FEDERAL COURT VERSUS ARBITRATION:

CONSIDERATIONS WHEN INITIATING YOUR CASE

January 25, 2023

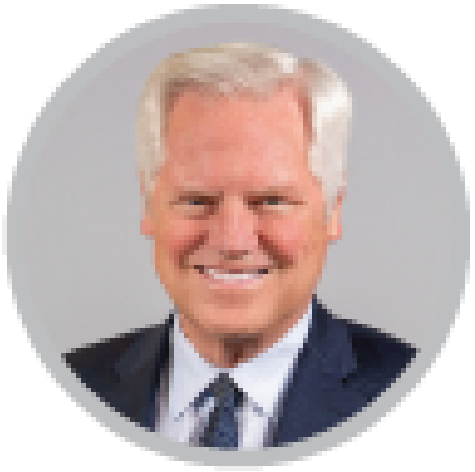
JUDICATE WEST

Alternative Dispute Resolution

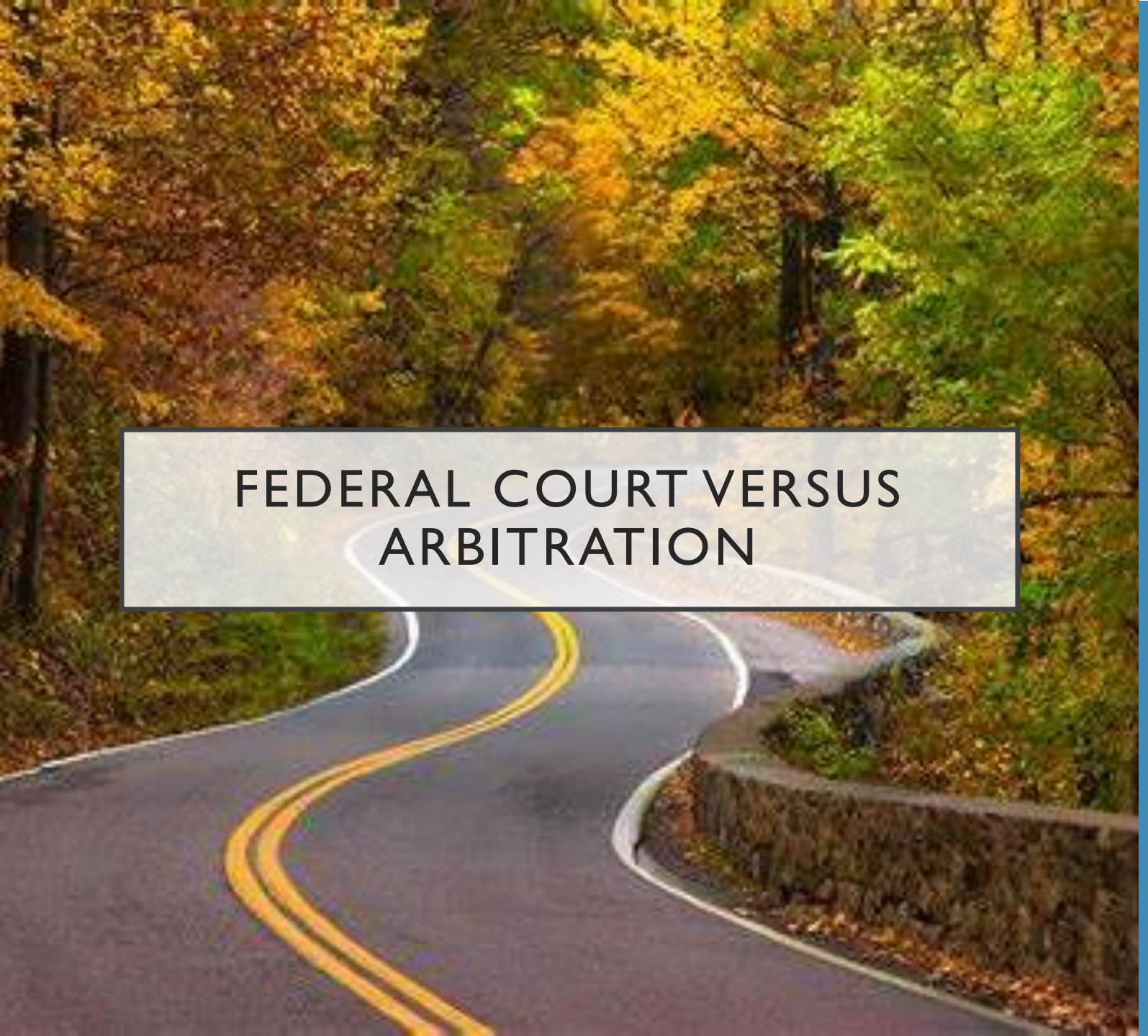
*Results Beyond Dispute*SM

OUR SPEAKERS

Hon. Margaret Morrow (Ret.)



Hon. Andrew Guilford (Ret.)



FEDERAL COURT VERSUS ARBITRATION

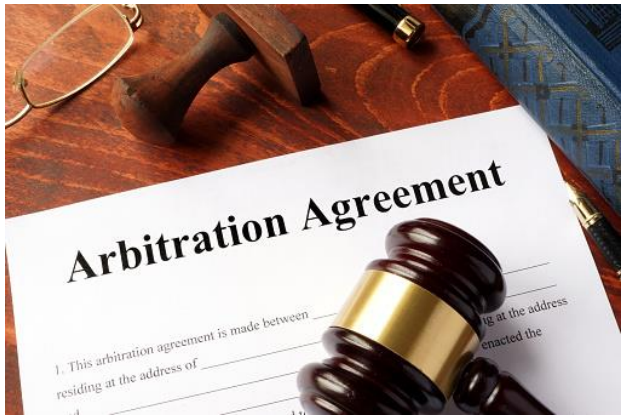
- "Subject Matter" Jurisdiction
- Initiating Your Case, including:
  - Motions to Compel Arbitration in Federal Court
  - Choice of Law Questions in Arbitration Procedure
- "Hearing Officer" Selection (and Challenges)
- Pleading Requirements (and Challenges)

Audience Questions: Please submit your questions using either zoom's Q&A feature or chat feature, and we will do our best to answer them.

"SUBJECT MATTER" JURISDICTION IN FEDERAL COURT VERSUS ARBITRATION

- **Federal Court**: Federal Question / Diversity Jurisdiction

- **Arbitration**: Pre- or Post-Dispute Agreement to Arbitrate



ARBITRATION IS A CREATURE OF CONTRACT

"The point of affording parties discretion in designing arbitration processes is to allow for efficient, streamlined procedures tailored to the type of dispute. It can be specified, for example, that the decisionmaker be a specialist in the relevant field, or that proceedings be kept confidential to protect trade secrets. And the informality of arbitral proceedings is itself desirable, reducing the cost and increasing the speed of dispute resolution."

AT&T Mobility LLC v. Concepcion, 563 U.S. 333, 344–45, 131 S. Ct. 1740, 1749, 179 L. Ed. 2d 742 (2011).

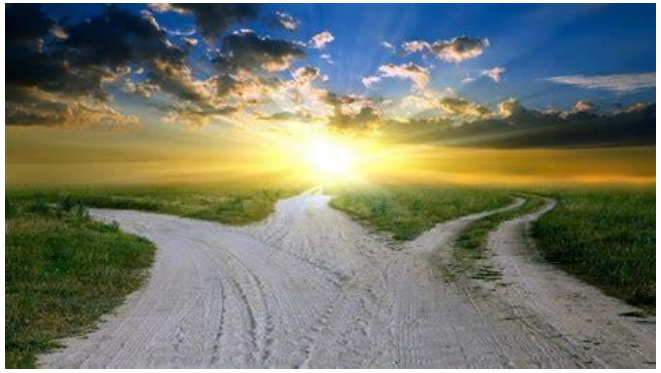
CASE INITIATION IN FEDERAL COURT VERSUS ARBITRATION

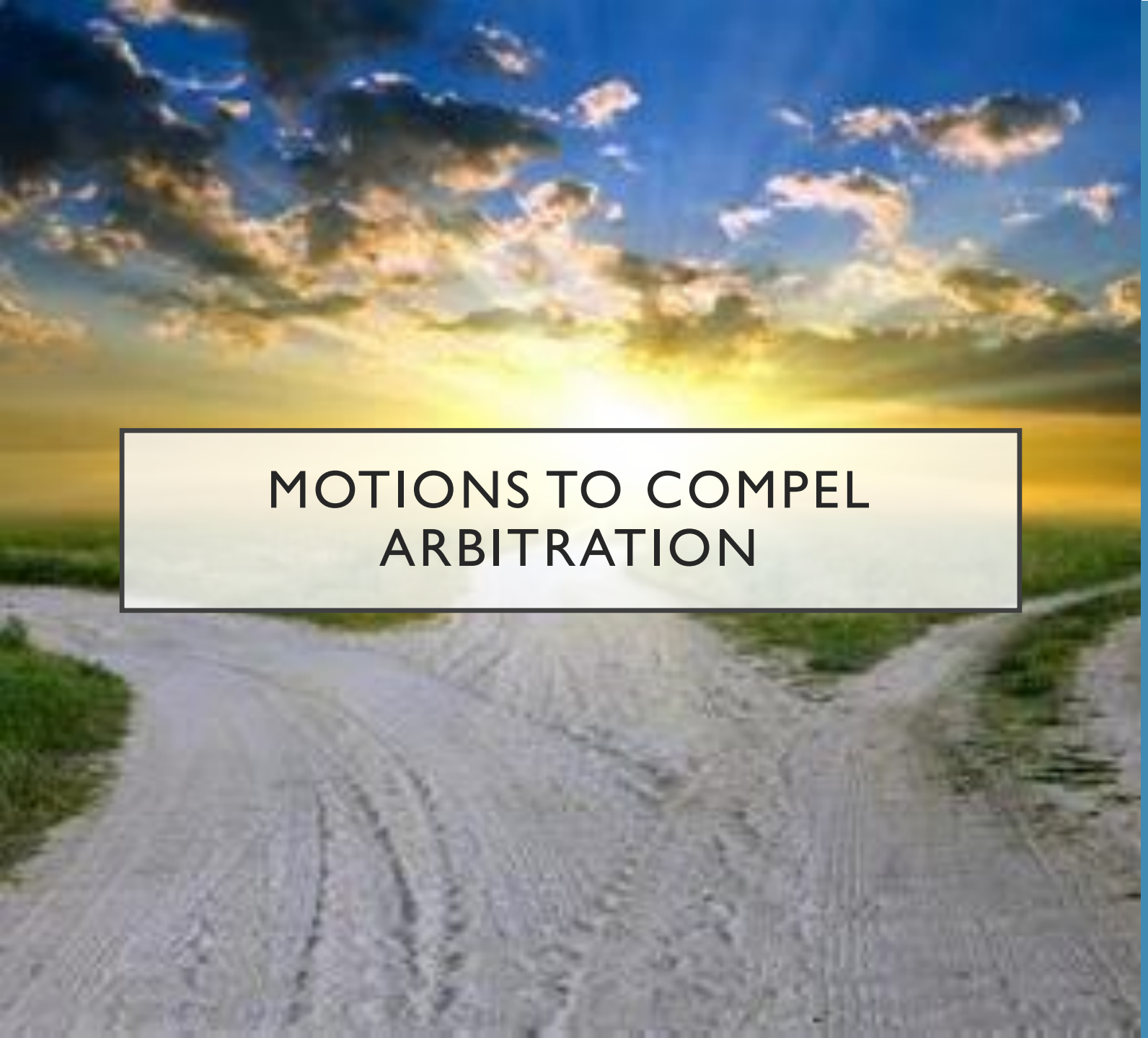
- **Federal Court**: FRCP 3 and 4. (*See also* applicable Local Rules)
- **Arbitration**:
  - Mutual Party Agreement to Contact an Arbitrator/ADR Provider
  - Serving/Filing a Demand for Arbitration with an Arbitrator/ADR Provider

  OR

  - Motion to Compel Arbitration filed in court

    (*See also* applicable contract requirements)





MOTIONS TO COMPEL ARBITRATION

- Do you take your motion to compel to federal or state court?
- Once you get there, do the procedural provisions of the Federal Arbitration Act or the California Arbitration Act apply?

WHY MIGHT IT MATTER?

- **Third-Party Litigation**
  - **CCP § 1281.2(c)**: permits a court to stay arbitration governed by the CAA, pending resolution of related litigation between a party to the arbitration agreement and third parties not bound by it, when "there is a possibility of conflicting rulings on a common issue of law or fact."
- **Waiver of Right to Compel Arbitration**:
  - **FAA**: Prejudice is not a condition of finding waiver. *Morgan v. Sundance, Inc.*, 212 L. Ed. 2d 753, 142 S. Ct. 1708, 1709 (**2022**).
  - **CAA:** prejudice requirement still applies. *Desert Reg'l Med. Ctr., Inc. v. Miller*, No. E076058, 2022 WL 18142878, at *15 (Cal. Ct. App. Dec. 13, 2022) (certified for publication, Jan. 6, 2023).

WHEN MOTIONS TO COMPEL ARBITRATION CAN BE HEARD IN FEDERAL COURT

- The "Look-Through" Test
- *Vaden v. Discovery Bank*, 556 U.S. 49 (2009):

  "[T]he [FAA] is something of an anomaly in the realm of federal legislation: It bestows no federal jurisdiction but rather requires for access to a federal forum an independent jurisdictional basis over the parties' dispute." *Id.* at 59.

  "[A] party seeking to compel arbitration may gain a federal court's assistance only if, 'save for' the agreement, the entire, actual 'controversy between the parties,' as they have framed it, could be litigated in federal court." *Id.* at 66.

LIMITS TO "LOOK-THROUGH"

"The question presented here is whether that same 'look-through' approach to jurisdiction applies to requests to confirm or vacate arbitral awards under the FAA's Sections 9 and 10. We hold it does not. Those sections lack Section 4's distinctive language directing a look-through, on which *Vaden* rested. Without that statutory instruction, a court may look only to the application actually submitted to it in assessing its jurisdiction."

Badgerow v. Walters, 142 S.Ct. 1310 (**2022**)

ANY TAKEAWAYS?

- Just because you can initiate your arbitration matter in federal court doesn't mean you can conclude your matter there.

- Filing and then seeking a stay of a federal matter following a motion to compel arbitration may present a way to ensure you're back in a federal forum after the arbitrator's award issues.
  - . . .Assuming your federal Judge is willing to grant such a stay.
  - . . .And assuming it's worth your client's additional time/expense compared to proceeding straight to arbitration.

THE FEDERAL COURT CAN HEAR THE MOTION TO COMPEL… BUT IS STATE OR FEDERAL LAW THEN APPLIED?

"it does not follow that the FAA prevents the enforcement of agreements to arbitrate under different rules than those set forth in the Act itself . . . . Arbitration under the Act is a matter of consent, not coercion, and parties are generally free to structure their arbitration agreements as they see fit."

Volt Info. Scis., Inc. v. Bd. of Trustees of Leland Stanford Junior Univ., 489 U.S. 468, 475 (1989).

CHOICE OF LAW FOR THRESHOLD ARBITRATION QUESTIONS HEARD BY A FEDERAL COURT

- State rules of contract interpretation apply. *See, e.g.*, *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995).
- Federal courts look for: express evidence of the parties' clear intent that state procedural arbitration law applies in place of or addition to the FAA. *Sovak v. Chugai Pharm. Co.*, 280 F.3d 1266, 1269 (9th Cir.), *opinion amended on denial of reh'g*, 289 F.3d 615 (9th Cir. 2002).
  - A general choice of law provision referencing state law is not enough. *See, e.g.*, *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 62-64 (1995).

BUT COMPARE WITH CHOICE OF LAW IN CALIFORNIA COURTS …

"where, as here, the parties do not '*expressly* designate that any arbitration proceeding should move forward under the FAA's procedural provisions rather than under state procedural law' ([*Cronus Invs., Inc. v. Concierge Servs.*, 35 Cal. 4th 376 (2005)]), California procedures necessarily apply."

Los Angeles Unified Sch. Dist. v. Safety Nat'l Cas. Corp., 13 Cal. App. 5th 471, 482, 220 Cal. Rptr. 3d 546, 553 (2017).

ANY TAKEAWAYS?

- Same contract, different court, different procedural rules likely applied.

"HEARING OFFICER" SELECTION & QUALIFICATIONS IN FEDERAL COURT VERSUS ARBITRATION

- **Federal Court**: "Randomized," with Judge *disqualification* governed by 28 U.S.C. § 455 (and no "peremptory challenges")

- **Arbitration**: Agreement controls or otherwise parties' choice, with Arbitrator *disclosures* required

ARBITRATOR DISCLOSURE REQUIREMENTS FOR FAA VERSUS CAA

- **FAA**:
  - General requirement to disclose "any dealings that might create an impression of possible bias." *Commonwealth Coatings Corp. v. Cont'l Cas. Co.,* 393 U.S. 145, 149, 89 S.Ct. 337, 21 L.Ed.2d 301 (1968),
  - No provisions for automatic disqualification.

- **CAA**:
  - Detailed arbitrator disclosures, per Ethics Standards for Neutral Arbitrators in Contractual Arbitrations.
  - Parties can automatically disqualify an arbitrator within 15 days of receiving their disclosures. (CCP 1281.91(b)(1).)

ARBITRATOR DISCLOSURE CHOICE OF LAW QUESTIONS

- Does the FAA preempt the CAA's disclosure requirements?
- Even if it does, what effect might *Badgerow* have on a California arbitrator's decision regarding the detail/scope to include in his/her disclosures?
- Does uncertainty for parties and arbitrators regarding applicability (or even simply the scope) of California disclosure requirements dissuade the use of arbitration in California?

PLEADING REQUIREMENTS

- **FRCP 8**: "[A] short and plain statement of the claim showing that the pleader is entitled to relief; and [ ] a demand for the relief sought."
- **Arbitration Generally**: Contract requirements and arbitrator philosophies matter.
  - **JW Commercial Rule 4.C.2**: "A statement describing the general nature of the claim or dispute, including its factual basis" and "[t]he relief or remedy(ies) sought."

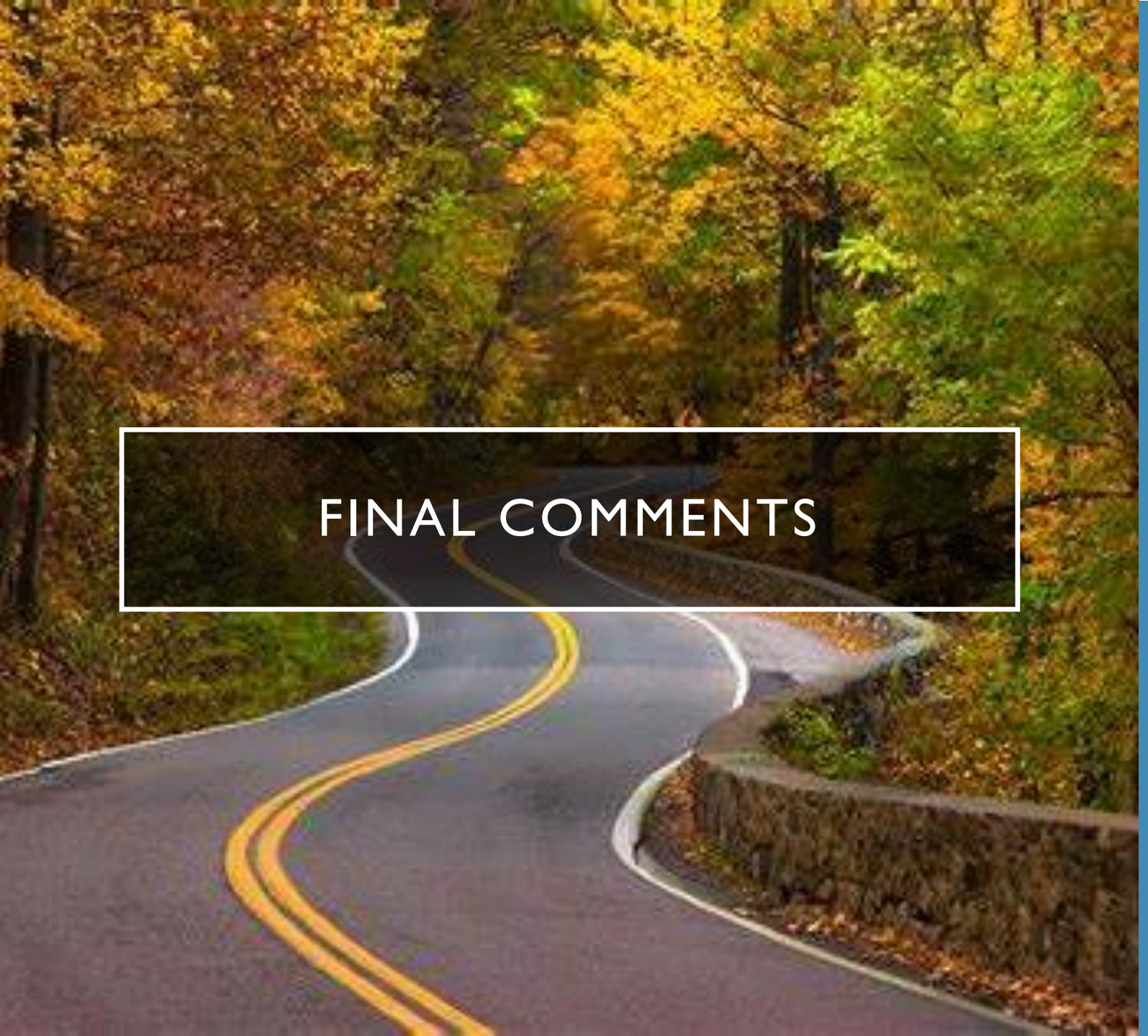
PLEADING CHALLENGES

- ***Twiqbal:***

  To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to "state a claim to relief that is plausible on its face." *Id.,* at 570, 127 S.Ct. 1955. A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged. *Id.,* at 556, 127 S.Ct. 1955. The plausibility standard is not akin to a "probability requirement," but it asks for more than a sheer possibility that a defendant has acted unlawfully. *Ibid.*

  Ashcroft v. Iqbal, 556 U.S. 662, 678, 129 S. Ct. 1937, 1949, 173 L. Ed. 2d 868 (2009) (quoting and citing *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 127 S. Ct. 1955, 167 L. Ed. 2d 929 (2007)).

- **Arbitration**: Federal and state caselaw support an Arbitrator's authority to decide a matter via motion practice, but must (should?) the Arbitrator do so?

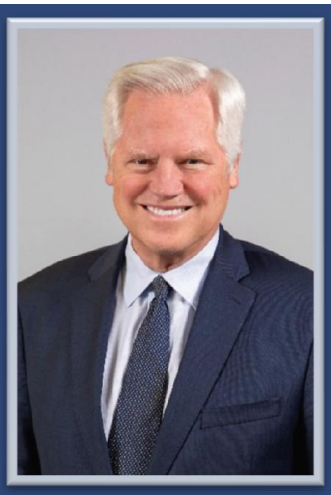


FINAL COMMENTS

- Contract drafting matters.
- But having a crystal ball would help, too.
- Efficiency goals of both federal court and arbitration … Where are we now?

AUDIENCE QUESTIONS?

THANK YOU!



HON. ANDREW J. GUILFORD, RET.

Following nearly 14 years of distinguished service on the bench for the U.S. District Court for the Central District of California, Southern Division, Honorable Andrew Guilford is available as a mediator, arbitrator, and private judge, including special master assignments, and case evaluator.

During his judicial tenure, Judge Guilford sat by designation on the United States Court of Appeals for the Ninth Circuit and is one of only two Central District Judges to have been invited to sit at the United States Court of Appeals for the Federal Circuit. He served as one of the few Patent Pilot Program judges in the Central District. As a federal judge, Guilford heard over a hundred trials, sometimes sitting without a jury, on matters including patent, trademark, copyright, defective products, securities, employment, civil rights, professional liability, class actions, MDL, and of course, criminal matters.

Before his appointment in 2006, Judge Guilford served as an arbitrator and Judge Pro Tem for the Orange County Superior Court, leveraging the experience he gained as a trial lawyer for more than 31 years. At Sheppard, Mullin, Richter & Hampton for his entire career as a lawyer, he tried complex commercial cases across a variety of industries, such as major league sports, medical devices, banking and finance, real property, telecommunications, and entertainment. At a young age, he was elected to the American College of Trial Lawyers.

Judge Guilford's love for the community and passion for giving back is evidenced in his more than four decades and countless hours lecturing and authoring for law schools, religious entities, legal publications, bar associations, and judicial organizations both nationally and internationally. As a trial lawyer and judge, he has received many prestigious awards from various bar associations, including the Orange County Bar Association's Franklin G. West Award—the organization's highest honor, presented to outstanding attorneys and judges whose lifetime achievements have advanced justice and law.

Judge Guilford has earned a reputation for his compassionate, intellectual, fair, intuitive and hardworking demeanor, all qualities he brings to the private sector. One attorney commented: "Judge Guilford always has been prepared, committed and well respected. Following many years of private practice on complex matters and on the bench, he treated lawyers with respect and gave them the opportunity to represent their clients, while achieving justice. He was always actively engaged and personable, and he operated with supreme verve. These attributes certainly will make him highly in demand, as both a private judge and a mediator, and rightly so."

LEGAL CAREER & PRIOR EXPERIENCE

- Mediator, Arbitrator, Private Judge, Judicate West (Present)
- United States District Judge, Central District of California, Southern Division (2006-2020)
- Partner & former Associate, Sheppard, Mullin, Richter & Hampton handling complex commercial litigation with an emphasis on patents, trademarks, finance including securities, banking, real estate, contracts, unfair competition, defamation, civil rights, partnership disputes, professional liability and class actions (1975-2006)

EDUCATION & PROFESSIONAL AFFILIATIONS

- J.D. University of California, Los Angeles; Editor for the UCLA Law Review (1975)
- A.B. University of California, Los Angeles, *summa cum laude*, Regent Scholar, Phi Beta Kappa (1972)
- Dean's Advisory Council, University of California, Irvine, School of Law (Present)
- Board of Visitors, Chapman University School of Law (Present)
- Board of Directors, Federal Bar Association (2001-2020)
- 9th Circuit Jury Instructions Committee (2018-2020)
- Judicial Conference Committee on Codes of Conduct (2011-2017)
- President & Co-Founder, Howard T. Markey Intellectual Property American Inn of Court (2013-2015)
- State Bar Commission on Access to Justice (2008-2013)
- Adjunct Professor, UC Irvine School of Law (2013)
- President, Public Law Center (2004-2006)
- California Supreme Court Advisory Task Force on Multijurisdictional Practice (2001-2003)
- President & Co-Founder, Association of Business Trial Lawyers (ABTL) of Orange County (2000-2001)
- President, District Judges Association (2017-2019)
- President, State Bar of California (1999-2000)
- Fellow, American College of Trial Lawyers (1992)
- President, Orange County Bar Association (OCBA) (1991)

- Chair, Orange County Bar Association Delegation to the Conference of Delegate
- Chair, Orange County Bar Association Business Litigation Section

ADR EXPERIENCE & SPECIALTIES

Business/Contractual, Finance/Securities, Trademark/Copyright, Patents, Real Estate, Civil Rights, Professional Liability, Class Actions, Multidistrict Litigation.

ACHIEVEMENTS & AWARDS

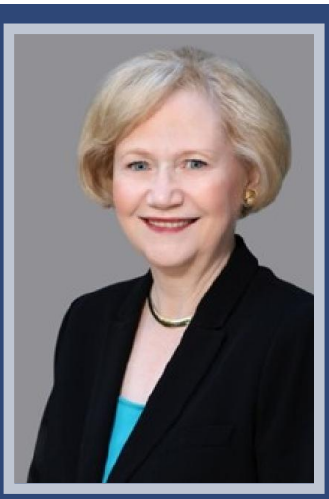
- Speaker, International Symposium on Judicial Enforcement of Intellectual Property, Beijing, China (Jan. 2020)
- Speaker, Best Practices in IP Litigation, Berkeley – Tsinghua Transnational IP Litigation Conference, Berkeley, CA (Oct. 2019)
- Speaker, Best Practices in Patent Litigation, The Sedona Conference, Philadelphia, PA (Mar.2019)
- Recipient, Professionalism Award, American Inns of Court (2018)
- Recipient, Distinguished Public Service Award, Los Angeles Intellectual Property Law Association (LAIPLA) (2016)
- Recipient, Judicial Excellence Award, Orange County Asian American Bar Association (2014)
- Named 5 times by the Daily Journal, "California's Top 100 Attorneys"
- Selected as a "Southern California Super Lawyer (2004-2006)
- Selected as one of 50 "Best Lawyers in Orange County"
- Selected as one of "Best Lawyers in America"
- Recipient, Franklin G. West Award, Orange County Bar Association (2003)
- Recipient, Jurisprudence Award, Anti-Defamation League (2002)
- Recipient, Distinguished Judge Award, Orange County Intellectual Property Law Association
- Recipient, Judge Alicemarie H. Stotler Award, Orange County Federal Bar Association
- Recipient, Judge of the Year Award, Orange County Hispanic Bar Association
- Recipient, J. Reuben Clark Award, J. Reuben Clark Society
- Recipient, Bernard E. Witkin Amicus Curiae Award, Judicial Council
- Named Business Litigation Trial Lawyer of the Year, Orange County Trial Lawyers Association
- Honored by UCI School of Law as a "True Founder of the School of Law"
- Contributing Editor, *Civil Procedure*, The Rutter Group
- Judge Guilford has written articles appearing in many places, including the UCLA Law Review, the Pennsylvania Law Review, the FIU Law Review, the Daily Journal, the California Bar Journal, and the Journal of the Litigation Section.
- A popular speaker, he has been asked to speak on many topics in many places from China to New York. His long list of hundreds of programs goes back to a 1978 CEB program on Civil Litigation, followed by a 1982 program on the leverage of negations, and a 1984 CEB program on negotiating civil settlements.

HOBBIES & INTERESTS

Judge Guilford's interests are varied and include traveling, writing, poetry, photography, theater, and sports, being a fan of UCLA, the Dodgers, Lakers, and Rams, and playing basketball and tennis. Time with his family is most valued, and he is proud of his grandson and two granddaughters.

LOCATIONS

Nationwide



HON. MARGARET M. MORROW, RET.

Following 18 years of distinguished service on the U.S. District Court for the Central District of California bench and five years as President and CEO of Public Counsel, Judge Margaret M. Morrow has retired and is available as a mediator, arbitrator, and private judge, including special master and neutral appellate and trial assignments.

During her judicial tenure, Judge Morrow developed the Central District Court's ADR program, overseeing it for 10 years. She also chaired the court's committee to secure funding for, design, and build a new federal courthouse, which opened in 2016. Before her appointment in 1998, Judge Morrow spent 24 years in private practice, handling a variety of civil trial and appellate litigation matters, mediating cases, and assisting clients with the arbitration process by filing motions to compel, vacate, and confirm. Throughout her career in practice and on the bench, she has been dedicated to finding creative ways to resolve disputes that often cannot be achieved through litigation.

Dedicated to helping ensure access to justice for all and to minimizing the impact of wealth disparities between parties, Judge Morrow most recently served as President and CEO of Public Counsel Law Center, a nonprofit, public-interest law firm that serves low-income communities and individuals.

Judge Morrow's commitment to the administration of justice and the legal community is evidenced by the various roles she played in the Los Angeles County Bar Association and the State Bar of California. She was the first woman president in the State Bar's history and devoted much of her time on the State Bar Board of Governors and in the leadership of the County Bar to improving our court system and increasing access to justice. One of her many accomplishments was sponsorship of a successful ADR Pledge Campaign directed to lawyers, law firms, and businesses statewide. Judge Morrow also helped draft and lobby the original California court mediation statute and was one of the authors of a bench-bar guide on court-related ADR.

With ADR experience at every level of her professional career, Judge Morrow has been praised by bar associations, lawyers and clients for her class, fairness, intelligence, and integrity. One attorney commented: "Margaret is thoughtful, compassionate, extremely bright, and has dealt with lawsuits, disputes and controversies from many angles, including as a talented and successful big law partner and a highly regarded federal judge. She applies rare insight and problem-solving skills to all aspects of her work and will be outstanding in assisting parties in resolving their cases."

LEGAL CAREER & PRIOR EXPERIENCE

- Neutral, Judicate West (2022 - Present)
- President/CEO, Public Counsel Law Center (2016-2021)
- Senior Judge of the United States District Court for the Central of California (2015-2016)
- Judge of the United States District Court for the Central of California: Developed and for 10 years oversaw the court's ADR program and chaired the court's committee to secure funding for, design, and build a new federal courthouse, which opened in 2016 (1998-2015)
- Partner, Arnold & Porter; General civil trial and appellate litigation, including a wide range of civil appeals, corporate and business disputes, and arbitration-related litigation, including motions to compel, vacate and confirm (1996-1998)
- Founding Partner, Quinn, Kully, & Morrow; General civil trial and appellate litigation, head of firm's appellate practice handling a wide range of civil appeals, arbitration-related litigation, including motions to compel, vacate and affirm, insurance coverage, and mediation (1987-1996)
- Partner, Kadison, Pfaelzer, Woodard, Quinn & Rossi; General civil trial and appellate litigation with an emphasis on business and contract disputes, professional malpractice, insurance coverage, and product liability (1974-1987)

EDUCATION & PROFESSIONAL AFFILIATIONS

- J.D., Harvard Law School, cum laude (1971-1974)
- B.A., Bryn Mawr College, magna cum laude (1968-1971)
- Pepperdine/Strauss Institute, 'Mediating the Litigated Case' Training Course (2022)
- American Arbitration Association, Addressing the Challenges of Demanding Arbitrations; Part I, The Pre-Hearing Landscape; Part II, The Hearing Phase, The Award and Beyond (2022)
- State Bar of California, President: Launched a successful ADR Pledge Campaign directed to lawyers, law firms, and businesses throughout California and participated in preparing an ADR primer for California attorneys (1993-1994); Member, Board of Governors: Participated in drafting and lobbying California's original court mediation statute and helped author a bench-bar guide on court-related ADR (1990-1993)
- Los Angeles County Bar Association, President (1988-1989); Oversaw the adoption of Litigation Guidelines governing practice in LA Superior Court and the Central District of California; Barrister's Section, President (1982-1983); Member, Board of Trustees (1981-1989)
- Legal Services Corporation, Member, Rural Legal Task Force (2021-Present); Member, Leadership Council (2021-Present)
- American Academy of Arts and Sciences, Member, Access to Justice Implementation Advisory Committee (2021-Present)
- American Bar Association, Member, House of Delegates (1990-1992); Member, Standing Committee on Legal Aid and Indigent Defendants (1989-1991); Director, Young Lawyers Division (1984-1985)
- Association of Business Trial Lawyers, Member of the Board of Governors (1982-1984, 1998-2000) and Annual Seminar Chair (1984); Seminar Panelist (1991, 1992, 1994)
- Inner City Law Center, Homeless Resources Center Board Member (1991-1992); Constitutional Rights Foundation, Board Member (1995-1999); Public Counsel Board of Directors (1984-1986)

AREAS OF FOCUS

Business Litigation, Civil Appeals, Civil Class Actions, Contract/Commercial, Consumer Class Actions, Employment, Insurance/Bad Faith, Personal Injury, Product Liability, Professional Malpractice, Securities Class Actions, Trademarks/Copyrights/Patents, Trade Secrets

ACHIEVEMENTS & AWARDS

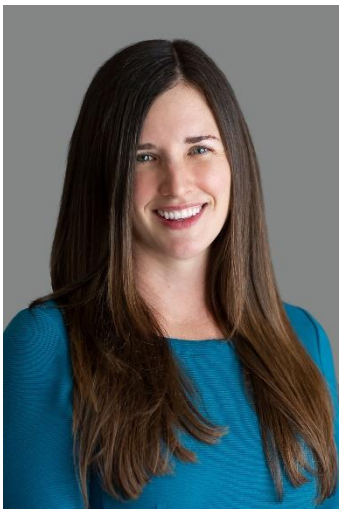
- Beacon of Justice Award, Friends of the L.A County Law Library (2022)
- Public Service Award, National Association of Women Lawyers (2019)
- Jim Robie Award for Professionalism and Civility, Los Angeles County Bar Association Litigation Section (2017)
- Impact Award, Southern California Chinese Lawyers Association (2016)
- Judge of the Year Award, Association of Southern California Defense Counsel (2011)
- Outstanding Jurist Award, Los Angeles County Bar Association (2010)
- Shattuck-Price Award, Los Angeles County Bar Association (1997)
- Bernard E. Witkin Amicus Curiae Award, Judicial Council of California (1995)
- Ernestine Stahlhut Award, Women Lawyers Association of Los Angeles (1994)
- President's Award, California Association of Court-Appointed Special Advocates (1994)
- Pro Bono Advocacy Award, Western Center on Law and Poverty (1992)
- Maynard Toll Award, Legal Aid Foundation of Los Angeles (1990)
- Daniel O'Connell Award, Irish American Bar Association (1989)
- Certificate of Appreciation, Los Angeles County Commission for Women (1988)

HOBBIES & INTERESTS

Margaret actively volunteers in the community. In her free time, she enjoys watching sports, reading, and baking. She loves spending time with her dog and grand dog and hopes to take up, after 20-plus years away, tennis and piano again soon!

LOCATIONS

Nationwide



JUDICATE WEST
Alternative Dispute Resolution
*Results Beyond Dispute*SM

JENNA KELLEHER

Research Attorney & Arbitration Resource Specialist
jennak@judicatewest.com

Jenna Kelleher is a Research Attorney and Arbitration Resource Specialist at Judicate West. She provides legal research and writing support to neutrals on the JW roster, including on matters governed by Federal or California law. She also provides legal guidance to JW and its staff.

Before joining Judicate West, Ms. Kelleher served as the Patent Pilot Program Law Clerk for the Central District of California. During her tenure with C.D. Cal., Ms. Kelleher assisted with patent matters assigned to the Honorable S. James Otero, James V. Selna, Andrew J. Guilford, Philip S. Gutierrez, George H. Wu, John A. Kronstadt, and André Birotte Jr. Ms. Kelleher also previously clerked in the Eastern District of Texas for the Honorable John D. Love, Magistrate Judge. During her four years with the courts, Ms. Kelleher researched, analyzed, and made recommendations on hundreds of law and motion hearings on a broad range of complex substantive and procedural issues.
Ms. Kelleher began her legal career at Knobbe Martens Olson & Bear, where her practice included both intellectual property litigation and patent prosecution.

Ms. Kelleher received her J.D. from the University of California, San Francisco Law (formerly UC Hastings College of Law) and her B.S. in bioengineering from the University of California, Berkeley.

Ms. Kelleher enjoys snow sports, reading, cooking, crafting, spoiling her chocolate lab Blue, and road-tripping across California (with Blue in tow).

Badgerow v. Walters – Answering Vaden's Questions and Limiting Its Application

By KRISTEN BLANKLEY

April 11, 2022

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Introduction

The Supreme Court's decision in *Vaden v. Discover Bank*, 556 U.S. 49 (2009), held that district courts can "look through" a motion to compel arbitration to the underlying case to determine if federal question jurisdiction exists. *Id.* at 70. Following this decision, district courts grappled with federal jurisdiction for other types of arbitration motions. Depending on how broadly the court read *Vaden*, courts split on whether the "look through" doctrine applied in four areas: 1) motions to stay and compel arbitration ("front end motions") in federal question cases (decided by *Vaden*); 2) front end motions in diversity cases; 3) motions to confirm, vacate, or modify arbitration awards ("back end motions") in federal questions cases; and 4) back end motions in diversity cases. *See* Kristen M.

Blankley, *A Uniform Theory of Federal Court Jurisdiction Under the Federal Arbitration Act*, 23 Geo. Mason L. Rev. 525, 554 (2016) (setting forth categories).

By the time the Court decided *Badgerow v. Walters*, __ U.S. __, 2022 WL 959675 (Mar. 31, 2022), lower courts created multiple tests for all of these categories, other than the one *Vaden* answered. While the *Badgerow* case could have clarified and simplified the law, it leaves more questions than it answers.

The Badgerow Decision

In *Badgerow*, Denise Badgerow arbitrated – and lost – a claim of unlawful termination against a firm run by, inter alia, Greg Waters. *Id.* at *3. Following the arbitration, Badgerow filed a motion to vacate in state court. Simultaneously, Waters filed a motion to confirm in federal court. Id. Both the district court and the court of appeals in the vacatur case held that the court had federal question jurisdiction by looking through the Section 9 motion to the federal question decided in the arbitration. *Id.* at **3-4.

The Supreme Court reversed, holding that the "look through" doctrine is only available to courts considering motions to compel under Section 4 of the Federal Arbitration Act (FAA). *Id.* at *5. Justice Kagan, writing for the majority, relies on a highly textualist reading of the FAA to reach this outcome. The majority correctly summarizes *Vaden*, which held that the text of Section 4 confers jurisdiction when the court would have had

jurisdiction "save for" the arbitration agreement. *Id.* However, the majority rejected the possibility of extending *Vaden*'s holding to Sections 9, 10, and 11 of the FAA because those provisions do not contain similar "save for" language. Id. The Court treats the lack of the "save for" language as a deliberative choice on the part of Congress. *Id.* at *6.

The majority opinion rejects the many practical concerns raised from treating jurisdiction differently on front-end motions and back-end motions. The Court, however, finds no reason to create uniform rules on jurisdiction when the textual provisions are different. *Id.* at *8. The Court also rejects concerns that different jurisdictional rules for different motions will cause consternation for the lower courts. *Id.* Finally, the Court surmises that Congress, in 1925, reasonably could have created broader jurisdiction for motions to compel arbitration than motions to confirm or vacate. *Id.*

Ultimately, the Court limits *Vaden* to other cases involving a similar procedural posture, *i.e.*, cases involving "front end" motions. For "back end" motions, no "look through" is available, and the court must find jurisdiction within the four corners of the motion. The Court reserved for another day questions involving jurisdiction on other parts of the FAA that similarly lack "save for" language.

Justice Breyer dissented, and his opinion unsurprisingly relies on a large host of tools of statutory interpretation. He begins by discussing the practical consequences of a system that utilizes different

jurisdictional rules for different motions and the confusion this ruling might give lower courts. *Id.* at *10. He relies on the whole act rule as a reason to treat jurisdictional requirements the same throughout the statute. *Id.* at *11. He questions the application of the majority's rule to FAA Section 5, dealing with the appointment of arbitrators, and FAA Section 7, dealing with arbitrator subpoena power, because neither of these provisions contains a "save for" clause. *Id.* Justice Breyer also considers the potential loss of jurisdiction by a federal court that has jurisdiction over a Section 4 motion prior to the arbitration but lacks a federal question in a motion to confirm or vacate. *Id.* at *12.

Justice Breyer cites precedent holding that Congress intended for the FAA to provide a simple, streamlined process for parties who need assistance from courts on matters relating to arbitration. *Id.* at *13. He noted that simple, uniform jurisdictional rules would meet this purpose, rather than creating a patchwork of jurisdictional rules based on the procedural posture of the case.

Implications and Unanswered Questions

The *Badgerow* holding answers one of *Vaden*'s lingering questions. The Court has now decided that federal court jurisdiction for motions under Section 9 (confirmation) and Section 10 (vacatur) must be evident from the four corners of the motion. In other words, there is no ability to "look through" the motion to support jurisdiction.

The *Badgerow* holding, however, fails to account for other complications arising from *Vaden*. Following *Vaden*, the lower courts split on the jurisdictional test for "front end" motions in diversity cases. The *Badgerow* case discusses generally that the "look through" doctrine is available for Section 4 motions, but the Court does not provide any guidance on amount-in-controversy jurisdiction (which is admittedly outside the question presented).

This opinion raises important unanswered questions regarding jurisdiction over "back end" motions as well. First, the Court's holding suggests that federal courts may *never* have jurisdiction on "back end" motions under federal question jurisdiction. The Court is clear that the underlying substance of the dispute cannot be used to justify federal question jurisdiction. The Court also suggests that these cases will almost always involve questions of enforcement under state law. The majority's decision casts doubt that *any* court has federal question jurisdiction over these petitions.

Second, Justice Breyer questions whether a court having jurisdiction over a motion to compel might lose jurisdiction on a "back end" motion. Prior to *Badgerow*, the courts were assumed to retain jurisdiction over cases involving a motion to compel. In fact, the stay provision in Section 3 suggests that the court's work may not be complete at the time the court compels arbitration. This new holding might lead courts to hold that they lose for

those “back end” motions, even when they properly decided ”front end” issues on these cases.

Third, the majority opinion leaves open the question of determining the amount-in-controversy for “back end” motions. Would a court have jurisdiction to hear a motion to confirm, vacate, or modify a complete defense award (i.e., a $0 award) or other award lower than $75,000? Currently, some lower courts consider the amount *demanded* in the arbitration, but *Badgerow* casts doubt on whether the court can “look through” to the amount originally demanded.

Fourth, the “save for” language only appears in Section 4, and Justice Breyer questions how jurisdiction may lie for motions to appoint an arbitrator and motions to subpoena witnesses. If these motions require jurisdiction from the four corners of the motions, significant questions arise as to whether these motions could ever meet *either* the federal question test or the amount-in-controversy test without looking through to the subject of the arbitration.

Although the majority relies on a simple, textual basis for its opinion and suggests that courts will find the rules in *Vaden* and *Badgerow* easy to implement, significant questions and concerns still remain for lower courts. Time will tell if these concerns are overblown or if wasteful, collateral litigation will follow from these narrow jurisdictional holdings.

Kristen Blankley

Professor Blankley joined the faculty in 2010. She received her B.A. in History and Political Science and graduated summa cum laude from Hiram College, and she received her J.D. from The Ohio State University, Mortiz College of Law, and graduating first in her class. After law school, Professor Blankley served...

What Law Applies to an Agreement to Arbitrate?

By Terry L. Trantina

When asked to resolve a dispute arising out of a contract containing an arbitration provision, the first question a lawyer must answer is what law governs the obligation to arbitrate a dispute. And that answer could — and often does — determine the dispute's outcome.

From experience, lawyers know that most contracts contain a boilerplate choice-of-law clause, so in searching for an answer, most lawyers immediately turn to that term in the parties' agreement. Although this a logical place to start, stopping there can lead to a significant and costly mistake. The mistake many lawyers (and courts) make at that point is to assume that the state law identified in that clause governs all legal issues, including issues involving the arbitration of the parties' disputes.

In fact, just the opposite is almost certainly the case because, with few exceptions, the state law identified in the contract is entirely preempted by the Federal Arbitration Act (FAA) and only the FAA will apply to the arbitration of the disputes arising under or related to the parties' agreement.[1]

In short, the FAA trumps all. The FAA applies to the parties' agreement to arbitrate disputes whether or not it is expressly mentioned in that agreement — and is presumed to preempt the state law selected in a general choice-of-law provision *unless the contract expressly evidences the parties' clear intent that state arbitration law applies* in place of or in addition to the FAA. This has been the applicable law since at least 1995,[2] but few practitioners know or understand the breadth of the FAA.

> "…[W]ith few exceptions, the state law identified in the contract is entirely preempted by the Federal Arbitration Act (FAA) and only the FAA will apply to the arbitration of the disputes arising under or related to the parties' agreement."

Common Assumptions and Mistakes

Three common misunderstandings about the FAA contribute to the mistaken assumption that state law applies. First, many practitioners assume that to be applicable, the FAA must be mentioned in the parties' agreement. But the US Supreme Court made clear in *Mastrobuono v. Shearson Lehman Hutton* that the FAA does not have to be mentioned in the contract or arbitration provision to apply and preempt state law.[3]

Second, under the FAA, the arbitration provision in a contract is treated as a separate agreement of the parties.[4] Therefore, a general choice-of-law provision is not viewed as applying to the agreement to arbitrate disputes (*unless* it expressly states that it does) and state law governs the substantive issues of the remainder of the contract.

Third, many practitioners also assume that the FAA is a procedural, rather than substantive, statute that applies only to transactions that are obviously interstate in nature. As a result, many often assume that the scope of the FAA's applicability (and its preemptive effect) is narrower than it actually is. However, the FAA, first enacted in 1925 and restated in 1947, has been held by the US Supreme Court to be a small body of substantive law that applies to all written agreements to arbitrate disputes evidencing a transaction "involving interstate commerce."[5]

This is far and away the most misunderstood part of the FAA. The scope of the FAA's applicability and preemptive effect is drastically underestimated. The US Supreme Court has held that the "involving commerce" language of Section 2 of the FAA does not mean "in commerce" (which would narrow the FAA's

applicability to activity obviously interstate in nature) but rather that "involving commerce" has the same meaning as "affecting commerce." Therefore, the US Supreme Court, in *Allied-Bruce Terminix Cos. v. Dobson*,[6] found the FAA has the full reach of the US Constitution's Commerce Clause and encompasses a wider range of activity than those "in commerce." The FAA applies to activity "within the flow of interstate commerce."[7]

The FAA's Scope

In *Allied-Bruce*, the Court enforced a consumer contract's arbitration provision in a contract between parties in a state, Alabama, whose statutes banned consumer pre-dispute arbitration provisions, holding that the FAA applied to and enforced a homeowner's obligation to arbitrate a dispute involving a contract to treat a home for insects because Allied-Bruce Terminix purchased the insecticide used to treat the home from an out-of-state source and the interstate sale of insecticide was something Congress could choose to regulate. The Court reached this conclusion in *Allied-Bruce* by finding that the FAA governs any agreement to arbitrate if some economic activity of one of the parties (not necessarily the parties' transaction or the contract itself) has a nexus to interstate commerce.[8]

In *US v. Lopez*,[9] a case striking down a federal statute banning the possession of a gun near a school as not being within Congress's power under the Commerce Clause (decided the same year but after *Allied-Bruce*), the Court summarized all of its prior decisions regarding the scope of the Commerce Clause. There was *dicta* in that case that caused some state courts with reservations about the FAA's applicability and preemptive scope (including the Alabama Supreme Court) to question the continued viability of *Allied-Bruce*.

In 2003, in *Citizens Bank v. Alafabco, Inc., per curium*,[10] the US Supreme Court reiterated the viability of the *Allied-Bruce* decision, holding that neither the parties' agreement nor underlying transaction need be "in" interstate commerce; only the economic activity of the parties involved has to have some nexus to interstate commerce. The Court in *Alafabco* noted that even under any strict analysis, interstate commerce was involved because the parties' agreement was a bank loan, which is clearly a general economic activity subject to federal control as "affecting" interstate commerce.[11] However, the

> "In this day and age, few party relationships giving rise to a contract have no nexus to interstate commerce, and therefore, there are very few agreements to arbitrate that are not governed solely by the FAA, absent an express contractual statement of intent otherwise."

Court in *Alafabco* also made clear that for the FAA to apply and preempt state law, the nexus to interstate commerce need not be substantial, as the *dicta* in *Lopez* might imply. The Court in *Alafabco* found that a loan secured by goods assembled from out-of-state parts and raw materials was a sufficient nexus to interstate commerce for the FAA to apply and preempt Alabama law.[12] In both *Allied-Bruce* and *Alafabco*, the nexus to interstate commerce was not substantial or central to the parties' agreement or relationship.

In this day and age, few party relationships giving rise to a contract have no nexus to interstate commerce, and therefore, there are very few agreements to arbitrate that are not governed solely by the FAA, absent an express contractual statement of intent otherwise.

When State Law Governs

Although the FAA applies generally and broadly, the US Supreme Court has recognized in its *Volt* and *First Options* decisions that the FAA permits the contracting parties to change the arbitration process to suit their needs and that the FAA will enforce those changes if the parties' intent to do so is expressly reflected or incorporated into their agreement. The Court has held that the parties may add portions of a state's arbitration law to the FAA's provisions or opt out of the FAA's provisions entirely.[13] However, the US Supreme Court has also held that a contract's general choice-of-law clause's selection of a particular state's law is an insufficient expression of the intent required to opt out of the FAA or add portions of a state's law to the FAA.[14]

Therefore, a contract's general choice provision selecting a particular state's law to govern the contract as a whole, without more, is not sufficient to trump the applicability of the FAA to the contract's arbitration obligation and preemption of the state law identified in the general choice of law provision.

The scope of the FAA's preemption is itself a very important issue and has been the subject of many court decisions faced with challenges to the applicability of and preemption by the FAA. The FAA has been held to preempt any state constitutional provision, statute, court rule, or decision that is not generally applicable to all contracts. If a state statute, constitutional provision, court ruling, or public policy singles out agreements to arbitrate for special treatment, then it is preempted by the FAA.[15] And even state provisions or rulings that are generally applicable to all contracts are preempted if they serve as an "obstacle to the accomplishment of the FAA's objectives" (i.e., enforcement of the arbitration agreement in accordance with its terms).[16]

The answer to the simple question of what law applies to an agreement to arbitrate is not the simple, contract-specified one that many lawyers might assume, and becoming familiar with the FAA and its body of substantive law is crucial for anyone working in this field who wants to be a skilled, competent practitioner. Until there is clear evidence to the contrary, practitioners will be better off assuming that the FAA, not state law, applies. ■

Endnotes

1 There is an express, but very limited statutory exception to the applicability of the FAA. Section 1 of the FAA, 9 U.S.C. § 1, expressly excludes arbitration agreements involving employment of any class of workers actually employed in foreign or interstate commerce, e.g., railroads, airlines, and telecommunications carriers.

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2 *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 62-64 (1995).

3 *See id.* at 60, n.4 (1995).

4 *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967); *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440 (2006) (affirming *Prima Paint*).

5 *Southland Corp. v. Keating*, 465 U.S. 1 (1984). Note, however, that the FAA does not provide a basis for subject matter jurisdiction, and an alternative basis for jurisdiction, e.g., diversity jurisdiction, is required to maintain an action in Federal Court. *Moses H. Cone Mem. Hosp. v. Mercury Constr. Corp.*, 460 U. S. 1, 26 n.32 (1983) (holding that the FAA applies and can be enforced in both state and federal court).

6 *Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265 (1995).*

7 *Id.* at 273-274 (citing *Perry v. Thomas*, 482 U.S. 483, 490 (1987).

8 *Id.*

9 *U.S. v. Lopez*, 514 U.S. 549 (1995).

10 *Citizens Bank v. Alafabco, Inc.*, 539 U.S. 52, (2003); see also *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, (2001).

11 *Id.* at 58.

12 *Id.* at 57, citing *Katzenbach v. McClung*, 379 U.S. 294, 304-305 (1964); *see also Crawford v. West Jersey Systems*, 847 F. Supp. 1232, 1240 (D.N.J. 1994) (the involving commerce connection is satisfied when the contract has only the smallest nexus with interstate commerce or when contractual activity affects this commerce, even if tangentially).

13 *Volt Information Sciences, Inc. v. Bd of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 479 (1989) (The FAA's central purpose is to ensure that private agreements to arbitrate are enforced according to their terms.); *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995).

14 *Mastrobuono id.* at 62-64 (1995). Some have viewed the US Supreme Court's decision in *Volt* as being inconsistent with *Mastrobuono*, but subsequent decisions, including *Allied-Bruce*, have determined otherwise and explained that in *Volt* the US Supreme Court was simply giving deference to the prior holding of the California Supreme Court as to the contracting parties' intent, a subject that was not before the US Supreme Court. *See R.R Package Sys, Inc. v. Kayser*, 257 F. 3d 287 (3d Cir. 2001).

15 *Perry v. Thomas*, 482 U.S. 483, 492-493 (1987); *Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 687 (1996).

16 *AT&T Mobility LLC v. Concepcion*, 563 U.S. 321, (2011).

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INFORMATIONAL HEARING

The Federal Arbitration Act, the U.S. Supreme Court, and the Impact of Mandatory Arbitration on California Consumers and Employees

A HEARING OF THE SENATE COMMITTEE ON JUDICIARY

March 1, 2016
1:30 p.m.
State Capitol, John L. Burton Hearing Room (Room 4203)

I. WELCOME AND OPENING REMARKS BY CHAIR AND COMMITTEE MEMBERS

II. OVERVIEW OF THE FEDERAL AND CALIFORNIA ARBITRATION ACTS, AND FEDERAL PREEMPTION ISSUES

- Paul Dubow, California Dispute Resolution Council
- Karla Gilbride, Cartwright-Baron Staff Attorney, Public Justice
- Robert A. Olson, Partner, Greines, Martin, Stein & Richland LLP

III. MANDATORY ARBITRATION CLAUSES AND THEIR IMPACT ON CALIFORNIA CONSUMERS AND EMPLOYEES

- Kathryn A. Stebner, Founding Partner, Stebner & Associates
- Alan Carlson, Owner, Italian Colors Restaurant
- Cliff Palefsky, Partner, McGuinn, Hillsman & Palefsky
- Steven Lively, Major, U.S. Army
- Paul W. Cane Jr., Partner, Paul Hastings LLP
- Donald M. Falk, Partner, Mayer Brown

IV. ARBITRATOR ETHICS: ISSUES RELATING TO THE APPEARANCE OF BIAS OR UNFAIRNESS IN ARBITRATIONS

- Heather Anderson, Supervising Attorney, Judicial Council of California
- Cliff Palefsky, Partner, McGuinn, Hillsman & Palefsky
- Jay Welsh, Executive Vice President and General Counsel, JAMS

V. PUBLIC COMMENT PERIOD

VI. CLOSING REMARKS BY CHAIR AND COMMITTEE MEMBERS

AN INFORMATIONAL HEARING OF THE SENATE COMMITTEE ON JUDICIARY

The Federal Arbitration Act, the U.S. Supreme Court, and the Impact of Mandatory Arbitration on California Consumers and Employees

March 1, 2016
1:30 p.m.
State Capitol, John L. Burton Hearing Room (Room 4203)

Section 2 of the Federal Arbitration Act (9 U.S.C. Sec. 2): ***A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.***

Section 1281 of the California Code of Civil Procedure: ***A written agreement to submit to arbitration an existing controversy or a controversy thereafter arising is valid, enforceable and irrevocable, save upon such grounds as exist for the revocation of any contract.***

BACKGROUND PAPER

I. Background

Arbitration is a form of alternative dispute resolution that allows for the resolution of disputes outside of the court system. The Federal Arbitration Act (FAA; 9 U.S.C. Sec. 1 et seq.), enacted in 1925, and the California Arbitration Act (CAA; Code Civ. Proc. Sec. 1280 et seq.), enacted in 1927, both provide that arbitration agreements are valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract. In other words, under federal and California law, arbitration agreements must be enforced, and such enforcement is limited only by certain general contract principles that would apply to any other contract (such as fraud, duress, or unconscionability).

On Tuesday, March 1, 2016, the Senate Judiciary Committee will hold an informational hearing to review the impact of mandatory arbitration clauses arising out of adhesion

contracts[1] on California's consumers, employees, employers, and businesses. The Committee will review the extent to which state action can be taken to address any issues arising out of such clauses, in light of the FAA and foreseeable federal preemption issues based upon the development of case law interpreting that act. Lastly, the Committee will review the efficacy of the ethical rules that were promulgated over the last 15 years to ensure the neutrality of arbitrators. The Committee will explore, among other things, the following questions:

- What is the status of current statutory and case law with regard to the enforceability of mandatory binding arbitration agreements?
- How pervasive is the use of mandatory binding arbitration agreements in the State of California?
- Are mandatory binding arbitration agreements beneficial from the perspective of consumers, employees, employers, and businesses? Why or why not?
- In light of federal preemption hurdles, how might the state be able to protect or improve the integrity of arbitration as an alternative dispute resolution tool?
- How do/how can arbitrators help ensure that people on both sides are treated fairly when involved in an arbitration arising out of a mandatory arbitration clause?
- What redress does a consumer or employee have under existing law if they believe ethical rules have been violated, or that incorrect laws or standards have been applied by the arbitrator in their case?
- What are the current ethical rules that apply to arbitrators and arbitration provider organizations? Are the current ethical rules effective in ensuring fairness and in combatting actual or perceived conflicts of interest?
- Are there ways to improve consumer and employee confidence and enhance the integrity of arbitration as an effective and fair form of alternative dispute resolution?

<u>Arbitration, Generally</u>

As noted above, arbitration is a form of dispute resolution that operates as an alternative to the court system. Alternative dispute resolution (or "ADR") such as arbitration, mediation, or settlement conferences, is said to usually be less formal, less expensive, and less time-consuming. As described on the California courts' website, the benefits of ADR, depending on the process used and the circumstances of the particular case, may include: saving time, saving money, increasing the ability of parties to shape

[1] An adhesion contract is a standard-form contract prepared by one party, to be signed by the party in a weaker position, usually a consumer, who adheres to the contract with little choice of the terms. (Black's Law Dictionary, *Contract of Adhesion* (8th Ed.) p. 342.)

the process and the outcome, preserving relationships (by being less adversarial or hostile), increasing party satisfaction, and improving attorney-client relationships. (*See* California Courts, the Judicial Branch of California, *ADR Types & Benefits*, <http://www.courts.ca.gov/3074.htm#tab4538> [as of Feb. 22, 2016].)

Under California law, there are two distinguishable types of arbitration: judicial arbitration (also known as court-annexed arbitration, governed under Code of Civil Procedure Sections 1141.10 -1141.31) and private arbitrations (also commonly known as "contractual," "voluntary," or "nonjudicial" arbitrations; governed under Code of Civil Procedure Section 1280 et seq.). Contractual arbitration differs markedly from judicial arbitration, as explained by the California Supreme Court, in some very basic ways:

- As to commencement, contractual arbitration arises solely out of an arbitration agreement, specifically, a written arbitration agreement between the parties, whereas judicial arbitration may be imposed upon the parties whether or not they agree in writing or otherwise.
- As to process, contractual arbitration allows the parties to an arbitration agreement to select the arbitrator, whereas judicial arbitration, absent a stipulation, selects the arbitrator by operation of law.
- Contractual arbitration allows the parties to an arbitration agreement to define the arbitrator's powers, whereas judicial arbitration defines the arbitrator's powers by operation of law.
- Contractual arbitration does not permit full and unconditional discovery, whereas judicial arbitration does.
- Contractual arbitration dispenses with any necessity to observe the rules of evidence and procedure, whereas judicial arbitration, although it does make certain modifications, does not.
- Contractual arbitration generally frees the arbitrator from making a decision in accordance with the law, whereas judicial arbitration does not (providing that, in judicial arbitration, the arbitrator has the power "to decide the law and facts of the case and make an award accordingly").
- As to a decision, contractual arbitration generally results in a binding and final decision, whereas judicial arbitration generally does not.

(Toker, California Arbitration and Mediation Practice Guide, Court-Connected ADR, 1.5(a)(1), citing *Mercury Ins. Group v. Superior Court* (1998) 19 Cal.4th 332, 344-345; other internal citations omitted.)

"Contractual" or "Private" Arbitrations

As discussed above, contractual arbitration agreements are often used when one or both sides to the agreement desire to have any disputes arising under the contract arbitrated by private arbitrators, rather than resolved by a court or jury. More frequently, however, it appears that such arbitration clauses are being unilaterally imposed by one party on the other in contracts of adhesion. These mandatory arbitration clauses are usually "binding," which limits the ability of the parties to move their dispute to court if they are unsatisfied with the outcome. As a practical matter, when such "take-it-or-leave-it" contracts are used by companies in the consumer context and the employment context, wherein the parties frequently possess unequal bargaining power, the prospective consumer or employee is left with the choice: to sign or not sign. As a result of that choice, if the consumer or employee does not sign the contract, then they do not get the job, cannot purchase the item, or obtain the services sought.

In recent years, there have been frequent discussions about the merits and benefits of mandatory binding private arbitration as an alternative forum to the civil justice system. Supporters of arbitration may argue that arbitration is a more efficient and less costly manner of resolving legal disputes, especially in light of budgetary cuts to the judiciary branch over recent years. Critics of private arbitration may contend that it is an unregulated industry, which can be costly, unreceptive, and biased against consumers. They may argue that this type of arbitration can create an uneven playing field.

Over the years, consumer and employee advocates have asserted that boilerplate form contracts are problematic because: arbitrators can disregard the law and can issue binding decisions that are legally enforceable but generally not reviewable by a court (*see Moncharsh v. Heily & Blasé* (1992) 3 Cal.4th 1); arbitrators can conduct arbitrations without allowing for discovery, complying with the rules of evidence, or explaining their decisions in written opinions (Code Civ. Proc. Secs. 1283.1, 1282.2, and 1283.4); and arbitrations may be conducted in private with no public scrutiny (*Ting v. AT&T*, 182 F.Supp.2d 902 (N.D. Cal. 2002), affirmed, 319 F.3d 1126 (9th Cir. 2003).)

Critics' concerns are compounded by the fact that there are little, if any, regulations or legal standards imposed on arbitrators or their decisions. Regardless of the level or type of mistake, or even misconduct, by the arbitrator, the grounds on which a court will allow judicial review of an arbitration are extremely narrow. (*See Moncharsh v. Heiley & Blase* (1992) 3 Cal.4th 1 (holding that a court is not permitted to vacate an arbitration award based on errors of law by the arbitrator, except for certain narrow

exceptions).) As a matter of statutory law, the relief that a court may grant to a party to the arbitration is limited to a potential vacatur of the award. If the court vacates the award under any of the circumstances listed in statute, the court may order a rehearing before new arbitrators or, in some cases, order a rehearing before the original arbitrators. (Code Civ. Proc. Sec. 1286.2.[2])

II. Brief Overview of Federal Preemption and Recent Court Cases Interpreting the Federal Arbitration Act

Federal Preemption and the FAA, Generally

The Federal Arbitration Act (FAA) was enacted by the United States Congress in 1925 in response to widespread judicial hostility to arbitration agreements. Section 2 of the FAA, the primary substantive provision of the Act, generally provides that a written provision in any contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract. (*See* 9 U.S.C. Sec. 2; similar language is contained within the California Arbitration Act at Code Civ. Proc. Sec. 1281.)

Separately, as a general matter, Article VI, Paragraph 2 of the United States Constitution—the "Supremacy Clause"—establishes that the federal Constitution, including federal laws made pursuant to it and treaties made under its authority, constitute the supreme law of the land. In other words, states are bound by the "supreme law," and in cases where the federal government has acted pursuant to its constitutional authority and there is a conflict between federal and state law on the same issue, federal law generally takes precedence (i.e., "preempts" state law) and must be applied.

The issue of federal preemption under the Supremacy Clause in the U.S. Constitution is generally both one of *express* preemption (when a federal statute explicitly confirms

[2] Under subdivision (a) of this section, the court is generally required to vacate the award if: (1) the award was procured by corruption, fraud or other undue means; (2) there was corruption in any of the arbitrators; (3) the rights of the party were substantially prejudiced by misconduct of a neutral arbitrator; (4) the arbitrators exceeded their powers and the award cannot be corrected without affecting the merits of the decision upon the controversy submitted; (5) the rights of the party were substantially prejudiced by the refusal of the arbitrators to postpone the hearing upon sufficient cause being shown therefor or by the refusal of the arbitrators to hear evidence material to the controversy or by other conduct of the arbitrators contrary to the provisions of this title; or (6) an arbitrator making the award either: (A) failed to disclose within the time required for disclosure a ground for disqualification of which the arbitrator was then aware; or (B) was subject to disqualification upon grounds specified in Section 1281.91 but failed upon receipt of timely demand to disqualify himself or herself as required by that provision.

Congress's intention to preempt state law) and *implied* preemption (which can arise in two ways: where the federal law is so pervasive as to imply that Congress intended to "occupy the field" in that area of law or where there is a conflict between federal and state law). Recent cases interpreting the FAA have made it increasingly difficult for states, by way of either judicially crafted rules or state legislation, to determine whether the use of private arbitration clauses under certain circumstances are unconscionable or against public policy, or to otherwise address or prevent some of the problems associated with mandatory binding arbitration.

Generally, as the 9th Circuit Court of Appeals recently explained in the 2015 case of *Sakkab v. Luxottica Retail N. Am., Inc*. (2015) 803 F.3d 425, 431-432:

> While "[t]he FAA contains no express pre-emptive provision" and does not "reflect a congressional intent to occupy the entire field of arbitration," [citing *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ*. (1989) 489 U.S. 468, 477] it preempts state law "to the extent that it 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress,'" [citing *id*., quoting *Hines v. Davidowitz* (1941) 312 U.S. 52, 67].
>
> The final clause of [Sec.] 2, [the FAA's] saving clause, "permits agreements to arbitrate to be invalidated by 'generally applicable contract defenses, such as fraud, duress, or unconscionability,' but not by defenses that apply only to arbitration or that derive their meaning from the fact that an agreement to arbitrate is at issue." [Citing *AT&T Mobility v. Concepcion* (2011) 131 S. Ct. 1740, 1746 (internal citations omitted).] Even if a state-law rule is "generally applicable," it is preempted if it conflicts with the FAA's objectives. [Citing *Concepcion*, 131 S. Ct. at 1748.]

The following appendix provides a brief, chronological overview of some recent, significant cases surrounding issues of preemption and the interpretation of the FAA by the U.S. Supreme Court, the California Supreme Court, and the 9th Circuit Federal Court of Appeal. These summaries are only of a select number of cases that are relevant to questions of federal preemption. The appendix provides a snapshot of the general court holdings of oft-cited cases in discussing FAA preemption and is not intended to be comprehensive.

Appendix of Decisions

Armendariz v. Found. Health Psychcare Servs., Inc. (2000) 24 Cal. 4th 83:

The California Supreme Court held that Fair Employment and Housing Act claims would be arbitrable *if* the arbitration permits vindication of the plaintiffs' statutory rights. (*Id*. at 90 (emphasis in original).) The court also held that the agreement at hand possessed a damages limitation that is contrary to public policy, and that it was unconscionably unilateral. (*Id*. at 91.) Finally, the court held that the entire arbitration agreement involved was unenforceable because it was not possible to make the agreement enforceable by severing the offending provisions. (*Id*. at 127.) More generally, the court set forth the standard for finding unconscionability in a contract. As stated by the court, unconscionability requires both "a 'procedural' and a 'substantive' element, the former focusing on 'oppression' or 'surprise' due to unequal bargaining power, the latter on 'overly harsh' or 'one-sided' results," though they need not be present in the same degree. (*Id*. at 114 (internal citations omitted).)

Discover Bank v. Superior Court of Los Angeles (2005) 36 Cal.4th 148:

The California Supreme Court held that when a class action waiver: (1) is found in a consumer contract of adhesion; (2) the dispute between the contracting parties predictably involves small amounts of damages; and (3) it is alleged that the party with the superior bargaining power has carried out a scheme to deliberately cheat large numbers of consumers out of individually small sums of money, then the waiver is unconscionable under California law and should not be enforced because that waiver effectively exempts a party "'from responsibility for [its] own fraud, or willful injury to the person or property of another.'" (*Id*. at 162-163.) This "*Discover Bank* rule" was abrogated in *AT&T Mobility LLC v. Concepcion,* below.

Gentry v. Superior Court (2007) 42 Cal. 4th 443:

The California Supreme Court announced an unconscionability rule that takes into consideration whether individual arbitration is an effective dispute resolution mechanism for employees when directly compared to the advantages of a class action. In considering whether class arbitration waivers in employment arbitration agreements may be enforced, the court concluded that "at least in some cases, the prohibition of classwide relief would undermine the vindication of the employees' unwaivable statutory rights and would pose a serious obstacle to the enforcement of the state's overtime laws. Accordingly, such class arbitration waivers should not be enforced if a trial court determines, based on the factors discussed below, that class arbitration

would be a significantly more effective way of vindicating the rights of affected employees than individual arbitration." (*Id*. at 450.)

In *Iskanian v. CLS Transportation of Los Angeles*, below, however, the California Supreme Court concluded that this ruling in *Gentry* (insofar as it refused to enforce a class waiver in the arbitration agreement) has been abrogated by the U.S. Supreme Court precedent in *AT&T v. Concepcion*, also below.

Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp. (2010) 559 U.S. 662:

The U.S. Supreme Court held that under the FAA, a party may not be compelled to submit class claims to arbitration unless there is a contractual basis for concluding that the party agreed to it. The Court explained that while in certain contexts, it is appropriate to presume that parties who enter into an arbitration agreement implicitly authorize the arbitrator to adopt procedures that are necessary to give effect to the parties' agreement, "[a]n implicit agreement to authorize class-action arbitration, however, is not a term that the arbitrator may infer solely from the fact of the parties' agreement to arbitrate. This is so because class-action arbitration changes the nature of arbitration to such a degree that it cannot be presumed the parties consented to it by simply agreeing to submit their disputes to an arbitrator." (*Id*. at 685.)

AT&T Mobility LLC v. Concepcion (2011) 563 U.S. 333:

The U.S. Supreme Court overruled a lower court decision finding a class waiver in an arbitration agreement unconscionable pursuant to California's *Discover Bank* rule. The Court held that "[r]equiring the availability of classwide arbitration interferes with fundamental attributes of arbitration and thus creates a scheme inconsistent with the FAA." (*Id*. at 344.) The Court held that state laws containing procedures that are inconsistent with the FAA are not valid and, as such, "'because it stands as an obstacle to the accomplishment and execution of the full purpose and objectives of Congress,' California's *Discover Bank* rule is preempted by the FAA." (*Id*. at 352.)

The Court emphasized that the FAA prohibits judicial hostility to arbitration agreements, and that the FAA reflects both a "liberal federal policy favoring arbitration" and the "fundamental principle that arbitration is a matter of contract." (*Id*. at 339, internal citations omitted.) Notably, the Court recognized that, "[s]tates remain free to take steps addressing the concerns that attend contracts of adhesion—for example requiring class-action waiver provisions in adhesive arbitration agreements to be highlighted." (*Id*. at 347, fn. 6.)

Sonic-Calabasas A, Inc. v. Moreno (2011) 51 Cal.4th 659 (*Sonic I*) and *Sonic-Calabasas A, Inc. v. Moreno* (2013) 57 Cal. 4th 1109 (*Sonic II)*:

The California Supreme Court in *Sonic I* held that it is contrary to public policy and unconscionable for an employer to require an employee, as a condition of employment, to waive the right to a Berman hearing (a dispute resolution forum established by the Legislature to assist employees in recovering wages owed). (51 Cal.4th 659, 684, 687.) The court further held that its rule prohibiting waiver of a Berman hearing does not discriminate against arbitration agreements and is therefore not preempted by the FAA. (*Id*. at 695.) The U.S. Supreme Court granted certiorari, vacated the judgment, and remanded the case to the California Supreme Court for consideration in light of *Concepcion*, which clarified the limitations that the FAA imposes on a state's capacity to enforce its rules of unconscionability on parties to arbitration agreements. (*Sonic-Calabasas A, Inc., Petitioner v. Moreno* (2011) 132 S. Ct. 496.)

In *Sonic II*, the California Supreme Court concluded, in light of *Concepcion*, that compelling the parties to undergo a Berman hearing would impose significant delays in the commencement of arbitration and the approach taken in *Sonic I* would be inconsistent with the FAA. As such, the *Sonic II* court held that the FAA preempts California's rule categorically prohibiting waiver of a Berman hearing in a predispute arbitration agreement imposed on an employee as a condition of employment. (57 Cal. 4th 1109, 1124.) At the same time, however, the court concluded that:

> [S]tate courts may continue to enforce unconscionability rules that do not "interfere[ ] with fundamental attributes of arbitration." [Citing *Concepcion*, 563 U.S. 333, 344.] Although a court may not refuse to enforce an arbitration agreement imposed on an employee as a condition of employment simply because it requires the employee to bypass a Berman hearing, such an agreement may be unconscionable if it is otherwise unreasonably one-sided in favor of the employer. As we explained in *Sonic I* and reiterate below, the Berman statutes confer important benefits on wage claimants by lowering the costs of pursuing their claims and by ensuring that they are able to enforce judgments in their favor. There is no reason why an arbitral forum cannot provide these benefits, and an employee's surrender of such benefits does not necessarily make the agreement unconscionable. The fundamental fairness of the bargain, as with all contracts, will depend on what benefits the employee received under the agreement's substantive terms and the totality of circumstances surrounding the formation of the agreement. (*Id*. at 1124-1125.)

Iskanian v. CLS Transportation Los Angeles, LLC (2014) 59 Cal. 4th 348:

The California Supreme Court held that the FAA did not preempt a state rule that bars the waiver of representative claims under the Private Attorneys General Act of 2004 (PAGA), Cal. Lab. Code Sec. 2698 et seq.[3] The court reasoned that the FAA's goal of promoting arbitration as a means of private dispute resolution does not preclude the California Legislature from deputizing employees to prosecute Labor Code violations on the state's behalf, and, as such, the FAA does not preempt a state law that prohibits waiver of PAGA representative actions in an employment contract. (*Id*. at 360.)

Separately, the California Supreme Court held that its 2007 ruling in *Gentry v. Superior Court*, above, insofar as it refused to enforce a term in the arbitration agreement on grounds of public policy and unconscionability, would be preempted by the FAA and had thus been abrogated by the 2011 U.S. Supreme Court's decision in *Concepcion*. (*Id*. at 359-360.)

American Express Co. v. Italian Colors Rest. (2013) 133 S.Ct. 2304:

The U.S. Supreme Court, in an action alleging violations of federal antitrust laws, held that the FAA does not permit courts to invalidate a contractual waiver of class arbitration on the ground that the plaintiff's cost of individually arbitrating a federal statutory claim exceeds the potential recovery. A class action waiver in an arbitration agreement must be enforced, even if the cost of individually arbitrating a federal statutory claim exceeds the potential recovery and renders arbitration economically infeasible. As stated by the Court, "[t]he antitrust laws do not guarantee an affordable procedural path to the vindication of every claim." (*Id*. at 2309.)

The Court rejected the plaintiff's argument that the "effective vindication" exception[4] to the FAA requires the availability of class arbitrations to bring claims, such as antitrust claims:

> The exception finds its origin in the desire to prevent "prospective waiver of a party's *right to pursue* statutory remedies[.]" That would certainly cover a provision in an arbitration agreement forbidding the assertion of certain statutory rights. And

[3] PAGA "authorizes an employee to bring an action for civil penalties on behalf of the state against his or her employer for Labor Code violations committed against the employee and fellow employees, with most of the proceeds of that litigation going to the state."

[4] As first established in the U.S. Supreme Court case of *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc*. (1985) 473 U.S. 614, 637, fn.19, the "effective vindication" exception expresses a judicial willingness to invalidate, on "public policy" grounds, arbitration agreements that "operat[e] . . . as a prospective waiver of a party's right to pursue statutory remedies."

> it would perhaps cover filing and administrative fees attached to arbitration that are so high as to make access to the forum impracticable. [. . .] But the fact that it is not worth the expense involved in proving a statutory remedy does not constitute the elimination of the right to pursue that remedy. [. . .]. (*Id*. at 2310-2311 (internal citations removed).)

Lastly, the Court emphasized that it specifically rejected the argument that class arbitration is necessary to prosecute claims "that might otherwise slip through the legal system" in its *Concepcion* decision. (*Id*. at 2311.)

Sakkab v. Luxottica Retail North America, Inc. (2015) 803 F.3d 425, 427:

The 9th Circuit held that the FAA did not preempt the California rule announced in *Iskanian* (the *Iskanian* rule), above, which bars any waiver of PAGA claims, regardless of whether the waiver appears in an arbitration agreement or a non-arbitration agreement. The court held that, following the logic of *Concepcion*, the *Iskanian* rule is a "generally applicable" contract defense that may be preserved by the FAA's saving clause (*see* 9 U.S.C. Sec. 2), provided that it did not conflict with the FAA's purposes. (*Id*. at 431-432.) To that end, the court further held that the *Iskanian* rule did not conflict with the FAA's purposes because it left parties free to adopt the kinds of informal procedures normally available in arbitration and only prohibited them from opting out of the central feature of the PAGA private enforcement scheme, which is the right to act as a private attorney general to recover the full measure of penalties the state could recover. (*Id*. at 439.)

Sanchez v. Valencia Holding (2015) 61 Cal. 4th 899:

The California Supreme Court held that the anti-waiver provision of the Consumer Legal Remedies Act (CLRA) (s*ee* Civ. Code Secs. 1750-1784), is preempted insofar as it bars class waivers in arbitration agreements covered by the FAA. The Court further determined that the plaintiff's "argument that enforcing the CLRA's anti-waiver provision merely puts arbitration agreements on an equal footing with other contracts is unavailing. *Concepcion* held that a state rule can be preempted not only when it facially discriminates against arbitration but also when it disfavors arbitration as applied." According to the court, "*Concepcion* further held that a state rule invalidating class waivers interferes with arbitration's fundamental attributes of speed and efficiency, and thus disfavors arbitration as a practical matter." (*Id*. at 924 (internal citations omitted).)

DirecTV, Inc. v. Imburgia (2015) 136 S. Ct. 463:

The U.S. Supreme Court, reversing a California Court of Appeal decision, upheld an arbitration provision in a DirecTV service agreement that included a class-arbitration waiver, despite the fact that: (1) the agreement specified that the entire arbitration provision was unenforceable if the "law of [the consumer's] state" made class-arbitration waivers unenforceable[5]; and (2) California law (both at the time that the contract was entered into and the time that the case was initiated) made class arbitration waivers unenforceable under certain circumstances pursuant to the 2005 *Discover Bank* rule, which was not abrogated and held preempted until 2011, nearly three years after the initiation of this case, by *AT&T v. Concepcion*.

The Court stressed that the issue at hand in *DirecTV* was not whether the lower court's decision was a correct statement of California law but, rather, whether it was consistent with the FAA. To that end, the Court held that the California Court of Appeal's interpretation is preempted by the FAA and thus the court must enforce the arbitration agreement. (*Id*. at 471.)

[5] The agreement also otherwise declared that the arbitration clause was governed by the FAA.

Are California's Arbitrator Disclosure Requirements Preempted by the FAA?

BETHANY L. APPLEBY

Many arbitration agreements, such as the Commercial Rules of the American Arbitration Association (AAA) or the JAMS Comprehensive Arbitration Rules, explicitly designate the particular rules that will govern any arbitration that arises. The specified rules generally address what information, if any, a potential arbitrator must disclose during the arbitrator selection process.

One issue that frequently arises in disclosure disputes is past service by a particular arbitrator in earlier proceedings involving one of the parties, particularly where one of the parties is a large corporation or other "repeat player" that has used the arbitrator in multiple proceedings.[1]

California has enacted its own rules that purport to override the parties' agreement to arbitrate with respect to these disclosures and other matters. The consequences for failing to follow California's rules when they apply can be dire because the arbitrator's mere failure to disclose certain information, even if there is no demonstrated bias or prejudice, can result in the vacation of an award. This article examines how California rules change the landscape and why parties may want to tread lightly in California arbitrations (and arbitrations governed by California law) until certain questions are answered by the courts.

AAA and JAMS Rules

Rule 16(a) of the AAA Commercial Rules provides that

> [a]ny person appointed or to be appointed as an arbitrator shall disclose to the AAA any circumstance likely to give rise to justifiable doubt as to the arbitrator's impartiality or independence, including any bias or any financial or personal interest in the result of the arbitration or any past or present relationship with the parties or their representatives. . . ."[2]

AAA Rule 16(c) makes clear that the mere disclosure of information does not mean that the arbitrator should be disqualified: "In order to encourage disclosure by arbitrators, disclosure of information pursuant to . . . Section 16 is not to be construed as an indication that the arbitrator considers that the disclosed circumstance is likely to affect impartiality or independence."[3]

Rule 15(h) of the JAMS Comprehensive Arbitration Rules provides that "[a]ny disclosures regarding the selected Arbitrator shall be made as required by law or within ten (10) calendar days from the date of appointment. The obligation of the Arbitrator to make all required disclosures continues throughout the Arbitration process." The JAMS Arbitrators Ethics Guidelines similarly require arbitrators to "promptly disclose, or cause to be disclosed all matters required by applicable law."[4]

In the author's experience, proposed arbitrators, particularly those who do not regularly practice or serve as arbitrators in California, do not routinely disclose information about all past service.

The California Rules

California is the first state to enact legislation purporting to override the private-provider ethical standards for California arbitrations, including those for preconfirmation disclosure.[5] These California ethics standards (Ethics Standards) were adopted by the California Judicial Council under the authority of the California Code of Civil Procedure section 1281.85 and apply to any person "sitting as a neutral arbitrator pursuant to an arbitration agreement" under most circumstances.[6] The Ethics Standards provide that they generally apply to arbitrations either conducted in California or to which California law applies.[7]

The Ethics Standards include a long list of required disclosures, including the disclosure of information about earlier arbitrations involving one of the parties over which the arbitrator presided as a neutral.[8] Arbitrators are also required to disclose relationships that their family members may have with arbitration participants, which one commentator calls "[p]erhaps the most obvious 'brother's keeper' responsibility that the standards place on arbitrators."[9] The Ethics Standards further provide that the arbitrator "must make a reasonable effort to inform himself or herself of matters that must be disclosed."[10]

Consequences for Failing to Disclose

Parties in proceedings to which the Ethics Standards apply can pay the ultimate price when an arbitrator fails to make the required disclosures: California law now specifically provides that failure to disclose the required information is grounds for vacating an award, regardless of any demonstrated arbitrator prejudice or bias.[11] As one commentator noted, the statutory and Ethics Standards changes "are significant not only because they expand the sphere of necessary disclosure, but also because they create 'California law providing for vacating decisions when arbitrators don't properly disclose.'"[12] This could lead opportunistic parties unhappy with an award to investigate possible minor disclosure violations and then move to vacate the award. Because the applicable statute does not require a party seeking to vacate to demonstrate any harm stemming from nondisclosure, vacation could punish the victor in the arbitration even when he had no knowledge of the violation and did not benefit from it in any way.

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The Federal Arbitration Act

The Federal Arbitration Act (FAA) was enacted in 1925 as "a response to hostility of American courts to the enforcement of arbitration agreements, a judicial disposition inherited from then-longstanding English practice."[13] The FAA provides that:

> A written provision in any maritime transaction of a contract evidencing a transaction involving [interstate][14] commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.[15]

The FAA does not make particular disputes arbitrable as a matter of law but simply provides for nationwide enforcement of arbitration clauses in privately negotiated agreements involving interstate commerce. It holds parties to their bargains and, as such, merely ensures the application of standard contract principles. The FAA therefore preempts statutes that "reincarnate the formerjudicial hostility towards arbitration."[16]

The FAA preempts statutes that "reincarnate the former judicial hostility towards arbitration."

Preemptive federal legislation may seem unnecessary for such a noncontroversial proposition as enforcing parties' private agreements. When the FAA was enacted, however, courts routinely refused to apply traditional contract rules to arbitration provisions. And despite widespread current acceptance of arbitration and the fact that over seventy-five years have passed since the FAA was enacted, parties still encounter judicial resistance to arbitration in state courts and require federal court intervention.[17] Since the FAA was enacted, the U.S. Supreme Court has broadened its applicability and repeatedly held that state law restrictions on arbitration are unenforceable in cases in which the FAA applies except, as noted above, when "grounds exist at law or in equity for the revocation of any contract."[18] Moreover, although the FAA preempts any conflicting state law when it applies, most states have also enacted some form of the Uniform Arbitration Act, which mirrors many of the provisions of the FAA and covers agreements that may not be covered by the FAA.[19]

The FAA also authorizes parties to bring federal court actions to confirm or vacate arbitration awards rendered in arbitrations to which it applies.[20] Under the FAA, an arbitral award can be vacated only in these limited circumstances:

> (1) Where the award was procured by corruption, fraud, or undue means.
>
> (2) Where there was evident partiality or corruption in the arbitrators, or either of them.
>
> (3) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced [or]
>
> (4) Where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.[21]

In order to meet the heavy burden of vacating an arbitration award under the FAA, an "appearance of bias" is generally not enough.[22] Under this standard, mere failure to disclose, without more, should not be grounds for vacating an award, particularly where the disclosures would not have been sufficient to disqualify the arbitrator under the rules applicable to the proceeding.[23]

Ethics Standards Versus the FAA

The inconsistencies between federal law and the Ethics Standards have been, and will likely continue to be, fertile ground for litigation. Furthermore, court holdings have not reconciled these inconsistencies: the few recent court cases dealing with FAA preemption of the Ethics Standards have not reached similar conclusions.

In *Mayo v. Dean Witter Reynolds, Inc.,*[24] an investor sued investment house Morgan Stanley in California state court, claiming that Morgan Stanley had improperly refused to reimburse him for improper withdrawals from his investment account. Morgan Stanley removed the lawsuit to the U.S. District Court for the Northern District of California and then moved to compel arbitration before the New York Stock Exchange, Inc., (NYSE) in accordance with the arbitration provision in the parties' client agreement. The court granted Morgan Stanley's motion to compel arbitration under the FAA and stayed the lawsuit pending arbitration. The investor then demanded arbitration before the NYSE shortly before the Ethics Standards took effect. NYSE arbitrations are governed by the NYSE Arbitration Rules, which have been approved by the Securities and Exchange Commission and which differ from the Ethics Standards. When the Ethics Standards took effect, the NYSE informed the investor that it would not appoint an arbitrator because it was temporarily suspending the assignment of all arbitrators in California. It then amended its rules to require California investors to either waive application of the Ethics Standards or arbitrate outside the state. The investor refused to arbitrate under the amended NYSE rules, claiming that he was entitled to proceed with the arbitration in California before an arbitration panel that complied with the Ethics Standards, and asked the court to excuse him entirely from his obligation to arbitrate. After considering the parties' arguments, the court concluded that both the FAA and the Securities Exchange Act of 1934 preempted the Ethics Standards and denied the investor's motion.

Similarly, in *Credit Suisse First Boston Corp. v. Grunwald,* the Ninth Circuit Court of Appeals held that the Ethics Standards do not apply to National Association of Securities Dealers (NASD) arbitrations because the Securities and Exchange Act of 1934 preempts application of the conflicting state law.[25] Before this ruling, the NASD, like the NYSE, had refused to arbitrate in California unless participants agreed to waive application of the Ethics Standards.[26] Since that ruling, the California

Supreme Court also held, in *Jevne v. Superior Court,* that the Securities and Exchange Act of 1934 preempts California's arbitrator disclosure standards and that the preempted portions of the Ethics Standards are not severable.[27]

Despite the aforementioned rulings, FAA preemption of the Ethics Standards is still an open question in California state courts. Although the *Jevne* court ruled that the Securities and Exchange Act of 1934 preempts the Ethics Standards, it did not address whether the FAA similarly preempts the standards.[28] Furthermore, in October 2005, the California Court of Appeal ruled in *Ovitz v. Schulman*[29] that the Ethics Standards controlled.

In *Ovitz*, an employment dispute arose between a film company and its president. The parties' employment contract required arbitration of disputes before the AAA, and the company eventually demanded arbitration in accordance with that requirement. After many hearing days, the arbitrator entered an award in favor of the company. After the arbitrator's ruling, the AAA faxed a letter to the parties directing their attention to a disclosure from the arbitrator making clear that he was also serving as the arbitrator in another pending AAA arbitration where a party was represented by the film company's lawyers. In the letter, the arbitrator claimed that he believed the AAA would have disclosed the information to the *Ovitz* parties and offered to recuse himself from the other case. After learning of the disclosure (which occurred after she knew that she had lost the arbitration), the employee-president requested the arbitrator's disqualification under the Ethics Standards. The AAA denied the disqualification request, reaffirmed the arbitrator's appointment, and denied a request for reconsideration.

The company then filed a petition to confirm the arbitration award in California Superior Court, which vacated the award at the employee's request. The California Court of Appeal affirmed the trial court's ruling. It held that the arbitrator had violated the disclosure requirements of the Ethics Standards by failing to timely disclose his prior service and that the employee had not forfeited or waived her right to vacate the award.

The court then turned to the company's argument that the FAA preempted the Ethics Standards. The company had argued that, because the FAA permits the vacating of an arbitration award for inadequate disclosure only under certain limited circumstances, the FAA must preempt the Ethics Standards, which "mandate[] the vacating of an arbitration award for any violation of California disclosure obligations, regardless of whether the undisclosed facts" would require vacation under the FAA.[30]

Considerable Debate Among the Circuits

The court noted that there "is considerable debate among the federal circuits" concerning the proper standards for vacating arbitration awards under the FAA for failures to disclose.[31] It then cited California state court precedent for the proposition that "[i]n cases where it applies, the FAA has a 'limited preemptive effect' on state law."[32] The court also cited some of the FAA's procedural provisions applicable to motions to vacate, concluding that language in those provisions "strongly suggests that [those provisions] apply only to federal district courts, not state trial courts" and that "the wording of the relevant sections of the FAA evidences a congressional intent not to preempt state law."[33] The court further concluded that vacating arbitration awards pursuant to the Ethics Standards is not inconsistent with the purpose of the FAA and that "'[n]othing in the legislative reports and debates [concerning the FAA] evidences a congressional intention that postaward and state court litigation rules be preempted so long as the basic policy upholding the enforceability of arbitration agreements remained in full force and effect.'"[34] It also commented that

> [b]y its terms, [the California provision for vacating] does not undermine the enforceability of arbitration agreements. It neither limits the rights of contacting parties to submit disputes to arbitration, nor discourages persons from using arbitration. [It] merely requires the vacating of an award if the arbitrator failed timely to disclose a ground for disqualification of which he is aware. Indeed, because it applies to vacating an arbitration award [the provision] presupposes that the arbitration agreement has been enforced and the arbitration held. If an award is vacated, the result is not a preclusion of further arbitration, but rather a new arbitration held in accordance with the disclosure requirements.[35]

In addition, the court noted that

> the legislative purpose of [the] section . . . like the California disclosure requirements as a whole, does not reflect hostility to arbitration or an attempt to limit the ability to enter arbitration agreements. The California scheme seeks to enhance both the appearance and reality of fairness in arbitration proceedings, thereby instilling public confidence. With increased public confidence, arbitration is more attractive as a means of resolving private disputes. Hence, far from posing an obstacle to implementing the purpose of the FAA, [the] section . . . actually serves that purpose. . . [and] . . . does not violate the letter or spirit of the FAA.[36]

Accordingly, the court concluded that the FAA does not preempt California's standard for vacating based on an arbitrator's failure to disclose, at least in California state court proceedings.[37]

Waiver Not Allowed

In addition, although courts are generally supposed to enforce parties' agreements to arbitrate as written,[38] another California Court of Appeal ruling held that parties cannot waive their statutory rights for disqualification under the California Ethics Standards when they agree to arbitrate under private rules.[39] Therefore, there is potential for real conflict between the Ethics Standards and the rules designated by the parties' arbitration agreement.

There is also the possibility for additional confusion whenever the contractually agreed-upon rules or other administrative standards or guidelines may be read to implicate the Ethics Standards. For example, the AAA's Arbitrator Disclosure Worksheet that the *Ovitz* arbitrator filled out referenced the Ethics Standards, but the AAA rules themselves do not. In addition, the JAMS Arbitrators Ethics Guidelines, cited above, require arbitrators to disclose all matters required by "applicable law." Not only is there a preemption question regarding which applicable law applies for disclosure purposes, but there is also the question of how the failure to disclose might affect the standards for vacating an award and whether the FAA vacation standards apply, regardless of the applicable disclosure standards.

There is also the very substantial potential for an increased risk of a lack of finality in arbitration, as well as the possibility of usurpation of the authority of the administrative bodies to which parties have submitted their disputes. For example, in *Ovitz,* the

California Court of Appeal affirmed the trial court's order vacating the award even though the AAA had denied a disqualification request and reaffirmed the arbitrator's appointment.[40]

Conclusion

Other than the Northern District of California and a California Court of Appeal, which reached opposite conclusions, the courts have yet to determine whether the Ethics Standards apply in arbitrations governed by the FAA. Until the issue is conclusively resolved, parties interested in preserving the finality of arbitral awards may want to consider avoiding proceedings in which the Ethics Standards apply, like the NASD did. This would mean avoiding arbitration in California and outside California where California law applies.[41] When that is not possible, parties (particularly corporate parties whose various departments and subsidiaries may have information about the arbitrator) may want to consider performing due diligence on their own to make sure that arbitrators have made all disclosures that the Ethics Standards purport to require and, where appropriate, submitting their own disclosures about an arbitrator's prior service.

Endnotes

1. *See* Jaimie Kent, *The Debate in California over the Implications of the New Ethical Standards for Arbitrator Disclosure: Are the Changes Valid or Appropriate?*, 17 GEO. J. LEGAL ETHICS 903, 908–09 (2004).

2. The AAA Code of Ethics requires arbitrators to make similar disclosures. AAA Code of Ethics for Arbitrators in Commercial Disputes (2004). *See also* John M. Townsend, *Clash and Convergence on Ethical Issues in International Arbitration*, 36 U. MIAMI INTER-AM. L. REV. 1, 12–16 (Fall 2004).

3. *See* Townsend, *supra* note 2, at 14.

4. JAMS Arbitrators Ethics Guidelines § V, *available at* www.jamsadr.com/arbitration/ethics.asp. According to JAMS, JAMS arbitrators are also required to comply with the American Bar Association's Code of Ethics for Arbitrators in Commercial Disputes, which does not explicitly require disclosure of past service but does note that the code does not "take the place of or supersede" the "arbitration rules to which the parties have agreed, applicable law, or other applicable ethics rules, all of which should be consulted by the arbitrators." *See* www.abanet.org/dispute/commercial_disputes.pdf.

5. *See* Kent, *supra* note 1, at 911–12 & n.66*; see also* Keisha I. Patrick, *A New Era of Disclosure: California Judicial Council Enacts Arbitrator Ethics Standards*, 2003 J. DISP. RESOL. 271, 281 (2003).

6. CAL. CIV. PROC. CODE § 1281.85.

7. CAL. RULES OF CONDUCT app. at div. VI, standard 3 (2002).

8. CAL. RULES OF CONDUCT app. at div. VI, standard 7 (2003); *see also* CAL. CIV. PROC. CODE § 1281.9.

9. Patrick, *supra* note 5, at 294 (discussing Ethics Standard 7, *supra* note 8).

10. CAL. RULES OF CONDUCT app. at div. VI, standard 9.

11. CAL. CIV. PROC. CODE § 1286.2(a)(6).

12. Kent, *supra* note 1, at 913 (quoting *Goin' Cali: Neutrals, Providers Settle in with New Rules and Laws*, 21 ALTERNATIVES HIGH COST LITIG. 1, 17 (2003)).

13. Circuit City v. Adams, 121 S. Ct. 1302, 1307 (2001).

14. The definition of *commerce* in 9 U.S.C. § 1 makes clear that the FAA only applies to commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation or between the District of Columbia and any State or Territory or foreign nation.

15. 9 U.S.C. § 2.

16. David L. Threlkeld & Co. v. Metallgesellschaft Ltd. (London), 923 F.2d 245, 250 (2d Cir. 1991). *See also* Doctor's Assocs., Inc. v. Casarotto, 517 U.S. 681, 687 (1996) (FAA "displaces" conflicting state statutes); Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52, 52–54 (1995) (central purpose of the FAA is to ensure "that private agreements to arbitrate are enforced according to their terms"); Volt Info. Scis., Inc. v. Bd. of Trustees of Leland Stanford Junior Univ., 489 U.S. 468, 474 (1989) (FAA "was designed to overrule the judiciary's longstanding refusal to enforce agreements to arbitrate"); Southland Corp. v. Keating, 465 U.S. 1, 11 (1984) (U.S. Supreme Court sees nothing in the FAA "indicating that the broad principle of enforceability is subject to any additional limitations under state law"); Doctor's Assocs. v. Hamilton, 150 F.3d 157, 162 (2d Cir. 1998) ("recognizing the FAA's strong policy in favor of rigorously enforcing arbitration agreements"). The law firm of Wiggin and Dana LLP, the author's firm, represented Doctor's Associates, Inc., in *Casarotto* and *Hamilton.*

17. *See e.g.,* Doctor's Assocs., Inc. v. Stuart, 85 F.3d 975, 978 (2d Cir. 1996). The law firm of Wiggin and Dana LLP, the author's firm, represented Doctor's Associates, Inc., in *Stuart.*

18. *See, e.g., Southland Corp., supra* note 16; *Casarotto, supra* note 16; Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265, 277 (1995); Do Quijas v. Shearson / Am. Express, Inc., 490 U.S. 477 (1989); Dean Witter Reynolds, Inc. v. Byrd, 470 U.S. 213 (1985). For a discussion of FAA state law preemption, see Christopher R. Drahozal, *Federal Arbitration Act Preemption*, 79 IND. L.J. 393, 409 (Spring 2004).

19. *See e.g.,* Steven K. Huber & E. Wendy Trachte-Huber, *Top Ten Developments in Arbitration in the 1990s,* 55 J. DISP. RESOL. 24, 32 (Jan. 2001).

20. 9 U.S.C. §§ 9–10.

21. 9 U.S.C. § 10.

22. *See, e.g.*, Morelite Constr. Corp. v. N.Y. City Dist. Council Carpenters Benefit Funds, 748 F.2d 79, 80–81, 83–84 (2d Cir. 1984). But see Crow Constr. Co. v. Jeffrey M. Brown Assoc., 264 F. Supp. 2d 217 (E.D. Pa. 2003) (explaining that appearance of bias is enough under some circumstances); Positive Software Solutions, Inc. v. New Century Mortgage Co., 436 F.3d 495 (5th Cir. 2006) (affirming vacation for failure to disclose), *reh'g en banc granted*, No. 04-11432, 2006 WL 1304690 (5th Cir. May 6, 2006).

23. *See* Jason v. Halliburton Co., 2002 WL 31319945, at *5–6 (E.D. La. Oct. 15, 2002) (denying motion to vacate where arbitrator had been selected in prior arbitration involving a party); *see also* Sphere Drake Ins. Ltd. v. All Am. Life Ins. Co., 307 F.3d 617, 621 (7th Cir. 2002), *cert. denied,* 538 U.S. 961 (2003) ("appearance of partiality" ground of disqualification for judges does not apply to arbitrators) (internal quotation omitted); *Morelite Constr. Corp.,* 748 F.2d at 83 ("[i]t comes as no surprise . . . that the standards for disqualification of arbitrators have been held to be less stringent than those for federal judges"); Washburn v. McManus, 895 F.Supp. 392, 399 (D. Conn. 1994) ("mere fact of prior relationship is not in and of itself sufficient to disqualify. . . . The relationship . . . must be so intimate–personally, socially, professionally, or financially–as to cast serious doubt on the arbitrator's impartiality") (internal quotations omitted); Fed. Vending, Inc. v. Steak & Ale of Fla., Inc., 71 F.Supp.2d 1245, 1250 n.2 (S.D. Fla. 1999) (noting AAA's refusal to disqualify arbitrator for past service).

24. 258 F. Supp. 2d 1097, *amended by* 260 F. Supp. 2d 979 (N.D. Cal. 2003).

25. 400 F.3d 1119 (2005).

26. *Id.*

27. 28 Cal. Rptr. 3d 685 (Cal. 2005).

28. *Id.* at 690.

29. 35 Cal. Rptr. 3d 117 (Cal. App. 2005).

30. *Id*. at 131.

31. *Id*. at 132.

32. *Id*. at 132 (quoting Hedges v. Carrigan*,* 11 Cal. Rptr. 3d 787 (2004)).

33. *Id*. at 133.

34. *Id*. at 134 (quoting Siegel v. Prudential Ins. Co., 79 Cal. Rptr. 2d 726 (1998)).

35. *Id*. at 134.

36. *Id*. at 134–35.

37. The court also held that application of the Ethics Standards for vacating for failure to disclose was not inconsistent with the parties' arbitration agreement. *Id*. at 135–36.

38. *See* 9 U.S.C. § 4; Dean Witter Reynolds, Inc. v. Byrd, 470 U.S. 213, 221 (1985).\

39. Azteca Constr., Inc. v. ADR Consulting, Inc., 18 Cal. Rptr. 3d 142, 151 (Cal. App. 2004).

40. It is interesting to note, as discussed above, that the disclosure form that the AAA provided to the arbitrator in *Ovitz* specifically referenced the Ethics Standards, but the AAA determined that the arbitrator should not be disqualified for failure to disclose.

41. The Ethics Standards purport to apply not just to arbitrations taking place in California, but also to arbitrations under California law. Ethics Standard 3. The courts have not yet addressed the extraterritorial application of the Ethics Standards.