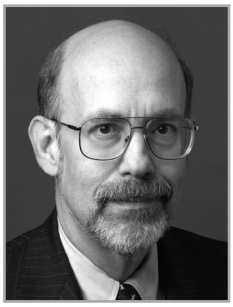
article

# On Ethics

By Edward P. Krugman

Edward P. Krugman



It is precisely because there are tensions in the existing regime that ethical discussions are important.

The Ethics Discussion Committee of ARIAS•U.S. was created in 2011 to provide information and education about ethical issues and concerns. It was tasked with incorporating the 2010 "Additional Guidelines" into the existing ARIAS•U.S. Code of Conduct and revising and updating the Code as appropriate. Since its creation, the Committee has been chaired by Eric Kobrick; with Eric's ascendancy to become Chair of ARIAS•U.S., Jim Rubin has assumed the leadership of the Committee.

Revising the Code took most of 2012 and 2013. The revisions were reported in the 4Q13 issue of the *Quarterly* and became effective on January 1, 2014. They have sparked a substantial amount of discussion, including Richard Waterman's article in the 2Q14 issue of the *Quarterly* and the all-arbitrator ethics panel at the 2014 Fall Conference.

Both to keep that discussion alive and to serve the Committee's broader purpose of providing information and education about ethical issues, members of the Committee will write regularly in the *Quarterly* (we hope in every other issue) on the Code and other ethics topics of interest. There will be reports on the ethics portion of ARIAS•U.S. conference programs, comments on recent cases and, perhaps, discussions of hypothetical fact patterns. ARIAS•U.S. members are encouraged to send in fact patterns for discussion and analysis[2], but it should be clearly understood that we are neither an appeals committee nor an advisory committee. In particular, if the Committee concludes that a submitted fact pattern relates to a pending or recently concluded arbitration, or is submitted by someone hoping to achieve a particular result in such a case, the Committee will not discuss the pattern in these pages. The articles will try to be clear about when the views expressed are those of the Committee and when they are those of the Committee member who wrote the piece. Here, as should be obvious from what follows, the views expressed are mine alone.

## The Ethics Program at the Spring 2014 Conference

One of the more persistent comments about the revised Code — driven, in part, by the phrasing for the first time of a number of provisions in mandatory terms — came from the arbitrator segment within the ARIAS•U.S. community: a number of arbitrators expressed the view that setting standards of behavior for arbitrators was "meaningless, unhelpful, unreasonable, an affront, futile" — the characterizations varied – without some effort to control the behavior of the other segments of the ARIAS•U.S. community as well. In fact, the revised Code had taken a significant step in that direction with the addition of the following language to the Preamble:

> Though these Canons set forth considerations and behavioral standards only for arbitrators, it is expected that the parties and their counsel will conform their own behavior to the Canons and will avoid placing arbitrators in positions where they are unable to sit or are otherwise at risk of contravening the Canons.

Nevertheless, there were real questions as to the effectiveness of such remarks, even if not purely hortatory, and it was decided to use the Ethics segment of the 2014 Spring Conference in Key Biscayne to explore issues related to the conduct of counsel and company representatives as well as arbitrators.

The full fact pattern used in the Ethics segment was distributed with the Conference materials and is available in the Members area of the ARIAS•U.S. website (http://arias-us.org/index.cfm?a=469). Rather than focusing on a single, narrow situation and asking "can so-and-so do X?," the fact pattern followed a reinsurance dispute from selection of arbitrators through the run-up to the Hearing and presented instances of questionable conduct by many of the players in the proceedings at each step along the way. There were many more issues than could possibly have been discussed; one of the purposes of the exercise was to see which issues attracted

**Edward Krugman** is a partner in Cahill Gordon & Reindel. He has thirty years of experience litigating and structuring transactions in insurance and reinsurance and has represented ceding companies and reinsurers in well over a hundred contested reinsurance matters, often involving massive financial exposure. He has been a faculty member at ARIAS•U.S. and Mealey's Reinsurance conferences and has advised on and litigated numerous other matters concerning the business of insurance and the business of insurers, including insolvency, MGA relations, bad faith, complex coverage issues, antitrust issues, and various governmental and regulatory investigations.

attention and discussion and which did not. The problem was framed in a general session and there were then six breakout groups (two each to discuss the issues facing the arbitrators, the lawyers, and the party representatives), followed by a wrap-up session.

My initial impression of the results of the breakout sessions — which I reported at the wrap-up session — was that notwithstanding the ostensible separate focus on party representatives and counsel as well as on arbitrators, it was difficult for participants to break away from an arbitrator-centric perspective. On party-arbitrator appointment, for example, the fact pattern focuses on Fred Forbush, an executive of Empire Re, who is a longtime friend of Gina Gallant and had given her a number of appointments when she retired from the industry and started looking for work as an arbitrator. A new big case comes along, "and Forbush really wants Gallant for his party arbitrator. 'You're the best Gina. You really understand this stuff, and you get along with people as well. We *win* with you.'" Most people agreed that "we *win* with you" was over the line, albeit only slightly. Some thought it was just "cheerleading," but most saw it as asserting that the arbitrator is an advocate whose job is to deliver a win — which is inconsistent with the requirement of Canon II, comment 2, that even party-appointed arbitrators must decide according to the evidence and "should not allow their appointment to influence their decision." Even in the rooms looking at issues regarding party representatives, however, the focus was less on whether Forbush should have said it than on how Gallant should have responded — something like "Thanks, Fred, but I'm sure you understand that I'm going to have to decide this one, like I did all the others, on the evidence in the case."

So what would happen next? Everyone knows the answer to that one: Forbush would say, "Of course, Gina; I never meant to suggest otherwise," and the conversation would move on. There can be, and are, plenty of circumstances in which such an exchange between the company and a potential arbitrator is appropriate and should be taken at face value, but this may not be one of them. Here, one can legitimately ask whether it is all a charade. Forbush knows how many appointments he has given her, and he knows she knows, and Gallant is not saying, "Thanks, Fred, but I guess I'd better not take this one; I'm getting too dependent on you."

I would go further. I suggest that what Forbush said at the outset — "We win with you," with all its implications — is in many circumstances what is being said by a party or lawyer who repeatedly appoints the same arbitrator, ***even if not a word is said on the subject.***

If that is true, then the party or lawyer who makes excessive repeat appointments — and not merely the arbitrator who accepts them — is engaging in unethical behavior and deserves criticism. The party or lawyer is flatly violating the expectation set forth in the Preamble of the Code, putting the arbitrator in a position where s/he ***should*** say "I guess I'd better not take this one," but hoping (or, worse, expecting) that s/he will not say it but will take the appointment. This is true, moreover, even if — as is certainly the case now — there is no mechanism for formally imposing the disapprobation the behavior deserves. It is a characteristic of discussions framed in ethical or moral terms that they speak to norms that exist independently of whether or not they are ever enforced. Bad behavior is bad behavior and should be called out as such, even if the calling out is all anyone can do about it.

For this reason, I have repented of my original view that the participants in Key Biscayne largely ducked the request to focus on Forbush as the party rep and not merely on Gallant as the arbitrator. They *did* focus on Forbush, and they came to a conclusion that his behavior was over the line. They did so, moreover, for a reason that they tied specifically to the Code: Under Canon II, comment 2, an arbitrator is not an advocate, and it is wrong — bad behavior — to tell the arbitrator that s/he is expected to be one. The Key Biscayne participants, in short, did exactly what one should do in a discussion of morals or ethics.

Of course, the conclusion reached in Key Biscayne is not universally shared. There is a respectable body of judicial opinion to the effect that a party-appointed arbitrator *should* be an advocate — or, at least, is always expected to be one. Judge Easterbrook expressed this view in the *Sphere Drake* case a decade ago:

> [I]n the main party-appointed arbitrators are supposed to be advocates. In labor

Wherever the Committee, or ARIAS•U.S., comes out on any particular issue, the existence of a robust debate is essential to make sure that all views are taken into account. It is a goal of this series of articles to spark and maintain that debate.

> arbitration a union may name as its arbitrator the business manager of the local union, and the employer its vice-president for labor relations. Yet no one believes that the predictable loyalty of these designees spoils the award .

Judge Easterbrook's opinion, however, is not the ARIAS•U.S. way. In ARIAS•U.S., party-appointed arbitrators may be pre-disposed to the appointing party's position, but they are not to be committed to it; they may labor to ensure that the appointing party's position is heard and understood, but they are not to advocate it without first having come to their own, independent conclusion that it is correct. And they are not to usurp the role of the party or its counsel by taking over the structuring or presentation of the case. Those are the rules that ARIAS•U.S. arbitrators — and, indeed, *all* ARIAS•U.S. members, including lawyers and company representatives — have agreed to live by.

One can say there are tensions in a system that says, "so far, but no further." There are. In particular, Canon V, Comment 6, which permits very substantive *ex parte* communications , lives in unavoidable tension with the "just decision" obligation of Canon I and the "decide objectively" obligation of Canon II, Comment 2.

One can also believe, as I do, that those tensions cannot be completely resolved under any system in which party-appointed arbitrators are supposed to decide objectively, including systems in which the party-appointed arbitrators are formally "neutral." Consider the International Centre for Dispute Resolution. The ICDR has an all-neutral system, but it permits party appointment. My experience has been that a visitor to an ICDR arbitration who heard enough testimony — and, in particular, who heard the arbitrators' questions of witnesses after counsel was done — would have little difficulty identifying which party appointed which arbitrator. The tensions in a party-appointed system are there, and they will not go away.

But that is just the point. It is precisely *because* there are tensions in the existing regime that ethical discussions are important. It may be difficult to draw a line in any given case, and judgments of behavior must acknowledge that overstepping an unclear line can easily be inadvertent and unintended. The point of Forbush's comment to Gallant — "we *win* with you" — is not so much whether those specific words are a covert message or merely cheerleading: different people can come down on different sides of that issue, although there was a pretty clear consensus in Key Biscayne on the side of "message." The point, rather, is the principle one extracts from the line-drawing discussion itself. Notwithstanding that repeat appointments are addressed in Comment 4 of Canon I of the Code ("should consider") and not in Comment 3 ("must refuse to serve"), lawyers, parties, and arbitrators do not get a free pass on the issue to do whatever they like.

Ethics, like life, can be seen as a series of both absolute rules and 80/20 rules. Some situations are too fraught to permit exceptions, and that is the reason that the provisions of Canon I, Comment 3 of the Code are framed in mandatory terms. The other situations, though, are ***not*** simply "do as you please." In fleshing out and analyzing the non-mandatory provisions of the Code, which is a core purpose of this series of articles, identifying the norm (the 80%) is important, even if there are exceptions (the 20%). The identification sets the frame for the discussion and places the onus on the person claiming an exception in a specific case to justify that claim.

So back to repeat appointments. How much is too much? There is no bright line standard, and the Committee considered and rejected attempting to establish one when it did the revisions to the Code. That the line may be difficult to draw in an individual case, however , does not mean that there is no line at all, or that the line-drawing exercise need not be attempted. There is a level above which repeat appointments corrupt the process, and there will be situations in which that level is clearly exceeded. When that happens, both the party or lawyer who continues to make such appointments and the arbitrator who continues to accept them are behaving unethically and can and should be criticized for their conduct.

> It is a characteristic of discussions framed in ethical or moral terms that they speak to norms that exist independently of whether or not they are ever enforced.

But it is not enough simply to identify miscreants for criticism. If the tensions are structural, one must look for structural solutions. And if complete solutions are not possible without wholly forbidding the party appointments that most arbitration clauses require and many parties prefer, one must do the best one can in the context of the existing structure. Accordingly, the Ethics Discussion Committee is looking at the intersection between procedural and ethical rules in areas such as *ex parte* communications. Because we have chosen a system with inherent tensions, how do we manage the procedures to reduce, to the extent possible, the strains on parties, arbitrators, and counsel who *want* to behave ethically? How do we reduce the temptation to get as close to the line as possible, citing (as lawyers are wont to do) the obligation to represent the client "zealously" within the bounds of the law? These are complicated questions, and there are tradeoffs involved in any set of procedural rules one adopts. None of this would be simple even if the Ethics Discussion Committee had arbitration procedure in its jurisdiction, which it does not, and even if ARIAS•U.S. could prescribe procedural rules as the AAA does, instead of adopting a set of suggested rules and procedures for parties and arbitrators to accept or not as they choose. Wherever the Committee, or ARIAS•U.S., comes out on any particular issue, the existence of a robust

debate is essential to make sure that all views are taken into account. It is a goal of this series of articles to spark and maintain that debate.

ENDNOTES

1. Edward P. Krugman is a member of Cahill Gordon & Reindel LLP and co-chairs its insurance and reinsurance practice. Commentary in this article is solely that of Mr. Krugman and should not be attributed to his Firm or its clients. Nor should it be attributed to the other members of the Ethics Discussion Committee.
2. Use the e-mail address ethicsdiscussioncommittee@arias-us.org or send the material directly to one of the members of the Committee.
3. Submitters of fact patterns for consideration should state that the pattern is not intended for use in an existing or recently concluded arbitration. The time lag between submission and possible use in an article would, we expect, be long enough to make attempted instrumental use of these discussions ineffective in any event.
4. Under Article II, § 5 of the ARIAS•U.S. By-Laws, the Board has the power to expel or suspend a member "for cause," and "cause" includes "violation of any of the by-laws or rules of The Society." The Code is part of the "rules of The Society" for these purposes, and the power of the Board extends to all members, including lawyers and company representatives, and not merely to arbitrators. Whether and how that power should be exercised (in the 20 years since ARIAS•U.S. was founded, the power has never been used), including whether there should be a true disciplinary process such as exists in some other organizations, is a subject of current discussion in the Committee and on the Board.
5. *Sphere Drake Insurance Co. v. All American Life Insurance Co.*, 307 F.3d 617, 620 (7th Cir. 2002) (emphasis in original).
6. Canon V, Comment 6 provides:
Where communications are permitted, a party-appointed arbitrator may (a) make suggestions to the party that appointed him or her with respect to the usefulness of expert evidence or issues he or she feels are not being clearly presented; (b) make suggestions about what arguments or aspects of argument in the case to emphasize or abandon; and (c) provide his or her impressions as to how an issue might be viewed by the Panel, but may not disclose the content or substance of communications or deliberations among the Panel members. An arbitrator should not edit briefs, interview or prepare witnesses, or preview demonstrative evidence to be used at the hearing.
7. Comments 4(g) to 4(j) to Canon I address the repeat appointments issue in various forms, focusing on whether the series of appointments is a "significant" source of revenue for the arbitrator. If they are so significant that the arbitrator believes his or her judgment will be affected, the situation becomes "must refuse to serve" under Comment 3(b). The point of the discussion here is to suggest that repeat appointments can be inappropriate *even if the arbitrator subjectively believes that s/he can render a fair decision.*
8. In commenting on a draft of this essay, one Committee member made a number of points on the way to suggesting that strongly discouraging multiple appointments might not be wise:

- What is a large number of appointments for a small company might not be for a larger one.
- There are times where repeat appointments should be seen not merely as permissible but almost necessary — as, for example, if a ceding company's diet of arbitrations arises from a single ceded treaty roster whose reinsurers tactically refused to consolidate, but where the same argument is made repeatedly against them, by a single arbitrator who has been hired by multiple reinsurers.
- In specialized markets such as London aviation, the same people are necessarily repeatedly sought out for their expertise in the particular market, and they do enough work for both cedents and reinsurers that the concept of "repeated" appointments, when looked at only from the perspective of one party, is not terribly meaningful.

I agree with all of these points (and further examples are surely possible), but I do not agree that multiple appointments do not in general present a serious issue. Most lawyers and company reps will acknowledge having a few "go to" arbitrators for high stakes cases, and it is not realistic to believe that the arbitrators in question do not understand that. Within certain limits, that is a fact of life one must live with, but the limits exist, and the Forbush comments present what appears to me to be a not uncommon way of getting closer to (or past) the limits than is healthy for the process.▼