BURR ALERT

Doctrinal Split Over Nonparty Discovery in Arbitration Continues

By Mignon A. Lunsford *December 2012*

The Federal Arbitration Act (FAA) was enacted to ensure the enforceability and validity of arbitration agreements. Through the enactment of this sweeping legislation, Congress signaled its approval of arbitration as a form of alternative dispute resolution and ushered in a national policy favoring arbitration. Currently, however, this national policy is frustrated by a circuit split regarding arbitrators' ability to issue nonparty subpoenas when not incident to an actual arbitration hearing.

The split specifically concerns Section 7 of the FAA and whether, by its vague language, the section permits an arbitrator to compel pre-hearing discovery depositions and document production from nonparties. Section 7 states in pertinent part:

> The arbitrators…or a majority of them, may summon in writing any person to attend before them or any of them as a witness and in proper case to bring with him or them any book, record, document or paper which may be deemed material as evidence in the case….[1]

Thus, while arbitrators have indubitable authority to summon witnesses and documents attendant to an actual arbitration hearing, the split arises because courts disagree as to whether this authority extends to nonparties where discovery is sought prior to the hearing. Two primary, and distinctly different, approaches to the matter have evolved through the circuits' decisions: the implicit powers approach and the express language approach. In formulating the two approaches, the circuits favoring the implicit powers approach have relied upon arbitration's general goals of efficiency and cost-effectiveness to support the finding of an inherent power to compel pre-hearing discovery from nonparties while the circuits adopting the express language approach have focused on the plain language of Section 7 to conclude that the statute does not grant such authority.

A. The Implicit Powers Approach

The first of the predominant views on pre-hearing, nonparty discovery is the implicit powers approach. Two circuits have applied this broad, permissive, and simplistic approach to interpreting the authority granted by Section 7, using the policy considerations underlying arbitration to bolster their position. In *American Federation of Television and Radio Artisits, AFL-CIO v. WJBK-TV*,[2] the Sixth Circuit determined that Section 7 "implicitly includes the authority to compel the production of documents for inspection by a party prior to the hearing." Even though the Court's decision endorsed pre-hearing discovery from nonparties, it limited arbitrators' authority to the production of documents. The Court concluded that the inherent authority should not extend to depositions because the nonparty witness could be summoned to testify at the actual hearing, and requiring the witness to also testify at a deposition would impose too heavy a burden.

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[1] 9 U.S.C. §7.

[2] *Am. Fed'n of Television & Radio Artists, Cleveland Local, AFL-CIO v. Storer Broad. Co.*, 660 F.2d 151 (6th Cir. 1981).

The Eighth Circuit likewise adopted a position favoring discovery in *In re Security Life Insurance Co. of America*.[3] There the Court found that Section 7 includes an implicit power for arbitrators to subpoena pre-hearing documents from third parties in order to best promote efficiency interests. The Court reasoned that by being able to review and analyze important documents prior to the actual hearing, the parties are able to expedite the proceedings and reach a more efficient resolution.

B. The Express Language Approach

The second predominant approach to arbitral nonparty discovery is the express language approach. Three circuits have followed this approach in determining whether Section 7 authorizes prehearing discovery from nonparties. The Fourth Circuit applied the approach in *COMSTAT Corp. v. National Science Foundation*[4] where a party to the arbitration sought enforcement of an arbitral subpoena for the production of a third party's documents prior to the hearing. The Court declined to enforce the subpoena, finding that the text of Section 7 unambiguously limits an arbitrator's subpoena power to instances in which the nonparty is called to appear in person at a hearing. The Court did announce an exception to this restricted prehearing subpoena power in instances where a party shows "special need or hardship." However, the Court declined to define "special need," and as a result, there is little guidance for applying the Fourth Circuit's exception, and it has rarely been followed.

In *Hay Group, Inc. v. E.B.S. Acquisition Corporation*,[5] the Third Circuit likewise followed the express language approach in ruling that a nonparty could not be compelled to produce documents unless appearing at a hearing before an arbitrator. In making its determination, the Court noted that neither the express language of Section 7 nor its legislative history support a finding of pre-hearing document discovery from third parties and thereby expressly rejected the implied powers approach. The Court further supported its ruling by noting that its narrow interpretation of Section 7 actually fosters the purposes of arbitration by discouraging unnecessary subpoenas and thereby reducing costs and promoting efficiency.

After declining to rule on the matter in two prior cases, in 2008, the Second Circuit adopted the express language approach in *Life Receivables Trust v. Syndicate 102 at Lloyd's of London*.[6] Similar to the Third and Fourth Circuits, the Second Circuit favored a narrow interpretation of Section 7, finding that the provision's express language did not empower arbitrators to issue pre-hearing document subpoenas to third parties. However, the Second Circuit did not foreclose nonparty, pre-hearing discovery entirely, but instead provided leeway to parties seeking pre-hearing documents by broadly defining "hearings." By extending arbitral subpoena power to "hearings covering a variety of preliminary matters," and not just hearings on the merits, the Court provided broader authority under the express language approach than previously granted by the Third or Fourth Circuits.

These three circuits support their narrow interpretation of Section 7 by noting that Congress is "fully capable" of expanding arbitral subpoena power if it chooses to do so, but until then, the courts are bound by the straightforward language of the statute. Additionally, these circuits assert that by agreeing to arbitration, parties "forego certain procedural rights attendant to formal litigation…including a limited discovery process." Accordingly, if pre-hearing discovery from third parties were allowed, the limited discovery process would be frustrated and extensive fishing expeditions would likely result. The Fourth Circuit alone acknowledges that while a limited discovery process is crucial to arbitration's goal of efficiency, if discovery is too limited it can

[3] *In re Sec. Life Ins. Co. of Am.*, 228 F.3d 865 (8th Cir. 2000).
[4] *COMSAT Corp. v. Nat'l Sci. Found.*, 190 F.3d 269 (4th Cir. 1999).
[5] *Hay Group, Inc. v. E.B.S. Acquisition Corp.*, 360 F.3d 404 (3d Cir. 2004).
[6] *Life Receivables Trust v. Syndicate 102 at Lloyd's of London*, 549 F.3d 210 (2d Cir. 2008).

actually detract from efficiency in complex matters where parties could benefit from exposure to pivotal documents prior to the actual hearing. This reasoning lends support to the Fourth Circuit's exception to an arbitrator's inability to compel third party, pre-hearing discovery upon a showing of "special need or hardship."

C. The Impact of the Split

The current circuit split over the scope of an arbitrator's authority to compel discovery from nonparties prior to an actual arbitration hearing impedes the national uniformity Congress attempted to achieve with the enactment of the FAA. Eventually, Congress will have to clarify the scope of Section 7, or the Supreme Court will be required to settle the dispute and render the proper, and peremptory, judicial interpretation as to whether nonparty, pre-hearing discovery is permissible in arbitration. However, at this point, no party to a case involving the interpretation of Section 7 has sought review with the Supreme Court.

Currently, the best option for parties to an arbitration agreement might be to address nonparty discovery issues in the agreement itself. Parties are permitted to set parameters for arbitral discovery in their agreement, making it as limited or expansive as is mutually desired. However, in order to avoid the dilemma posed by the split, the parties must get all third parties who are likely to be involved or connected in a dispute covered by the agreement to consent to the discovery procedures. This measure requires a large degree of foresight and planning, and is infrequently utilized because many parties consider it more trouble than it is worth. In any case, the current split is a significant drawback to arbitration, and until the conflict is resolved, parties are well advised to understand their circuit's posture on the issue.

For more information, contact:

Mignon A. Lunsford in Birmingham at (205) 458-5477 or mlunsford@burr.com

or your Burr & Forman attorney with whom you regularly work.