COMPARING THE ORIGINAL WITH THE REVISED AMERICAN BAR ASSOCIATION – AMERICAN ARBITRATION ASSOCIATION CODE OF ETHICS FOR ARBITRATORS IN COMMERCIAL DISPUTES

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The Code of Ethics for Arbitrators in Commercial Disputes (Code), originally formulated in 1977 by a special joint committee of the American Bar Association (ABA) and the American Arbitration Association (AAA), was revised in 2003 and became effective March 1, 2004. This article compares the original with the revised Code.

The Code does not apply to labor arbitration, which is conducted under the Code of Professional Responsibility for Arbitrators of Labor-Management Disputes. Further, the Code will have limited effect in cases having international components, as the United States is in a class by itself in institutionalizing the concept of party-appointed non-neutral arbitrators. In international arbitrations, party-appointed arbitrators are expected to be neutral and to avoid *ex parte* communications with the appointing party after appointment. ICC Rules of Arbitration, Art. 7; AAA International Arbitration Rules, Art. 7.

The original Code consisted of seven "canons" covering the following topics:

Canon I	The Arbitration Process
Canon II	Disclosure
Canon III	Communicating with the Parties
Canon IV	Fairness and Diligence
Canon V	Decision Making
Canon VI	Confidentiality
Canon VII	Party-Appointed Arbitrators

The revised Code is comprised of ten canons, which relate to the original Code as follows:

Canons I-V	same subject matter as original Code

Canon VI	same subject matter as original Code except for the question of compensation which comprises Canon VII
Canon VII	Compensation
Canon VIII	Promoting Arbitral Services (new)
Canon IX	Party-Appointed Arbitrators. Same topic as original Canon VII.
Canon X	Neutrality for Party-Appointed Arbitrators (called "Canon X Arbitrators," originally called "Non-Neutral Arbitrators")

There are important revisions to all of the canons of the original Code excepting Canon V (Decision Making). The other six original canons have been revised as follows:

CANON I AN ARBITRATOR SHOULD UPHOLD THE INTEGRITY AND FAIRNESS OF THE ARBITRATION PROCESS.

While the title of Canon I remains unchanged, and several changes are merely rhetorical, there are the following significant revisions:

1. Canon I A. The revised Code notes that the arbitrator's responsibility to the arbitration process "may" include pro bono service "where appropriate."

2. Canon I B (originally I C), addressing the acceptance of appointment as an arbitrator, notes that in addition to the matter of availability, an arbitrator should ensure that he or she can serve competently and can also serve impartially and independently from the parties, witnesses and other arbitrators. However, Canon X arbitrators are exempt from the requirements of impartiality and independence.

3. Canon I C (originally I D) notes, consistent with the principle of party autonomy, that notwithstanding a conflict of interest, it is not unethical to serve if, after full disclosure, the parties consent. Canon X arbitrators are excepted.

4. Canon I D (originally I E), referring to avoiding being swayed by various interests, notes that an arbitrator should avoid giving even the appearance of partiality, except for Canon X arbitrators.

5. Canon I E (originally I F) provides that an arbitrator should not exceed his or her authority, but an arbitrator has no ethical obligation to comply with any agreement, procedure or rule that is unlawful or "would be inconsistent with this Code."

6. Canon I H (new). An arbitrator may withdraw where compelled "by unanticipated circumstances that would render it impossible or impractical to continue" or where a party breaches a compensation agreement.

7. Canon I I (new). An arbitrator who withdraws should protect the interests of the parties which includes returning evidence and protecting confidentiality.

The Comment to Canon I clarifies what is meant by "partiality." It states that an arbitrator is not considered partial merely by having acquired knowledge of the parties, the applicable law and the practices of the business involved. The Comment acknowledges that arbitrators may have experience or expertise in the commercial area and that Canon I is not violated if, by reason of such experience or expertise, the arbitrator has views on issues likely to arise in the arbitration. However, the arbitrator "may not have prejudged any of the specific factual or legal determinations to be addressed during the arbitration."

It should be noted that the judiciary has generally supported the concept of non-neutrality both before and after the adoption of the original Code. *Compare Astoria Medical Group v. Health Ins. Plan of Greater New York,* 11 N.Y.2d 128, 182 N.E. 85 (1962), *with Sunkist Soft Drinks, Inc. v. Sunkist Growers, Inc.,* 10 F.3d 753 (11th Cir. 1993). The original Code assumed that the business community desired and expected non-neutrality; however, the modern rules of the major institutional ADR providers require neutrality for party-appointed arbitrators.

Courts recognize that party-appointed arbitration provides an advantage, as a party-appointed arbitrator may give technical assistance to the neutral member. It also provides a

better opportunity for the parties to "keep the neutral arbitrator informed as to their real positions, which may not be exactly as their formal positions." *Clifton Parker v. Anheuser-Busch, Inc.*, 1982 WL 4245 (Ohio App. 10 Dist.). See, *Delta Mine Holding Co. v. AFC Coal Properties*, 280 F.3d 815 (8th Cir. 2001).

The courts recognize that the commercial community prefers a tribunal "knowledgeable about the subject matter of their dispute to a generalist court with its austere partiality but limited knowledge of subject matter." *ANR Coal Co., Inc. v. Cogentrix of North Carolina, Inc.*, 173 F.3d 493 (4th Cir. 1999), citing *Merit Ins. Co. v. Leatherby Ins. Co.*, 714 F.2d 673 (7th Cir. 1983). Thus, the judiciary recognizes a tradeoff between impartiality and expertise. "No one 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 [appellant] chose – presumably because it preferred a more expert to a more impartial tribunal – when it wrote an arbitration clause into its reinsurance contract with [appellee]." *Merit Ins. Co.*, 714 2d at 679.

The Comment to Canon I further notes that during the arbitration, an arbitrator may engage in discourse with the parties or their counsel, draw out arguments, comment on the law or the evidence and make interim rulings.

CANON II AN ARBITRATOR SHOULD DISCLOSE ANY INTEREST OR RELATIONSHIP LIKELY TO AFFECT IMPARTIALITY OR WHICH MIGHT CREATE AN APPEARANCE OF PARTIALITY.

The Canon II includes three primary areas of revision:

1. In addition to the disclosures originally required, including interests or relationships likely to affect impartiality and independence, Canon II A requires disclosure of the extent of an arbitrator's prior knowledge of a dispute and "other matters" required to be disclosed by law or the rules of an institutional provider.

2. Canon II F (new) provides that where the parties know an arbitrator's interest and relationship and nevertheless desire the arbitrator to serve, the arbitrator may properly do so.

3. Canon II H (new) provides that if, to comply with the Code, a prospective arbitrator would be obliged to disclose confidential or privileged information, the arbitrator must either obtain appropriate consents or withdraw.

In *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145, 89 S.Ct. 337, 21 L.Ed.2d 301 (1968), the only Supreme Court case addressing an arbitrator's duty to disclose, Justice Black, writing for a plurality of four, suggested, in dictum, that arbitrators are subject to the same ethical standards as judges. However, the Code effectively adopted the approach of Justice White, who, concurring, drove home the point that "the Court does not decide today that arbitrators are to be held to the standards of judicial decorum of Article III judges." *Commonwealth Coatings Corp.*, 393 U.S. at 150, 89 S.Ct. at 340. Justice White stated that arbitrators "should err on the side of disclosure" but recognized that "an arbitrator's business relationships may be diverse indeed, involving more or less remote commercial connections with great numbers of people" and that therefore an arbitrator cannot be expected to provide "his complete and unexpurgated business biography," nor is an arbitrator required to disclose interests which are merely trivial. *Commonwealth Coatings Corp.*, 399 U.S. at 151-152, 89 S.Ct. at 340-341. See also *ANR Coal Co., Inc.*, 173 F.3d at 498-499; *Merit Ins. Co.*, 714 F.2d at 682.

An arbitration award can be reversed for "evident partiality," Federal Arbitration Act, §10(a) (2); Revised Uniform Arbitration Act, §23 (a) (2) (A); however, "mere non-disclosure does not in itself justify vacatur." *ANR Coal Co., Inc.*, 173 F.3d at 500.

To determine whether there is "evident partiality," the court may examine four factors:

(1) the extent and character of the personal or pecuniary interest of the arbitrator of the proceeding;

(2) the directness of the relationship between the arbitrator and the party alleged to be favored;

(3) the connection of that relationship to the arbitration; and

(4) the proximity in time between the relationship and the arbitration proceeding. *ANR Coal Co., Inc.*, 173 F.3d at 500.

The courts recognize that although the Code is entitled to "great respect," it does not have the force of law. *Merit Ins. Co.*, 714 F.2d at 680. The grounds for setting aside an arbitrator's award under the statutory "evident partiality" test are distinctly narrower than the grounds for disqualification under the Code. "The fact that the AAA went beyond the statutory standards in drafting its own code of ethics does not lower the threshold for judicial intervention." *Merit Ins. Co.*, 714 F.2d at 681. The judiciary cautions against encouraging the losing party to conduct a background investigation of each arbitrator in an effort to uncover evidence of a former relationship with the adversary. *Merit Ins. Co.*, 714 F.2d at 683.

Thus, notwithstanding non-disclosure, vacatur was denied in *The Norwood Co. v. Bennett Composites, Inc.*, 2004 WL 1895193 (E.D.Pa.) (arbitrator "semi-retired" from a company run by his son which belongs to a contractors' association of which arbitration party is also a member); *Daiichi Hawaii Real Estate Corp. v. Lichter*, 82 P.3d 411 (Haw. 2003) (arbitrator's disclosure of prior representation of party lessor held sufficient); *Sphere Drake Ins. Ltd. v. All American Life Ins. Co.*, 307 F.3d 617 (7th Cir. 2002) (failure to fully disclose extent of prior representation of appointing party does not constitute evident partiality); *Michael v. Aetna Life & Casualty Ins.*

Co., 88 Cal. App. 4th 925 (2001) (business connection insufficient to support vacatur); *ANR Coal Co., Inc. v. Cogentrix of North Carolina, Inc.*, 173 F.3d 493 (4th Cir. 1999) (attenuated connections between arbitrator's law firm and one of parties in arbitration); *Betz v. Pankow*, 38 Cal.Rptr.2d 107 (App. Ct. 1995) (arbitrator held former partnership interest in law firm which previously represented party to arbitration); *DeVore v. IHC Hospitals, Inc.*, 884 P.2d 1246 (Utah 1994) (arbitrator held church positions with witness who testified on behalf of employer in wrongful termination dispute). The burden of proof is on the objecting party to prove that the partiality of a party-appointed arbitrator prejudicially affected an award. *Delta Mine Holding Co. v. AFC Coal Properties*, 280 F.3d 815 at 822.

Arbitration awards were vacated for non-disclosure in *Houston Village Builders, Inc. v. Falbaum*, 105 S.W.3d 28 (Tex.App. 2003) (arbitrator represented home builders association of which party builder and party builder's parent company were members); *Morgan Guaranty Trust Company of New York v. Solow Building Co., LLC*, 720 N.Y.S.2d 69 (App. Div. 2001) (arbitrator appointed by defendant did not disclose close involvement with plaintiff's counsel on prior arbitrations; arbitrator was scheduled to testify against defendant in unrelated matter); *Valrose Maui, Inc. v. Maclyn Morris, Inc.*, 105 F.Supp.2d 1118 (D.Haw. 2000) (arbitrator did not disclose ex parte discussion with plaintiff's attorney concerning possibility of service as mediator in upcoming unrelated action); *Texas Commerce Bank v. Universal Technical Institute of Texas, Inc.*, 985 S.W.2d 678 (Tex.App. 1999) (arbitrator formerly represented party bank in a $1.5 million lawsuit).

It should be noted that effective January 1, 2002, California adopted a particularly broad standard of disclosure requiring that in any contractual arbitration, a neutral arbitrator must disclose "all matters that could cause a person aware of the facts to reasonably entertain a doubt

that the proposed neutral arbitrator would be able to be impartial." Cal. Code of Civil Procedure §1281.9(a) Thus, in *International Alliance of Theatrical Employees v. Laughon,* 118 Cal. App. 4th 1380 14 Cal. Rptr.3d 341 (2004), the court vacated an award in favor of plaintiff union for the arbitrator's failure to disclose his service in a matter in which another union was represented by the same law firm that represented the plaintiff union notwithstanding the fact that on the first day of the arbitration an exhibit disclosed this information to which defendant failed to object. The court held that under §1281.9, defendant was entitled to "an explicit, formal proffer of the disqualifying information." *International Alliance v. Laughon*, 118 Cal. App.4th at 1390 14 Cal. Rptr.3d at 349.

CANON III AN ARBITRATOR SHOULD AVOID IMPROPRIETY OR THE APPEARANCE OF IMPROPRIETY IN COMMUNICATING WITH PARTIES.

Canon III revisions address ex parte communications between a prospective or sitting arbitrator and a party as follows:

1. Prospective arbitrators may ask about the identities of the parties, counsel or witnesses and the general nature of the case, and may respond to inquiries regarding his or her suitability, during which discussion the prospective arbitrator may receive information regarding the general nature of the dispute but not the merits of the case.

2. Party-appointed arbitrators may consult with the appointing party concerning the choice of the third arbitrator.

3. Party-appointed arbitrators may consult with the appointing party concerning the party appointed-arbitrator's compensation, and requests for payment need not be sent to other parties.

4. Party-appointed arbitrators may consult with the appointing party regarding communications between any other arbitrator and the party appointing that arbitrator pursuant to Canon IX C.

CANON IV AN ARBITRATOR SHOULD CONDUCT THE PROCEEDINGS FAIRLY AND DILIGENTLY.

The revisions add a new subsection, IV B, which requires that the arbitrator afford all parties the right to be heard and represented by counsel "or by any other person chosen by the party," and that the arbitrator provide due notice of the time and place of all hearings. The revision also adds a clause to the subsection regarding settlement, stating that an arbitrator should not participate in settlement discussions or act as a mediator unless requested to do so by all of the parties.

CANON V AN ARBITRATOR SHOULD MAKE DECISIONS IN A JUST, INDEPENDENT AND DELIBERATE MANNER.

No change from original Code.

CANON VI AN ARBITRATOR SHOULD BE FAITHFUL TO THE RELATIONSHIP OF TRUST AND CONFIDENTIALITY INHERENT IN THAT OFFICE.

The revised Code extracts from the original Code the subsection relating to compensation and constitutes it as Canon VII. The revision also adds to the general confidentiality caveat that an arbitrator may obtain help from an associate "or other persons in connection with reaching his or her decision," if (1) the arbitrator informs the parties, and (2) such other persons agree to be bound by Canon VI.

CANON VII. (new) AN ARBITRATOR SHOULD ADHERE TO STANDARDS OF INTEGRITY AND FAIRNESS WHEN MAKING ARRANGEMENTS FOR COMPENSATION AND REIMBURSEMENT OF EXPENSES.

The 1977 Code barred arbitrators from soliciting business. The revised Code abolishes that prohibition with Canon VII A generally providing that compensated arbitrators should adhere to standards of integrity and fairness in negotiating compensation.

Canon VII B provides that arbitration practices that preserve such standards include:

1. Negotiating all compensation components, e.g., cancellation fee, study time, expenses, before accepting the appointment and putting compensation terms in writing except for party-appointed arbitrators.

2. Where there is an institutional provider, compensation arrangements should be made through the provider. If there is no such provider, communications regarding compensation should be made in the presence of all of the parties except for party-appointed arbitrators.

3. Arbitrators should not request compensation increases "absent extraordinary circumstances."

CANON VIII (new) AN ARBITRATOR MAY ENGAGE IN ADVERTISING OR PROMOTION OF ARBITRAL SERVICES WHICH IS TRUTHFUL AND ACCURATE.

Statements regarding the quality of the arbitrator's work or the success of the practice must be truthful and must not imply any willingness to accept an appointment other than in accordance with the Code.

CANON IX (originally Canon VII) ARBITRATORS APPOINTED BY ONE PARTY HAVE A DUTY TO DETERMINE AND DISCLOSE THEIR STATUS AND TO COMPLY WITH THIS CODE, EXCEPT AS EXEMPTED BY CANON X.

1. Canon IX A provides that in tripartite arbitrations, all three arbitrators are "presumed to be neutral and are expected to observe the same standards as the third arbitrator." This is contrary to Canon VII of the original Code which presumed party-appointed arbitrators to be non-neutral. This states the single most significant distinction between the original and revised Code.

2. Canon IX B provides that notwithstanding this presumption, in "certain types of tripartite arbitration party-appointed arbitrators" may be predisposed toward the party appointing them. These arbitrators, originally called "non-neutral arbitrators," now referred to as "Canon X arbitrators," are not held to the same standards of neutrality as other arbitrators.

3. Canon IX C provides that a party-appointed arbitrator must ascertain, as early as possible, but not later than the first meeting of the arbitrators and parties, whether he or she is appointed as neutral or as Canon X arbitrator and also must provide a report of his or her conclusions to the parties and the other arbitrators. To do this, a party-appointed arbitrator should review the arbitration agreement, applicable rules, and law as well as the course of dealings of the parties. Unless and until the party-appointed arbitrator concludes that he or she is not neutral, he or she should observe all the Canons applicable to neutral arbitrators."

In *Sunkist Soft Drinks, Inc. v. Sunkist Growers, Inc.*, 10 F.3d 753 (11th Cir. 1993), the court refused to vacate an award where the party-appointed arbitrator assisted the party in preparing its case by participating in meetings with witnesses, suggesting areas of testimony, selecting a consultant and advising an expert witness on how to improve his testimony where "none of [the party's] representatives nor the third party witness were placed under oath before

being interviewed, and none gave testimony in any sense of the word," and appellant "made no showing that [the arbitrator] discussed any information that he received during the pre-hearing interviews with the other arbitrators, or that any of the arbitrators, including [the subject arbitrator] based their deliberations and award on anything other than the evidence of record." *Sunkist Drinks, Inc.* at p. 759. The subject arbitrator had announced in his formal disclosure letter that he had been in contact with the appointing party and its experts before the parties were notified of his appointment and that he intended to continue to communicate with the appointing party after his formal appointment. The court characterized the arbitrator's conduct as "commonplace."

In *Aetna Casualty & Surety Co. v. Grabbert,* 590 A.2d 88 (S.C.R.I. 1991), a party-appointed arbitrator was held to have violated his ethical obligation by charging a contingent fee, but the court refused to vacate the award because appellant failed to demonstrate that there was a "causal nexus" between the arbitrator's improper conduct and the award, and because the appellant did not know of the contingent fee arrangement until six months after the award was rendered.

In *Metropolitan Property and Casualty Ins. Co. v. J.C. Penney Casualty and Co.,* 780 F.Supp. 885 (D.Conn. 1991), where a party-appointed arbitrator had ex parte meetings with the non-appointing party to discuss the merits of its defenses and also examined potential documentary evidence prior to selection of the arbitration panel, the award was vacated for both evident partiality and arbitrator misconduct.

CANON X (new) EXEMPTIONS FOR ARBITRATORS APPOINTED BY ONE PARTY WHO ARE NOT SUBJECT TO RULES OF NEUTRALITY.

Canon X expands on the original Canon VII, and refers to the extent to which Canon X arbitrators must observe the other Canons.

1. A Canon X arbitrator should observe all of the process obligations of Canon I, except that a Canon X arbitrator may be predisposed toward the appointing party. However, notwithstanding this predisposition, a Canon X arbitrator should not engage in delaying tactics, harassment or misleading statements to the other arbitrators. A Canon X arbitrator is obviously not subject to Canon I requirements requiring impartiality.

2. A Canon X arbitrator should observe all the disclosure requirements of Canon II, except that he or she is not obligated to withdraw if requested to do so by the party who did not appoint them.

3. A Canon X arbitrator is subject to the communication requirements of Canon III except as follows:

a. A Canon X arbitrator must, at the earliest practicable time, disclose to the other arbitrators and to the parties whether he or she intends to communicate with the appointing party. Only after doing so may he or she thereafter communicate with the appointing party concerning the merits or "any other aspect of the case." If a Canon X arbitrator communicates with the appointing party prior to the first hearing, the Canon X arbitrator must inform the other arbitrators of the fact that ex parte communications occurred but need not disclose the content of pre-hearing communications.

b. During the arbitration, a Canon X arbitrator may not disclose any deliberations on any matter or issue submitted to the arbitrators for decision and may not communicate with the appointing party concerning any matter or issue under consideration by

the panel after the record is closed and may not disclose any final decision or interim decision in advance of the time that it is disclosed to all parties.

c. A Canon X arbitrator may not communicate with the neutral arbitrator concerning "any matter or issue" unless the other Canon X arbitrator is present, and may not communicate in writing with the neutral without providing a copy to the other parties or arbitrators.

4. A Canon X arbitrator should observe the Canon IV obligations regarding fairness and diligence, the Canon VI obligations regarding confidentiality, the Canon VII obligations regarding compensation, the Canon VIII obligations regarding promoting arbitral services and the Canon V obligations regarding independence, except that a Canon X arbitrator may obviously be predisposed before deciding in favor of the appointing party.

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