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ARTICLES

Seventh Circuit Allows Arbitrator to Hear Dispute over Original Award

By Adam Waskowski

After an arbitration award has been issued, a party may learn information that undermines the validity of that award and challenge the award in a second arbitration proceeding. Several questions may arise in this situation. For example, can a party arbitrator in the first proceeding also serve as an arbitrator in the proceeding that challenges the award? If the arbitrators signed a confidentiality agreement in the first proceeding, who construes how that agreement will affect evidentiary issues in the second proceeding? If the arbitration panel in the second proceeding rules on these issues, and a party seeks to enjoin the proceeding, can the expense of going forward with the second proceeding constitute the kind of irreparable harm needed to support the injunction? The United States Court of Appeals for the Seventh Circuit recently addressed each of these issues in *Trustmark Insurance Co. v. John Hancock Life Insurance Co.*, 631 F.3d 869 (7th Cir. 2011), *cert. denied*, 131 S. Ct. 2465 (2011).

Background, Arbitration, and Trial Court Proceedings

In *Trustmark*, the Trustmark Insurance Company and John Hancock Life Insurance Company had arbitrated a reinsurance dispute. *Id.* at 871. Thereafter, Trustmark allegedly refused to comply with the award. Hancock commenced new arbitration proceedings; as a defense, Trustmark argued that the first award had been procured by fraud based on Hancock’s failure to produce material documents. Hancock nominated Mark S. Gurevitz—its party arbitrator in the first arbitration proceeding—as its party arbitrator in the second proceeding. In the first proceeding, Gurevitz had signed a confidentiality agreement. The panel ruled that the confidentiality agreement did not prevent it from hearing evidence about whether the first award was procured by fraud.

Trustmark then commenced a diversity lawsuit in federal court to enjoin the second arbitration proceeding. The district court enjoined the proceeding, finding that (1) Gurevitz was not a “disinterested” arbitrator; (2) the confidentiality agreement prevented the panel from hearing evidence about the first award in the second arbitration proceeding; and (3) Trustmark would suffer irreparable harm if it were forced to participate in the proceeding. *See generally Trustmark Ins. Co. v. John Hancock Life Ins. Co.*, 680 F. Supp. 2d 944 (N.D. Ill. Jan 21, 2010).

Seventh Circuit Reverses: No Irreparable Harm

The Seventh Circuit reversed. The court held that the district court should not have entered the preliminary injunction because Trustmark failed to establish irreparable harm. *Trustmark*, 631 F.3d at 872. The court held that Trustmark’s anticipated legal fees in the arbitration proceeding

could not be irreparable harm as a matter of law. This holding is arguably inconsistent with decisions from the Seventh Circuit and other federal circuits that have enjoined arbitration proceedings on the ground that the dispute was not arbitrable; in those cases, the only alleged harm arguably was (or appeared to be) the expense and inconvenience of arbitration. *See, e.g., Md. Cas. Co. v. Realty Advisory Bd. on Labor Relations*, 107 F.3d 979, 985 (2d Cir. 1997) (party “would be irreparably harmed by being forced to expend time and resources arbitrating an issue that is not arbitrable”); *see also McLaughlin Gormley King Co. v. Terminix Int’l Co.*, 105 F.3d 1192, 1194 (8th Cir. 1997) (enjoining arbitration proceeding pending determination of whether dispute was subject to arbitration); *Duthi v. Matria Healthcare, Inc.*, 540 F.3d 533, 537–40 (7th Cir. 2008) (affirming preliminary injunction of arbitration proceeding because party did not agree to arbitrate, but not directly addressing issue of irreparable harm).

Arbitrator Was “Disinterested” Despite Involvement with First Proceeding

The court also found that Gurevitz qualified as a disinterested arbitrator even though he had served as an arbitrator in the first proceeding and had personal knowledge of what occurred in that proceeding. *Trustmark*, 631 F.3d at 873. The court explained that, unlike juries, which are expected to have little or no knowledge of the facts at the outset of trial, arbitrators are often selected precisely because of their knowledge of the underlying facts. The court further found that “disinterested” in the arbitration context means “lacking a financial or other personal stake in the outcome.” It has nothing to do with the arbitrator’s knowledge of the underlying facts or prior involvement in related arbitration proceedings. To that end, the court observed that federal judges frequently hear multiple cases that involve the same issues or that require them to take into account prior, related proceedings between the parties. These judges are nonetheless disinterested in the proceedings.

Arbitration Panel Had Authority to Interpret Confidentiality Agreement

The court also addressed the arbitration panel’s authority to rule on whether the confidentiality agreement in the first proceeding prevented the panel from hearing evidence about that proceeding. *Id.* at 874. The court held that it was the panel’s responsibility to interpret the confidentiality agreement and its impact on what evidence could be heard in the arbitration proceeding. The panel’s authority to interpret the confidentiality agreement arose from its authority to decide issues collateral to the parties’ agreement to arbitrate their reinsurance disputes, which, in this particular instance, required the panel to decide what evidence was admissible in light of the prior confidentiality agreement. The panel’s decision regarding the impact of the confidentiality agreement could be challenged only after the conclusion of the arbitration proceeding, and, even then, the panel’s ruling could be reversed only if the panel grossly erred in interpreting the agreement.

Keywords: seventh circuit, confidentiality agreement, arbitrator authority, subsequent proceeding

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Discovery Subpoenas in Arbitration—Due Care Required

By David T. Lopez

The use of subpoenas for discovery in arbitration cases can be subject to significant obstacles, particularly when the discovery is directed at third parties. Practitioners must take care to consider the underlying statutory authority for the subpoenas, including the authority for effectively serving them on the potential respondents.

Generally, rules of arbitral organizations for both domestic and international arbitrations make provisions for obtaining discovery from parties, but they do not address how discovery might be compelled from nonparties.

Procedure Provided by Statutes

The Federal Arbitration Act (FAA), 9 U.S.C. § 7, provides arbitrators the authority, enforceable by a U.S. district court, to compel appearance and testimony of individuals before one or more arbitrators and to compel production at that time of any documents that might be material to the case. Recourse to the provisions of 28 U.S.C. § 1782 might be utilized to obtain aid in discovery of evidence found within the United States for use in international arbitration.

The 50 states and the District of Columbia all have enacted statutes providing for and regulating arbitration proceedings within their jurisdictions. Those statutes mostly follow the discovery provisions in the model laws, the Uniform Arbitration Act of 1956, or the Uniform Arbitration Act of 2000, also referred to as the Revised Uniform Arbitration Act. The state statutes provide the authority and means of service of subpoenas for depositions and the production of documents.

Before Drafting an Arbitration Agreement

Because arbitration is intended to provide more expedient resolution and increasing attention is directed at simplifying, limiting, or even eliminating discovery, reference to the applicable statutory provisions must be made even before the parties enter into an agreement providing for arbitration. If a party considers the need for discovery from a source other than a party to the arbitration to be significantly material, or even essential, a determination must be made of whether such discovery will be possible in arbitration, and if not, whether the risk of not having discovery might counsel reconsidering arbitration.

The text of the FAA clearly gives arbitrators the power to subpoena a witness to appear at a hearing before a single arbitrator, panel, or member of a panel, and, if appropriate, to produce documents at the hearing. Federal circuit courts are split on whether such power extends to the



authorization of subpoenas compelling testimony or production other than before one or more arbitrators.

Split among the Circuits

The Circuit Courts of Appeal for the Sixth and Eighth Circuits have held that even though the FAA does not explicitly grant authority to subpoena discovery to a party outside the presence of an arbitrator, the efficiency of the arbitral process is furthered by implicitly finding such authority in the statute. *Am. Fed. of TV & Radio Artists v. WJBK-TV*, 164 F.3d 1004 (6th Cir. 1999); *In Re Sec. Life Ins. Co. of Am.*, 228 F.3d 865 (8th Cir. 2000). Their reasoning has been adopted by some trial courts, for example, *Festus & Helen Stacy Foundation v. Merrill Lynch*, 432 F. Supp. 2d 1375 (N.D. Ga. 2006); *Rogers v. Davidson Homes*, No. B199193 (Cal. Ct. App. 2d Dist. June 30, 2008) (unpublished).

The Second and Third Circuits have concluded to the contrary, relying on a strict textual reading of the statute. *Life Receivables Trust v. Syndicate 102*, 549 F.3d 210 (2d Cir. 2008); *Hay Group, Inc. v. E.B.S. Acquisition Corp.*, 360 F.3d 404 (3d Cir. 2004). Following *Hay Group*, a district court in New York held that the internal rules of the Financial Industry Regulatory Authority (FINRA) could not expand the specific FAA authority to permit discovery from a nonparty. *In Re Proshare Trust Secs. Litig. v. Proshare Trust*, No. 09 Civ. 6935 (S.D.N.Y. Dec. 1, 2010). In *Kennedy v. American Express Travel Related Services*, 646 F. Supp. 2d 1342 (S.D. Fla. 2009), the court cited favorably to what it characterized as an excellent analysis in *Hay Group* and also distinguished the provisions of the FAA from the more generous Rule 45 of the Federal Rules of Civil Procedure.

A middle course has been taken by the Fourth Circuit, holding that a nonparty may be compelled to give prehearing discovery if there is a showing of a special need or hardship. *COMSAT Corp. v. Nat'l Sci. Found.*, 190 F.3d 269 (4th Cir. 1999).

The disparate views of the federal courts strongly suggest that a party seeking to rely on state statutory provisions must not only carefully refer to case law but also determine whether the state provisions or the FAA will apply.

Obtaining Service May Be a Problem

Another potentially serious problem to consider is whether a subpoena issued by arbitrators can be served. Section 7 of the FAA provides that once issued by an arbitrator or panel, a subpoena is to be served in the same manner as if it were issued by a federal court. Accordingly, the provisions of Rule 45 have been held to apply both as to the manner of service and the manner of enforcement of an arbitral subpoena. In *Dynegy Mainstream Services v. Trammochem*, 451 F.3d 89, 94 (2d Cir. 2006), the federal appellate court held that procedures under Rule 7 do not contemplate nationwide service of process or enforcement. Each is subject to specific territorial limitations.



In accordance with Rule 45(b)(2), the subpoena may be served within the federal district in which the arbitrator or panel is sitting, outside the district but within 100 miles of the site for deposition or production, within the state of the arbitration if a state statute or court rule allows service at that location of a subpoena issued by a state court of general jurisdiction sitting at the site of the arbitration, or otherwise as a federal statute might provide. The manner and requisite of service is specified in the rule.

A possible alternative to a territorial problem of service is suggested in *Alliance Healthcare Services v. Argonaut Private Equity*, No. 11-C-3275, 2011 U.S. Dist. LEXIS 87808 (N.D. Ill. Aug. 9, 2011). If records sought are beyond the territorial limitation, but the entity that controls the records is within the subpoena area, the court held Rule 45 permits the entity to be made subject to a subpoena to produce the records, regardless of where the records are located.

Nonparty Discovery in International Arbitration

Provisions for assistance to tribunals in international arbitration and for service of subpoenas in a foreign country of a national or resident of the United States are made in 28 U.S.C. §§ 1782 and 1783.

In *Intel Corp. v. Advanced Micro Devices, Inc.*, 542 U.S. 241 (2004), the U.S. Supreme Court identified factors to be considered by a federal court in the application of § 1782, including whether the information is sought from a nonparty. Following *Intel*, federal courts began to allow discovery by subpoenas issued by international commercial arbitrators, which previously generally had been denied upon a narrow application of the term “tribunal.” The matter appears to be unsettled, at least in some jurisdictions. The U.S. Court of Appeals for the Fifth Circuit applied as precedent the opinion in *Republic of Kazakhstan v. Biedermann International*, 168 F.3d 880 (5th Cir. 1999), to hold that § 1782 does not apply to discovery for use in international arbitration. *El Paso Corp. v. La Comision Ejecutiva Hidroelectrica del Rio Lempa*, No. 08-20771 (5th Cir. Aug. 6, 2009) (unpublished). *Cf. Ecuadorian Plaintiffs v. Chevron Corp.*, 619 F.3d 373 (5th Cir. 2010). (If requisites set in *Kazakhstan* are met, § 1782 may be applied.)

For a more comprehensive discussion of third-party discovery in international arbitration, see Charles Owen Verrill, “Discovery from Non-Parties in International Arbitration,” 76 *Arbitration* 113–124 (2010).

Keywords: subpoena, arbitration, discovery, international arbitration

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When Is Arbitration a Tribunal under 28 U.S.C. § 1782?

By Jonathan Straw

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Persons with interests in foreign or international tribunals are not solely at the mercy of the foreign proceeding's discovery devices. Generally, 28 U.S.C. § 1782 provides a discovery mechanism for use by persons with interests in foreign or international tribunals.

This article will discuss the statutory requirements and renewed interest among the district courts in § 1782 because it was most recently interpreted by the Supreme Court in 2004. Thereafter, this article will discuss the application of § 1782 in arbitration matters by highlighting the differences among various district court opinions, particularly in the Second and Fifth Circuits' disagreement over whether and to what extent § 1782 applies to private arbitrations.

Statutory Background

Under 28 U.S.C. § 1782(a), “[t]he district court of the district in which a person resides or is found may order him to give his testimony or statement or to produce a document or other thing for use in a proceeding in a foreign or international tribunal, including criminal investigations conducted before formal accusation.” Such discovery is typically sought “upon the application of any interested person” and usually produced “in accordance with the Federal Rules of Civil Procedure.” *Id.*

Section 1782 has existed in its form pertinent to this article since 1964. From 1964 to 2004, the district courts applying § 1782 almost uniformly held that it did not apply in arbitration matters. However, after the Supreme Court's decision in *Intel Corp. v. Advanced Micro Devices, Inc.*, 542 U.S. 241 (2004), the district courts have frequently granted § 1782 requests for arbitration matters and even for private arbitrations. *See, e.g., In re Application of Chevron Corp.*, 709 F. Supp. 2d 2834 (S.D.N.Y. 2010), *aff'd on other grounds*, 629 F.3d 297 (2d Cir. 2011) (litigation and related arbitration under the rules of the United Nations Commission on International Trade Law (UNCITRAL)); *Chevron Corp. v. Shefftz*, 2010 WL 4985663 (D. Mass. Dec. 7, 2010) (international arbitration under UNCITRAL rules); *OJSC Ukrnafta v. Carpaty Petroleum Corp.*, 2009 WL 2877156 (D. Conn. Aug. 27, 2009) (private arbitration under UNCITRAL rules); *In re Babcock Borsig AG*, 583 F. Supp. 2d 233 (D. Mass. 2008) (private arbitration under International Chamber of Commerce rules); *but see El Paso Corp. v. La Comision Ejecutiva Hidroelectrica del Rio Lempa*, 341 F. App'x 31 (5th Cir. 2009) (§ 1782 did not apply to private arbitration conducted under UNCITRAL rules).

The Supreme Court's Interpretation in *Intel v. AMD*

The Supreme Court's 2004 opinion in *Intel v. AMD* spawned this flurry of activity. In *Intel*, Advanced Micro Devices, Inc. (AMD) filed an antitrust complaint against Intel Corporation with the directorate-general for competition of the Commission of the European Communities. 542 U.S. at 246. Seeking discovery, AMD filed a § 1782 application in the U.S. District Court for the Northern District of California. In the majority opinion by Justice Ginsburg, with only Justice Breyer dissenting, the Court affirmed the Ninth Circuit's reversal of the district court's denial of AMD's § 1782 application. The Court held that (1) an “interested person” need not be a party, private litigant, or sovereign agent; (2) a “proceeding” before a “tribunal” need not be pending or

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imminent; and (3) there is no requirement of foreign discoverability (i.e., that the discovery sought by a § 1782 request must also be discoverable by the procedures of the foreign tribunal). *Id.* at 253.

In applying the statutory elements, the Court found that § 1782 authorizes, but does not require, that a district court order such discovery. *Id.* at 247. Accordingly, the Court established a set of factors for district courts to apply in exercising their discretion to decide § 1782 discovery requests. *Id.* at 264–65. On remand, the district court applied the factors, finding they weighed against granting AMD’s § 1782 request. *Advanced Micro Devices, Inc. v. Intel Corp.*, 2004 U.S. Dist. LEXIS 21437, at *4–8 (N.D. Cal. Oct. 1, 2004). The factors, however, are not discussed here because they are not pertinent to the circuit split at issue in this article. Rather, the Second and Fifth Circuits are split over whether the statutory requirement of a “foreign or international tribunal” includes an arbitration matter.

In *Intel*, when the Court discussed the tribunal requirement of § 1782, the Court’s dicta fueled a new split between the federal circuits in deciding whether a tribunal includes an arbitration. The language at issue appears in that portion of the Court’s opinion when considering “whether the assistance in obtaining documents here sought by an ‘interested person’ meets the specification ‘for use in a foreign or international tribunal.’” *Intel*, 542 U.S. at 257 (quoting 28 U.S.C. § 1782(a)).

The Court referenced the congressional charge to the 1958 Commission on International Rules of Judicial Procedure (Rules Commission) “to recommend procedural revisions ‘for the rendering of assistance to foreign courts and quasi-judicial agencies.’” *Id.* at 257–58 (citing Act of Oct. 3, 1964, Pub. L. No. 88-619, § 9, 78 Stat. 997) (emphasis added by the Court). In 1964, the Rules Commission responded to the congressional charge by recommending a change from § 1782’s prior language of “any judicial proceeding” to “tribunal,” thus broadening § 1782’s application. *Id.* at 258. The Court also quoted a law review article defining the term “tribunal” as “includ[ing] investigating magistrates, administrative and arbitral tribunals, and quasi-judicial agencies, as well as conventional civil, commercial, criminal, and administrative courts.” *Id.* at 258 (quoting Hans Smit, “International Litigation under the United States Code,” 65 *Colum. L. Rev.* 1015, 1026–27, nn.71 & 73) (emphasis added). The Court reasoned that the commission was a tribunal “to the extent that it acts as a first-instance decision maker,” in a “proceeding that leads to a dispositive ruling.” *Id.* at 255, 258.

The Second and Fifth Circuits Disagree

The Second Circuit has since held that this portion of *Intel*—the quotations from the law review article and the Rules Commission revisions in 1964 from “any judicial proceeding” to “tribunal”—made § 1782 applicable to international arbitrations. *In re Application of Chevron Corp.*, 709 F. Supp. 2d 2834 (S.D.N.Y. 2010), *aff’d on other grounds*, 629 F.3d 297 (2d Cir. 2011). However, *Intel* involved an antitrust complaint and not an arbitration. It is primarily on this fact that the Fifth Circuit found that *Intel* did not overrule its own circuit’s precedent. *El*



Paso Corp. v. La Comision Ejecutiva Hidroelectrica del Rio Lempa, 341 F. App'x 31, 34 (5th Cir. 2009).

After *Intel*, the Fifth Circuit held in *El Paso* that a private Swiss arbitration conducted pursuant to a private agreement under the UNCITRAL rules was not a “tribunal” under § 1782. 341 F. App'x at 34. The Fifth Circuit found it was bound by its own precedent in *Republic of Kazakhstan v. Biedermann International*, 168 F.3d 880 (5th Cir. 1999), because a private arbitration was not at issue in *Intel*, and for that reason, the Supreme Court’s citations to the Rules Commission and the law review article were mere dicta. 341 F. App'x at 33–34. “We cannot overrule the decision of a prior panel unless such overruling is *unequivocally* directed by controlling Supreme Court precedent.” *Id.* at 34 (italics in original). The *El Paso* court further noted that *Intel* did not consider the reasoning behind *Biedermann*, which supported the result in *El Paso*.

In *Biedermann*, the court denied a § 1782 request relative to an arbitration before the Arbitration Institute of the Stockholm Chamber of Commerce (AISCC). Like the *Intel* court, the *Biedermann* court also reviewed the congressional intent, finding that “[t]here is no contemporaneous evidence that Congress contemplated extending § 1782 to the then-novel arena of international commercial arbitration.” 168 F.3d at 882. The *Biedermann* court also noted that interpreting “tribunal” to include arbitration could create a broader discovery scope than that provided under the Federal Arbitration Act. *Id.* at 883. “It is not likely that Congress would have chosen to authorize federal courts to assure broader discovery in aid of foreign private arbitration than is afforded its domestic dispute-resolution counterpart.” *Id.* Further, the *Biedermann* court reasoned that permitting such a broad range of discovery under § 1782 in an arbitration matter would be counterproductive to the efficiency of arbitration as a “speedy, economical, and effective means of dispute resolution” without the encumbrances of protracted discovery. Ironically, *Biedermann* relied on the Second Circuit’s opinion in *National Broadcasting Co. v. Bear Stearns & Co.*, 165 F.3d 184 (2d Cir. 1999), which had previously held that § 1782 did not apply to private international arbitrations.

Since 2004 when *Intel* was decided, however, the Second Circuit has uniformly held that § 1782 applies to private international arbitrations. Most Second Circuit cases, however, have involved arbitrations pursuant to UNCITRAL. The District Court for the District of Connecticut has further compared arbitrations pursuant to UNCITRAL versus arbitrations by private agreement with no governmental involvement. It is on this point that the circuit split may be resolved. That is, when the arbitration is conducted pursuant to some government-endorsed agreement or the government is involved, then § 1782 applies. Conversely, when the arbitration is merely by private agreement between two private parties with no recourse for substantive judicial review, then § 1782 does not apply.

In *OJSC Ukrnafta v. Carpathy Petroleum Corp.*, the District Court for the District of Connecticut granted a § 1782 request in an arbitration before the AISCC, which was governed by

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the UNCITRAL rules. 2009 WL 2877156, at *5 (D. Conn. Aug. 27, 2009). The district court reasoned that the AISCC was a tribunal because UNCITRAL is government sanctioned and not wholly a private arbitration, the AISCC's decision was subject to judicial review, and the AISCC did not prohibit such discovery. *Id.* at *4. The court in *Carpatsky* reasoned in part that, unlike the arbitration at issue in *Biedermann*, which was also before the AISCC, the arbitration at issue in *Carpatsky* was governed by the UNCITRAL rules. *Id.*; see also *In re Application of Oxus Gold PLC*, 2006 WL 2927615, at *6 (D.N.J. Oct. 11, 2006) (holding that § 1782 applied to arbitration conducted by UNCITRAL, but noting that “international arbitral panels created exclusively by private parties . . . are not included in the statute’s meaning”). “Thus, AISCC is acting as a first-instance decision-maker,” whose decision may be subject to review and thus falls within the purview of Section 1782.” *Carpatsky*, 2009 WL 2877156, at *4 (quoting *Intel*, 542 U.S. at 258).

The *Carpatsky* court’s analysis comports with *Intel*’s findings of congressional intent “to recommend procedural revisions ‘for the rendering of assistance to foreign courts and quasi-judicial agencies.’” *Intel*, 542 U.S. at 257–58 (citing Act of Oct. 3, 1964, Pub. L. No. 88-619, § 9, 78 Stat. 997) (emphasis added by the Court). Accordingly, the *Carpatsky* court, and quite possibly the *El Paso* court, understood the fine distinction in the *Intel* opinion between any international arbitration and one that is quasi-judicial (i.e., subject to judicial review or further judicial proceedings during or after the arbitration). See *Intel*, 542 U.S. at 258.

Practitioner’s Application

For the practitioner, the differences highlighted between the Second and Fifth Circuit opinions underscore the importance of analyzing the differences between pending arbitration matters and applicable case law. First, carefully consider whether the foreign proceeding is a purely private arbitration or an arbitration governed by rules such as the UNCITRAL rules. Alternatively, the arbitration could be government sanctioned or could involve governmental review of the decision. In each of these instances, § 1782 likely applies regardless of which circuit is deciding the § 1782 application. However, if the arbitration is purely private and untainted by governmental sanction, review, or involvement, then § 1782 will not apply if a district court situated in the Fifth Circuit is deciding the § 1782 application. Further, based on the dicta in *Carpatsky*, even a district court situated in the Second Circuit may not grant the § 1782 application.

Keywords: arbitration, 1782, discovery, tribunal, foreign, circuit, split, UNCITRAL

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Ninth Circuit Departs from Fifth Circuit's Prohibition of Ex Parte Conduct by Arbitrators

By Olivia St. Clair

If an arbitration panel has ex parte communications with expert witnesses, is that grounds for vacating the award? The Ninth Circuit recently addressed this question in *United States Life v. Superior National Insurance*, 591 F.3d 1167 (9th Cir. 2010), and held that the award should not be vacated unless the ex parte activity constitutes misconduct as described in section 10(a)(3) of the Federal Arbitration Act (FAA), 9 U.S.C.A. §§ 2–16. The Ninth Circuit expressly declined to follow the broad prohibition of ex parte meetings that the Fifth Circuit articulated in *Totem Marine Tug & Barge, Inc. v. North American Towing, Inc.*, 607 F.2d 649 (5th Cir. 1979). Instead, the court held that it was bound by the Supreme Court's decision in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 552 U.S. 576 (2008), to limit grounds for vacatur to those described in section 10 of the FAA. The ex parte conduct between the panel and its appointed experts did not violate either party's rights, and so vacatur was not a proper remedy.

Section 10 of the FAA Lists Exclusive Grounds for Vacatur

In *Hall Street Associates*, the Supreme Court held that section 10 of the FAA lists the exclusive grounds for vacating an arbitration award. *Id.* at 583. Under section 10, vacating an arbitration award is appropriate if it was obtained by corruption, fraud, or misconduct. Section 10 defines misconduct as refusing to postpone the hearing where cause to postpone has been offered, refusing to hear evidence pertinent and material to the controversy, or engaging in any misbehavior that prejudices any party's rights. It also provides for vacating an award where the arbitrators exceeded their powers or acted so erroneously that their determination cannot be considered a mutual, final, and definite award on the subject matter. Any conduct that a party uses as grounds for an argument for vacatur must fit into one of these descriptions.

The cases in which federal courts have vacated arbitration awards generally involve serious misconduct. For example, in *Gulf Coast Industrial Workers Union v. Exxon Co., USA*, 70 F. 3d 847 (5th Cir. 1995), an arbitrator misled a party into believing that certain evidence had been admitted but then ruled against the party because it had failed to present evidence on the very point to which the excluded evidence was central. In *Teamsters, Chauffeurs, Warehousemen and Helpers, Local Union No. 506 v. E.D. Clapp Corp.*, 551 F. Supp. 570, 578 (N.D.N.Y. 1982), the party was not allowed to complete its presentation of evidence before the panel ended the hearing. In both cases, these actions were deemed to be misconduct that justified setting aside the arbitration award.

The Fifth Circuit Prohibits Ex Parte Conduct

Before *Hall Street Associates* explicitly made FAA section 10 the only grounds on which an award could be vacated, the Fifth Circuit vacated an award under section 10(d) because of an ex parte meeting that it believed was prejudicial to one of the parties. In *Totem Marine Tug &*

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Barge, Inc. v. North American Towing, Inc., which involved an agreement to charter a vessel, questions arose about the vessel's earnings. None of the arbitrators was sure that the earnings figure he had was correct, and all of the figures were different. After the hearings had been closed for several days, the arbitrators telephoned North American to get the correct earnings figure. The panel used that figure to calculate its award without ever notifying Totem of the phone call or allowing Totem an opportunity to provide its own position as to the vessel's earnings. *Id.* at 652. The court had no trouble finding that the panel's ex parte communication on a critical and disputed issue of damages was improper and justified setting aside the award.

The Ninth Circuit Allows Ex Parte Conduct Where Rights Are Protected

In *U.S. Life*, a significantly different situation was presented. There, the arbitration panel heard evidence and arguments from both parties for 13 days. The panel described themselves as having reached a stalemate, because they had been faced with so many conflicting reports from each side's experts that they were unable to determine U.S. Life Insurance's reinsurance obligations or the quality of the claims handling that had occurred. To assist in making a decision, the panel retained two workers' compensation claims-handling experts (the reviewers), who reviewed 25 percent of the claims samples the parties had provided. The reviewers' conclusions were provided in writing to the panel and parties, and the parties were permitted to submit briefs responding to the reviewers' conclusions. After that, the parties were provided a hearing in which they could question the experts as to their qualifications (but not their conclusions). The parties also were permitted to submit post-hearing briefs to the panel.⁵⁹¹ 591 F.3d at 1171–72. Inasmuch as the parties were kept informed of all ex parte contact throughout the process and had opportunities to comment on and object to the reviewers' findings at several points in the process, the Ninth Circuit held that the parties' due process rights had been adequately respected by the arbitrators, notwithstanding their ex parte meeting with the reviewers. *Id.* at 1176–77. The court noted that nothing in the FAA explicitly prohibits such ex parte conduct, and held that, absent a showing of prejudice, there was no misconduct and no valid basis to vacate the award. U.S. Life attempted to portray the panel's ex parte meeting with the reviewers as misconduct by alleging that "by closing the meeting of the panel with reviewers, the panel refused to hear pertinent and material evidence." *Id.* at 1173. The court rejected this argument, concluding that both parties were given ample opportunity to assess the evidence and voice their concerns.

U.S. Life and *Totem Marine* would arguably have the same outcome even if the Fifth Circuit had decided to use section 10 of the FAA as an exclusive list of grounds for vacatur of arbitration awards. The panel consulted ex parte with North American and did not notify Totem of the communication or give Totem the opportunity to respond to North American's estimate of damages, which violated section 10(d) because it prejudiced Totem's rights. Limiting the grounds for vacatur to the list in section 10 of the FAA keeps arbitration quick and efficient by reducing frivolous appeals while still safeguarding the parties against arbitrator misconduct.

Keywords: ninth circuit, fifth circuit, ex parte, FAA, ex parte conduct, vacatur



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Negotiation Basics for Young Lawyers

By P. Jean Baker

Too many attorneys make the tragic mistake of relying on intuitive knowledge and skill when negotiating on behalf of a client. Not surprisingly, this approach probably accounts for the low percentage of effective attorney negotiators. In the seminal study conducted by Professor Gerald Williams, regardless of whether the attorney was a competitive games player or a cooperative problem solver, only 40 percent of the hundreds of practicing attorneys surveyed were found to be effective negotiators. One way to improve one's effectiveness as a negotiator is by enhancing one's knowledge of the basics.

Zero-Sum Contest

In zero-sum or win-lose contests, one side's gain is the other side's loss. The interests of the two sides rarely overlap. In the vast majority of negotiations, the interests of the participants must overlap if resolution is to be achieved. It is easier to achieve overlapping interests with some types of conflicts than with others.

Conflicts typically fit into one of four classifications. Low-stakes, low-relationship conflicts involve disputes with strangers over minor issues. Most misunderstandings involving friends, family, or coworkers can be characterized as low-stakes, high-relationship conflicts. High-stakes, high-relationship conflicts typically involve serious disputes with business partners. The only contests that approach zero-sum are those characterized by high-stakes, low-relationship concerns, such as litigation of a third-party auto personal-injury dispute. When relationship concerns are high, the desire by both sides to preserve the relationship may make it easier to achieve overlapping interests. Approaching high-relationship conflicts as competitive zero-sum contests can negatively impact the sustainability of the relationship.

Bargaining Style

When confronted with conflict, Thomas Kilmann discovered that individuals tend to instinctively respond in one of five ways: by avoiding, accommodating, compromising, collaborating or competing. Research has shown that the manner in which we respond to conflict has a direct impact on our ability to communicate. For example, having emotionally fled the scene, the avoider isn't able to accurately receive or transmit messages. The accommodator can easily and accurately process messages from others but struggles with expressing his or her own needs or wishes. Competitors are really good at telling others what they think or want but woefully inadequate when it comes to finding out what the other person thinks or wants. The person who favors compromise is really good at both receiving and transmitting information but solely in a

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reactive way. The collaborator is the only bargaining type that can accurately transmit and receive information in a proactive manner.

The highest chance of achieving a minimally acceptable result occurs when you are using either a collaborative or competitive approach, because both are high in assertiveness. Competitive behavior, however, can lead to impasse, because competitors, unlike collaborators, are uncooperative. The chance of a minimally acceptable result is low when one or both parties adopt avoidance, because this approach is low in both assertiveness and cooperation. Equally low chances of a minimally acceptable result occur when both parties are competing. Accommodation can result in unfavorable concessions because the accommodator is low in assertiveness but high in the need to cooperate. Professional negotiators seek to adopt an assertive, but not aggressive, approach. The degree of cooperation they display directly depends on the level of cooperation demonstrated by their opponent—referred to in the literature as the “tit for tat” approach to negotiation.

Persuading the Other Side

Persuasion is ultimately based on your ability to get the other person to listen to what you have to say. Professional negotiators understand the best way to accomplish this goal is by tailoring their communication so that it matches the communication preferences of their opponent. For example, if you want to influence the avoider, plan and present your arguments like an analyst, that is, be thorough, meticulous and accurate. The accommodator tends to be an idealist, so appeal to their high standards and values. With a competitor, project a strong and confident demeanor while focusing the discussion on the end result. The compromiser wants to have some fun while brainstorming a win-win solution with their opponent, so keep it light. Collaborators have a real need to try to create something new, so you must let them spend a sufficient amount of time weighing all the options.

Setting Goals and Expectations

It is easy to spot the novice negotiator, who is relatively unprepared concerning the facts, the law, their client’s needs, or the other side’s interests; fails to consider and discuss with their client in advance settlement options or the need for concessions; is unable or unwilling to crunch the numbers; and has high, but unrealistic, expectations.

Experienced legal negotiators seek to obtain a better—not necessarily the best—deal for their client by engaging in extensive preparation. They investigate the facts, research the law, determine their client’s needs, make assessments concerning the interests of the other side, crunch the numbers with the client while weighing settlement options and potential concessions, and set expectations that are optimistic but realistic. Having done their homework, effective negotiators know when they have a good deal on the table. This enables them to quickly make critical decisions at crunch time.



Determining the Other Party's Interests

The most effective negotiators are characterized by their listening—not their talking—skills. To determine the other party's interests, you must be able to listen carefully with an open mind no matter how inflammatory the other side's message. Your best chance of getting your opponent to talk is by appearing likable. Ask open ended, non-confrontational questions that test your understanding of the other side's perspectives and interests. Because listening involves interpretation, and communication at best can be imprecise—especially when dealing with educational, cultural, and language differences—always verify the validity of your interpretations by summarizing what you think you heard. Paying close attention to changes in tone and body language will help you to surface hidden agendas that could negatively impact the outcome of the negotiation.

Building Effective Relationships

Effective negotiators understand that they must build trust. Use of principled negotiation techniques, such as those expressed in the book *Getting to Yes*, increase one's ability to build good interpersonal relationships and influence others. Separate the people from the problem, focus on interests rather than positions, generate options for mutual gain, and link outcomes to objective criteria.

Competitive types tend to be hard on the people, which can easily lead to an impasse. Avoiders tend to be withdrawn, which can cause others to not bond well with them. Accommodators fail to generate options for mutual gain. In contrast, professional negotiators routinely adopt a cooperative style while seeking competitive objectives.

Assessing and Using Leverage

Effective use of leverage separates the novice from the experienced negotiator. Leverage provides the experienced negotiator with the ability not just to reach an agreement but also to obtain that agreement on more of their own terms. The goal is to develop sufficient leverage for your bargaining positions while creating doubts about the other side's bargaining positions.

The party with the most to lose has the least leverage, while the party with the least to lose has the most leverage. Both parties have roughly equal leverage when they both stand to lose equivalent amounts should the deal fall through. The party with zero leverage is at the mercy of the other side. Factors influencing leverage include necessity, desire, assertiveness, perceived status or authority, use of standards or norms, and timing constraints. Leverage is based on perception, so it is constantly waxing and waning. Bottom line: Use it or lose it.

Information Exchange

Effective negotiators understand that clear speaking does not guarantee clear communication. It is important to verify that the other side got the message you intended to convey. To do this, ask the other side to restate what they think they heard.



Give out information sparingly, but honestly. Always maintain a healthy skepticism, because opponents do lie. To protect yourself and your client against material misrepresentations, indicate in the settlement the material representations that you relied on. Specify that your opponent has a stated period of time to establish the validity of those representations. Should your opponent fail to provide supporting documentation within the time stated, clearly indicate that the settlement agreement will be null.

Body Language

In the United States, 80 percent of us prefer to process information visually. Recent studies have found that when there is a disconnect between a person's body language and their spoken words—such as shaking your head no while saying yes—the listener will remember the visual message. Clear body language is important. Your facial expressions can influence your counterpart's expectations, as can the tone of your voice. Effective negotiators use demonstratives and flip charts to keep the listener engaged. But as with any form of communication, always confirm with the listener that he or she got the message you intended to send.

Opening Offers

Truly gifted negotiators adopt an initial position that is exaggerated enough to allow for a series of concessions that will yield a desirable final offer from the opponent. The initial offer, however, cannot be so outlandish as to seem illegitimate from the start; in other words, open with the maximum plausible position or risk losing credibility and trust. An ideal opening offer is the highest (or lowest) number for which there is a supporting standard or argument. Justification for offers is crucial to final acceptance of the deal by the other side, so attempt to provide standards or arguments that will resonate with your opponent.

Negotiators should make the opening offer if they think they have a better understanding of the value of the negotiation than their counterparts. Research has shown that by opening first, you are able to anchor your opponent's expectations. This is especially effective if the anchor is viewed by the opponent as being reasonable.

Concessions

It has been said that concessions play a vital psychological role in negotiation. Making concessions triggers the law of reciprocity; when you make a concession, the other party will usually respond with one. Failing to respond to a concession will cause the other party to feel like you are trying to dupe or out-manuever them. If a party fails to reciprocate, you are typically dealing with a negotiator with either a competitive or avoiding bargaining style. Accommodators tend to easily make too many big concessions, which results in the other side discounting their value. Compromisers are very comfortable making concessions that seek to split the difference, but tend to make such concessions too early in the process to gain agreement. Collaborators are very effective at making and responding to concessions.



Integrity

Personal integrity is the cornerstone for long-term effectiveness as a professional negotiator. It enhances your credibility, which leads to trust and the ability to influence others. But that doesn't mean that you should expect all negotiators to behave ethically. Always do some research concerning whether your opponent has a reputation for ethical behavior, and don't let your guard down.

Obtaining Closure and Commitment

To achieve settlement, you must get agreement from your opponent. Begin by focusing on areas of agreement. Listen for the emotional content of the other side's message, for example, their fears, anger, and needs for reassurance or respect. Use active listening techniques, such as facing the person who is talking and opening your arms to indicate an open mind. Be assertive, but not aggressive. Use I and we statements instead of you statements to reduce defensiveness. Repeat key phrases or sentences exactly as the speaker has spoken them to indicate that you are listening and trying to understand. Take a time out if emotions start to get out of control.

Remember, if you force the other side into a deal that is ultimately found to be extremely unfair, chances are you will need to go to court to enforce compliance—a solution your client may find unacceptable for a number of reasons. Conversely, parties must carefully assess the potential upside and downside before rejecting a settlement proposal.

A study in the September 2008 edition of the *Journal of Empirical Legal Studies* reviewed 2,054 California civil cases. In 61.2 percent of these cases, the plaintiff failed to do better at trial, while 24.3 percent resulted in the defendant failing to do better than the lowest demand made by the plaintiff. On average, plaintiffs recovered \$43,000 less than the highest offer they rejected. In sharp contrast, defendants paid a whopping \$1,140,000 more than the plaintiffs' lowest demands.

What does this tell us? Unless the parties are so far apart that both sides are reasonably certain to obtain a better outcome by going to trial, resolution short of trial will always be a better option for one if not both of the parties.

Ideal Settlement

Commentators have described an ideal settlement as follows: It meets the legitimate interests of each party to the extent possible, it revolves the conflicting interests fairly, it is durable, it takes societal interests into account, it is efficient to implement, and it improves, or at the very least, does not damage further the relationship between the parties.

To accomplish all these goals, bring a carefully drafted settlement proposal to the negotiation on your laptop and revise it as necessary as the session progresses. Include monetary provisions as well as necessary terms and conditions established during in-depth discussions with your client. If you aren't good at number-crunching, bring someone to assist you with that task. Never rely on the other side to crunch the numbers. Never agree to a concession without first crunching the

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numbers. Never rely on the other side to keep score concerning concessions made or terms and conditions agreed to.

Conclusion

Negotiation is extensively used and badly practiced, but performance can be improved through instruction in the basics. Effective negotiators understand that negotiation is a dance that moves through four stages or steps: preparation, information exchange, opening and making concessions, and commitment and drafting the agreement. Regardless of your innate bargaining style, you can develop into a more effective negotiator if you prepare more intelligently; develop high, but principled, expectations; concentrate on listening; maintain a commitment to personal integrity; and know when to seek help.

Keywords: zero sum, bargaining, negotiation, settlement

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NEWS & DEVELOPMENTS

\$22 Million Award Vacated Due to Arbitrator's Non-Disclosures

Vacating a \$22 million JAMS arbitration award, the Texas Court of Appeals held that a purportedly neutral arbitrator with a 13-year history of social and business encounters with a party's attorney should have disclosed, at a bare minimum, the general nature of the friendship and thus permit the parties to further investigate the relationship before proceeding with the hearing. *Kariseng v. Cooke*, 286 S.W.3d 51 (Tex. App. – Dallas 2009, no pet. (Karseng I) and *Karseng v. Cooke*, ---S.W.3d---, 2011 WL 2536504 (Tex. App. – Dallas June 28, 2011, no pet. (Karseng II)).

The party-selected arbitrator had completed a disclosure form in which he generally disclosed that, in the previous five years, he had served as a neutral arbitrator and mediator with one of the attorneys for a party. Four days later, another attorney from the same firm was added as the party's lead counsel. The arbitrator did not supplement his disclosure to disclose his prior contact with the lead counsel, notwithstanding his receipt of wine, sports tickets, and expensive meals from the attorney.

The court acknowledged that there is always a competitive market for an experienced arbitrator whose livelihood depends upon reputation and skill, such that business and social relationships between arbitrators and attorneys are to be expected. At the same time, however, the court

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pointed out that disclosure of these relationships is essential to the fair and impartial nature of the arbitration process. Such disclosure, the court held, is crucial because of the enormous power, responsibility, and discretion vested in the arbitrator and the limited judicial review of the arbitrator's decisions.

Texas courts adhere to the generally accepted principle that an arbitration award should be vacated when the arbitrator shows "evident partiality." The test is an objective one and asks whether an observer would develop a reasonable impression of partiality from the facts as stated. In this case, the arbitrator's friendship with the attorney dated back to the attorney's clerkship for a district court judge while the arbitrator served as a magistrate for the same judge. Through nearly 10 years leading up to the arbitration, both the attorney and the arbitrator hosted expensive social events and private dinners for each other, and their spouses actively participated in their socializing.

Because "evident partiality" is established objectively by the nondisclosure itself rather than the subjective standard of whether partiality actually exists, arbitrators should always err in favor of disclosure. As the *Karlseng* court held, "Parties can gauge the neutrality of an arbitrator only if they have access to all the information that could reasonably affect the arbitrator's partiality."

The simple solution is for an arbitrator to disclose any facts that the parties would want to consider, and to understand that this obligation continues throughout the arbitration.

—David T. Lopez, *David T. Lopez & Assoc., Houston, TX*

Class Arbitration Is Not Considered a Class Action under CAFA

In a case concerning the application of the Class Action Fairness Act (CAFA), the Fifth Circuit ruled recently that a case that presents class claims in arbitration is not a class action. In *Williams v. Homeland Ins. Co. of New York*, ___ F.3d ___ (5th Cir., No. 11-30646, decided Sep. 19, 2011), the court held that a previous class arbitration filing did not preclude application of the local controversy exception to the CAFA.

Plaintiff filed this class action in Louisiana state court on behalf of a group of medical providers seeking redress from several insurers regarding PPO reimbursements. One of the defendants removed the case to federal court. In a remand proceeding, plaintiff alleged that the class satisfied all the elements of the CAFA exception: Two-thirds of the class members were Louisiana citizens, there was a significant Louisiana defendant, the principal alleged injuries occurred in Louisiana, and no other class actions had been filed within three years. Defendant

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Alternative Dispute Resolution

FROM THE SECTION OF LITIGATION ALTERNATIVE DISPUTE RESOLUTION COMMITTEE

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attacked each element in turn, including that a class arbitration had been commenced by a class member within the prohibited three years, applying "rules that mimic Rule 23 [on class actions]." The district court found for the plaintiff class and remanded the matter. This appeal followed.

In reaching its conclusion, the district court distinguished an arbitration, defined as a form of resolution outside of court, from a class action, a form of a lawsuit. The court of appeals agreed, relying on the definition of a class action in CAFA as any civil action filed under Rule 23 of the Federal Rules of Civil Procedure or similar state statute or procedural rule: "We hold that a class arbitration is not a class action, and consequently, a prior class arbitration does not frustrate the CAFA exception."

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ABA Section of Litigation Alternative Dispute Resolution
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