# *The Arbitration Newsletter*

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*The Arbitration Newsletter* is published periodically by Whitaker Chalk Swindle & Schwartz PLLC, Fort Worth, Texas, to explore the rapidly developing law and practice of commercial arbitration both in the U.S. and other countries.[1]

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## CAREFUL PLEADINGS AND RESPONSES: RESPONDING TO ISSUES BEYOND CONTRACTUAL OBLIGATIONS TO ARBITRATE MAY WIDEN ARBITRATOR'S SCOPE OF ISSUES TO RESOLVE

### *OMG, L.P.; John Gallo; Greg Martin v. Heritage Auctions, Inc.*, No. 14-10403, 612 Fed. Appx. 207 (5th Cir. May 8, 2015)[2]

An arbitration award that found no "meeting of the minds" and contract cancellation as to unperformed contract obligations was vacated by a federal district court for the Northern District of Texas on "exceeded powers" ground of 9 U.S.C. §20(a)(4). The Fifth Circuit reversed the trial court and instructed the court to confirm the award.[3] John Gallo, Greg Martin, and OMG, L.P. ("OMG") entered into an Asset Purchase Agreement ("APA") and a Consulting Agreement ("CA") with Heritage Auctions, Inc. ("Heritage") in 2011. Both the APA and CA contained the following broad arbitration provision:

> **Any dispute** or difference between the Parties hereto **arising out of or in any way related to this Agreement or the transactions contemplated hereby** that the Parties are unable to resolve themselves shall be submitted to and resolved by arbitration administered by the American Arbitration Association (the "AAA") **in accordance with the Commercial Arbitration Rules of the AAA** in effect on the date such dispute is submitted to the AAA to be arbitrated . . . The arbitrator shall have the authority to grant any equitable and legal remedies that would be available in any judicial proceeding to resolve any claim hereunder. **This arbitration clause is to be interpreted to the broadest extent allowable by Law**. The Parties understand that **issues subject to such arbitration include any controversy or claim arising out of or relating to this Agreement or any document or instrument delivered in connection herewith** or the breach hereof or thereof. The Parties further agree

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[1] Nothing in *The Arbitration Newsletter* is presented as or should be relied on as legal advice to clients or prospective clients. The sole purpose of *The Arbitration Newsletter* is to inform generally. The application of the comments in *The Arbitration Newsletter* to specific questions and cases should be discussed with the reader's independent legal counsel. My thanks to Tave Parker Doty, a third-year law student at Texas A&M University School of Law, for her research and drafting assistance.

[2] *Cert. denied*, 136 S.Ct. 503, 193 L.Ed.2d 396 (2015).

[3] 612 Fed. Appx. 207, 209.

> that **disputes as to whether a valid agreement to arbitrate has been made in the first instance and whether certain disputes are subject to arbitration under this [Section] shall be submitted to the arbitrators** in accordance herewith.[4]

The CA set forth a plan in Exhibit A to the CA where Gallo and Martin would receive commissions on "Merchandise," defined as:

> Consultant and Martin shall be responsible for procuring for Company firearms and firearm related merchandise on consignment for auction (the "Merchandise"), using their reasonable best efforts.[5]

After the first auction, where items Martin procured were sold, a dispute arose concerning the meaning of "Merchandise" in the CA. OMG contended it should receive commissions on all firearm and firearm related items sold by Heritage, including western art, correspondence, and antique items, regardless of who procured the items.[6] Heritage interpreted "Merchandise" to mean items OMG procured and merchandise with a direct relationship to firearms, including items like bullets, bayonets, and holsters.[7] Ivy determined the relationship between OMG and Heritage could not be saved.[8] On February 27, 2012, Heritage sent a letter to OMG terminating the CA, and Heritage filed a demand for arbitration with AAA.[9]

In Heritage's demand for arbitration, it sought damages from OMG for breach of the CA and for fraud in the inducement.[10] Heritage pled in the alternative that if the arbitrator found the CA was ambiguous as to whether or not OMG was entitled to commissions for sales of firearms and firearms related merchandise procured by others, then Heritage asked the arbitrator to find that there was not a meeting of the minds between the parties and the CA should be rescinded.[11] This request was also presented in Heritage's first and second amended demands for arbitration.[12] Heritage claimed OMG did not challenge the arbitrator's authority to consider the "meeting of the minds" question or Heritage's rescission request.[13] OMG filed a pre-hearing brief that did not contest the arbitrator's authority.[14] During the arbitration, the arbitrator questioned the parties about the meeting of the minds argument in the following dialogue:

> ARBITRATOR: When we started, when y'all were doing your opening statements and Mr. Bayer [counsel for Heritage] made the argument about no meeting of the minds, I seem to recall somebody on the [Plaintiffs'] side saying that that argument was made in the pre-trial brief but not in a pleading. Did somebody say that or did I just dream that?

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[4] Defendant-Appellant Heritage Auction, Brief of Appellant ¶ D (emphasis not present in CA or APA).
[5] OMG, L.P.; John Gallo; Greg Martin v. Heritage Auctions, Inc., No. 14-10403, 612 Fed. Appx. 207, 208 (5th Cir. May 8, 2015).
[6] *Id.*
[7] *Id.*
[8] *Id.*
[9] Defendant-Appellant Heritage Auction, Brief of Appellant ¶ D.
[10] *Id.*
[11] *Id.*
[12] OMG, L.P., 612 Fed. Appx. at 210.
[13] *Id.*
[14] *Id.*

> MR. MAYNE [counsel for OMG]: There was -- the mutual mistake was made -- the term, "mutual mistake," I believe, was asserted for the first time in a brief. There was a reference in the prior pleadings to a meeting of the minds.
>
> ARBITRATOR: Okay. So, I'm not going to -- I mean, because I think it is an issue in the case, just like everything else is an issue in the case, if I make a decision on that -- on that, I'm not going to hear from somebody that is not supported by the pleading or they don't have fair notice?
>
> MR. BAYER [counsel for Heritage]: I guess I'd ask for a trial amendment if they're going to make that argument.
>
> ARBITRATOR: I'll grant the trial amendment to the extent -- and so that's -- okay. That's taken care of. Thank you.[15]

The arbitration lasted ten days, with eight days of hearings and two days of post-hearing briefing.[16] The arbitrator found that there was no meeting of the minds between the parties and ordered partial, prospective rescission ("cancellation") of the CA.[17] The order relieved parties of future obligations under the CA, but it allowed the parties to retain benefits of past performance under the CA.[18]

OMG filed a motion to vacate the arbitrator's award in the Northern District of Texas Court claiming the arbitrator exceeded his authority, committed prejudicial misconduct, ruled on a matter not submitted to him, and committed a manifest error of law.[19] Heritage filed a motion with the same court to confirm the award.[20] The District Court adopted the Magistrate's recommendation that the court, not the arbitrator, was the proper decision-maker as to contract formation.[21] The District Court found the arbitrator exceeded his authority in deciding there was no meeting of the minds between parties and granted OMG's motion to vacate the arbitrator's award.[22] Heritage appealed the District Court's order to the Fifth Circuit Court of Appeals.[23] The Fifth Circuit reversed the District Court's order and remanded with instructions for the District Court to confirm the arbitration award.[24]

Review of a district court's confirmation or vacatur of an arbitrator's award is *de novo*.[25] Courts are highly deferential to arbitrator's awards, and judges defer to the arbitrator's resolution whenever possible.[26] "In deciding whether the arbitrator exceeded [his] authority, [all doubts are resolved] in favor of arbitration."[27] Narrow constraints are placed on federal courts reviewing

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[15] Defendant-Appellant Heritage Auction, Brief of Appellant ¶ D.
[16] *Id.* ¶ E.
[17] OMG, L.P., 612 Fed. Appx. at 209.
[18] *Id.*; 612 Fed. Appx. at 209.
[19] *Id.*
[20] Defendant-Appellant Heritage Auction, Brief of Appellant ¶ D.
[21] OMG, L.P., 612 Fed. Appx. at 209.
[22] OMG, L.P. v. Heritage Auctions, Inc., 11 F. Supp. 3d 740, 741–42 (2015); 612 Fed. Appx. at 209.
[23] OMG, L.P., 612 Fed. Appx. at 209.
[24] *Id.* at 213–14.
[25] *Id.* at 209 (citing Timegate Studios, Inc. v. Southpeak Interactive, L.L.C., 713 F.3d 797, 802 (5th Cir. 2013) (citing Executone Info. Sys. v. Davis, 26 F.3d 1314, 1320 (5th Cir. 1994)).
[26] *Id.* at 209 (citing Anderman/Smith Operating Co. v. Tenn. Gas Pipeline Co., 918 F.2d 1215, 1218 (5th Cir. 1990)).
[27] *Id.* at 209 (citing Executone Info Sys. v. Davis, 26 F.3d 1314, 1320 (5th Cir. 1994)).

arbitration awards by the Federal Arbitration Act ("FAA").[28] Here, OMG argued that the arbitrator exceeded his authority in cancelling the CA.[29] Specifically, OMG argued: (1) since the arbitrator found a contract did not exist between OMG and Heritage, he could not draw authority from the CA and APA to decide the contract formation dispute, and (2) since the contract formation issue was not submitted to arbitration by either party, OMG did not consent to arbitrate the contract formation issue.[30]

The Fifth Circuit observed that "[a]rbitration is a matter of contract, and the FAA requires courts to honor parties' expectations."[31] The Fifth Circuit also pointed out that "once the parties have gone beyond their promise to arbitrate and have actually submitted an issue to an arbiter, we must look both to their contract and to the submission of the issue to the arbitrator to determine his authority."[32] The actions of parties may also allow arbitration of issues outside their contractual arbitration agreements.[33]

The Fifth Circuit determined that the arbitrator had the authority to resolve the contract formation issue. Heritage and OMG, from initial pleadings to post-arbitration briefings, disputed whether a meeting of the minds had occurred and whether rescission would be a proper remedy. Therefore, the parties had submitted the issue to the arbitrator for resolution.[34] Heritage "sufficiently asserted" there had been no meeting of the minds, OMG never contested the arbitrator's authority to resolve the issue, OMG disputed the meeting of the minds issue, and, as a result, the parties agreed to arbitrate the issue of contract formation.[35]

The Fifth Circuit noted that if OMG did not believe the arbitrator had the authority to decide the meeting of the minds and contract formation issues, it should have refused to arbitrate the issues and allowed the court to determine the arbitrator's authority.[36] Instead, OMG responded to the issues throughout the arbitration proceedings.[37] "OMG simply cannot wait until it receives a decision with which it disagrees before challenging the arbitrator's authority."[38]

## OBSERVATIONS

1. The parties entered into a clear and unmistakable delegation of arbitrability to the arbitrator.

2. The parties granted unlimited equitable powers to the arbitrator, much broader than the equitable powers granted by R-47(a) of the AAA Commercial Arbitration Rules (2013).

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[28] 9 U.S.C. §§ 1–16; *see* Hall Street Assocs. v. Mattell, Inc., 552 U.S. 576, 586 (2008).
[29] OMG, L.P.; John Gallo; Greg Martin v. Heritage Auctions, Inc., No. 14-10403, 612 Fed. Appx. 207, 209–10 (5th Cir. May 8, 2015).
[30] *Id.* at 210.
[31] *Id.* (quoting AT&T Mobility LLC v. Concepcion, 131 S.Ct. 1740, 1752 (2011)).
[32] *Id.* (quoting Piggly Wiggly Operators' Warehouse, Inc. v. Piggly Wiggly Operators' Warehouse Indep. Truck Drivers Union, Local No. 1, 611 F.2d 580, 584 (5th Cir. 1980)).
[33] *Id.* (citing Executone Info Sys. v. Davis, 26 F.3d 1314, 1323 (5th Cir. 1994)).
[34] *Id.* at 210.
[35] *Id.*
[36] *Id.* at 211–12.
[37] *Id.* at 210.
[38] *Id.* at 212; *see* Jones Dairy Farm v. Local No. P-1236, United Food & Commercial Workers Int'l Union, 760 F.2d 173, 175 (7th Cir. 1985).

3. Consent to arbitrator authority can occur by conduct of the arbitration parties.

4. Footnote 5 to the Fifth Circuit's opinion in this case recognizes the importance of the arbitrator's "informed judgment" in formulating remedies.

5. In footnote 3 the Fifth Circuit chose not to decide two questions: (i) whether a court only could decide "meeting of the minds" issues when faced with "a contested motion to compel arbitration based on a potentially non-existent contract" (citing U.S. Supreme Court cases); and (ii) whether the "clear and unmistakable evidence" standard should be applied in review of whether the parties agreed to submit arbitrability to the arbitrator.

6. Although this is a no precedent case under the Fifth Circuit R.47.5.4, it offers helpful procedural and practice guidance to arbitration practitioners.