PUBLICATION

Fifth Circuit Refuses to Vacate Arbitration Award for Nondisclosure of Trivial or Insubstantial Prior Relationship Between Arbitrator and Party

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Hard Hat Case Notes

In an *en banc* decision filed on January 18, 2007, the United States Fifth Circuit Court of Appeals held that an arbitrator's failure to disclose a trivial former business relationship with a party does not require vacatur of the arbitration award on the ground of "evident partiality" under the Federal Arbitration Act (FAA).

The case involved the arbitration of a software licensing dispute between New Century Mortg. Corp. and Positive Software Solutions, Inc. After the arbitrator ruled in favor of New Century on all counts in a proceeding administered by the American Arbitration Association, Positive Software conducted an investigation into the arbitrator's background and discovered that the arbitrator had failed to disclose that several years earlier he and his former law firm had represented the same party as New Century's counsel in unrelated patent litigation. The names of the arbitrator and New Century's counsel had appeared together on ten pleadings in the patent litigation, but they never met or spoke to each other before the New Century/Positive Software arbitration.

Positive Software filed a motion to vacate the arbitration award on the ground that the arbitrator's nondisclosure amounted to "evident partiality" under the FAA. The district court vacated the award on that basis, and a panel of the Fifth Circuit affirmed same, holding "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." However, New Century's petition for rehearing *en banc* was granted, where an 11-5 majority of the Fifth Circuit disagreed with the panel decision.

The Fifth Circuit decided that the FAA does not mandate the extreme remedy of vacatur for nondisclosure of a trivial past association. The court arrived at that decision based on a "holistic" reading of Justice White's concurrence in *Commonwealth Coatings Corp. v. Continental Cas. Co.*, 393 U.S. 145, 89 S. Ct. 337, 21 L.Ed.2d 301 (1968).The Fifth Circuit's narrow interpretation of *Commonwealth Coatings*, characterized as a "plurality-plus" opinion, resulted in the articulation of the following standard: "[I]n nondisclosure cases, an award may not be vacated because of a trivial or insubstantial prior relationship between the parties to the proceeding." Applying that standard, the court held that the arbitrator's failure to disclose his trivial former business relationship with New Century's counsel did not require vacatur of the award. (The court noted that even if *Commonwealth Coatings* required disclosure of dealings that might create an impression of possible

bias, such a disclosure duty was not breached due to the "tangential, limited, and stale contacts" between the arbitrator and New Century's counsel.)

The court offered three policies to support its decision against vacatur of the award. First, the finality of arbitration would be jeopardized if vacatur was granted in similar cases, *i.e.*, vacatur would cause a proliferation of expensive satellite litigation over nondisclosure. Second, if vacatur was required for the mere appearance of bias for nondisclosure, arbitrators would be held to a higher standard than Article III judges. Third, arbitration would lose the benefit of expert arbitrators if vacatur was granted in similar cases, because the best lawyers and professionals, who normally have the longest lists of potential connections to disclose, would choose not to risk blemishes on their reputations from post-arbitration lawsuits attacking them as biased.

Five judges joined in a dissenting opinion, contending that the majority evaded the rule in *Commonwealth Coatings* requiring the disclosure of dealings that might create only an impression of possible bias.

Positive Software Solutions, Inc. v. New Century Mortg. Corp., No. 04-11432, 2007 WL 111343 (5th Cir. Jan. 18, 2007). Contributed by Daniel S. Terrell, of Baker, Donelson, Bearman, Caldwell & Berkowitz, P.C., in New Orleans (Northshore location).