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## NATIONAL ARBITRATION FORUM

The National Arbitration Forum is a leading provider of dispute resolution services with over 1,500 legally-trained mediators and arbitrators located in all 50 states and 35 countries. All of our neutrals are retired judges or seasoned attorneys with at least 15 years of experience. Our *Code of Procedure* embodies our "best practices" philosophy and has been judicially recognized as a "model for fair cost and fee allocation."

## Fifth Circuit Rejects Nondisclosure of Trivial Arbitral Relationships as a Basis for Vacatur

*Decision bolsters award finality and preserves the availability of expert arbitrators*

In an en banc decision, an 11-5 majority of the Fifth Circuit Court of Appeals held that an arbitrator's nondisclosure of a trivial business relationship between the arbitrator and a party to the proceeding is not a proper basis for vacating an award.

In ***Positive Software Solutions, Inc. v. New Century Mortgage Corp.***, No. 04-11432, 2007 WL 111343 (5th Cir. Jan. 18, 2007), Positive and New Century submitted a software licensing dispute to arbitration. Following a seven-day hearing, arbitrator Peter Shurn issued an award in favor of New Century.

Positive subsequently discovered that Shurn and New Century's attorney, Ophelia Camiña, had represented the same party in complex patent litigation. Though their names appeared together on pleadings, Shurn and Camiña never appeared together for meetings or hearings.

Based on that information, Positive moved to vacate the award. The district court vacated the award on the ground that Shurn's nondisclosure of "a significant prior relationship with New Century's counsel" created an appearance of partiality. After a three-judge panel affirmed, the court granted en banc review.

The issue on appeal was whether Shurn's nondisclosure required vacatur on the ground of "evident impartiality." 9 U.S.C.A. § 10(a)(2). To resolve this issue, the court examined the Supreme Court's interpretation of that provision in ***Commonwealth Coatings Corp. v. Continental Casualty Co.***, 393 U.S. 145 (1968).

A ***Commonwealth Coatings*** plurality held that arbitrators must "disclose to the parties any dealings that might create an impression of possible bias." In a concurring opinion, Justice White expressed his view that arbitrators are not "automatically disqualified by a business relationship with the parties before them if...[the parties] are unaware of the facts but the relationship is trivial."

*Nondisclosure of "a trivial or insubstantial prior relationship between the arbitrator and the parties to the proceeding" is not a basis for vacating an award.*

According to a majority of the court, Justice White's concurrence did not lend majority status or binding effect to the plurality opinion because Justice White did not ascribe to the broad scope of the plurality opinion. In support of this conclusion, the court cited several circuit court decisions that have similarly interpreted ***Commonwealth Coatings***.

Based on its interpretation of ***Commonwealth Coatings***, the court held that nondisclosure of "a trivial or insubstantial prior relationship between the arbitrator and the parties to the proceeding" is not a basis for vacating an award, and that Shurn's

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nondisclosure of his “trivial” relationship with New Century’s attorney did not warrant vacatur. In reaching this conclusion, the court noted that Shurn and Camiña had “never met or spoke to each other before the arbitration.”

The court offered several policy reasons for its holding. First, vacating under these circumstances would spawn “[e]xpensive satellite litigation” by giving losing parties “incentive to conduct intensive, after-the-fact investigations to discover the most trivial of relationships.” The court further explained that “requiring vacatur based on a mere appearance of bias for nondisclosure would hold arbitrators to a higher ethical standard than federal Article III judges.”

Finally, vacating an award “on these attenuated facts would rob arbitration of one of its most attractive features apart from speed and finality—expertise.” The benefit of expertise would be in jeopardy because seasoned and successful attorneys “normally have the longest lists of potential connections to disclose.”

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the award of prejudgment interest on punitive damages and confirming the rest of the award.

On appeal, the Second Circuit determined that “default judgments in confirmation/vacatur proceedings are generally inappropriate” because “they are motions in an ongoing proceeding rather than a complaint initiating a plenary action.” Still, Gottdiener “should have responded in some fashion,” but the court allowed her “some slack” given “the prior dearth of caselaw on the treatment of removed petitions to confirm or vacate arbitration awards.”

According to the court, the motion to confirm should have been treated as an unopposed motion for summary judgment because Gottdiener raised no

## Courts Will Not Consider Allegations of Arbitrator Bias Until Award Is Issued

In denying a motion to disqualify an arbitrator for “evident partiality,” a federal court in Utah held that the Federal Arbitration Act does not allow courts to inquire into an arbitrator’s qualifications until an award is issued.

In *Barlow v. Healthextras Inc.*, No. 2:05cv00189 PGC, 2006 WL 3306802 (D. Utah Nov. 13, 2006), the court ordered the parties to arbitrate their dispute. The arbitration agreement provided for arbitration before a panel of three neutral arbitrators.

Several months after the arbitrators were selected, one of the arbitrators, Rich Humphreys, filed a lawsuit on behalf of his client against a sister company of one of the Defendants. The Defendants subsequently moved to disqualify Humphreys as an arbitrator, arguing that the pending lawsuit constituted “evident partiality” under section 10(a)(2) of the Federal Arbitration Act (FAA).

In opposing the motion, Barlow argued that courts do not have authority to

disqualify an arbitrator until an award is issued. As support for this argument, Barlow noted that section 10(a)(2) refers to arbitration awards in the past tense.

The court agreed with Barlow’s interpretation of the FAA and held that the FAA does not allow judicial inquiry into an arbitrator’s qualifications until an award has issued. In reaching this holding, the court relied largely on the Fifth Circuit’s interpretation of the FAA in *Gulf Guaranty Life Insurance Co. v. Connecticut General Life Insurance Co.*, 304 F.3d 476 (5th Cir. 2002).

The court’s decision does not mean that a party should withhold allegations of arbitrator bias until an award is issued. On the contrary, the party should raise those allegations as part of the arbitration proceeding. If a party sits on evidence of arbitrator bias while awaiting an award, the party risks waiving the objection. See *Van Pelt v. UBS Financial Services*, No. 3:05CV477, 2006 WL 1698861 (W.D.N.C. June 14, 2006).

defense to that motion. Conversely, the motion to vacate should have been treated as a contested motion for summary judgment because Gottdiener raised the defense that the arbitrators were never apprised of the rule against prejudgment interest on punitive damages.

Applying that framework, the court confirmed the award because the motion to confirm was unopposed.” However, vacatur was improper because D.H. Blair failed to carry the “very high” burden of proof necessary to vacate. Specifically, D.H. Blair failed to demonstrate manifest disregard of the law because there was no evidence that the arbitrators were aware of the rule against prejudgment interest on punitive damages.

This decision should not be misconstrued as raising the bar for an

unopposed motion to confirm an arbitration award. Under section 9 of the FAA, the court “must grant” a motion to confirm “unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title.” Sections 10 and 11 allow the court to vacate or modify award only “upon application” by a party.

Accordingly, the moving party is entitled to confirmation in an uncontested motion to confirm. See *Eichleay Corp. v. International Ass’n of Bridge, Structural & Ornamental Iron Workers*, 944 F.2d 1047, 1061 (3d Cir. 1991) (“the district court may not sua sponte raise a motion to vacate when a party has failed to file a timely petition.”); *Taylor v. Nelson*, 788 F.2d 220, 225 (4th Cir. 1986) (“confirmation can only be denied if an award has been corrected, vacated, or modified in accordance with the [FAA]”).

## Florida Supreme Court: Arbitrator Decides Timeliness Defenses

In construing an arbitration agreement that expressly precluded arbitration demands for time-barred claims, the Florida Supreme Court held that the statute of limitations is a procedural question for the arbitrator and not a question of arbitrability for the court.

In *O'Keefe Architects, Inc. v. CED Construction Partners, Ltd.*, No. SC05-1417, 2006 WL 2971783 (Fla. Oct. 19, 2006), CED was general contractor on two housing projects designed by O'Keefe. Both contracts contained provisions requiring arbitration of "[c]laims...arising out of or relating to" the contract. The arbitration clause further provided: "In no event shall the demand for arbitration be made after the date when institution of legal or equitable proceedings...would be barred by the applicable statutes of limitations."

When CED filed a demand for arbitration seeking damages for negligent

design, O'Keefe objected on the ground that the claims were barred by the statute of limitations and therefore not arbitrable. After the arbitrators decided the statute of limitations issue in favor of CED, O'Keefe filed suit seeking a judicial determination. The trial court found that statute of limitations issues were for the arbitrators.

A Florida district court of appeal affirmed the trial court's ruling but certified a conflict with *Reuter Recycling of Florida, Inc. v. City of Dania Beach*, 859 So.2d 1271 (Fla. Dist. Ct. App. 2003), in which a court construing a similar arbitration agreement held that the court should rule on a statute of limitations defense. The Florida Supreme Court granted review in order to resolve the conflict.

The Court held that the statute of limitations and other defenses are questions for the arbitrator and not questions of arbitrability for the court.

As support for its holding, the Court relied partly on *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79 (2002), in which the Supreme Court explained that "gateway procedural disputes" do not present "questions of arbitrability."

Other state supreme courts have used the same analysis to reach this conclusion. In *Industra/Matrix Joint Venture v. Pope & Talbot, Inc.*, 142 P.3d 1044 (Or. 2006), the Oregon Supreme Court distilled *Howsam* down to distinguishing "substantive" questions of arbitrability from "procedural" questions of arbitrability. For example, the scope of an arbitration agreement presents "substantive" questions which the court must decide unless the parties "clearly and unmistakably provide otherwise." Conversely, the statute of limitations presents a "procedural" question that the arbitrator must decide.

## Arbitrator Exceeded Powers By Failing to Apply Notice and Cure Provision

The California Court of Appeals held that an arbitrator exceeded his powers by finding a party liable for breach of contract even though the contract's notice and cure requirement was not satisfied.

In *Gueyffier v. Ann Summers, Ltd.*, No. B186996, 2006 WL 3028272 (Cal. Ct. App. Oct. 26, 2006), Gueyffier and Ann Summers entered into a franchise agreement allowing Gueyffier to open an Ann Summers store in Los Angeles.

The franchise agreement provided that Ann Summers could not "be held in breach" without written notice of the breach and an opportunity to cure. The agreement further provided that the notice and cure requirement was a "material term" that could "not be modified or changed by any arbitrator."

Gueyffier opened an Ann Summers store, but the store closed almost immediately. Shortly thereafter, Ann Summers filed an arbitration demand, and Gueyffier filed a counterclaim for breach of contract.

The arbitrator found Ann Summers liable for breach of contract based on its limited efforts "to mitigate the potential negative reaction from opening a lingerie and sex

toy shop in an upscale mall." Citing the store's "disastrous opening," the arbitrator found that the notice and cure requirement was moot because "the effect of the breaches was not curable." The trial court confirmed the award.

On appeal, the court considered whether the arbitrator exceeded his powers by finding Ann Summers liable for breach of contract even though the notice and cure requirement was not satisfied.

In analyzing this question, the Court cited *Advanced Micro Devices, Inc. v. Intel Corp.*, 885 P.2d 994 (Cal. 1994) for the rule that parties may restrict an arbitrator's powers via "the arbitration agreement, the submission or the rules of arbitration." Applying that rule, the court held that the arbitrator exceeded his powers because Gueyffier and Ann Summers "explicitly and unambiguously" restricted the arbitrator's authority to moot the notice and cure requirement, and the court remanded with instructions to vacate the award.

As the court observed, "parties may agree to limit or restrict an arbitrator's authority and powers." For example, parties can adopt a rule that requires the arbitrator to follow the applicable substantive law. See Rule 20D of the National Arbitration Forum *Code of Procedure*.

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## Default Judgment Proceedings Are Inappropriate to Confirm or Vacate an Arbitration Award

*Court still “must grant” confirmation unless statutory grounds for vacatur apply*

The Second Circuit Court of Appeals held that default judgments are “generally inappropriate” in proceedings to confirm or vacate an arbitration award. The significance of the holding is limited primarily to challenges to arbitration awards since the Federal Arbitration Act (FAA) requires courts to grant an unopposed motion for confirmation.

In *D.H. Blair & Co., Inc. v. Gottdiener*, No. 04-3260, 2006 WL 2551218 (2nd Cir. Sep. 5, 2006), D.H. Blair and Gottdiener submitted an investment dispute to arbitration. The arbitrators awarded Gottdiener \$255,000 in compensatory and \$450,000 in punitive damages. The award also included prejudgment interest on all damages.

Following arbitration, D.H. Blair filed a petition in New York state court, seeking an order vacating part of the award—specifically, the award of prejudgment interest on punitive damages—and confirming the remainder. Gottdiener removed the case to federal court, explicitly reserving all defenses but taking no further action.

Gottdiener did not respond and D.H. Blair moved the district court for default judgment pursuant to Rule 55(b)(2) of the Federal Rules of Civil Procedure. In opposing the motion, Gottdiener argued there was no default under the rule because the petition was a motion rather than a complaint or pleading. The district court granted a default judgment, vacating

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