Must the Number of Arbitrators Selected by Each Side Be Equal?

Judge Abraham J. Gafni (Ret.)
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Imagine that you and another respondent in an arbitration have the opportunity to select two arbitrators. You then discover that the opposing five claimants may select seven arbitrators. You are outraged, but confident that no court would ever allow an arbitration to proceed which is so clearly unfair. Right? Wrong!

In fact, it may be possible for a party to find that its appointed arbitrators are outnumbered, and the court will not intervene because the parties had agreed to this possibility in the arbitration agreement.

Such a situation presented itself recently in a case arising in the U.S. Court of Appeals for the Fifth Circuit in *Soaring Wind Energy v. Catic USA,* 946 F. 3rd 742 (5th Cir. 2020).

The dispute arose out of an agreement among seven Class A Members, which had created Soaring Wind as a vehicle for wind-energy marketing and project development. One of the member companies was Tang Energy (Tang). The agreement further provided that each member would "conduct activities constituting the business only in and through Soaring Wind and its controlled subsidiaries."

Eventually, Tang claimed that Catic, together with Paul Thompson (Thompson), one of the other Class A Members, through their affiliates, had violated the agreement and demanded arbitration against both Catic and Thompson and their affiliates.

The agreement provided that "any controversy, dispute or claim arising under or related to the agreement"… shall be submitted to binding arbitration." The agreement further provided that each "disputing member" of Soaring Wind, defined as "each member that is a party to the dispute," would then have the opportunity to name its own arbitrator. The selected arbitrators would themselves choose an additional arbitrator (or two additional arbitrators, if necessary, to achieve an odd-numbered arbitration panel).

Based upon the agreement, Tang and the four other Class A Members, who sided with Tang, selected their five arbitrators. Catic and Thompson selected their two arbitrators. As noted, the agreement provided for the appointment of one or two additional arbitrators by those arbitrators who had already been selected so that there would be an odd-numbered panel. Thus, two more arbitrators were appointed by a majority of the seven already selected. As five of those seven had been selected by the "Tang arbitrators," they, presumably, controlled the selection of the remaining two arbitrators, resulting in seven arbitrators selected by the Tang group, and only two by Catic and Thompson.

Catic objected to the arbitration on the ground that the panel was improperly constituted. It acknowledged that while there may be more than two "sides" to a dispute (and more than three arbitrators), the agreement must be interpreted to required that each "side" has an equal say in arbitrator selection; and, in addition, that this situation violated due process and public policy in that it was fundamentally unfair. It submitted that "the formation of a stacked, unfair arbitration is an absurd result to which no reasonable party would ever agree"

The court rejected these arguments.

It noted that the Federal Arbitration Act (FAA) at Section 5 requires that "if in the agreement provision be made for a method of naming or appointing an arbitrator or arbitrators or an umpire, such method shall be followed." Moreover, arbitrators appointed in a manner that departed from the contractual selection process would be exceeding their powers if they acted. Any order they might enter would be subject to vacatur.

The court enforced the agreement as written and concluded that the parties had not departed from the Agreement's arbitrator-selection procedure. While it was true that there were only two sides to the dispute, the agreement unambiguously contemplated a selection procedure based upon the number of parties, not the number of sides to the dispute. The agreement specifically provided that with respect to any dispute, "each member that is a party to such dispute is a 'disputing member.'" Moreover, each such disputing member was entitled to name an arbitrator.

In a striking reference to Greek mythology, the court noted the "Apple of Discord" thrown by the goddess Eris into the middle of a room of goddesses where the goddess who secured it would be deemed the most beautiful. Similarly, if "Eris had tossed the Apple of Discord into a Soaring Wind conference room, prompting a free-for-all among the parties—the arbiter selection process would have remained the same.".

The court recognized the absurdity of the Apple of Discord and other types of selection procedures, Nonetheless, it stated that a court may not choose from among competing reasonable interpretations while discarding the plain text of the agreement. "It is not the court's role to rewrite the contract between sophisticated market participants, allocating the risk after the fact, to suit the court's sense of equity or fairness." "One must assume that Catic USA did not expect to be outnumbered in any dispute falling under the agreement; that its expectations were frustrated does not render the agreement absurd or unfair."

The court also rejected Catic's argument, based upon the New York Convention, which provides that a court may refuse to recognize or enforce an award where the party against whom the award was invoked was not given proper notice of the appointment of the arbitrator or arbitration proceedings or was unable to present its case. This has always been understood as "essentially sanctioning the application of the forum state's standards of due process." Catic contended that the arbitrator-selection

procedure did not meet minimal standards of due process or fairness that would result in an impartial decision because the two sides had appointed an unequal number of arbitrators.

The court noted that this argument, taken to its logical conclusion, would require the court to invalidate any arbitral award not issued by an evenly-appointed panel.

In rejecting this contention, the court noted that this was not a contract of adhesion, but a deal made between extremely sophisticated parties. It “did not inherently favor one party over another; it just so happened that Catic USA was outnumbered.” Courts, otherwise stated, are not going to invalidate an agreement-selection process that was followed precisely in accordance with its terms.

In short, if there is some ambiguity or lack of clarity, courts will, in all likelihood, adopt a fair and equitable result. However, when there is no such ambiguity, and the contract is not one of adhesion, the courts are not going to rewrite an agreement just to make it fairer.

Of critical importance here is recognition that the “unfair” arbitration in this situation resulted from a party not thinking through how the procedures set out in the arbitration agreement might play out in the future.

In preparing arbitrator-selection agreements, therefore, parties must look down the road and envision what might occur. Here, Catic should have considered the possibility of being on the minority side of a members’ dispute allowing it to appoint only a minority of the arbitrator panel members. In fact, such a possibility is contemplated in the AAA’s Commercial Arbitration Rule R-12(c), which provides that, “Unless the parties agree otherwise, where there are two or more claimants or two or more respondents, the AAA may appoint all the arbitrators”.

Of course, reference to rules provided by ADR providers can be helpful in focusing on issues and potential problems that should be considered in any arbitration agreement. These might include what rules of evidence should apply, what discovery will be permitted, whether witnesses may testify by affidavit or remotely, what certifications are required for the admission of documents, etc.

Whether the rules of a particular provider should be acceptable as the default rules for an arbitration or whether and how rules should be specially tailored in light of current or future circumstances, however, is a critical issue that parties must consider. Otherwise, they may end up, as did Catic, with an arbitration panel of seven against two. •

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