

**What Does an Arbitration Panel Do When a Party
Does Not Pay Its Share of Arbitration Costs?**

By

Robert M. Hall and Debra J. Hall

Mr. Hall is an attorney, a former law firm partner, a former insurance and reinsurance executive and acts as an insurance consultant as well as an arbitrator and mediator of insurance and reinsurance disputes and as an expert witness. He is a veteran of over 170 arbitration panels and is certified as an arbitrator and umpire by ARIAS - US. Mr. Hall has authored over 100 articles that may be viewed at his website: www.robertmhall.com.

Ms. Hall is an attorney, the former Senior Vice President & General Counsel of the Reinsurance Association of America and a former reinsurance company executive. She is an ARIAS-US certified arbitrator, accepting only umpire appointments and arbitrator appointments for neutral panels. Ms. Hall also serves as a consultant and expert witness. She has authored and supervised the creation of multi-volume compilations of reinsurance law and practice and was the initiator and facilitator of the original Procedures for the Resolution of U.S. Insurance and Reinsurance Disputes, now largely incorporated into the ARIAS-US Rules with the same name. Articles and other information can be obtained from her website at: www.hallarbitrations.com.

The views expressed in this article are those of the authors and do not reflect the views of their individual clients. Copyright by the authors 2016.

I. Introduction

On rare occasions, a party to a dispute subject to arbitration does not pay arbitration costs *i.e.* the fees of its party arbitrator, half the costs of the umpire, and court reporter fees. This may be tactical as a means of preventing the arbitration from going forward or it may be due to a lack of assets. Whatever the cause, it presents a dilemma for the arbitration panel.

Some arbitration forums, such as the AAA, have procedural rules that allow panels significant discretion in fashioning remedies for such situations.¹ Reinsurance arbitrations, which have been *ad hoc*, traditionally, lack such formalized procedures. The recently adopted ARIAS – US Rules for the Resolution of U.S. Insurance and Reinsurance Disputes do not address this issue.

The purpose of this article is to explore the case law and practice around several options available to reinsurance arbitration panels when dealing with a party that does not pay its share of arbitration costs.

II. Breach and Waiver

It appears that the most common result of a party's failure to pay arbitration costs is that such party is in breach of the contract containing the agreement to arbitrate and waives its arbitration rights. For instance, *Pre-Paid Legal Servs. v. Cahill*, 786 F.3d 1287 (10th Cir. 2015) involved a dispute over an employment contract containing an arbitration clause. The employer alleged breach of the contract and sued in court. The employee obtained a stay and an order to arbitrate but did not pay AAA arbitration fees. When the AAA terminated the arbitration, the employer went back to court. The employee then asked the court to defer to arbitration again since the employee had obtained sufficient funds to pay the AAA arbitration fees. The court declined to do so ruling: "[A] party's failure to pay its share of arbitration fees breaches the arbitration agreement and precludes any subsequent attempt by that party to enforce that agreement."²

A very similar fact situation but with the employer not paying arbitration fees is presented by *Sink v. Aden Enters.* 352 F.3d 1197 (9th Cir. 2003). The court ruled similarly that the employer had breached the contract containing the arbitration clause and had waived arbitration:

Accepting [the employer's] reading of the [Federal Arbitration Act] would . . . Allow a party refusing to cooperate with arbitration to indefinitely postpone litigation. Under [the employer's] interpretation, the sole remedy available to a party prejudiced by default [in paying arbitration fees] would be a court order compelling a return to arbitration. The same offending party could then default a second time, and the prejudiced party's sole remedy, again, would be another order compelling arbitration. The cycle could continue, resulting in frustration of the aggrieved party's attempt to resolve its claims. . . . [The employer's failure to pay required costs of arbitration was a material breach of its obligations in connection with the arbitration.]³

A dispute over a purchase agreement with an arbitration clause provided the backdrop to *Norgren, Inc. v. Ningbo Prance Long, Inc.*, 2015 U.S. Dist. Lexis 126716 (D. CO). NPL, a Chinese manufacturer, initiated arbitration proceedings for non-payment against Norgen, a Colorado corporation that intended to incorporate the parts manufactured by NPL into larger products. Norgen counterclaimed for breach of contract by NPL. After long and involved negotiations, the arbitrator dismissed the arbitration without prejudice for failure to pay arbitration fees. Later, NPL initiated a second arbitration on the same dispute and paid the appropriate arbitration fees. Norgen objected arguing that NPL had waived its arbitration rights by not paying the appropriate arbitration fees in the first arbitration. The court agreed: "[T]his

court finds that by virtue of its actions in the First Arbitration, NPL defaulted on or waived its arbitration rights under the parties' Purchase Agreement and is thereby barred from asserting those rights anew in the Second Arbitration."⁴

See also Sanderson Farms, Inc. v. Gatlin, 848 So. 2nd 828 (MS 2003) that involved a dispute between a chicken distributor, Sanderson Farms, and a chicken grower. When the chicken grower's contract was cancelled, he initiated arbitration pursuant to the arbitration clause in the contract. Sanderson Farms declined to pay certain arbitration fees and the chicken grower filed suit in court. Sanderson Farms filed a motion to dismiss but the court refused finding that Sanderson Farms had waived its right to arbitrate:

Sanderson Farms waived its right to arbitrate by refusing to pay its one-half of the costs associated with filing and administrative fees and/or the additional charges presented for payment one month before the scheduled hearing. This refusal amounts to an act inconsistent with the right to arbitrate. By waiving its right to arbitrate, Sanderson Farms has relinquished the right to seek the protections of the arbitration provision in the boiler contract.

Furthermore, the [Federal Arbitration Act] provides that a party in default essentially waives his right or is precluded from invoking the arbitration agreement. Section 3 of the FAA provides that a party may compel arbitration and stay the trial court proceedings if he 'is not in default in proceeding with such arbitration.'⁵

III. Alternatives to Litigation When One Party Defaults on Arbitration Fees

If the non-defaulting party prefers litigation to arbitration as a dispute resolution method, then that party is free to pursue litigation. But what if the non-defaulting party prefers to enforce their contractual right to arbitration? Declaring a breach of contract can simply feed into the strategy of a defaulting party who wants out of arbitration. It is unlikely that courts would find fairness in allowing a party that contractually agreed to arbitration the ability to avoid the arbitration process simply by not paying its share of the costs of the arbitration. The authors, and other ARIAS-US arbitrators have confronted these situations and worked with their respective panel members and the parties to craft a variety of satisfactory solutions. The strategies are nuanced and are a function of the factual contexts.

One Party is Required to Pay all Costs

One such solution *requires* the non-defaulting party to pay all fees to arbitrators and to pay fully the other costs of the arbitration such as court reporter fees. The payment of such fees and costs is conditioned on the agreement by the panel to incorporate them into the panel's ultimate award. This is not a perfect solution as there are no guarantees that the non-defaulting party: (a) will win the arbitration, or even if it does win; (b) that there will be sufficient available funds to pay the award of the panel. However, in the appropriate situation, it can enable the arbitration process to go forward to a ruling on the merits.

Order to Show Cause/Default

Another approach is to issue an order to show cause why a default judgment should not be entered against the party who has failed to comply with the arbitration payment terms of its contract. The award can include the unpaid fees and costs, state that the award will not be final until the fees are paid, and that the award will carry the statutory rate of interest until paid by the loser to the winner. A hearing can be convened with a court reporter to make sure the record reflects why the bills are not being paid. As with any default judgment, the panel should address procedural safeguards needed to address the merits of the underlying dispute, a topic beyond the scope of this article.

Dispositive Motions and Non-Final Order

In the event that the parties have filed dispositive motions, and the panel is in agreement with respect to those motions, the panel can issue a non-final order that sets forth preliminary findings of fact and conclusions of law but specifically states that the order is not to be considered a final award until the panel's fees and costs are paid by some party (not designating which party). The award can state that upon payment of fees and costs, the final award shall be issued within a prescribed time period, consistent with the preliminary findings and conclusions expressed in the non-final order, and will include any fees and costs advanced on behalf of a defaulting party. In this situation the parties know which way the panel intends to rule, and if the winning party is the non-defaulting party, it may well be worthwhile to advance the fees and costs of the defaulting party in order to obtain the issuance of the final award in its favor which it also knows will include reimbursement of its fees and costs. This alternative may result in the panel expending

time that might not be fully reimbursed, but depending on the factual context, it might result in recovering panel fees and costs that would otherwise never be paid.

Attorneys Fees' and Costs

To the extent that the non-defaulting party may have incurred excess fees and costs due to the defaulting party's failure to pay as required by the contract, the panel may also consider imposition of attorneys' fees and costs against the defaulting party. In doing so the panel must be cognizant of providing the defaulting party the opportunity to review and object to the imposition as well as the amount of fees and costs. Details of awarding attorneys' fees and costs are beyond the scope of this article.

Judicial Support

There is some judicial support for such approaches. The procedural rules of the AAA give arbitrators broad authority over payment and apportionment of arbitration fees. The methodology of allowing the non-defaulting party to pay arbitration costs and recoup them from the award on the merits is cited with approval in a AAA context in *Dealer Computer Servs. v. Old Colony Motors, Inc.* 588 F.3d 884, 888 (5th Cir. 2009) and *Lifescan, Inc. v. Premier Diabetic Servs.*, 363 F.3d 1010 (9th Cir. 2004).

IV. Conclusion

One remedy for the problem of non-paying parties is for the ARIAS – US Rules for the Resolution of U.S. Insurance and Reinsurance Disputes to be amended to include remedies and sanctions similar to those contained in the AAA's Commercial Arbitration Rules and Mediation Procedures.⁶ However, such an amendment would only be applicable to arbitrations utilizing the ARIAS rules.

In an environment where parties do not favor retainers or other advanced funds to allow arbitrators to protect themselves in the event of non-payment from a defaulting party, arbitration panels can and should be creative in delivering on their obligation while using incentives to ensure that appropriate payment is made for their services. While a party's payment or non-payment of fees and costs should never affect the outcome of the arbitron on the merits, the panel

has broad authority and discretion to time or condition the issuance of a final award on the proper and contractually bargained for payment of the panel.

¹ See sections R-57 and R-58 of the AAA's Commercial Arbitration Rules and Mediation Procedures that allow a panel to suspend a proceeding or limit the non-paying party's participation therein.

² 786 F.3d 1287 at 1294.

³ 352 F.3d 1197 at 1201.

⁴ 2015 U.S. Dist. Lexis at *38-9.

⁵ 848 So. 2d 828 at 838.

⁶ See fn. 1 and accompanying text.