Arbitration in Wonderland – Why The Reticence of The Appellate Courts Encourages *Gaming* the System

Bosworth v. Whitmore(McCoy,) (2006) 135 Cal.App 4th 536

by

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What happens when an arbitration has stalled for over 2 years and the arbitrator refuses to schedule hearings because the defendants refuse to pay their share of the arbitration fees? The just published *Bosworth v. Whitmore* case partially answers that question and provides a case study on the shortcomings of the current arbitration system.

Our office substituted into the *Bosworth* case in December of 2001, after the case had languished in "arbitration limbo" for over 2 years. Within days, we notified the arbitrator that we were new counsel and requested a hearing to determine why the case had stalled. To our utter astonishment, the arbitrator refused to convene a hearing because the very defendants the Bosworths were suing, and who had compelled arbitration, refused to pay their arbitration fees. We were caught in a classic "*Catch 22*" position: we sought to compel payment of the fees, but the arbitrator would not set a hearing to order payment of those fees until the fees were paid. Compounding the dilemma, the appellate courts are unyieldingly strict on plaintiffs who are not diligent in prosecuting their arbitration claims or who fail to apply to the trial court for relief.

CCP §1286.1: When Can Arbitration Parties Seek Court Intervention?

In the *Bosworth* case, we filed an unusual Superior Court motion to dismiss the arbitration because the defendants failed to pay their arbitration fees. We argued that the Legislative intent was frustrated and undermined when a party who seeks to compel arbitration brings the arbitration process to a standstill by deliberately refusing to pay the arbitration fees as a tactic designed solely to delay and stall the arbitration process. Moreover, we asserted that the failure to pay fees can only be viewed as inconsistent with, and therefore a *waiver* of, an intent to arbitrate.

Thus the first seminal *Bosworth* question was presented not to the arbitrator, but to the trial judge who had ordered the matter to binding arbitration:

> Can a defendant compel arbitration and then abuse the arbitration process to defeat the prosecution of plaintiff's claims?

Although we found no California case that dealt specifically with the refusal of a party who sought arbitration to pay arbitration fees, the case of *Engalla v. Kaiser Permanente Medical Group, Inc.* (1997) 15 Cal.4th 951 recognized that a party can *waive a right* to arbitration. Additionally, Code of Civil Procedure §1281.6 provides a method for petitioning the Superior Court to *replace* the arbitrator.

In *Engalla*, the plaintiff served Kaiser Permanente with a written demand for arbitration in May of 1991, and requested that the parties meet and confer regarding the selection of arbitrators. After the parties each selected their "party arbitrators," the party arbitrators had sixty days under the Kaiser arbitration rules, to select a neutral arbitrator. However, 144 days elapsed before the neutral arbitrator was selected. The next day, the plaintiff died. In the meantime, plaintiff attempted to obtain discovery from Kaiser and to take depositions. Plaintiff was met with delays in scheduling the depositions. Frustrated with the slow pace of the arbitration, plaintiff filed a lawsuit and Kaiser moved to compel arbitration.

The first issue raised by Kaiser was whether the waiver claim should be resolved by the arbitrator rather than by the court. The Supreme Court disagreed, and stated that the issue was different and more fundamental--whether Kaiser by its delay or other acts or omissions, had waived its right to compel arbitration and that *this issue was within the jurisdiction of the trial court* under section 1281.2 of the Code of Civil Procedure. *Id.*, 15 Cal 4th at 982.

Although a waiver is a voluntary relinquishment of a known right, the Supreme Court noted that waiver can also mean the *loss of an opportunity or right* as a result of a party's failure to perform an act it is required to perform, regardless of the party's intent to relinquish that right. *Id.,* 15 Cal 4th at 983. The Supreme Court concluded that Kaiser's course of delay, if unreasonable or undertaken in bad faith, might show that Kaiser had waived its right to arbitrate. *Id.,* 15 Cal 4th at 984.

In *Bosworth*, the trial court threatened to dismiss the arbitration and remand the case to Superior Court for trial if the defendants did not pay their arbitration fees forthwith. The trial judge noted for the record that the arbitration had moved so slowly that it *violated the intent of the arbitration legislation* and that the case would have already been tried and completed had it remained in the Superior Court system.[1]

TRIAL COURTS CAN ORDER AND ENFORCE ARBITRATION COMPLETION DATES

Analyzed purely in terms of its black letter holding, *Bosworth* represents good news for practitioners. For the first time, a reported California appellate decision expressly empowers aggrieved arbitration parties to use the trial courts as tools of enforcement to set specific arbitration deadlines against anyone who unreasonably delays an arbitration. *Bosworth's* explicit holding, set forth twice in the opinion, could not be clearer:

> "We hold that absent an arbitration completion deadline established by agreement, [Code of Civil Procedure] section 1283.8 gives the trial court the power, on petition of a party to the arbitration, to set a date by which the arbitration proceeding must be completed and the award rendered. The better practice is to establish that date when the case is first ordered to arbitration. However, the court has discretion to entertain a petition and set a completion date even after the arbitration is in progress..." (*Bosworth,* at 2, 19)

Under *Bosworth*, arbitrators who fail or refuse to arbitrate cases timely will now be subject to trial court scrutiny and intervention. Arbitration parties now have the enforcement tools needed to keep arbitrations from remaining in a state of suspended animation. Not so clear under *Bosworth* is how to replace an intransigent arbitrator with one who will comply with the court's arbitration completion date.

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[1] THE COURT: "Two years down the line and the case is sent to arbitration. The whole point is, you're supposed to get these done in an efficient speedy manner. This whole case has been contrary to the whole goal for sending it to arbitration. If this case had been my case from the beginning, we would be done with this by now. We would get this case done at length within a year and a half, if not a year." Reporter's Transcript (February 1, 2002, Judge Cesar Sarmiento) page 162, lines 20-28.

THE FUNDAMENTALLY DIFFERENT BASIS FOR ARBITRATION PROCEEDINGS

Arbitration was devised to offer litigants a *fast-track*, cost-effective alternative to courtroom litigation. Like most benefits in life, however, arbitration requires litigants to make some significant trade-offs.

In a very real sense, arbitration is significantly different from civil law, which arises out of the fundamental principles of democracy and constitutionalism. By its very nature, arbitration constitutes a *denial of access to the courts* and the civil litigation rules of law. Parties considering arbitration as an alternative to civil action should be mindful of the following:

(1) Parties who draft contracts with arbitration clauses (often non-negotiable) can "arbitrarily" and unilaterally deny other contracting parties entree to the constitutional protections of our judicial system;

(2) Arbitrations do not require arbitrators to be lawyers or even judges;

(3) Arbitrators do not have to follow the law;

(4) Arbitration litigants generally waive trial by jury;

(5) Arbitration litigants generally waive the right of discovery; and

(6) Arbitration litigants generally waive the right of appeal.

(7) Once a matter is ordered into arbitration, it is critical for parties to understand that there is no relief from the court system for errors of law or fact [" the arbitrator's findings on both law and fact are conclusive. The court cannot set aside an arbitrator's error of law no matter how egregious." *Moncharsh v. Heily* (1993) 3 Cal.4th 1, 8)]

AAA Rules: IS THERE EVER EXTRAORDINARY RELIEF IN ARBITRATION?

Some would argue that the root cause of the Bosworth appeal was AAA Rule 55, which states:

"If arbitrator compensation or administrative charges have not been paid in full, the AAA may so inform the parties in order that one of them may advance the required payment. If such payments are not made, the arbitrator may order the suspension or termination of the proceedings. If no arbitrator has yet been appointed, the AAA may suspend the proceedings."

Suspension of the arbitration because the defendant who compelled it has not paid arbitration fees hardly seems equitable. This rule appears to reward the intransigent party because it permits derailing the proceedings even if the aggrieved party was without blame.

AAA Rule 55 arguably rewards unethical litigants by allowing them to delay and ultimately derail arbitrations without imposing any penalty for such behavior.

This loophole for gamesmanship frustrates the goal of expedited dispute resolution supported by AAA rules, statutory enactments and case law. Under AAA Rule 55, a defendant can simply refuse to pay fees and, if the claimant cannot or will not advance the fee, watch the case disappear.

IS *ANTICIPATORY FAILURE TO ACT* A NEW STANDARD?

Having affirmed the court's authority to set an arbitration completion date and avoid the legislative "Catch 22," the appellate court then *diluted* its decision by overturning the trial court's removal and replacement of the arbitrator who advised *"point blank"* that he was *unable to represent that he could complete* the arbitration by the ordered completion date. The Court of Appeal reached this dubious conclusion by accepting the argument that the arbitrator's *failure to act* was only "*anticipatory*." (*Bosworth*, at 552)

Bosworths had filed their motion to set an arbitration completion date because their home was only 40% completed but the contractor was 90% paid by the disbursement company that should have been watching the progress and protecting the Bosworth's construction loan funds. The construction lender, less than pleased that almost all construction loan proceeds had been paid out, refused to grant further extensions and commenced foreclosure proceedings. The only way the Bosworths could dodge this foreclosure bullet was to pursue their claims to judgment. The trial court used the arbitrator's declaration that he was unable to complete the arbitration between *all parties* by the arbitration completion date as the basis for appointing a new arbitrator who would comply with the court's completion order.

> "In the event Builder's Disbursement participates then *I can make no representations or otherwise to the Court* that the arbitration proceedings between all parties will be complete by the Court ordered date of March 31, 2002." (Arbitrator Dymond's February 1, 2002 Report to the Court (*Bosworth,* at 542)

The trial court correctly found Dymond's statement was a "failure to act" under the statute. Since the trial court had already ordered an arbitration completion deadline, and Dymond could not comply with that deadline, the only recourse was to replace the arbitrator. The trial court's reasonable rationale for doing so was *exigent circumstances*: a new arbitrator was needed to issue an arbitration award in sufficient time to prevent irreparable injury.

> "Regardless, even if Dymond could not complete the arbitration by March 31, this inability was not caused by his "fail[ure] to act" within the meaning of section 1281.6. The arbitration had been delayed for various reasons, none of which were attributable to Dymond. For instance, the Bosworths failed to comply with Dymond's order to provide their final defect list, damages estimate, and expert reports by October 15, 2000. They did not submit the required documentation until February 28, 2001. Similarly, McCoy was also responsible for a two-month delay because he did not pay his arbitration fees in a timely manner. The AAA (not Dymond) also caused delay because it failed to properly notify the subcontractors of the arbitration, an administrative error that required Dymond to continue the arbitration hearing (with the consent of the parties) for two months. Even drawing all inferences in favor of the trial court's ruling, this record does not support a finding that Dymond failed to act within the meaning of section 1281.6. Thus, the trial court's removal of Dymond was an abuse of discretion." (*Bosworth, at* 552)

It is perplexing that the *Bosworth* court affirmed the trial court's imposition of an arbitration completion date, yet reversed the removal of the arbitrator who advised that he could not comply with the completion date. According to *Bosworth*, the arbitrator's *future unavailability to perform his court-ordered duties* was only an "*anticipatory failure*" and it was an abuse of discretion for the trial court to remove him for such a "failure to act."

> "Although an arbitrator's inability to meet a court ordered deadline might in some circumstances constitute a failure to act justifying removal, the record does not support such a finding here. Dymond simply informed the court that he could not promise that the arbitration would be complete by March 31 if the Bosworths insisted (as they did) on the participation of BDI. Consequently, as of February 1 -- the day the trial court removed Dymond as arbitrator -- there was at best an *anticipatory failure* by Dymond to comply with the March 31 deadline." (*Bosworth*, 551-552, emphasis in original)

The *Bosworth* court seems to suggest that the trial court should have delayed replacing the arbitrator until his stated inability to comply with a court order became "actual." Waiting for the actual failure on March 31, however, would have left no time to appoint a new arbitrator, would have resulted in *actual foreclosure*.

Waiting for March 31 would have made a nullity of the court's order mandating an arbitration completion date.

A fundamental problem with the *Bosworth* decision is the lack of a *"bright line test",* to determine when the trial court can or cannot replace an arbitrator**.** While the opinion makes passing reference to "some circumstances" (*Bosworth*, at 551) or "limited circumstances" (*Bosworth*, at 551) which might justify the removal of an arbitrator, the court never explains what those "circumstances" are.

If Dymond had a duty to meet the court-ordered deadline, he therefore also had a duty to promise he could meet that deadline. His refusal to guarantee compliance was thus a refusal to fulfill his duties and an unequivocal "failure to act."

SUMMARY

Trial courts should have *unfettered* discretion to remove arbitrators who do not keep arbitrations on a fast track or who fail or refuse to comply with court orders to expedite the proceedings. While trial courts under *Bosworth* may question their power to remove arbitrators who flout or ignore their responsibility to expedite proceedings, they should *not refrain* from intervening to protect litigants who wish nothing more than to expedite arbitrations and prevent irreparable injury. If a trial court feels uncertainty in appointing a substitute arbitrator it must ask "if not now, then when?"

Arbitrations have become the "*Wild West*" in California and, unfortunately, we have no marshal. We must await future appellate decisions to provide guidelines on when a trial court can remove an arbitrator. Meanwhile, attorneys will continue "*gaming*" the system. It seems clear that the historic reluctance of courts to intervene in arbitrations has simply outlived its erstwhile usefulness.