

The Arbitration Process In The United States

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In this time of market globalization, many industrial companies are including detailed arbitration clauses in their international contracts, in order to avoid the potential costs, delays, and uncertainties of litigation in foreign courts. Arbitration is less expensive and more flexible, procedurally, than court proceedings, and arbitral awards enjoy much greater international recognition than judgments of national courts. More than 134 countries have signed the 1958 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, known as the "New York Convention", which facilitates the enforcement of arbitral awards internationally. There are several other similar arbitration conventions that provide for the enforcement of cross-border arbitral awards. Additionally, arbitral awards are not subject to appeal, whereas judgments of national courts are routinely subjected to a lengthy appeals process, and there are very few viable bases to challenge arbitral awards.

This discussion will review key considerations in drafting arbitration clauses, including choice of law and choice of forum considerations; issues surrounding the selection of arbitrators; the discovery process; presentation of evidence; and enforcement of arbitral awards.

I. The Arbitration Agreement

Parties may agree to resolve future disputes through arbitration, or they may agree to submit an existing dispute to arbitration, but the Federal Arbitration Act requires that arbitration agreements in the United States be in writing. 9 U.S.C. § 2.

A written arbitration agreement between contracting parties should establish the following critical issues:

(1) The jurisdiction of an arbitrator, or a panel of arbitrators (often a panel of three arbitrators) to decide the dispute, and a hearing locale;

(2) The parties should clearly articulate limitations, if any, on the arbitrator's power to decide disputes. Contracting parties may wish to limit an arbitrator's power to decide only certain contractual issues, for example, rather than empowering an arbitrator to decide any and all issues that may arise between the parties during their course of dealing.

(3) The parties may choose to specify a procedure for attempting to resolve disputes through non-binding mediation prior to submitting claims to binding arbitration.

(4) The parties should choose the procedural rules for administering the arbitration process. The selected body of rules will then govern the process for initiating arbitration, appointing arbitrators, completing discovery, presenting evidence at the hearings, and related administrative and procedural matters. Many arbitration agreements, for example, provide for the application of the rules of the American Arbitration Association, or JAMS, organizations dedicated to administering alternative dispute resolution. In international disputes, parties may

also choose to administer their arbitration through the Commercial Arbitration and Mediation Center for the Americas (CAMCA) Rules, the Rules of the Inter-American Commercial Arbitration Commission (IACAC); the United Nations Commission on International Trade Law (UNCITRAL) Arbitration Rules; or some combination of these organizations' procedural rules.

(5) The parties should also include a "choice of law" provision to determine the substantive law applicable to the dispute, and an attorneys fees provision if they wish for the prevailing party to recovery attorneys fees.

Examples of standard arbitration, choice of law, and attorneys fees provisions follow:

"Arbitration. The parties agree that all controversies arising out of or relating to this contract, or the breach thereof, shall, upon written demand of any party hereto, be submitted to and determined by arbitration before the American Arbitration Association, in San Diego, California, in accordance with the Commercial Rules of the Association then in effect. Any award or decision rendered shall be made by means of a written opinion explaining the arbitrator's reasons for the award or decision, and the award or decision shall be final and binding upon the parties hereto. The arbitrator may not amend or vary any provision of this Agreement. Judgment upon the award or decision rendered by the arbitrators shall be entered in any court of competent jurisdiction.

Choice of Law. This agreement and the rights and obligations of the parties hereunder shall be construed in accordance with and governed by the laws of the State of California, without giving effect to the conflict of law principles thereof.

Attorneys Fees. In the event of any dispute between the parties concerning the meaning or effect of this Agreement, or for the purpose of enforcing or challenging this Agreement, or any term or condition thereof, the prevailing party shall be entitled to recover reasonable attorney fees and costs incurred in any arbitration or judicial proceeding. The term "prevailing party" shall mean the party, if any, that obtained the principal relief or result it sought in the proceeding, as shall be determined by the Court or arbitrators."

II. Initiating Arbitration

_____ Typically, the process for initiating an arbitration is set forth in the particular rules of procedure selected by the parties in the arbitration agreement. Invariably, the claimant commences the process by filing a demand for arbitration and "Statement of Claim", which describes the facts and circumstances of the dispute in detail. The claimant must also submit the appropriate filing fees, and an arbitrator compensation deposit, if required. The amount of the filing fees and arbitrator deposits vary considerably depending on the arbitration forum, and the amount of money at stake in the arbitration.

The Statement of Claim should read like a compelling story, and, unlike many court pleadings, the Statement of Claim should, in our experience, be narrowly tailored to the most central causes of action alleged in the case. If a claimant alleges a full panoply of wrongs, using the "shotgun" approach common in court litigations, some of which just don't fit the fact pattern,

the claimant may lose credibility with the arbitrator(s). The Statement of Claim, and the respondent's Answering Statement, may be the first and only documents the arbitrator(s) review before the hearings. Claimants using the "shotgun" approach may risk poisoning their own well if the first thing the Panel learns about their case is that some of the causes of action either are untimely (ie. subject to a short statute of limitations); don't provide a private cause of action (ie. statutory claims limited to enforcement by State or Federal agencies); or simply do not clearly apply to the facts of the case.

If a party named in an arbitration Statement of Claim refuses to arbitrate the dispute, or fails to respond, a claimant may petition a court of competent jurisdiction to compel arbitration to proceed. In *AT&T Technologies, Inc. v. Communications Workers of America*, 475 U.S. 643 (1986), the United States Supreme Court held that courts, not arbitration panels, should decide threshold issues of whether a party should be compelled to arbitrate. The Supreme Court held: "Unless the parties clearly and unmistakably provide otherwise, the question of whether the parties agreed to arbitrate is to be decided by the court, not the arbitrator." *Id.* at 649.

Arbitration is a matter of contract, however, and a party cannot be required to submit to arbitration any dispute which he has not agreed to submit." *AT&T Technologies, Inc.*, 475 U.S. at p. 649 (1986). Generally, only parties to an arbitration agreement may be compelled to arbitrate, and non-parties, or "non-signatories" to the written arbitration agreement, may only be compelled to arbitrate in circumstances in which the non-party is: (1) a third-party beneficiary to the contract containing the arbitration agreement; (2) a successor-in-interest; or (3) one of a class of agents whom the arbitration clause was intended to benefit. *Britton v. Co-op Banking*, 4 F.3d 742, 745-746 (9th Cir. 1993).

III. Selection of Arbitrators

After the parties have either voluntarily submitted to arbitration, or been compelled by a court to arbitrate, they must commence the selection of neutral arbitrator(s) to decide their dispute. In most cases, the administrative forum selected by the parties dictates the process for arbitrator selection and provides the parties with lists of available "neutrals" to select from.

Typically, the parties are each provided a list of prospective arbitrators and their current curriculum vitae. The parties then rank the arbitrators they deem acceptable, and strike the remaining arbitrators from their list. The administrator compares the parties lists and selects an arbitrator, or panel of arbitrators, in accordance with the parties stated preferences, if possible. Otherwise, if the parties are unable to agree upon any arbitrators, the administrator will typically appoint one, unilaterally, from a database of available arbitrators in the area.

It is extremely important for the parties and/or their representatives to carefully screen prospective arbitrators for bias. A cautious arbitration lawyer will perform extensive background analyses of each of the prospective arbitrators' work experience, articles and treatises, personal litigation history, and perhaps most important, the history and patterns of their arbitration awards. Some aggressive arbitration counsel retain private investigators for this purpose.

_____ Arbitrators are, of course, required to make disclosures of actual and potential conflicts of interest, and any other information that would create an appearance of bias. The parties are also free to submit written interrogatories to the arbitrators, before or after their appointment, to inquire about matters perceived to impact their impartiality. If any information surfaces that forms a basis to challenge an arbitrator's impartiality, a party may take steps to remove the arbitrator.

_____ **IV. The Discovery Process**

In most arbitral forums, the rules of procedure governing discovery and evidence are relatively simple: courtroom rules of evidence are not strictly applicable; there usually is no motion practice or formal discovery; and there is no requirement for transcripts of the proceedings or for written opinions of the arbitrators.¹

For example, the use of depositions and written interrogatories, which are common practice in court litigations, are strictly limited in arbitral forums. Although most arbitrators allow parties to request certain information during discovery through written interrogatories, arbitrators will generally limit interrogatories to the identification of witnesses and relevant dates and documents. The American Arbitration Association's Guide for Commercial Arbitrators generally instructs arbitrators as follows:

“4. Exchanging of Information and a Schedule for the Exchange (Including Reports from Experts) You should inform the parties that they are required to cooperate in committing to, conducting, and completing an exchange of information concerning their documents and witnesses. If they do not agree to exchange particular information, you should hear their disagreement and make a ruling on the issue. When the information to be exchanged has been specified, you should establish a schedule for the exchange.”

The AAA Guide contemplates that the parties should exchange information concerning “their documents and witnesses”, and not their detailed factual and legal theories of the case. In connection with securities industry disputes before the National Association of Securities Dealers, the NASD Discovery Guide specifically provides that information requests should be limited in arbitration to “..identification of individuals, entities, and time periods relevant to the dispute; such requests should be reasonable in number and not require exhaustive answers or fact finding. In other words, the standard (and extremely expensive) use of written interrogatories, as utilized in state and federal courts, are generally not permitted in arbitration.

Similarly, the AAA Guide explains the limited power of Arbitrators to allow parties to take oral depositions of witnesses:

“Consistent with the expedited nature of arbitration, the arbitrator may, at the preliminary hearing, establish (I) the extent of and schedule for the production of relevant documents and other information;(ii) the identification of any witnesses to be called, and (iii) a

¹ For examples of typical arbitral discovery and evidentiary rules, see NASD Notice to Members 99-90; AAA Commercial Arbitration Rule R-21.

schedule for further hearings to resolve the dispute... Although this rule vests in the arbitrators the discretion to direct documentary exchanges, it does not contemplate full-blown, litigationlike discovery...Some arbitrators, albeit rarely, interpret the "other information" portion of Section 10 quoted above to provide for depositions... Before making a ruling on discovery, the arbitrator must first ascertain whether the request is valid and reasonable." A Guide for Commercial Arbitrators, Discovery.

Also unlike court litigation practice, Federal and State law strictly limit the use of attorney-issued subpoenas to compel third parties to appear and testify at hearings, or to produce documents or information during discovery. Some states (including New York and Utah, for example) permit attorney-issued arbitration subpoenas, to compel attendance at the hearing, or to produce documents *at the hearing*. But such state laws cannot be used by attorneys to compel production of documents in the lawyer's office before the hearing. Additionally, some arbitral forum rules may further limit attorneys' right to issue third party subpoenas. ²

The Federal Arbitration Act, however, clearly authorizes *arbitrators* to issue third party subpoenas to compel attendance or produce documents at the hearing. An important difference between an FAA arbitrator issued subpoena and an attorney issued subpoena is jurisdictional. The FAA imposes national jurisdiction for arbitrator issued subpoenas, whereas attorney issued subpoenas are only permitted in states that allow for them. The law is unclear, however, as to whether arbitrators may issue pre-hearing "discovery" subpoenas on third parties. ³

V. Presenting the Law and Evidence at the Hearings

Many experienced arbitration practitioners utilize the "Keep it Simple Stupid" or "KISS" method of presenting evidence at an arbitration hearing. Oftentimes, practitioners forget that the arbitration Panel has not been spending the last few months researching the relevant law in preparation for the hearing. Most arbitrators try to be as prepared as possible, but often do not read the relevant papers until the evening before, or the morning before the hearing or telephonic motions. Often, a Claimant will submit a 10 page pre-hearing brief, and the Respondent will submit a 20 page brief with 150 citations, most of them "string cites", and the Panel comes to the hearing either "dazed and confused" if they actually read the briefs, or "wide-eyed" and usually unsure of what the relevant law really is.

In our experience, the K.I.S.S. method is certainly the way to go. We prepare a simple pre-hearing brief focusing on favorable law. Forget long recitations of the facts; the facts will come out at hearing and the Panel will have read a diametrically opposed factual scenario in the opposing papers. Prior to the hearing, we find it very helpful to prepare simple handouts for the panel and present them on an E.L.M.O. (much better than the old fashioned overhead projectors) during our opening. We display relevant, simple quotes and statements of the law in our "show and tell" presentation. Panels typically will recall a simple quote shown bigger than life on a screen than they will finding it buried in a lengthy complicated brief. Most panelist are not attorneys and briefs and string cites mean nothing to most of them. They need to be spoon-fed, in very small spoonfuls, the few, salient legal points. This forces the

² Third Party Discovery and Subpoenas in Arbitration, by Seth E. Lipner, p. 58.

³ Third Party Discovery and Subpoenas in Arbitration, by Seth E. Lipner, p. 59.

panel to read and listen to the law; while at the same time giving them something simple they can rely on when awarding damages.

We have also found it very helpful to use a law professor to assist in presenting legal authority. Not only does this enhance the credibility of your argument, it also really helps the Panel understand the law. Remember, law professors, at least the good ones, are accustomed to teaching concepts to law students in a way they will understand. Obviously, hiring a law professor as an expert can be costly and may be economical only in a large damage case, but we have had excellent results using law professors who are specialists in their respective areas. For example, we have used a Dean of a law school whose specialty was securities law; a Professor who wrote the book on broker-dealer law and, most recently, a professor who wrote a two-volume treatise on "State Securities Laws", published by the popular West legal publishing company. He put his two volumes on the table and proceeded to give a complete and thorough discourse on why the various state securities laws did not apply in our case (it was a defense case for a national charity). Law professors are like "talking briefs", and arbitrators, in our experience, are much more apt to listen to what an expert has to say than they are to read a brief.

VI. Enforcement of the Award

Arbitral awards enjoy much greater international recognition than judgements of national courts. Over 134 countries have signed the 1958 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, known as the "New York Convention". The Convention facilitates enforcement of awards in all contracting states. There are several other multilateral and bilateral arbitration conventions that may also help enforcement of arbitral awards. Additionally, arbitral awards are not subject to appeal, whereas judgements of national courts are routinely subjected to a lengthy appeals process, and there are very few viable bases to challenge arbitral awards.

Immediately after the arbitrator renders a favorable award, we routinely petition a court of competent jurisdiction to "confirm" the award, and thereby convert the arbitral award into a court judgment which can be enforced for collection purposes. The losing party in an arbitration, on the other hand, may petition a court to vacate the arbitral award, but such petitions are rarely granted.

Section 10 of the Federal Arbitration Act delineates the grounds for setting aside an arbitration award:

“§ 10. Same; vacation; grounds; rehearing

(a) In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration--

(1) where the award was procured by corruption, fraud, or undue means;

(2) where there was evident partiality or corruption in the arbitrators, or either of them;

(3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or

(4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

(b) If an award is vacated and the time within which the agreement required the award to be made has not expired, the court may, in its discretion, direct a rehearing by the arbitrators.

(c) The United States district court for the district wherein an award was made that was issued pursuant to section 580 of title 5 may make an order vacating the award upon the application of a person, other than a party to the arbitration, who is adversely affected or aggrieved by the award, if the use of arbitration or the award is clearly inconsistent with the factors set forth in section 572 of title 5.

The four basic grounds for vacating an award enumerated above are exceedingly difficult to establish, and petitions to vacate are almost never granted.