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Arbitration: The New Litigation?

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I. INTRODUCTION

Although arbitration was intended to keep disputes out of court, collateral litigation about arbitration remains an active area of litigation in American courts.[1] During the past two terms, the U.S. Supreme Court decided several arbitration cases, which included: *Vaden v. Discover Bank*,[2] *Arthur Anderson LLP v. Carlisle*,[3] *14 Penn Plaza LLC v. Pyett,* [4]*Rent-A-Center v. Jackson*,[5] *Stolt-Nielsen S.A., et al. v. AnimalFeeds International Corp.*,[6] and *Granite Rock v. Teamsters.*[7] The case law overwhelmingly demonstrates a judicial deference to arbitration. More and more types of cases are subject to binding arbitration and arbitral awards have become more and more insulated from judicial scrutiny each day.[8] Perhaps one of the best examples of this limited judicial review of arbitral awards is the 2008 U.S. Supreme Court case *Hall Street v. Mattel*,[9] in which the Court held that the exclusive grounds for vacating or modifying arbitral awards are those stated by the Federal Arbitration Act (FAA). Thus, the Court overruled the common-law grounds for judicial review of arbitral awards under the FAA. Furthermore, the Justices agreed to decide in the next term whether a class action ban in a cell phone arbitration agreement is unconscionable --one of the hottest issues in arbitration today.[10]

On the other hand, a general sense seems to be emerging among some that the arbitration tidal wave may be going too far, and a legislative movement has emerged at the federal level that promotes the so-called Arbitration Fairness Act of 2009,[11] which, if passed, would limit the use of binding arbitration in consumer, employment, franchise and civil rights disputes. In Texas, a similar bill was introduced at the 81st Regular Session of the Texas Legislature (S.B. 222). [12] The bill did not make it out of committee, however.[13]

2009 saw no shortage of changes in the area of consumer arbitration. In a surprising move, the National Arbitration Forum (NAF) —the country's largest administrator of credit card and consumer collections arbitrations— agreed to step aside from the credit card and consumer debt arbitration business.[14] This agreement came only a few days after Minnesota's Attorney General filed suit against NAF on July14, 2009 alleging consumer fraud, deceptive trade practices and false advertisement.[15] Following a U.S. Congressional Hearing[16] on consumer arbitration held on July 22, the American Arbitration Association (AAA) said that it would not initiate arbitrations to collect from consumers until new guidelines are established.[17] Soon after, JPMorgan Chase[18] and Bank of America[19] announced that they will no longer require mandatory arbitration on customers' credit card disputes. For recent developments in the area of dispute resolution, we invite you to read our legal blog ***Disputing*** at http://www.karlbayer.com/blog.

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[1] *See* Donald Philbin, *Trends in Litigating Arbitration: Using Motions to Compel Arbitration and Motions to Vacate Arbitration Awards*, 76 DEF. COUNS. J. 338 (2009) *available at* http://adrtoolbox.com/docs/Trends_in_Litigating_Arbitration.pdf; *See also* Litigating Alternative Dispute Resolution in the Fifth Circuit, 41 TEX. TECH L. REV. 739 (2009) *available at* http://adrtoolbox.com/docs/Litigating_in_the_Fifth_Circuit_2009.pdf (discussing noteworthy arbitration cases decided by the Fifth Circuit Court of Appeals).

[2] Vaden v. Discover Bank, 129 S.Ct. 1262 (2009) (federal court may look through a petition to compel arbitration to determine whether it has jurisdiction).

[3] Arthur Anderson LLP v. Carlisle, 129 S.Ct. 1896 (2009) (third party to arbitration agreement could invoke stay provision if state contract law allowed him to enforce agreement.)

[4] 14 Penn Plaza LLC v. Pyett, 129 S.Ct. 1456 (2009) (collective bargaining agreement that clearly and unmistakably required union members to arbitrate ADEA claims was enforceable as a matter of federal law).

[5] Rent-A-Center, West, Inc. v. Jackson 130 S. Ct. 2772 (2010) (holding that the issue of unconscionability was a matter for the arbitrator).

[6] Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.,130 S. Ct. 1758 (2010) (holding that arbitrators cannot impose class arbitration on a party when the arbitration agreement is silent on that issue.)

[7] Granite Rock Co. v. International Brotherhood of Teamsters, 130 S. Ct. 2847 (2010), (holding that a district court, not an arbitrator, should decide the CBA ratification date.)

[8] *See* The Honorable Royal Furgeson, *Civil Jury Trials R.I.P.? Can It Actually Happen In America?* 40 ST. MARY'S L.J. 795, 869-70 (2009).

[9] Hall Street Associates, L.L.C. v. Mattel, Inc., 128 S.Ct. 1396, 1405 (2008).

[10] Victoria VanBuren, *U.S. Supreme Court Agrees to Hear Class Arbitration Waiver Case: AT&T v. Concepcion, available at* http://www.karlbayer.com/blog/?p=9148.

[11] H.R. 1020; S. 931. In addition to the Arbitration Fairness Act, several alternative dispute resolution bills are currently pending in the U.S. Congress, *see* Victoria VanBuren, *U.S. Dispute Resolution Update*, June 23, 2009, *available at* http://www.karlbayer.com/blog/?p=2693.

[12] *See* Victoria VanBuren, *Texas Legislature Update: Alternative Dispute Resolution Bills*, June 6, 2009, *available at* http://www.karlbayer.com/blog/?p=2227.

[13] *Id.*

[14] Victoria VanBuren, *National Arbitration Forum Settles with Minnesota's Attorney General*, July 20, 2009, *available at* http://www.karlbayer.com/blog/?p=3682.

[15] The Complaint and press releases can be found at www.karlbayer.com/blog/?p=3448.

[16] Find the prepared testimony by witnesses at http://www.karlbayer.com/blog/?p=3797 and the videos of the hearing at http://www.karlbayer.com/blog/?p=4954.

[17] Find the AAA press release at http://www.karlbayer.com/blog/?p=3768.

[18] Ashby Jones, *The Revolution Rolls On: JPMorgan Chase Suspends Arbitration Activity*, July 24, 2009, The WALL STREET JOURNAL'S LAW BLOG, *available at* http://blogs.wsj.com/law/2009/07/24/the-revolution-rolls-on-jpmorgan-chase-suspends-arbitration-activity/.

[19] Dionne Searcey, *Bank of America Says 'No Mas' To Arbitration*, THE WALL STREET JOURNAL'S LAW BLOG, August 13, 2009, *available at* http://blogs.wsj.com/law/2009/08/13/bank-of-america-says-no-mas-to-arbitration/?mod=djemWEB&reflink=djemWEB&reflink=djemWLB.

Also in 2009, *Jones v. Halliburton*, an employment arbitration case coming out of the Fifth Circuit made national headlines and prompted Congress to act. In the case, the Court held that claims for (1) assault and battery; (2) intentional infliction of emotional distress; (3) negligent hiring, retention and supervision of employees involved in a sexual assault; and (4) false imprisonment were not related to the plaintiff's employment contract and refused to compel arbitration.

Despite that the plaintiff in *Halliburton* prevailed, the case prompted Congress to pass the first anti-arbitration piece of legislation in decades. In December 2009, President Barack Obama signed into law a Department of Defense spending bill that included the so-called Franken amendment, named after Minnesota Senator Al Franken.[20] The amendment bars funds to defense contractors who require workers to arbitrate "any claim under Title VII of the Civil Rights Act of 1964 or any tort related to or arising out of sexual assault or harassment, including assault and battery, intentional infliction of emotional distress, false imprisonment, or negligent hiring, supervision, or retention."[21] Trial lawyer and consumer groups hope the amendment's passage will lead to an effort to ban mandatory arbitration of civil rights claims in all private employment contracts.

In 2010, major financial reform legislation signed by President Obama also included anti-arbitration provisions.[22] The legislation gave the U.S. Securities and Exchange Commission authority to ban or limit mandatory arbitration in brokerage and investment advisory agreements.[23] The law also created a consumer financial protection agency that could restrict or prohibit mandatory arbitration for credit cards, mortgages and other financial products.[24]

This paper is not an exhaustive review on the topic of arbitration, but instead seeks to simply expose Texas litigators to some of the myriad issues at play. Accordingly, Part II outlines the issue of arbitrability, that is, whether or not a party to a dispute can force the dispute into binding arbitration. Part III discusses recent case law regarding whether a non-signatory can be bound by an arbitration agreement. Part IV examines discovery issues in arbitration proceedings. Part V outlines evidentiary rules in arbitration. Part VI addresses the enforceability of arbitral awards, that is, how one can either reduce an arbitration award to judgment or seek to have an arbitral award vacated. Finally, Part VII concludes the paper.

II. ARBITRABILITY: MOTIONS TO COMPEL ARBITRATION

Arbitrability is a term used to describe whether or not a dispute can be forced from litigation into binding, private, arbitration. It comes up chiefly in appellate opinions on *mandamus* or interlocutory appeal of trial court orders refusing to compel arbitration because a trial court order compelling arbitration is not appealable.[25] In the most common scenario, a party sues another party in a traditional court setting and the defendant asks the trial court to either abate or dismiss the case in favor of an order compelling the parties to arbitrate their dispute.

In Texas, an order to compel arbitration is most commonly requested pursuant to either the Federal Arbitration Act (FAA) or the Texas Arbitration Act (TAA).[26] The FAA allows parties to initiate independent, distinct proceedings in a federal district court solely for the purpose of asking that court to compel arbitration against a party resisting arbitration.[27] The TAA contains a similar provision.[28] The TAA also allows parties to initiate independent proceedings to stay arbitrations "commenced or threatened" so that a court has an opportunity to decide the question of arbitrability.[29] In addition, Texas also has an International Arbitration Act (TIAA), which contains some interesting and potentially useful features absent from either the TAA or FAA. International arbitration is beyond the scope of this paper, however.[30]

A. FAA or TAA: Which One Applies?

[20] H.R. 3326.
[21] H.R. 3326.
[22] *Id*.
[23] *Id*.
[24] *Id*.
[25] *See* Perry Homes v.Cull, 258 S.W.3d 580, 586 (Texas 2008).
[26] 9 U.S.C. §§1-16; TEX. CIV. PRAC. & REM. CODE §§ 171.001-098.
[27] 9 U.S.C. §4.
[28] *See* TEX. CIV. PRAC. & REM. CODE §171.024.
[29] TEX. CIV. PRAC. & REM. CODE §171.023.
[30] *See* TEX. CIV. PRAC. & REM. CODE §§ 172.001-215.

As a threshold matter, a party seeking to compel arbitration should consider whether or not the FAA or the TAA applies to their case. The first place to look in any arbitration question is the arbitration clause itself because parties are free to specify which statute will apply in an arbitration clause. If an arbitration clause is silent as to which statute applies, the clause can be said to potentially invoke both federal and state law. [31] In order to determine if the FAA can apply in a state-court proceeding, Texas courts look at the relationship between the parties and extend the FAA "to any contract affecting commerce, as far as the Commerce Clause of the United States Constitution will reach."[32]

Given the state of current Commerce Clause jurisprudence, the FAA can be said to apply to many disputes. In *Nexion*, for example, the Texas Supreme Court found the FAA to apply to a Texas medical malpractice case brought by a Texan, against Texans, in a Texas state court, for torts committed in Texas because Medicare had paid for some of the plaintiff's medical expenses.[33]

The simple fact that the FAA can be said to apply to a dispute does not deprive Texas courts of TAA jurisprudence, however. Both the TAA and the FAA can simultaneously apply to a dispute, and the FAA only preempts the TAA in cases where the TAA is inconsistent with the FAA.[34] Because the FAA is designed to be enforceable and enforced in state courts, most Texas litigants will have the ability to choose which statute they wish to apply and whether or not federal courts have jurisdiction over the claim,. Indeed, the FAA itself does not confer federal question jurisdiction. A petition under to compel arbitration under the FAA must have some independent basis for federal court jurisdiction in order to be brought in federal court.[35]

Regardless of which statute applies, court actions brought to either compel arbitration or to enforce an arbitral award are brought pursuant to either state or federal statute and may generally be brought in either state court or federal court. This has resulted in a number of opinions where Texas state courts interpret the FAA and where Texas federal courts analyze Texas state common law as it pertains to arbitral contracts.

B. Does the Court Have Jurisdiction to Hear the Dispute?

In *Vaden v. Discover Bank*, the U.S. Supreme Court weighed in on the issue of jurisdiction.[36] There, Discover Bank sued cardholder Vaden in Maryland state court to recover past due charges ($10,610.74 plus interest and attorney's fees). Discover's pleading raised only state law issues and the parties did not qualify for diversity-of-citizenship jurisdiction because the amount in controversy did not exceed $75,000. Vaden answered with the affirmative defense of usury and filed several class-action styled counterclaims. Discover responed by filing a motion to compel arbitration in federal court based on a clause in the credit card agreement providing for arbitration. The district court granted Discover's request for arbitration and Vaden appealed. The Fourth Circuit remanded the case for a determination whether the controversy presented "a properly invoked federal question." On remand, the district court held that the controversy presented a federal-question and ordered arbitration once again. The case was appealed to the Fourth Circuit for the second time and the Fourth Circuit affirmed.[37]

The U.S. Supreme Court granted certiorari and examined two questions concerning subject-matter jurisdiction over a petition under Section 4 of the FAA:

1. Whether a district court asked to compel arbitration should "look through" the petition and grant the relief if the court would have federal-question jurisdiction of the controversy. The Court held that a court **may** "look through" a Section 4 petition in order to make this determination.
2. Whether a district court should exercise jurisdiction over the petition when the petitioner's complaint rests on state law but an actual or potential counterclaim rests on federal law. Here, the Court held that a federal court

[31] *See* In re D. Wilson Constr. Co., 196 S.W.3d 774, 779 (Tex. 2006).
[32] In re: Nexion Health at Humble, Inc., 173 S.W.3d 67, 69 (Tex. 2005); *See also* Citizens Bank v. Alafabco, Inc., 539 U.S. 52, 56-57, 123 S.Ct. 2037, 156 L.Ed.2d 46 (2003) (interpreting the meaning of "commerce" within the FAA).
[33] *Nexion*, 173 S.W.3d at 69.
[34] *Wilson*, 196 S.W.3d at 779-780.
[35] *See* 9 U.S.C. §4.
[36] 129 S.Ct. 1262 (2009).
[37] *Id*.

> **may not** entertain a Section 4 petition based on the contents of a counterclaim when the entire controversy between the parties does not qualify for federal-court adjudication.[38]

The Court refused to compel arbitration because the federal court did not have jurisdiction over the entire controversy. However, the Court noted that Discover could still petition a Maryland state court to enforce the arbitration agreement.[39]

The dissent in *Vaden* argued that the "controversy" to be decided by the Court should be the subject matter of the arbitration: whether Discover Bank charged illegal finance charges, interest and late fees, which is a matter controlled by the Federal Deposit Insurance Act, rather than the complaint initially filed by Discover and based on state law. [40]

An issue barely discussed in footnote 13 of *Vaden* is worth noting. Discover first sought court adjudication of the dispute and only invoked the arbitration clause contained in the cardholders' agreement after Vaden countered with class-action allegations. Usually, it is the defendant who files to compel arbitration in an effort to avoid litigating the dispute. Courts generally find "forum-shopping" distasteful and some courts have held that a party has waived its right to arbitrate once they invoke the judicial process.[41]

C. Must a Court Compel Arbitration? The Basic Test

According to the Texas Supreme Court, "a party seeking to compel arbitration under the FAA must establish that (1) there is a valid arbitration agreement, and (2) the claims raised fall within that agreement's scope."[42] Whether or not a valid arbitration agreement exists is determined by state contract law and is a legal question determined by a trial court.[43] Once a valid agreement to arbitrate is found, the trial court, "should not deny arbitration 'unless it can be said with positive assurance that an arbitration clause is not susceptible of an interpretation which would cover the dispute at issue.'"[44] If both prongs of the arbitration question are met, the party opposing arbitration may offer any affirmative defense that would apply in any other kind of contract dispute to the arbitration clause, such as duress, unconscionability, fraudulent inducement or the like.[45]

The basic test under the TAA is more or less the same as under the FAA, and like FAA analysis, is ultimately governed by common-law concepts of Texas contract law:

> A party attempting to compel arbitration must first establish that the dispute in question falls within the scope of a valid arbitration agreement. If the other party resists arbitration, the trial court must determine whether a valid agreement to arbitrate exists. The trial court's determination of the arbitration agreement's validity is a legal question subject to de novo review. If the trial court finds a valid agreement, the burden shifts to the party opposing arbitration to raise an affirmative defense to enforcing arbitration.[46]

Under either statutory scheme, a court determines whether an agreement to arbitrate exists, whether the dispute in question is within the agreement's scope and finally, whether any affirmative defenses to arbitration have any merit.

D. Does an Agreement to Arbitrate Exist?

Numerous recent court opinions have discussed an employer's imposition of arbitration agreements on their at-will employees. The landmark case is *Halliburton*. In that case, a Brown & Root employee for thirty years named

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[38] *Id*.
[39] *Id*.
[40] *Id*.
[41] *Id*.
[42] In re Dillard Dept. Stores, Inc., 186 S.W.3d 514, 515 (Tex. 2006), quoting In re: Kellogg Brown & Root, Inc., 166 S.W.3d 732, 737 (Tex. 2005) (hereinafter "*Dillard I*", since the Texas Supreme Court actually handed down opinions on two separate *mandamus* petitions in early 2006 involving Dillard Department Store's arbitration clause).
[43] *Id.*
[44] *Id.* at 516, quoting Prudential Sec. Inc. v. Marshall, 909 S.W.2d 896, 899 (Tex. 1995).
[45] In re: FirstMerit Bank, N.A., 52 S.W.3d 749, 756 (Tex. 2001). *See also* In re Poly-America, *L.P.*, 262 S.W.3d 337 (Tex. 2008).
[46] J.M. Davidson, Inc. v. Webster, 128 S.W.3d 223, 227 (Tex. 2003) (internal citations, including to the TAA, omitted).

James Myers received a notice that his employer – now a subsidiary of Halliburton – had adopted a binding arbitration program for resolving employment disputes.[47] The notice stated that by continuing to come to work after a short time had passed, Myers would be deemed to have accepted the new program.[48] Myers kept coming to work but eventually he was demoted.[49] Myers claimed that the demotion was discrimination based on his age and race, and filed a lawsuit under the Texas Commission on Human Rights Act.[50] Halliburton asked the trial court to compel arbitration and the trial court denied the motion.[51] The Court of Appeals denied a subsequent *mandamus* petition and the Texas Supreme Court stepped in.[52]

According to Texas contract law, an at-will employer can change the terms of an at-will employment contract by providing notice of the change and proving the employee's acceptance of the change.[53] "When an employer notifies an employee of changes to the at-will employment contract and the employee 'continues working with knowledge of the changes, he has accepted the changes as a matter of law.'"[54]

In early 2006, the Texas Supreme Court re-affirmed the *Halliburton* rule in *Dillard I*, but the Court added a potential wrinkle.[55] In that case, the Court noted that "the arbitration agreement and the 2000 rules do not provide Dillard any right to unilaterally modify the agreement.[56] For that reason, and because the parties agreed to and signed the agreement, the agreement is binding on Martinez."[57] In other words, presumably not even an at-will employer can impose an arbitration agreement that gives the employer the unilateral right to change the rules or procedures governing arbitration.[58]

Several months later, the Court wrote another opinion on the same arbitration policy.[59] In *Dillard II*, the El Paso store had presented its arbitration policy to its employees at a meeting in August 2000.[60] Later, an employee named Delia Garcia sued the company for retaliatory discharge, claiming that she was fired after applying for workers' compensation insurance benefits.[61] The store offered evidence that it had given its employees notice of the policy at the meeting, but it could not produce a signed acknowledgment form for Ms. Garcia and it could not find a witness who could testify that Ms. Garcia had been at the meeting and received the forms.[62]

Ms. Garcia testified that at some point she was presented with a document about the arbitration program, but that she refused to sign it because she did not wish to be bound by mandatory arbitration.[63] According to the Supreme Court, since Ms. Garcia had clearly been given some sort of notice of the arbitration plan, she was bound to the plan by her decision to continue coming to work every day. Her refusal to sign, therefore, had no legal significance.[64]

Dillard II also, in a sideways fashion, addresses the issue of whether Dillard's right to unilaterally modify the agreement would render it illusory and thus non-binding on Ms. Garcia.[65] Dillard apparently put a new arbitration plan in place in 2002, more than a year after notifying Ms. Garcia of the first plan.[66] Since Ms. Garcia clearly did not receive notice of the changed plan, Ms. Garcia argued that Dillard obviously retained the right to modify the plan unilaterally, since it had in fact done so.[67] The Supreme Court was un-moved by this argument. In point of fact, said the Court, since Dillard never gave Ms. Garcia notice of the changed plan, it had not as a legal matter effectively

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[47] *Id.* at 568.
[48] In re Halliburton Co., 80 S.W.3d 566, 568 (Tex. 2002).
[49] *Id.*
[50] *Id.*
[51] *Id.*
[52] *Id.*
[53] *Halliburton*, 80 S.W.3d at 568.
[54] *Id.* at 568 (quoting *Hathaway v. General Mills*, 711 S.W.2d 227, 229 (Tex. 1986)).
[55] *See* Dillard I, 186 S.W.3d 514
[56] *Id*.
[57] *Dillard I*, 186 S.W.3d at 516.
[58] *See also Davidson*, 128 S.W.3d at 228-29 (discussing the clause: "[t]he Company reserves the right to unilaterally abolish or modify any personnel policy without prior notice.").
[59] *See* In re Dillard Department Stores, Inc., 198 S.W.3d 778 (Tex. 2006) (hereinafter *Dillard II*).
[60] *Id.* at 780.
[61] *Id.*
[62] *Id.*
[63] *Dilllard II*, 198 S.W.3d 778 at 781.
[64] *Id.* at 781.
[65] *See Dilllard II*, 198 S.W.3d 778.
[66] *Id.* at 781-82.
[67] *Id.* at 782.

changed the plan, since notice is required to change an at-will employment arrangement.[68] Therefore, Dillard did not unilaterally modify the plan, since an at-will employer cannot modify an at-will arrangement without providing notice and an opportunity for the employee to reject the change by quitting.

In June 2006, the Texas Supreme Court ruled that "notice" under the *Halliburton* analysis does not actually require that an employee receive a copy of the arbitration agreement itself.[69] In the case, an employee received a "Summary Plan Description of Agreement to Arbitrate Claims" that described the plan, which "constitutes effective notice because it unequivocally provided [employee] with knowledge of the arbitration agreement."[70] Although the employee testified that he never received the plan itself, he had signed the summary description.[71]

E. Is the Dispute Within the Scope of the Arbitration Clause?

Once the existence of an agreement to arbitrate is established, a court must compel arbitration if the dispute falls within the scope of the arbitration clause. Generally, Texas courts perform less analysis on the scope question than the existence question, largely because both state and federal courts in Texas employ a legal test designed to be expansively inclusive, and most arbitration clauses are worded broadly enough to encompass more or less any claim that might be conceived of between parties to an arbitration agreement.

In evaluating whether a claim is within the scope of an arbitration clause, "a court should not deny arbitration 'unless it can be said with positive assurance that an arbitration clause is not susceptible of an interpretation which would cover the dispute at issue."[72] In *Dillard I*, an ex-employee sued Dillard for defamation. Dillard sought arbitration based on language in its arbitration clause covering claims for "personal injuries arising from a termination, except those covered by workers' compensation."[73] According to the Supreme Court, since a reasonable interpretation of "personal injuries" includes injuries to reputation, the defamation claims were arbitrable.[74]

The former employee further argued that since her claim was based on defamatory comments, and not her actual termination, the claim did not "arise from a termination."[75] The Court ruled that since the comments were made "near the time of her termination," "any damage in this case could be viewed as intertwined with her employment and termination, and any ambiguity as to whether 'arising from' should mean intertwined, or occurring as a direct result from, is resolved in favor of arbitration."[76]

Within such a context, the scope prong of arbitrability analysis ought not to be a difficult hurdle for a party seeking to compel arbitration to overcome.

F. Who Decides: a Court or the Arbitrator?

Recently, the U.S. Supreme Court handed down three cases dealing with the discretion of an arbitral tribunal. First, the Court held in *Stolt-Nielsen S.A. v Animalfeeds International Corp*., that under the FAA, "[A] party may not be compelled . . . to submit to class arbitration unless there is a contractual basis for concluding that the party agreed to do so." [77]

The majority in *Stolt-Nielsen* departed from *Green Tree Financial Corp. v. Bazzle*, an earlier decision regarding class arbitration.[78] In *Bezzle*, the Court had resolved the question of whether the parties' agreement authorized class arbitration to be one of a procedural nature for the arbitral tribunal to resolve.[79] In *Stolt-Nielsen*, however, the majority emphasized that the plurality opinion in *Bazzle* neither settled "for the Court" the question of "who should

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[68] *Id.*
[69] In re Dallas Peterbilt, Ltd., L.L.P., 196 S.W.3d 161, 162-63 (Tex. 2006).
[70] *Id.* at 163.
[71] *Id.* at 162.
[72] *Dillard I*, 186 S.W.3d at 516, citing *Prudential Sec. Inc. v. Marshall*, 909 S.W.2d 896, 899 (Tex. 1995), quoting *Neal v. Hardee's Food Sys., Inc.*, 918 F.2d 34, 37 (5th Cir. 1990); *See also Kellogg*, 166 S.W.3d at 737; *Wilson*, 196 S.W.3d at 782-83.
[73] *Id.*
[74] *Id.*
[75] *Id.*
[76] *Id.*
[77] Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.,130 S. Ct. 1758 (2010).
[78] Green Tree Financial Corp. v. Bazzle, 539 U.S. 444 (2003).
[79] *Id*. at 452-53.

decide" whether class action is authorized under a contract, nor provided the standard for resolving the underlying issue.[80]

In *Stolt-Nielsen,* the Court placed a significant substantive limitation upon the discretion that would ordinarily be enjoyed by any arbitral tribunal. This decision will likely heighten considerably the hurdle to be cleared before class arbitration procedures are upheld under the FAA.[81]

The second case was *Rent-A-Center, West v. Jackson.* [82] There, Antonio Jackson sued his employer for race discrimination and retaliation. The trial court granted the employer's motion to dismiss and to compel arbitration according to an agreement in Jackson's employment contract. Jackson appealed, arguing the arbitration agreement was procedurally and substantively unconscionable and that the issue of unconscionability must be decided by a court, not the arbitrator. The Court of Appeals for the Ninth Circuit held that the threshold issue of unconscionability is for a court to decide even if the agreement assigns that issue to the arbitrator.[83]

The U.S. Supreme Court reversed the Ninth Circuit and concluded that the getaway question of unconscionability was for the arbitrator to decide. The Court held when an agreement delegates the authority to determine the arbitrability of the agreement to an arbitrator, claims which challenge the enforceability and validity of an agreement as a whole will be determined by the arbitrator, while claims which specifically challenge the enforcement of the delegation provision will be considered by a district court.[84]

Because most challenges to the enforceability or validity of an agreement will apply to the entire agreement rather than to the specific arbitration provision, the *Rent-A-Center* decision will likely limit the number of challenges to arbitration agreements which include a delegation clause heard in the courts. As a result, more cases will be decided by arbitrators than the courts.[85]

Finally, the U.S. Supreme decided *Granite Rock v. Teamsters*. In *Granite,* the responder is a local union (Local) supported by its parent international (IBT). The petitioner is Granite Rock (Granite), the employer of some of Local's members. The case is about Granite's claims against Local and IBT for economic damages arising out of a strike. In the case, the parties had reached a collective bargaining agreement (CBA), but disagreed about the date it was formed and who should decide that question. Granite contended that the agreement was ratified on July 2 (containing non-strike and arbitration clauses) while Local argued that it was formed on August 22.[86]

The Court held that a district court, not an arbitrator, should decide the CBA ratification date. The Court noted that "[t]he CBA requires arbitration of disputes that 'arise under' the agreement. The parties' ratification-date dispute does not clearly fit that description."[87]

G. Personal Injury Cases

As stated above, the FAA and the TAA can co-exist peacefully with the FAA will only pre-empting the TAA when they differ. The most common example of this happens in personal injury cases. The Texas Arbitration Act requires that an agreement to arbitrate a personal injury case is only enforceable under the TAA if each party and each party's attorney sign the agreement.[88] In other words, pre-injury arbitration agreements are not valid in personal injury cases since personal injury clients typically do not retain counsel before they become injured. Therefore, in a Texas personal injury case, one can generally disprove the existence of a valid agreement to arbitrate because the injured plaintiff's lawyer did not sign the agreement.

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[80] *Stolt-Nielsen* at 15-16.
[81] *Id*.
[82] Rent-A-Center, West, Inc. v. Jackson 130 S. Ct. 2772 (2010).
[83] *Id*.
[84] *Id*.
[85] *Id*.
[86] *Id*.
[87] *Id*.
[88] TEX. CIV. PRAC. & REM. CODE §171.002(a)(3) and (c).

The FAA has no such requirement. In a personal injury case governed by the FAA, the FAA's silence on this point preempts the TAA's attorney-signature requirement and the default rules described above apply.[89] In other words, although it usually does not matter whether the FAA or the TAA applies, **in personal injury cases the FAA/TAA determination is critical and case determinative on the issue of arbitrability.**

Jones v. Halliburton Co. is a recent case with tragic facts which made national headlines, including a story by the National Public Radio (NPR).[90] In the case, the Fifth Circuit held that claims for (1) assault and battery; (2) intentional infliction of emotional distress; (3) negligent hiring, retention and supervision of employees involved in a sexual assault; and (4) false imprisonment are not related to the plaintiff's employment contract and refused to compel arbitration.[91]

In 2004, at the age of 19, Jamie Leigh Jones began working as an administrative assistant for Halliburton Company/Kellogg Brown & Root (Halliburton/KBR) in Houston, Texas.[92] On July 21 2005, Jones signed an employment contract with a subsidiary of Halliburton/KBR to work in Baghdad, Iraq that included the following clause:

> You . . . agree that you will be bound by and accept as a condition of your employment the terms of the Halliburton Dispute Resolution Program which are herein incorporated by reference. You understand that the Dispute Resolution Program requires, as its last step, that any and all claims that you might have against Employer **related to your employment**, including your termination, and any and all **personal injury claim[s] arising in the workplace**, you have against other parent or affiliate of Employer, must be submitted to binding arbitration instead of to the court system. (Emphasis added.) [93]

The incorporated Dispute Resolution Program, provides:

> "Dispute" means all legal and equitable claims, demands, and controversies, of whatever nature or kind, whether in contract, tort, under statute or regulation, or some other law, between persons bound by the Plan or by an agreement to resolve Disputes under the Plan . . . including, but not limited to, any matters with respect to . . . any **personal injury allegedly incurred in or about a Company workplace**. (Emphasis added.) [94]

Jones arrived in Baghdad on July 25, 2005.[95] Halliburton/KBR provided Jones with housing in a barracks (where the ratio of men to women was 20 to one) as a term of her employment contract.[96] On July 27, 2005 Jones complained of sexual harassment by co-workers and requested to be moved to a different housing location.[97] Jones alleges that no action was taken, and her managers told her to "go to the spa."[98]

Jones alleges that on July 28, 2005, she was drugged, beaten and gang-raped in her barracks bedroom by several Halliburton/KBR employees after a social function.[99] Jones reported the incident promptly. After her rape-kit was administered, Jones alleges that she was placed under armed guard in a container and not permitted to leave or call her family.[100] She further alleges that Halliburton/KBR human resources interrogated her for several hours and gave her two options: to stay and "get over it," or to return to the U.S. without "guarantee" of a job.[101] In the end, Jones' father was able to get the help of a Congressman to secure his daughter's return to the United States. [102] As a result of

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[89] *See Nexion*, 173 S.W.3d at 69; *See also* In re AdvancePCS Health L.P., 172 S.W.3d 603, 606 (Tex. 2005) (explaining that the FAA does not require that arbitration clauses be signed and the TAA's requirement did not apply to the case); In re Weekley Homes, 180 S.W.3d 127, 130 n.4 (Tex. 2005)(holding that the FAA preempts any state requirements that apply only to arbitration clauses.).

[90] Jones v. Halliburton, No. 08-20380, 2009 U.S. App. LEXIS 20543 (5th Cir. Tex. Sept. 15, 2009); *See* Wade Goodwyn, *Rape Case Highlights Arbitration Debate*, National Public Radio, Sept. 23, 2009, available at http://www.npr.org/templates/story/story.php?storyId=105153315.

[91] *Jones v. Halliburton*, at *36.

[92] *Id*. at *2-*3.

[93] *Id*. at *3.

[94] *Id*.

[95] *Id*. at *4.

[96] *Id*. at *4-*5.

[97] *Id*. at *5.

[98] *Id*.

[99] *Id*. at *6.

[100] *Id*.

[101] *Id*.

[102] *Id*.

the alleged incident, Jones received several serious injuries which later required reconstructive surgery.[103] Upon arrival to the U.S., Jones filed a complaint with the Equal Employment Opportunity Commission.[104] The agency conducted an investigation and concluded that: Jones "had been sexually assaulted by one or more employees; physical trauma was apparent; and that Halliburton/KBR's investigation had been inadequate."[105]

In February 2006, Jones filed a request for arbitration against Halliburton/KBR.[106] While the arbitration was pending, Jones obtained new counsel and filed a lawsuit claiming negligence, negligent undertaking, sexual harassment and hostile working environment under Title VII, and retaliation, false imprisonment, breach of contract, fraud in the inducement to enter the employment contract, fraud in the inducement to enter the arbitration agreement, assault and battery and intentional infliction of emotional distress.[107]

In November, 2007, Halliburton/KBR moved to compel arbitration pursuant to the employment contract.[108] On May 9, 2008, the district court refused to compel arbitration of Jones' claims for: (1) assault and battery; (2) intentional infliction of emotional distress arising out of an alleged assault; (3) negligent hiring, retention and supervision of employees involved in the assault; and (4) false imprisonment.[109] The district court concluded that those claims fell outside of the scope of the arbitration provision because they were **not related to Jones' employment** and were beyond the outer limits of even a broad arbitration provision.[110] The Court stayed litigation of those claims until the parties completed arbitration of the rest of the claims found arbitrable by the Court, however.[111] In June 2008, Halliburton/KBR appealed.[112]

The Fifth Circuit stated that the issue before the Court was whether the alleged rape fell within the scope of the arbitration agreement.[113] First, the Court rejected Jones' argument that the public policy of the Texas Arbitration Act (TAA) governed the scope of the arbitration provision.[114] Under the TAA, agreements to arbitrate personal injury claims must be signed by each party's lawyer.[115] The Court concluded that to the extent that the TAA affected the enforceability of the agreement, the Federal Arbitration Act preempted it.[116] Next, the Court reviewed the case law split regarding similar arbitration clauses and claims premised on sexual assault.[117] The Court explained that a liberal construction of "scope of employment" for purposes of workers' compensation was not necessarily the same standard to be applied when construing a similar arbitration provision.[118]

Finally, the Fifth Circuit agreed with the district court and concluded that although the arbitration provision extended to personal-injury claims "arising in the workplace," the Court "d[id] not believe [Jones'] bedroom should be considered the workplace, even though her housing was provided by her employer."[119] The Court also cautioned that its analysis was fact-specific.[120]

H. Does any Affirmative Ground Exist with which to Oppose Arbitration?

"As a matter of federal law, arbitration agreements and clauses are to be enforced unless they are invalid under principles of state law that govern all contracts. Therefore, 'generally applicable contract defenses, such as fraud, duress, or unconscionability may be applied to invalidate arbitration agreements without contravening §2 [of the

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[103] *Id*. at *5-*6.
[104] *Id*. at *6-*7.
[105] *Id*. at *7
[106] *Id*.
[107] *Id*. at *8-*9.
[108] *Id*.
[109] *Id*.
[110] *Id*. at *9.
[111] *Id*. at *9-*10.
[112] *Id*. at *11.
[113] *Id*. at *13.
[114] *Id*..
[115] *Id.* The Texas Arbitration Act requires that an agreement to arbitrate a personal injury case is only enforceable under the TAA if each party and each party's attorney signs it. *See* TEX. CIV. PRAC. & REM. CODE §171.002(a)(3) and (c). In other words, pre-injury arbitration agreements will not be valid in personal injury cases, since personal injury clients typically do not retain counsel before they get hurt. Therefore, in a Texas personal injury case, one can disprove the existence of a valid agreement to arbitrate if the injured plaintiff's lawyer did not sign the agreement.
[116] *Id*. at *14-*15.
[117] *Id*. at *15-*27.
[118] *Id*. at *28-30.
[119] *Id*. at *10-*11.
[120] *Id*. at *30.

FAA]."[121] In other words, even if a party seeking to compel arbitration makes a showing as to arbitrability, a resisting party can assert a variety of affirmative defenses.

1. The Defense must be Specific to the Arbitration Clause, and Not to the Contract as a Whole

While a party opposing arbitration may offer any affirmative defense normally available in contract cases, the party must take care to assert defenses only as they apply specifically to the arbitration clause and not to the contract as a whole. A February 2006 U.S. Supreme Court case made it clear that any challenge to the entire contract's enforceability must be decided by an arbitrator, not by a trial court at the motion to compel arbitration stage.[122] That case involved a contract which the Florida Supreme Court had found criminally usurious, but which contained an arbitration clause.[123] The Florida court found that enforcing an arbitration clause in a usurious contract "could breathe life into a contract that not only violates state law, but also is criminal in nature."[124] Maybe so, said the U.S. Supreme Court, but the determination is one for an arbitrator because the affirmative defense of illegality would have applied to the contract as a whole and not specifically to the arbitration clause.[125]

2. Unconscionability

The most common affirmative defense raised to an arbitration clause is unconscionability. "Under Texas law, unconscionability includes two aspects: (1) procedural unconscionability, which refers to the circumstances surrounding the adoption of the arbitration provision, and (2) substantive unconscionability, which refers to the arbitration provision itself."[126] Although there was previous confusion on the issue, the *Halliburton* Court clarified that courts, rather than arbitrators, may consider both procedural and substantive unconscionability challenges to arbitration.[127]

"[T]he basic test for unconsionability is whether, given the parties' general commercial background and the commercial needs of the particular trade or case, the clause involved is so one-sided that it is unconscionable under the circumstances existing when the parties made the contract. The principle is one of preventing oppression and unfair surprise and not of disturbing allocation of risks because of superior bargaining power."[128] "Unequal bargaining power does not establish grounds for defeating an agreement to arbitrate absent a well-supported claim that the clause resulted from the sort of fraud or overwhelming economic power that would provide grounds for revocation of any contract."[129]

The basic test appears to require a showing of overwhelming economic power. It is difficult to provide any input as to what kind of showing would suffice, since we are unaware of any recent Texas cases where such a showing has been upheld with the exception of the high cost of arbitration cases, which are described separately below. It is easy to demonstrate the kind of factors that do not constitute unconscionability, however.

An arbitration clause that allows a lender to seek judicial remedies to protect its security interest but which requires borrowers to arbitrate all of their claims is not unconscionable, but "most federal courts, however, have rejected similar challenges on the grounds that an arbitration clause does not require mutuality of obligation, so long as the underlying contract is supported by adequate consideration."[130]

In the employment context, "take it or leave it" arbitration policies that require an at-will employee to either accept them or quit with no opportunity for negotiation are not unconscionable.[131]

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[121] *Iberia Credit Bureau, Inc. v. Cingular Wireless LLC*, 379 F.3d 159, 166 (5th Cir. 2004), *quoting Doctor's Assocs. v. Casarotto*, 517 U.S. 681, 687, 116 S.Ct. 1652 (1996).
[122] Buckeye Check Cashing v. Cardegna, 126 S.Ct. 1204 (2006).
[123] *Id.*, at 1207.
[124] *Id.*
[125] *See also FirstMerit*, 52 S.W.3d at 756 ("We again note that these defenses must specifically relate to the Arbitration Addendum itself, not the contract as a whole, if they are to defeat arbitration. Defenses that pertain to the entire installment contract can be arbitrated.")
[126] *Carter v. Countrywide Credit Indus., Inc.*, 362 F.3d 294, 301 (5th Cir. 2004), *citing Halliburton*, 80 S.W.3d at 571.
[127] *Halliburton*, 80 S.W.3d at 572.
[128] *FirstMerit*, 52 S.W.3d at 757.
[129] *AdvancePCS*, 172 S.W.3d at 608.
[130] *FirstMerit*, 52 S.W. 3d at 757-58.
[131] *Halliburton*, 80 S.W.3d at 572.

"Take it or leave it" arbitration policies are also enforceable in a commercial, non-employment context which includes those contained in contracts of adhesion.[132]

Contracts of adhesion between "unsophisticated" consumers and lenders which inure to the benefit of third parties who may unilaterally "opt-out" of the obligation to arbitrate are also not unconscionable. [133]

3. Costs as a Basis for Unconscionability

The U.S. Supreme Court has written that "the existence of large arbitration costs could preclude a litigant . . . from vindicating her federal statutory rights in the arbitral forum."[134] The Texas Supreme Court has acknowledged that substantial costs and fees associated with the arbitral forum can render an arbitration agreement unconscionable.[135] In neither the *Green Tree* case nor the *FirstMerit* case, however, did the Court find that the party opposing arbitration had made an adequate evidentiary showing of what the costs of arbitration would actually be.

A Texas Court of Appeals in Houston found an arbitration agreement to be unconscionable on the basis of a local attorney's testimony as to the proposed arbitration's cost.[136] In that case, the arbitration agreement in question actually contained a limit on the costs which provided some protection to the party resisting arbitration.[137] In the *Luna* case, the party resisting arbitration put on evidence regarding not only what the costs would be, but also his net worth, in order to demonstrate the unconscionable effect of the costs. On appeal, the Texas Supreme Court concluded that fee-splitting schemes in an arbitration agreement which "operate to prohibit from fully and effectively vindicating statutory rights are not enforceable."[138] It held that the agreement provisions precluding Luna's remedies under the Texas Workers' Compensation Act were substantively unconscionable and void under Texas law.[139] The Court compelled arbitration of Luna's retaliatory-discharge claim, however.[140]

The San Antonio Court of Appeals affirmed a trial court decision to refuse to compel arbitration when, after an evidentiary hearing, the Court found that the costs of the arbitration made it unconscionable.[141] In that case, the party resisting arbitration put forth evidence that the arbitration would cost almost $70,000 when the contract which was the subject of the dispute was only worth $22,600.[142] According to the Court, it would be unconscionable to require the parties to spend $70,000 to arbitrate a $22,650 claim. On October 27, 2006, the Texas Supreme Court denied a petition for review of the case, so it is good law at least until the *mandamus* opinion in the *Luna* case comes out.

The Fifth Circuit beat the Texas Supreme Court to the punch with an August 23 opinion that rejected cost-unconscionability.[143] In that case, a Mississippi chicken farmer named Gertrude Overstreet sued a chicken provider for fraudulent inducement and the chicken provider filed a motion to compel arbitration.[144]Ms. Overstreet asserted the high cost of arbitration as grounds for unconscionability:

> [T]he district court found that the arbitration clause was unconscionable because arbitration pursuant to that clause would cost Appellee between $27,500 and $29,000. The Court reasoned that the cost made the clause unconscionable because Appellee is now extremely poor. As evidence of Appellee's current financial status, the Court considered the following facts in the record: Appellee and her husband (1) receive less than $1,000 per month in social security benefits, (2) own no land, (3) have no cash savings, (4) receive food stamps, and (5) rely on Medicaid to pay for their required medical prescriptions.[145]

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[132] *AdvancePCS*, 172 S.W.3d at 608.
[133] *Palm Harbor Homes*, 195 S.W.3d at 678-79.
[134] *Green Tree Fin. Corp. – Alabama v. Randolph*, 531 U.S. 79, 90, 121 S.Ct. 513, 522 (2000).
[135] *FirstMerit*, 52 S.W.3d at 756.
[136] *In re: Luna*, 175 S.W.3d 315, 319-22 (Tex. App. - Houston [1st Dist.] 2004, orig. proceeding, app. for *mandamus* filed).
[137] *Id.*, at 319.
[138] In re Poly-America, L.P., 262 S.W.3d 337 (Tex. 2008).
[139] *Id.*
[140] *Id.*
[141] Olshan Foundation Repair Co. v. Ayala, 180 S.W.3d 212 (Tex. App. – San Antonio, 2005, pet. denied).
[142] *Id.*, at 216.
[143] *Overstreet v. Contigroup Companies, Inc.*, 462 F.3d 409 (5th Cir. 2006).
[144] *Id.*, at 411.
[145] *Id.*, at 412.

Despite this record, the Fifth Circuit reversed the trial court's unconscionability finding based on Georgia unconscionability law which requires that the analysis take into account the party's position at the time the contract was executed.[146] Since Ms. Overstreet did not prove up her 2001-era destitution, she did not establish her unconscionability defense.

4. Arbitration Waiver

An argument can be made that a party seeking arbitration has waived its right to arbitrate if that party has "substantially invoked the judicial process to his opponent's detriment."[147] Like all other impediments to arbitration, however, courts are loath to find waiver. In a recent case, the Texas Supreme Court found that a party had not waived its right to arbitration despite two years of litigation, extensive discovery and attorneys' fees in excess of $200,000.[148]

In February of this year, the Texas Supreme Court issued a short *per curiam* opinion further closing the door on a potential waiver argument against arbitration.[149] In that case, the Court refused to find waiver against a party that had filed a motion for new trial in the face of a default judgment at the trial court level.[150] After Bank One was defaulted for failure to answer, filed a motion for new trial, the trial court granted the motion and Bank One filed an answer, Bank One moved to compel arbitration eight months later.[151] The party resisting arbitration argued waiver, claiming that in filing a motion for new trial Bank One had "invoked the judicial process to [the resisting party's] detriment."[152] The Texas Supreme Court rejected this argument, holding that "This Court has repeatedly rejected waiver when parties participated much more extensively than Bank One in judicial proceedings."[153] In Texas, so far as waiver analysis is concerned (at least in this context), the question is simply one of sheer quantity of judicial process. Unless a party can show more litigation than that in *Vesta*, a waiver argument cannot work, even when the party seeking to arbitrate had to fight to get back into the litigation in the first place.

Perry Homes has once again been applied to describe what constitutes an arbitration waiver, except this time no waiver was found. As we have mentioned before in While We Were Out, a blog post from May, waiver is hard to come by in a Texas Supreme Court opinion. *Perry Homes* could have moved us into a parallel universe in which claiming waiver of arbitration is a winning argument. But those who criticized the opinion knew we would be making no such move, not because of the particulars involved but because of who the players were. As we wrote before, Perry Homes was the party seeking waiver and was also a big supporter of many justices of the Court. Many critics of the opinion did not see *Perry Homes* as precedent for a shift in the Court's policy due to that fact. Well critics, you were probably right. In *Fleetwood Homes*, the Texas Supreme Court applied *Perry Homes*, but decided that waiting eight months to compel arbitration, during which time the parties engaged in some discovery and set a trial date (or in this case, postponed it), did not waive arbitration.

"[A] party waives an arbitration clause by substantially invoking the judicial process to the other party's detriment or prejudice." This quote from *Perry Homes* sums up the standard that will now be applied by the Court in these matters. Gulf in *Fleetwood* relied on *Vesta Ins. Group*'s precedent that a party would waive its right to arbitrate when it engaged in "full discovery," filed motions going to the merits of the case and sought arbitration "only on the eve of trial." The Court did not, however, agree with Gulf that Fleetwood fit that description. Moreover, the Court focused on a party's detriment as the dispositive issue in cases of arbitration waiver. Because no detriment was found to have befallen Gulf by Fleetwood's pretrial activities, the Court found no waiver.

Fleetwood made it clear that unless a party truly waits to the very last minute before trial to compel arbitration, having already engaged in full discovery, no waiver will be found. The fact that Fleetwood had taken no depositions (although it noticed one after canceling it) may have had an impact on the Court but the decision hinged on the detriment to Gulf. The Court found that Gulf suffered no detriment by trading emails with Fleetwood regarding a trial

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[146] *Id.*
[147] *Vesta*, 192 S.W.3d at 763; *Wilson*, 196 S.W.3d at 783.
[148] *Vesta*, 192 S.W.3d at 763.
[149] In re: Bank One, N.A., ___ S.W.3d ___, 2007 Tex. LEXIS 161 (Tex. 2007) (Cause No. 06-0093).
[150] *Id.*
[151] *Id.*, at *1.
[152] *Id.*, at *4.
[153] *Id.*

date. The opinion also pointed out that those emails did not constitute an implied waiver, much less sufficed as evidence for an express waiver as Gulf claimed.

Apart from the implications on arbitration waivers, this opinion seriously impacts fee-shifting clauses. The agreement between Fleetwood and Gulf contained a fee-shifting clause which allowed for a prevailing defendant's attorney fees. Gulf attempted to throw out the arbitration agreement on unconscionability grounds based on this fee-shifting clause, but to no avail. The Court found that even though Texas law only allows for prevailing plaintiff's attorney fees, an arbitration clause that would allow for a prevailing defendant to get attorney's fees would not make such agreement unconscionable; in fact, it would make it more fair. This statement leaves us to wonder whether we can expect more resistance against arbitration clauses from here on out…

5. The Agreement is Invalid

Even when parties have agreed to arbitrate, it is possible that a court may find an agreement to arbitrate contrary to law. That was the issue in *14 Penn Plaza L.L.C. v. Pyett*, in which an employer sought to compel union workers to arbitrate their age discrimination claims arising under the Age Discrimination in Employment Act. (ADEA).[154]

The district court denied the employer's motion to compel, and the U.S. Court of Appeals for the Second Circuit affirmed, reasoning that the U.S. Supreme Court case of *Gardner-Denver* held "that a collective bargaining agreement could not waive covered workers' rights to a judicial forum for causes of action created by Congress." The Second Circuit noted the tension between *Gardner-Denver* and the latter case of *Gilmer v. Interstate/Johnson Lane Corp.*, and explained that although an individual may waive his right to a judicial forum, a union cannot waive that right on behalf of an individual.[155]

The U.S. Supreme Court reversed, rejecting the union workers' claim that "an individual employee must personally 'waive a '(substantive right)' to proceed in court for a waiver to be 'knowing and voluntary' under the ADEA." The Court stated that an agreement to arbitrate ADEA claims is not a waiver. The Court said that "the unsuccessful arbitration did not preclude the federal lawsuit." At the same time, the Court explained that "the decision to resolve ADEA claims by way of arbitration instead of litigation does not waive the statutory right to be free from workplace age discrimination; it waives only the right to seek relief from a court in the first instance."[156]

In *14 Penn Plaza*, the Court held that a provision in a collective-bargaining agreement that clearly and unmistakably requires union members to arbitrate claims arising under the (ADEA) is enforceable as a matter of federal law.[157]

III. RECENT DEVELOPMENTS IN BINDING NONSIGNATORIES TO ARBITRATION

This section of the paper will, by necessity, consider the unusual cases since the courts do not spend much time discussing the issue in the face of actual, signed arbitration agreements between parties. Recent opinions from the U.S. Supreme Court, the Texas Supreme Court and the Fifth Circuit demonstrate that it is quite possible for an agreement to arbitrate to exist in the absence of a written agreement signed by both purportedly bound parties to the litigation.

A. U.S. Supreme Court

In March 2009, the U.S. Supreme Court held in *Arthur Anderson LLP v. Carlisle*, that a non-party to an arbitration agreement could appeal a trial court ruling that rejected the third party's motion to compel arbitration.[158] Justice Scalia delivered the majority opinion, joined by Justices Kennedy, Thomas, Ginsburg, Breyer and Alito. Justice Souter filed a dissenting opinion, in which Chief Justice Roberts and Justice Stevens joined.[159]

[154] 14 Penn Plaza LLC v. Pyett, 129 S.Ct. 1456 (2009)
[155] *Id.*
[156] *Id.*
[157] *Id.*
[158] Arthur Andersen LLP v. Carlisle, 129 S.Ct. 1896, 1898 (2009).
[159] *Id.*

In *Carlisle*, the accounting firm of Arthur Andersen LLP, together with Bricolage Capital, LLC, a financial advisor, and Curtis, a law firm, designed a tax strategy for Carlisle to limit its tax liability.[160] Only the agreements between Carlisle and Bricolage provided for arbitration of disputes.[161] As it turns out, the Internal Revenue Service (IRS) determined that the investment strategy was an illegal tax shelter and Carlisle brought suit in federal court against all three entities.[162] The suit alleged fraud, civil conspiracy, malpractice, breach of fiduciary duty and negligence. Anderson and Curtis sought a stay invoking Section 3 of the FAA and demanded the dispute be referred to arbitration.[163] The district court denied the motion and the Court of Appeals for the Sixth Circuit dismissed for want of jurisdiction.[164]

The first issue the Court decided was whether appellate courts have jurisdiction under Section 16(a) of the FAA to review denials of stays of litigation requested by nonparties to the arbitration agreement.[165] The Court concluded that Section 16(a) with "clear and unambiguous terms" expressly authorizes interlocutory appeals of motions denying Section 3 stays.[166] Stressing that "[t]he jurisdictional statute here unambiguously makes the underlying merits irrelevant," the Court rejected an argument that such an interpretation would produce frivolous interlocutory appeals.[167]

Next, the Court explained that Section 2 of the FAA makes arbitration agreements "valid, irrevocable, and enforceable " requiring courts "to place [arbitration] agreements upon the same footing as other contracts."[168] Section 3 also allows enforcement of Section 2, by requiring the courts to stay litigation, "on application of one of the parties" if the issue is "referable to arbitration under an agreement in writing."[169] When interpreting the phrase "one of the parties," the Court clarified in footnote 4, that the word "parties" refers to parties to the litigation, and not to the parties to the contract.[170]

Then, the Court reasoned that Section 3 does not restrict the enforceability of Section 2. As a result, state law should be applied to determine which contracts are binding under Section 2 and enforceable under Section 3.[171] The Court added that because state law allows contracts to be enforced by or against nonparties through different theories such as assumption, piercing the veil, alter ego, incorporation by reference, third-party beneficiaries, waiver and estoppel, nonparties may invoke Section 3.[172]

In sum, in *Carlisle*, the U.S. Supreme Court ruled that appellate federal courts have jurisdiction to review the denial of a request for a Section 3 stay and that a litigant who was not a party to the arbitration agreement may invoke Section 3 if the relevant state contract law allows the nonparty to enforce the agreement.[173]

B. Texas Supreme Court

Texas courts have employed different and unusual theories in order to find that an agreement to arbitrate exists in the absence of a traditional written agreement. They include: direct-benefits estoppel, incorporation by reference, assumption, agency, alter ego and third-party beneficiary.[174] These theories stem from contract law, since an agreement to arbitrate is simply a contract.

1. Wrongful Death Cases: *Labatt* and *Jindal*

[160] *Id*. at 1899.
[161] *Id*.
[162] *Id*. Also named in the suit were two employees of Bricolage (Andrew Beer and Samyak Veera); Curtis, Mallet-Prevost, Colt & Mosle, LLP; William Bricker (the lawyer respondents worked with at the law firm); Prism Connectivity Ventures, LLC (the entity from whom the worthless warrants were purchased); Integrated Capital Associates, Inc. (a prior owner of the worthless warrants who had also been a client of the law firm); and Intercontinental Pacific Group, Inc. (a firm with the same principals as Integrated Capital Associates). *Id*.
[163] *Id*. at 1899-1900.
[164] *Id*. at 1900.
[165] *Id*.
[166] *Id*.
[167] *Id*. at 1901.
[168] *Id*.
[169] *Id*. at 1901-02.
[170] *Id*. at 1901.
[171] *Id*. at 1902.
[172] *Id*.
[173] *Id*. at 1898.
[174] *See* In re Kellogg Brown & Root, 166 S.W.3d 732, 739 (mentioning the legal theories used by Texas courts to find an agreement to arbitrate).

In *Labatt*, the Texas Supreme Court resolved the issue of whether non-signatories to an arbitration agreement should be compelled to arbitrate claims when the decedent's claims would have been arbitrated.[175] Plaintiffs in this case were family members who brought a wrongful death action against the decedent's employer Labatt Food Service, L.P.[176] Labatt filed a motion to compel arbitration, pursuant to an arbitration agreement signed by the decedent.[177] The trail court denied Labatt's motion and Labatt appealed.[178]

The Texas Supreme Court stated it "is well established that statutory wrongful death beneficiaries' claims place them [the family members] in the exact 'legal shoes' of the decedent, and they are subject to the same defenses to which the decedent's claims would have been subject."[179] The Court reasoned that if the employee had not died from his injuries, his claims would have been arbitrated.[180] Accordingly, the Court held that beneficiaries are required to arbitrate their wrongful death claims.[181]

Similarly, in *Jindal*, the Texas Supreme Court held that an arbitration agreement between a decedent and his employer required the non-signatory beneficiaries to arbitrate their claims against the employer.[182]

2. Agents and Affiliates: *Merrill Lynch* and *Kaplan*

In *Merrill Lynch*, the Texas Supreme Court refused to adopt concerted-misconduct equitable estoppel as a means by which non-signatories to an agreement to arbitrate can nonetheless compel arbitration.[183] In *Merrill Lynch*, Juan Alaniz settled a personal injury lawsuit and opened several accounts with Merrill Lynch to manage his settlement proceeds.[184] All of his contracts with Merrill Lynch contained arbitration clauses.[185] Part of his investment plan, however, required that he also enter into contracts with Merrill Lynch Trust Company (MLT) and Merrill Lynch Life Insurance Company (MLLI), so that he could create a life insurance trust.[186] Mr. Alaniz's contracts with MLT and MLLI did not contain arbitration clauses.[187] The broker who handled all of his accounts was named Henry Medina.[188] In April 2003, Alaniz sued Medina, MLT and MLLI, but not Merrill Lynch.[189] All defendants moved to compel arbitration based on the Merrill Lynch contracts that contained arbitration clauses.[190] Both the trial court and the Thirteenth Court of Appeals denied the motions to compel arbitration.[191]

The Texas Supreme Court reversed those decisions insofar as the Alaniz claims against Mr. Medina were concerned.[192] The majority opinion held that Alainz could not sue an agent of a company with whom he had an agreement to arbitrate and thus avoid the agreement to arbitrate.[193] The Court reasoned that in substance the claims were against Merrill Lynch, so arbitration was the appropriate forum. This holding is certainly consistent with prior Texas case law.

The majority refused to compel arbitration with respect to Alaniz's claims against MLT and MLLI, however.[194] MLT and MLLI entered into separate contractual relationships with Alaniz.[195] They had an opportunity to negotiate for an arbitration clause and they chose not to. Compelling arbitration against them, therefore, would allow them to re-write their agreements with Alaniz after the fact. In Texas, if you're a non-signatory hoping to compel arbitration

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[175] In re Labatt Food Service, L.P., 279 S.W.3d 640 (Tex. 2009).
[176] *Id.* at 642.
[177] *Id.*
[178] *Id.*
[179] *Id.* at 644.
[180] *Id.* at 649.
[181] *Id.*
[182] In re Jindal Saw Ltd., __ S.W.3d __ (Tex. 2009); 2009 LEXIS 33.
[183] In re Merrill Lynch Trust Co. FSB, 235 S.W.3d 185 (Tex. 2007).
[184] *Id* at 188.
[185] *Id.* Each account agreement contained the following clause: "I agree that all controversies which may arise between us, including but not limited to those involving any transaction or the construction, performance, or breach of this or any other agreement between us, whether entered into prior, on or subsequent to the date hereof, shall be determined by arbitration." *Id.*
[186] *Id.*
[187] *Id.*
[188] *Id.*
[189] *Id.*
[190] *Id.*
[191] *Id.*
[192] *Id.* at 190.
[193] *Id.*
[194] *Id.* at 191.
[195] *Id.*

based on someone else's contract with the Plaintiff, you're much better off if you don't have a contract of your own with the Plaintiff.

Next, MLT and MLII urged the Court to find an agreement to arbitrate pursuant to a theory called concerted-misconduct equitable estoppel (CMEE).[196] Like direct benefits estoppel, CMEE is an estoppel theory some courts have adopted to require non-signatories to arbitration agreements to arbitrate their claims. Since the Texas Supreme Court has enthusiastically applied direct benefits estoppel to compel arbitration, MLT and MLII apparently decided to have a go at CMEE.

After discussing other jurisdictions' approach to CMEE, the Texas Supreme Court decided not to adopt it here:

> Similarly, while Texas law has long recognized that nonparties may be bound to a contract under traditional contract rules like agency or alter ego, there has never been such a rule for concerted misconduct. Conspiracy is a tort, not a rule of contract law. And while conspirators consent to accomplish an unlawful act, that does not mean they impliedly consent to each other's arbitration agreements. As other contracts do not become binding on nonparties due to concerted misconduct, allowing arbitration contracts to become binding on that basis would make them easier to enforce than other contracts, contrary to the Arbitration Act's purpose.[197]

Merrill Lynch required the plaintiff to arbitrate against the employee and to proceed with litigation against the affiliated entities. The Court compelled arbitration of claims against one defendant, but not the other two. What, then, happens next? Well, the rule in Texas is that the arbitration is held first. The Court stays the litigation between Alaniz and the Merrill Lynch companies until the arbitration against Medina is complete. The Court stated that "the case illustrates one of many circumstances in which litigation must be abated to ensure that an issue two parties have agreed to arbitrate is not decided instead in collateral litigation."[198]

In *Kaplan*, the Texas Supreme Court cited *Merrill Lynch* and held that a fraudulent inducement claim must be arbitrated if the contract which was allegedly fraudulently induced contained an arbitration clause, even if the party seeking to compel arbitration is not a signatory to that contract.[199] *Kaplan* involves fraudulent inducement claims by a group of student electricians against a vocational college.[200] The students alleged that the college induced them to enroll by making false promises that they would be eligible for journeyman or master electrician licenses upon graduation.[201]

The college, with whom the students had entered into the arbitration agreements, was wholly owned by Kaplan Higher Education Corporation.[202] When the students sued the college, the college moved to compel arbitration and the students dropped their claims against the college, choosing instead to proceed against Kaplan.[203] Kaplan was not a signatory to the enrollment agreement containing the arbitration clause, and neither the trial court nor the Thirteenth Court of Appeals would compel arbitration.[204]

The Texas Supreme Court directed the trial court to compel arbitration and added that "when an agreement between two parties clearly provides for the substance of a dispute to be arbitrated, one cannot avoid it by simply pleading that a nonsignatory agent or affiliate was pulling the strings."[205]

3. Securities Firm as Beneficiary of Employee's Agreement: *In re NEXT Financial*

In *NEXT Financial*, the Texas Supreme Court held that a third party beneficiary of an arbitration agreement was entitled to enforce the arbitration provision.[206] Michael Clements was an employee of NEXT Financial Group, Inc., a

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[196] *Id.*
[197] *Id.* at 194.
[198] *Id.* at 196.
[199] In re Kaplan Higher Educ. Corp., 235 S.W.3d 206, 210 (Tex. 2007).
[200] *Id.* at 208.
[201] *Id.*
[202] *Id.*
[203] *Id.*
[204] *Id.*
[205] *Id.* at 210.
[206] In re NEXT Financial Group, Inc., 271 S.W.3d 263 (Tex. 2008).

securities firm, since September 2006.[207] Surprisingly, the parties did not have a written employment contract.[208] Clements was required to register with the National Association of Securities Dealers (NASD) by executing a Uniform Application for Securities Industry Registration or Transfer form (U-4) as a condition of employment, however.[209] The U-4 form contained an agreement to "arbitrate any dispute, claim or controversy that may arise between me and my firm . . . that is required to be arbitrated under the rules, constitutions, or bylaws of [the NASD] . . . as may be amended from time to time . . . ."[210] In August 2007, NEXT Financial fired Clements claiming that he failed to perform some of the duties required by his job.[211] Clements sued NEXT Financial claiming he was fired for refusing to conceal a trader's fraudulent transactions.[212] NEXT Financial moved to compel arbitration based on the arbitration clause in the U-4.[213] The trial court denied the motion and the court of appeals denied *mandamus* relief.[214]

The Texas Supreme Court held that Clements' claims fell within the scope of his arbitration agreement with NASD and was not subject to an exception limited to statutory employment discrimination.

4. Automobile Dealership Transfer: *Meyer*

In *Meyer*, the Texas Supreme Court emphasized that non-signatories to arbitration agreements can still be required to arbitrate certain disputes.[215] The Court analyzed circumstances in which a non-signatory can compel arbitration pursuant to a contract to which the non-signatory was, of course, not a party. The majority opinion, written by Justice Hecht, continues the trend of judicial empowerment of arbitration contracts.

In this case, a jilted potential purchaser of a Ford dealership sued Ford, the dealership and the eventual successful purchaser when Ford exercised a right of first refusal and caused the purchase and sale agreement (PSA) between first purchaser and the dealership to be terminated.[216] The PSA was a contract between the dealership and the first purchaser. Ford and the eventual purchaser were not parties.[217]

The first purchaser sued based on a theory that Ford's right of first refusal was not valid and did not allow Ford to terminate the PSA or allow the dealership to get out of the PSA.[218] The first purchaser also sued the eventual purchaser for interfering with the PSA.[219] The PSA, which was between only the dealership and the first purchaser, included an arbitration clause.[220] In what could be described as the "flip side" of the normal fact pattern, Ford and the eventual purchaser, who were never parties to the PSA, moved to compel arbitration based on the PSA's arbitration clause.[221] The trial court and the Court of Appeals refused to compel arbitration, but the Texas Supreme Court saw the issue differently.[222] According to Justice Hecht, since the plaintiff-first purchaser's claims against Ford and the eventual purchaser were completely intertwined with its claims against the dealership and since a arbitration agreement existed between it and the dealership, equitable estoppel required that all of the claims be arbitrated.[223]

In her dissent, Justice O'Neill argues that a claim for tortious interference with a contract could not be so intertwined with a claim for breach of that contract to support equitable estoppel, especially since the arbitration clause itself was not a traditional, sweepingly broad clause.[224]

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[207] *Id.* at 265.
[208] *Id.*
[209] *Id.*
[210] *Id.*
[211] *Id.*
[212] *Id.* The court cited Sabine Pilot, 687 S.W.2d at 734-35 (holding that an at-will employee can recover damages from an employer who terminated his employment solely for refusing to perform an illegal act). *Id.*
[213] *Id.* at 266.
[214] *Id.*
[215] Meyer v. WMCO-GP, L.L.C. 211 S.W.3d 302 (Tex. 2008).
[216] *Id.* at 304.
[217] *Id.*
[218] *Id.*
[219] *Id.*
[220] *Id.*
[221] *Id.*
[222] *Id.* at 305.
[223] *Id.* at 307.
[224] *Id.* at 308-09.

The opinion in *Meyer* discussed in detail the doctrine of equitable estoppel as it applies to the enforcement of arbitration agreements and continues a powerful trend in Texas jurisprudence of making arbitration clauses extremely difficult to avoid.

C. Fifth Circuit

Recently, the Fifth Circuit held in *Graves* that non-signatory plaintiffs were bound by the arbitration agreement between a decedent and his employer.[225] Plaintiffs in *Graves* were the surviving relatives of an employee of defendant JV Industrial Companies, who died in a work-related accident at a BP facility in Texas.[226] The plaintiffs sued under the Texas wrongful death statute and the Texas survival statute.[227] Defendants moved to compel arbitration pursuant to the arbitration clause in the decedent's employment contract.[228] The district court granted the motion with respect to the survival claims because it found those claims to be "wholly derivative of the decedent's rights."[229] On the other hand, the Court refused to compel arbitration of the wrongful death claims, as it found them to be "personal to the plaintiffs."[230] Defendants appealed.[231]

The issue before the Fifth Circuit was whether non-signatories suing a decedent's employer under the Texas wrongful death statute are bound by an arbitration agreement between the employer and the decedent.[232] The Court first considered whether state or federal choice of law applied by setting out the two-prong analysis presented by a motion to compel arbitration:

1. Validity: whether there is a valid agreement to arbitrate.[233] Here, the Court answered that state law principles that govern contract formation must be applied to resolve this question. [234]
2. Scope: whether the dispute is within the scope of the arbitration agreement.[235] The Court pointed out that this question is resolved by applying the federal substantive law of arbitrability.[236]

Next, the Court noted that the issue before them fell somewhere between validity and scope and added that current case law is inconsistent as to the choice of law.[237] The Fifth Circuit reasoned that it was not required to decide the applicable choice of law, however, because under both federal and state law the outcome was the same.[238]

Using Texas law and citing *Labatt*, the Court determined that non-signatories were bound by the agreement because they "stand in the decedent's legal shoes."[239] Similarly, applying federal law, the Court stated that the "direct benefits" version of estoppel applied. [240] Accordingly, "a nonsignatory cannot sue under an agreement while at the same time avoiding its arbitration clause."[241] Then, the Court found that the statutory wrongful death action was, at least in part, premised on the decedent's employment agreement.[242] Finally, the Fifth Circuit reversed, holding that the plaintiffs were bound by the arbitration agreement made by the decedent.[243]

IV. DISCOVERY IN ARBITRATION

In 1991, the United States Supreme Court decided in *Gilmer v. Interstate/Johnson Lane Corp*. that age discrimination claims under the Age Discrimination in Employment Act (ADEA) could be subject to binding

[225] Graves v. BP America, Inc., 568 F.3d 221, 223 (5th Cir. 2009).
[226] *Id*. at 222.
[227] *Id*.
[228] *Id*.
[229] *Id*.
[230] *Id*.
[231] *Id*.
[232] *Id*.
[233] *Id*. at 222.
[234] *Id*.
[235] *Id*.
[236] *Id*.
[237] *Id*. at 222-23.
[238] *Id*. at 223.
[239] *Id*.
[240] *Id*.
[241] *Id*.
[242] *Id*. at 223-24.
[243] *Id*. at 224.

arbitration.[244] In other words, nothing about the nature of the claims themselves (i.e. that they involved allegations of depravations of statutory rights) meant that employees could not waive their right to pursue those claims in courts by way of arbitration agreements. The underlying plaintiffs in the case argued, unsuccessfully, that one reason ADEA claims ought not to be arbitrable was the limited availability of discovery in arbitral proceedings.[245] Since discovery is limited in arbitration proceedings, the argument went, plaintiffs in those proceedings do not have the same tools at their disposal that they would have in court and therefore the claims ought not to be arbitrable at all, since arbitration by its nature would deprive claimants of their full ability to pursue the claims.[246]

The Supreme Court rejected this argument and the basis for the rejection, although fairly terse, is an important framework within which to discuss discovery in arbitration. First, the Court noted that discovery in some fashion was in fact available under the arbitral rules that would apply in the *Gilmer* case (the New York Stock Exchange and NASD rules).[247] This is also the case with virtually every mainstream and major provider of arbitration administration (like the AAA – more on this later). Second, the Court reflected that even though the parties could, in all fairness, expect some limitations on their ability to conduct discovery in the arbitration process, those limitations are a trade-off the parties made in exchange for "the simplicity, informality, and expedition of arbitration."[248] In other words, some discovery is to be expected in arbitration, if not even required, but some limitations on discovery are part of the policy rationale for favoring arbitration in the first place. In 2004, the Fifth Circuit followed *Gilmer* in its rejection of an argument against arbitration made on the basis of arbitration's assumed limitations on the discovery process.[249]

There is nothing in the Federal Arbitration Act (FAA), the Texas Arbitration Act (TAA) or the Texas International Arbitration Act (TIAA) that precludes discovery in the arbitration process.[250] Indeed, as discussed in Section B below, those statutes provide a basis for parties in arbitration proceedings to seek court intervention to enforce arbitral orders compelling discovery. However, Section C presupposes that an arbitral order compelling discovery exists. Whether or not an arbitrator will issue such an order is another, and frankly more important, question.

A. Is Discovery Permitted in the First Place?

It is quite well-settled that arbitration is a creature of contract between parties, and the arbitration clause, can also set out the administrative rules that will govern an arbitration. Most familiar would be those rules promulgated by the American Arbitration Association (AAA). Other organizations exist, however, that provide arbitration administration services and it is permissible for parties to craft their own procedural rules. Almost all of these rules allow for the potential for discovery at the arbitrator's discretion.

1. American Arbitration Association

The AAA promulgates several different sets of rules. This paper will set out their discovery rules in the major rule-sets. The AAA's Rules for Commercial Arbitrations are commonly used. That set of rules includes the following:

> **R-21. Exchange of Information**
>
> (a) At the request of any party or at the discretion of the arbitrator, consistent with the expedited nature of arbitration, the arbitrator may direct
>
> i) the production of documents and other information, and

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[244] Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 111 S.Ct. 1647 (1991); S*ee also supra* note 4.
[245] *Id.* at 31, 1654-55.
[246] *Id.*
[247] *Id.*
[248] *Id.*, at 31, 1655 (quoting *Misubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc*., 473 U.S. 614, 628, 105 S.Ct. 3346 (1985)). This begs several questions beyond the scope of this paper, but worth mentioning, such as: Can employment dispute plaintiffs in Texas really be said to bargain for the arbitration process? Is arbitration actually simple, informal, and expeditious? We will leave it for your own experience and biases to answer these questions, but U.S. arbitration policy rests on an assumption that the answers are "yes."
[249] *See* Carter, et al. v. Countrywide Home Loans, Inc., 362 F.3d 294, 298-99 (5th Cir. 2004) (holding that the employees failed to meet their burden of overcoming the "strong presumption" in favor of arbitration necessary to invalidate the arbitration agreements).
[250] *See* Federal Arbitration Act, 9 U.S.C. § 1 *et seq*.; Texas General Arbitration Act, TEX. CIV. PRAC. & REM. CODE ANN. § 171.001 *et seq*.; Texas International Arbitration Act, TEX. CIV. PRAC. & REM. CODE ANN. § 172.001 *et seq*.

ii) the identification of any witnesses to be called.

(b) At least five business days prior to the hearing, the parties shall exchange copies of all exhibits they intend to submit at the hearing.

(c) The arbitrator is authorized to resolve any disputes concerning the exchange of information.[251]

The Rule is silent on the availability of depositions. We take the position that there is nothing that precludes depositions but again, their availability will be up to the arbitrator. Rule 22, however, states that in a preliminary hearing, an arbitrator may establish "the extent of and schedule for the production of relevant documents and other information."[252] Some arbitrators interpret the "other information" language to include the power to order depositions.

The AAA Rules for Commercial Arbitrations apply to complex cases which are defined by the AAA as cases where the claim is in excess of $500,000 exclusive of interest and attorneys' fees. The Rules specifically mention the possibility of depositions but also leave their availability up to the arbitrator:

L-4. Management of Proceedings

(a) Arbitrator(s) shall take such steps as they may deem necessary or desirable to avoid delay and to achieve a just, speedy and cost-effective resolution of Large, Complex Commercial Cases.

(b) Parties shall cooperate in the exchange of documents, exhibits and information within such party's control if the arbitrator(s) consider such production to be consistent with the goal of achieving a just, speedy and cost-effective resolution of a Large, Complex Commercial Case.

(c) The parties may conduct such discovery as may be agreed to by all the parties provided, however, that the arbitrator(s) may place such limitations on the conduct of such discovery as the arbitrator(s) shall deem appropriate. If the parties cannot agree on production of documents and other information, the arbitrator(s), consistent with the expedited nature of arbitration, may establish the extent of the discovery.

(d) At the discretion of the arbitrator(s), upon good cause shown and consistent with the expedited nature of arbitration, the arbitrator(s) may order depositions of, or the propounding of interrogatories to, such persons who may possess information determined by the arbitrator(s) to be necessary to determination of the matter.

(e) The parties shall exchange copies of all exhibits they intend to submit at the hearing 10 business days prior to the hearing unless the arbitrator(s) determine otherwise.

(f) The exchange of information pursuant to this rule, as agreed by the parties and/or directed by the arbitrator(s), shall be included within the Scheduling and Procedure Order.

(g) The arbitrator is authorized to resolve any disputes concerning the exchange of information.

(h) Generally hearings will be scheduled on consecutive days or in blocks of consecutive days in order to maximize efficiency and minimize costs.[253]

Again, AAA writes into its rules that arbitration has as a goal, "just, speedy and cost-effective resolution of . . . Large, Complex Commercial Case[s]," and it codifies the notion that things like depositions are contrary to the achievement of that goal.[254] That being the case, we certainly acknowledge that seeking such discovery could be met with some resistance but it really does depend on the arbitrator. None of these rules precludes discovery, they simply tacitly discourage it. Presumably, in a Large, Complex Commercial Case experienced counsel and their client

[251] *AAA Commercial Arbitration Rules and Mediation Procedures* (amended and effective June 1, 2009), *available at* http://www.adr.org/sp.asp?id=22440.
[252] *Id.*
[253] *Id.*
[254] *Id.*

representatives will see the benefit of some pre-trial discovery. In our experience, it has not been difficult to obtain discovery in arbitration, but admittedly the rules do not allow it as a matter of right.

2. Judicial Arbitration and Mediation Services

Rule 17 of the Judicial Arbitration and Mediation Services (JAMS) Comprehensive Arbitration Rules and Procedures governs discovery procedures in a matter arbitrated using this group of neutrals.[255] If the parties hold a preliminary conference, they may at that point address exchange of information in accordance with Rule 17 and the schedule for the exchange.[256] Rule 17 sets forth the procedures the exchange of information as follows:

> **RULE 17. Exchange of Information**
>
> (a) The Parties shall cooperate in good faith in the voluntary, prompt and informal exchange of all non-privileged documents and other information relevant to the dispute or claim immediately after commencement of the Arbitration.
>
> (b) The Parties shall complete an initial exchange of all relevant, non-privileged documents, including, without limitation, copies of all documents in their possession or control on which they rely in support of their positions, names of individuals whom they may call as witnesses at the Arbitration Hearing, and names of all experts who may be called to testify at the Arbitration Hearing, together with each expert's report that may be introduced at the Arbitration Hearing, within twenty-one (21) calendar days after all pleadings or notice of claims have been received. The Arbitrator may modify these obligations at the Preliminary Conference.
>
> (c) Each Party may take one deposition of an opposing Party or of one individual under the control of the opposing Party. The Parties shall attempt to agree on the time, location and duration of the deposition, and if the Parties do not agree these issues shall be determined by the Arbitrator. The necessity of additional depositions shall be determined by the Arbitrator based upon the reasonable need for the requested information, the availability of other discovery options and the burdensomeness of the request on the opposing Parties and the witness.
>
> (d) As they become aware of new documents or information, including experts who may be called upon to testify, all Parties continue to be obligated to provide relevant, nonprivileged documents, to supplement their identification of witnesses and experts and to honor any informal agreements or understandings between the Parties regarding documents or information to be exchanged. Documents that have not been previously exchanged, or witnesses and experts not previously identified, may not be considered by the Arbitrator at the Hearing, unless agreed by the Parties or upon a showing of good cause.
>
> (e) The Parties shall promptly notify JAMS when an unresolved dispute exists regarding discovery issues. JAMS shall arrange a conference with the Arbitrator, either by telephone or in person, and the Arbitrator shall decide the dispute. With the written consent of all Parties, and in accordance with an agreed written procedure, the Arbitrator may appoint a special master to assist in resolving a discovery dispute. [257]

3. Financial Industry Regulatory Authority

In July 2007, the National Association of Securities Dealers (NASD) and the arbitration functions of the New York Stock Exchange (NYSE) consolidated to form the Financial Industry Regulatory Authority (FINRA). FINRA is now the entity that conducts securities arbitration pursuant to what we used to refer to as the NASD Code of Arbitration Procedure. FINRA continues to enforce NASD arbitration rules, and two rule-sets exist: one for customer disputes (a dispute between a customer and a licensed securities professional, like a broker) and one for industry disputes (disputes between licensed securities professionals or firms).[258]

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[255] *JAMS Comprehensive Arbitration Rules and Procedures* (effective July 15, 2009), *available at* http://www.jamsadr.com/rules-comprehensive-arbitration/.
[256] *Id.*
[257] *Id.*
[258] *See FINRA Code of Arbitration Procedures* (FINRA Manual), *available at* http://www.finra.org/ArbitrationMediation/Rules/CodeofArbitrationProcedure/.

In FINRA arbitration of customer disputes, some discovery, particularly document exchange, is permitted and expected.[259] However, the NASD Code also specifically and strongly discourages depositions:

> Depositions are strongly discouraged in arbitration. Upon motion of a party, the panel may permit depositions, but only under very limited circumstances, including:
> • To preserve the testimony of ill or dying witnesses;
> • To accommodate essential witnesses who are unable or unwilling to travel long distances for a hearing and may not otherwise be required to participate in the hearing;
> • To expedite large or complex cases; and
> • If the panel determines that extraordinary circumstances exist.[260]

In other words, an NASD arbitrator has the discretion under the Code to permit depositions, but the Code on its face seeks to limit that discretion.

The FINRA/NASD Code of Arbitration Procedure for Industry Disputes is largely the same as the Code for Customer Disputes, with one significant exception: In Customer Arbitration, certain documents are presumed discoverable and must be automatically produced in every case. [261] No corresponding Rule exists in the NASD Code of Arbitration Procedure for Industry Disputes.

4. International Chamber of Commerce

The International Chamber of Commerce (ICC) maintains a Court of Arbitration which administers international arbitration and is commonly used in that context. ICC promulgates its own set of Rules as well. These Rules do not address the issue of discovery. The Rules do, however, allow the Arbitrator to revert to the procedural rules of the national law that applies to the arbitration in question in the event an issue is raised that the Rules do not address:

> **Article 15**
> **Rules Governing the Proceedings**
>
> 1. The proceedings before the Arbitral Tribunal shall be governed by these Rules and, where these Rules are silent, by any rules which the parties or, failing them, the Arbitral Tribunal may settle on, whether or not reference is thereby made to the rules of procedure of a national law to be applied to the arbitration.
>
> 2. In all cases, the Arbitral Tribunal shall act fairly and impartially and ensure that each party has a reasonable opportunity to present its case.[262]

In other words, if the arbitrator(s) in an international case administered by the ICC decide to apply U.S. law, then in the absence of a contrary agreement between the parties one could argue that the Federal Rules of Civil Procedure ought to apply, which in turn would provide for relatively robust discovery given the general anti-discovery prejudice that is part of the arbitration process.

5. International Bar Association

Article 3 of the International Bar Association (IBA) Rules on the Taking of Evidence in International Commercial Arbitration states, in part: "Within the time ordered by the Arbitral Tribunal, each Party shall submit to the Arbitral Tribunal and to the other Parties all documents available to it on which it relies, including public documents and those in the public domain, except for any documents that have already been submitted by another Party. [A]ny Party may submit to the Arbitral Tribunal a Request to Produce.[263]

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[259] *See FINRA (NASD) Code of Arbitration Procedures for Customer Disputes* (effective April 16, 2009), Rules 12505, 12506 and 12507, *available at* http://www.finra.org/web/groups/arbitrationmediation/@arbmed/@arbrul/documents/arbmed/p117546.pdf.
[260] *Id.* at Rule 12510.
[261] *Id*, at Rule 12506.
[262] *ICC Rules of Arbitration* (effective January 1, 2008), *available at* http://www.iccwbo.org/uploadedFiles/Court/Arbitration/other/rules_arb_english.pdf .
[263] *IBA Rules on the Taking of Evidence in International Commercial Arbitration* (adopted June 1, 1999), *available at http://www.ibanet.org/Publications/publications_IBA_guides_and_free_materials.aspx.*

6. Non-Administered Arbitration

The AAA and the NAF are corporations that administer arbitrations. They not only promulgate rules and sample arbitration clauses (which in turn require the use of their rules and services), but they also administer the arbitration, acting as a go-between between counsel for the parties and the arbitrator(s). Parties "file" pleadings by faxing or emailing them to AAA, and AAA in turn provides them to the arbitrator. The procedure is cumbersome and, in our experience, rife with opportunity for administrative error. The procedure is also quite expensive.

The International Institute for Conflict Prevention and Resolution (CPR) also promulgates rules and sample clauses but it advocates non-administered or ad-hoc arbitration, wherein the parties decide how the case will be arbitrated and the arbitrator self-administrates.[264] The only administration CPR is willing to perform is to help parties select an arbitrator or arbitrators if they are unable to do so.

CPR Promulgates a set of Rules for Non-Administered Arbitration and its rule on discovery is predictably deferential to the arbitrator's discretion:

> **Rule 11: Discovery**
>
> The Tribunal may require and facilitate such discovery as it shall determine is appropriate in the circumstances, taking into account the needs of the parties and the desirability of making discovery expeditious and cost effective. The Tribunal may issue orders to protect the confidentiality of proprietary information, trade secrets and other sensitive information disclosed in discovery.[265]

B. What if the Arbitrator Will Not Permit Discovery?

Arbitral discretion, of course, is the key. In Section C, we will explain how one can take an order compelling discovery issued by an arbitrator and ask a court to enforce it with all of the enforcement mechanisms available to the court. There is not, however, a corresponding mechanism to request immediate relief from an arbitrator's decision to deny a motion to compel. While the TAA, as set out below, empowers courts to enforce arbitral orders and empowers arbitrators to order discovery, it does not allow courts to order discovery in arbitrations in the absence of an arbitral order for the same relief.[266] Parties must ask an arbitrator for discovery first and if the arbitrator declines, the buck almost always will stop there.

As a last resort, both the TAA and the FAA allow parties, after an arbitration award has been issued, to ask a court to vacate the award on the basis that the arbitrator refused to hear evidence material to the controversy.[267] A party not permitted to conduct basic discovery could argue that he or she had not been allowed to put forth material evidence, but it is always difficult to demonstrate the materiality of evidence a party has not been allowed to discover and the cases on vacatur of arbitral awards require courts to interpret these statutory provisions with a strong eye towards enforcement of arbitral awards. We will discuss vacating awards later on this paper.

C. What Can I Do with an Arbitral Order Compelling Discovery?

1. The Legal Basis for Court Enforcement of Arbitral Orders Compelling Discovery

In Texas, a party to an arbitration is authorized by the TAA to apply for a court order "to require compliance by an adverse party or any witness with an order made under this chapter by the arbitrators during the arbitration."[268]

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[264] *CPR Rules for Non-Administered Arbitration* (effective November 1, 2007), *available at* http://www.cpradr.org/ClausesRules/2007CPRRulesforNonAdministeredArbitration/tabid/125/Default.aspx#11.

[265] *Id.*

[266] *See* Transwestern Pipeline Co. v. Blackburn, 831 S.W.2d 72, 78 (Tex. App. – Amarillo 1992, orig. proceeding) (discussing that discovery is allowed only at the discretion of the arbitrator).

[267] *See* TEX. CIV. PRAC. & REM. CODE §171.088(a)(3)(C); 9 U.S.C. §10(a)(3).

[268] TEX. CIV. PRAC. & REM. CODE §171.086(b)(2). Recently, the Texas Supreme Court decided whether the trial court abused its discretion by permitting discovery on damage calculations and other potential defendants, instead of ruling on the motion to compel arbitration. *See* In re Houston Pipe Line Co., No. 08-0800, 2009 Tex. LEXIS 468 (Texas 2009). Pre-arbitration discovery is authorized under the Texas Arbitration Act, the court noted, when a court lacks sufficient information on the scope of the arbitration provision, and therefore, cannot make a decision on the motion to compel arbitration. *Id.* However, the court concluded that this is not the case because determinations of liability must be answered by the arbitrator. *Id.* The court pointed out that a party cannot avoid

The TAA also provides arbitrators with the authority to order depositions and to issue subpoenas to require either the attendance of witnesses or the production of documents or other evidence.[269] In other words, once a party asks for and receives an arbitral order compelling discovery, the TAA provides that party with a basis by which the party can ask for court enforcement of the order.

The FAA is less specific than the TAA in terms of what it explicitly authorizes arbitrators to do, but Section 7, which authorizes arbitrators to order the attendance of witnesses and the production of documents, has for the most part also been interpreted to allow arbitrators to order discovery.[270] If a case arises where a party tries to take the position that the FAA does not specifically authorize arbitral depositions, so long as the arbitration is pending in Texas, one could argue that the TAA authorizes the depositions because the FAA does not always or necessarily preempt the TAA.

As a threshold matter, a party seeking to compel arbitral discovery should consider whether or not the FAA or the TAA applies to the case. The first place to look is the arbitration clause itself. Parties are free to specify which statute should apply in an arbitration clause. If the arbitration clause is silent as to which statute applies, the clause can be said to potentially invoke both federal and state law.[271] In order to determine if the FAA can apply in a state-court proceeding, Texas courts look to the relationship between the parties and extend the FAA "to any contract affecting commerce, as far as the Commerce Clause of the United States Constitution will reach." [272]

In other words, the FAA can be said to apply to many disputes, given the state of current Commerce Clause jurisprudence. For example, in *Nexion* the Texas Supreme Court found the FAA applied to a Texas medical malpractice case brought by a Texan against Texans in a Texas state court for torts committed in Texas because Medicare had paid for some of the plaintiff's medical expenses.[273]

The simple fact that the FAA can be said to apply to a dispute does not deprive a Texas Court of TAA jurisprudence. The TAA and the FAA can simultaneously apply to a dispute and the FAA only preempts the TAA in cases where the TAA is inconsistent with the FAA.[274] In other words, most Texas litigants will be able to choose which statute they wish to apply, whether or not the federal courts have jurisdiction over the claim, since the FAA is designed to be enforceable and enforced in state courts. Indeed, the FAA itself does not confer federal question jurisdiction. In order to be brought in federal court, a petition to compel arbitration under the FAA must have some independent basis for federal court jurisdiction. [275]

All of this means that since the FAA does not specifically preclude discovery, including depositions (and most courts have found that Section 7 specifically allows for discovery), the fairly general Section 7 should not preempt the more specific but not inconsistent TAA. There is no case on this of which we are aware, but the argument should be in line with the current case law in these areas.

Finally, in the world of international arbitration Chapter 172 of the Texas Civil Practice and Remedies Code, like the TAA, allows arbitrators to issue interim awards and allows parties to ask district courts to enforce those awards.[276] Additionally, the TIAA specifically adopts Section 171.051 of the TAA which in turn specifically empowers an arbitrator to issue subpoenas for documents or witnesses.[277] Interestingly, the TIAA does not adopt Section 171.050 of the TAA, which specifically empowers arbitrators to order depositions. However, other portions of the TIAA give arbitrators broad discretion to fashion procedural rules for arbitrations within the confines of the

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arbitration by merely alleging that there may be other potential defendants. *Id.* Accordingly, the court directed the trial court to vacate the discovery order and rule on the motion to compel arbitration. *Id.*

[269] *See* TEX. CIV. PRAC. & REM. CODE §§171.050 and 171.051. The Texas General Arbitration Act has no provision for interrogatories or requests for admissions. Courts have reasoned that limited discovery in arbitration make arbitration under the TAA "an inexpensive, rapid alternative to traditional litigation." Glazer's Wholesale Distributors, Inc. v. Heineken USA, Inc., 95 S.W.3d 286, 295-96 (Tex. App.—Dallas 2001, pet. dism'd by agrm't) (citing Prudential Securities, Inc. v.Marshall, 909 S.W.2d 896, 900 (Tex. 1995) (orig. proceeding)).

[270] 9 U.S.C. §7; *see e.g.,* Recognition Equip., Inc. v. NCR Corp., 532 F.Supp. 271, 273-74 (N. Dist. TX 1981).

[271] In re D. Wilson Construction Co., 196 S.W.3d 774, 779 (Tex. 2006) ("Contracts that reference neither the Federal Arbitration Act, 9 U.S.C.S. §§ 1-16, nor the Texas Arbitration Act, Tex. Civ. Prac. & Rem. Code Ann. §§ 171.001-171.098, but merely note that the contracts shall be governed by the law of the place where the project is located, invoke federal and state law.").

[272] In re Nexion Health at Humble, Inc., 173 S.W.3d 67, 69 (Tex. 2005), quoting In re: L&L Kempwood Assocs., L.P., 9 S.W.3d 125, 127 (Tex. 1999); citing Citizens Bank v. Alafabco, Inc., 539 U.S. 52, 56-57, 123 S.Ct. 2037, 156 L.Ed.2d 46 (2003).

[273] *Nexion*, 173 S.W.3d at 69.

[274] *Wilson*, 196 S.W.3d at 779-780.

[275] 9 U.S.C. §4.

[276] TEX. CIV. PRAC. & REM. CODE §§172.083 and 172.175.

[277] TEX. CIV. PRAC. & REM. CODE §172.105.

arbitration agreement itself.[278] That being the case, if a party to an international arbitration taking place in Texas obtains an arbitral order compelling a deposition, that party ought to be able to seek an order from a Texas court enforcing the arbitral order under the TIAA.

2. What You Might Do if the Arbitrator Orders Discovery that you Strongly Oppose

There is very little one can do if an arbitrator orders discovery against the strong wishes of a party. If the discovery sought is clearly inconsistent with the rules governing that particular arbitration, the party may later argue that the arbitrator exceeded his or her authority when ordering the discovery, which in turn is a basis for opposing entry of the arbitral award as a judgment under either the TAA or the FAA.[279]Any party seeking to prevent the entry of an arbitral award as a judgment faces a remarkably steep burden, however, as arbitral awards are for the most part not appealable in Texas.

The various statutory mechanisms set out above to seek court intervention for enforcement of arbitral awards do, by their nature, take time so a party theoretically could at least seek to delay complying with an arbitral order compelling discovery but at some point that party needs to consider the wisdom of such a tactic. The same arbitrator who issued the order will be the arbitrator who will be deciding the case and that arbitrator is given spectacular flexibility in weighing the evidence and making his or her decision by the applicable statutory and case law. The final decision will be, for the most part, impossible to appeal. Irritating or agitating the arbitrator, even if the arbitrator is wrong, is not advisable. In Texas, a party may seek *mandamus* help as a last resort in the face of an overly onerous discovery order when litigating a case. No such remedy exists in the arbitral setting. So, while it may be more difficult for a party to an arbitration to obtain an order compelling discovery, once the order is obtained that party may well be in a stronger position than the party would be at the courthouse.

3. Can the Arbitrator Compel Discovery from Non-Parties?

1. Federal Arbitration Act

The question of when one party to an arbitration may acquire the necessary evidence from a third party (a non-party to the arbitration) has become a common theme in arbitration. Over the past decade, courts have begun to establish limitations on arbitral powers within the context of third party discovery.[280]

Section 7 of the FAA states that the arbitrators: "may summon in writing any person to attend before them or any of them as a witness and in a proper case to bring with him or them any book, record, document, or paper which may be deemed material as evidence in the case."[281] The summons issued by arbitrators "shall be served in the same manner as subpoenas to appear and testify before the court" and shall be enforced "upon petition [to] the United States district court for the district in which such arbitrators, or a majority of them, are sitting" whereby the district court "may compel the attendance of" or "punish said person or persons for contempt in the same manner provided by law . . . in the courts of the United States."[282]

The FAA is unclear as to the scope of the discovery it authorizes. While Section 7 has been interpreted by most courts to empower arbitrators to subpoena non-parties to produce documents at an arbitration **hearing**,[283] some courts have disagreed as to whether Section 7 grants an arbitrator authority to compel a non-party to attend a **prehearing**

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[278] TEX. CIV. PRAC. & REM. CODE §172.103.
[279] TEX. CIV. PRAC. & REM. CODE §171.088(a)(3); 9 U.S.C. §10(a)(4).
[280] For an article providing an excellent review of arbitration discovery and non-parties, *see* Rau, Alan Scott Rau, *Evidence and Discovery in American Arbitration: The Problem of 'Third Parties'. American Review of International Arbitration*, Fall 2009; U of Texas Law, Public Law Research Paper No. 146, *available at* http://ssrn.com/abstract=1397617.
[281] 9 U.S.C. § 7.
[282] *Id.*
[283] *See e.g.*, In re Sec. Life Ins. Co. of Am., 228 F. 3d 865, 870 (8th Cir. 2000) (acknowledging "an arbitration panel's power [under the FAA] to subpoena relevant documents for production at a hearing"); Festus & Helen Stacy Found. v. Merrill Lynch, Pierce Fenner & Smith Inc., 432 F. Supp. 2d 1375, 1379 (N.D. Ga. 2006) (holding that the district court has jurisdiction to order non-party private equity firm to comply with subpoenas issued under the Federal Arbitration Act); Amgen Inc. v. Kidney Ctr. of Del. County, Ltd., 879 F. Supp. 878, 883 (N.D. Ill. 1995) (a district court in the Northern District of Illinois held that an arbitrator's subpoena duces tecum, issued to a third person not party to the arbitration proceeding and located outside the district in which the arbitrator sat or beyond 100 miles of the site of the arbitration, was valid and enforceable); Meadows Indem. Co. v. Nutmeg Ins. Co., 157 F.R.D. 42, 45 (M.D. Tenn. 1994) (stating that "[T]he power of the panel to compel production of documents from third-parties for the purposes of a hearing implicitly authorizes the lesser power to compel such documents for arbitration purposes prior to a hearing.").

deposition.[284] Currently, a circuit split exists with regard to an arbitrators' authority to compel discovery from non-parties under the FAA.

In *Am. Fed'n of Television and Radio Artists, AFL-CIO v. WJBK-TV*,[285] citing analogous cases interpreting Section 7 of the FAA, the Sixth Circuit Court of Appeals held that under Section 301 of the Labor Management Relations Act of 1947 an arbitrator has the power to compel a non-party to produce material records either before or during an arbitration hearing.

In 1999, the Fourth Circuit Court of Appeals held in *COMSAT Corp. v. National Science Foundation*[286] that an arbitrator may not compel a third party to comply with an arbitral subpoena for prehearing discovery **unless** there is a "special need" for the documents. The Court did not define "special need" except to say that "at a minimum, a party must demonstrate that the information it seeks is otherwise unavailable." The Court reasoned that the "hallmark of arbitration - and a necessary precursor to its efficient operation - is a limited discovery process." The Court made no distinctions between depositions and document production.

On the other hand, in 2000 the Eight Circuit Court of Appeals held in *Arbitration Between Security Life Insurance Company of America and Duncanson & Holt, Inc.*, [287] that an arbitrator impliedly has the power under Section 7 of the FAA to compel pre-hearing discovery from non-parties because the FAA authorizes arbitrators to subpoena non-parties to bring documents to the arbitration in conjunction with their testimony.

Perhaps the narrowest interpretation of Section 7 comes from the Third Circuit Court of Appeals. In 2004, in *Hay Group, Inc. v. E.B.S. Acquisition Corp.*,[288] the Circuit stated that pursuant to the "unambiguous" language of Section 7 of the FAA, an arbitrator's subpoena power is limited to "situations in which the non-party has been called to appear in the physical presence of the arbitrator and to hand over the documents at that time."[289] The Court held that an arbitrator lacks authority to compel **prehearing** discovery from nonparties, whether it be deposition testimony or document production.

In 2008, the Second Circuit Court of Appeals joined the Third Circuit and held that Section 7 does not authorize an arbitrator to compel pre-hearing document discovery from non-parties to the arbitration. In *Life Receivables Trust v. Syndicate 102 at Lloyd's of London*,[290] the Court, citing Section 7, explained that arbitrators may "order 'any person' to produce documents so long as that person is called as a witness at a hearing." The Court also noted that a non-party could be subpoenaed to produce documents at a preliminary hearing on non-merits issues before one or more arbitrators.[291]

2. International Arbitration

Under 28 U.S.C. Section 1782 (Assistance to Foreign and International Tribunals and to Litigants Before such Tribunals), a federal court has authority to compel discovery for many types of proceedings conducted outside the United States:

> The 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.[292]

[284] Rau, *supra* note 46.
[285] In Am. Fed'n of Television and Radio Artists, AFL-CIO v. WJBK-TV, 164 F.3d 1004 (6th Cir. 1999).
[286] Comsat Corp. v. Nat'l Sci. Found., 190 F.3d 269, 275 (4th Cir. 1999).
[287] Arbitration Between Security Life Insurance Company of America and Duncanson & Holt, Inc., 228 F.3d 865 (8th Cir. 2000).
[288] Hay Group, Inc. v. E.B.S. Acquisition Corp., 360 F. 3d 404 (3rd Cir. 2004).
[289] *Id.* at 407.
[290] Life Receivables Trust v. Syndicate 102 at Lloyd's of London, 549 F3d 210 (2d Cic. 2008).
[291] *See Id*. More recently, a federal district court from Dallas followed the approach of the Second and Third Circuit holding that the FAA does not allow non-party subpoenas for pre-hearing document discovery, but only permits such subpoenas if they require the non-party to appear at an arbitration hearing and to bring the documents to the hearing. Empire Financial Group, Inc. v. Penson Financial Services, Inc., 2010 U.S. Dist. LEXIS 18782 (N.D. Tex. Mar. 3, 2010).
[292] 28 U.S.C. § 1782(a) (2000).

The statute does not define the term "foreign or international tribunal." In 1999, the Second[293] and Fifth[294] Circuits held that "foreign or international tribunals" **do not include** private arbitration panels. In 2004, the U.S. Supreme Court interpreted the language of Section 1782 in *Intel Corp. v. Advances Microdevices, Inc* [295] The Court did not reach the question of arbitral tribunals, however.[296]

In 2009, the Fifth Circuit, in the unpublished opinion *El Paso Corporation v. La Comision Ejecutiva*, reaffirmed *Republic of Kazakhstan* and held that Section 1782 does not apply for a discovery motion for use in a private international arbitration.[297] La Comision Ejecutiva Hidroelectrica Del Rio Lempa (CEL) is a state-owned utility company in El Salvador and Nejapa Power Company (NPC) is a utility company related to El Paso Corporation (El Paso), an energy corporation based in Houston, Texas.[298] CEL and NPC were arbitrating a contract dispute in Geneva, Switzerland, under the arbitration rules of the United Nations Commission on International Trade Law (UNCITRAL), El Salvadoran substantive law, and Swiss procedural law.[299] CEL sued to obtain discovery (production of documents and depositions) from El Paso (a non- party to the arbitration) pursuant to 28 U.S.C. Section 1782 to use in its international private arbitration proceeding with NPC.[300]

The Texas District Court denied CEL's request for discovery and held that Section 1782 does not apply to discovery for use in a *private* international arbitration.[301] The Court also held that, even if it did have the authority under Section 1782, "it would not [grant the application], out of respect for the efficient administration of the Swiss arbitration."[302] The Court granted a Rule 60(b) motion for relief from a judgment or order, vacated its *ex parte* order and quashed the outstanding discovery requests.[303] CEL appealed.[304]

The Fifth Circuit first considered El Paso's argument that CEL's appeal was moot.[305] Because the evidentiary hearing for the arbitration had concluded and the panel had closed the evidence, El Paso argued that "there is no longer a live case or controversy."[306] The Court noted that under UNCITRAL arbitration rules, an arbitral tribunal may reopen the hearings at any time before the award is made.[307] If CEL discovered new evidence with a Section 1782 application, the Court reasoned, that evidence could still be considered if the tribunal reopened the evidentiary hearing.[308] The Court concluded that a live controversy still existed and proceeded to address the merits of the appeal.[309]

Next, the Fifth Circuit reviewed the granting of the Rule 60(b) motion. [310] The Court stated that "[s]uch a motion can be granted for a number of reasons, including mistake, inadvertence, surprise, or excusable neglect" and "any other reason that justifies relief. The law of this circuit permits a trial judge, in his discretion, to reopen a judgment on the basis of an error of law." [311] The Court noted that in *Republic of Kazakhstan,* the court held "a 'tribunal' within the meaning of Section 1782 did not include a private international arbitral tribunal and thus Section 1782 did not apply to discovery sought for use in such a tribunal."[312] CEL argued that *Republic of Kazakhstan* was no longer controlling in light of the Supreme Court's decision in *Intel Corp. v. Advanced Micro Devices.*[313] However, the Fifth Circuit was not persuaded by CEL's argument.[314] The Court concluded that the issue of whether a private

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[293] Nat'l Broad. Co. v. Bear Stearns & Co., 165 F3d 184 (2d Cir. 1999).
[294] Kazakhstan v. Biedermann Int'l, 168 F.3d 880 (5th Cir. 1999).
[295] Intel Corp. v. Advanced Micro Devices, Inc, 542 U.S. 241(2004).
[296] *See* Jessica Weekley, *Comment: Discovering Discretion: Applying Intel to § 1782 Requests for Discovery in Arbitration*, CASE W. RES. 535 (2009); Walter B. Stahr, *Discovery Under 28 U.S.C. § 1782 for Foreign and International Proceedings*, 30 VA. J. INT'L. L. 597, 615-19 (1990).
[297] El Paso Corporation v. La Comision Ejecutiva, No. 08-20771, 2009 U.S. App. LEXIS 17596 (5th Cir. 2009).
[298] *Id.* at *2.
[299] *Id.*
[300] *Id.*
[301] *Id.* at *4.
[302] *Id.*
[303] *Id.*
[304] *Id.*
[305] *Id.* at *4-*5.
[306] *Id.*
[307] *Id.* at *5-*6.
[308] *Id.*
[309] *Id.* at *6.
[310] *Id.*
[311] *Id.*
[312] *Id.* at *7 citing *Republic of Kazakhstan v. Biedermann International*, 168 F.3d 880 (5th Cir. 1999).
[313] *Id.* citing *Intel Corp. v. Advanced Micro Devices, Inc*, 542 U.S. 241, 258 (2004).
[314] *Id.* at *8-*9.

international arbitration tribunal qualifies as a "tribunal" under Section 1782 was not before the U.S. Supreme Court in *Intel.*[315]

Citing *Republic of Kazakhstan,* the Court explained that "empowering parties in international arbitrations to seek ancillary discovery through federal courts could destroy arbitration's principal advantage as a speedy, economical, and effective means of dispute resolution if the parties succumb to fighting over burdensome discovery requests far from the place of arbitration."[316]Accordingly, the Court denied El Paso's motion to dismiss the appeal as moot and affirmed the district court's grant of the Rule 60(b) motion.[317]

D. Guidelines on Discovery in Arbitration

The Dispute Resolution Section of the New York State Bar Association recently issued a report on Arbitration Discovery in Domestic Commercial Cases."[318] The objective of the report was to issue some guidelines regarding use to counsel and arbitrators to best handle the unpredictability issue of discovery proceedings in arbitration.[319] The report provides ten precepts to help enable arbitrators to control the discovery process: (1) Good Judgment of the Arbitrator, (2) Early Attention to Discovery by the Arbitrator, (3) Party Preferences, (4) E-discovery, (5) Legal Considerations, (6) Arbitrator Tools (7) Artfully Drafted Arbitration Clauses, (8) Depositions, (9) Discovery Disputes, and (10) Discovery & Other Procedural Aspects of Arbitration.[320]

In addition, the report includes an exhibit with advice on relevant factors for arbitrators to determine the appropriate scope of arbitration discovery:

Nature of the Dispute

The factual context of the arbitration and of the issues in question with which the arbitrator should become conversant before making a decision about discovery.

The amount in controversy.

The complexity of the factual issues.

The number of parties and diversity of their interests.

Whether any or all of the claims appear, on the basis of the pleadings, to have sufficient merit to justify the time and expense associated with the requested discovery.

Whether there are public policy or ethical issues that give rise to the need for an in depth probe through relatively comprehensive discovery.

Whether it might be productive to initially address a potentially dispositive issue which does not require extensive discovery.

Agreement of the Parties

Agreement of the parties, if any, with respect to the scope of discovery.

Agreement, if any, by the parties with respect to duration of the arbitration from the filing of the arbitration demand to the issuance of the final award.

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[315] *Id.*
[316] *Id.*
[317] *Id.* at *9.
[318] New York State Bar Association Dispute Resolution Section Arbitration Committee, *Report on Arbitration Discovery in Domestic Commercial Cases* (2009), *available at* http://www.nysba.org/Content/NavigationMenu42/April42009HouseofDelegatesMeetingAgendaItems/DiscoveryPreceptsReport.pdf.
[319] *Id.*
[320] *Id.*

The parties' choice of substantive and procedural law and the expectations under that legal regime with respect to arbitration discovery.

Relevance and Reasonable Need for Requested Discovery

Relevance of the requested discovery to the material issues in dispute or the outcome of the case.

Whether the requested discovery appears to be sought in an excess of caution, or is duplicative or redundant.

Whether there are necessary witnesses and/or documents that are beyond the tribunal's subpoena power.

Whether denial of the requested discovery would, in the arbitrator's judgment (after appropriate scrutinizing of the issues), deprive the requesting party of what is reasonably necessary to allow that party a fair opportunity to prepare and present its case.

Whether the requested information could be obtained from another source more conveniently and with less expense or other burden on the party from whom the discovery is requested.

To what extent the discovery sought is likely to lead, as a practical matter, to a case-changing "smoking gun" or to a fairer result.

Whether broad discovery is being sought as part of a litigation tactic to put the other side to great expense and thus coerce some sort of result on grounds other than the merits.

The time and expense that would be required for a comprehensive discovery program.

Whether all or most of the information relevant to the determination of the merits is in the possession of one side.

Whether the party seeking expansive discovery is willing to advance the other side's reasonable costs and attorneys' fees in connection with furnishing the requested materials and information.

Whether a limited deposition program would be likely to: (i) streamline the hearing and make it more cost-effective; (ii) lead to the disclosure of important documents not otherwise available; or (iii) result in expense and delay without assisting in the determination of the merits.

Privilege and Confidentiality

Whether the requested discovery is likely to lead to extensive privilege disputes as to documents not likely to assist in the determination of the merits.

Whether there are genuine confidentiality concerns with respect to documents of marginal relevance. Whether cumbersome, time-consuming procedures (attorneys' eyes only, and the like) would be necessary to protect confidentiality in such circumstances.

Characteristics and Needs of the Parties

The financial and human resources the parties have at their disposal to support discovery, viewed both in absolute terms and relative to one another.

The financial burden that would be imposed by a broad discovery program and whether the extent of the burden outweighs the likely benefit of the discovery.

> Whether injunctive relief is requested or whether one or more of the parties has some other particular interest in obtaining a prompt resolution of all or some of the controversy.
>
> The extent to which the resolution of the controversy might have an impact on the continued viability of one or more of the parties.[321]

Based on the New York report, the Los Angeles Bar published the following seven recommendations for a more effective discovery:

> 1) Draft or select arbitration clauses that limit discovery and that provide arbitrators with the ability to exercise their judgment to control the process. Do not incorporate the Code of Civil Procedure and broad discovery. An arbitrator can advise against invoking these rules but lacks the authority to control the process. The arbitration clause you draft will determine the arbitration you get.
>
> 2) Designate an arbitration provider that uses rules that are compatible with your goal of an efficient, cost-effective arbitration, and allow high-quality arbitrators to actively manage it from start to finish.
>
> 3) Focus document production requests narrowly with respect to relevant date ranges, number of custodians, and material evidence. Eliminate common boilerplate language such as wide-ranging demands for "all documents that refer to...."
>
> 4) The parties should cooperate in producing documents in a convenient and usable (i.e., searchable) format.
>
> 5) Agree upon search terms and use sampling to confirm the effectiveness of the terms. Cooperate in agreeing to the clawback of inadvertently produced privileged documents, eliminating the necessity for extensive and detailed review of all the electronic files being produced. Document review is incredibly expensive and often accomplishes little if the search terms have been properly defined.
>
> 6) Institute cost shifting if a requesting party demands broad and expensive production. Grant the arbitrator the authority to allocate costs after the usefulness of the production has been determined.
>
> 7) Balance need and burden, and give the arbitrator the ability to do so. Educate your client on the benefits of cost-effective arbitration and how it differs from litigation. [322]

In response to criticism that arbitration has become as time consuming and costly as litigation, several institutions have published arbitration guidelines recently. The International Chamber of Commerce (ICC) Commission on Arbitration has published a report entitled “Techniques for Controlling Time and Costs in Arbitration.” The report covers guidelines for the creation of an arbitration agreement, selection of an arbitrator and preliminary procedural issues, as well as subsequent procedural issues.[323]

Similarly, the International Centre for Dispute Resolution (ICDR), the international arm of the American Arbitration Association has promulgated its “ICDR Guidelines for Arbitrators Concerning Exchanges of Information.”[324] The Guidelines provide that "while arbitration must be a fair process, care must also be taken to prevent the importation of procedural measures and devices from different court systems, which may be considered conducive to fairness within those systems, but which are not appropriate to the conduct of arbitrations in an international context and which are inconsistent with an alternative form of dispute resolution that is simpler, less

[321] *Id.*
[322] Kenneth C. Gibbs and Barbara Reeves Neal, *Closing Argument: It’s Time to Fix Arbitration Discovery*, 32 LOS ANGELES LAWYER 48, January, 2010.
[323] *See* ICC, *Techniques for Controlling Time and Costs in Arbitration, available at* http://www.iccwbo.org/uploadedFiles/TimeCost_E.pdf.
[324] *See ICDR Guidelines for Arbitrator Concerning Exchanges of Information, available at* http://www.adr.org/si.asp?id=5288.

expensive, and more expeditious."[325] Under the Guidelines, the only documents to be exchanged are those on which a party relies.[326] The Guidelines address electronic documents, and state:

> When documents to be exchanged are in electronic form, the party in possession of such documents may make them available in the form (which may be paper copies) most convenient and economical for it, unless the tribunal determines, on application and for good cause, that there is a compelling need for access to the documents in a different form. Requests for documents maintained in an electronic form should be narrowly focused and structured to make searching for them as economical as possible. The Tribunal may direct testing or other means of focusing and limiting any search. [327]

Finally, the CPR International Institute for Conflict Prevention & Resolution has also issued its "Global Rules for Accelerated Commercial Arbitration" which, when agreed by the parties, provides for one neutral with significant new powers to control discovery and requires rendering the award within six (6) months of the selection of the Arbitral Tribunal.[328]

V. Evidence in Arbitration

A. Which Rules of Evidence Apply?

Do the formal rules of evidence have a place in the arbitration context? Well it depends on the arbitrator.

1. Federal Arbitration Act

The FAA only mentions 'evidence' in Section 10(c), which states that an award may be vacated where arbitrators refused "to hear evidence pertinent and material to the controversy."[329] Case law supports the proposition that "the arbitrator is the judge of the relevance and admissibility of evidence introduced in an arbitration proceeding."[330] The principles which may be deduced from these cases are:

- Arbitrators are the judges of relevance and materiality;
- Arbitrators may reject even relevant and material evidence in order to streamline the process; and
- Arbitrators' decision on these subjects are final and may not be overturned unless they amount to a failure to provide a fundamentally fair hearing.[331]

2. Texas Rules of Evidence

The Texas Rules of Evidence apply only in court proceedings.[332] "It is an established principle of arbitration law that the arbitrator is the judge of the relevance and admissibility of evidence introduced in an arbitration

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[325] *Id.*
[326] *Id.*
[327] *Id.*
[328] *See Global Rules for Accelerated Arbitration* (effective August 20, 2009), *available at* http://www.cpradr.org/ClausesRules/GlobalArbitrationRules/tabid/422/Default.aspx
[329] *See* 9 U.S.C. § 10(3).
[330] *See* Bruce A. McAlister & Amy Bloom, *Use of Evidence in Admiralty Proceedings: Evidence in Arbitration*, 34 J. MAR. L. & COM. 35, 35 (2003) citing Castleman v. AFC Enterprises, Inc., 995 F. Supp. 649, 653 (N.D. Tex. 1997). *See, e.g.*, Robbins v. Day, 954 F.2d 679, 685 (11th Cir. 1992); Forsythe Int'l SA v. Gibbs Oil Co., 915 F.2d 1017 (5th Cir. 1990) (misconduct by counsel in stone-walling discovery not basis for overturning award); Sunshine Mining Co. v. United Steelworkers, 823 F.2d 1289 (9th Cir. 1987); Legion Ins. Co. v. Ins. Gen. Agency, Inc., 822 F.2d 541, 543 (5th Cir. 1987) (arbitration requires "expeditious and summary hearing, with only restricted inquiry into factual issues"); Grahams Service, Inc. v. Teamsters Local 975, 700 F.2d 420 (8th Cir. 1982) (exclusion of evidence not improper); Bell Aerospace Co. v. Local 516, 500 F.2d 921 (2d Cir. 1974) (exclusion of affidavit not improper); Reed & Martin, Inc. v. Westinghouse Elec. Corp., 439 F.2d 1268 (2d Cir. 1971); Newark Stereotypers Union No. 18 v. Newark Morning Ledger Co., 397 F.2d 594, 599 (3d Cir.) (refusal to investigate witnesses' refusal to testify not improper); Warth Line, Ltd. v. Merinda Marine Co., 778 F. Supp. 158, 1992 AMC 1406 (S.D.N.Y. 1991) Essex Cement Co. v. Italmare SpA, 763 F. Supp. 55, 1991 AMC 2406 (S.D.N.Y. 1991); Ohio Center for Dance Columbus Festival Ballet v. BLO Prod., Inc., 760 F. Supp. 677 (S.D. Ohio 1991); Fairchild & Co. v. Richmond, Fredericksburg & Potomac R.R. Co., 516 F. Supp. 1305 (D.D.C. 1981) ("arbitrators are charged with the duty of determining what evidence is relevant"); Cobec Brazilian Trading & Warehousing Corp. v. Isbrandtsen, 524 F. Supp. 7, 10, 1982 AMC 1355, 1357-58 (S.D.N.Y, 1980) (no denial of opportunity to present evidence). But see Hoteles Condado Beach v. Union of Tranquistes Local 901, 763 F.2d 34 (1st Cir. 1985) (exclusion of evidence improper).
[331] *See* McAlister, *supra* note 97 at 38.
[332] *See* Castleman v. AFC Enters., Inc., 995 F. Supp. 649, 653-54 (N.D. Tex. 1997) (holding that arbitration proceedings are not governed by formal rules of evidence).

proceeding."[333] Thus, arbitrators have a great deal of discretion to exclude evidence as redundant or otherwise unnecessary to the decision-making process.[334]

3. Texas International Arbitration Act

The TIAA provides that "[t]he power of the arbitration tribunal under Section 172.103(b) includes the power to determine the admissibility, relevance, materiality, and weight of any evidence."[335] The TIAA also mentions the power of an arbitral tribunal to appoint experts:

> **§ 172.116. Appointed Expert**
>
> (a) Except as agreed by the parties, the arbitration tribunal may:
>
> (1) appoint an expert to report to it on a specific issue to be determined by the tribunal; and
>
> (2) require a party to:
>
> (A) give the expert relevant information; or
>
> (B) produce or provide access to relevant documents, goods, or other property.
>
> (b) Except as agreed by the parties, if a party requests or if the arbitration tribunal considers it necessary, the expert shall, after delivery of a written or oral report, participate in an oral hearing at which each party may:
>
> (1) question the expert; and
>
> (2) present an expert witness on the issue.[336]

4. American Arbitration Association

The AAA's Rules for Commercial Arbitrations includes the following rules of evidence:

> **R-31. Evidence**
>
> (a) The parties may offer such evidence as is relevant and material to the dispute and shall produce such evidence as the arbitrator may deem necessary to an understanding and determination of the dispute. Conformity to legal rules of evidence shall not be necessary. All evidence shall be taken in the presence of all of the arbitrators and all of the parties, except where any of the parties is absent, in default or has waived the right to be present.
>
> (b) The arbitrator shall determine the admissibility, relevance, and materiality of the evidence offered and may exclude evidence deemed by the arbitrator to be cumulative or irrelevant.
>
> (c) The arbitrator shall take into account applicable principles of legal privilege, such as those involving the confidentiality of communications between a lawyer and client.

[333] *See Id.* at 653 (citing Cordis Corp. v. C.R. Bard, Inc., 1993 U.S. Dist. LEXIS 20445, 1993 WL 723844 *3, No. H-92-1623 (S.D. Tex Mar. 11, 1993)).
[334] See Id. (citing Totem Marine Tug & Barge, Inc. v. North American Towing, Inc., 607 F.2d 649, 651 (5th Cir. 1979)).
[335] TEX. CIV. PRAC. & REM. CODE ANN. § 172.104.
[336] *Id.*

(d) An arbitrator or other person authorized by law to subpoena witnesses or documents may do so upon the request of any party or independently.[337]

R-32. Evidence by Affidavit and Post-hearing Filing of Documents or Other Evidence

(a) The arbitrator may receive and consider the evidence of witnesses by declaration or affidavit, but shall give it only such weight as the arbitrator deems it entitled to after consideration of any objection made to its admission.

(b) If the parties agree or the arbitrator directs that documents or other evidence be submitted to the arbitrator after the hearing, the documents or other evidence shall be filed with the AAA for transmission to the arbitrator. All parties shall be afforded an opportunity to examine and respond to such documents or other evidence.[338]

In addition, the AAA International Rules contain the following provision regarding experts:

Article 22. Experts

1. The tribunal may appoint one or more independent experts to report to it, in writing, on specific issues designated by the tribunal and communicated to the parties.

2. The parties shall provide such an expert with any relevant information or produce for inspection any relevant documents or goods that the expert may require. Any dispute between a party and the expert as to the relevance of the requested information or goods shall be referred to the tribunal for decision.

3. Upon receipt of an expert's report, the tribunal shall send a copy of the report to all parties and shall give the parties an opportunity to express, in writing, their opinion on the report. A party may examine any document on which the expert has relied in such a report.

4. At the request of any party, the tribunal shall give the parties an opportunity to question the expert at a hearing. At this hearing, parties may present expert witnesses to testify on the points at issue.[339]

5. Judicial Arbitration and Mediation Services

JAMS Rule 22 sets forth the rules concerning evidence in the arbitration hearing as follows:

(d) Strict conformity to the rules of evidence is not required, except that the Arbitrator shall apply applicable law relating to privileges and work product. The Arbitrator shall consider evidence that he or she finds relevant and material to the dispute, giving the evidence such weight as is appropriate. The Arbitrator may be guided in that determination by principles contained in the Federal Rules of Evidence or any other applicable rules of evidence. The Arbitrator may limit testimony to exclude evidence that would be immaterial or unduly repetitive, provided that all Parties are afforded the opportunity to present material and relevant evidence.

(e) The Arbitrator shall receive and consider relevant deposition testimony recorded by transcript or videotape, provided that the other Parties have had the opportunity to attend and cross-examine. The Arbitrator may in his or her discretion consider witness affidavits or other recorded testimony even if the other Parties have not had the opportunity to cross-examine, but will give that evidence only such weight as the Arbitrator deems appropriate.

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[337] *AAA Commercial Arbitration Rules and Mediation Procedures (*amended and effective June 1, 2009), *available at http://www.adr.org/sp.asp?id=22440.*
[338] *Id.*
[339] *AAA International Arbitration Rules* (amended and effective June 1, 2009), *available at* http://www.adr.org/sp.asp?id=33994.

> (f) The Parties will not offer as evidence, and the Arbitrator shall neither admit into the record nor consider, prior settlement offers by the Parties or statements or recommendations made by a mediator or other person in connection with efforts to resolve the dispute being arbitrated, except to the extent that applicable law permits the admission of such evidence.[340]

6. International Chamber of Commerce

ICC Article 20, concerning establishing the facts of the case, states:

> 1
> The Arbitral Tribunal shall proceed within as short a time as possible to establish the facts of the case by all appropriate means.
>
> 2
> After studying the written submissions of the parties and all documents relied upon, the Arbitral Tribunal shall hear the parties together in person if any of them so requests or, failing such a request, it may of its own motion decide to hear them.
>
> 3
> The Arbitral Tribunal may decide to hear witnesses, experts appointed by the parties or any other person, in the presence of the parties, or in their absence provided they have been duly summoned.
>
> 4
> The Arbitral Tribunal, after having consulted the parties, may appoint one or more experts, define their terms of reference and receive their reports. At the request of a party, the parties shall be given the opportunity to question at a hearing any such expert appointed by the Tribunal.
>
> 5
> At any time during the proceedings, the Arbitral Tribunal may summon any party to provide additional evidence.
>
> 6
> The Arbitral Tribunal may decide the case solely on the documents submitted by the parties unless any of the parties requests a hearing.
>
> 7
> The Arbitral Tribunal may take measures for protecting trade secrets and confidential information.[341]

7. International Bar Association

Article 9 of the IBA Rules on the Taking of Evidence in International Commercial Arbitration states the following regarding the admissibility and assessment of evidence:

> 1. The Arbitral Tribunal shall determine the admissibility, relevance, materiality and weight of evidence.
>
> 2. The Arbitral Tribunal shall, at the request of a Party or on its own motion, exclude from evidence or production any document, statement, oral testimony or inspection for any of the following reasons:

[340] *JAMS Comprehensive Arbitration Rules and Procedures* (effective July 15, 2009), *available at* http://www.jamsadr.com/rules-comprehensive-arbitration/.
[341] *ICC Rules of Arbitration* (effective January 1, 2008), *available at* http://www.iccwbo.org/uploadedFiles/Court/Arbitration/other/rules_arb_english.pdf.

(a) lack of sufficient relevance or materiality;
(b) legal impediment or privilege under the legal or ethical rules determined by the Arbitral Tribunal to be applicable;
(c) unreasonable burden to produce the requested evidence;
(d) loss or destruction of the document that has been reasonably shown to have occurred;
(e) grounds of commercial or technical confidentiality that the Arbitral Tribunal determines to be compelling;
(f) grounds of special political or institutional sensitivity (including evidence that has been classified as secret by a government or a public international institution) that the Arbitral Tribunal determines to be compelling; or
(g) considerations of fairness or equality of the Parties that the Arbitral Tribunal determines to be compelling.

3. The Arbitral Tribunal may, where appropriate, make necessary arrangements to permit evidence to be considered subject to suitable confidentiality protection.[342]

Additional IBA Articles of interest within this set of rules are: Documents (Art. 3), Witnesses of Fact (Art. 4), Party Appointed Experts (Art. 5), Tribunal-Appointed Experts (Art. 6), On Site Inspection (Art. 7) and Evidentiary Hearing (Art. 8).[343]

B. Guidelines on Evidence in Arbitration

Alfred G. Feliu, an experienced arbitrator and mediator, wrote an excellent paper discussing evidence in arbitration.[344] In the paper, Mr. Feliu provides the following guidelines for litigators to strengthen their evidentiary arguments before an arbitrator:

1. **Mere relevance is not enough; evidence should be both relevant and material.** Arbitration is intended to be an expeditious and inexpensive method of resolving legal disputes. The notion that all relevant evidence, that is not cumulative, is admissible in arbitration is not fully in keeping with this goal. Evidence that is relevant is not always material; in contrast, material evidence is always relevant. The relevance standard is too loose a concept and too wide a door to be the sole measure for the admissibility of evidence in arbitration. Arbitrators who admit all evidence, even if only tangentially material, and litigators who go overboard with their offers of evidence, both act contrary to arbitration's companion goals of expedition and cost-effectiveness.

   To be material, the evidence offered must be probative of a substantial issue in the case. Put another way, if the proof addresses an issue that is not likely to have an impact on the arbitrator's decision, it is not material. Immaterial evidence, however, may be admissible for other purposes, for example, to impeach a witness. Consequently, advocates should be prepared to respond to the arbitrator's question as to the relevance of this evidence or risk a ruling of inadmissibility.

   Take, for example, the evidence offered in an age discrimination case in which the claimant seeks to offer into evidence the ages of employees previously terminated in his department. This evidence is clearly relevant in an age discrimination case. If the employer shows, however, that the previous termination decisions were made by another manager applying different performance criteria, the evidence might not be material to claimant's case. In sum, the requirement of materiality serves to limit the scope of admissible evidence, and produce a more efficient and focused hearing.

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[342] *IBA Rules on the Taking of Evidence in International Commercial Arbitration* (adopted June 1, 1999), *available at* http://www.ibanet.org/Publications/publications_IBA_guides_and_free_materials.aspx.
[343] *See Id*.
[344] *See* Alf Alfred G. Feliu, *Evidence in Arbitration: A Guide for Litigators*, NEW YORK LAW JOURNAL, March 4, 1999, at 3, *available at* http://www.vanfeliu.com/publications/EVIDENCE%20IN%20ARBITRATION1.doc.

2. **Focus less on the admissibility and more on reliability of the evidence.** Arbitrators serve as both judge and jury. They tend to care less about the issue of admissibility of any particular evidence and more about the reliability and weight to be given to it. Long battles over admissibility seem beside the point to most arbitrators and, consequently, they tend to be more willing to admit evidence, even if it has little probative value and will be given little weight. Arbitrators are likely to admit evidence, even if the FRE argues for its exclusion, if the arbitrator determines that the evidence is of some probative value.

3. **Focus on the probative value of admitted evidence, and seek to convince the arbitrator that it should be given greater or lesser weight.** Now that the question of admissibility is behind you, remind the arbitrator that not all evidence was created equal. Point out that certain key evidence in the case will be more reliable and convincing than other evidence. In doing so, look for and emphasize for the arbitrator indicia of reliability or unreliability of the evidence.

   Address such questions as: (i) should the event at issue have been memorable to the witness at the time it occurred? (ii) what were the interests of the witness in testifying, i.e., does the witness have anything to gain by the result of the arbitration; (iii) was the testimony corroborated? (iv) how probable or improbable is it that individuals, in the circumstances described, would act in the manner testified to by the witness?; and (v) is the testimony of the witness internally consistent? By doing so, you will be indirectly turning the simple issue of admissibility into an opportunity to argue the merits of your case to the arbitrator.

4. **Remember at all times that the rules of evidence are not ends in themselves but rather means for eliciting reliable evidence at the hearing**. Litigators are skilled in the nuances of practicing before the courts. Even though the rules of litigation may not be imported fully into the arbitration setting, the skills of a litigator are. The packaging and selling of evidence to a fact-finder is just as essential in arbitration as it is in litigation. What is different are the rules of the game and the expectations of the finder of facts. Recognize at all times that arbitration is designed to reach the merits of the dispute with the least amount of resistance. A successful litigator in this setting is one who uses his or her persuasive skills rather than procedural prowess to present evidentiary arguments to an arbitrator in a winning way.[345]

VI. MOTIONS TO CONFIRM, VACATE OR MODIFY ARBITRATION AWARDS

The criteria a court relies on to confirm, vacate or modify an arbitrator's award differ depending on the character of the arbitration itself. If an arbitration is between Texans and does not involve interstate commerce, the court looks to the Texas General Arbitration Act for its guidance If an arbitration brushes up against the Commerce Clause, then the Federal Arbitration Act is the starting point. If an arbitration is "international," which does not necessarily require that at least one party be foreign, then the reviewing court should break out its copy of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (commonly referred to as the "New York Convention" after the city in which it was enacted). Each of these starting points invokes a slightly different set of rules and interpreting case law, and a potentially different standard of review. This paper will not discuss confirming, vacating, modifying or enforcing international arbitral awards, though that is a fascinating topic worthy of examination.

A. Arbitral Awards Governed by the Federal Arbitration Act

Arbitration provides a final and binding decision that is very difficult to successfully appeal in court. Sections 10 and 11 of the Federal Arbitration Act (FAA) provide the bases for vacatur and modification of arbitration awards. Under Section 10, the grounds to vacate an arbitration award are:

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

[345] *Id.*

(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.[346]

The FAA also provides for modification of an erroneous award:

In either of the following cases the United States court in and for the district wherein the award was made may make an order modifying or correcting the award upon the application of any party to the arbitration --

(a) Where there was an evident miscalculation of figures or an evident material mistake in the description of any person, thing or property referred to in the award.

(b) Where the arbitrators have awarded upon a matter not submitted to them, unless it is a matter not materially affecting the merits of the decision upon the matter submitted.

(c) Where the award is imperfect in matter of form not affecting the merits of the controversy.

The order may modify and correct the award, so as to effect the intent thereof and promote justice between the parties.[347]

The general standard of review a court in the Fifth Circuit employs when considering a motion to vacate an award under the FAA is well-established and severe: "[w]e review de novo an order vacating an arbitration award. Our review of the award itself, however, is exceedingly deferential. We can permit vacatur of an arbitration award only on very narrow grounds."[348] While courts describe the standard of review under the FAA as *de novo*, the review of the award itself (as theoretically opposed to the decision to vacate the award, but the two seem to always conflate) requires a much restricted version of *de novo* review as a "normal" do novo review of an award is grounds for reversal of a vacatur.[349]

1. Award Procured by Corruption, Fraud or Undue Means

Upon proper application by a party, a court may vacate an arbitral award procured by corruption, fraud or other undue means.[350] The Fifth Circuit has interpreted this ground for vacatur "as requiring a nexus between the alleged fraud and the basis for the panel's decision."[351] In other words, a party seeking vacatur must allege more than just fraud during the arbitration process. The allegation must link the alleged fraud to the arbitral award complained of. "The requisite nexus may exist where fraud prevents the panel from considering a significant issue to which it does not otherwise enjoy access."[352]

In the *Forsythe* case, the arbitral panel clearly considered a party's allegations of fraud when making its award.[353]According to the Fifth Circuit, "the panel effectively ruled that the asserted fraud was immaterial."[354] The Court reversed the trial court's vacatur of the arbitral award on the grounds of fraud or undue means.[355] In other words, when fraud upon the panel is discovered and explored before the rendition of a final award, it will be quite difficult for a party to obtain a vacatur on those grounds.

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[346] 9 U.S.C. § 10(a).
[347] 9 U.S.C. §11.
[348] *Brabham*, 376 F.3d at 380 (citations omitted); *See also* Prescott v. Northlake Christian School, 369 F.3d 491 (5th Cir. 2004) ("the district court's review of an arbitration award, under the [FAA], is 'extraordinarily narrow'").
[349] *See* Kergosien v. Ocean Energy, Inc., 390 F.3d 346, 357 (5th Cir. 2004).
[350] 9 U.S.C. §10(a)(1).
[351] *Forsythe Int'l, S.A. v. Gibbs Oil Co. of Texas*, 915 F.2d 1017, 1022 (5th Cir. 1990).
[352] *Id*.
[353] *Id.*, at 1022-23.
[354] *Id*.
[355] *Id*. at 1023.

Interestingly, the Court also noted that the arbitral panel seemed a bit irritated that the parties spent so much time dwelling on the alleged fraud, which seemingly entailed deposition shenanigans (a former employee of a party was represented to be a current employee so the party could exert more control over his deposition).[356] As the Court states, "submission of disputes to arbitration always risks an accumulation of procedural and evidentiary shortcuts that would properly frustrate counsel in a formal trial. . . . whatever indignation a reviewing court may experience in examining the record, it must resist the temptation to condemn imperfect proceedings without a sound statutory basis for doing so."[357]

A later district court opinion from the Southern District of Texas which the Fifth Circuit later adopted examined fraud and undue influence as grounds for vacating an arbitral award and offered a bit more explanation:

> Under the FAA a party who alleges that an arbitration award was procured through fraud or undue means must demonstrate that the improper behavior was (1) not discoverable by due diligence before or during the arbitration hearing, (2) materially related to an issue in arbitration, and (3) established by clear and convincing evidence. Although "fraud" and "undue means" are not defined in section 10(a) of the FAA, courts interpret the terms together. Fraud requires a showing of bad faith during the arbitration proceedings, such as bribery, undisclosed bias of an arbitrator, or willfully destroying or withholding evidence. Similarly, undue means connoted behavior that is 'immoral if not illegal' or otherwise in bad faith. Section 10(a)(1) also requires a nexus between the alleged fraud or undue means and the basis for the arbitrator's decision.[358]

2. Evident Partiality or Corruption in the Arbitrators

In its *TUCO* decision, the Texas Supreme Court created TAA evident partiality jurisprudence, but the Court stated from the outset that it based its holding on cases interpreting the FAA's identical provision.[359] Therefore, while *TUCO* is not controlling, it is certainly helpful with respect to federal evident partiality analysis, particularly since vacatur cases employing FAA analysis are often heard in state courts rather than federal courts. The *TUCO* Court's holding was based on what it characterized as "the seminal evident partiality case," the 1968 U.S. Supreme Court opinion in *Commonwealth Coatings*.

Commonwealth Coatings established the simple rule that it is the nondisclosure of a potential bias, rather than evidence of actual bias itself, which triggers a potential vacatur under the FAA.[360] "We can perceive of no way in which the effectiveness of the arbitration process will be hampered by the simple requirement that arbitrators disclose to the parties any dealings that might create an impression of possible bias."[361] Justice White's concurrence explains a bit more the policy rationale for the *Commonwealth Coatings* rule: "it is often because [arbitrators] are men of affairs, not apart from but of the marketplace, that they are effective in their adjudicatory function."[362] Since arbitrators, unlike judges, function as part of the world in which they make decisions and are chosen because of their prominence in that world, potential conflicts may abound. The solution to this is frankness, so that the parties can decide from the outset whether or not they wish to proceed.

As a slight aside, the Supreme Court's analytical basis for its decision is germane to the overall thrust of this paper: "we should, if anything, be even more scrupulous to safeguard the impartiality of arbitrators than judges, since the former have completely free reign to decide the law as well as the facts and are not subject to appellate review."[363] There you have it.

A three-justice dissent in *Commonwealth Coatings* argued that vacatur for an arbitrator's undisclosed conflict is too harsh a result when all parties seem to agree that no actual bias or impartiality in the challenged arbitrator's ruling

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[356] *Id*., at n.7 ("the neutral arbitrator, however, expressed impatience with protracted diversion from the merits").
[357] *Id*., at 1022.
[358] In the matter of the Arbitration Between Trans Chemical Ltd. and China Nat'l Machinery Import & Export Corp., 978 F.Supp.266 (S.D. Texas 1997), *aff'd* 161 F.3d 314 (5th Cir. 1998) (citations omitted).
[359] *TUCO*, 960 S.W.2d at 632.
[360] Commonwealth Coatings Corp. v. Continental Casualty Co., 393 U.S. 145, 147-48, 89 S.Ct. 337, 338-39 (1968).
[361] *Id*., at 149, 339.
[362] *Id*., at 150, 340 (J. White, concurring).
[363] *Id*., at 149, 339.

existed.[364] As the *TUCO* court explained, some federal circuits have declined to follow *Commonwealth Coatings* or have diluted its mandate.[365]

In 1987, the Fifth Circuit, in dicta, suggested that it would adopt the Second Circuit's narrower standard of evident partiality analysis: "evident partiality means more than a mere appearance of bias."[366] As the Court stated:

> Having analyzed the case law, we address what standard to apply in this case. This is a nondisclosure case in which the parties chose the arbitrator. Striking the balance of the competing goals of expertise and impartiality in the selection process, maintaining faithfulness to the Court's opinion in *Commonwealth Coatings*, and agreeing with the policy arguments set out in *Schmitz*, we hold that an arbitrator selected by the parties displays evident partiality by the very failure to disclose facts that might create a reasonable impression of the arbitrator's partiality. The evident partiality is demonstrated from the nondisclosure, regardless of whether actual bias is established.[367]

However, on May 5, 2006, the Circuit ordered the case re-heard *en banc*.[368] The *en banc* majority opinion, written by Judge Jones, reverses the previous opinion and joins the federal circuits that treat Justice Black's *Commonwealth Coatings* opinion as a mere plurality.[369]According to the majority "the better interpretation of *Commonwealth Coatings* is that which reads Justice White's opinion holistically."[370] What that means, according to Justice Jones, "is that in nondisclosure cases, an award may not be vacated because of a trivial or insubstantial prior relationship between the arbitrator and the parties to the proceeding."[371] In other words, the Fifth Circuit is now firmly entrenched in the camp that has chosen to reject *Commonwealth Coatings* in favor of a standard to be "interpreted practically rather than with utmost rigor."[372] "The draconian remedy of vacatur is only warranted upon nondisclosure that involves a significant compromising relationship."[373]

Judge Reavely's dissent offers a more thorough review of the factual basis for the district court's decision to vacate the arbitral award and it demonstrates that the relationship between arbitrator and party characterized by the majority as being trivial was, in fact, not trivial.[374] Judge Reavely, like Justice Phillips and the Texas Supreme Court, further examined the rationale behind Justice White's *Commonwealth Coatings* opinion and based his dissent on that language, noting that the various opinions in the case are "easily compared and easily reconciled."[375] According to the dissent:

> In 1968, the Supreme Court held that an arbitral award could not stand where the arbitrator had failed to disclose a past relationship that might give the impression of possible partiality. The Court has never changed that holding; it is the law that rules us today. But the majority of this court disapproves of that law because they prefer to protect arbitrators and their awards when they fail to disclose prior relationships with parties or counsel. They therefore change the law for this case and, to make it appear as if their transgression does not matter, trivialize their report of the past relationship. I dissent because this court may not overrule a decision of the Supreme Court.[376]

Finally, in an opinion that concurs with Judge Reavely's dissent, Judge Wiener stressed the difference between arbitration and litigation and argued that Justice White's concurrence was based on those distinctions: "he and the other justices who joined the Black opinion knew full well who it is that has the sole authority and duty to determine

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[364] *Id*., at 152-55, 341-42.
[365] *TUCO*. 960 S.W.2d at 633-34 ("Although Justices White and Marshall joined fully in Justice Black's opinion for the Court, some lower federal courts have purported to see a conflict between the two writings. By treating Justice Black's opinion as a mere plurality, they have felt free to reject the suggestion that 'evident partiality' is met by an 'appearance of bias,' and to apply a much narrower standard.")
[366] Bernstein Seawell & Kove v. Bosarge, 813 F.2d 726, 732 (5th Cir. 1987) (quoting *Florasynth, Inc. v. Pickholz*, 750 F.2d 171, 173 (2d Cir. 1984)). In early 2006, however, it fully adopted the *Commonwealth Coatings* rule, and in so doing offered a detailed discussion of the history of the current split amongst the circuits with respect to that opinion. *Positive Software Solutions, Inc. v. New Century Mortgage Corp.*, 436 F.3d 495, 502-504 (5th Cir. 2006).
[367] *Id.*, at 502.
[368] Positive Software Solutions, Inc. v. New Century Mortgage Corp., 449 F.3d 616 (5th Cir. 2006).
[369] Positive Software Solutions, Inc. v. New Century Mortgage Corp., 476 F.3d 278 (5th Cir. 2007).
[370] *Id.*, at 283.
[371] *Id.*
[372] *Id.*
[373] *Id.*, at 286.
[374] *Id.*, at 289.
[375] *Id.*, at 287.
[376] *Id.*, at 286.

whether a candidate for the post of arbitrator should be accepted or rejected: the parties and they alone."[377] Put another way, Justice Phillips of the Texas Supreme Court reached the same conclusion almost ten years ago:

> We emphasize that this evident partiality is established from the *nondisclosure itself*, regardless if whether the nondisclosed information necessarily establishes partiality or bias. Those courts which have failed to recognize a comparable standard have, we believe, needlessly involved themselves in evaluation of partiality that are better left to the parties.[378]

Since *TUCO* was based on *Commonwealth Coatings*, it is unclear what effect the Fifth Circuit's holistic deconstruction of that opinion will have on TAA evident partiality law. We would note, though, that of the members of the *TUCO* Court, only Justice Hecht remains on the Texas Supreme Court today. He joined in Justice Phillips' majority.

3. Arbitrator Misconduct, Refusal to Postpone Hearing or Hear Material Evidence

The Fifth Circuit provided clear precedent on the kind of arbitrator misconduct which will support vacatur under FAA Section 10(a)(3) when it affirmed a district court vacatur of an award on the ground that "the arbitrator misled Exxon into believing that evidence was admitted, and then refused to consider that evidence."[379]

In *Gulf Coast*, Exxon attempted to discharge a union worker for just cause when a substance found in her vehicle tested positive for marijuana, which would have violated Exxon's policy with respect to controlled substance misuse.[380] At the arbitration, Exxon's attorney began to prove up the "DLR test" which had identified the substance found as marijuana, but the arbitrator stopped him.[381] The arbitrator specifically ruled that the test had been admitted into evidence and that arbitral time did not need to be spent establishing it as a business record.[382] The Court cited references to the arbitration record, which included both a transcript of the proceedings and a stipulation between the parties as to the DLR tests' accuracy and reliability.[383] In the end, however, the arbitrator ruled against Exxon on the basis that Exxon had not proven that the substance found was in fact marijuana, since the DLR test was inadmissible hearsay.[384] "[T]he arbitrator then spent five pages of his decision in a diatribe on the unreliability of hearsay."[385] Relying on Section 10(a)(3) of the FAA, the Fifth Circuit found that the arbitrator misled Exxon's attorney into not adequately proving up the DLR test and therefore triggered vacatur under the FAA.[386]

Of course, *Gulf Coast* must be considered within a larger context of great deference to arbitral awards. The general rule is that arbitrators are given significant leeway on evidentiary issues: "arbitrators are not bound to hear all of the evidence tendered by the parties; however, they must give each of the parties to the dispute an adequate opportunity to present its evidence and arguments."[387] In other words, it would seem that an arbitrator must pro-actively lure a party into evidentiary hot water for Section 10(a)(3) to apply. Given many arbitrators' willingness to simply admit all evidence, 10(a)(3) may, as a practical matter, be a rather rare ground for vacatur (one wonders if the *Gulf Coast* result would have differed had the arbitrator admitted the DLR test result into evidence but perhaps even without cogent explanation, ruled against Exxon anyway - such a result would have been much more difficult for Exxon to overcome it would seem).

In 2009, the Fifth Circuit provided further guidance concerning FAA Section 10(a)(3) in *The Householder Group v. Caughran*.[388] The Court rejected appellant's argument that he did not receive a fair hearing because the panel did not allow him to introduce certain evidence. The Court stated:

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[377] *Id.*, at 286.
[378] *TUCO*, 960 S.W.2d at 636 (emphasis in original).
[379] Gulf Coast Indus. Workers Union v. Exxon Co., *USA*, 70 F.3d 847, 848 (5th Cir. 1995).
[380] *Id.* at 848-49.
[381] *Id.* at 849.
[382] *Id.*
[383] *Id.*
[384] *Id.*
[385] *Id.*
[386] *Id.* at 850.
[387] *Prestige Ford*, 324 F.3d at 395.
[388] Householder Group v. Caughran , 2009 U.S. App. LEXIS 25507 (5th Cir. Tex. Nov. 20, 2009) (unpublished decision).

> The arbitrator is not bound to hear all of the evidence tendered by the parties; however, he must give each of the parties to the dispute an adequate opportunity to present its evidence and argument. An evidentiary error must be one that is not simply an error of law, but which so affects the rights of a party that it may be said that he was deprived of a fair hearing.[389]

4. The Arbitrator Exceeded His or Her Powers

The Fifth Circuit has also recently explained in some detail the analysis that must take place when a party asks a court to vacate an arbitral award on the basis that the award exceeds the arbitrator's powers.[390] The *Kergosien* case explains that an arbitrator's jurisdiction is defined by both the contract containing the arbitration clause and the parties' submissions, but that a failure to provide a reviewing court with a full record of an arbitration proceeding makes it exceedingly difficult for a court to find in favor of vacatur.[391]

> [I]n deciding whether the arbitrator exceeded his jurisdiction, 'any doubts concerning the scope of arbitral issues should be resolved in favor of arbitration.' . . . arbitration should not be denied 'unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute.' We held that the decision as to whether or not an issue is arbitrable is for the arbitrator to decide 'if the subject matter of the dispute is arguably arbitrable,' and that courts have no business overruling an arbitrator 'because their interpretation of the contract is different from his.'[392]

This quoted passage leaves little room for doubt as to the limits of any argument that an arbitrator exceeded his or her power in issuing an arbitral award.

An earlier U.S. Supreme Court case explained the operation of this basic rule when that Court found, in a case within the parameters of the FAA (more on this below), an arbitration clause combined with the arbitration rules of the National Association of Securities Dealers allowed an arbitrator to award punitive damages in the case, even though 1) New York law specifically prohibited arbitral awards of punitive damages, and 2) the arbitration clause specified that New York substantive law applied to any disputes under the contract.[393] The Court found that the FAA trumped New York law prohibiting arbitral punitive damages award and consequently, if the arbitration clause allowed punitive damages, the FAA required their enforcement.[394] The arbitration clause was silent on the issue, but silence in these cases is significant only to the extent it means that the clause did not specifically prohibit punitive damages.[395]

A recent Fifth Circuit decision held that, even in the face of an arbitrator's obvious abandonment of an arbitration clause's scriptures, a court cannot award vacatur of the eventual award when a party does not formally and properly object to the arbitrator's deviation from the clause.[396] The *Brook* case involved an arbitration administered by the American Arbitration Association (AAA) pursuant to the AAA's rules and procedures.[397]According to the Court, "parties to an arbitration agreement may determine by contract the method for appointment of arbitrators," and an arbitrator exceeds his or her powers when he or she does not adhere to this contractually determined methodology.[398] Within this context, the Court writes, "To state that the AAA failed to follow the simple selection procedure outlined in Brook's Employment Agreement is insufficient: the AAA flouted the prescribed procedures and ignored complaints from both sides about the irregular selection process. . . . Because arbitration is a creature of contract, the AAA's departure from the contractual selection process fundamentally contradicts its role in voluntary dispute resolution."[399]

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[389] *Id.*
[390] Kergosien v. Ocean Energy, Inc., 390 F.3d 346, 354-55 (5th Cir. 2004).
[391] *Id.*
[392] *Id.*, at 355 (citations omitted, emphasis in original).
[393] Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S.52, 115 S.Ct. 1212 (1995).
[394] *Id.*, at 58, 1216.
[395] *Id.*, at 59, 1217; *See also Action Indus., Inc. v. United States Fidelity & Guaranty Co.,* 358 F.3d 337, 343 (5th Cir. 2004); Bridas S.A.P.I.C. v. Government of Turkmenistan, 345 F.3d 347, 365-66 (5th Cir. 2003).
[396] Brook v. Peak Int'l, Ltd., 294 F.3d 668 (5th Cir. 2002).
[397] *Id.* at 670.
[398] *Id.*, at 672.
[399] *Id.*, at 673.

The Court clearly found that the arbitration award was issued in manner completely outside the scope of the parties' agreement to arbitrate, since the AAA wholly botched the arbitrator selection process. However, even in this blatant case, it does not matter. Even though the parties complained during the selection process, failing to object in formal writing or at the commencement of the arbitration hearing constituted waiver of their potential complaint.[400] The Fifth Circuit reversed the district court's decision to vacate the award.[401]

At this point it is worth mentioning again a recent Texas Supreme Court case on arbitration, *AdvancePCS*. That case, although it would fall under the scope of the FAA, did not involve a motion to vacate an award under the FAA and does not discuss FAA grounds for vacatur but the clause at issue raises an interesting point. The clause used in *AdvancePCS* reads, in part:

> Any and all controversies in connection with or arising out of this Agreement will be exclusively settled by arbitration before a single arbitrator in accordance with the Rules of the American Arbitration Association. **The arbitrator must follow the rule of law**, and may only award remedies provided in this Agreement. [402]

The Texas Supreme Court has now ordered the parties to arbitrate this dispute. The clause would clearly allow a post-award vacatur under Section 10(a)(4) of the FAA in the event that the arbitrator does not "follow the rule of law," since the contract which provides this arbitrator's power contains the limitation. While it is unclear exactly what this means, the unusual requirement that an arbitrator follow the rule of law may well, at least in this specific case, reign in the arbitrator's discretion under the default rule. This discretion is exceedingly broad and may well encompass decision-making that cannot be claimed to be within the confines of the rule of law (see below).

Most recently, the Fifth Circuit examined the burden a party must meet when challenging the entry of an arbitral award on the basis that the arbitrator exceeded his or her powers in the context of an arbitration about off-shore oil exploration in the Bohai Bay of China.[403] The arbitrator in the case awarded Texaco more than $71M, some $20M of which was an award of consequential damages.[404] The contract between the parties contained both an arbitration clause and a provision which read:

> Notwithstanding any other provision of the Agreement, neither party shall in any circumstance be liable to the other party under, arising out of or in any way connected with this Agreement or the Deed of Assignment for any consequential loss or damage whether arising in contract or tort (including negligence).[405]

In his arbitral award, the arbitrator found that the no-consequential-damages clause (the "exculpatory clause") was unenforceable under New York law (the law that he applied pursuant to a different provision of the contract).[406] Apache Bohai Corporation (Apache) argued that the arbitrator exceeded his powers in making this award of consequential damages because the contract clearly seemed to preclude an award of consequential damages.[407]

Apache argued that since the "exculpatory clause" which, on its face, suggested that consequential damages were not available to Texaco, begins with the language "notwithstanding any other provision of the Agreement." Since the arbitration clause was, in fact, another provision of the Agreement, the exculpatory clause trumped the arbitration clause and removed the issue of consequential damages from the arbitrator's purview.[408]In other words, argued Apache, the arbitrator did not have the authority to review the exculpatory clause at all.[409]

The Fifth Circuit was unmoved by this argument. In distinguishing the cases on which Apache relied, the opinion discussed a scenario in which such an argument can work: where a contract gives an arbitrator jurisdiction over some, but not all, potential disputes between the contracting parties.[410] In such a case, where some claims must

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[400] *Id.*, at 673-74
[401] *Id.*
[402] *AdvancePCS*, 172 S.W.3d at 605-606 (emphasis added).
[403] Apache Bohai Corp. et al. v. Texaco China BV, ___ F.3d ___, 2007 U.S. App. LEXIS 4403 (5th Cir. 2007) (Cause No. 05-20413).
[404] *Id.*, at *4.
[405] *Id.*, at *4 n.1.
[406] *Id.*, at *4.
[407] *Id.*, at *6-7.
[408] *Id.*, at *9.
[409] *Id.*, at *9-10.
[410] *Id.*, at *11-17.

be arbitrated but others litigated, the arbitrator would exceed his authority by ruling on the claims not set aside for arbitration.[411] In this case, however, the arbitration clause was broad and clearly intended for all disputes between the parties to be arbitrated.[412] According to the Court, the arbitrator was within the scope of his authority when he ruled on the legal effect of the exculpatory clause.[413]

5. Manifest Disregard after *Hall Street v. Mattel*

In addition to the grounds for vacating awards provided by the FAA, courts developed the doctrine of "manifest disregard" of the law as a common-law ground to vacate awards.[414] Generally, an arbitral panel is said to have manifestly disregarded the law if, knowing the existence of a clear legal principle, it refuses to apply it. In 2008, in *Hall Street Associates, LLC v. Mattel, Inc.*, the U.S. Supreme Court concluded that the statutory grounds for vacating arbitration awards are exclusive when a party seeks judicial review under the FAA.[415] The Court indicated that "manifest disregard" of the law was not a basis for reviewing such awards.

Over the past year, the circuit courts have differed over whether the "manifest disregard" doctrine survives the Supreme Court's holding in *Hall Street*. The First Circuit, in *Ramos-Santiago v. United Parcel Serv.*,[416] concluded that *Hall Street* abolished "manifest disregard" as a ground for vacating or modifying an award under the FAA. Similarly, in *Citigroup Global Mkts v. Bacon*,[417] the Fifth Circuit strongly rejected "manifest disregard" as an independent, non-statutory ground for setting aside an award. It stated that "the term itself, as a term of legal art, is no longer useful in actions to vacate arbitration awards."[418] But because the Court in *Citigroup* remanded the case to the district court to determine whether vacatur is available under any of the FAA statutory grounds, it is possible that the district court could reconceptualize "manifest disregard" of the law within the "excess of powers" ground.[419]

Other circuit courts have reached a different conclusion. In *Stolt-Nielsen SA v. AnimalFeeds Int'l Corp.*, the Second Circuit held that "manifest disregard" survived *Hall Street.*[420] The Court explained that "manifest disregard" was shorthand for a statutory ground, merely that 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"[421] The Court stressed that arbitration is a creature of contract law and that the parties did not agree to an arbitration carried out in "manifest disregard" of the law. Likewise, the Ninth Circuit concluded in *Comedy Club Inc. v. Improv. West Assocs.*[422] that *Hall Street* did not abolish "manifest disregard" because its case law considers it as a shorthand for the statutory grounds in Section 10(a)(4). Also, in *Coffee Beanery, Ltd. v. WW, L.L.C.*,[423] the Sixth Circuit interpreted *Hall Street* to limit only the contractual expansions of the grounds for review.

6. Standard for Modifying an Award

As allowed by the TAA, the FAA allows a court to modify an arbitral award under certain circumstances, notably in the event of an "evident material miscalculation."[424] The Fifth Circuit has recently explained this basis for

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[411] *Id.*
[412] *Id.*
[413] *Id.*
[414] In addition to "manifest disregard of the law, the Fifth Circuit had adopted the "public policy" as a non-statutory ground for vacatur. *See* Prestige Ford v. Ford Dealer Computer Services, Inc., 324 F.3d 391, 396 (5th Cir. 2003) (stating that the Fifth Circuit also "does recognize some circumstances in which a court may refuse to enforce an arbitration award that is contrary to public policy.").
[415] Hall Street Associates, LLC v. Mattel, Inc., 128 S.Ct. 1396 (2008).
[416] Ramos-Santiago v. United Parcel Serv., 524 F.3d 120 (1st Cir. 2008).
[417] Citigroup Global Mkts v. Bacon, 562 F.3d 349 (5th Cir. 2009); *See also* Victoria VanBuren, *Hall Street Meets S. Maestri Place: What Standards of review will the Fifth Circuit Apply to Arbitration Awards Under FAA Section 10(a)(4) after Citigroup?* May 4, 2009, *available at* http://loreelawfirm.com/blog/guest-post-hall-street-meets-s-maestri-place-what-standards-of-review-will-the-fifth-circuit-apply-to-arbitration-awards-under-faa-section-10a4-after-citigroup (last visited Sept. 3, 2009).
[418] *Citigroup* at *24.
[419] *See* Victoria VanBuren, *Hall Street Meets S. Maestri Place: What Standards of review will the Fifth Circuit Apply to Arbitration Awards Under FAA Section 10(a)(4) after Citigroup?* May 4, 2009, *available at* http://loreelawfirm.com/blog/guest-post-hall-street-meets-s-maestri-place-what-standards-of-review-will-the-fifth-circuit-apply-to-arbitration-awards-under-faa-section-10a4-after-citigroup (last visited Sept. 3, 2009).
[420] Stolt-Nielsen SA v. AnimalFeeds Int'l Corp., 548 F.3d 85 (2d Cir. 2008). *See also* Philip J. Loree Jr., *Hall Street Meets Pearl Street: Stolt Nielsen and the Federal Arbitration Act's New Section 10(a)(4),* May 29, 2009, *available at* http://loreelawfirm.com/blog/hall-street-meets-pearl-street-stolt-nielsen-and-the-federal-arbitration-act%E2%80%99s-new-section-10a4 (last visited Sept. 3, 2009). On June 15, 2009, the U.S. Supreme Court has granted certiorary to *Stolt-Nielsen* on the issue of class arbitration. *See* Victoria VanBuren, *U.S. Supreme Court Grants Cert to Stolt-Nielsen: Class Action Arbitration Case,* June 16, 2009, *available at* http://www.karlbayer.com/blog/?p=2576 (last visited Aug. 27, 2009).
[421] 9 U.S.C. § 10 (a)(4).
[422] Comedy Club Inc. v. Improv. West Assocs., 553 F.3d 1277 (9th Cir. 2009).
[423] Coffee Beanery, Ltd. v. WW, L.L.C., 300 Fed. Appx. 415 (6th Cir. 2008).
[424] 9 U.S.C. §11.

modification: "an 'evident material miscalculation' occurs 'where the record before the arbitrator demonstrates an unambiguous and undisputed mistake of fact and the record demonstrates strong reliance on that mistake by the arbitrator in making his award.'"[425]

B. Arbitral Awards Governed by the Texas General Arbitration Act

The Texas Arbitration Act (TAA) sets forth several independent grounds under which a court must vacate an arbitral award:

> On application of a party, the court shall vacate an award if:
>
> (1) the award was obtained by corruption, fraud, or other undue means;
>
> (2) the rights of a party were prejudiced by:
> (A) evident partiality by an arbitrator appointed as a neutral arbitrator;
>
> (B) corruption in an arbitrator; or
>
> (C) misconduct or willful misbehavior of an arbitrator;
>
> (3) the arbitrators:
>
> (A) exceeded their powers;
>
> (B) refused to postpone the hearing after a showing of sufficient cause for the postponement;
>
> (C) refused to hear evidence material to the controversy; or
>
> (D) conducted the hearing, contrary to Section 171.043, 171.044, 171.045, 171.046 or 171.047, in a manner that substantially prejudiced the rights of a party; or
>
> (4) there was no agreement to arbitrate, the issue was not adversely determined in a proceeding under Subchapter B, and the party did not participate in the arbitration hearing without raising the objection.[426]

The enumerated list of grounds for vacatur is nearly identical to that contained in Section 10 of the FAA. Also, in certain rare cases a court may vacate an arbitral award that violates public policy although the Texas Supreme Court has been careful to note that "an arbitration award cannot be set aside on public policy grounds except in an extraordinary case in which the award clearly violates carefully articulated, fundamental policy."[427]

The TAA authorizes a court to modify or correct errors in an award when:

> (1) the award contains:
> (A) an evident miscalculation of numbers; or
> (B) an evident mistake in the description of a person, thing, or property referred to in the award;
>
> (2) the arbitrators have made an award with respect to a matter not submitted to them and the award may be corrected without affecting the merits of the decision made with respect to the issues that were submitted; or
>
> (3) the form of the award is imperfect in a manner not affecting the merits of the controversy.[428]

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[425] *Prestige Ford*, 324 F.3d at 396 (citations omitted).
[426] TEX. CIV. PRAC. & REM. CODE §171.088.
[427] *CVN Group*, 95 S.W.3d at 239.
[428] Tex. Civ. Prac. & Rem. Code §171.091.

1. Corruption, Fraud and Undue Means

Upon proper application by a party, a court must vacate an arbitral award obtained by corruption, fraud or other undue means.[429]A recent court of appeals opinion from El Paso provides an example. *Tri-Star Petroleum v. Tipperary* involved an appeal of a trial court's decision to vacate an arbitral award due to undue means and a refusal to order that a new arbitration take place.[430] The arbitration clause at issue was itself the product of a prior settlement agreement and it required the parties to hire a neutral accounting firm to make certain calculations and factual determinations that would be enforced as a binding arbitral award under the TAA.[431]

The *Tri-Star* trial court refused to confirm the arbitral award based on its finding that Ernst & Young, the accounting firm hired, acted not as a neutral but as retained accountants on behalf of one of the parties.[432] According to the trial court, Ernst & Young refused to conduct a hearing, refused to communicate with the party that did not hire them and otherwise consciously excluded one of the parties due to its own professional obligations to the party which hired it as its accountants.[433] While Ernst & Young's conduct may have been appropriate as a retained professional advisor to a client, it certainly did not allow for an open, impartial and efficient dispute resolution procedure.

In affirming the trial court's decision, under Section 171.088(a)(1), to vacate Ernst & Young's award, the Court of Appeals also specifically found that, post vacatur, a court is not required to order a new arbitration.[434] Starting the arbitration process over after the prolonged disastrous first arbitration would have defeated the policy of arbitration as an efficient and inexpensive dispute resolution mechanism.[435] Instead, the Court of Appeals found that Tri-Star Petroleum materially breached the arbitration clause of the settlement agreement and that the arbitration clause was revoked under Section 171.001(b) of the TAA.[436] In so doing, the Court of Appeals explicitly found that the TAA's revocation analysis is not limited to formation defenses, such as lack of consideration, mistake and duress. Arbitration agreements are not, according to the Court, more enforceable than other types of contracts. [437] Material breach of an arbitration agreement, which presumably will take place whenever a party obtains an arbitral award through undue means, can revoke the arbitration agreement itself. Establishing undue means, therefore, can serve to not only vacate an award but also to eliminate arbitration altogether.

Rogers v. Maida, while not a vacatur case, is still helpful with respect to establishing corruption, fraud or undue means, as it provides an example of a Court of Appeals affirming a trial court's refusal to compel arbitration due to duress.[438] *Rogers* is an employment case, whereby an employee of RLS Legal Solutions refused to sign an arbitration agreement and her employer refused to pay her for services already rendered until she capitulated.[439] Litigation eventually ensued, the employer moved to compel arbitration and the trial court found that the arbitration agreement was a product of duress because the employer did not have the legal right to refuse to pay its employee wages already earned.[440] This would be a classic case of a defect in the formation of an arbitration clause.

Rogers is also obviously distinguishable from the classic case of a contract of adhesion, whereby an employer refuses to continue to employ an employee unless the employee agrees to an arbitration clause. This latter situation is absolutely kosher in Texas, as described above.

2. Evident Partiality, Willful Misconduct, Corruption

Upon proper application by a party, a court must vacate an arbitral award if the rights of a party to the arbitration were prejudiced by the evident partiality of a neutral arbitrator, by corruption in an arbitrator, or by misconduct or willful misbehavior of an arbitrator. [441]

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[429] TEX. CIV. PRAC. & REM. CODE §171.088(a)(1).
[430] *Tri-Star Petroleum Co. v. Tipperary Corp.*, 107 S.W.3d 607, 614 (Tex. App. - El Paso 2003, pet. denied).
[431] *Id.*, at 610-11.
[432] *Id.*, at 612.
[433] *Id.*
[434] *Id.*, at 614-16.
[435] *Id.*
[436] *Id.*, at 613-16.
[437] *Id.*
[438] *Rogers v. Maida*, 126 S.W.3d 643 (Tex. App. - Beaumont 2004, orig. proceeding).
[439] *Id.*, at 645.
[440] *Id.*
[441] TEX. CIV. PRAC. & REM. CODE §171.088(a)(2).

The Texas Supreme Court issued its first opinion explaining the evident partiality standard within the context of the TAA in 1997.[442] The *TUCO* court explained, however, that it based its opinion on federal jurisprudence interpreting an identical provision in the Federal Arbitration Act.[443] The *TUCO* rule is as follows: "a neutral arbitrator selected by the parties or their representatives exhibits evident partiality under this provision if the arbitrator does not disclose facts which might, to an objective observer, create a reasonable impression of the arbitrator's partiality." [444] The *TUCO* rule only applies with respect to neutral arbitrators and in a situation where the parties or their representatives select the challenged arbitrator. Such a definition means the rule applies to many, but not all, arbitrators.

In the *TUCO* case, each party selected a friendly arbitrator and the friendly arbitrators selected a third, neutral arbitrator whose partiality was challenged.[445] After the panel made its decision, the friendly arbitrator for *TUCO* overheard the neutral arbitrator thank the friendly arbitrator for Burlington Northern for referring him a large piece of litigation work.[446] TUCO filed suit pursuant to Section 171.088(a)(2)'s predecessor, asking the Court to vacate the award due to evident partiality.

The Texas Supreme Court, realizing that it was making new Texas law, provided a thorough history of the evident partiality standard as it applies to the FAA, which I will not recap in this paper but which I do recommend to any party challenging an arbitral award under either the TAA or the FAA on the ground of evident partiality. The Court ruled that since arbitration is a creature of contract between parties and since parties have an incentive to choose the most qualified and experienced arbitrators who would naturally be the most likely to have conflicts, it is critical that the arbitrators disclose potential conflicts as fully as is reasonable.[447] This early and complete disclosure allows the parties, and not subsequent courts, to evaluate potential bias and decide whether or not to proceed.[448] The Court emphasized that evident partiality does not stem from the potential conflict, but from the fact of nondisclosure itself, "regardless of whether the undisclosed information necessarily establishes partiality or bias."[449] Under *TUCO*, arbitrators are not required to disclose trivial relationships or connections but they are required to disclose, for example, a familial or close social relationship and "the conscientious arbitrator should err in favor of disclosure."[450] Finally, in a footnote, the *TUCO* court noted that "a party who learns of a conflict before the arbitrator issues his or her decision must promptly object to avoid waiving the complaint."[451]

In 2002, the Texas Supreme Court revisited the issue and added complexity to the analysis.[452]After restating the *TUCO* rule, the Court affirmed the Court of Appeals' decision to reverse a summary judgment confirming an award that had been challenged based on evident partiality grounds.[453] In *Mariner*, about two months after an arbitral award was issued the Bossleys' expert witness realized that she had earlier testified against one of the arbitrators in a malpractice proceeding.[454] The Bossleys filed a proceeding to vacate the award and Mariner, the prevailing party at arbitration, moved for summary judgment on the grounds that no legal basis existed to vacate the award.[455]

Procedurally, Mariner's decision to move for summary judgment on this issue proved determinative. Ordinarily, the party challenging an award under 171.088(a) has the burden of proving evident partiality. In this case, however, since Mariner filed a "traditional" motion for summary judgment Mariner had to establish as a matter of law that no issue of material fact existed with respect to the arbitrator's evident partiality in order to prevail.[456] Under *TUCO*, the arbitrator had an affirmative obligation to disclose his previous relationship with the Bossleys' expert if he knew of it.[457] The summary judgment evidence, however, was "silent about whether [the arbitrator]

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[442] Burlington Northern Railroad Co. v. TUCO, Inc., 960 S.W.2d 629, 633 (Tex. 1997).
[443] *Id.*
[444] *Id.*, at 630.
[445] *Id.*, at 630-31.
[446] *Id.*
[447] *Id.*, at 635.
[448] *Id.*
[449] *Id.*, at 636.
[450] *Id.*, at 637.
[451] *Id.*, n.9.
[452] Mariner Fin. Group, Inc. v. Bossley, 79 S.W.3d 30 (Tex. 2002).
[453] *Id.*
[454] *Mariner*, at 31-32.
[455] *Id.*, at 32.
[456] *Id.*; *See also* TEX. R. CIV. P. 166a(c).
[457] *Id.*

remembered [the expert] or even knew of her."[458] That being the case, the trial court should not have granted the motion for summary judgment.

In its analysis, the *Mariner* court emphasized the fact-intensive inquiry that must take place with respect to evident partiality analysis.[459] While some cases involve "common knowledge" of a potentially conflicting relationship which does not require additional formal disclosure, others absolutely require disclosure since only the arbitrator would know of the potential conflict.[460] While the *Mariner* court appeared to suggest that its set of facts was somewhere in the middle, it could not even make that assertion based on the record before it. What is clear, though, is that the duty to disclose is the arbitrator's, so the arbitrator's state of mind is the critical factual inquiry. Although a party with knowledge of a conflict must object immediately to avoid a waiver of a potential challenge, a party is not required to conduct independent research in order to discover potential conflicts.[461] "[T]he whole purpose of an arbitrator's duty to disclose is to avoid this very type of speculative presumption and let the parties to the arbitration make the call."[462]

The Austin Court of Appeals recently applied the *TUCO* rule, reversed a trial court's decision to vacate an arbitral award on the basis of evident bias and rendered a judgment enforcing the arbitral award.[463] *Kendall* involved an arbitration award issued against a homeowner in favor of a remodeling contractor.[464] The homeowner was an employee of Vignette Corporation who had moved to Austin due to work obligations and had bought a house in need of repair. [465] During a break in the arbitration, the arbitrator complained to the homeowner about the price of Vignette stock.[466]

After the arbitrator issued an award in the contractor's favor, the homeowner mentioned the exchange about Vignette stock to his attorney, who promptly deposed the arbitrator and filed an application to vacate the award based on evident partiality.[467] The trial court vacated, but the Court of Appeals reversed finding that the homeowner waived his right to complain about any alleged anti-Vignette bias because he failed to object during the arbitration.[468] According to the Court, the logical basis for disclosure is to allow the parties themselves to decide whether to complain about potential conflicts so parties can and often will "waive an otherwise valid objection to the partiality of the arbitrator despite knowledge of facts giving rise to such an objection."[469]

The *Kendall* court's analysis is in line with *TUCO* and based on the factual record as presented in the opinion. It is difficult, as an arbitrator and as an attorney who represents clients in arbitration, to believe that the price of Vignette stock had anything to do with the arbitrator's decision. However, it seems worth considering the burden the Court places on parties to arbitrations left alone in rooms with arbitrators. In order to preserve his complaint, the party here would have been required to make an objection to an off-hand remark in what is supposed to be a less-formal proceeding during a pending arbitration. On the other hand, had the remark evidenced serious and relevant bias, perhaps immediate objection would seem a more reasonable expectation.[470]

Finally, given the Fifth Circuit's recent decision to interpret *Commonwealth Coatings* "holistically," one should review *Positive Software*, described above, before making any assumptions about *TUCO*'s continued viability.

3. Did the Arbitrator Exceed His or Her Power, Refuse to Postpone a Hearing or Refuse to Hear Material Evidence?

Upon proper application by a party, a court must vacate an award if the arbitrator exceeded his or her powers, refused to postpone the hearing after a showing of sufficient cause for the postponement, or refused to hear evidence

[458] *Id.*, at 33.
[459] *Id.*, at 34.
[460] *Id.*
[461] *Id.*, at 34-35.
[462] *Id.*, at 35.
[463] Kendall Builders, Inc. v. Chesson, 149 S.W.3d 796 (Tex. App. - Austin 2004, pet. denied).
[464] *Id.*, at 800.
[465] *Id.*, at 801.
[466] *Id.*
[467] *Id.*
[468] *Id.*, at 804-805.
[469] *Id.*, at 804.
[470] The actual complained-of comment was the question of whether Vignette stock was "ever going to go up." *Kendall Builders*, 149 S.W.3d at 801.

material to the controversy. [471] Determining whether or not an arbitrator has exceeded his or her power requires an examination of the arbitration clause itself at the outset: "the authority of an arbitrator derives from the arbitration agreement and is limited to a decision of the matters submitted therein."[472] This means establishing that the arbitrator made rulings specifically outside the scope of the arbitration clause. It is not enough that the arbitrator decided matters within his or her purview wrongly or haphazardly. In the *Action Box* case, for example, the party seeking vacatur alleged that the "arbitrator exceeded his powers by misinterpreting the operative agreement and erroneously admitting parol evidence to construe it even though it was unambiguous."[473] The Court found that even if those allegations were proven, they would not amount to the arbitrator's exceeding his or her power and so they could not support vacatur.[474] Put another way, it is well within an arbitrator's power to decide an issue incorrectly.

What's more, when courts read arbitration clauses to determine whether an arbitrator's ruling was within the scope of his or her power, they read them broadly: "every presumption will be indulged to uphold the arbitrators' decision, and none is indulged against it."[475] The *J.J. Gregory* court held that, in a case with a broad form arbitration clause (like the standard clauses promulgated by all of the major arbitration providing organizations), an arbitrator has authority to decide any issue that the clause does not specifically take out of his or her scope.[476] In other words, the clause need not specifically provide an arbitrator with the authority to act, it must simply not specifically prevent the arbitrator from acting.[477]

The San Antonio Court of Appeals has reversed a trial court's judgment confirming an arbitral award to the extent the trial court confirmed an improperly modified award.[478] The Court ruled that since arbitral awards are treated "very deferentially" under Texas law, an arbitrator exceeds his or her powers by modifying his or her award absent a finding that statutory grounds for modification exist under the TAA.[479] Once the arbitrator made his or her final decision, the merits of the arbitration were no longer before him or her except as allowed by the narrow guidelines of Section 171.054(a) of the TAA. The trial court, therefore, was required to vacate the modification as it exceeded the arbitrator's power.

At least one Texas Court of Appeals has analyzed a party's claim that an arbitrator's failure to postpone an arbitration required vacatur.[480] In that case, the Court applied an analysis similar to that a court would use in the context of a trial court's refusal to grant a continuance in determining that a failure to postpone in the face of sufficient notice did not warrant vacatur.[481] Other recent Texas cases seeking vacatur of an arbitral award on the grounds that the arbitrator excluded or limited material evidence have not succeeded.[482]

The end result of Texas law interpreting the TAA in this area is that, in most cases and in the "default" cases where a party uses a form or standard arbitration clause, there is no opportunity for meaningful appeal of an arbitral decision on the basis that the arbitrator was obviously wrong on the facts, the evidence or the law. Indeed, since the

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[471] TEX. CIV. PRAC. & REM. CODE §171.088(a)(3).
[472] Action Box Co., Inc. v. Panel Prints, Inc., 130 S.W.3d 249, 252 (Tex. App. - Houston [14th Dist.] 2004, no pet.) (citing Gulf Oil Co. v. Guidry, 160 Tex. 139, 327 S.W.2d 406, 408 (Tex. 1959).
[473] *Id.*
[474] *Id.*
[475] J.J. Gregory Gourmet Services, Inc. v. Antone's Import Co., 927 S.W.2d 31, 36 (Tex. App. - Houston [1st Dist] 1995, no writ).
[476] *Id.*
[477] *See also* Hisaw & Assocs. Gen. Contractors, Inc. v. Cornerstone Concrete Sys., Inc., 115 S.W.3d 16, 20 (Tex. App. - Fort Worth 2003, no pet.) ("The Texas Supreme Court has stated that "the authority of arbitrators is derived from the arbitration agreement and is limited to a decision of the matters submitted therein either expressly or by necessary implication." citing Gulf Oil Corp. v. Guidry, 160 Tex. 139, 327 S.W.2d 406, 408, 2 Tex. Sup. Ct. J. 416 (Tex. 1959)).
[478] Barsness v. Scott, 126 S.W.3d 232, 241-42 (Tex. App. - San Antonio 2003, pet. denied).
[479] *Id.*
[480] *See* Hoggett v. Zimmerman, Axelrad, Meyer, Stern & Wise, P.C., 63 S.W.3d 807, 811 (Tex. App. - Houston [14th Dist.] 2001, no pet.).
[481] *See Id. See also* Crossmark, Inc. v. Hazar, 124 S.W.3d 422, 432 (Tex. App. - Dallas 2004, pet. denied) (court refused, with no analysis, to require vacatur when party did not ask for postponement until six days before arbitral hearing).
[482] *See e.g.* Kosty v. S. Shore Harbour Cmty. Ass'n, 226 S.W.3d 459 (Tex. App. Houston 1st Dist. 2006) (Assuming that the homeowners could have asserted defenses under the Texas Property Code, those defenses were no longer applicable to the disagreement over the breach of the settlement agreement; the arbitrator did not err, for purposes of Tex. Civ. Prac. & Rem. Code Ann. § 171.088(a)(3)(C) by excluding evidence of defenses that might have been asserted in the underlying dispute because they were not material to the matters before the arbitrator); Whiteside v. Carr, Hunt & Joy, L.L.P., 2007 Tex. App. LEXIS 409 (Tex. App. Amarillo Jan. 23 2007) (In view of the parties' express agreement limiting the evidence to be considered by the arbitrator, a trial court did not err in declining to vacate the arbitrator's award on the grounds that he exceeded his powers or refused to hear material evidence by giving effect to the agreement); Affiliated Pathologists, P.A. v. McKee, 261 S.W.3d 874, 2008 (Tex. App. Dallas 2008) (In an employment dispute, there was no error in a failure to an arbitration award in favor of a former employee based on an alleged exclusion of material evidence because an employment addendum agreement was not ambiguous; therefore, extrinsic evidence concerning the parties' intent should not have been heard during the arbitration proceedings. Moreover, the evidence at issue was admitted, but it did not persuade the arbitrators); Graham-Rutledge & Co. v. Nadia Corp., 281 S.W.3d 683 (Tex. App. Dallas 2009) (For purposes of Tex. Civ. Prac. & Rem. Code Ann. § 171.088(a)(2)(C), the record did not reveal such misconduct or willful misbehavior in the arbitrator's decision to limit a lessee's evidence to rebuttal evidence; the lessee waived any error by agreeing to the procedure utilized in the hearing).

Supreme Court's opinion in *CVS Group v. Delgado*, courts treat any attempt to appeal an arbitration as an affront to jurisprudential efficiency. However, since arbitration is a creature of contract it is possible for parties to build some sort of appeal, either in limited or full common-law form, into the arbitration clause.

4. No Agreement to Arbitrate

Finally, the TAA allows a party to seek vacatur of an arbitral award on the grounds that no agreement to arbitrate existed, the issue was not adversely determined under Subchapter B of the TAA and the party did not participate in the arbitration hearing without raising an objection.[483] Subchapter B controls that arise at the beginning of an arbitral proceeding disputes over whether or not a dispute is arbitrable. So, for 171.088(a)(4) to apply, a party would object to arbitration, the objection would be overruled at the outset, the party would participate in the arbitration under objection and the party would move to vacate the award within ninety days of the award.

While this scenario is plausible, most disputes (and there are lots) as to a dispute's arbitrability occur at the outset. A court's refusal to compel arbitration under the TAA is an immediately appealable interlocutory order.[484] Therefore, numerous reported opinions exist concerning a trial court's refusal to compel arbitration. The arbitrability analysis, however, is similar to the vacatur analysis in that the strongest argument one can make at either point in the process must be based on the language of the arbitration clause itself.

5. Public Policy as a Grounds for Vacating an Arbitral Award under Texas Law

As has been noted above, Texas law allows a court to vacate a Texas arbitration award (i.e. one that does not fall under the auspices of the Federal Arbitration Act) if the award contravenes public policy.[485] However, the Texas Supreme Court makes such a remedy quite difficult to obtain: "an arbitration award cannot be set aside on public policy grounds except in an extraordinary case in which the award clearly violates carefully articulated, fundamental policy."[486] The example the Court uses comes from a 1936 case in which the Court refused to confirm an award which enforced a gambling debt.[487] So, under *CVN Group* at least, it is clear than a party ought to be able to vacate an arbitration award which supports an illegal activity.

The *Action Box* Court was careful to note that arbitral errors of contract interpretation, even if clear, "do not begin to approach such a fundamental policy contravention."[488] Similarly, the *Crossmark* Court made it clear that the public policy ground for vacatur cannot be used to complain of arbitral errors in applying the law: "any alleged errors by the arbitrators in applying the substantive law are not subject to review in the courts."[489] "Because Crossmark's arguments at most raise issues as to the application of law, as opposed to presenting fundamental public policy arguments, the trial court could not have set aside the arbitrators' award."[490] In other words, just as it is within an arbitrator's power to be wrong so long as he or she is wrong on an issue properly before him or her, it is also no violation of the public policy of the State of Texas to make mistakes of contract construction or in the application of the law to the facts.

6. Modifying an Arbitral Award Due to Evident Miscalculations

Upon proper application by a party, a court must modify or correct an award if the award contains an evident miscalculation of numbers or an evident mistake in the description of a person, thing or property referred to in the award.[491]

In a 1994 opinion, the Houston Court of Appeals considered a challenge to an arbitral award where the challenging party claimed an arbitrator made errors of arithmetic in assessing liquidated damages.[492] The *Baytown* court refused to modify the award in the absence of a transcription of the arbitration proceeding because: "we do not

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[483] TEX. CIV. PRAC. & REM. CODE §171.088(a)(4).
[484] See TEX. CIV. PRAC. & REM. Code §171.098.
[485] *CVN Group, Inc. v. Delgado*, 95 S.W.3d at 237-38.
[486] *Id.*, at 239.
[487] *Id.*, at 237.
[488] *Action Box*, 130 S.W.3d at 253.
[489] *Crossmark*, 124 S.W.3d at 435.
[490] *Id.*
[491] TEX. CIV. PRAC. & REM. CODE §171.091(a)(1).
[492] City of Baytown v. C.L. Winter, Inc., 886 S.W.2d 515, 519 (Tex. App. - Houston [1st Dist.] 1994, no writ).

know what evidence the arbiters considered in making their award, and the award on its face does not reflect a miscalculation."[493] In other words, if you are arbitrating a case involving a lot of arithmetic, you may well want to have the proceedings recorded.

The *Crossmark* court refused to modify an award on the basis of a claimed miscalculation when the party to the arbitration requesting the modification requested during the arbitration that the arbitrators employ his methodology with respect to calculation.[494] Based on these facts, the Court found the arbitral math to be a concerted decision to not adopt the party's proposed calculation, as opposed to an error.[495] The miscalculation ground for modification of an award, therefore, clearly seems to apply only to legitimate errors in arithmetic and not to arbitral decisions as to the proper measure of damages even if those decisions may seem unusual or unfair. In *Crossmark*, for example, the arbitrators refused to discount an accelerated liquidated damages payment to present value of the funds, awarding instead in one lump sum all payments that were to be paid out over ten years originally - this may not in fact have been unusual or unfair, but even if it were, it would not be grounds for modifying an award.

VII. CONCLUSION

Although arbitration was intended to keep disputes out of court, collateral litigation about arbitration remains an active area of litigation in American courts today. In order to expose Texas litigators to some of the myriad issues at play when engaging in arbitration, this paper outlined the issue of arbitrability, recent case law regarding whether a non-signatory can be bound by an arbitration agreement, discovery issues in arbitration proceedings, evidentiary rules in arbitration and the enforceability of arbitral awards.

[493] *Id.*, at 520.
[494] *Crossmark*, 124 S.W.3d at 436.
[495] *Id.*