Second Circuit Addresses Enforceability of Non-Party Discovery Under Federal Arbitration Act

Parties seeking to enforce arbitral subpoenas in federal court through section 7 of the Federal Arbitration Act ("FAA") "must establish a basis for subject matter jurisdiction independent of the FAA." *Doscher v. Sea Port Group Securities, LLC*, 832 F.3d 372, 386 (2d Cir. 2016). On May 1, 2020, the United States Court of Appeals for the Second Circuit published an important decision detailing how diversity jurisdiction of the federal courts is evaluated in cases concerning discovery aimed at non-party witnesses in arbitration.

In *Washington National Insurance Co. v. OBEX Group LLC, and Randall Katzenstein*, --- F.3d ----, 2020 WL 2092597 (2d Cir. May 1, 2020), the Court affirmed the district court's enforcement of a summons for documents and testimony issued to non-party witnesses in an arbitration case. The Second Circuit determined that diversity jurisdiction in cases arising from the FAA depends on the citizenship of the parties involved in the petition — not the citizenship of the parties to the underlying arbitration — and confirmed that Fed. R. Civ. P. 45 ("Rule 45") does not require the reviewing district court to consider the non-party's objections to the scope and manner of the arbitral discovery.

Given the increasing trend toward arbitration of claims and the corresponding need to obtain non-party discovery relevant to the underlying arbitration, the Second Circuit's decision provides greater clarity regarding the proper methods of obtaining non-party discovery and enforcing summonses issued by an arbitration panel.

I. Background

Washington National Insurance Company ("WNIC") is an Indiana based company, while its affiliate and co-claimant in arbitration, Bankers Conseco Life Insurance Company ("BCLIC"), is a New York based company. 2020 WL 2092597 at *3. In 2013, WNIC and BCLIC (together, the "Claimants") sought reinsurance from several reinsurance companies, including Beechwood Re Ltd. Claimants eventually entered into an agreement with Beechwood but subsequently accused Beechwood of fraud. At the heart of this fraud claim was that two of the founders of Beechwood owned and managed Platinum Partners, an investment fund allegedly disfavored by investors. Claimants brought an arbitration claim against Beechwood following a *Wall Street Journal* article reporting ties between Beechwood and Platinum Partners.

During the arbitration proceeding, Claimants requested documents and testimony from OBEX Securities LLC (Platinum's broker-dealer) and Randall Katzenstein (President and CEO of OBEX Securities LLC's parent company, OBEX Group LLC). Both Katzenstein and OBEX Group LLC (together, the "Respondents") are New York citizens. The arbitration panel issued summonses to OBEX Securities LLC and Katzenstein, ordering them to appear at the arbitration hearing and bring documents with them in accordance with section 7 of the FAA.[1]

Claimants and Respondents agreed to search terms for documents a week after Respondents filed their objections to the subpoena with the arbitration panel. WNIC expressly "reserved their right to 'come back' if the terms did not 'yield the appropriate responsive documents.'" 2020 WL 2092597 at *2. Additionally, Claimants requested — and Respondents agreed — that Respondents provide the documents "without appearing for a hearing." *Id.* Respondents provided the documents without appearing for the hearing as negotiated, and four months later, Claimants requested that Respondents run an additional search for documents to address deficiencies.

[1] The relevant text of section 7 states: "The arbitrators . . . may summon in writing any person to attend before 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." 9 U.S.C. § 7.

Respondents rejected this request and refused to comply with further summonses issued by the arbitration panel to appear at a hearing and bring the requested documents.

WNIC sought to enforce the summonses under section 7 of the FAA in the United States District Court for the Southern District of New York (Briccetti, J.). WNIC filed the action against Respondents alone — BCLIC did not join the petition — invoking diversity jurisdiction given that WNIC was a citizen of Indiana and Respondents were citizens of New York. Respondents moved to dismiss the summonses for lack of subject matter jurisdiction, making three main arguments. First, Respondents claimed the citizenship of the parties in the underlying arbitration determined diversity jurisdiction. Second, "BCLIC was a necessary and indispensable party that could not be joined without destroying diversity." Finally, the value of the documents and testimony would be less than the $75,000 threshold amount in controversy required for diversity jurisdiction cases. Respondents also sought to quash the summonses, invoking Rule 45 to challenge the propriety and scope of the discovery being sought. Specifically, Respondents claimed the summonses were overbroad, unduly burdensome, sought privileged and protected information, and would constitute "impermissible prehearing discovery."

The district court denied Respondents' motion on all points. Identifying that WNIC and Respondents had diverse citizenship and that respondents failed to move to join BCLIC as a necessary party, the district court determined that all of the necessary parties in the action were diverse. Furthermore, the district court ruled that the amount in controversy was met because the underlying arbitration involved a claim of $134 million in damages, and the documents and testimony sought related to that claim. The district court denied the motion to quash, reasoning "that any overbreadth, privilege, or undue burden objections were issues better left to the arbitration panel to resolve." 2020 WL 2092597 at *4.

II. The Second Circuit Affirms the District Court

Applying *de novo* review, the Second Circuit affirmed the district court on all grounds, determining that the district court had subject matter jurisdiction to enforce the summonses and "properly declined to rule on the respondents' objections."[2] 2020 WL 2092597 at *10.

Respondents' primary argument against subject-matter jurisdiction was that the court must "look through" the petition to the underlying arbitration to determine diversity of citizenship. Respondents' argument relied on Second Circuit and U.S. Supreme Court precedent from federal-question and maritime jurisdiction cases that analyzed jurisdiction based on the underlying arbitration. *Id.*; *Stolt-Nielsen SA v. Celanese AG*, 430 F.3d 567, 572 (2d Cir. 2005) (finding subject jurisdiction of subpoena based on district court's prior exercise of maritime jurisdiction in underlying arbitration). The basis for looking through to the underlying arbitration in federal question cases is that "existence of federal-question jurisdiction over an FAA petition turns on whether the district court would possess jurisdiction over the underlying dispute under the standards of § 1331." 2020 WL 2092597 at *5.

Relying upon its prior decision in *Hermès of Paris, Inc. v. Swain*, 867 F.3d 321 (2d Cir. 2017), the Second Circuit observed that the "same is not true of jurisdictional inquiries under section 1332." 2020 WL 2092597 at *6. Instead, FAA petitions based on section 1332 require that the court look only to the citizenship of the parties in the action before it. Because a citizen of Indiana was moving to compel citizens of New York to produce documents and testimony, diversity was met. Additionally, the Second Circuit agreed with the district court that the amount in controversy is measured by the underlying arbitration claim. The claimed damages in the underlying arbitration

[2] The Second Circuit observed that it "need not, of course, determine hypothetically whether district courts have the power to rule on such objections and we do not consider it here. We decide only that under section 7 of the FAA, the district court was not obliged to consider objections based on Rule 45." 2020 WL 2092597 at *10.

were over $130 million. Because it did not appear to a legal certainty that the underlying arbitration claim was for less than $75,000, jurisdiction was proper.

Because WNIC's co-claimant, BCLIC, was a New York citizen not joined in the action, Respondents again raised their necessary joinder argument at the Second Circuit. The Second Circuit agreed with the district court, however, and found that the district court could accord complete relief (i.e., ordering production of the sought discovery) without BCLIC joining the action. Accordingly, motions to compel arbitral discovery pursuant to the FAA may be brought in federal court even where one or more claimants share citizenship with a non-party, so long as only diverse claimants pursue the summons.

The Second Circuit also rejected Respondents' argument that the summonses were invalid under the FAA for being "pre-hearing discovery." 2020 WL 2092597 at *1. The summonses at issue required Respondents to appear at the hearing and to bring with them the requested documents. Such requirements are entirely consistent with section 7 of the FAA, and an otherwise "properly issued summons is not rendered invalid by a claimant's offer, a respondent's offer, or a joint agreement to produce documents without a hearing." *Id.* at *8. In fact, the Second Circuit observed that Respondents' argument on this point "approach[ed] the frivolous and 'vexatious'" because Respondents had requested to produce documents in lieu of appearing and benefitted from this arrangement. *Id.*

Finally, Respondents' arguments in favor of quashing the summonses were rejected as neither the FAA nor policy considerations impose an "obligation to quash" a subpoena pursuant to the framework embodied at Rule 45. The Second Circuit reasoned that text of section 7 has never been interpreted to "impose Rule 45's obligations on district courts in proceedings to enforce arbitrations summonses under section 7 of the FAA."[3] Furthermore, it would upset policy favoring arbitration if the district court became a '"full-bore legal and evidentiary appeals"' body that disrupted the swift and efficient nature of arbitration. 2020 WL 2092597 at *10 (quoting *Hall St. Assocs., LLC* v. *Mattel, Inc.*, 552 U.S. 576, 588, 128 S.Ct 1396, 170 L.Ed.2d 254 (2008)). Finally, the Second Circuit deemed that arbitration panels determining the evidentiary matters of subpoenas comported with due process and fundamental fairness.

III. Implications

The Second Circuit's decision in *Washington National Insurance Co.* confirms that parties to an arbitration may enforce summonses and subpoenas against non-parties in federal court, even where there does not exist complete diversity among the parties to the arbitration. Assuming the non-party from whom documents and testimony is sought is a citizen of a different state than at least one of parties seeking the information in an arbitration claim, federal courts can and will enforce these summonses under diversity jurisdiction.

Future litigation will likely determine to what extent — if any — federal courts can consider and resolve Rule 45 objections to arbitration subpoenas in the Second Circuit. Although the Second Circuit agreed with the district court's decision not to consider Respondents' Rule 45 objections, the contours of a district court's ability to determine these matters remains an open question. It certainly is not clear based on the Second Circuit's reasoning that judicial review of the summonses is foreclosed under the FAA. The Second Circuit merely held that the district court did not have to consider the objections, while also observing that there may be no remedy available to non-parties challenging summonses absent appropriate judicial review.

[3] The Second Circuit found that the only authority cited by Respondents that addressed this issue directly contradicted Respondents' position. *Odfell ASA v. Celanese AG*, 348 F. Supp. 2d 283 (S.D.N.Y. 2004), *aff'd sub nom Stolt-Nielsen SA v. Celanese AG*, 430 F.3d 567 (2d Cir. 2005) (observing that the district court did not address objections to arbitration subpoenas, as arbitrators possess the authority to rule on matters such as admissibility and privilege).

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to call or email authors Joel Kurtzberg at 212.701.3120 or jkurtzberg@cahill.com; Peter J. Linken at 212.701.3715 or plinken@cahill.com; Zachary M. Missan at 212.701.3577 or zmissan@cahill.com; or email publications@cahill.com.