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Defining 'Arbitrability'

The United States vs. the rest of the world.

BY LAURENCE SHORE

OUTSIDE THE United States, the term "arbitrability" has a reasonably precise and limited meaning: i.e., whether specific classes of disputes are barred from arbitration because of national legislation or judicial authority. Courts often refer to "public policy" as the basis of the bar.

This international understanding of arbitrability stems from the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, which in Article II(1) provides that each contracting state shall recognize an arbitration agreement "concerning a subject matter capable of settlement by arbitration," and in Article V(2)(a) provides that an arbitral award may be refused recognition and enforcement if the "subject matter of the difference is not capable of settlement by arbitration under the law of that country."

Thus, the subject matter of the claim is the key to "arbitrability" in international commercial arbitration, and the question to be asked is, "Under the law of the place of arbitration or the State where award enforcement is being sought, are the specific claims capable of settlement by arbitration or must they be resolved in a national court?"

The United States also calls this subject matter issue "arbitrability." The U.S. courts and, at least to date, the U.S. Congress have kept with international trends and have sometimes even established approaches that other states with rich arbitration histories have followed by permitting an ever-widening body of disputes to be heard by arbitral tribunals.[1] The U.S. Supreme Court has stated that such "questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration."[2]

However, "arbitrability" in the United States also means—and in this the United States is different from the rest of the world, and the difference can create confusion—the preliminary question of whether an arbitral tribunal has the authority to decide, as an initial matter, that a given dispute should be submitted to arbitration for a determination of whether the arbitral tribunal has jurisdiction over the dispute.

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The federal policy favoring arbitration has not traditionally applied to the initial determination of whether a valid arbitration agreement exists, such that the arbitral tribunal may then assess whether the scope of that agreement covers the dispute and the parties in question.

This aspect of what the United States calls "arbitrability" can be an exceedingly complicated question, both here and internationally. This is so even where, as here, the principles of "separability" (or in the civil law lexicon "autonomy")[3] and "competence-competence"[4] are firmly established. Indeed, these principles actually engender the "arbitrability" problem, the essence of which is whether the arbitration agreement itself in a contract has been sufficiently attacked as invalid by a respondent such that it would be improper for an arbitral tribunal constituted under that "agreement" to make the initial determination of its validity.

Traditionally, U.S. courts have had the power to determine all questions of "arbitrability," in the non-international sense, before or after a dispute has been submitted to arbitration. In recent years, however, this "gateway" approach has given ground to arbitrators having the authority to make the initial decisions. Still, this trend toward initial decision-making by arbitrators remains qualified by the problem noted above when the arbitration clause itself is attacked. In grappling with this problem, despite the awkward use of terminology, the United States is very much in the mainstream of international commercial arbitration.[5]

A Non-U.S. Perspective

It may first be useful to understand a non-U.S. perspective by considering the judgment of the House of Lords (United Kingdom) in *Premium Nafta Products Limited v. Fili Shipping Co.*,[6] which addressed, inter alia, the issue of whether a party could be bound by submission to arbitration when the party alleged that, but for an act of bribery, he would not have entered into the contract containing the arbitration clause.

The House of Lords concluded that:

(i) the principle of separability required that the arbitration agreement must be treated as a "distinct agreement" that "can be void or voidable only on grounds which relate directly to the arbitration agreement";

(ii) there may be cases where the grounds for invalidity of the main contract are identical to the grounds of invalidity for the arbitration agreement, e.g., forgery, but in this case the ground of attack still must be that the signature to the arbitration agreement was forged;

(iii) an allegation that an agent exceeded his authority by entering into the main agreement is not necessarily an attack on the arbitration agreement, as it would still need to be alleged and shown that the agent had no authority to enter into the arbitration agreement; and

(iv) an allegation that an agent was bribed to enter into the main agreement does not necessarily constitute an allegation that he was bribed to enter into the arbitration agreement: "the arbitration agreement can be invalidated only on a ground which relates to the arbitration agreement and is not merely a consequence of the invalidity of the main agreement."

As Lord Hope commented in his concurring judgment, this approach "serves to underline the golden rule that if the parties wish to have issues as to the validity of their contract decided by one tribunal and issues as to its meaning or performance decided by another, they must say so expressly, otherwise they will be taken to have agreed on a single tribunal for the resolution of all such disputes."

'Separability' in U.S. Courts

Courts in the United States have, in recent years, issued opinions that are similar to the English, and indeed, European, approach and its strong devotion to separability (and competence-competence) as enunciated in *Premium Nafta Products*.

To be sure, in some of these opinions, one may still discern a degree of skepticism about too great a devotion to separability in the context of the gatekeeper question (i.e., who should decide first, a court or an arbitral tribunal, on the issue of the arbitration agreement's validity).

For example, the U. S. Court of Appeals for the Fifth Circuit has held, in the case of *Will-Drill Resources Inc. v. Samson Resources Co.*, that when the actual existence of a contract is challenged, rather than the enforceability of a pre-existing contract, a court rather than an arbitral tribunal may make the initial determination as to whether there was in fact a contract.[7] Such challenges may include lack

of agency authority to bind a party as well as forgery, thus pointing to a less rigid approach to separability than that in *Premium Nafta Products*.

The Fifth Circuit acknowledged that "where parties have formed an agreement which contains an arbitration clause, any attempt to dissolve that agreement by having the entire agreement declared voidable or void is for the arbitrator. Only if the arbitration clause is attacked on an independent basis can the court decide the dispute; otherwise, general attacks on the agreement are for the arbitrator."[8]

Nonetheless, the court in *Will-Drill* stated that where "the very existence of any agreement is in dispute, it is for the courts to decide at the outset whether an agreement was reached." *Will-Drill* supplied both a "golden rule" of policy that the House of Lords was apparently less interested in and a reminder of the limits of separability: (a) it would be unfair to force a party to submit to arbitration when there had never, in fact, been a contract; and (b) separability assumes an underlying contract, so a challenge to the very existence of that underlying contract should not be for the arbitrator to decide.[9]

In certain respects, *Will-Drill* keeps intact the Supreme Court's 1995 determination in *First Options of Chicago Inc. v. Kaplan*,[10] that courts should determine gateway questions of arbitrability and should not assume that the parties agreed to arbitrate arbitrability unless there is clear evidence of such an agreement. *Will-Drill* in effect followed the *First Options* admonition that it would be unjust to force parties to arbitrate when they never contracted to do so.

However, after the *First Options* decision, the Supreme Court has further considered which gateway issues qualify as questions of arbitrability to be decided by the courts, and the Court has limited this category in favor of arbitral tribunals making initial determinations, thus bolstering the federal policy in favor of arbitration.

For example, in 2002 in *Howsam v. Dean Witter Reynolds*,[11] the Court held that a question about a time-bar on arbitration was not a question of arbitrability and was therefore to be determined by an arbitrator. During oral argument, the Court questioned counsel on the meaning of the term "arbitrability" to determine whether a "gateway" question necessarily qualified as a question of arbitrability appropriate for a court.

Justice Stephen Breyer, who eventually wrote for a unanimous Court, commented during oral argument that a presumption that is hostile to finding the intent to have arbitrators arbitrate the issue of arbitrability should not apply "at first blush" when the issue concerned rules of an arbitration forum. With the *Howsam* decision, the Supreme Court made its first important limitation on gateway matters that a court would be expected to decide, and its first important distinction between questions of arbitrability and dispositive-on-the-merits gateway issues that do not qualify as questions of arbitrability.

The *Pacificare*[12] and *Green Tree*[13] decisions further limited the category of arbitrability questions for courts to consider by explaining that when there is an ambiguity in a contract or arbitration agreement, an arbitrator, not a court, must make the initial clarifications and determinations.

Thus, in *Pacificare* the Court held that a potential waiver of a statutory remedy is not a question of arbitrability because an arbitrator can interpret the ambiguous remedy clause of a contract in a way that does not conflict with statutory law. In *Green Tree*, while observing that the issue as to whether the parties have a valid arbitration agreement is reserved for judicial determination, the Court held that when an arbitration clause is silent or ambiguous on the question of class certification, this question is one for an arbitrator, not a court.

Circuit Court 'Arbitrability' Decisions

After *Howsam*, *Pacificare* and *Green Tree*, the category of "arbitrability" questions reserved for the courts has been substantially narrowed, as is apparent from a large number of circuit court decisions.

To choose just one recent decision, in *Emilio v. Sprint Spectrum, L.P.*, the Second Circuit clarified that whether a gateway question is one of substantive arbitrability or one of arbitration procedure is irrelevant if the arbitration agreement in a given contract states that the parties' intentions was to arbitrate all matters.[14]

'Arbitrability' in the United States also means—and in this the United States is different from the rest of the world, and the difference can create confusion—the preliminary question of whether an arbitral tribunal has the authority to decide, as an initial matter, that a given dispute should be submitted to arbitration for a determination of whether the arbitral tribunal has jurisdiction over the dispute.

Sprint argued that the question of whether arbitration was barred under the doctrine of res judicata should have been decided by a court, not an arbitrator. The court held that the arbitration forum was appropriate for answering this question, and focused on Sprint being a sophisticated business that knowingly agreed to "'arbitrate any and all claims controversies or disputes…arising out of or relating to' its agreement with Emilio."

The determining factor for the court was that this arbitration agreement "clearly intended for the arbitrator to decide a defense of res judicata." The agreement also incorporated by reference the JAMS rules, which further provided that the arbitrator shall rule on jurisdictional and arbitrability disputes. Given that arbitration clauses in commercial contracts are typically written broadly, as in *Emilio*, the scope of the tribunal's authority in deciding gateway matters has clearly broadened as well.

Are We Out of Step?

It is a widely held view in the international arbitration community that in certain important respects, e.g., scope of discovery and in general importing litigation procedures into the arbitral process, thereby damaging arbitral autonomy, the United States is at odds with, or at least out of step with, best practices.

U.S. courts and arbitration practitioners' use of the term "arbitrability" has, in the past, contributed to a sense that somehow the United States is different from the rest of the world in dealing with matters relating to the jurisdiction of arbitral tribunals. In part, this is merely an unfortunate difference in word usage: Internationally, "arbitrability" refers only to whether specific classes of disputes are barred from arbitration because of the subject matter of the dispute, whereas in the United States "arbitrability" also refers to the complicated balance between courts and arbitrators regarding who should be the initial decision-maker on issues such as the validity of the arbitration agreement.

In the past several years, U.S. court cases have demonstrated a determination that arbitral tribunals shall have the authority to rule on disputes over arbitration procedure and contract interpretation; these are no longer considered "gateway" questions for the courts to decide. Moreover, the gatekeeper function of the courts has been limited in other significant ways. In this, the United States is no longer out of step with international practice.

However, the thorny question of how far to rely on the principle of separability in circumstances raised by such cases as *Premium Nafta Products* in England and *Will-Drill* in the Fifth Circuit suggest that the international "golden rule"—i.e., it is appropriate to have a single tribunal resolve all disputes—is still probably subject to more skepticism in the United States, where the unfairness of subjecting a party to arbitration when it may not have agreed to it leaves a significant opening for court intervention.

1. The proposed U.S. Arbitration Fairness Act, which has been the subject of intensive criticism by, among others, New York bar committees and arbitration practitioners in the United States and abroad, poses a significant danger to the long-standing openness to "arbitrability" in the United States, as this term is understood outside the United States. This article assumes that Congress will not wrench this country out of the international mainstream of "arbitrability." If that assumption were to be proved wrong, then the terminological differences between the United States and the rest of the world would be very minor compared to the huge gulf on which types of disputes could be heard by international arbitral tribunals.

2. *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 24-25 (1983).

3. I.e., the arbitration agreement is separable from the main contract, such that the invalidity or rescission of the main contract does not necessarily entail the invalidity or rescission of the arbitration agreement. See *Goodman v. THF Construction*, 321 F.3d 1094, 1095-96 (11th Cir. 2003) (citing *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, 388 U.S. 395, 402-05 (1967)); see also *Kayne v. Thomas Kinkade Co.*, 2007 U.S. Dist. LEXIS 97195, *11-13 (N.D. Cal. Dec. 5, 2007).

4. I.e., the arbitral tribunal has jurisdiction to determine its own jurisdiction. *Telenor Mobile Communications AS v. Storm, LLC*, 524 F. Supp. 2d 332, 351 (2d Cir. 2007).

5. In an article with a different focus, I have addressed some aspects of "arbitrability" in the U.S. lexicon. L. Shore, "The United States' Perspective on 'Arbitrability,'" in L. Mistelis and S. Brekoulakis, editors, "Arbitrability: International & Comparative Perspectives" (Kluwer Law International, 2009).

6. [2007] 4 All ER 951, paragraphs 17-19.

7. *Will-Drill Resources Inc. v. Samson Resources Co.*, 352 F.3d 211 (5th Cir. 2003).

8. *Will-Drill*, 352 F.3d at 218.

9. The *Will-Drill* approach is still controlling in the Fifth Circuit: see, e.g., *Gulfside Casino Partnership v. Mississippi Riverboat Council*, 2008 U.S. App. LEXIS 12903, *2-3 (5th Cir. June 18, 2008) ("When a party challenges the very existence of an agreement, as opposed to its continued validity or enforcement, the court, not the arbitrator, must first resolve the dispute."). For a Second Circuit opinion on the question of a forgery attack on the main contract and its relation to the arbitration agreement, see *Opals on Ice Lingerie v. Body Lines Inc.*, 320 F.3d 362 (2d Cir. 2003) (declining to compel arbitration where signature was forged).

10. 514 U.S. 938, 944-45 (1995).

11. 537 U.S. 79, 83-86 (2002).

12. *Pacificare Health Sys. Inc. v. Book*, 538 U.S. 401 (2003).

13. *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444 (2003).

14. 2009 U.S. App. LEXIS 5011, *3 (2d Cir. March 12, 2009).