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Practical Solutions To The Umpire Selection Quagmire

Law360, New York (September 10, 2012, 1:05 PM ET) -- As a number of recent cases highlight, selecting an appropriate arbitration panel to preside over a reinsurance dispute has become a contentious, expensive and time-consuming exercise.

Parties who contractually agreed to have their disputes resolved via arbitration are now spending an inordinate amount of time in courtrooms, asking judges to resolve disputes over umpire selection. Such fights serve only to make reinsurance disputes longer, more expensive and more public — three of the most important problems arbitration was designed to solve.

Moreover, depending on the identity of the person a court selects, if it selects anyone, a fourth benefit of arbitration — resolution of disputes by knowledgeable industry professionals — may be undermined.

Concerns over panel selection certainly are not new, but prior efforts to address them must be viewed through the prism of recent experiences and new case law. One popular proposal has involved so-called "all-neutral" panels. Such an approach is unquestionably appealing in theory, if not in practice, but the last two decades have shown that when a dispute arises, industry participants in the United States typically are not interested in "all neutral" panels. The market, for now, has spoken.

Others have suggested, and likely genuinely believe, that the debate over umpire selection is overblown because the identity of the umpire is not a particularly significant factor in the resolution of a dispute. Although it is difficult to prove definitively whether they are right — there is no public data on the outcomes of (largely) confidential arbitrations — there can be little doubt that many industry representatives do not generally share this view, as the recent spate of litigation over umpire selection proves.

The Problem With Panel Selection

Many current reinsurance disputes arise under contracts that do not provide a detailed mechanism for selecting an umpire. Those contracts most often specify that each party will name its own arbitrator, and the two arbitrators will select an umpire. Unfortunately, the contracts often fail to set forth a concrete timetable for completing the umpire selection process and lack a mechanism for resolving a deadlock when the arbitrators do not agree.

Those flaws are exacerbated by the fact that many clients believe that the identity of the umpire is case-altering, if not case-dispositive. The confluence of those factors often results in a long, drawn-out selection process that may result in litigation.

Recent Case Law

Three lessons in particular emerge from a review of recent case law. First, the sheer number of recent reinsurance cases in which courts are asked to select an arbitrator or umpire reveals how critical and contentious this issue has become. See, e.g., IRB-Brasil Resseguros S.A. v. Nat'l Indemn. Co. (S.D.N.Y. Oct. 6, 2011); Safety Nat'l Cas. Corp. v. Certain Underwriters at Lloyd's (M.D. La. Aug. 16, 2011); Arrowood Indemn. Co. v. Clearwater Ins. Co., No. 11-6018055-S (Conn. Super. Ct. July 26, 2011).

As recently as a decade ago, one would see very few cases in which parties sought judicial intervention in the umpire selection process. Now, virtually every issue of any reinsurance litigation reporter references at least one umpire selection dispute.

Second, courts often refuse to select an umpire on the grounds that no impasse in the selection process has occurred. See, e.g., IRB-Brasil Resseguros, which found no lapse in umpire selection process where contract allowed 30 days for the party arbitrators to agree on an umpire, and after which they were to "draw lots," causing the party to ask the court to select an umpire twenty days after arbitrator appointment. Thus, after a significant expenditure of time and money, the parties in these cases ended up right back where they started.

Third, courts remain hesitant to allow pre-award challenges to arbitrators, as long as they meet contractually mandated criteria or qualifications.

Some example cases include IRB-Brasil Resseguros, which rejected pre-award attempts by one party to remove a party-appointed arbitrator and the other party to disqualify a potential umpire candidate abd B/E Aerospace Inc. v. Jet Aviation St. Louis Inc. (S.D.N.Y. July 1, 2011), in which "the Second Circuit has interpreted the FAA to preclude pre-award removal of arbitrators in most cases".

Post-award challenges similarly are unsuccessful in the vast majority of cases. See, e.g., Ario v. Cologne Reins. (Barbados) Ltd. (M.D.Pa. Nov. 13, 2009): there was no evident partiality where an umpire was selected to serve as umpire in an unrelated arbitration by the party-appointed arbitrator in the pending proceeding.

As a result, parties and their counsel know that contractually qualified umpire candidates are most likely immune from a successful challenge, thereby potentially emboldening parties to nominate candidates who may not be perceived as true neutrals.

Some Proposed Solutions — Pre-Dispute

- Include detailed selection criteria in the reinsurance contract itself. This is the easiest and least controversial solution to the umpire selection problem. In fact, many companies are inserting intricately detailed arbitration clauses, including very specific panel selection procedures, in their newer contracts. While this approach will help streamline disputes under these newer contracts, it does not resolve issues under older contracts.

- Agree an a selection criteria before a dispute arises. Much like a couple embarking on marriage who cringe at the notion of a prenuptial agreement, companies in a harmonious contractual arrangement may be hesitant to consider the prospect of a dispute before one arises.

  However, just like statistics tell us that almost one in two marriages ends in divorce, history teaches that long-standing contractual partners may have disputes. Nothing prevents such parties from negotiating a detailed amendment to a long-standing contractual arbitration provision, without a pending or looming dispute.

  Parties can even agree to a pool of potential umpire candidates as part of any such agreement, thereby further streamlining any future panel selection process. Doing so in the absence of an actual dispute has numerous benefits.

First, once a dispute has arisen, parties tend to be less inclined to compromise on anything — particularly since they are likely to be suspicious of anything proposed by their adversary.

Second, the parties' incentives may change in a dispute context. For example, one party may favor delay or may feel the need to adopt a selection mechanism that has the potential of resulting in a more favorably disposed umpire.

Third, by the time a dispute arises, specific counsel will be in place, and the relationships between counsel and potential panel members may become another factor. Thus, although parties do not often do so, it may be advantageous for them to seek agreement on a selection protocol while in a period of relative détente.

Some Proposed Solutions — Post-Dispute

Unfortunately, umpire selection protocols typically are not discussed in detail until after a dispute is initiated, which brings into play many of the difficulties identified above. The old standby of nominating three candidates, striking two and letting a "coin flip" decide the umpire is not always amenable to both parties, and it may, in certain circumstances, provide the wrong incentives.

Specifically, a party — knowing that a court will not intervene in the selection process and fearing that the other side will nominate three "homers" — may feel constrained to nominate three candidates that may be pre-disposed to its position, so that it at least has a 50-50 chance of a potentially favorable panel. This fear that the other side will seek to "game the system" is a significant driver of disputes over the umpire selection process: parties are unwilling to risk disadvantaging themselves by "unilaterally disarming."

As a result, any good selection method must encourage the selection of experienced, knowledgeable and neutral umpires, without relying on the hope that parties and counsel will do so voluntarily. Although there is no one system that works for all companies and in all circumstances, effective selection procedures often involve one or more of the following characteristics:

- Early Discussion Of Procedures. No matter how detailed a contractual selection procedure may be, mechanical details will need to be worked out by the parties. Those details almost always take longer to finalize than the parties expect or want. Thus, conversations about the process and the substance of questionnaires (see below) should begin as soon as possible after arbitration is initiated.

- Larger Candidate Pools. Parties are more likely to agree on an acceptable candidate, or at least to find one that they feel is not necessarily catastrophic to their case, if the umpire pool is larger. Those candidate pools can be further narrowed down through a ranking system, which gives the parties continuing involvement in and control over the process.

- Eliminating Certain Candidates. The parties can agree that certain candidates are ineligible to serve. Criteria that parties may want to consider include: those that have served as party-appointed arbitrator or umpire for a party or counsel over some defined time period; those who have served as party-appointed arbitrator or umpire for a party or counsel more than a certain number of times over the course of their career; and those who have served on behalf of either cedents or reinsurers in more than an agreed-upon percentage of their engagements. This list is neither exclusive nor is every one of these suggestions appropriate for every case.

- Questionnaires. Questionnaires allow parties to make decisions based on something approaching a complete record. However, parties should be careful to put strict timelines in place and to adopt specific processes with short turn-around times to address the circumstances in which arbitrators can be replaced by either side and the procedures to follow when candidates do not respond or indicate that they cannot serve.

One Final Proposal

Despite all of the downsides involved in initiating litigation to effectuate the panel selection process, there is one aspect of the court approach that may be worth replicating. When parties are forced to present umpire candidates to a court, they have an incentive to present people who appear (and may actually be) neutral to increase the odds that one of their candidates is selected.

Neither a coin flip nor a ranking methodology has the same effect. Thus, inserting a third party into the process can be a useful exercise. And, if that party is not a court, but rather a person or (more likely) organization on which the parties have agreed, the process can be completed more quickly and cost-effectively than via litigation, while maintaining confidentiality.

To be clear, such a proposal may not entail simply using the selection method and umpire pool of a third-party organization. Parties may not want to give up that level of control, especially where they may not know the identity or qualifications of the umpire candidates on any particular third-party organization's list. Rather, this process assumes that the parties employ a process by which they select (and maybe narrow through cross-striking or ranking) the candidates, but a third-party organization makes the final choice.

There are, of course, practical problems in utilizing such an approach. One certainly could ask how parties that cannot agree on an umpire could agree on a third-party organization to select an umpire or whether a particular person or organization is willing to serve in the role. However, as problems regarding umpire selection not only fail to improve but also appear to be getting affirmatively worse, it may be worth considering some new solutions. Otherwise, there is a risk that parties will throw out the baby of arbitration with the bath water of the umpire selection quagmire.

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