Arbitrator Impartiality: What Should be Disclosed?

Judge Abraham J. Gafni (Ret.)
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Arbitration integrity is based upon an assumption that arbitrators will not accept appointments unless they are impartial in fact or disclose any information that might raise a question as to their impartiality. But what must be disclosed to assure that the parties are appropriately and sufficiently apprised of the prospective arbitrator's relationship to the parties or matter to be arbitrated?

A recent case from the U.S. Court of Appeals for the Ninth Circuit, and provisions now included in the Pennsylvania version of the Revised Uniform Arbitration Act (RUAA), reflect that both arbitrators and parties should give careful attention to the issue of "evident partiality" in the arbitrator-selection process.

Monster Energy v. City Beverages, 943 F. 32d 1130 (9th Cir., 2019) (hereafter *Monster* and *Beverages*) involved a dispute as to whether Monster had improperly terminated Beverages' distribution rights under their agreement.

As their agreement provided for arbitration to be conducted by JAMS, an arbitrator was selected by the parties from a list provided by JAMS. The arbitrator submitted a disclosure statement at the commencement of the arbitration. It recited: "I practice in association with JAMS. Each JAMS neutral, including me, has an economic interest in the overall financial

success of JAMS. In addition, because of the nature and size of JAMS, the parties should assume that one or more of the other neutrals who practice with JAMS has participated in an arbitration, mediation or other dispute resolution proceeding with the parties, counsel or insurers in this case and may do so in the future."

After the arbitrator ruled in favor of Monster, Beverages filed a motion for vacatur, claiming evident arbitrator partiality based on undisclosed, later-discovered information that the arbitrator was a co-owner of JAMS.

In a 2-1 decision, the court granted vacatur, finding that Beverages had not waived its evident partiality claim by failing to timely object upon being apprised of the potential "repeat player" bias and the arbitrator's economic interest reflected in the disclosure statement.

Admittedly, Beverages reasonably understood from the arbitrator's disclosure statement that the arbitrator's interest was similar to that of "'each JAMS neutral' who has an interest in the 'overall financial success of JAMS.'"

The Ninth Circuit decided, however, that the disclosure statement failed to inform the parties that this specific arbitrator, unlike other JAMS neutrals, was also a co-owner of JAMS and was, therefore, potentially not neutral based upon the "totality" of JAM's Monster-related business. The court further noted that JAMS had apparently stymied Beverages' efforts to obtain information about its ownership structure. Beverages, therefore, could not be deemed to have waived its evident partiality claim by reason of constructive notice.

The court set out the following two questions, which if responded to in the affirmative required disclosure by the arbitrator:

- Whether the arbitrator's ownership interest in JAMS was sufficiently substantial; and,
- Whether JAMS and Monster engaged in nontrivial, substantial business dealings.

The court concluded that as this arbitrator had a right to a portion of profits from all JAMS distributions, not just from proceedings in which he had participated, his ownership interest was substantial in that it greatly exceeded the interests of other JAMS neutrals.

Moreover, because of contracts with Orange County, over a period of five years, JAMS had administered 97 arbitrations for Monster, an average rate of more than one a month. Such business dealings could not be deemed "trivial," regardless of the exact profit share realized by the arbitrator from such activity.

The court held, therefore, that the arbitrator had an undisclosed, substantial interest in the success of JAMS, which had been doing nontrivial, substantial business with Monster.

Accordingly, vacatur was appropriate as this interest created an impression of evident partiality that should have been disclosed.

The dissent, however, contended that the majority's view failed to reflect the reality of the arbitration world. It emphasized that:

- When electing to arbitrate, the parties essentially give up Article III protections, which assure impartiality in the federal courts.
- As arbitrators are hired and paid by the parties for whom they conduct arbitrations, they have an economic interest in cultivating repeat customers.
- An arbitrator affiliated with an arbitration firm has an economic interest in not causing the firm to lose its top clients.
- Thus, to some extent, arbitrators have an incentive to make decisions that are viewed favorably by parties who frequently engage in arbitration.

It concluded that "this feature of private arbitration, even if distressing, is an inevitable result of the structure of the industry." Parties are fully aware of this and, nonetheless, accept this "distressing" feature because of arbitration's other positive benefits.

Moreover, the dissent felt that the arbitrator had:

- Sufficiently disclosed a financial interest in JAM's success; and,
- Made clear that he and other JAMS arbitrators had conducted arbitrations with the parties and were likely to conduct future arbitrations with them.

In addition, Beverages should be deemed to have waived a claim of "evident impartiality" as a record search would have disclosed that JAMS had conducted dozens of arbitrations between Monster and its consumers, and that Monsters had an agreement calling for all such arbitrations with JAMs.

The dissent disagreed that the interest of the owner-arbitrator to retain business significantly exceeded the interest of the other nonowner JAMS neutrals; rather, both have a similar interest in advancing their careers, maintaining their status with JAMS and assuring that it not be terminated.

Finally, the dissent predicted that uncertainty about what must be disclosed will generate endless litigation as an owner-arbitrator may have to consider:

- The size of this interest;
- How it relates to the ADR firm's total profits over one or several years;
- How many prior arbitrations are necessary to clarify whether prior business dealings were nontrivial;
- The amount of fees earned by the ADR provider in the prior arbitration(s); and,

- How many prior arbitrations have been held with the lawyers and law firms to the parties (whom, presumably, the arbitrator would also wish to please)?

Thus, the dissent warned that the majority's expansive ruling will generate years of after-the-award litigation over the extent of disclosures required of arbitrators. In addition, it suspected that as a result of the threat inherent in the majority opinion, parties may turn to unaffiliated arbitrators who may have less expertise in a particular area (although they will, in all likelihood, have a similar desire to retain the business of repeat customers).

The disclosure required of arbitrators has similarly become the focus of attention in many states adopting the RUAA, which is also relied upon by the Ninth Circuit. Unlike the Federal Arbitration Act and the predecessor UAA, which stated that vacatur is warranted where there was evident partiality, Pennsylvania's RUAA, 42 Pa. C. S. Section 7321.13 sets out in greater detail a continuing duty to disclose "any known facts that a reasonable person would consider likely to affect the impartiality of the arbitrator in the arbitration proceeding." This would include not only a "financial or personal interest in the outcome of the arbitration proceeding," but also "an existing or past relationship with any of the parties to the agreement to arbitrate or the arbitration proceeding, their counsel or representatives, a witness or another arbitrator." Most significantly, the RUAA establishes a presumption of evident partiality when the arbitrator "does not disclose a known, existing and material interest in the outcome of the arbitration proceeding or a known, existing and substantial relationship with a party."

As the Ninth Circuit opinion and the RUAA reflect, arbitrator disclosure of potential conflict is a subject that is drawing significant attention. The opposing opinions in the Ninth Circuit case further highlight not only what must be disclosed by the arbitrator but also what responsibility arbitrators, parties and counsel may have in investigating such potential conflicts, including within an arbitrator's or party counsel's own law firm.

Courts will, presumably, be reluctant to vacate awards if it can be demonstrated that the parties, counsel and arbitrators acted reasonably in disclosing such potential conflicts. The guidelines for such reasonable action, however, will likely remain unclear in the immediate future. Parties, counsel and arbitrators are well-advised, therefore, to err on the side of disclosure of any such questionable information. •

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