Calif. Arbitration Ruling May Curb 3rd-Party Discovery

By **Drew Harbur** (July 29, 2020)

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Obtaining prehearing discovery from third parties in California arbitration proceedings had historically been plagued by uncertainty and disagreement, which undermined arbitration goals of increased efficiency and the right to a full and fair hearing.

That is because California state courts provided zero guidance on the scope of prehearing, third-party discovery in arbitration proceedings. This lack of clarity required parties to engage in unnecessary and time-consuming disagreements/hearings, which further undermined the very efficiencies parties expected when opting for arbitration.[1]

The scope and limitations of third-party discovery in arbitration proceedings is clearer at the federal level.[2] Indeed, a majority of federal circuit courts — including the U.S. Court of Appeals for the Ninth Circuit — hold that an arbitrator lacks the power under the Federal Arbitration Act to compel third-party discovery before the actual hearing.[3] However, note that there is at least some disagreement among the circuits.[4]

But the California Court of Appeal has finally weighed in via its recent decision in Aixtron Inc. v. Veeco Instruments Inc.[5] In Aixtron, the California Court of Appeal reached a number of important findings clarifying the power, or lack thereof, of arbitrators to order prehearing, third-party discovery.

First, the court specifically agreed with the Ninth Circuit and ruled that the Federal Arbitration Act does not grant arbitrators the power to order document discovery from nonparties prior to a hearing.[6] Second, the court reaffirmed prior rulings finding that where arbitration did not arise out of wrongful death/personal injury, the parties must have specifically provided for enhanced discovery rights in their arbitration agreement, or such rights would not be inferred.[7]

Third, the court rejected the argument that California Code of Civil Procedure Section 1282.6 grants arbitrators unlimited power to issue discovery subpoenas,[8] further finding that such an interpretation would be inconsistent with that code section's legislative history and related statutes.[9]

The holdings and reasoning provided by the Aixtron court are important. Prior to Aixtron, parties disputing their right to third-party discovery were forced to largely rely on the case of Berglund v. Arthroscopic & Laser Surgery Center of San Diego LP,[10] a California Supreme Court case that dealt with specific provisions of the Code of Civil Procedure applicable to arbitration arising out of wrongful death/personal injury cases.[11]

Thus, Berglund's application to arbitration involving business, employment and other matters was unclear, which even the Vice President and Managing Director of JAMS' arbitration practice, Richard Chernick, acknowledged.[12] This led to the protracted disputes/hearings mentioned above.

How does this affect my practice?

What does Aixtron mean for lawyers arbitrating disputes in California? Aixtron will most likely be read to significantly limit third-party prehearing discovery in any arbitration where the parties have not specifically agreed to certain discovery rights in the text of their arbitration agreement — i.e., where there is no provision for full discovery by code or reference to Code of Civil Procedure Section 1283.05.

As such, counsel should review the Aixtron decision and factor it into their early case analysis when determining the discovery rights their client will have, or not have, in arbitration proceedings. While Aixtron's limitations may have little consequence in, for example, a straightforward contract dispute among two parties, its implications are immense for complex disputes involving the need to access third-party records and take depositions related thereto.

For example: What if a party needs to access financial or other business records from a third party that are not in the possession, custody or control[13] of another party to the arbitration? Sure, parties still have the ability to subpoena documents and witnesses to the arbitration hearing itself, but query the practicality and effectiveness of that in the age of electronically stored information productions.[14]

Additionally, counsel should be mindful of Aixtron in drafting arbitration clauses, as the discovery means agreed to — or unaddressed — will greatly affect future arbitration proceedings. Some parties may wish to include broader rights while others may be incentivized to limit discovery. The bottom line is that, following Aixtron, the decision might be made by the courts in the absence of a clear agreement.

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[1] Armendariz v. Found. Health Psychcare Servs., Inc., 24 Cal.4th 83, fn. 11 (2000) ("We recognize, of course, that a limitation on discovery is one important component of the simplicity, informality, and expedition of arbitration.") (internal quotations and citations omitted).

[2] Cara Bayles, Law360 - Arbitrators Can't Demand Third-Party Docs, 9th Circ. Says (2017); Neal Klausner and Scott M. Singer, Law360 - Arbitration Discovery Has Its Limits (2009).

[3] See, e.g., CVS Health Corp. v. Vividus, LLC, 878 F.3d 703 (9th Cir. 2017) ("Given the clear statutory language, we reject the proposition that Section 7 grants arbitrators implicit powers to order document discovery from third parties prior to a hearing."); accord Managed Care Advisory Grp., LLC v. CIGNA Healthcare, Inc., 939 F.3d 1145, 1159 (11th Cir. 2019) (holding "that the plain language of the statute is unambiguous in requiring witnesses to appear before an arbitrator and bring any documents with them, thus prohibiting pre-hearing discovery from non-parties").

[4] See In re Sec. Life Ins. Co. of America, 228 F.3d 865, 870-871 (8th Cir. 2000) ("We thus hold that implicit in an arbitration panel's power to subpoena relevant documents for production at a hearing is the power to order the production of relevant documents for review by a party prior to the hearing."); see COMSAT Corp. v. Nat'l Sci. Found., 190 F.3d 269, 276 (4th Cir. 1999) (reasoning that pre-hearing, third-part discovery may be appropriate upon a showing of "special need" or "hardship").

[5] Aixtron, Inc. v. Veeco Instruments Inc., No. H045126, 2020 WL 4013981, at *1 (July 16, 2020).

[6] Aixtron at *17 ("We find this reasoning persuasive and adopt the holding in CVS Health.").

[7] Id. at 18 ("Subdivision (b) of section 1283.1 provides that in all other arbitrations, the arbitrator may grant discovery only if the parties by their agreement so provide ....") (internal quotations omitted).

[8] C.C.P. § 1282.6 reads as follows:

(a) A subpoena requiring the attendance of witnesses, and a subpoena duces tecum for the production of books, records, documents and other evidence, at an arbitration proceeding or a deposition under Section 1283, and if Section 1283.05 is applicable, for the purposes of discovery, shall be issued as provided in this section. In addition, the neutral arbitrator upon his own determination may issue subpoenas for the attendance of witnesses and subpoenas duces tecum for the production of books, records, documents and other evidence.

(b) Subpoenas shall be issued, as of course, signed but otherwise in blank, to the party requesting them, by a neutral association, organization, governmental agency, or office if the arbitration agreement provides for administration of the arbitration proceedings by, or under the rules of, a neutral association, organization, governmental agency or office or by the neutral arbitrator.

(c) The party serving the subpoena shall fill it in before service. Subpoenas shall be served and enforced in accordance with Chapter 2 (commencing with Section 1985) of Title 3 of Part 4 of this code.

[9] See Aixtron at 21-22.

[10] Berglund v. Arthroscopic & Laser Surgery Ctr. of San Diego, L.P., 44 Cal. 4th 528 (2008).

[11] See Civ. Proc. Code § 1283.05.

[12] See Richard Chernick, Witnesses in Arbitration – California Arbitration Act (2015) (referring to Berglund and noting: "This was a case that arose under § 1283.05; it is unclear whether third-party discovery initiated under different authority would require same procedure"), available https://www.jamsadr.com/files/uploads/documents/articles/chernick-witnesses-in-arbitration-part-1-law-dot-com-2015-10-23.pdf.

[13] See Civ. Proc. Code § 2031.230.

[14] See In re Sec. Life Ins. Co. of America, 228 F.3d 865, 870-871 (8th Cir. 2000)

("Although the efficient resolution of disputes through arbitration necessarily entails a limited discovery process, we believe this interest in efficiency is furthered by permitting a party to review and digest relevant documentary evidence prior to the arbitration hearing.").