New York Law Journal

ANALYSIS

Sanctions in Commercial Arbitration

As a matter of practice, arbitrators rarely impose sanctions, although sometimes the need arises. This article discusses the tools arbitrators can use to respond to sanctionable behavior in arbitration.

December 20, 2022 at 10:00 AM

Alternative Dispute Resolution

By Richard L. Mattiaccio and David C. Singer | December 20, 2022 at 10:00 AM

An arbitrator's responsibility to actively manage and shape the arbitration process is a well-accepted best practice protocol. Institutional arbitration rules call on arbitrators to control the proceedings in order to deliver on arbitration's promise of fairness and efficiency. AAA Commercial Arbitration Rules (2022) (AAA Rules) R-24; ICC Arbitration Rules (2021) Article 22.1; CPR Domestic Administered Arbitration Rules (2019) (CPR Rules) Preamble, Article 9.2. As a practical matter, to deliver on that promise, arbitrators need the authority to enforce the rules that they set for the arbitration.

Arbitrators sometimes derive their enforcement authority directly from governing statutes. The Revised Uniform Arbitration Act (RUAA), which has been adopted in twenty-two jurisdictions in the United States, empowers arbitrators to grant broad relief, including the imposition of sanctions for failure to comply with discovery orders and an award of fees and expenses. RUAA Sections 17, 21.

In contrast, the laws of some states that have not adopted the RUAA, such as New York's Civil Practice Law and Rules Article 75 dating back to the 1920's, are silent on the subject.

Arbitration rules also provide arbitrators with the authority to impose sanctions. For example, AAA Rules R-24 states, in relevant part: "The arbitrator shall have the authority to issue any orders necessary to enforce … any … rule or procedure and to otherwise achieve a fair, efficient and economical resolution of the case …"

AAA Rules R-60 states, in relevant part: "(a) The arbitrator may, upon a party's request, order appropriate sanctions where a party fails to comply with its obligations under these rules or with an order of the arbitrator."

AAA Rules R-60 does not require a finding of willful noncompliance; rather, it only requires a finding that a party has failed to comply with its obligations. Arbitration rules of other major institutional providers similarly authorize arbitrators to issue a range of sanctions for material violations of rules or orders. See JAMS Arbitration Rule (JAMS Rules) 29; CPR Rule 16.

Authority to impose sanctions, including attorney fees, may also be found in case law, particularly in cases involving broad arbitration clauses. *ReliaStar Life Ins. v. EMC Nat'l Life Co.*, 564 F.3d 81, 88 (2d Cir. 2009); *Salus Cap. Partners v. Moser*, 289 F. Supp. 3d 468, 477-478 (S.D.N.Y. 2018); *General Sec. Nat. Ins. Co. and Aequicap Program Administrator*s, 785 F. Supp. 2d 411, 418-19 (S.D.N.Y. 2011); *Nat'l Union Fire Ins. Co. of Pittsburgh, PA. v. Odyssey Am. Reinsurance*, No. 05 CV. 7539 (DAB), 2009 WL 4059183, at *6 (S.D.N.Y. Nov. 18, 2009).

Sanctions may be based on various grounds, including destruction, non-retention or non-production of documents, particularly in violation of an arbitration hold or other arbitrator's order. Sanctions also may be based on dilatory conduct. *Landmark Ventures v. InSightec, Ltd.*, 63 F. Supp. 3d 343, 358 (S.D.N.Y. 2014); *Bigge Crane & Rigging Co. v. Docutel*, 371 F. Supp. 240, 246 (dicta) (E.D.N.Y. 1973).

Sanctions can take various forms, including monetary sanctions, an award of attorneys' fees, re-allocation of costs or an order excluding evidence or drawing an adverse inference.

AAA Rules R-24 provides several tools, including the power to (a) issue appropriate orders to preserve confidentiality; (b) impose reasonable search parameters for electronic and other documents if the parties are unable to agree; and (c) allocate the costs of producing documents, including ESI. None of these remedies requires a finding of willful non-compliance.

AAA Rules R-24 further provides that, in matters involving willful non-compliance with an arbitrator's order, the arbitrator may draw adverse inferences, exclude evidence and other submissions, make special allocations of costs or an interim award of costs arising from such non-compliance, or issue other enforcement orders allowed under applicable law.

Arbitration rules differ as to whether arbitrators may impose the ultimate sanction, i.e. enter an award on default. AAA Rules R-60(a) provides that an arbitrator "may not enter a default award as a sanction." In contrast, CPR Rules 16 authorizes entry of a default award as a sanction. JAMS Rules 29 authorizes arbitrators to limit a party's participation in the arbitration or make an "adverse determination" of an issue in "extreme cases."

The Federal Arbitration Act, Title 9 U.S.C. (FAA), governs arbitrations that involve interstate commerce, and provides only limited bases for vacatur. One FAA basis for vacatur is that the arbitrators "exceeded their powers" granted in the arbitration agreement. FAA §10(a)(4). Although vacatur is rare, in certain circumstances arbitrators arguably might be deemed to exceed their powers, warranting vacatur or partial vacatur, if they award sanctions without express authorization in the arbitration clause or under applicable arbitration rules. *In re Transvenezualian Shipping Co., S.A.*, 1981 WL 164383, at *2 (S.D.N.Y. Dec. 30, 1981).

A request to exclude evidence as a sanction raises special considerations. Under FAA §10(a)(3), "refusing to hear evidence pertinent and material to the controversy" can constitute a basis to vacate an award. In deciding whether to exclude evidence, arbitrators need to balance potential claims of prejudice to the party seeking preclusion and the risk of vacatur for refusing to hear evidence.

Arbitrators may fashion more limited remedies than preclusion in light of these considerations. For example, arbitrators may adjourn the hearing to allow a surprised party additional time and may assess the incremental costs against the party that did not produce the evidence in a timely manner.

Arbitrator authority to award sanctions against counsel for improper conduct is very much in doubt. Arbitration rules generally focus on sanctions against parties, not counsel. AAA Rules R-24 and R-60, JAMS Rule 29, CPR Rule 16. Reviewing courts tend to consider the sanctioning of attorneys to be the province of courts, not arbitrators. *Porzig v. Dresdner, Kleinwort, Benson, N. Am.*, 497 F.3d 133, 141-143 (2d Cir. 2007); *InterChem Asia 2000 Pte. Ltd. v. Oceana Petrochemicals AG*, 373 F. Supp. 2d 340, 354-55 (S.D.N.Y. 2005); *Bidermann Indus. Licensing v. Avmar N.V.*, 173 A.D.2d 401, 402 (1991); see also *In re Arb. Between UBS Warburg*, 294 A.D.2d 245, 246 (2002); *Stewart Tabori & Chang v. Stewart*, 282 A.D.2d 385, 386 (2001); *Asturiana De Zinc Mktg. v. LaSalle Rolling Mills*, 20 F. Supp. 2d 670, 674-75 (S.D.N.Y. 1998); *MKC Dev. Corp. v. Weiss*, 203 A.D.2d 573, 574 (1994). But cf. *Polin v. Kellwood Co.*, 103 F. Supp. 2d 238, 264-68 (S.D.N.Y. 2000).

The timing of sanctions may turn on the nature of the sanctions requested. Monetary sanctions may be imposed during the arbitration, particularly if the offending conduct imposes identifiable expense on the party seeking sanctions. However, anecdotal evidence suggests that arbitrators, perhaps to avoid side shows, postpone monetary sanctions until issuance of the final award.

Arbitration rules that authorize adverse inferences may not specify when such inferences should be drawn. It may be prudent to wait until all evidence has been submitted and the record has been closed before deciding whether to draw an adverse inference. Deferring this decision may discourage excessive reliance on the inference and result in a more complete record on which to consider applying the inference.

Arbitration rules tend to treat due process as a key consideration in sanctions determinations. AAA Rules R-60; CPR Rule 16. The rules appear to anticipate that a reviewing court may inquire whether arbitrators afforded due process to the parties before imposing sanctions. Accordingly, arbitrators should give parties fair notice that they are considering the imposition of sanctions before any sanction is imposed.

Whenever sanctions are considered, arbitrators should provide parties a full and fair opportunity to present the facts and legal issues relating to the potential sanctions prior to the sanctions determination. When asked by a party to issue sanctions, arbitrators should have the requesting party brief the extent of arbitral authority to issue sanctions and the nature of any sanction the arbitrators can impose, provide the other party an opportunity to respond, and then wait until the sanctions submissions are complete before deciding whether to impose any sanction.

In view of the duty of arbitrators to exercise reasonable efforts to issue enforceable awards, it is important for arbitrators to afford the parties procedural fairness prior to imposing sanctions and to make a clear record of having done so. If arbitrators award sanctions for "willful noncompliance," they should find that the non-compliance was willful based on the record. If such a finding cannot be made, arbitrators need to look elsewhere in the applicable rules for a basis to sanction *non*-willful behavior.

Arbitrators should explain their decision to impose a sanction in writing and should do so with care, especially when the sanction limits an unruly party's participation in the arbitration or involves an adverse inference that has an impact on the merits.

Counsel, in turn, should welcome the opportunity to brief all issues relating to possible sanctions. Arbitrators generally have little or no experience in awarding sanctions. Counsel opposing sanctions will want to make the arbitrators aware of any limits on arbitral authority under the applicable law. The party seeking sanctions, on the other hand, should want to educate the arbitrators as to their power to sanction, and, assuming counsel hopes to win a favorable award, not argue for sanctions that might jeopardize confirmation or enforcement of the award.

The party seeking sanctions also should want to meet head-on any argument made in opposition to sanctions, including, for example, the argument that state law prohibiting an arbitrator from awarding punitive damages also prevents the arbitrator from issuing sanctions. *Garrity v. Lyle Stuart*, 40 N.Y.2d 354 (1976); *Grynberg v. BP Exploration Operating Co. Ltd.*, 92 A.D.3d 547 (2012) (citing *Garrity* and *MKC Dev. v. Weiss*, 203 A.D.2d 573 (1994). But see *Mastrobuono v. Shearson Lehman Hutton*, 514 U.S. 52, 59 (1995) and *Flintlock Constr. Servs. v. Weiss*, 122 A.D.3d 51, 55 (1st Dep't 2014).

As a matter of practice, arbitrators rarely impose sanctions. Good case management skills, combined with the commonsense advocacy point of not antagonizing decision-makers especially when, as a practical matter, no appeal is available, usually suffice to prevent matters from getting so out of hand that sanctions become appropriate and necessary.

Unfortunately, common sense in advocacy and an arbitrator's management and people skills sometimes are not enough to get the job done. Parties may be excessively obstructive, perhaps based on prior experience in court litigation in which such conduct may have been effective. It may take one or more cases for counsel to get the message that aggressive tactics usually backfire in arbitration.

When the need arises, arbitrators have multiple tools that they can use to respond to sanctionable behavior of parties in arbitration. Nonetheless, when considering sanctions, arbitrators should tread lightly. Any sanction should be imposed thoughtfully and reluctantly, and never in the heat of the moment.

An arbitrator should proceed with the same degree of deliberation in deciding whether to issue sanctions as they should in deciding the merits of the case. Although sanctions are in the arbitrator's toolbox, like any other sharp-edged tool, this tool should be handled with care.

Richard L. Mattiaccio *and* **David C. Singer** *are full-time independent neutrals based in New York, with decades of experience as counsel and arbitrators in the field of commercial arbitration.*