You have options. Choose the one that suits your circumstances best.

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What To Do When A Party Fails To Pay Its Portion Of Arbitration Fees

THE PROBLEM OF failure of a party to an arbitration proceeding to pay its share of arbitration administrative expenses and arbitrator fees has long been recognized. Richard DeWitt & Rick DeWitt, No Pay No Play: How to Solve the Nonpaying Party Problem in Arbitration, 60 Disp. Resol. J. 27, 28 (Feb.-Apr. 2005). This article examines the issue in light of modern case law, and suggests some practical solutions to the problem.

Many commercial contracts and employment agreements contain arbitration clauses stipulating that, in the event of a dispute, such dispute will be resolved by binding arbitration. Often, arbitration agreements provide that the American Arbitration Association (“AAA”) Rules will govern. In accordance with AAA rules, the AAA may require that parties deposit a share of the arbitrator compensation and administrative fees in advance of proceedings. Thus, Rule 46 of the AAA Employment Arbitration Rules, as well as Rule 52 of the AAA Commercial Arbitration Rules, state that “[t]he AAA may require deposits in advance of any hearings such sums of money as it deems necessary to cover the expenses of the arbitration, including the arbitrator’s fee, if any, and shall render an accounting and return any unexpended balance at the
conclusion of the case.” One party’s refusal or inability to pay its share may disrupt the arbitration proceeding, causing delay and expense in resolving the dispute. Additionally, one party’s failure to pay its share of the costs may lead to suspension or dismissal of the proceedings. AAA Employment Arbitration Rule 47 and AAA Commercial Arbitration Rule 54 both provide that “[i]f such payments are not made, the arbitrator may order the suspension or termination of the proceedings. If no arbitrator has yet been appointed, the AAA may suspend or terminate the proceedings.”

Parties may include a clause in their arbitration agreement stipulating how fees will be divided in the event of a dispute. If no stipulation is made, AAA rules govern. In commercial arbitration, the claimant pays the filing fee and then both parties equally share any advance deposit costs. Dewitt & Dewitt, supra, at 30. In employment disputes, AAA fee allocation depends on whether the employment contract was “individually negotiated” or “employer-promulgated.” When “individually negotiated,” the arbitration fee apportionment is subject to the arbitrator’s discretion and later reallocation, and when “employer-promulgated,” the employer is responsible for all arbitration fees so long as the claim was not frivolous or intended to harass the employer. Williams v. Tully, 2005 WL 645943 (N.D. Cal. Mar. 18, 2005). When the initial claimant refuses to pay its share of the arbitration costs, it may appear fair for the arbitrator to suspend or dismiss the case. See Mitchell L. Marinello & Alison T. Schwartz, What to Do When a Party Refuses to Pay its Share of Arbitration Costs, 18 Disp. Resol. Mag. 29, 30 (Winter 2012) (stating that “if the claimant does not pay its share of the expenses, then it is eminently fair to suspend the arbitration until the claimant makes such payment, or if payment is not made within a certain time, to dismiss the claimant’s case. A claimant should not be permitted to hold a case open and waste the arbitrator’s and other party’s time if it is not able or willing to pay its share of the costs for the proceeding that it initiated.”). Note that the non-paying party issue typically arises in the reverse scenario, with the respondent failing to pay. In that event, several options arise.

**OPTION: GIVE THE OPPOSING PARTY THE OPPORTUNITY TO ADVANCE THE FEES** • One option is for the opposing party to advance the fees of the party that fails to pay its pro-rata share of the costs, thus enabling the arbitration to proceed. The paying party may recoup the extra money paid as part of the final award. This is the most commonly used option, which the AAA explicitly endorses. AAA Employment Arbitration Rule 47 and AAA Commercial Arbitration Rule 54 state: “If arbitrator compensation or administrative charges have not been paid in full, the AAA may so inform the parties in order that one of them may advance the required payment.”

The Ninth Circuit, in Lifescan, Inc. v. Premier Diabetic Services, Inc., 363 F.3d 1010, 1013 (9th Cir. 2004), confirmed the arbitrator’s discretion to choose this solution. In Lifescan, after participating in the initial stages of the arbitration proceedings but prior to the final hearing, the respondent explained that it was no longer able to pay the arbitration fees. As a result, the arbitrators gave the claimant the option of advancing the fees owed. The claimant refused to advance the non-paying party’s fees and the arbitrators suspended the proceedings. On appeal, the Ninth Circuit determined that the arbitrators acted within their discretion to suspend and dismiss the arbitration proceeding. Id. at 1013. See also Dealer Computer Services, Inc. v. Old Colony Motors, Inc., 588 F.3d 884, 887-88 (5th Cir. 2009); Marinello & Schwartz, supra, at 29-30. The court acknowledged that the option “may not be an ideal solution to the problem of a party’s failure to pay its share of the fees, but it is well within the discretion of the arbitrators.” Lifescan, supra, 363 F.3d at 1013. The court noted that there is “no totally satisfactory solution in such circumstances,” but that is “why the AAA
rules give arbitrators the flexibility to make the best of a bad situation... [and] allow the arbitrators to adjust the payment of costs in light of the circumstances.” Id. The Fifth Circuit, in Dealer Computer Services, Inc. v. Old Colony Motors, Inc., reached a similar conclusion, finding that “arbitrators are within their discretion to ask one or the other party to pay the entire fee, and tax the fee as part of the award, or alternatively, suspend the arbitration.” Dealer, supra, 588 F.3d 887 (5th Cir. 2009).

Giving the opposing party the opportunity to advance the non-paying party’s fees is clearly within an arbitrator’s power. Yet arbitrators should maintain options other than requiring the opposing party to deposit the non-paying party’s share of the arbitration costs. An alternative may appear essential where one party does not have the financial resources to deposit the full advance or where paying the entire advance would cause the compliant party financial distress. Further, “having to advance a nonpaying adversary’s deposit imposes an unfair burden... [which can] deplete a party’s resources and ability to prosecute its case... [and] involves substantial risk that the nonpaying party will not be able to pay the amount advanced or any eventual award.” Brandifino v. CryptoMetrics, Inc., 896 N.Y.S.2d 623, 628 (N.Y. Sup. Ct. 2010) (quoting DeWitt & DeWitt, supra, at 28).

**OPTION: FILE SUIT TO COMPEL THE NON-PAYING PARTY TO PAY** • Filing suit in court to require the non-paying party to pay its share of the fees is a potential, albeit generally unsuccessful, remedy for one party’s failure to pay its share of the arbitration costs. This approach was unsuccessful in Lifescan and in Dealer Computer Services. In both cases, the courts found no basis to compel the non-paying parties to pay, reasoning that the non-paying parties did not “fail, neglect, or refuse to arbitrate” because the AAA rules gave the arbitrator “full discretion and flexibility to change allocation of fees, or suspend arbitration, as a solution to an otherwise bad situation.” Dealer, supra, 588 F.3d at 888 (citing Lifescan, 363 F.3d at 1012-13).

Nevertheless, in cases where the compliant party is fiscally unable to advance the entire costs of the arbitration proceeding, that party may prevail in compelling the non-paying party to pay its share of the costs. Thus, in Brady v. Williams Capital Group, L.P., 64 A.D.3d 127 (N.Y. App. Div. 2009), the employer refused to pay the entire advance cost of arbitration, as mandated by the AAA, and instead demanded that the parties split the fees, as specified by the arbitration clause in the employment contract. The AAA sent the employer a bill for the entire costs of arbitration in accordance with AAA rules, but the employer refused to pay the full advance of over $40,000 and the former employee refused to split the fees, causing the arbitrator to cancel the proceeding. On appeal, the New York Supreme Court Appellate Division determined that the employee “provided sufficient information about her precarious financial situation[,...] demonstrating that she was not in a position to afford the cost associated with the arbitration, and was therefore effectively precluded from vindicating her rights in the AAA forum.” Id. at 700. Even though fee-splitting clauses in arbitration agreements may supersede the AAA’s compensation rules, “public policy dictate[d] that [the court] not enforce its fee-splitting provision under the circumstances of [the] claim [because the employee] met her burden of establishing that the arbitration fees and costs are so high as to discourage her from vindicating her state and federal statutory rights in the arbitral forum, rendering the subject arbitration clause unenforceable.” Id. at 702. Due to these financial considerations, the court ordered that the employer should be compelled to pay the costs of arbitration, subject to later reallocation. On further appeal, the New York Court of Appeals remitted the matter to the New York Supreme Court, requiring further fact-finding on the fees issue. Brady v. Williams Capital Group, L.P., 928 N.E.2d 383, 384 (N.Y. 2010).