Arbitration FAQs: When is an Arbitrator Considered Neutral in a Federal-Arbitration-Act-Governed Arbitration?

Single arbitrators are required under the Federal Arbitration Act to be neutral unless the parties otherwise agree. See, e.g., Morelite v. N.Y.C. Dist. Council Carpenters, 748 F.2d 79, 81-85 (2d Cir. 1984). In tripartite arbitration, one arbitrator (usually designated the umpire or chair) is ordinarily required to be neutral, while party-appointed arbitrators are presumed to be non-neutral, except to the extent otherwise required by the parties' arbitration agreement. See Certain Underwriting Members London v. Florida Dep't of Fin. Serv., 892 F.3d 501, 510-11 (2d Cir. 2018); Sphere Drake Ins. v. All American Life Ins., 307 F.3d 617, 622 (7th Cir. 2002); Trustmark Ins. Co. v. John Hancock Life Ins. Co. (U.S.A.), 631 F.3d 869, 872-74 (7th Cir. 2011). Arbitration provider rules, which may govern arbitrator qualifications in appropriate cases, often provide that all three arbitrators of a tripartite panel are required to be neutral.

Section 10(a)(2) of the Federal Arbitration Act which authorizes federal district courts to vacate arbitration awards "where there was evident partiality in the arbitrators???imposes in part and enforces these neutrality requirements. Section 10(a)(2) establishes that parties who agree to arbitrate can legitimately expect that neutral arbitrators will meet a certain minimal standard of arbitral impartiality, and that arbitrators not appointed as neutrals can, in appropriate circumstances, be held to a substantial, material breach of a stipulated arbitrator qualification requirement related-to, but not necessarily coextensive with, neutrality. See Certain
Underwriting Members, 892 F.3d at 510-11; Sphere Drake, 307 F.3d at 622; Trustmark, 631 F.3d at 872-74.

The requirement that an arbitrator be "neutral" can be divided into three, distinct components. The arbitrator must be (a) impartial; (b) disinterested; and (c) independent.

**Independence**

An arbitrator is independent when he or she is not subject to the control of one of the parties. For example, an arbitrator would not be independent if he or she were an employee of one of the parties to the dispute.

**Disinterestedness**

"Disinterested" means "lacking a financial or other personal stake in the outcome." Trustmark, 631 F.3d at 872-73 (citing Caperton v. A.T. Massey Coal Co., 556 U.S. 868 (2009)); Certain Underwriting Members, 892 F.3d at 510; see Caperton, 556 U.S. at 876-81 (discussing cases).

The requirement of "disinterest" does not address whether the arbitrator has predispositions concerning any of the parties, witnesses, or issues. It is designed to prohibit a decision maker from deciding a case when he or she has an interest in the outcome. The "rule," said the Caperton Court, "reflects the maxim that "[n]o man is allowed to be a judge in his own cause; because his interest would certainly bias his judgment, and, not impossibly, corrupt his integrity." Caperton, 556 U.S. at 876 (quoting The Federalist No. 10, p. 59 (J. Cooke ed.1961) (J. Madison)).

**Impartiality**

To be neutral an arbitrator must not only be disinterested, but also impartial. See, e.g., Trustmark, 631 F.3d at 872-73; U.S.Care, Inc. v. Pioneer Life Ins. Co. of Ill., 244 F.Supp.2d 1057, 1062 (C.D. Cal., 2002). To be "impartial" means to be free from "bias or prejudice in favor of one of the parties. See Liteky v. United States, 510 U.S. 540, 550, 552 (1994).

In Liteky the U.S. Supreme Court explained, in a case concerning judicial partiality standards, that the terms "bias," "prejudice," and "partiality" all connote a favorable or unfavorable disposition or opinion that is somehow wrongful or inappropriate, either because it is undeserved, or because it rests upon knowledge that the subject ought not to possess or because it is excessive in degree." 510 U.S. at 550, 552.

Arbitral or judicial predispositions may be formed as a result of any number things, and can be appropriate or inappropriate, reasonable or unreasonable. But such predispositions do not constitute "partiality," bias or prejudice unless they are wrongful or inappropriate. The Supreme Court's interpretation of what "bias," "prejudice" and "partiality" mean in the judicial context in Liteky is right in line with Section 10(a)(2) itself, which authorizes vacatur where the arbitrator is "guilty" of "evident partiality." 9 U.S.C. § 10(a)(2) (emphasis added).

**Neutral versus Impartial: Terminology Glitches**

Frequently, the requirement of disinterestedness is considered to be a component of impartiality, rather than a standalone requirement. While a case can be made for lumping together an arbitrator's economic or personal interest in a dispute with the existence of an improper predisposition in favor of or against a party, analyzing disinterestedness separately from impartiality promotes clarity and a more precise understanding of what comprises arbitrator neutrality. That, in turn, makes it easier for us to spot its possible absence in a given case.

Unfortunately, the terminology used by Section 10(a)(2), and courts interpreting it, is not consistent with that used by arbitration
providers and other arbitration professionals.

Section 10(a)(2) refers only to "evident partiality," not neutrality. Under the terminology commonly employed by arbitrator providers, "evident partiality" would not encompass an arbitrator's lack of independence from a party. But courts generally, and we think correctly, consider evident partiality to include an evident personal or financial interest in the outcome of the dispute, an evident inappropriate predisposition in favor of or against a party, or an evident lack of independence.

Neutral Arbitrators: Enforcement of Neutrality Requirements under Section 10(a)(2)

Unlike the standards for disqualifying judges, which are set forth for federal judges in 28 U.S.C. § 455, arbitrator neutrality standards are not set forth by statute?Section 10(a)(2) merely authorizes a court to vacate an award if an arbitrator is "guilty" of "evident partiality." 9 U.S.C. § 10(a)(2).

Evident Partiality Standard in the Second Circuit

The "evident partiality" standard?which encompasses all three components of arbitrator neutrality?is judicially created. And while the standard is articulated in different ways in certain jurisdictions, under Second Circuit authority an award may be vacated ?if a reasonable person would have to conclude? that an arbitrator was biased against one party or partial in favor of another. See National Football League Mgmt. Council v. National Football League Players Ass'n, 820 F.3d 527, 549 (2d Cir. 2016) (?NFL Council?); Scandinavian Reinsurance Co. v. Saint Paul Fire and Marine Ins. Co.), 668 F.3d at 64; Applied Indus. Materials Corp. v. Ovalar, 492 F.3d 132, 137 (2d Cir. 2007); Morelite, 748 F.2d at 83-84.

The standard does not require a showing that an arbitrator was actually biased against one party or partial toward another, only that a reasonable person would have to conclude that was so. A determination that a reasonable person would have to conclude that an arbitrator was financially or personally interested in the outcome, or not independent, would likewise satisfy the standard.

Absent disclosure and a waiver, an arbitrator should be free from any relationships with the parties that a reasonable person would have to conclude would materially compromise his or her ability to decide the case in an impartial manner. See Morelite, 748 F.2d at 84-85 (father-son relationship); Scandinavian Re, 668 F.3d at 72 (?Among the circumstances under which the evident-partiality standard is likely to be met are those in which an arbitrator fails to disclose a relationship or interest that is strongly suggestive of bias in favor of one of the parties?).

Neutral Arbitrators: Evident Partiality Standards versus Judicial Impartiality Standards

Even an arbitration agreement that expressly requires an arbitrator to be neutral will not be construed to subject the neutral arbitrator to the standards of impartiality applicable to judges. The "reasonable person would have to conclude" standard applicable to disqualify a neutral arbitrator is considerably more demanding than that required to disqualify a federal judge under Section 455. See Morelite, 748 F.2d at 83; Leatherby, 714 F.2d at 681.

Federal judges are disqualified for bias or partiality "in any proceeding in which [their] impartiality might reasonably be questioned"?a/k/a the "appearance of bias" standard. See 28 U.S.C. § 455(a). While neither the judicial nor the arbitral standard requires a challenger to establish ?actual bias,? see Morelite, 748 F.2d at 84, showing that a person ?might reasonably? ?question? a decisionmaker's impartiality is considerably easier than proving that a ?reasonable person would have to conclude? that a decisionmaker was partial.

The more exacting standard for establishing evident partiality of a neutral arbitrator is not designed simply to make it more difficult to set aside arbitration awards but to reflect realistically what reasonable expectations of neutrality a party who agrees to arbitrate may have. ?Parties agree to arbitrate precisely because they prefer a tribunal with expertise regarding the particular subject matter of their dispute,? said Circuit Judge Irving R. Kaufman, speaking for the Court in Morelite, and ?[f]amiliarity with a discipline often comes at the expense of complete impartiality.? Morelite, 748 F.2d at 83:
Some commercial fields are quite narrow, and a given expert may be expected to have formed strong views on certain topics, published articles in the field and so forth. Moreover, specific areas tend to breed tightly knit professional communities. Key members are known to one another, and in fact may work with, or for, one another, from time to time. As this Court has noted, "Expertise in an industry is accompanied by exposure, in ways large and small, to those engaged in it. . . . To disqualify any arbitrator who had professional dealings with one of the parties (to say nothing of a social acquaintanceship) would make it impossible, in some circumstances, to find a qualified arbitrator at all."

Morelite, 748 F.2d at 83 (quoting Andros Compania Maritima, S.A. v. Marc Rich & Co., 579 F.2d 691, 701 (2d Cir.1978); other citations omitted).

This "tradeoff between impartiality and expertise," was likewise discussed by the U.S. Court of Appeals for the Seventh Circuit in Merit Ins. Co. v. Leatherby Ins. Co., 714 F.2d 673, 679 (7th Cir. 1983), which was decided approximately 16 months before Morelite.

There, Circuit Judge Richard A. Posner explained that the "differential weighting of impartiality and expertise in arbitration compared to adjudication is dramatically illustrated by the practice whereby each party appoints one of the arbitrators to be his representative rather than a genuine umpire. . . . No one, said the Court, "would dream of having a judicial panel composed of one part-time judge and two representatives of the parties, but that is the standard arbitration panel, the panel Leatherby chose--presumably because it preferred a more expert to a more impartial tribunal--when it wrote an arbitration clause into its reinsurance contract with Merit." 714 F.2d at 679.

"If Leatherby had wanted its dispute? to be resolved by an Article III judge. . . . it would not have inserted an arbitration clause in the contract, or having done so move for arbitration against Merit's wishes. 714 F.2d at 679. 'Leatherby wanted something different[;]' said the Court, "it wanted dispute resolution by experts in the insurance industry, who were bound to have greater knowledge of the parties, based on previous professional experience, than an Article III judge or jury. 714 F.2d at 679.

Another reason the law does not hold neutral arbitrators to the same standards as judges is because arbitration is a voluntary. See Leatherby, 714 F.2d at 679.

"Courts are coercive, not voluntary, agencies,? and "fear of government oppression? has, over time, prompted the creation of "a judicial system in which impartiality is prized above expertise." Leatherby, 714 F.2d at 679. Persons elect to submit their disputes to arbitration "do so because they prefer a tribunal knowledgeable about the subject matter of their dispute to a generalist court with its austere impartiality but limited knowledge of subject matter." Leatherby, 714 F.2d at 679.

**Enforcing Arbitrator Neutrality: Arbitrator Disclosure**

Section 10(a)(2), as interpreted by the Courts, is enforced principally through a process by which arbitrators are required to disclose at the outset of the arbitration material relationships and interests that a reasonable person would conclude are highly-suggestive of evident partiality. This requirement (coupled with arbitrator provider rules, where applicable) encourages arbitrators to disclose all relationships and interests that are even arguably relevant to evident partiality.

After hearing arbitrator disclosures, and having an opportunity to ask follow-up questions, the parties may either: (a) object to the arbitrator serving; or (b) accept the arbitrator as qualified and thereby waive any evident partiality claim it might otherwise make based on the matters disclosed. If a party objects, then the arbitrator may either withdraw (allowing the selection of another) or continue to serve.

If the arbitrator continues to serve, and makes an award adverse to the objecting party, then the objecting party may move to vacate the award on evident partiality grounds. But if the party did not object to the disclosed matters, it will be deemed to have waived any evident partiality challenge based on those matters.

This all assumes that the arbitrator discloses the relationship or interest that may form the basis of an evident partiality claim. If the
arbitrator does not do so, a party saddled with an adverse award may assert an evident partiality claim.

But courts should not overturn arbitration awards simply because an arbitrator fails to consistently live up to his or her announced standards for disclosure, or to conform in every instance to the parties' respective expectations regarding disclosure. The nondisclosure does not by itself constitute evident partiality. Scandinavian Re, 668 F.3d at 76-77; Sun Refining & Mktg. Co. v. Statheros Shipping Corp., 761 F. Supp. 293, 299-301 (S.D.N.Y.), aff'd, 948 F.2d 1277 (2d Cir. 1991). The undisclosed facts must show a material interest in the outcome or a material relationship that is so strongly suggestive of bias in favor of one of the parties? that a reasonable person would have to conclude that the arbitrator was biased. Scandinavian Re, 668 F.3d at 72-73 (emphasis added).

The purpose of arbitrator disclosure is to provide the parties with an opportunity to vet arbitrators and to facilitate the waiver of objections, so that a suspicious or disgruntled party can seize on [them] as pretext[s] for invalidating. . . award[s]. See Andros 579 F.2d at 698 (citations and quotation omitted); see also York Research Corp. v. Landgarten, 927 F.2d 119, 121-23 (2d Cir. 1991) (challenger waived right to object by not timely raising it); Cook Industries, Inc. v. C. Itoh & Co.(America) Inc., 449 F.2d 106, 107-08 (2d Cir. 1971); Sun Refining & Mktg. Co., 761 F. Supp. at 299-301.

Broad disclosure of information by arbitrators is and should be encouraged, but not by vacating awards where undisclosed facts do not meet Morelite/Scandinavian Re evident partiality standards. See Scandinavian Re, 668 F.3d at78; Andros, 579 F.2d at 1265; Leatherby Ins. Co., 714 F.2d at 681. Arbitrators have, for example, reputational interests, that encourage disclosure, and arbitrators who want to be appointed or approved by arbitration providers that encourage extensive disclosure have a direct financial incentive to comply. See Leatherby, 714 F.2d at 681.

About the Author]

Philip J. Loree Jr. is a partner and founding member of Loree & Loree. He has nearly 30 years of experience handling matters arising under the Federal Arbitration Act and in representing a wide variety of clients in arbitration, litigation, and arbitration-related litigation. He is a former partner of the litigation departments of the New York City firms of Rosenman & Colin LLP (now known as Katten Munchin Rosenman LLP ) and Cadwalader, Wickersham & Taft LLP.

Loree & Loree focuses its practice on solving arbitration problems for small businesses and professional practices, usually by representing them in arbitration proceedings and in arbitration-related litigation.

It represents private and government-owned-or-controlled business organizations, and persons acting in their individual or representative capacities, and often serves as co-counsel, local counsel or legal adviser to other domestic and international law firms requiring assistance or support.

Loree & Loree was recently selected by Expertise.com out of a group of 1,763 persons or firms reviewed as one of Expertise.com's top 18 Arbitrators & Mediators? in New York City for 2019, and now for 2020. (See here and here.)

If you have any questions about arbitration, arbitration-law, arbitration-related litigation, this article, or any other legal-related matter, you can contact Phil Loree Jr. at (516) 941-6094 or at PJL1@LoreeLawFirm.com.

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