The Repeat Player, Arbitration Providers, Evident Partiality, and the Ninth Circuit

Federal Arbitration Act (?FAA?) Section 10 permits Courts to vacate awards ?where there was evident partiality. . . in the arbitrators. . . .? 9 U.S.C. § 10(a)(2). If an arbitrator fails to disclose an ownership interest in an arbitration provider, which has a nontrivial, repeat player relationship with a party, should the award be vacated for evident partiality?

What constitutes evident partiality and under what circumstances is a controversial and sometimes elusive topic. We've written about it extensively over the years, including **here**, **here**, **here**, and **here**, as well as in other publications. The author has briefed, argued, or both, a number of U.S. Courts of Appeals and federal district court cases on the subject over the years, including, among others, **Certain Underwriting Members of Lloyds of London v. State of Florida, Dep't of Fin. Serv.**, 892 F.3d 501 (2018); and **Nationwide Mutual Ins. Co. v. Home Ins. Co.**, 429 F.3d 640 (2005).

The most recent significant evident partiality development is the U.S. Court of Appeals for the Ninth Circuit's 2-1 decision in **Monster Energy Co. v. City Beverages, LLC**, ___ F.3d ___, No. 17-55813, slip op. (9th Cir. Oct. 22, 2019), a case that involved an award made in favor of a repeat player party in an administered arbitration. Monster held that an arbitrator who failed to disclose his ownership interest in an arbitration provider was guilty of evident partiality because the arbitration provider had nontrivial business relationship with the repeat player party.

The Repeat Player Problem

In administered arbitration the (inevitable) existence of repeat players raises important questions that bear on evident partiality. Repeat players are parties who use the services of an arbitration provider on a regular basis, and therefore are a source of repeat business for the provider.

Arbitrators who are part of an arbitration provider's appointment pool have earned their appointments by satisfying certain criteria set by the arbitration provider, and may also be trained by the arbitration provider. Ordinarily they are not employees of the arbitration provider, and, at least ostensibly, are independent from the arbitration provider.

But the economic interests of these arbitrators are aligned with those of the arbitration provider. What's good for the arbitration provider is generally good for the arbitration provider's pool of arbitrators. Repeat business is good for arbitration providers, just as it is good for lawyers and others.

Let's assume that an arbitrator appointed in an arbitration administered by provider X has never before served as an arbitrator for parties A and B. If the contract between A and B is a form contract used by Party A that appoints X to administer arbitrations, and the contract concerns a subject matter in which disputes are fairly common (e.g., a consumer, employment, or franchise matter), then the arbitrator knows or has reason to know that the customer is either a repeat player or is likely to be one in the not too distant future.

If party B is, for example, a consumer, employee, or franchisee, and is not a repeat player, then one might suggest that our hypothetical arbitrator has at least an indirect interest in the outcome of the arbitration, specifically, one that would be best served by an outcome favoring party A, the repeat player.

That creates a potential evident partiality problem, for to be neutral, arbitrators have to be not only independent, and unbiased, but also disinterested. To be disinterested, the arbitrator cannot have have "a personal or financial stake in the outcome of the arbitration." Certain Underwriting Members, 892 F.3d at 510 (citations and quotations omitted).

Does the kind of indirect and general financial or personal interest in the outcome described above, without more, establish evident partiality? It should not, although arbitrators are well-advised to disclose the existence of such indirect or general financial or personal interests.

We think an argument for evident partiality based solely on an arbitrator having reason to believe that one of the parties is a repeat player with respect to the arbitration provider's services would prove too much. Carried to its logical conclusion it would destroy, or at least severely diminish, the utility of the arbitration-provider-administered arbitration model in a large number of cases.

But that doesn't mean that administered-arbitration awards in favor of repeat players and against non-repeat-players are immune from evident partiality challenge in all circumstances. Monster Energy provides an example and may be a harbinger of closer scrutiny of repeat player evident partiality challenges.

We discuss the majority opinion in Monster Energy below. In a future post or posts, we will discuss the dissenting opinion, what to make of the case, and how it might (or not) influence how other courts address repeat-player-related issues that may arise in future cases.

Monster Energy Repeat Player Case: Majority Opinion

Monster Energy was a dispute between a franchisor (the ?Franchisor?) and a franchisee (the ?Franchisee?), many of the details of which are not critical to our discussion. The dispute was submitted to arbitration under a form contract that contained an arbitration agreement that specified JAMS as the administrator.

The parties selected the arbitrator (the ?Arbitrator?) from a slate of seven-candidates proposed by JAMS.

The Arbitrator was not only a member of the JAMS arbitrator pool, but also had an ownership interest in JAMS. He did not disclose that ownership interest, but his pre-arbitration disclosure stated:

I practice in association with JAMS. Each JAMS neutral, including me, has an economic interest in the overall financial success of JAMS. In addition, because of the nature and size of JAMS, the parties should assume that one or more of the other neutrals who practice with JAMS has participated in an arbitration, mediation or other dispute resolution proceeding with the parties, counsel or insurers in this case and may do so in the future.
Slip op. at 6.

The Arbitrator also disclosed that he had served in a prior arbitration involving the Franchisor and had ruled against it in that matter, making an award against the Franchisor in the amount of nearly $400,000. The arbitrator did not disclose?and it is not clear from the opinion whether during the arbitration he knew?that JAMS had, over a five-year period, administered 97 arbitrations for the Franchisor, i.e., an average of more than one per month.

The Arbitrator made an award against the Franchisee, which included attorney fees; the Franchisor moved to confirm the award; and the Franchisee cross-moved to vacate it on evident partiality grounds. The district court confirmed the award, finding that the Franchisee waived its evident partiality claim, and made an award of attorney fees against Franchisee for fees incurred post-award.

(apparently pursuant to a fee sharing provision in the parties' contract).

The Ninth Circuit reversed the district court's judgement confirming the award and vacated the post-award attorney fee award.

Monster Energy Repeat Player Case: **The Franchisee did not Waive its Evident Partiality Claim**

The district court determined, and the Franchisor argued on appeal, that the Franchisee waived its evident partiality claim ?because it did not timely object when it first learned of potential ?repeat player' bias and the Arbitrator disclosed his economic interest in JAMS.? Slip op. at 9. It appears that knowledge of ?potential ?repeat player' bias? may have been deemed imputed from: (a) the Franchisor's use of a form contract appointing JAMS as arbitrator; and (b) the Arbitrator's disclosure that ?because of the nature and size of JAMS, the parties should assume that one or more of the other neutrals who practice with JAMS has participated in an arbitration, mediation or other dispute resolution proceeding with the parties, counsel or insurers in this case and may do so in the future.? It appears that the Franchisee did not learn until after the award was made that JAMS had administered 97 arbitrations for the Franchisor.

The Ninth Circuit held that the Franchisee did not waive its evident partiality claim. The question before it was whether the Franchisee had ?constructive knowledge? of the arbitrator's ownership interest in JAMS. ?Unlike. . . prior cases[]? involving waiver of evident partiality, said the Court, ?the situation here is more akin to a partial disclosure?the Arbitrator disclosed his ?economic interest' in JAMS prior to arbitration, but [the Franchisee] did not know it was an ownership interest.? Slip op. at 9-10. And while ?the district court correctly noted that an ownership interest is ?merely a type of economic interest,' the key issue is whether [the Franchisee] had constructive notice of the Arbitrator's potential non-neutrality.? Slip op. at 10.

The Ninth Circuit determined there was no waiver, slip op. at 10, for even though the Franchisee ?knew that the Arbitrator had some sort of ?economic interest' in JAMS[,]? ?the Arbitrator expressly likened his interest in JAMS to that of ?each JAMS neutral,' who has an interest in the ?overall financial success of JAMS.'? Slip op. at 9. Further, the ?Arbitrator. . . disclosed his previous arbitration activities that directly involved Monster, in which he ruled against the company.? Slip op. at 9. ?In context,? the Court explained, ?these disclosures implied only that the Arbitrator, like any other JAMS arbitrator or employee, had a general interest in JAMS's reputation and economic wellbeing, and that his sole financial interest was in the arbitrations that he himself conducted.? Slip op. at 9.

In view of these disclosures, ?even if the number of disputes that [Franchisor] sent to JAMS was publicly available, that information alone would not have revealed that this specific Arbitrator was potentially non-neutral based on the totality of JAMS's [Franchisor]-related business.? Slip op. at 9.

The ?crucial fact[]? ?that triggered the specter of partiality[,]? said the Court, was ?the Arbitrator's ownership interest[,]? and [the Franchisee] did not have constructive notice? of that fact. Slip op. at 9 & 10. That ?ownership interest[]? ?was not unearthed through

public sources, and it is not evident that [the Franchisee] could have discovered this information prior to arbitration.? Slip op. at 9. And after the arbitration, ?JAMS repeatedly stymied [the Franchisee's] efforts to obtain details about JAMS' ownership structure and the Arbitrator's interest. . . .? Slip op. at 9.

Noting that the Court has ?repeatedly emphasized an arbitrator's duty to investigate and disclose potential conflict[,]? the Court said that here, ?the Arbitrator undoubtedly knew of his ownership interest in JAMS prior to arbitration yet failed to disclose it.? Slip op. at 10. A waiver finding ?would put a premium on concealment in a context where the Supreme Court has long required full disclosure.? Slip op. at 10 (citations and quotations omitted).

The District Court Should have Vacated the Award on Evident Partiality Grounds

Different circuits have interpreted the standard for evident partiality in different ways, and the standard articulated in the Ninth Circuit is that an award may be vacated for evident partiality where dealings or relationships between the arbitrator and a party create a ?reasonable impression of partiality.? Slip op. at 11 (quotations and citations omitted). Following Associate Justice Byron R. White's concurrence in **Commonwealth Coatings v. Continental Cas. Co.**, 393. U.S. 145 (1968), the Court explained that an arbitrator must disclose a ??substantial interest in a firm which has done more than trivial business with a party. . . .'? Slip op. at 10 (quoting 393 U.S. at 151-52 (White, J., concurring)).

Applying Justice White's rationale to the facts of Monster, the Court explained that it had to undertake a two-pronged ?inquiry?[:] we must determine (1) whether the Arbitrator's ownership interest in JAMS was sufficiently substantial, and (2) whether JAMS and [the Franchisor] were engaged in nontrivial business dealings.? Slip op. at 12 (emphasis in original). ?If[,]? said the Court, ?the answer to both questions is affirmative, then the relationship require disclosure, and supports vacatur.? Slip op. at 12.

The Arbitrator's Ownership Interest in JAMS was Substantial

The Court found that the Arbitrator's interest in JAMS was substantial because the Arbitrator ?has a right to a portion of profits from all of [JAMS'] arbitrations, not just those that he personally conducts.? Slip op. at 12. That interest ?greatly exceeds the general economic interest that all JAMS neutrals naturally have in the organization. . . .? Slip op. at 12.

JAMS and the Franchisor were Engaged in Nontrivial Business Dealings

The Court found that JAMS and the Franchisor were in engaged in nontrivial business dealings because the Franchisor's ?form contracts contain an arbitration provision that designates JAMS Orange County as its arbitrator[,]? and accordingly, ?over the past five years, JAMS has administered 97 arbitrations for [the Franchisor: an average rate of more than one arbitration per month.? That

?rate of business dealing is hardly trivial, regardless of the exact profit-share that the Arbitrator obtained.? Slip op. at 12.

The Court concluded by holding ?that before an arbitrator is officially engaged to perform an arbitration, to ensure that the parties' acceptance of the arbitrator is informed, arbitrators must disclose their ownership interests, if any, in the arbitration organizations with whom they are affiliated in connection with the proposed arbitration, and those organizations' nontrivial business dealings with the parties to the arbitration.? Slip op. at 17.

?Here,? held the Court, the Arbitrator's failure to disclose his ownership interest in JAMS?given its nontrivial business relations with [the Franchisor]?creates a reasonable impression of bias and supports vacatur of the arbitration award.? Slip op. at 17.

More to Come?.

In an upcoming post or posts we'll discuss Circuit Judge Michelle Taryn Friedland's dissent and what to make of Monster.

Photo Acknowledgment

The photo featured in this post was licensed from **Yay Images** and is subject to copyright protection under applicable law.