

What if the Party is Unable or Unwilling to Pay for Arbitration?

Judge Abraham J. Gafni (Ret.)

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Parties who have entered into a valid arbitration agreement understand that under the Federal Arbitration Act (FAA), the matter generally must be resolved through arbitration rather than court litigation. Only after such resolution may they seek enforcement of the arbitration award or other relief in court.

But what if a party is unable to pay the costs of the arbitration? Conversely, what if a party has the financial wherewithal, but simply refuses to pay? May the arbitration be dismissed by the arbitrator; and, if dismissed, may a court, nonetheless, consider the dispute on the merits?

This issue was addressed recently by a federal appellate court in the case of *Tillman v. Tillman*, No. 13-56624, (9th Cir., June 15, 2016).

Renee Tillman brought a malpractice action against her law firm claiming that it had failed to advise her of the need to include other heirs in a wrongful death action arising from the death of her husband.

The court granted the law firm's motion to stay the court litigation and compel arbitration in accordance with the arbitration clause in its retainer agreement with Tillman. The arbitration proceeded with Tillman objecting to what she characterized as

"unnecessarily increasing costs." Eventually, Tillman was unable to deposit the \$18,562.50 required by the AAA as a condition of continuing with the arbitration.

The law firm declined the AAA's inquiry as to whether it was prepared to cover the required deposit. Then, Tillman requested that the AAA require "the firm to pay the deposit going forward under AAA Rules authorizing interim relief." The arbitrator, however, did not grant this motion. Rather, a deadline was set for Tillman to submit the funds. Ultimately, the arbitrator "terminated the arbitration due to the missing deposits."

Thereafter, the law firm requested that the court: lift the stay on the court proceedings, to be followed by the dismissal of Tillman's complaint pursuant to Fed. R.C.P. 41(b) which allows dismissal if a party fails to comply with a court order. It asserted that Tillman's failure to pay the required deposit violated the court's order compelling arbitration.

Tillman disagreed, contending that she had not violated the court order but had done "everything in her power" to comply. Moreover, the law firm could have continued with the arbitration if it had accepted the AAA's suggestion that it pay the deposit pursuant to AAA rules.

Before ruling on the Rule 41(b) motion, the district court conducted a hearing into Tillman's financial status. It determined that, in fact, she was "unable to pay for her share of the arbitration," and, therefore, the complaint should not be dismissed on the ground that she had violated a court order.

Nonetheless, the district court did order dismissal. It concluded that because the AAA rules required that Tillman and the law firm "bear the costs of the arbitration equally and allowed the arbitrator to suspend the proceedings if such costs were not deposited, the [FAA] deprived the district court of authority to hear 'the claims that would have been subject to the arbitration agreement.'"

The appellate court agreed that when, as here, there was a valid arbitration agreement that encompassed the dispute, the role of the district court would ordinarily be limited to enforcing the agreement. In the circumstances of this case, however, the meaning of "enforcing the agreement" was not clear. It concluded that while the district court correctly lifted the stay on the court proceedings, it erred in dismissing the case under its interpretation of the arbitration agreement and not allowing it to proceed in court.

In reaching this decision the court noted that the FAA requires courts to stay - proceedings in disputes subject to arbitration "'until such arbitration has been had in accordance with the terms of the agreement' 9 U.S.C. Section 3."

But how should the action of the arbitrator in terminating the proceedings without entering an award because one of the parties could not pay costs be characterized? Does this satisfy the requirement that the arbitration "has been had" so that a stay on court proceedings is no longer required?

In reaching its decision, the court referred to the AAA's Rules which had been explicitly incorporated into the retainer agreement. They provided that:

- The AAA might not only prescribe fees but also reduce them in the event of hardship;
- The AAA is allowed to require parties to pay deposits in advance in such sums as it deems necessary;
- In the event of nonpayment, the AAA may limit a party's ability to assert or pursue its claim and "order the suspension of the arbitration;"
- Following such a suspension, if the parties have still not made the full deposit within a designated time period, the arbitrator "may terminate the proceedings."

The court concluded that as all of these steps, including termination without the issuance of an award, had occurred, the arbitration had "been had in accordance with the terms of the agreement." Therefore, there was no longer a basis for the stay which was properly lifted. It also agreed with the district court that it would have been unduly harsh to dismiss Tillman's complaint under Rule 41(b) for not complying with a court order requiring arbitration as her failure resulted only from her inability to pay and the law's firm unwillingness to front the costs.

The court, however, could find no section of the FAA or case law warranting dismissal where the arbitration had been terminated due to a party's inability to pay required fees. Because the arbitration "had been had," and, in effect, completed through termination, the arbitration agreement was no longer in effect. However, as no award had been made, the dispute had not yet been resolved. Accordingly, the district court was obliged to decide the case still remaining before it and erred in deciding that "it lacked the power to allow further litigation".

But, the court does make clear that a party may not frustrate the arbitration agreement merely by refusing to pay its costs. Here, Tillman had satisfied the court that she had given not only given early notice of her inability to pay and "made genuine efforts to make alternate payment arrangements," but was, in fact, unable to pay. Had she refused to pay, when she had a capacity to do so, however, the court's order to dismiss under Fed. R. Civ. P. 41(b) would have been perfectly appropriate "for failure to comply with the order to arbitrate despite its ability to do so".

As the court summarized, "Here, Tillman and the firm chose rules that allowed the - arbitrator to terminate their arbitration in the event of non-payment without any resulting award or judgment. Tillman cooperated with these rules as long as she was able to. No section of the FAA compelled the district court to dismiss her case once the arbitration had concluded in accordance with the agreed upon rules governing but without resolution".

Some other considerations would appear to emerge from this opinion.

First, a party who is unable to pay arbitration costs cannot object to court litigation on the ground that there was an arbitration agreement in existence.

Second, and perhaps most important, the opinion reflects that poorer parties may be able to avoid arbitration by reason of an inability to pay while richer ones cannot. This may become particularly relevant in light of recent objections, particularly by consumers and employees, who contend that they have been unfairly coerced to submit to arbitration.

Finally, parties with sufficient funds may wish to consider up fronting all of the costs including those of their adversary (which the law firm here refused to do) to avoid possible delay, additional expense and public notoriety resulting from a court proceeding. •

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