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# Supreme Court Continues Down Pro-Arbitration Road

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Although arbitration features regularly on the Supreme Court's docket, a number of significant cases have been before the Court recently. The gist of these rulings is a continued pro-arbitration approach, consistent with the Federal Arbitration Act (FAA), 9 U.S.C. § 1. The Supreme Court also confirmed that parties to an arbitration contract are bound by the words of that contract. In addition, by denying certiorari in the *Delaware Coalition for Open Government v. Strine* case, the Court struck a blow to efforts by Delaware to entice litigants to bring commercial disputes to the state through a confidential arbitration program. The refusal to grant cert in the *Delaware* case indicates that, at least for now, there are some limits on confidential arbitration programs administered by courts. This article discusses the lessons of these cases for business litigators who frequently find themselves involved in arbitrations.

**Contractual Class Arbitration Waivers after *Concepcion***

Retail businesses swiftly adapted their consumer contract language to include class arbitration waivers after the Court's decision in *AT&T Mobility, LLC v. Concepcion*, 563 U.S. 321 (2011). In the 2013 term, the Supreme Court made clear in *American Express Co. v. Italian Colors Restaurant*, 133 S. Ct. 2304 (2013), that class arbitration waivers are here to stay and do not offend notions of fairness. The *American Express* case involved merchants who accepted American Express cards as a form of payment and claimed that American Express violated the Sherman Act and used its monopoly power to force them to pay much higher fees than the fees for competing credit cards. *Id.* at 2308.

When the merchants filed their putative class action suit, American Express moved to compel individual arbitrations based on the FAA and the contract between the parties, which provided that there would be "no right or authority for any [c]laims to be arbitrated on a class action basis." *Id.* The merchants opposed the motion, claiming they would be left without a remedy because the cost of the expert analysis needed to prove the antitrust claims was far in excess of the maximum recovery for any individual plaintiff. *Id.* While *AT&T Mobility* addressed class action waivers under the lens of a state-law prohibition, the *American Express* decision addressed the propriety of class action waivers in the context of the "effective vindication" exception articulated in *Mitsubishi Motors Corp. v. Soler Chrysler–Plymouth, Inc.*, 473 U.S. 614, 628 (1985), and *Green Tree Financial Corp. v. Randolph*, 531 U.S. 79 (2001). That exception invalidates arbitration agreements "that operat[e] . . . as a prospective waiver of a party's right to pursue statutory remedies." *American Express*, 133 S. Ct. at 2309–2310. The Supreme Court, in an opinion authored by Justice Scalia, distinguished a party's inability to pursue statutory remedies (which is proscribed under *Mitsubishi*) and a party's inability to prove the statutory

claim due to prohibitive expert costs. *Id.* at 2311. The Supreme Court held that the former would violate public policy but that the latter would not. *Id.*

Justice Kagan, in dissent, identified the decision's practical consequence: Monopolies may choke off a plaintiff's ability to enforce statutory rights using their power to "insist on a contract effectively depriving its victims of all legal recourse." *American Express*, 133 S. Ct. at 2313 (Kagan, J., dissenting). She summarized the majority's decision as concluding such a result was "too darn bad." *Id. American Express* is certainly a win for big businesses, but corporations should remain wary of highly restrictive arbitration agreements limiting prosecution of certain claims as the Supreme Court still maintains the "effective vindication" exception to be valid in certain respects. The words of the arbitration clause in the contract matter, but whether the parties to the clause have equal bargaining power does not appear to be a significant consideration.

**Even Where the Underlying Contract Is Invalid, an Arbitration Clause Is Still Enforceable**
The FAA's strong presumption favoring arbitration applies even if the underlying contract containing the arbitration provision is found invalid. The Supreme Court's *per curiam* opinion in *Nitro-Lift Technologies, L. L. C. v. Howard*, 133 S. Ct. 500, 503 (2012),reinforced prior interpretations of the FAA. Attacks on the validity of the arbitration clause may be resolved by a court or an arbitrator, but attacks on the validity of the underlying contract overall may be resolved only by the arbitrator.

The *Nitro-Lift* case involved a confidentiality and noncompetition agreement between Nitro-Lift and two employees working on oil wells in Oklahoma, Texas, and Arkansas. *Id.* at 502. When the employees quit to work for one of Nitro-Lift's competitors, Nitro-Lift served the employees with a demand for arbitration. *Id.* The employees then filed suit in Oklahoma state court. The state court dismissed the complaint, finding that the agreement contained a valid arbitration clause and that an arbitrator, not the court, must resolve the parties' dispute. *Id.*

The employees appealed to the Oklahoma Supreme Court, which ruled that noncompetition agreements are "void and unenforceable as against Oklahoma's public policy." *Id.*; *see also* Okla. Stat. tit. 15, § 219A. Despite several cases interpreting the FAA as applicable to both state and federal courts, the Oklahoma Supreme Court found the "existence of an arbitration agreement in an employment contract" did not "prohibit judicial review of the underlying agreement." *Nitro-Lift*, 133 S. Ct. at 502. The Oklahoma Supreme Court further determined that its decision rested on "adequate and independent state grounds." *Id.*

The Supreme Court rejected the Oklahoma Supreme Court's reliance on the "adequate and independent state grounds." Reiterating that the FAA declares a *national* policy favoring arbitration, the Supreme Court held that "attacks on the validity of the contract, as distinct from attacks on the validity of the arbitration clause itself, are to be resolved 'by the arbitrator in the first instance, not by a federal or state court.'" *Id.* Furthermore, "an arbitration provision is severable from the remainder of the contract"; hence, despite the unenforceability of the

underlying contract under a particular state's law, the validity of the underlying contract is for the arbitrator to decide. *Id.*

The irony of the *Nitro-Lift* case is that, given the clear state of the law in Oklahoma, an arbitrator would have likely found in favor of the employees and against Nitro-Lift on the substantive claims. Nonetheless, the *Nitro-Lift* case removes all doubt as to the question of whether a court, as opposed to an arbitrator, may determine a contract's validity once the dispute has been deemed to be arbitrable. Savvy practitioners will likely short-circuit the issue altogether by expressly contracting for the specific tribunal to determine the applicability and enforceability of their contract's arbitration clause. Even if they do not go that route, practitioners will in any event want to take a critical eye to their standard arbitration clauses and be sure to tailor the language to the specific situation.

**International Arbitration: Similar Lessons from a Surprising Corner**

The *BG Group* case recently decided by the Supreme Court is another example of the tension that exists between arbitration tribunals and courts as to which tribunal evaluates the arbitrability of a particular dispute and whether certain procedural conditions are preconditions to arbitration or simply claims-processing requirements. *BG Grp., PLC v. Republic of Argentina*, No. 12-138, slip op. (Mar. 5, 2014). The former requires court evaluation; the latter does not. BG Group, a British firm invested in an Argentine utility, disagreed with the Republic of Argentina over interpretation of an investment treaty between Argentina and the United Kingdom. *BG Group*, slip op. at 3. The treaty established a dispute-resolution mechanism whereby a dispute would be submitted to arbitration if it had first been submitted to an Argentine court and the court had not issued a final decision after 18 months had passed. *Id.*

BG Group disputed the validity of certain tariffs enacted by Argentina that affected BG Group's investment and contended that Argentina had violated the treaty. BG Group submitted its claim to arbitration in Washington, D.C. *Id.* at 4. Argentina argued that the arbitrators could not render a decision because BG Group failed to bring its dispute to an Argentine court for 18 months prior to commencing arbitration. *Id.* at 4. The arbitration panel ultimately found BG Group was excused from its failure to comply with the local litigation requirement, and the panel awarded BG Group $185 million in damages. *Id.* at 3–4. The District Court for the District of Columbia confirmed the arbitration award, but the Court of Appeals for the D.C. Circuit reversed, finding that interpretation of the local litigation requirement was a matter for the courts to decide de novo. *Id.* at 4–5.

The Supreme Court granted certiorari on the question of whether the arbitrators' interpretation of the local litigation provision should be reviewed de novo or be granted the deference typically afforded arbitrators' decisions on questions committed to the arbitrator. *Id.* at 5–6. The Supreme Court first analyzed the document as if it were an ordinary contract, not a treaty, and held that the evaluation of the local litigation requirement was a matter for the arbitrators. The Supreme Court relied on its prior jurisprudence that arbitrators, not courts, decide disputes about the meaning and application of procedural preconditions to arbitration. *Id.* at 8 (quoting *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 25 (1983)). In contrast, courts decide

questions of substantive arbitrability, such as whether a claim is covered by an arbitration clause or a party is subject to the clause. *Id.* at 7.

Considering the treaty's local litigation requirement in this light, the Supreme Court found that the local litigation requirement determined "*when* the contractual duty to arbitrate arises, not *whether* there is a contractual duty to arbitrate at all." *Id.* at 8 (emphasis in original). Finding nothing in the treaty suggesting otherwise, the Supreme Court held that if the treaty were an ordinary contract, the interpretation of the local litigation requirement would be the arbitrators' domain. However, the Supreme Court then analyzed whether its reasoning would remain valid given the fact that the document was a treaty. *Id.* at 12–13. The Supreme Court pointed out that the Treaty did not have an explicit "condition of consent to arbitration," as some other treaties do, and that therefore its special nature did not alter the Court's conclusion. *Id.*

The significance of *BG Group* is twofold. First, the Supreme Court granted certiorari to provide clarity on the issue of substantive versus procedural arbitrability to the international arbitration community, extending familiar reasoning from the domestic to the international context. Second, the Supreme Court adhered to earlier precedent from *Moses H. Cone* that arbitrators determine whether the parties have met procedural conditions precedent. Again, the lesson for business lawyers is to draft arbitration provisions carefully and, when faced with one in litigation, to understand and distinguish between substantive and procedural arbitrability.

**The Constitutionality of Confidential Arbitrations Before Sitting Judges**

Finally, in a case closer to home, the Supreme Court recently denied certiorari in *Delaware Coalition for Open Government v. Strine*, 733 F.3d 510 (3d Cir. 2013), *cert. denied*, No. 13-869 (Mar. 24, 2014). In so doing, the Court let stand a decision of the Third Circuit Court of Appeals that a confidential arbitration program implemented by the Delaware Court of Chancery violated the First Amendment. Time will tell as to whether the Delaware program will be renewed in a different format.

To further bolster its reputation as the preferred forum for incorporations and business litigation, Delaware enacted a statute, Del. Code Ann. tit. 10, § 349 (2009), which enabled sitting chancellors of the Delaware Court of Chancery to adjudicate specified commercial cases and make binding decisions that were immediately enforceable as state court judgments. To be eligible for the program, at least one party had to be a Delaware entity, the case could not involve consumer rights, and the amount in controversy had to exceed $1 million. *See* Del. Code Ann. tit. 10, § 347(a)3–5 (2009). The filing fee was set at $12,000, with a per day cost of $6,000. *See* Standing Order of Del. Ch. (Jan. 4. 2010). The program was intended to bring sophisticated commercial disputes before judges experienced in handling such disputes, while allowing the confidentiality found in private alternative dispute resolution and enabling the victor to obtain immediate entry of the arbitral order in state court. Critically, all of the documents and all of the proceedings were to be confidential. (In the interest of full disclosure, Ms. Fenton, one of the authors of this article, participated in the first and only arbitration conducted under the program.)

The Delaware Coalition for Open Government prevailed in its constitutional challenge to the program before the Honorable Mary McLaughlin, a judge of the United States District Court for the Eastern District of Pennsylvania sitting by designation in the District of Delaware. Among other things, the district court found problematic this confidentiality as well as the use of state resources, such as the courthouse, court personnel, and other court infrastructure. *See Del. Coal. for Open Gov't v. Strine*, 894 F. Supp. 2d 493, 500 (E.D. Pa. 2012). The Third Circuit agreed with the district court that the program offended the constitutional right of public access to trials, but the appeals court applied the experience and logic test. *See Del. Coal. for Open Gov't*, 733 F.3d at 514–15. Under that test, the court of appeals determined that the tradition of openness applicable to proceedings held in courthouses before judges was worthy of deference, as were the benefits to the public of openness. *Id.* at 520–21.

Given the lack of a circuit split on the application of the "logic and experience" test and the fact that no other jurisdictions have programs quite like the Delaware program, the Supreme Court's denial of cert is perhaps no surprise. In any event, litigants who might have elected to proceed through the Delaware program instead of private alternative dispute resolution no longer have that option.

**Conclusion**

The Supreme Court makes clear in these cases that arbitration is here to stay and that it will continue to implement the policy of the FAA favoring arbitration when the parties have entered into agreements allowing for it. However, the Supreme Court decisions discussed above confirm that arbitrations, unlike judicial proceedings, are creatures of contract. As the *Delaware* case illustrates, there are boundaries and differences between arbitrations and courts. Ultimately, these boundaries come down to the fact that the courts must provide due process, while the arbitrators must provide the process to which the parties have agreed. As a result, drafters of arbitration clauses must go beyond the default clause and should counsel their clients signing off on those clauses on their meaning as well.

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