Obtaining Pre-hearing Discovery From Non-parties In Arbitration

By Jeremy M. Taylor and David P. Saunders

One of the great advantages of the arbitration process -- in theory -- is a streamlined and efficient discovery process. As one federal court of appeals explained: “Parties to a private arbitration agreement forego certain procedural rights attendant to formal litigation in return for a more efficient and cost-effective resolution of their disputes. A hallmark of arbitration -- and a necessary precursor to its efficient operation -- is a limited discovery process.”

Still, in some arbitrations, the “streamlined” discovery process can become anything but that. After all, today’s arbitrations are not limited to simple, straightforward cases -- disputes of enormous complexity routinely are submitted to arbitration. Those matters can involve mountains of evidence, and, of course, that evidence is not always exclusively in the hands of the parties that agreed voluntarily to submit their dispute to arbitration. Thus, as in the case of court-based litigation, discovery from non-parties often will be an important part of the arbitral process.

When it comes to obtaining discovery from non-parties in the arbitration context, however, what does the process for obtaining such discovery look like? In the world of litigation, the game plan is fairly straightforward: you serve your subpoenas on the non-parties; collect and review the documents those non-parties produce to you; take the non-parties’ depositions when you and your opponent can agree to schedule them; learn what relevant information is out there -- both good and bad -- and then package the gathered information for presentation at trial. Thus, while the process can be long, costly, frustrating, grueling, or all of the above, the rules of the game are well established and well known.

That is not the case in arbitration, where the rules of the game for obtaining prehearing discovery from non-parties are far less clear. Indeed, those rules can vary significantly from case to case.

At least -- and perhaps, at most -- everyone generally agrees on the starting point: Section 7 of the Federal Arbitration Act, 9 U.S.C. § 7. Section 7 provides arbitrators with authority to issue subpoenas, including to obtain evidence from non-parties to the arbitration: “The arbitrators … 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.”

In the context of prehearing discovery, however, Section 7’s language begs an obvious question for the practitioner: Can a non-party be compelled by an arbitrator’s subpoena to appear for a deposition or produce documents to a requesting party as part of prehearing discovery? Looking only at the language of Section 7, the answer would appear to be “no.” After all, under Section 7, the attendance of the witness, with or without documents, is to be “before them or any of them,” with “them” being the arbitrators.

Reading that “before them” language in Section 7 for the first time, many a seasoned litigator might respond, “That just cannot be right.” No prehearing discovery from non-parties? “Impossible.” No non-party depositions unless it is before the arbitrator? “Ridiculous.” No documents from non-parties until the arbitration hearing itself? “Absurd.”

So, going on instinct and based on past practice, many litigators new to the world of arbitration simply assume that the answer must be “yes” and that they can proceed with prehearing discovery against non-parties by following the same process common in court-based litigation.

Not so fast. In fact, three federal courts of appeal have directly addressed the Section 7 question of whether a non-party can be compelled by an arbitrator’s subpoena to appear for a deposition or produce documents as part of prehearing discovery, and each of those courts has offered a different answer -- answers that fairly can be summed up as “yes,” “no,” and “maybe.” A practitioner must understand those different interpretations of Section 7 and know what options may be available for obtaining prehearing discovery from non-parties.

“A party might, under unusual circumstances, petition the district court to compel pre-arbitration discovery upon a showing of special need or hardship.” [Fourth Circuit]

“Maybe” The Fourth Circuit’s “Special Need” Approach

The Fourth Circuit squarely addressed the question of whether Section 7 authorizes an arbitrator to subpoena non-parties for prehearing discovery in COMSAT Corp. v. National Science Foundation.2 While the Fourth Circuit declined to read Section 7 as broadly authorizing prehearing discovery from non-parties, the court -- as the first of the federal circuits to address the question -- not surprisingly left itself some wiggle room by creating an exception to its own rule that such prehearing discovery generally is not available.
by holding that such discovery might be obtainable if a party can show that a “special need” exists.3

In COMSAT, the National Science Foundation (“NSF”) entered into an agreement with Associated Universities, Inc. (“AUI”) to have AUI administer a nationwide network of research telescopes. AUI then entered into a contract with COMSAT to build such a telescope in West Virginia. A dispute arose between COMSAT and AUI over AUI’s liability for cost overruns, as a result of which COMSAT and AUI submitted their claim to arbitration.4

As part of the prehearing discovery process, and at COMSAT’s request, the arbitrator issued a subpoena to NSF requiring the agency to produce to COMSAT all documents related to the telescope at issue. NSF refused to comply. In response, COMSAT requested, and the arbitrator issued, three additional subpoenas -- all returnable to COMSAT’s counsel -- directing two NSF employees and NSF’s “Document Custodian” to appear and produce certain documents. When NSF again refused to comply with the subpoenas, COMSAT turned to the federal district court to enforce the subpoenas. The district court ordered NSF to comply.5

Thus, what “minimum” showing of “special need” a party needs to make remains an open question. In COMSAT, for example, the Fourth Circuit noted that COMSAT would not have been able to make the “minimum” showing because the documents it had requested were obtainable either from the opposing party or through a Freedom of Information Act request.13 By comparison, in In re Campania, the District Court for the Eastern District of New York found that a “special need” existed when the subpoena related to evidence located on a ship that was about to leave port with its return to the United States uncertain.12 What qualifies as a “special need” short of such an extreme situation, however, remains a case-by-case determination with little guiding precedent.

“Yes” The Eighth Circuit’s Implied Powers Approach

If the Fourth Circuit left the door for obtaining prehearing discovery from non-parties cracked open in COMSAT, the Eighth Circuit kicked that same door wide open in In re Security Life Insurance Company of America.13 While not the first court to do so,14 the Eighth Circuit was the first federal circuit to read Section 7 as implicitly authorizing arbitrators to issue subpoenas to non-parties to compel their attendance at prehearing depositions or to compel prehearing document production.

The case involved a reinsurance contract between Security Life and a group of seven reinsurers, including Transamerica. The contract, to be managed by Duncanson & Holt (“D&H”), provided that the seven reinsurers would assume 85% of the risk under Security Life’s policies. Subsequently, a $14 million judgment was entered against Security Life, but the reinsurers refused to acknowledge liability for their share of the judgment, taking the position that Security Life had failed in its dealings with D&H to honor the “counsel and concur” provision of the reinsurance contract.15

Pursuant to an arbitration clause in the reinsurance contract, Security Life demanded arbitration against D&H. As part of prehearing discovery, Security Life petitioned the arbitration panel for a subpoena against Transamerica, “requir[ing] Transamerica to produce documents and to provide the testimony of a certain employee.” Transamerica refused to respond, however, claiming that, because it was not a party to the arbitration, the subpoena issued by the panel was not authorized under the FAA. Security Life then successfully petitioned the district court to compel Transamerica to comply with the subpoena.16

On appeal, the Eighth Circuit affirmed, taking a very different approach from that of the Fourth Circuit in COMSAT.17 The Eighth Circuit acknowledged that Section 7 “does not … explicitly authorize the arbitration panel to require the production of documents for inspection by a
party.” But the court chose not to end its analysis there. Instead, the court decided that, on balance, the “efficiency” of the arbitration process was furthered by permitting litigation-like prehearing discovery with regard to non-parties: “Although the efficient resolution of disputes through arbitration necessarily entails a limited discovery process, we believe this interest in efficiency is furthered by permitting a party to review and digest relevant documentary evidence prior to the arbitration hearing.” Driven by this policy consideration, and finding some comfort in Transamerica’s close relationship to the underlying arbitration, 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.”

“No” The Third Circuit’s Textualist Approach

After the COMSAT and Security Life rulings, parties to arbitral proceedings could expect that they either could obtain litigation-style prehearing discovery from non-parties or, at the very least, could have an opportunity to show why they had a “special need” for such discovery. Then, the Third Circuit jumped into the fray. Rather than choose sides in the somewhat-limited debate between the Fourth and Eighth Circuits, the Third Circuit rejected the rationale of both, holding instead, in Hay Group, Inc. v. E.B.S. Acquisition Corp., that a third party may not be compelled by an arbitrator’s subpoena to produce documents to a party as part of prehearing discovery.

The facts of the case were straightforward. An employee of Hay Group left to join another company. The employee’s separation agreement included an anti-solicitation provision that Hay Group later alleged the employee violated. Arbitration followed. At Hay Group’s request, the arbitration panel issued a subpoena against the employee’s current employer, E.B.S., for the production of certain related documents. E.B.S. refused to comply with the subpoena and Hay Group sought enforcement from the district court. The district court enforced the subpoena.

In quashing the subpoena, the Third Circuit -- with now-Supreme Court Justice Samuel Alito writing the opinion -- took a textualist approach to interpreting Section 7, holding that “Section 7’s language unambiguously restricts an arbitrator’s subpoena power to situations in which the non-party has been called to appear in the physical presence of the arbitrator and to hand over the documents at that time.” The court broke down the language of Section 7, noting that “[t]he only power conferred on arbitrators with respect to the production of documents by a non-party is the power to summon a non-party ‘to attend before them or any of them as a witness’ and in a proper case to bring with him or them any book, [or] record.” Going a step further, the court reasoned that “the use of the word ‘and’ makes it clear that a non-party may be compelled ‘to bring’ items ‘with him’ only when the non-party is summoned ‘to attend before [the arbitrator] as a witness.’” The court found support for its strict reading of Section 7 in the similar language of the pre-1991 version of Rule 45 of the Federal Rules of Civil Procedure, which also had been interpreted to prohibit the issuance to non-parties of prehearing document subpoenas.

The Third Circuit went on to explain why it did not consider its strict reading of Section 7 to be “absurd.” In fact, the court stated that “we believe that a reasonable argument can be made that a literal reading of Section 7 actually furthers arbitration’s goal of ‘resolving disputes in a timely and cost efficient manner.’” The court offered three reasons for its ruling. First, the court took comfort in the fact that the federal courts had operated for decades within the boundaries set by the pre-1991 version of Rule 45.

Second, the court recognized the arbitrator’s limited power to affect those parties who had not agreed to the arbitrator’s jurisdiction. Third -- and perhaps most practically given what is supposed to be the “limited discovery process” in arbitration -- the court reasoned that its interpretation of Section 7 would “encourage the issuance of large-scale subpoenas upon non-parties,” while a contrary interpretation of Section 7 would create “less incentive to limit the scope of discovery and more incentive to engage in fishing expeditions that undermine some of the advantages of the supposedly shorter and cheaper system of arbitration.”

Notably, the Third Circuit was clear that it considers itself to be in direct conflict with the Fourth Circuit’s COMSAT decision and the Eighth Circuit’s holding in Security Life. While the Third Circuit found the Fourth Circuit’s interpretation of Section 7 to be “largely consistent” with its own, the Third Circuit stated that it “cannot agree” with the Fourth Circuit’s “dicta” allowing for the possibility of a “special need” exception. As the Third Circuit stated, “while such a power might be desirable, we have no authority to confer it.” The Third Circuit was just as blunt in rejecting the Eighth Circuit’s “power-by-implication analysis” in Security Life, reasoning that, because the FAA confers the power to compel a non-party witness to bring documents to a hearing before the arbitrator, but is silent with regard to the power to compel prehearing discovery, “the FAA implicitly withholds the latter power.”

Where does this leave the practitioner?

Given the growing popularity of arbitration in recent years, the frequent importance of obtaining prehearing discovery from non-parties, the general acceptance of that practice in
litigation, and the conflict that currently exists among the federal circuits as to the ability to obtain prehearing discovery from non-parties in arbitration, something will have to give. Perhaps it will come in the form of an amendment to Section 7 of the FAA, as Rule 45 of the Federal Rules of Civil Procedure previously was amended. Perhaps it will come in the form of the U.S. Supreme Court resolving the conflict. But, for the practitioner with an arbitration currently in the prehearing discovery stage, those longer-term resolutions are of little help today. Today’s question is more straightforward: What do I do?

Outside [the Third, Fourth, or Eighth Circuit], … practitioners have to guess…

For the practitioner whose arbitration falls under the umbrella of the Third, Fourth, or Eighth Circuit, the answer is fairly clear. If you are in the Eighth Circuit, you may charge ahead with obtaining prehearing discovery from non-parties, just as you would if your case was before a federal district court. If you are in the Third Circuit, you cannot. If you are in the Fourth Circuit, you contemplate what “special need” for the discovery you may have, perhaps looking to see if a ship -- proverbial or not -- with your evidence aboard is heading out of port.

Outside those circuits, however, practitioners have to guess at the rules of the game when it comes to obtaining prehearing discovery from non-parties.

District courts have faced the same problem. In one case in the Southern District of New York, for example, the district court followed the Eighth Circuit’s approach, but only to the extent it required a non-party to produce documents on a prehearing basis.37 The district court decided that the logic of Security Life could not be extended to require non-parties to appear for prehearing depositions.38 A nother district court, the Northern District of Georgia, weighed the logic of the Eighth Circuit’s and Third Circuit’s competing approaches and decided to adopt the Eighth Circuit’s approach in full.39

So, is there a “safe” option for obtaining discovery from non-parties on a prehearing basis in arbitration, one that would be acceptable to each of the federal circuits that has interpreted Section 7? Perhaps, but with one important caveat -- the prehearing discovery must be conducted, at least in part, before the arbitrator.

This option was suggested by Judge Chertoff in his concurring opinion in the Third Circuit’s Hay Group case when he wrote separately “to observe that our opinion does not leave arbitrators powerless to require advance production of documents when necessary to allow fair and efficient proceedings.”40 Judge Chertoff’s solution was for the arbitrator to compel the non-party witness to appear with documents before the arbitrator, who then could adjourn the hearing to allow the parties to review the produced documents.41 Judge Chertoff surmised -- correctly, in all likelihood -- that many non-parties would agree to produce the requested documents to the parties without the need for a hearing to forego the inconvenience of an appearance.42

Proceeding in the manner suggested by Judge Chertoff would not be without its potential downsides -- be it in terms of cost, time, or case strategy -- particularly if the arbitrator chooses to have a more active role than simply adjourning the hearing. In the case of a prehearing deposition, for example, Judge Chertoff’s process probably would require the arbitrator to remain present throughout the testimony unless the non-party waived that requirement. As a result, counsel would have to decide whether they want the arbitrator to hear raw testimony. And, all of this assumes, of course, that the arbitrator is willing to proceed with discovery in this manner, hardly a given. But, in that case, when counsel makes the reasoned decision that prehearing discovery from a non-party is necessary -- and the arbitrator agrees -- counsel choosing to proceed can take some comfort in the fact that another federal circuit -- the Second Circuit -- has examined a somewhat similar process and essentially blessed it.

In Stolt-Nielsen SA v. Celanese AG,43 Celanese was a party to an arbitration dealing with anti-competitive behavior in the shipping business. The arbitration arose after a supplier, Stolt-Nielsen SA (“Stolt”), pled guilty to charges of criminal conspiracy to rig bids and fix prices. Stolt was not a party to the actual arbitration.44

At Celanese’s request, the arbitrators issued a series of subpoenas to Stolt’s former general counsel and its custodian of records, seeking both testimony and the production of documents. But, in contrast to the subpoenas at issue in COMSAT, Security Life, and Hay Group, the subpoenas issued in Stolt directed the recipients to “appear and testify in an arbitration proceeding” and to bring the requested documents with them. Stolt nonetheless refused to comply with the subpoenas and moved to quash the subpoena issued to its former general counsel in the district court. Celanese countered by moving to compel Stolt’s compliance with the subpoenas issued to Stolt’s custodian of records.45 The district court enforced the subpoenas, holding that subpoenas that “call for the non-party to appear before the arbitrators themselves”46 comply with Section 7’s requirement that the “arbitrators … summon witnesses to testify ‘before them.’”47

On appeal to the Second Circuit, Stolt argued that, because the hearing that the witnesses were called to attend was not a “trial-like arbitration hearing on the merits,” the challenged subpoenas were a “thinly disguised attempt” to compel prehearing discovery beyond Section 7’s authorization.48 Thus, while Stolt asked the Second Circuit “to decide
whether Section 7 authorized arbitrators to issue subpoenas to non-parties to compel pre-hearing discovery” -- the same issue squarely addressed by the Fourth, Eighth, and Third Circuits -- the Second Circuit declined to do so.49

Instead, the Second Circuit held that “Section 7 unambiguously authorizes arbitrators to summon non-party witnesses to give testimony and provide material evidence before an arbitration panel,”50 determining that this power was “limited only by the requirement that the witness be summoned to appear ‘before [the arbitrators] or any of them’ and that any evidence requested be material to the case.”51 Moreover, the court read Section 7 to “authorize[] the use of subpoenas at preliminary proceedings even in front of a single arbitrator.”52 The court rejected Stolt’s argument that subpoenas at preliminary proceedings even in front of a single arbitrator.53

Conclusion

At some point in the not-too-distant future, an answer likely will be provided to the question of whether a non-party can be compelled by an arbitrator’s subpoena to appear for a deposition or produce documents as part of prehearing discovery in arbitral proceedings. The Supreme Court may choose to weigh in on the question, for example, or the FAA may be amended. Until that time, however, practitioners may have to be aware of the competing interpretations of Section 7 and of the option to proceed with prehearing discovery pursuant to the process suggested by Judge Chertoff in Hay Group and recently endorsed by the Second Circuit in Stolt.

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1 COMSAT Corp. v. Nat’l Science Found., 190 F.3d 269, 276 (4th Cir. 1999) (citing Burton v. Bush, 614 F.2d 389, 390-91 (4th Cir. 1980) ("When contracting parties stipulate that disputes will be submitted to arbitration, they relinquish the right to certain procedural niceties which are normally associated with a formal trial.")
2 190 F.3d 269 (4th Cir. 1999).
3 Id. at 275-76.
4 Id. at 271-72.
5 Id. at 272-74.
6 Id. at 278.
7 Id. at 275.
8 Id.
9 Id. at 276 (following Burton, 190 F.2d at 391).
10 Id. at 276.
11 Id. at 276-77.
12 In re Campana, No. 03 CV 5382(ERK), 2004 WL 1084243, *3 (E.D.N.Y. Feb. 6, 2004); see also In re Deiulenaer Compagnia Di Navigazione, 198 F.3d 473, 479 (4th Cir. 1999).
13 228 F.3d 865 (8th Cir. 2000).
15 Id. at 867.
16 Id. at 868-69.
17 Id. at 872.
18 Id. at 870.
19 Id.
20 Id. at 870-71 (citing Meadows).
21 360 F.3d 404, 411 (3d Cir. 2004).
22 Id. at 405-06.
23 Id. at 407.
24 Id. at 407 (quoting 9 U.S.C. § 7) (emphasis in original).
26 Id.
27 Id. at 409.
28 Id. at 409 (quoting Painewebber Inc. v. Hofmann, 984 F.2d 1372, 1380 (3d Cir. 1993)).
29 Id.
31 COMSAT, 190 F.3d at 276.
32 Hay Group, 360 F.3d at 409 (citing COMSAT, 190 F.3d at 269).
33 Id. at 408-10.
34 Id. at 409-410.
35 Id. at 410.
36 Id. at 408.
38 Atmel Corp., 371 F. Supp. 2d at 403.
40 Hay Group, 360 F.3d at 413.
41 Id. at 413-14.
42 Id. at 413.
43 430 F.3d 567 (2d Cir. 2005).
44 Id. at 569-70.
45 Id. at 569-71.
46 Id. at 571.
48 Id. at 577.
49 Id. at 569.
50 Id. at 580.
51 Id. at 578-79 (quoting 9 U.S.C. § 7).
52 Id. at 579.
53 Id. at 580.