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Mid-Arbitration Is Not The Time For Complaints

Law360, New York (January 11, 2012, 1:52 PM ET) -- A reinsurer or ceding company that has a complaint over how an arbitration is being conducted, including an objection over whether its contracts authorize the consolidation of multiple disputes, is not entitled to court review until the arbitration is completed, according to the Seventh Circuit Court of Appeals' recent ruling in Blue Cross Blue Shield of Mass. Inc. v. BCS Ins. Co., Nos. 11-2343 & 11-2757 (7th Cir. 2011).

Moreover, a party cannot avoid this rule and obtain court review earlier by artfully pleading in a way to engender review under the Federal Arbitration Act (FAA)

As a result, companies that have complaints about the nature of an arbitration would be wise to bring those to court before party arbitrators are appointed, or they will have to wait until after the arbitration is completed.

The Arbitration Between Blue Cross and BCS

The underlying dispute in Blue Cross involved reinsurance agreements between a captive reinsurer, BCS Insurance Co. and 12 different Blue Cross plans. Each of the plans was reinsured by BCS.

When the plans were sued in a Florida-based class action, each made a claim against BCS under its captive reinsurance agreement. BCS denied coverage, and the 12 plans then jointly demanded arbitration and named a single party-appointed arbitrator to represent them all. Id. at 1-2.

BCS responded to the plans' joint demand with a single response that likewise named just a single arbitrator. It appears that BCS did not then object to having a single arbitration proceeding against all 12 plans.

After exchanging the initial arbitration pleadings and naming arbitrators, the arbitration proceeding ground to a halt as BCS and the plans were unable to agree on an umpire. Id.

The Parties' Competing Positions in Federal Court

In order to move the arbitration forward, 7 of the 12 plans filed a petition in the United States District Court for the Northern District of Illinois under 9 U.S.C. § 5, which gives a federal court authority to "designate and appoint" an arbitrator or umpire.

BCS responded with its own filing, which it called a "cross-petition to compel a de-consolidated arbitration." Blue Cross at 2. BCS argued that under the U.S. Supreme Court's decision in Stolt-Nielsen SA v. AnimalFeeds Int'l Corp., 130 S.Ct. 1758, (2010), the plans could not require it to participate in a consolidated proceeding without its consent.

BCS further contended that the issue of consolidation was one for the court, not the panel of arbitrators, to decide. Blue Cross at 2.

The district court ultimately issued two rulings, addressing BCS's cross petition first and the plans' initial petition second. The district court denied BCS's request that it preclude a consolidated arbitration proceeding, concluding that under Employers Ins. Co. of Wausau v. Century Ind.. Co., 443 F.3d 573 (7th Cir. 2006), consolidation was a procedural issue that the arbitrators must resolve in the first instance.

In a strange procedural twist, BCS then filed a notice of appeal from this ruling, even though the plans' petition to appoint an umpire remained pending. Blue Cross at 3. Under federal practice, appeals are usually not proper until a final judgment is entered and the entire case resolved. See Fed. R. App. P. 4(a).

BCS contended that its immediate appeal was proper under Section 16(a)(1)(B) of the FAA, which allows an appeal from any order "denying a petition ... to order arbitration to proceed." According to BCS, the district court's denial of its cross-petition to compel the plans to proceed with a de-consolidated arbitration was such an order. Blue Cross at 3-4.

The district court disagreed and concluded that BCS's appeal was improper. It thus proceeded to issue its second ruling, addressing the plans' petition. The district court granted the petition and appointed a single umpire to preside over the parties' arbitration. BCS then filed a second notice of appeal from this ruling. Blue Cross at 3.

The Seventh Circuit's Rulings

In what is likely the only appellate court decision that references Humpty Dumpty, President Abraham Lincoln and Ludwig Wittgenstein, the Seventh Circuit dismissed BCS's first appeal for lack of appellate jurisdiction. The Court of Appeals also rejected BCS's second appeal, concluding the district court had properly appointed an umpire to preside over the parties' disputes.

In explaining its rulings, the Court of Appeals emphasized the limited role courts have in ongoing arbitration proceedings and reiterated that decisions over the consolidation of multiple arbitrations are to be made in the first instance by arbitrators, not court.

The Court of Appeals' references to a nursery rhyme character, former president and German existentialist philosopher all related to its dismissal of BCS's first appeal. The Seventh Circuit concluded that while the FAA authorizes appeals from the denial of a petition "to order arbitration to proceed," BCS's request for a "de-consolidated arbitration" was not such a petition.

That BCS may have cleverly labeled its petition as seeking to compel arbitration was merely artful pleading. Because the meaning of words is "objective and external to the speaker," BCS's attempt to label its motion so that it would fall within the terms of the FAA was ineffective.

In reality, its motion was not to compel an arbitration to proceed, but to disrupt the ongoing arbitration that was "already proceeding" between BCS and the plans. Blue Cross at 4-5.

In support of its ruling, the Court of Appeals explained that court involvement in arbitration proceedings "comes at the beginning or the end, but not in the middle." Blue Cross at 5.

If the captive reinsurer wished to get earlier court review on the consolidation issue, it should have "refused to appoint an arbitrator" and then raised the issue when the plans went to court to have an arbitrator appointed for BCS.

Once both sides had appointed their arbitrators, "the proceedings got underway," and court review was not allowed until the arbitration was completed. Id.

Even though BCS's appeal on the consolidation issue was dismissed for lack of appellate jurisdiction, the Court of Appeals, "for completeness," explained that even if BCS had presented the consolidation issue properly procedurally, it would have lost anyway.

Citing its decision in Employers Ins. Co. of Wausau, the Seventh Circuit noted that the issue of whether a consolidated proceeding is permissible under the parties' contracts, and, if so, whether consolidation is appropriate, is an issue to be decided by the arbitrators in the first instance.

It rejected the notion that the Supreme Court's decision against nonconsensual class arbitration in Stolt-Nielsen compelled a different conclusion. Blue Cross at 7. Ultimately, the arbitrators "must both interpret the contract and exercise any discretion that the contract allows." Id. at 10.

Conclusion

Under Blue Cross, reinsurers and ceding companies can expect little help from federal courts in resolving arbitration-related disputes mid-arbitration, at least in the Seventh Circuit.

Any disputes over arbitration procedure or even the scope of a proceeding, such as a dispute over the consolidation of multiple disputes, must be raised in court either before arbitrators are appointed or wait until the arbitration is completed.

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