbitrator's decision here.[4]

A complaint to a lawyer disciplinary board about *ex parte* communication was the issue in *In re Conduct of Merkel*, 341 Ore. 142 (2006). The attorney for one of the parties had issued subpoenas to two witnesses but they could not be physically present on the designed hearing date. The attorney called the arbitrator, without the participation of the other attorney, to ask if the arbitrator had a speakerphone and was willing to accept telephonic testimony. The arbitrator responded that he had a speakerphone and was willing to accept such testimony if opposing counsel did not object. The attorney thereafter informed opposing counsel who filed objected and filed an ethics complaint. The relevant standard under the ethics code was whether the communication was on the merits of the dispute meaning whether it "affects any legal right or duty of the parties." The court ruled that the conversation with the arbitrator was not on the merits and not an ethics violation:

> The conversation concerned the procedural issues of whether the arbitrator had speaker phone technology and the arbitrator's policy regarding telephone testimony, not whether [the opposing party] had a right to agree or to object to the presentation of a testimony by telephone. The accused did not ask for such a ruling and, nor did the arbitrator make such a ruling. . . . It does not appear that the communication was "on the merits" of the pending proceeding.[5]

The arbitrator inadvertently neglected to rule on a claim in *A.M. Classic Construction, Inc. v. Tri-Build Development Co.,* 70 Cal. App. 4th 1470 (Ct. App. 1999). The arbitrator found for the sub-contractor on the primary issue but failed to rule on a claim necessary for the contractor to collect on the primary issue. The attorney for the sub-contractor wrote to the arbitrator asking for such a ruling and enclosing a proposed order. The attorney followed-up with a call to arbitrator. Both communications were *ex parte.* Thereafter, the arbitrator amended his original order to rule in favor of the sub-contractor on the omitted issue. Opposing counsel moved to vacate based on the California arbitration statute. The court declined to do so:

> We agree the arbitrator should have advised appellants' counsel of the *ex parte* communication and that he would be issuing an amended arbitration award resolving the stop loss notice claim. In the absence of a showing that the arbitrator was improperly influenced or actually considered evidence outside the original arbitration proceedings such that appellants needed a further opportunity to be heard on the stop notice claim, appellants cannot demonstrate that the amended award was procured by corruption,

> fraud, undue means, or misconduct of the arbitrator within the meaning of section 1286.2, subdivisions (a), (b) or (c).

B. Cases in Which the Court Vacated an Order

There are relatively few cases in which arbitration orders were vacated for *ex parte* communications. One such case is *Maaso v. Singer*, 203 Cal. App. 4th 362 (Ct. App. 2012). After an arbitration hearing, but while an order was pending, one of the arbitrators faxed argument to the umpire and indicated a carbon copy to the opposing arbitrator but the copy was sent by ground mail to the opposing arbitrator's former address when he actually had the opposing arbitrator's fax number. Before the errant communication reached opposing counsel, the arbitrator issued an order in favor of the client of the attorney who faxed the argument. The trial court vacated the order finding that the motive and actions of the arbitrator who issued the argument highly questionable and that such actions improperly influenced the umpire's decision. The appellate court noted that *ex parte* contacts between a party arbitrator and an umpire justifies vacating the arbitration award. The court upheld that lower court: "We agree with the trial court that an *ex parte* communication undermines the fairness and integrity of the arbitration process."[6]

Pacific & Artic Ry. & Navigation Co. v. United Transp. Union, 952 F.2d 1144 (9th Cir. 1991) was the review of the district court vacation of an arbitration order for fraud under the Railroad Liability Act and the court characterized their review as "among the narrowest known to the law."[7] The lower court found:

> In light of the entire record, including the procedural improprieties; egregious non-disclosures and unbelievable *post facto* explanations by the [arbitrator for the union and umpire], the [umpire's] assumption of an advocate's role and active assistance to the union in shaping the record so that it might support his awards; numerous *ex parte* communications between [the party arbitrator for the union and umpire]; [the umpire's] acceptance of gratuities and other favors from [the party arbitrator for the union] or union officials; the actual and demonstrated bias of [the umpire] and the irrational awards that are the product [of the umpire's] bias and favoritism, I conclude that the awards are tainted by the functional equivalent of fraud . . . .[8]

Based on this record, the court of appeals upheld the lower court.

An arbitration concerning a ship charter provided the backdrop for *Totem Marine Tug & Barge, Inc. v. North American Towing, Inc.,* 607 F.2d 649 (5th Cir. 1979). After the close of the arbitration hearing and during deliberations, the arbitrators determined that they needed verification of the earnings of the vessel in question and they placed an *ex parte* call to the vessel owner. The panel adopted the figures supplied by the vessel owner without an opportunity by the opposing party to challenge such figures. The court vacated the award holding:

> After the arbitration panel improperly extended the scope of the arbitration to include charter hire, the extent of Totem's liability hinged on the determination of the earnings of the [vessel] . . . . The ex parte receipt of evidence bearing on this matter constituted misbehavior by the arbitrators prejudicial to Totem's rights in violation of 9 U.S.C.A. § 10 (c).[9]

Mor Katz v. Hugo Uvegi, 187 N.Y.S.2d 511 (S.C.N.Y. 1959) involved an arbitration in which the panel ordered the respondent from the hearing room for one-half hour during which the petitioner provided testimony that the respondent was unable to rebut. The court declined to confirm the subsequent award stating: "Arbitrators cannot conduct ex parte hearings or receive evidence except in the presence of each other and of the parties, unless otherwise stipulated."[10]

III. Alternative Standards for Addressing *Ex Parte* Communications

A. Breach of Arbitration Agreement

Star Ins. Co. v. Nat'l Union Fire Ins. Co., 2016 U.S. App. LEXIS 15306 (6th Cir.) involved an arbitration pursuant to Michigan law with a three-member arbitration panel. The panel adopted a scheduling order that cut off *ex parte* communication at the submission of the first brief on the merits. The day that the panel issued an interim final award, the party arbitrator and counsel for the reinsurer had an *ex parte* conversation, again two days later and thereafter. The party arbitrator for the reinsurer and the umpire had a number of *ex parte* communications and issued two orders adverse to the cedent without the participation of the party arbitrator for the cedent who, they were told, was sailing in northern Canada and out of reach. When the reinsurer filed briefs supporting its motion for costs, the cedent discovered the extensive *ex parte* contacts noted above and filed motions to stay the arbitration and to reconsider certain rulings but they were denied.

When the panel issued a final order, the cedent filed a suit asking the court vacate two of the panel's orders based on "misconduct" under Michigan's arbitration statute due to *ex parte* communications in violation of the panel's scheduling order and the arbitration agreement between the parties. The appellate court rejected the reinsurer's argument that the interim final award was actually a final order on the merits thus allowing *ex parte* communications to resume. The court vacated the orders issued without the participation of the cedent's party arbitrator:

> We hold that because [the reinsurer's counsel's] *ex parte* communications with [the reinsurer's party arbitrator] violated the plain terms of the parties' scheduling orders, [the cedent] need not demonstrate prejudice for us to vacate the Arbitration Panel's two awards.[11]

Nonetheless, the court went on to state that the time line of events in the arbitration demonstrated prejudice.

B. Disqualification of Counsel

Another way to penalize *ex parte* communications between counsel and party arbitrator is demonstrated by *Northwestern Nat'l Ins. Co. v. Insco, Ltd.* 2011 U.S. Dist. LEXIS 113626 (S.D.N.Y.). In this case, the reinsurer's party arbitrator offered, and the reinsurer's counsel accepted, 182 pages of internal panel emails, some dealing with issues still under deliberation by the panel. The court observed that turning over such documents to counsel violated the ARIAS-US Code of Conduct and Ethical Guidelines, the American Bar Association's Code of Ethics for Arbitrators in Commercial Disputes and the New York State Rules of Professional Conduct and that the court has the power to discipline counsel for ethical violations. The court found that these disclosures were not justified as an effort to obtain feedback from a party arbitrator or an effort to prove bias on the part of the opposing party arbitrator. The court further found that these disclosures tainted the arbitration proceeding which justified disqualification of counsel in further proceedings. The court stated:

> [D]isclosure of the [panel emails] tended to taint the proceedings, and to the extent there is any doubt, it should be resolved in favor of disqualification. In an age in which electronic communications play a central role in arbitrator deliberations, it is imperative that such communications remain as protected as all other forms of private panel interactions. Deliberate action to obtain such records is a disservice to the integrity of the adversarial process, and is strictly and unambiguously prohibited. Allowing parties to obtain confidential panel deliberations would provide an unfair advantage in the legal proceedings and have a chilling effect on the ability of arbitrators to communicate freely.[12]

IV. *Ex Parte* Panel Discussions with Experts

U.S. Life Ins. Co. v. Superior National Ins. Co. et al., 591 F.3d 1167 (9th Cir. 2010) involved Phase II of a long-running arbitration. Phase II focused on the quality of the cedent's workers compensation claim handling on over 12,000 files. The panel could not reach a decision based on the divergent opinions of the experts on 500 sample files and retained two experts ("reviewers") to assist.

> The panel and the parties exchanged correspondence discussing what review process to use. Ultimately, the panel determined that the following process would be used: (1) the reviewers would review 162 of the 500-claim sample . . .; (2) the reviewers would meet with the panel for three days (hereinafter, "the ex parte meeting") and no transcript would be prepared of the ex parte meeting; (3) reviewers would provide their conclusions in writing to the panel and the parties; (4) the parties could submit briefs responding to the reviewers' conclusions; (5) a two-day hearing would be held during which the parties could question the reviewers, under oath, for five hours each as to

> their qualifications and the reasons for their conclusions, but not as to the ex parte meeting; and (6) the parties could submit post-hearing briefs to the panel.[13]

At the conclusion of this process, the panel decided, by majority vote, that the claims were properly handled.

The reinsurer contended that the procedure adopted by the panel violated § 10 of the Federal Arbitration Act in that closing the meeting of the panel with the reviewers constituted a refusal by the panel to hear pertinent and material evidence in the form of commentary from counsel. The reinsurer also charged procedural misbehavior, all to the prejudice of the reinsurer.

Noting the broad protocols for the submission of evidence adopted by the parties, the court ruled that there was no procedural misbehavior:

> [A]fter discussions with counsel, the panel unanimously determined that it would hold an ex parte meeting with the reviewers, the reviewers' written conclusions would be shared, pre- and post-hearing briefing would be allowed, and questions regarding the reviewers' qualifications and conclusions would be permitted. Because of the broad authority granted by the protocols to the panel, we hold that this process does not constitute misbehavior. . . . It is noteworthy that [the reinsurer's] party arbitrator agreed to this process and that he did not mention arbitral misconduct or misbehavior in his dissent [on the merits].[14]

Similarly, the court ruled that there was no violation of substantive due process:

> The panel advised the parties of its dilemma and determined what process to use only after receiving input from counsel through extensive and detailed correspondence. The process employed ensured due process by allowing the parties to present their respective arguments regarding the reviewers' conclusions by (1) reviewing the written conclusions, (2) submitting briefing addressing these conclusions, (3) questioning the reviewers about their qualifications and conclusions, and (4) submitting post-hearing briefing. Although the parties were not privy to what occurred during the ex parte meeting, the panel gave the parties ample opportunity to discover and critique the reviewers' conclusions.[15]

Finally, the court found that the reinsurer had not demonstrated the necessary element of prejudice by the use of neutral experts or the procedures related thereto.[16]

IV. Commentary

From the above case law, it is evident that there is no clear rule for determining whether *ex parte* communication will result in a penalty of some sort. In those jurisdictions that require a demonstration

that the *ex parte* communication resulted in an adverse panel order, it will be very difficult prove this unless the evidence is completely one sided. If this is the case, it is likely that the *ex parte* communication will need to be coupled with other bad behavior, which is the source of a number of the cases that vacated panel orders.

Star Ins. Co., supra, dealing with breach of the arbitration agreement and scheduling order, and *Northwestern Nat'l Ins. Co., supra,* dealing with providing private panel emails to, and disqualification of, counsel show more promise in deterring and punishing behavior which is far outside the bounds of arbitration ethics.

ENDNOTES

[1] 868 F.2d 52 at 57.
[2] 32 F.3d 143 at 149.
[3] 48 Kan. App. 237 at 249.
[4] *Id.* at 252 (internal citations omitted).
[5] 341 Ore. 142 at 147 – 8.
[6] 203 Cal. App. 4th 362 at 375.
[7] 952 F.2d 1144 at 1147.
[8] *Id.* at 1148.
[9] 607 F.2d 649 at 653.
[10] 187 N.Y.S.2d 511 at 518.
[11] 2016 U.S. App. LEXIS 15306 *43.
[12] 2011 U.S. Dist. LEXIS 113626*36
[13] 591 F.3d 1167 at 1171-2.
[14] *Id.* at 1176-7.
[15] *Id.* at 1175.
[16] *Id.*