The Act is not the entire story: How to make sense of the U.S. Arbitration Act

Kluwer Arbitration Blog
April 4, 2018

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Please refer to this post as: Ylli Dautaj, 'The Act is not the entire story: How to make sense of the U.S. Arbitration Act', Kluwer Arbitration Blog, April 4 2018, http://arbitrationblog.kluwerarbitration.com/2018/04/04/act-not-entire-story-make-sense-u-s-arbitration-act/

The central point of this note is that the U.S. law of arbitration is not clear from the text of the Federal Arbitration Act (FAA). The FAA is archaic and in need of updating. The FAA is the oldest – but still functioning – arbitration statute in the world. Case law has rewritten much of its content, so that the statute's true content is buried in federal decisional law. Foreign-trained lawyers or scholars especially are unlikely to understand the U.S. law of arbitration through the statute.

The U.S. Supreme Court has played an important role in developing international commercial arbitration (ICA), which in turn has played a huge role in developing and recrafting the U.S. law of arbitration. The Supreme Court early on distinguished international and domestic agreements in order to broaden the subject-matter arbitrability of the former. This would account for, among other things, global realities and international comity. For example, securities and antitrust disputes came to fall within the ambit of arbitrability in ICA.

The Supreme Court later relied on the precedents established in ICA related cases in order to justify the creation of, for example, securities arbitration in domestic arbitration (*see Shearson/Am. Express, Inc. v. McMahon,* 482 U.S. 220 (1987) and *Rodriguez de Quijas v. Shearson/Am. Express, Inc.,* 490 U.S. 477 (1989)). This author thinks that the U.S. Supreme Court has justified the widening of subject-matter arbitrability in a domestic setting on the basis of (1) being pro-arbitration, and (2) on precedent that was initially based on the distinction between international and domestic agreements.

This note will highlight three cases that demonstrate the importance of judge-made law in U.S. arbitration: *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, *reh'g denied*, 419 U.S. 885 (1974); *and Mitsubishi Motors Corp. v. Soler Chrysler-Playmouth, Inc.*, 473 U.S. 614 (1985). In Arbitration Law in a Nutshell, Professor Carbonneau describes this "trilogy" as one of four pillars of U.S. arbitration. It represents the fourth pillar – the international one. As Professor Carbonneau writes, the case law has established that: (1) arbitration is vital to the resolution of labor and management disputes; (2) the FAA can preempt contrary state laws on arbitration; (3) arbitrators have substantial authority to resolve matters of arbitral procedure; and (4) some of the international arbitration cases have "played a decisive role in crafting the general domestic doctrine on arbitration [and] […] [given] rise to another string of cases on subject-matter or statutory arbitrability." This note will discuss part of the fourth – international – pillar, only.

Case Analysis

In *Scherk*, the parties agreed to arbitrate in Paris. Alberto-Culver alleged that Scherk's breach violated

the 1933 Securities Act and the 1934 Securities Exchange Act. Could that issue of regulatory law be resolved by arbitrators? The court in *Scherk* held that:

> A parochial refusal by the courts of one country to enforce an international arbitration agreement would not only frustrate these purposes, but would invite unseemly and mutually destructive jockeying by the parties to secure tactical litigation advantages.
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> […]
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> For all these reasons, we hold that the agreement of the parties in this case to arbitrate any dispute arising out of their international commercial transaction is to be respected and enforced by the federal courts in accord with the explicit provisions of the [FAA].

With this decision, the Supreme Court of the United States took a leadership position in the elaboration of the legal doctrine on ICA. It concluded that contracts for arbitration were vital to both global commerce and international contracting. The ruling in favor of "international comity" was followed by the Court's decision in *Mitsubishi*. There, the Court cited *Scherk* with approval and determined that there was a virtually irrebuttable presumption favoring enforcing freely-negotiated transborder contracts. It decided that antitrust disputes arising from national law were arbitrable as a general matter, and international arbitrators could rule on the application in that particular case.

U.S. courts also favor arbitration and arbitrability at the enforcement stage of the arbitral process. For example, in *The Bremen* (which involved the enforcement of a forum-selection-clause) the Court stated that international commercial contracts implicate special policy concerns and the "[d]omestic strictures on judicial jurisdiction and the enforceability of contract provisions had to yield to the provisions in the parties' bargain." Professor Carbonneau has analyzed this case as follows:

> The Court emphasized new global commercial realities and asserted that legal doctrine should be made to respond to them in a nonsectarian fashion. In matters of transborder litigation, the function of domestic courts was not to create legal roadblocks to, or compete with, arbitration for jurisdictional supremacy.
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> […]
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> *The Bremen* is the first case in which the Court established a marked boundary between law for domestic and international matters, holding that domestic rules could be unsuitable for application in the international sector and that these rules should be disregarded or modified when such a conflict emerged.

As Professor Carbonneau has written, *Scherk* and *Mitsubishi* established that a "special regime emerged for international business contracts "allowing international arbitrators" to rule upon claims based upon U.S. regulatory law." The Court blurred the distinction between domestic and international arbitration in relation to subject-mattter arbitrability and "made universal subject-matter arbitrability an integral part of U.S. domestic law." The Court was willing to facilitate arbitration and protect and implement its "purposes." Through the Court's doctrine, the U.S. legal system had taken a business efficient and effective pro-arbitration stance. U.S. courts would enforce international dispute resolution clauses providing for arbitration that may not have been enforceable domestically. The Court had established a federal policy favoring international commerce and arbitration.

In both *McMahon* and *Rodriguez de Quijas* the Supreme Court interpreted *Mitsubishi* and *Scherk* to support its reasoning in order to discredit the *Wilko Doctrine* (*see Wilko v. Swan,* 346 U.S. 427 (1953)). These two cases led to the creation of what Professor Carbonneau calls "securities arbitration." This author is of the view that the Supreme Court failed to mention that the international aspects in the above-mentioned trilogy was crucial for those holdings.

Concluding Remarks

The pro-arbitration stance has led to the growing scope of arbitrability in ICA and subsequently in domestic arbitration, too. Possibly, a growing scope of arbitrability might lead to "judicialization" of arbitration. "Judicialization" of arbitration might be a good thing, but it can also be the opposite. This author wants to remind the reader of two crucial distinctions; that is, (1) there is a significant difference between domestic and international arbitration, and (2) the "pros" of arbitration—confidentiality, flexibility, speed, costs, etc.—might slowly diminish with a "judicialization" of arbitration. However, the growing scope of arbitrable cases may help in reducing the back-log of courts in civil matters and provide for further expertise to the dispute, and therefore the pro-arbitration stance might sit well with judges and the business community. Notwithstanding this, cases including, among other things, issues of antitrust and securities might have a public importance that trumps the pro-arbitration stance in domestic arbitration. While public interest may trump pro-arbitration sentiments domestically, it could be decided that it does not trump the growing scope of arbitrable cases in ICA. This is because of "international comity" and the need for a predictable ICA system. With that said, the U.S. courts will still have the enforcement stage available to ensure that their securities and antitrust laws have been properly enforced. The New York Convention guarantees the public policy exception to enforcement or recognition of arbitral awards.

While these cases do not paint the entire picture of U.S. arbitration law, they indicate the origins of its evolution. For purposes of informing oneself on the content of U.S. arbitration law, the case law on the FAA is vital. This author has benefited extensively from – and would take this opportunity to recommend – Professor Thomas Carbonneau's 4th edition on "Arbitration Law in a Nutshell."