A Practical Guide for Applying Rule 59 of the AAA Construction Industry Arbitration Rules

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Under the Construction Industry Arbitration Rules of the American Arbitration Association, the cost of arbitrator compensation is typically born equally by the parties (see Rule R-57). Deposits are assessed by the AAA based upon arbitrator compensation estimates (see Rule R-58). When a party to a valid arbitration proceeding fails or refuses to honor the commitment to pay its fair share of the cost of arbitration, what happens? Rule R-59 provides various remedies, including suspension and termination. If the only answer is to suspend or terminate the arbitration proceeding, however, that may reward such party's noncompliance.

Properly invoked[1] and applied, Rule 59 (Remedies for Nonpayment)[2] can prevent unfairness and support the policy of enforcing arbitration agreements in parties' contracts. (The complete text of Rule 59 is set forth in Appendix "A.") Generally, Rule 59 allows a party to arbitrate its affirmative claims against the party who fails to or refuses to pay its share of the deposits for arbitrator compensation, expenses, and administrative charges.

Subpart (a) of Rule 59 allows one party (the "Paying Party") to elect to bear the unpaid costs of the other party (the "Non-Paying Party") and subpart (b) allows the Paying Party to seek the protection of Rule 59 when the Non-Paying Party fails or refuses to pay its share of arbitration costs in violation of the AAA's rules. Pursuant to Rule 59, the arbitrator may

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[1]If the AAA's rules have not been expressly adopted by the parties' arbitration agreement and have not otherwise been invoked by them through proceeding in the AAA arbitration process, the arbitrator should consider the implications of the Federal Arbitration Act for an arbitrator's "refusal to hear evidence pertinent and material to the controversy" before applying Rule 59. *See* Federal Arbitration Act, 9 U.S.C. § 10(a)(3).

[2]In preparing this article, the author found little background or history as to the origin of Rule 59 and the circumstances that led to its adoption.

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bar the Non-Paying Party from presenting evidence of its own affirmative claims and limit it to presenting only evidence in defense against the Paying Party's affirmative claims.[3] This is obviously a devastating consequence for the Non-Paying Party's affirmative claims.

An arbitrator may consider a lesser measure than limiting the Non-Paying Party's pursuit of its affirmative claims. Perhaps the arbitrator could limit only certain of the Non-Paying Party's affirmative claims, but not all. Or, the arbitrator could elect to bear the cost of proceeding without payment of full deposits. Proceeding to hear the case with knowledge that the Non-Paying Party is in violation of its arbitration agreement, however, warrants caution to avoid any appearance of compromising the arbitrator's neutrality on the ultimate fact issues. This is something the arbitrator may want to affirmatively confirm in granting a remedy for non-payment under Rule 59.

The last sentence of Subpart (b) of Rule 59 suggests that the arbitrator could, in granting relief, simply cancel the in-person Evidentiary Hearing in favor of a documents-only process, by directing that the Paying Party "submit such evidence as the arbitrator may require for the making of an award." In doing so, however, the arbitrator should also allow for the Non-Paying Party to provide evidence in its defense to the Paying Party's affirmative claims, within the parameters of the restrictions on offering any other evidence. This, however, may open the door to a dispute over what is or is not proper evidence. Therefore, in most circumstances, it would seem the best approach to granting relief under Rule 59 is that described by the third sentence of Subpart (b) of the Rule: "In no event, however, shall a party be precluded from defending a claim or counterclaim." Of course, if the Non-Paying Party has no affirmative claims, Rule 59's impact on the Non-Paying Party is somewhat hollow. In such case, cancelling the Evidentiary

[3]While Rule 59 contemplates barring the presentation of evidence on the Non-Paying Party's affirmative claims, those claims still remain subject to the arbitration until an ultimate determination is made by the arbitrator. It is, in theory, possible that the Paying Party could offer evidence that would support a finding in favor of the Non-Paying Party's affirmative claims. Absent some extremely unusual development, though, barring the Non-Paying Party from introducing any evidence in support of its affirmative claims (not its defenses) is tantamount to a "death penalty" sanction for the Non-Paying Party's affirmative claims.

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Hearing and requiring submission of "such evidence as the arbitrator may require for the making of an award" may very well be appropriate.

The balance of this article will focus on the use of Rule 59 to allow the Paying Party a path forward in arbitration of a dispute that involves competing affirmative claims, rather than suffer termination of the proceedings. The arbitrator will first learn of the fact of non-payment from the AAA Case Manager. By that time, the Case Manager presumably will have informed the parties of the fact of non-payment "in order that one of them may advance the required payment." The Rule implies that the Case Manager will have already pointed out to the parties that Rule 59 is a basis for seeking remedies against a Non-Paying Party, and a threat to the Non-Paying Party's affirmative claims. The arbitrator would do well to confirm that the Case Manager has indeed done so, as the presence of the Rule may encourage the Non-Paying Party to reconsider the consequences of its breach of the arbitration agreement.

Let us assume that the arbitration agreement expressly adopts the AAA Rules, and that the arbitrator has been informed of the fact of non-payment. Further assume the Non-Paying Party has certain affirmative claims, including a claim to recover attorney fees if found to be the prevailing party. What steps should the arbitrator take to fairly apply Rule 59?

First, the arbitrator must be concerned with maintaining the Non-Paying Party's right to due process, fairness, and neutrality. The fact of non-payment should not infringe on either the arbitrator's impartiality or the Non-Paying Party's right to be heard on the circumstances behind the non-payment of its share of the assessed deposits. The arbitrator may enter an order suspending the Arbitration for non-payment of deposits and setting a deadline for the Paying Party to request interim relief pursuant to Rule 59. The order should make it clear that the seeking of relief under Rule 59 should be in the form of a Motion for Relief, in which the Paying Party will declare whether it will pay the Non-Paying Party's share of unpaid deposits. The arbitrator should also indicate in the order that the application of Rule 59 may result in the Non-Paying Party being barred from asserting or pursuing its affirmative claims. The order may also indicate that if the Paying Party does not seek relief under Rule 59, the arbitrator will then consider

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whether to terminate the arbitration for non-payment of the deposits. For an example of an "Order Setting Deadline to Seek Remedies Pursuant to Rule 59," see Appendix "B."

Let us next assume that the Paying Party affirmatively responds to the order by filing a Motion for Relief under Rule 59. What next? Another order should be issued to continue the suspension and set a deadline for the Non-Paying Party to respond to the Paying Party's motion. For an example of an "Order on [Paying Party]'s Motion for Remedies Under Rule 59," see Appendix "C." It is important to allow the Non-Paying Party to be heard. For example, the Non-Paying Party may simply be unable to afford payment, in which case the arbitrator may want to encourage the Case Manager to inform the Non-Paying Party that it may seek an extreme hardship waiver of the AAA's administrative fees under Rule 55 (if such information has not already been provided).

The Non-Paying Party who simply refuses to pay its share of deposits might also ignore the deadline to respond to the Paying Party's Motion for Relief under Rule 59. If so, the arbitrator will be in position to enter an order granting relief to the Paying Party by restricting the Non-Paying Party's presentation of evidence in support of its affirmative claims. In granting relief under Rule 59, the arbitrator should recite the history of how the fact of non-payment has been handled, to demonstrate both due process and impartiality. The arbitrator should require the Paying Party to work with the Case Manager to (i) determine the amount of the deposit that must be paid to the AAA to continue the arbitration and cover the cost of the interim measure proceedings and orders, and (ii) declare whether it will elect to pay the full amount of the deposits so that the arbitration may proceed to hearing. The arbitrator should make it clear that if the Paying Party does so elect, and the AAA has received payment of the required deposit on or before a date certain, then the arbitration will proceed to Evidentiary Hearing, to be rescheduled following confirmation from the AAA that the requirement for payment of deposits has been met.

The order granting relief may also require the parties to use the AAA's on-line calendaring tool to determine a suitable date for the Evidentiary Hearing. The order should declare the Non-Paying Party is prohibited from

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asserting or pursuing its affirmative claims, and that it shall be limited to presenting only such evidence as is relevant to the defense of the affirmative claims of the Paying Party. It is also good form for the arbitrator to recognize that the Non-Paying Party may still salvage the situation by paying its share of the deposits prior to an established deadline. The arbitrator may also require that the Non-Paying Party must, as a condition of seeking to reinstate its right to present evidence on its affirmative claims, file a motion requesting this by the appointed deadline, and indicate that such a motion shall be subject to a showing of good cause prior to setting a new date for the Evidentiary Hearing. Finally, the arbitrator should make it clear that, if the AAA confirms that it has not received the full deposit by a date certain, from either the Paying Party or from both parties, the arbitrator will proceed to terminate the arbitration without further proceedings. For an example of an "Order Granting *[Paying Party]*'s Motion for Remedies Under Rule 59," see Appendix "D."

Once measures for relief have been granted, and the Evidentiary Hearing has been rescheduled, the arbitrator should issue a revised Scheduling Order. Depending on the timing of events, it is possible that further action must be taken with respect to the Non-Paying Party's filings prior to the granting of relief under Rule 59. For example, the Non-Paying Party may have already submitted Exhibits to the arbitrator under the prior Scheduling Order. If so, the arbitrator may need to require the Paying Party to present argument on which of the Non-Paying Party's exhibits should be barred on the grounds that they are only relevant to the Non-Paying Party's affirmative claims. The parties may dispute whether certain exhibits are relevant to the Non-Paying Party's right to defend against the Paying Party's affirmative claims. If so, this can be taken up either in advance or at the commencement of the Evidentiary Hearing.

The arbitrator must then prepare to manage the Evidentiary Hearing subject to the order barring the presentation of any evidence in support of the Non-Paying Party's barred claims. The arbitrator should be prepared to begin the Evidentiary Hearing with an appropriate explanation to both parties of the process for requiring the Non-Paying Party to adhere to the restriction to evidence of a defensive nature. The arbitrator should remind

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the parties that the arbitrator remains neutral and has an open mind to hearing all the evidence to be presented on the ultimate fact issues related to the Paying Party's affirmative claims, and that the granting of prior orders relating to the non-payment of deposits will not have any influence on the arbitrator's consideration of such evidence and the arguments of both parties as to whether the Paying Party will prevail on its affirmative claims. During the Evidentiary Hearing, the Non-Paying Party may nevertheless attempt to present evidence in support of its barred claims. If so, the arbitrator must be prepared to put a halt to this and remind the Non-Paying Party that this is no longer permissible.

After the Evidentiary Hearing is closed, the Award must be rendered with recognition of the order that barred the Non-Paying Party's presentation of evidence on its affirmative claims. In doing so, the arbitrator may want to recite in the Award the due process steps taken before the barring of such evidence as support for denying any affirmative claims of the Non-Paying Party. For an example of an "Arbitration Award" in favor of the Paying Party, with due process recitations, see Appendix "E." Finally, in rendering the Award, the arbitrator will need to consider whether to award costs to the Paying Party. In doing so, the arbitrator should be careful to work with the Case Manager to determine the portion of any costs paid by the Non-Paying Party prior to the granting of relief under Rule 59. Such costs should obviously be excluded from any award of costs to the Paying Party.

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Appendix "A"

American Arbitration Association Construction Industry Rule 59

Rule R-59. Remedies for Nonpayment

(a) 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.

(b) Upon receipt of information from the AAA that payment for administrative charges or deposits for arbitrator compensation have not been paid in full, to the extent the law allows, a party may request that the arbitrator issue an order directing what measures might be taken in light of a party's non-payment. Such measures may include limiting a party's ability to assert or pursue their claim. In no event, however, shall a party be precluded from defending a claim or counterclaim. The arbitrator must provide the party opposing a request for such American Arbitration Association measures with the opportunity to respond prior to making any such determination. In the event that the arbitrator grants any request for relief which limits any party's participation in the arbitration, the arbitrator shall require the party who is making a claim and who has made appropriate payments, to submit such evidence as the arbitrator may require for the making of an award.

(c) Upon receipt of information from the AAA that full payments have not been received, the arbitrator, on the arbitrator's own initiative, may order the suspension of the arbitration. If no arbitrator has yet been appointed, the AAA may suspend the proceedings.

(d) If the arbitrator's compensation or administrative fees remain unpaid after a determination to suspend an arbitration due to nonpayment, the arbitrator has the authority to terminate the proceedings. Such an order shall be in writing and signed by the arbitrator.

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Appendix "B"

American Arbitration Association
Construction Industry Arbitration Rules
Case Number: _____

In the matter of the Arbitration between:
_____ (Claimant)
-vs-
_____ (Respondent)

Order Setting Deadline to Seek Remedies Pursuant to Rule 59

On _____, the AAA confirmed to the Arbitrator that deposits have not been paid. This arbitration is hereby suspended for non-payment of deposits. The parties shall have until _____ to arrange for payment of the deposits. Accordingly, it is hereby Ordered:

1. Any party who has properly paid its portion of the required deposit to the AAA shall have until, 5:00 p.m. on _____, to file a motion for remedies under Rule 59 of the American Arbitration Association's Construction Industry Rules. Such remedies may include restricting any party who has not properly paid its deposit from asserting or pursuing any of such non-paying party's affirmative claims or counterclaims.

2. The non-paying party shall respond to any such Motion within ten (10) days after receiving notice that it has been filed.

3. This arbitration proceeding shall remain suspended until (i) the Arbitrator rules on any timely filed motion for remedies under Rule 59, (ii) the Scheduling Order has been modified to provide for an Evidentiary Hearing on the affirmative claims or counterclaims to be presented, and (iii) the AAA has confirmed to the Arbitrator that all deposits have been paid to the AAA.

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4. If, by 5:00 p.m. on _____, no motion has been filed by the party who is a paying party to request remedies under Rule 59, this arbitration shall, without further order, be deemed terminated.

_____

_____, Arbitrator

Date issued: _____

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Appendix "C"

American Arbitration Association
Construction Industry Arbitration Rules
Case Number: _____

In the matter of the Arbitration between:
_____ (Claimant)
-vs-
_____ (Respondent)

Order on *[PAYING PARTY]*'s Motion for Remedies Under Rule 59

The Arbitrator is in receipt of ***[PAYING PARTY]***'s motion for remedies under Rule 59. ***[PAYING PARTY]*** seeks to restrict ***[NON-PAYING PARTY]*** from putting on evidence in support of its affirmative claims. Pursuant to Rule 59 of the American Arbitration Association's Construction Industry Rules, it is hereby Ordered:

Within ten (10) days, on or before 5:00 p.m. on _____, and unless the American Arbitration Association has previously confirmed in writing that all deposits have been paid, ***[NON-PAYING PARTY]*** is hereby ordered to file its response to the such motion.

_____

_____, Arbitrator

Date issued: _____

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Appendix "D"

American Arbitration Association
Construction Industry Arbitration Rules
Case Number: _____

In the matter of the Arbitration between:
_____ (Claimant)
-vs-
_____ (Respondent)

ORDER GRANTING *[PAYING PARTY]*'S MOTION FOR REMEDIES UNDER RULE 59

On _____, the AAA confirmed to the Arbitrator that the deposits assessed for this arbitration had not been fully paid. Therefore, on _____, the Arbitrator issued an order suspending this arbitration for non-payment of deposits, and allowing the filing of a motion for remedies pursuant to Rule 59 of the Construction Industry Rules of the AAA.

On _____, ***[PAYING PARTY]*** timely filed its motion for remedies under Rule 59, seeking an order barring the ***[NON-PAYING PARTY]*** from asserting or pursuing the ***[NON-PAYING PARTY]***'s affirmative claims.

[NON-PAYING PARTY] was given the opportunity to file, but has not filed, any response to ***[PAYING PARTY]***'s motion, which response was due to have been filed by no later than 5:00 p.m., on _____.

Based on the foregoing, and pursuant to Rule 59, it is hereby Ordered:

[PAYING PARTY] shall, on or before 5:00 p.m. on _____, (i) confer with the AAA's Case Manager to determine the amount of the deposit that must be paid to the AAA to continue this arbitration and cover

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the cost of the additional proceedings pursuant to Rule 59, and (ii) elect whether to pay the amount of any such unpaid deposits in full so that this arbitration may proceed to hearing. If ***[PAYING PARTY]*** so elects, and the AAA confirms receipt of payment of the required deposits on or before _____, then this arbitration shall proceed to an Evidentiary Hearing, the date for which shall be re-scheduled following such confirmation. The Evidentiary Hearing shall be re-scheduled for such date and time as the AAA determines by the on-line postings of availability by the parties and the Arbitrator to be appropriate for their respective schedules. Pursuant to Rule 59, ***[NON-PAYING PARTY]*** is hereby prohibited from asserting or pursuing ***[NON-PAYING PARTY]***'s affirmative claims, and ***[NON-PAYING PARTY]*** is hereby limited to presenting only evidence relevant to the defense of the claims of the ***[PAYING PARTY]***.

The foregoing notwithstanding, if prior to 5:00 p.m., on _____, the AAA confirms in writing that ***[NON-PAYING PARTY]*** has paid to the AAA ***[NON-PAYING PARTY]***'s share of the required deposits to continue this arbitration, ***[NON-PAYING PARTY]*** may file a motion requesting that ***[NON-PAYING PARTY]*** be permitted to pursue ***[NON-PAYING PARTY]***'s affirmative claims and present evidence in support thereof, which motion shall be subject to a showing of good cause, to be heard prior to the date set for rescheduling of the Evidentiary Hearing.

It is further ordered that, if receipt of payment of the full amount of the deposits has not been confirmed by the AAA in writing to the parties and the Arbitrator by 5:00 p.m., on _____, from either the ***[PAYING PARTY]***, or both parties, this arbitration shall be deemed terminated without further proceedings.

_____

_____, Arbitrator

Date issued: _____

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Appendix "E"

American Arbitration Association
Construction Industry Arbitration Rules
Case Number: _____

In the matter of the Arbitration between:
_____ (Claimant)
-vs-
_____ (Respondent)

ARBITRATION AWARD

On _____, the Evidentiary Hearing in this arbitration was conducted.

The following party representatives were again present:

For the Claimant:

_____

_____

For the Respondent:

_____

_____

The Evidentiary Hearing in this arbitration was rescheduled to _____, following the entry of an **Order Granting *[PAYING PARTY]*'s Motion for Remedies Under Rule 59**. Pursuant to such Order, ***[NON-PAYING PARTY]*** was barred from asserting or pursuing ***[PAYING PARTY]***'s affirmative claims for having failed to pay its share

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of the deposits assessed by the AAA for this arbitration proceeding. Prior to entry of such Order, ***[NON-PAYING PARTY]*** was provided notice and opportunity to be heard on such motion, but the ***[NON-PAYING PARTY]*** failed to respond. Accordingly, ***[NON-PAYING PARTY]*** was limited at the Evidentiary Hearing to presenting only evidence relevant to the defense of the ***[PAYING PARTY]***'s claims, and no evidence was presented on ***[NON-PAYING PARTY]***'s claims for affirmative relief.

Having reviewed the evidence and exhibits received on ***[PAYING PARTY]***'s claims, and the parties' submissions, pleadings, briefs, in this matter, the following AWARD is hereby rendered:

1. ***[NON-PAYING PARTY]***'s claims are hereby denied.

2. ***[PAYING PARTY]*** is the prevailing party under Paragraph _ of the parties' Construction Contract.

3. ***[NON-PAYING PARTY]*** is hereby ordered to pay to ***[PAYING PARTY]*** as the prevailing party, damages as follows:

a. An amount of $ _____ as the amount of damages awarded to ***[PAYING PARTY]*** on its affirmative claims in this dispute;

b. An amount of $ _____ to compensate ***[PAYING PARTY]*** for the amount of its attorney fees that I find ***[PAYING PARTY]*** has reasonably and necessarily incurred in this dispute;

c. An amount of $ _____, which I find was paid by ***[PAYING PARTY]*** for the administrative fees of the American Arbitration Association;

d. An amount of $ _____, which I find was

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paid by the ***[PAYING PARTY]*** for the compensation of the Arbitrator; and

e. Such additional sums, if any, as a court of law with jurisdiction over this matter in the future may finally determine to be appropriate to award to ***[PAYING PARTY]*** in the event of any appeal of this award by ***[NON-PAYING PARTY]***, or any proceeding required to be instituted to confirm and enforce this Award.

4. All claims, counterclaims and relief sought, and not otherwise addressed above or by any prior rulings of the Arbitrator are hereby expressly denied.

_____

_____, Arbitrator

Date issued: _____

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