

# Enforcing Third-Party Discovery in Arbitration

## Location of Arbitrators May Impact Ability to Obtain Documents/Testimony Prior to Hearing

By Lisa M. Eddington and Howard S. Suskin, Litigation News Guest Editors

**A** party's ability to compel production of discovery subpoenas directed to nonparties in cases governed under the Federal Arbitration Act (FAA) may vary significantly based on the venue of the arbitration. Depending on the circuit, the court will either enforce the subpoena or decline to do so at any time short of actual appearance at a hearing before the arbitrator(s).

A decision from the Northern District of Illinois highlights this issue. Specifically, in *Alliance Healthcare Services, Inc. v. Argonaut Private Equity, LLC*, nonparties received subpoenas calling for oral testimony and production of records before a member of the arbitration panel at a preliminary hearing. Addressing a motion to compel, the *Alliance Healthcare* court recognized the split in the circuits over the arbitrator's ability to order pre-hearing discovery from a nonparty.

Relying in part on a Second Circuit decision quashing a pre-hearing subpoena, the court held that any rule against compelling nonparties to participate in discovery does not apply to a situation in which a nonparty is to appear at a pre-hearing conference before any of the arbitrators. The court further found that nothing in the language of the FAA states that an arbitrator may invoke the subpoena power only at the time of the final hearing.

### CIRCUITS SPLIT

In arbitration proceedings conducted by the Financial Industry Regulatory Authority (FINRA) and other securities self-regulatory organizations, issues often arise as to the permissible scope of discovery. When parties to an arbitration seek judicial enforcement of arbitrators' discovery subpoenas, courts have not always agreed on what the FAA allows.

The split regards the proper interpreta-

tion of Section 7 of the FAA and, specifically, whether Section 7 grants an arbitrator the authority to order pre-hearing discovery from nonparties. The Sixth and Eighth Circuits have held that the power to order pre-hearing document production from a nonparty is implicit in the power to order the production of documents at a hearing.

The Second and Third Circuits disagree, finding that Section 7 of the FAA unambiguously limits an arbitrator's subpoena power to instances in which the nonparty is to appear (literally) before the arbitrator. Although generally following the Second and Third Circuits, the Fourth Circuit has suggested that an exception might be appropriate upon a showing of special need or hardship.

In reaching their decisions, the circuits have viewed the goals of arbitration differently. On the one hand, some have reasoned that a reduction in the efficiency of the arbitration process may occur if parties do not have the opportunity to review and digest relevant evidence prior to an arbitration hearing.

On the other hand, some courts have reasoned that allowing pre-hearing discovery from nonparties will lessen the incentive to limit the scope of discovery. This strengthens the incentive to engage in costly and time-consuming fishing expeditions.

### SECTION 7 OF THE FAA

Section 7 of the FAA governs discovery from nonparties in arbitrations. Section 7 provides in pertinent part as follows:

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 a proper case to bring with him or them any book, record, document or paper which may be deemed material as evidence in

the case. . . . [I]f any person or persons so summoned to testify shall refuse or neglect to obey said summons, upon petition the United States district court for the district in which such arbitrators, or a majority of them, are sitting may compel the attendance of such person or persons before said arbitrator or arbitrators, or punish said person or persons for contempt in the same manner provided by law for securing the attendance of witnesses or their punishment for neglect or refusal to attend in the courts of the United States.

### SUBPOENAS UPHELD: THE SIXTH AND EIGHTH CIRCUITS' IMPLICIT POWER

In *American Federation of Television and Radio Artists, AFL-CIO v. WJBK-TV*, a party sought to enforce a subpoena that directed a nonparty to appear and produce documents prior to the arbitration hearing. The Sixth Circuit looked to Section 7 of the FAA for guidance in deciding whether the district court had authority to enforce the subpoena in an arbitration.

The court found that Section 7 "implicitly include[d] the authority to compel the production of documents for inspection by a party prior to the hearing." The court, however, did not reach the question of whether the arbitrator may subpoena a third party for a discovery deposition relating to a pending arbitration proceeding.

Similarly, in *In re Security Life Insurance Co. of America*, a third party was subpoenaed to produce documents prior to an arbitration hearing. The Eighth Circuit held that "implicit in an arbitration panel's power to subpoena relevant documents for production at a hearing is the power to order the production of relevant documents for review by a party prior to the hearing." In reaching its decision, the court reasoned that "[a] lthough the efficient resolution of disputes

through arbitration necessarily entails a limited discovery process . . . this interest in efficiency is furthered by permitting a party to review and digest relevant documentary evidence prior to the arbitration hearing."

#### **SUBPOENAS QUASHED: THE SECOND AND THIRD CIRCUITS' RESTRICTED POWER**

In *Hay Group, Inc. v. E.B.S. Acquisition Corp.*, the Third Circuit looked first to the text of Section 7 in deciding whether to enforce a subpoena to a nonparty to produce documents prior to a hearing. The court found that the language unambiguously restricts an arbitrator's subpoena power to situations in which the nonparty is called to appear in the physical presence of the arbitrator.

In reaching its decision, the court relied on the language requiring a nonparty "to bring" items "with him" as well as the word "and" in the first sentence of Section 7. The court noted that requiring document production to be made at an actual hearing may discourage parties from issuing large-scale subpoenas to nonparties.

This chilling effect is due in part to the parties being "forced to consider whether the documents are important enough to justify the time, money, and effort that the subpoenaing parties will be required to expend if an actual appearance before an arbitrator is needed." The court noted that if it permitted pre-hearing document production from nonparties, there is "more incentive to engage in fishing expeditions that undermine some of the advantages of the supposedly shorter and cheaper system of arbitration."

The Second Circuit in *Life Receivables Trust v. Syndicate 102 at Lloyd's of London*, joined the Third Circuit in holding that Section 7 does not authorize an arbitrator to compel pre-hearing document discovery from a nonparty. As in *Hay Group*, the court found the language of Section 7 to be straightforward and unambiguous, noting that although "[t]here may be valid reasons to empower arbitrators to subpoena documents from third parties, [the court] must interpret a statute as it is, not as it might be. . . ."

#### **THE FOURTH CIRCUIT'S SHOWING OF SPECIAL NEED OR HARSHSHIP**

In an earlier decision, *COMSAT Corp. v. National Science Foundation*, the Fourth

Circuit generally took the approach favored by the Second and Third Circuits. It found that the FAA does not grant an arbitrator the authority to order nonparties to appear at deposition or to demand pre-hearing document production from nonparties. Unlike the Second and Third Circuits, however, the Fourth Circuit suggested, in dicta, that a court might compel the pre-hearing production of documents from a nonparty upon a showing of special need or hardship.

The court acknowledged that the rationale for constraining an arbitrator's subpoena power is clear: A "hallmark of arbitration—and a necessary precursor to its efficient operation—is a limited discovery process." The court reasoned, however, that in a complex case, "the much-lauded efficiency of arbitration will be degraded if the parties are unable to review and digest relevant evidence prior to the arbitration hearing." The Fourth Circuit did not define "special need" but noted that, at a minimum, a party would be required to demonstrate that the information it seeks is otherwise unavailable.

#### **CONCLUSION AND PRACTICAL CONSIDERATIONS**

The current split among the courts as to the scope of pre-hearing arbitration discovery undermines the national uniformity in the arbitration process that the FAA was designed to promote. Ultimately, the U.S. Supreme Court may step in to resolve the split among the circuits regarding the proper interpretation of the FAA, unless Congress acts first and clarifies the FAA's provisions. To date, however, none of the parties in the cases discussed above has sought U.S. Supreme Court review. Accordingly, it may be a long time before the split is resolved.

Predicting how the Supreme Court would resolve the split is not easy. On the one hand, in strongly favoring enforcement of arbitration agreements, the Supreme Court has expressed its view that arbitration procedures afford parties a full and fair mechanism to resolve their disputes. For that reason, the inability of parties to enforce arbitrators' subpoenas against nonparties under the FAA might lead the Court to take an expansive approach in

facilitating that discovery. On the other hand, the Supreme Court also has recognized that arbitration procedures, including the availability of discovery, are more limited than what is available under the Federal Rules of Civil Procedure. As a result, the inability of parties to conduct discovery from nonparties might not be of great concern to the Court.

As long as the split among lower courts remains, attorneys handling FINRA and other self-regulatory organization arbitrations need to be up-to-date about the law on this issue in the particular jurisdiction in which they are arbitrating. Parties seeking to enforce arbitrators' subpoenas may do so under Section 7 of the Federal Arbitration Act only in the U.S. district court for the district in which the arbitrators, or a majority of them, are sitting. Seeking enforcement from another court where the nonparty may be located is not an option. Therefore, when a claimant has a choice of places in which to conduct the arbitration, knowing how that district's courts have weighed in on discovery from nonparties may be one factor to consider in selecting the arbitration forum, particularly where the claimant expects to require significant discovery from nonparties.

---

Full story at <http://tinyurl.com/LNw12-fc-FAA>

An earlier version of this article appeared under the title "Can an Arbitrator Order Prehearing Discovery from a Nonparty?" in Vol. 22, No. 1 (Fall 2011) of the Securities Litigation Committee newsletter.

---

#### **RESOURCES:**

- *American Federation of Television and Radio Artists, AFL-CIO v. WJBK-TV (New World Communications of Detroit, Inc.)*, 164 F.3d 1004 (6th Cir. 1999).
- *In re Security Life Insurance Co. of America*, 228 F.3d 865 (8th Cir. 2000).
- *Hay Group, Inc. v. E.B.S. Acquisition Corp.*, 360 F.3d 404 (3d Cir. 2004).
- *Life Receivables Trust v. Syndicate 102 at Lloyd's of London*, 549 F.3d 210 (2d Cir. 2008).
- *COMSAT Corp. v. National Science Foundation*, 190 F.3d 269, 275 (4th Cir. 1999).
- *Alliance Healthcare Services, Inc. v. Argonaut Private Equity, LLC*, No. 11 C 3276, 2011 WL 3489807 (N.D. Ill. Aug. 9, 2011).