Arbitration -- The Arbitrator's Duty to Disclose Past Business Relationships With a Party

John M. Murchison Jr.
Container Corporation indicates that the Supreme Court is acutely aware of the economic setting in which the cooperative activities of businessmen take place. The Court is particularly insistent that oligopolists, because of the tremendous control they already have over the market, the natural tendency to price uniformity in oligopolistic industries, and the advantageous position they are in to defeat the competitive processes, not be allowed to remove any of the uncertainties that prevent them from obtaining even firmer control of the market. The corrugated container industry was ideally conducive to oligopolistic manipulation, except for the uncertainty created by the individualized nature of the product. The exchanges of price information eliminated that uncertainty. The Supreme Court was unwilling to allow the defendants, already rich in power, that additional luxury.

Ben F. Tennille

Arbitration—The Arbitrator’s Duty to Disclose Past Business Relationships With a Party

"[W]here your treasure is, there will your heart be also."1 This generally recognized element of human nature—that a man will be partial toward his own self-interest—is the reason for the rule that "no man shall be a judge in his own cause."2 Acceptance of society's insistence that disputes among its members be resolved through the use of a judicial process, rather than through the use of violence or other forms of "self-help," depends to a great extent on the evident fairness and impartiality of the judicial system.3 In the leading case of Tumey v. Ohio,4 the Supreme Court held that it was a violation of due process to subject a defendant's liberty or property "to the judgment of a court the judge of which has a direct, personal, substantial, pecuniary interest in reaching a conclusion against him in his case."5 In Tumey, the defendant was tried and convicted by the village mayor, who received additional compensation from all those tried by him only if they were found guilty. The Supreme

1 Matthew 6:21.
2 Dr. Bonham's Case, 8 Co. 113b, 77 Eng. Rep. 646 (C.P. 1610).
3 See Hart & McNaughton, Evidence and Inference in the Law, in The Hayden Colloquium on Scientific Concept and Method 51-56 (1958).
5 Id. at 523.
Court reversed the defendant’s conviction; it did not matter that there was no evidence of actual bias against the defendant:

[T]he requirement of due process of law in judicial procedure is not satisfied by the argument that men of the highest honor and the greatest self-sacrifice could carry it on without danger of injustice. Every procedure which would offer a possible temptation to the average man as a judge to forget the burden of proof required to convict the defendant, or which might lead him not to hold the balance nice, clear and true between the State and the accused, denies the latter due process of law.6

The extent of the judge’s self-interest needed to constitute a denial of due process cannot be defined with precision.7 “Circumstances and relationships must be considered.”8 But “the administration of justice should reasonably appear to be disinterested as well as be so in fact.”9

The law regarding disqualification of judges because of self-interest applies equally to administrative adjudicators.10 In both the administrative and judicial setting, the law forces the parties to accept the findings and judgment of the adjudicator; their right to a fair and impartial hearing is guaranteed by the due process clause of the Constitution.11 A related, but different, problem regarding impartiality is presented when parties by agreement go outside the judicial system for settlement of their disputes, as in arbitration, where the constitutional right of a fair trial would not be applicable.12

“Arbitration . . . is a process by which parties voluntarily refer their disputes to an impartial third person, an arbitrator, selected by them for a decision based on the evidence and arguments to be presented before the arbitration tribunal.”13 Protection against a partial arbitrator must come either from the arbitration agreement itself, or from an applicable statute.14

---

6 Id. at 532.
8 Id. at 136.
11 U.S. Const. amend. XIV, § 1.
14 See discussion and cases cited in M. Domke, supra note 13, § 33.02.
In Commonwealth Coatings Corp. v. Continental Casualty Co., a subcontractor had sued the sureties on the bond of the prime contractor for money allegedly due for a painting job. The painting contract included an agreement to arbitrate such controversies. Each party named one arbitrator, and these two selected the third. The third arbitrator, owner of an engineering firm that provided services to construction companies, had in the past done business with the prime contractor involved in the dispute. The panel voted unanimously in favor of the prime contractor.

The subcontractor challenged the award in the district court on grounds, inter alia, that it did not know and had not been informed by either the "neutral" arbitrator or the prime contractor of these previous dealings between them. There was no contention that the arbitrator was not entirely fair and unbiased. The district court refused to set aside the award and the court of appeals affirmed. The Supreme Court granted certiorari and a divided Court reversed the lower courts and vacated the arbitration award.

The United States Arbitration Act governed the controversy in this

---

17 The decision by the United States District Court for Puerto Rico is not reported.
18 Commonwealth Coatings Corp. v. Continental Casualty Co., 382 F.2d 1010 (1st Cir. 1967).
20 393 U.S. 145 (1968).
Section 10 of this act denotes the reasons for which an award may be vacated. The Court felt that the provisions allowing vacation of the award where it was “procured by corruption, fraud, or undue means” or “where there was evident partiality . . . in the arbitrators” showed an intent on the part of Congress that arbitration be impartial. While there was no charge that the third arbitrator was guilty of fraud or bias or that he had any improper motives, the failure to disclose the past business relationship with one party violated “the strict morality and fairness Congress would have expected on the part of the arbitrator and the other party in this case.”

The Court reasoned that the constitutional basis of the rule in *Tumey* should not prevent its application to non-judicial adjudication that is governed by statutory language embodying the same concept of impartiality. A rule of the American Arbitration Association providing for disclosure by arbitrators of past relationships with parties, as well as

---

22 393 U.S. at 146-47.
24 393 U.S. at 148.
26 393 U.S. at 147.
27 Id. at 148.
28 Id. at 149, quoting AMERICAN ARBITRATION ASSOCIATION, COMMERCIAL ARBITRATION RULES § 18.
a canon of judicial ethics providing for the avoidance of actions that might raise suspicions, neither of which were directly applicable to this controversy, were noted to show that these concepts of disclosure and of avoidance of suspicions were accepted elements of what is to be considered fair conduct on the part of those who perform adjudicatory functions.

The concurring opinion by Mr. Justice White declared that the Court's ruling did not hold arbitrators to the standards of judicial decorum required of judges, but only that disclosure was required "where the arbitrator has a substantial interest in a firm which has done more than trivial business with a party . . . ." Mr. Justice Fortas' dissent denied that the failure to volunteer information constituted "evident partiality" under the Arbitration Act where there was no claim of any actual partiality, or bias, or improper motive.

In its successful efforts in the lower courts, the respondent prime contractor relied on the case of *Ilios Shipping & Trading Corp. v. American Anthracite & Bituminous Coal Corp.* for the proposition that "the mere fact that there is some business relationship between the arbitrator and one of the parties to the arbitration is not in and of itself sufficient to disqualify the arbitrator." The court in *Ilios* reasoned that since the objecting party knew the arbitrator was employed in the insurance business, he should have inquired as to any relationship between the arbitrator and the other party. Failing to do this, knowledge of the relationship will be imputed to the objecting party and he will be deemed to have waived his objection for failure to assert it earlier. Thus, one basis of the holding in *Ilios* is the imputed knowledge the objecting party had of the relationship between the arbitrator

---

29 33 Social Relations. ... [A judge] should, however, in pending or prospective litigation before him be particularly careful to avoid such actions as may reasonably tend to awaken the suspicion that his social or business relations or friendships constitute an element in influencing his judicial conduct. *Id.* at 149-50, quoting ABA CANONS OF JUDICIAL ETHICS No. 33.

30 *Id.* at 149-50.

31 *Id.* at 150 (Mr. Justice Marshall joining).

32 *Id.* at 151-52.

33 *Id.* at 152 (Justices Harlan and Stewart joined in the dissent).

34 *Id.* at 154.

35 382 F.2d 1010 (1st Cir. 1967).


37 *Id.* at 700.

38 *Id.*

39 *Id.*
and the other party. In *Commonwealth*, on the other hand, the Supreme Court emphasized that

the facts concerning the close business connections between the third arbitrator and the prime contractor were unknown to petitioner and were never revealed to it by this arbitrator, by the prime contractor, or by anyone else until after an award had been made.\(^4\)

While this may be one manner of distinguishing the *Ilios* case, there is considerable authority supporting the view that an arbitrator’s failure to disclose past business relations with a party does not constitute “evident partiality” under the Arbitration Act.\(^4\) At the same time, there are instances where the opposite view has prevailed—where the failure to disclose the relationship resulted in vacating the contested award.\(^4\)

The differences in result would seem to hinge on fine distinctions in the fact situations. Should the possibility of the relationship have been apparent to the objecting party?\(^4\) Was the relationship vague and remote,\(^4\) or was it close enough to cause concern as to the arbitrator’s impartiality?\(^4\) Although finding in favor of respondent in *Commonwealth*, the court of appeals noted the closeness of the distinctions involved:

In our opinion there is a difficult line between what should, in good faith, be volunteered, and what may be left for inquiry. We may agree with appellant that where there is a disturbingly close relationship the very failure to make disclosure could be evidence of partiality, and we think it would have been far better if there had been disclosure here. However, we cannot say that the relationship was sufficiently close to establish ‘evident partiality’ within the statute as a matter of law.\(^4\)

Undoubtedly, the trend of the courts has been to set strict limits on judicial interference with arbitration awards.\(^4\) Frequent court inter-

\(^{40}\) 393 U.S. at 146. In a Petition for Rehearing filed January 16, 1969, the respondent contends “[t]here is not a scintilla of evidence to support” the Court’s conclusion that “the facts concerning the close business connections between the third arbitrator and the prime contractor were unknown to petitioner ....” Respondent’s Petition for Rehearing at 1.


\(^{45}\) See *American Guar. Co. v. Caldwell*, 72 F.2d 209 (9th Cir. 1934).

\(^{46}\) 382 F.2d at 1011-12.

ference might frustrate "the basic purpose of arbitration, which is to dispose of disputes quickly and avoid the expense and delay of extended court proceedings." Although the action of the Court in *Commonwealth* in vacating the arbitration award and imposing a rule requiring disclosure on the arbitrator might at first glance appear to run counter to this ideal, a closer analysis indicates that the contrary is more likely. Certainly it was the aim of the Court, in formulating its rule requiring disclosure, to minimize the judicial role in arbitration. The rule formulated by the Court—that an arbitrator has a duty to disclose to the parties any dealings that might create an impression of possible bias—should strengthen the arbitration process and minimize judicial interference in at least two ways. First, requiring disclosure should give the parties additional faith in the fairness of the proceedings. Mr. Dooley advised: "Trust everybody—but cut the cards." A duty of disclosure is an additional "cut of the cards" that should tend to lessen suspicions of a losing party that he was treated unfairly. With this additional confidence in the settlement process, the loser is less likely to take his complaint to the courts. Second, the rule requiring disclosure will provide an easily recognizable standard of conduct for the arbitrator. A hazy standard regarding impartiality might lead the losing party to attempt to obtain a favorable court interpretation. Judicial review of an arbitration award would appear to be sought less often where the demarcation between acceptable and unacceptable conduct is clear. Thus, the decision in *Commonwealth* should serve to strengthen the participants' confidence in arbitration, and should decrease further the possibility of unnecessary judicial interference in the arbitration process.

JOHN M. MURCHISON, JR.

Civil Procedure—Attachment of Liability Insurance Policies

The plaintiff, a New York resident, is injured in an automobile accident in another state. The wrongdoer, who is not subject to personal jurisdiction in New York, is insured under a liability policy issued in the state of his residence by an insurance company that does business in New


48 Saxis Steamship Co. v. Multifacs Int'l Traders, Inc., 375 F.2d 577, 582 (2d Cir. 1967).

49 F. DUNNE, MR. DOOLEY'S PHILOSOPHY (1900).