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How Alleged Conflicts of Interest and Partiality of Arbitrators Are Resolved in the Context of the Selection of an Arbitrator in Hospitality Industry Disputes

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Key Takeaway: *JAMS and AAA rules require arbitrators to disclose any circumstances that could raise doubts about impartiality—parties should scrutinize these disclosures carefully at the outset.*

Hotel management agreements (HMAs) and franchise agreements (FAs) often contain dispute resolution provisions mandating that the owner and manager, or the franchisor and franchisee, arbitrate any disputes between the parties. The business of hospitality is unique and specialized, and so too are its laws — such that the parties negotiating those HMAs and FAs often demand that the arbitrator have sufficient knowledge of the legal nuances of the hospitality industry. As such, HMAs and FAs frequently have strict eligibility requirements for arbitrators in these instances. For example, a dispute resolution clause in an HMA or FA may contain the

following provision, or something substantially similar:

> The parties agree that such Arbitrator shall have not less than ten (10) years' experience in or for the hospitality industry in the area of expertise on which the dispute is based (e.g. with respect to operational matters, experience in the management and operation of hotels of a similar nature as the Hotel or, with respect to financial matters, experience in the financial or economic evaluation or appraisal of hotels).

These types of clauses often result in a more narrow pool of individuals who are eligible to arbitrate these matters.

Because there can be such a narrow universe of eligible arbitrators under these circumstances, conflicts (or perceived conflicts) often arise.[1] For example, an arbitrator may have previously worked or consulted for the hotel brand that is a party to the dispute. A party may believe that this creates a conflict such that the individual should not be permitted to resolve the dispute.

Dispute resolution providers such as JAMS and the American Arbitration Association (AAA) contain rules to address what a party may perceive as a conflict. JAMS and the AAA require upfront and fulsome disclosure of potential conflicts. *See* Rule 18(a) of the AAA Commercial Arbitration Rules and Procedures (the AAA Rules) ("Any person appointed or to be appointed as an arbitrator … shall disclose to the AAA any circumstance likely to give rise to justifiable doubt as to the arbitrator's impartiality or independence, including any bias or any financial or personal interest in the result of the arbitration or any past or present relationship with the parties or their representatives"); Rule 15(h) of the JAMS Comprehensive Arbitration Rules and Procedures (the JAMS Rules) ("Any disclosures regarding the selected Arbitrator shall be made as required by law

or within ten (10) calendar days from the date of appointment").

JAMS further specifies that "[a]n Arbitrator should not proceed with the process unless all Parties have acknowledged and waived any actual or potential conflict of interest" and instructs that an arbitrator should withdraw if any conflict of interest "casts serious doubt on the integrity of the process." JAMS *Arbitrators Ethical Guidelines*, at V(C); *see also Applied Indus. Materials Corp. v. Ovalar Makine Ticaret Ve Sanayi, A.A.*, 492 F.3d 132, 138 (2d Cir. 2007) ("arbitrators must take steps to ensure that the parties are not misled into believing that no nontrivial conflict exists. It therefore follows that where an arbitrator has reason to believe that a nontrivial conflict of interest might exist, he must (1) investigate the conflict ...or (2) disclose his reasons for believing there might be a conflict and his intention not to investigate.").

Following disclosure, the parties then have the opportunity to lodge their objections to the appointment or continued service of the arbitrator. The determination as to whether to disqualify the arbitrator on the basis of a conflict or bias is generally left to the alternative dispute resolution (ADR) provider (unless the arbitrator voluntarily decides to resign). *E.g.*, AAA Rule 19(c); JAMS Rule 15(i). The AAA considers the following standards in potentially disqualifying an arbitrator: (i) partiality or lack of independence; (ii) inability to perform his or her duties with diligence and good faith; (iii) any grounds for disqualification provided by applicable law. AAA Rule 19(a).

The ADR provider's decision on a conflicts issue is generally not subject to immediate challenge in the courts, and the Federal Arbitration Act (FAA) does not provide an avenue for a party to seek disqualification or a ruling on the perceived conflict of an arbitrator in advance of the award. *In re Sussex*, 781 F.3d 1065 (9th Cir. 2015) (finding that district court improperly provided mid-arbitration

intervention in removing arbitrator); *Smith v. Am. Arbitration Ass'n, Inc.*, 233 F.3d 502, 506 (7th Cir. 2000) ("The time to challenge an arbitration, on whatever grounds, including bias, is when the arbitration is completed and an award rendered"); *Aviall, Inc. v. Ryder Sys., Inc.*, 110 F.3d 892, 895 (2d Cir. 1997) ("Although the FAA provides that a court can vacate an award '[w]here there was evident partiality or corruption in the arbitrators,' *id.* § 10(a)(2), it does not provide for pre-award removal of an arbitrator").

Courts have, however, left open the possibility of mid-arbitration relief in extreme circumstances. *See McCluskey v. Henry*, 2021 WL 11653039, *4 (suggesting that while there is no absolute bar on mid-arbitration intervention, the Ninth Circuit has indicated that such relief may be appropriate in an "extreme case"); *Application of York Hannover Holding A.G. v. Am. Arbitration Ass'n*, 1993 WL 159961, *3 (S.D.N.Y. 1993) ("While the court generally does not have jurisdiction to intervene in an ongoing arbitration proceeding, it may have such power 'where intervention has been sought under the general equity powers of [the] court.'").

However, the law is clear that, following the arbitration, a party may seek to vacate an award on the basis that "there was evident partiality or corruption in the arbitrators." 9 U.S.C. § 10(a)(2). This is generally a high bar to meet. *See In re Sussex*, 781 F.3d at 1074 ("In applying this standard, we have held there was 'evident partiality' in cases that involved direct financial connections between a party and an arbitrator or its law firm, or a concrete possibility of such connections."); *id.* ("In contrast, we have recognized, courts have rejected claims that undisclosed facts relating to 'long past, attenuated, or insubstantial connections between a party and an arbitrator' created a reasonable impression of partiality"); *Morelite Const. Corp. v. New York City District Council Carpenters Benefit Funds*, 748 F.2d 79 (2d Cir. 1984) (holding that a father-son relationship between an arbitrator and an officer of

one party to the arbitration rose to the level of ‘evident partiality’”).

In sum, parties involved in hospitality disputes should make sure to demand that an arbitrator disclose any and all potential conflicts at the onset of an arbitration. It is also critical that the party challenge any potential conflicts immediately as they arise. Otherwise, the party may be deemed to have consented to the appointment or continued service of the arbitrator, and waived the right to challenge that conflict on a later date. Additionally, attorneys and business people drafting dispute resolution clauses should take a careful look at those clauses and determine if there are additional qualifications or limitations that they want add to those clauses. For example, while an arbitrator’s former affiliation with a party may not be sufficient to disqualify that arbitrator or vacate the award, a party can contract to prevent that person’s appointment in the dispute resolution clause.

[1] It should be noted that, where the parties are permitted to select party-appointed arbitrators, those arbitrators often need not be impartial or independent, and may not be subject to disqualification for partiality or lack of independence.