

ValpoScholar

Valparaíso University Law Review

Volume 47
Number 4 Summer 2013

pp.83-109

Summer 2013

The Arbitration Seesaw: Federal Act Preempts General Law Thereby Restricting Judicial Review

Tanya M. Marcum

Elizabeth A. Campbell

Follow this and additional works at: <https://scholar.valpo.edu/vulr>

 Part of the [Law Commons](#)

Recommended Citation

Tanya M. Marcum and Elizabeth A. Campbell, *The Arbitration Seesaw: Federal Act Preempts General Law Thereby Restricting Judicial Review*, 47 Val. U. L. Rev. 83 (2013).

Available at: <https://scholar.valpo.edu/vulr/vol47/iss4/6>

This Article is brought to you for free and open access by the Valparaíso University Law School at ValpoScholar. It has been accepted for inclusion in Valparaíso University Law Review by an authorized administrator of ValpoScholar. For more information, please contact a ValpoScholar staff member at scholar@valpo.edu.



Articles

THE ARBITRATION SEESAW: FEDERAL ACT PREEMPTS GENERAL LAW THEREBY RESTRICTING JUDICIAL REVIEW

Tanya M. Marcum* and Elizabeth A. Campbell**

I. INTRODUCTION

Within the past three decades, the U.S. Supreme Court has teetered from its position that “the purpose of Congress in 1925 [for enacting the Federal Arbitration Act] was to make arbitration agreements as enforceable as other contracts, but not more so,”¹ and, through judicial interpretation, it has tottered to a position whereby “the Court has abandoned all pretense of ascertaining congressional intent with respect to the Federal Arbitration Act, building instead, case by case, an edifice of its own creation.”² Consequently, arbitration contracts, once subject to review under the common law doctrines of unconscionability and public policy as applied to all contracts,³ now appear exempt from such review and are enforceable absent such legal concerns.⁴ This results in the proposition that all contracts are equal, but some contracts are more

* Associate Professor, Foster College of Business Administration, Entrepreneurship, Technology and Law Department, Bradley University.

** Professor, College of Business Administration, Department of Finance & Law, Central Michigan University.

¹ *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404 n.12 (1967). The Court went on to say that “[t]o immunize an arbitration agreement from judicial challenge on the ground of fraud in the inducement would be to elevate it over other forms of contract—a situation inconsistent with the ‘saving clause.’” *Id.*

² *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 283 (1995) (O’Connor, J., concurring) (citation omitted).

³ The Federal Arbitration Act, 9 U.S.C. §§ 1-16 (2006). Section 2 allows the courts to determine the enforceability of arbitration agreements “upon such grounds as exist at law or in equity for the revocation of any contract.” *Id.* § 2.

⁴ See Thomas J. Stipanowich, *The Third Arbitration Trilogy: Stolt-Nielsen, Rent-A-Center, Concepcion and the Future of American Arbitration*, 22 AM. REV. INT’L ARB. 323, 327 (2012) (“[P]ro-arbitration federal policy circumscribes judicial authority to police arbitration agreements under state law.”); Thomas Stipanowich, *The Third Arbitration Trilogy: Revelation, Reaction and Reflection on the Direction of American Arbitration*, SCOTUSBLOG (Sept. 21, 2011, 8:36 AM), <http://www.scotusblog.com/2011/09/the-third-arbitration-trilogy-revelation-reaction-and-reflection-on-the-direction-of-american-arbitration/> [hereinafter *Revelation, Reaction and Reflection*] (“[P]ro-arbitration federal policy trumps state law affecting arbitration agreements . . .”).

966 VALPARAISO UNIVERSITY LAW REVIEW [Vol. 47]

equal than others.⁵ The seesaw in jurisprudence is both applauded and criticized for the economic and social consequences it either affords or denies, depending on varying viewpoints.

The shift in positions occurred incrementally and seemingly culminated in the recent decision *AT&T Mobility LLC v. Concepcion*, where the Court held that nothing in the Federal Arbitration Act of 1925 ("FAA") "suggests an intent to preserve state-law rules that stand as an obstacle to the accomplishment of the FAA's objectives."⁶ This decision suggests that the FAA preempts general law doctrines, which prohibit traditional common law defenses previously relied upon to invalidate arbitration clauses. The end result of the *AT&T Mobility* holding is that pre-dispute arbitration agreements—often referred to as adhesion contracts⁷—will be enforced without the safeguards of general law defenses against enforcement, no matter the language in the contract or disparity in bargaining positions. Scholars agree that the implications of *AT&T Mobility* are far-reaching, as it will be applicable to a myriad of consumer and employment contracts.⁸ Furthermore, the High Court

⁵ Cf. GEORGE ORWELL, *ANIMAL FARM* 118 (1945) ("All animals are equal but some animals are more equal than others.").

⁶ See *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1748 (2011) (holding that state law may not be used to invalidate a pre-dispute arbitration agreement that prohibited class action lawsuits).

⁷ Matthew Parrott, Note, *Is Compulsory Court-Annexed Medical Malpractice Arbitration Constitutional? How the Debate Reflects a Trend Towards Compulsion in Alternative Dispute Resolution*, 75 *FORDHAM L. REV.* 2685, 2697 (2007).

Adhesion contracts are not defined by their subject matter, but rather by the relationship of power between the contracting parties. Adhesion contracts allow the powerful party—i.e., the drafting party—"to legislate in a substantially authoritarian manner." This notion of legislating is not in any sense figurative. It dramatizes the point that the drafter has the power to create new and different 'law' to govern the relations and disputes between itself and the adherer."

Id. (footnotes omitted). "An adhesion contract is 'a privately created document drafted by the dominant party to a legal relationship and imposed on the adherent without opportunity for negotiation or change.'" *Id.* at n.97 (quoting Stephan Landsman, *ADR and the Cost of Compulsion*, 57 *STAN. L. REV.* 1593, 1596 (2005)).

⁸ See *Revelation, Reaction and Reflection*, *supra* note 4 (discussing the far-reaching effects of the Court's decision on consumers and employers); see also Press Release, Gibson Vance, AAJ Response to *AT&T Mobility v. Concepcion* SCOTUS Decision, (Apr. 27, 2011), available at <http://www.justice.org/cps/rde/justice/hs.xml/15220.htm> (stating the negative effects the decision will have on consumers). According to Vance, the *AT&T Mobility Concepcion* decision will permit massive corporate wrongdoing, because smaller claims will likely go unheard when the damages amount is too small to justify an individual claim and class action suits are not allowed. *Id.* See generally Jean R. Sternlight & Elizabeth J. Jensen, *Using Arbitration to Eliminate Consumer Class Actions: Efficient Business Practice or Unconscionable Abuse?*, *LAW & CONTEMP. PROBS.*, Winter & Spring 2004, at 75 (2004) (examining the public policy reasons for and against eliminating consumer class action suits against unfair business practices). Arbitration can be found in a variety of contexts including American

continues to re-enforce its previously established position that where an arbitration agreement exists, it must be implemented even where statutory violations are alleged.⁹

This Article explores the current uncertainty in valid review of arbitration agreements and the unsettling trend by the U.S. Supreme Court to restrict the use of general law in such a review. In doing so, this Article discusses the judicial justifications for supporting arbitration, the inconsistency in court cases' holdings, and the historical validity of arbitration clauses.¹⁰ This Article also addresses the problem with judicial review in private arbitration, the consequences of recent court holdings, and the potential conflict between the language of the FAA and general law.¹¹

II. RATIONALE FOR THE JUDICIAL SHIFT TO ARBITRATION

Due to the use of private arbitration by disputants, the actual number of civil lawsuits has decreased in recent years.¹² Instead of appointed or elected judges deciding the outcome of civil disputes, private arbitrators now resolve private conflicts and make private arbitration awards. Various economic and social reasons have been put forth to explain this shift by the courts. The following section discusses the economic, social, and constitutional reasons why the court shifted from a historically hostile attitude towards arbitration to one that embraces private arbitration.

sports. See, e.g., Michael L. Meyer, Note, *If Nobody Picks up the Ball, Is It Really a Fumble, or Is It a Forfeit? The NFL Players Association Request for Legislative Changes to the Labor-Management Relations Act of 1947*, 43 VAL. U. L. REV. 1375, 1396 n.105, 1409 n.176, 1410 n.177 (2009) (discussing the role of arbitration as provided in the *NFLPA White Paper* with regards to retired player benefits); Joshua A. Reece, Note, *Throwing the Red Flag on the Commissioner: How Independent Arbitrators Can Fit into the NFL's Off-Field Discipline Procedures Under the NFL Collective Bargaining Agreement*, 45 VAL. U. L. REV. 359 (2010) (arguing that arbitration can be used in the sports context to preserve player's rights when punished for improper off-the-field conduct).

⁹ See *CompuCredit Corp. v. Greenwood*, 132 S. Ct 665, 673 (2012) (holding that alleged violations of the Credit Repair Organizations Act, 15 U.S.C. § 1679c(a), must be submitted to arbitration as agreed by the consumer in the credit card agreement).

¹⁰ See *infra* Parts II, III, IV (discussing the benefits and consequences of arbitration, current irregularities in court holdings, and the historical approach to arbitration clauses).

¹¹ See *infra* Parts V, VI, VII (explaining the problems concerning judicial review of private arbitration, the effects of recent court cases, and potential issues in the language of the FAA).

¹² Stacey Keare, *Reducing the Cost of Civil Litigation*, PUB. LAW RESEARCH INST., <http://gov.uchastings.edu/public-law/docs/plri/adr.pdf> (last visited May 16, 2013).

968 VALPARAISO UNIVERSITY LAW REVIEW [Vol. 47]

A. *Economic and Social Justifications for Arbitration*

Some have suggested that the privatization of civil disputes through arbitration likely saves money for the judiciary. In contrast, any legislatively imposed anti-arbitration limitation would create an increased burden on the courts and a heightened cost to taxpayers who subsidize the judiciary.¹³ Budget information from various states reflects a court's savings for every civil case that goes to arbitration rather than litigation. Costs range from roughly \$1,500 per case in Colorado to \$3,000 per case in New Jersey,¹⁴ which demonstrates that the total cost of civil litigation is greatly reduced through the use of private arbitration. Therefore, at a time when judicial budgets have been cut, any reduction or prohibition on arbitration would result in a need for more judges, courtrooms, staffing, wages, and other related expenses.¹⁵

¹³ Mark Fellows, *Limits on Arbitration Would Burden Courts and Taxpayers*, METRO. CORP. COUNSEL, Dec. 2007, at 8, 8, available at www.metrocorpcounsel.com/pdf/2007/December/08.pdf.

¹⁴ *Id.* But see Richard H.C. Clay & J. Tanner Watkins, *Methods for Cost-Efficient Resolution in Arbitrations*, FOR THE DEFENSE, Aug. 2010, at 36, 36–41 (2010) (explaining the costs that are associated with arbitration). Arbitration costs typically include administrative costs, arbitrators' fees, and litigation-related costs, like attorneys' fees. *Id.* at 37. The arbitrator's fee depends on the arbitrator's hourly rate and the time it takes to arbitrate. *Id.* Costs for commercial arbitrators range from \$600 to \$5,000 per day. *Id.*; see Christopher R. Drahozal, *Arbitration Costs and Forum Accessibility: Empirical Evidence*, 41 U. MICH. J.L. REFORM 813, 820 tbl.2 (2008) (synthesizing data on arbitrator fees from Chicago, Colorado, Ohio, and Indiana).

¹⁵ See generally Andrew Kloster, *Why Congress and the Courts Must Respect Citizens' Rights to Arbitration*, BACKGROUNDER (Heritage Found., Washington D.C.), Mar. 27, 2013, http://s3.amazonaws.com/thf_media/2013/pdf/bg2784.pdf (arguing in favor of arbitration in order to administer quick and affordable solutions for the business community). But see The Arbitration Fairness Act of 2009, H.R. 1020, 111th Cong. (2009) (arguing that certain limitations be placed on arbitration). This bill was introduced again in Congress on May 12, 2011, by Minnesota Senator Al Franken. See Arbitration Fairness Act of 2011, S. 987, 112th Cong. (2011). If enacted, this Act would amend the FAA to prevent the use and enforceability of pre-dispute arbitration agreements in all consumer and employment contracts. *Id.* In proposing this Act, Congress stated the following:

(1) The Federal Arbitration Act . . . was intended to apply to disputes between commercial entities of generally similar sophistication and bargaining power.

(2) A series of decisions by the Supreme Court of the United States have changed the meaning of the Act so that it now extends to consumer disputes and employment disputes.

(3) Most consumers and employees have little or no meaningful choice whether to submit their claims to arbitration. Often, consumers and employees are not even aware that they have given up their rights.

Private arbitration is a way for the judiciary to be relieved of some of these expenses. Attorney Mark Fellows has reiterated this point and offers the following support for his argument:

Armed with this information, we can begin to view the current crop of anti-arbitration legislation in a new light. Arbitration opponents argue their case as if the public court system is a cost-free resource available at unlimited capacity. In reality, any legislative restrictions on contractual arbitration will necessarily produce an increased burden on the court system that will require increased budget allocations to the judiciary. Legislators and policymakers considering measures that would hinder private arbitration need to understand—and account for—their significant fiscal impact.¹⁶

Additional studies have reached similar results, finding it to be “incontestable that private [alternative dispute resolution] has saved the court system money by preventing a number of disputes from entering the court system altogether.”¹⁷ The California Court’s Administrative Office has estimated a savings of over a half million dollars within a year earned from the reduced number of court days per case.¹⁸

In addition, economically speaking, arbitration provides a savings to businesses that then passes to the consumer. The reasoning is that

[t]he cost savings of arbitration accrue not only to the parties but also to the marketplace because the business’s costs savings are ultimately passed on to the consumer in the form of reduced prices or to the employee in the form of increased wages. The debate

(4) Mandatory arbitration undermines the development of public law because there is inadequate transparency and inadequate judicial review of arbitrators’ decisions.

(5) Arbitration can be an acceptable alternative when consent to the arbitration is truly voluntary, and occurs after the dispute arises.

Id. § 2. This bill died in committee.

¹⁶ Fellows, *supra* note 13.

¹⁷ Keare, *supra* note 12, at 6. In a study by the Administrative Office of the Courts, arbitration was estimated to save litigants about \$957 per case, totaling an estimated \$300,000. *Id.* at 3. A consumer survey from 2005 found that about fifty-one percent of 609 adults participating in arbitration believe it to be cheaper than litigation. Sarah Rudolph Cole & Theodore H. Frank, *The Current State of Consumer Arbitration*, DISP. RESOL. MAG., Fall 2008, at 30, 33.

¹⁸ Keare, *supra* note 12, at 3.

970 VALPARAISO UNIVERSITY LAW REVIEW [Vol. 47]

over arbitration usually fails to account for these indirect benefits. It is important to point out that these indirect benefits are contingent on the enforceability of pre-dispute agreements to arbitrate because it is assent to a pre-dispute arbitration agreement that lowers overall dispute resolution costs and thus enables businesses to offer lower prices and higher wages.¹⁹

But, consumers criticize the shift away from judicial resolution to private resolution of civil disputes. Gibson Vance, the President of the American Association for Justice, stated that, by virtue of the shift,

[t]he Supreme Court has allowed major corporations to grant themselves immunity when they cheat consumers or employees. This decision leaves Americans with practically no recourse to challenge corporate wrongdoing and gives corporations a blueprint to draft forced arbitration clauses to avoid accountability for a wide range of unfair or illegal practices.²⁰

As a result, every lawyer will now advise business entities to utilize arbitration agreements containing class action waivers,²¹ which theoretically would allow an overall contract breach with impunity when individual consumer losses are too small for individual arbitration claims.²² Small recoveries do not encourage an individual to bring a sole action, and, as a result,

putative defendants can engage in low stakes frauds and law violations with impunity and, if the number of occurrences is large enough, quite profitably. Not

¹⁹ Fellows, *supra* note 13.

²⁰ Vance, *supra* note 8.

²¹ Professor Paul F. Kirgis of St. John's University School of Law has stated, "I would submit that any attorney who does not now advise her business clients to put arbitration agreements in all consumer contracts risks a finding of legal malpractice." Kimberly A. Kralowec, *Blogsphere Commentary on AT&T Mobility v. Concepcion*, THE UCL PRACTITIONER (May 2, 2011, 5:00 AM), <http://www.uclpractitioner.com/2011/05/blogsphere-commentary-on-att-mobility-v-concepcion.html>.

²² See *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1761 (2011) (Breyer, J., joined by Ginsburg, Sotomayor & Kagan, J.J., dissenting) ("What rational lawyer would have signed on to represent the Concepcions in litigation for the possibility of fees stemming from a \$30.22 claim?"); see also, e.g., *Carnegie v. Household Int'l, Inc.*, 376 F.3d 656, 661 (7th Cir. 2004) ("The realistic alternative to a class action is not 17 million individual suits, but zero individual suits, as only a lunatic or a fanatic sues for \$30.").

surprisingly, it has been an open secret for over a decade that a major motivation—“perhaps *the* dominant motivation”—for the imposition of arbitration clauses in adhesion contracts has been the hope that these clauses would blossom into class action waivers.²³

Another explanation for the judiciary’s shift from being historically hostile towards arbitration to embracing private arbitration is that jury awards are sometimes astronomical, leading to cries for legislative enactment of tort reform. Such proposed statutes seek to limit the award of certain types of damages, particularly those of a punitive nature.²⁴ Calls for legislative reforms are often defeated through the lobbying efforts of the American Trial Lawyers Association; as such, the judiciary has taken up the sword and banner, accomplishing reform by encouraging and supporting arbitration agreements.²⁵ These agreements contain contract language that achieves the same reform objectives.²⁶

²³ David S. Schwartz, *Do-It-Yourself Tort Reform: How the Supreme Court Quietly Killed the Class Action*, SCOTUSBLOG (Sept. 16, 2011, 10:52 AM), <http://www.scotusblog.com/2011/09/do-it-yourself-tort-reform-how-the-supreme-court-quietly-killed-the-class-action/>.

²⁴ See, e.g., *Punitive Damages Reform*, AM. TORT REFORM ASS’N, <http://www.atra.org/issues/punitive-damages-reform> (last visited May 16, 2013) (illustrating state-by-state examples of limitations on punitive damages and exhibiting support for the limitation of punitive damages).

²⁵ David S. Schwartz, *The Federal Arbitration Act and the Power of Congress over State Courts*, 83 OR. L. REV. 541, 564 (2004) (noting that the “enforce[d] as written” approach by the U.S. Supreme Court has essentially allowed for tort reform). Schwartz explains that under this “enforce[d] as written” approach, the drafting party creates an arbitration agreement with the opposing party, which typically conflicts with state contract regulations. *Id.* Because the arbitration clause is part of a federal mandate that is enforceable under the FAA, the conflicting state contract law is then preempted and the arbitration agreement is enforced. *Id.* Courts, in some cases, have expanded the ability of arbitrators to hear punitive damage claims. Stephen J. Ware, *Punitive Damages in Arbitration: Contracting out of Government’s Role in Punishment and Federal Preemption of State Law*, 63 FORDHAM L. REV. 529, 529 (1994); see, e.g., *Davis v. Prudential Sec., Inc.*, 59 F.3d 1186 (11th Cir. 1995) (permitting a private arbitrator to award punitive damages). Permitting arbitrators to hear claims on punitive damages is problematic because it is largely seen as a way to punish a party for conduct that is considered socially heinous. Ware, *supra*, at 530. By allowing private arbitrators to determine punitive damage awards, the arbitrator is performing an action typically reserved for the public. *Id.*

²⁶ See *supra* note 8 and accompanying text (citing concerns relating to using pre-dispute arbitration clauses in consumer and employment contracts). The merger of tort reform and arbitration is most evidenced in the medical malpractice arena, where the growing use of private arbitration to accomplish tort reform was embraced by courts in mandating arbitration in medical malpractice suits. See, e.g., *Baker v. Sadick*, 208 Cal. Rptr. 676 (Cal. Ct. App. 1984) (holding that an arbitration agreement to address any issue of medical malpractice included punitive damages). Many allege that consumer debt arbitration systems are methods of do-it-yourself tort reform, because common consumer contracts for cell phones, credit cards, and auto loans agreements contain mandatory pre-dispute

972 VALPARAISO UNIVERSITY LAW REVIEW [Vol. 47]

While arbitration has fostered support both in the judiciary and among scholars, constitutional issues emerge when privatizing adjudication.

B. Constitutional, Economic, and Social Concerns of Arbitration

One of the most important issues that arises from the shift away from governmental adjudication and into private adjudication is a constitutional one. The Seventh Amendment of the U.S. Constitution preserves the right to a trial by jury.²⁷ One might argue that jury trials, comprised of fellow citizens, should determine factual disputes, rather than paid professional arbitrators who may be more interested in their fees than the disputes at hand.²⁸ Arbitration clauses eliminate this fundamental right to a jury trial, which denies due process rights protected by the Fifth and Fourteenth Amendments.

As recently as June 2011, the West Virginia Supreme Court of Appeals agreed with this constitutional argument. The court cited West Virginia's Constitution, which preserves the right of the people to a jury trial with language identical to that of the Seventh Amendment.²⁹ The court also criticized the U.S. Supreme Court's "tendentious reasoning" to turn the FAA into substantive law that preempts most state law.³⁰ The West Virginia Supreme Court of Appeals stated that "Congress did not intend for arbitration agreements, adopted prior to an occurrence of negligence that results in a personal injury or wrongful death, and which require questions about the negligence be submitted to arbitration, to be

arbitration clauses, thereby preventing the jury system from imposing large damage awards. See generally Richard M. Alderman, *Why We Really Need the Arbitration Fairness Act: It's All About Separation of Powers*, 12 J. CONSUMER & COM. L. 151 (2009) (discussing the problems associated with pre-dispute arbitration clauses for consumer contracts and why it is important for Congress to implement legislation to prohibit pre-dispute arbitration).

²⁷ U.S. CONST. amend. VII ("In Suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury, shall be otherwise reexamined in any court of the United States, than according to the rules of the common law.").

²⁸ See, e.g., *In re Nat'l Arbitration Forum Trade Practices Litig.*, 704 F. Supp. 2d 832, 835 (D. Minn. 2010) (discussing how the bias of the National Arbitration Forum ("NAF") arbitrators resulted in a high number of arbitrations being resolved in favor of creditors, rather than being dismissed). The Minnesota Attorney General charged the NAF with several crimes including fraud, racketeering, deceptive and unfair trade practices, and tortious interference with contracts. *Id.* at 836. The parties settled and agreed for the defendants to pay \$3.2 million to the plaintiffs. *In re Nat'l Arbitration Forum Trade Practices Litig.*, No. 09-1939 (PAM/JSM) (D. Minn. Apr. 28, 2011) (order granting preliminary injunction).

²⁹ *Brown (ex rel. Brown) v. Genesis Healthcare Corp.*, 724 S.E.2d 250, 270 (W. Va. 2011), vacated 132 S. Ct. 1201 (2012).

³⁰ *Id.* at 278.

governed by the Federal Arbitration Act.”³¹ The court went on to say, “In essence, our *Constitution* recognizes that factual disputes should be decided by juries of lay citizens rather than paid, professional fact-finders (arbitrators) who may be more interested in their fees than the disputes at hand.”³² Furthermore, the federal judiciary’s expansion of the FAA to encourage the use of arbitration, even when it raises issues of unconscionability and frustrates the protections of the Fifth, Seventh, and Fourteenth Amendments, appears to contradict concepts of federalism, which creates an affront to states’ rights.³³

This shift by the U.S. Supreme Court gives rise to a curious question: What ever happened to the conservatives’ rigid adherence to the concept of federalism?³⁴ As stated by Justice Stephen Breyer in his dissenting opinion in *AT&T Mobility*:

By using the words “save upon such grounds as exist at law or in equity for the revocation of any contract,” Congress retained for the States an important

³¹ *Id.* at 262.

³² *Id.* at 271.

³³ Recently, the U.S. Supreme Court overruled *Brown ex rel. Brown*, which had previously held that pre-dispute arbitration clauses in nursing home agreements were invalid. *Marmet Health Care Ctr., Inc. v. Brown*, 132 S. Ct. 1201, 1203 (2012). The Supreme Court repeated its stance that state and federal courts must enforce the FAA with respect to all arbitration agreements. *Id.* The Court held that the West Virginia courts had misread and disregarded precedent in this area. *Id.* It further held that there were no exceptions for personal injury or wrongful death claims: “When state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA.” *Id.* (quoting *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1747 (2011)). Yet, not all pre-dispute arbitration clauses are considered valid. *See, e.g., Noohi v. Toll Bros., Inc.*, 708 F.3d 599 (4th Cir. 2013) (finding pre-dispute arbitration between a real estate developing company and potential luxury homebuyers to be unenforceable where there was no mutual consideration, because only the buyer was required to submit disputes to arbitration but not the seller).

³⁴ *See* Dale B. Thompson, *Immigration Policy Through the Lens of Optimal Federalism*, 2 WM. & MARY POL’Y REV. 236, 237 (2011) (discussing further the concepts of federalism and preemption); Dale B. Thompson, *Optimal Federalism Across Institutions: Theory and Applications from Environmental and Health Care Policies*, 40 LOY. U. CHI. L.J. 437, 437 (2009) (analyzing when federal action is appropriate and when a problem would be better addressed by individual states); *see, e.g.,* Amanda Terkel, *The Federalist Society: Where Are They Now?*, HUFFINGTON POST (Nov. 18, 2010, 8:43 AM), http://www.huffingtonpost.com/2010/11/18/federalist-society-post-bush_n_785049.html (illustrating the growth of the Federalist Society and particularly its role during George W. Bush’s administration). *See generally* Rosalie Berger Levinson, *Will the New Federalism Be the Legacy of the Rehnquist Court?*, 40 VAL. U. L. REV. 589, 590 (2006) (“[I]t cannot be denied that Justice Rehnquist presided over a major shift in U.S. law from the liberal Warren Court, and much of the conservative agenda was accomplished in the name of one overriding doctrine—federalism.”).

role incident to agreements to arbitrate. Through those words Congress reiterated a basic federal idea that has long informed the nature of this Nation's laws. We have often expressed this ideal in opinions that set forth presumptions. But federalism is as much a question of deeds as words. It often takes the form of a concrete decision by this Court that respects the legitimacy of a State's action in an individual case. Here, recognition of that federalist ideal, embodied in specific language in this particular statute, [the FAA], should lead us to uphold California's law, not to strike it down. We do not honor federalist principles in their breach.³⁵

There is one last point to be made about the economic and social consequences of this shift in policy. It will affect all types of consumer agreements, employment contracts, insurance contracts, franchise agreements, health provider agreements—the list is endless. Arbitration agreements can affect tort law, contract law, and certain statutory rights.³⁶ Due to the policy shift exhibited by the Court, Congress renewed its support for the Arbitration Fairness Act.³⁷ It also empowered the creation of the Consumer Financial Protection Bureau in section 1028 of the Dodd-Frank Wall Street Reform and Consumer Financial Protection Act, which prohibits pre-dispute arbitration agreements altogether or imposes conditions or limitations on the use of

³⁵ *AT&T Mobility*, 131 S. Ct. at 1762 (Breyer, J., dissenting) (citations omitted).

³⁶ See *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, 111–12 (2001) (noting the FAA's language includes contract law, including language pertaining to employment contracts); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985) ("By agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than judicial form."); *Morrison v. Circuit City Stores, Inc.*, 317 F.3d 646, 672–73 (6th Cir. 2003) (finding that an arbitration agreement was not enforceable for tort law, particularly claims alleging race and sex discrimination).

³⁷ The Arbitration Fairness Act of 2009, H.R. 1020, 111th Cong. (2009). The original Arbitration Fairness Act notes that the FAA is limited to disputes among commercial entities with similar sophistication and bargaining power. *Id.* § 2. The bill goes on to say that "[p]rivate arbitration companies are sometimes under great pressure to devise systems that favor the corporate repeat players who decide whether those companies will receive their lucrative business." *Id.* § 2(4). The Arbitration Fairness Act of 2009, however, died in Committee. The Arbitration Fairness Act was reintroduced on May 12, 2011, which some believe was a direct response to the *AT&T Mobility* case. Arbitration Fairness Act of 2011, S. 987, 112th Cong. (2011); see *supra* note 15 (explaining how the Arbitration Fairness Act of 2011 was re-introduced in Congress, though ultimately the bill was not successful).

such agreements.³⁸ In addition to Congress, federal courts have also embraced arbitration agreements. Yet, these holdings have been inconsistent and problematic.

III. A FINE STATE OF AFFAIRS³⁹ — ANOMALY OF RECENT DECISIONS

Recently, the U.S. Supreme Court has reviewed challenges to arbitration clauses in a number of cases. Yet the Court's argument as to the validity of arbitration agreements has been erratic. In *Buckeye Check Cashing, Inc. v. Cardegna*, for example, the Court held that when there is an arbitration clause in a contract, "a challenge to the validity of the contract as a whole, and not specifically to the arbitration clause, must go to the arbitrator."⁴⁰ The Court re-emphasized that point, stating that "unless the challenge is to the arbitration clause itself, the issue of the

³⁸ Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 2003-04 (2010) (to be codified at 12 U.S.C. § 5518(b) (2012)). According to section 1028(a):

The Bureau . . . may prohibit . . . the use of an agreement between a covered person and a consumer for a consumer financial product or service providing for arbitration of any future dispute between the parties, if the Bureau finds that such a prohibition . . . is in the public interest and for the protection of consumers.

Id. See generally Catherine Moore, Note, *The Effect of the Dodd-Frank Act on Arbitration Agreements: A Proposal for Consumer Choice*, 12 PEPP. DISP. RESOL. L.J. 503 (2012) (discussing arbitration agreements in the context of securities disputes). The new "Consumer Czar," Richard Cordray, was recently appointed to the position of head of the Consumer Financial Protection Bureau, which may, by virtue of future regulations, curb practices that adversely affect consumers. Eyder Peralta, *New Consumer Czar: 'This is a Valid Appointment'*, NPR (Jan. 5, 2012, 5:28 PM), <http://www.npr.org/blogs/thetwo-way/2012/01/05/144753031/new-consumer-czar-this-is-a-valid-appointment>. The Dodd-Frank Act has been criticized for being an incomplete framework for consumer protection and corporate responsibility. See generally Eric C. Chaffee, *The Dodd-Frank Wall Street Reform and Consumer Protection Act: A Failed Vision for Increasing Consumer Protection and Heightening Corporate Responsibility in International Financial Transactions*, 60 AM. U. L. REV. 1431 (2011) (arguing that the Dodd-Frank Act is cracked and fragmented because it fails to consider globalization and creates problems for consumers). Under the Dodd Frank Act, mandatory pre-dispute arbitration between broker-dealers and customers is also prohibited, as are pre-dispute arbitration claims involving whistle-blowers. 23A THOMAS L. HAZEN & JERRY W. MARKHAM, *BROKER-DEALER OPERATIONS SEC. & COMM. LAW* § 12:14.50 (2012); see 15 U.S.C. § 78o(o) (2006) ("The Commission . . . may prohibit, or impose conditions or limitations on the use of, agreements that require customers or clients of any broker, dealer, or municipal securities dealer to arbitrate any future dispute between them . . ."); 12 U.S.C. § 5567(d)(2) (2006) ("[N]o predispute arbitration agreement shall be valid or enforceable to the extent that it requires arbitration of a dispute arising under this section.").

³⁹ As frequently stated by the early American slapstick comedy duo, Stan Laurel and Oliver Hardy, "Here's another nice mess you've gotten me into." ROBERT ANDREWS, *FAMOUS LINES: A COLUMBIA DICTIONARY OF FAMILIAR QUOTATIONS* 389 (1997).

⁴⁰ *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 449 (2006).

976 VALPARAISO UNIVERSITY LAW REVIEW [Vol. 47]

contract's validity is considered by the arbitrator in the first instance."⁴¹ This decision authorizes the courts, not the arbitrators, to decide issues regarding the validity of an arbitration agreement in a contract,⁴² unless the language of the arbitration clause explicitly permits the arbitrators to decide the validity of the arbitration clause and the contract as a whole.⁴³ In accord with the *Buckeye* decision, numerous courts have addressed the validity of arbitration agreements contained in a contract, often holding that such clauses are unconscionable and thus unenforceable—this also was one of the issues that the Ninth Circuit decided in *AT&T Mobility*.⁴⁴

But, in the decision reached by the Supreme Court in *AT&T Mobility*, courts may no longer rely on principles of general law when reviewing an arbitration agreement if such principles would “stand as an obstacle to the accomplishment of the FAA’s objectives.”⁴⁵ If such an obstacle of general law exists, then one could argue that almost all general law defenses to enforcement of a well-drafted arbitration agreement would be futile, as they would have a disproportionate impact on arbitration agreements and thus would be preempted by the FAA.

However, such may not be an accurate reading of the *AT&T Mobility* decision. When substantive federal laws—for example, the FAA—and substantive state laws conflict, as they have regarding the validity of arbitration agreements, then a question arises as to the precise meaning and scope of the recent *AT&T Mobility* decision.

The final sentence in the *AT&T Mobility* opinion reads, “Because it ‘stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress,’ California’s *Discover Bank* rule is preempted by the FAA.”⁴⁶ This creates a question as to which general

⁴¹ *Id.* at 445–46.

⁴² *Thibodeau v. Comcast Corp.*, 912 A.2d 874, 887 (Pa. Super. Ct. 2006) (holding that a bar on class-wide proceedings rendered an arbitration agreement unconscionable and unenforceable).

⁴³ *Rent-A-Center, West, Inc. v. Jackson*, 130 S. Ct. 2772, 2778–79 (2010) (ruling that when an arbitration agreement delegates to the arbitrator the authority to determine whether the agreement should be arbitrated, claims that challenge the enforceability and validity of such agreement as a whole will be determined by the arbitrator, while claims that specifically challenge the enforcement of the delegation provision will be considered by the court).

⁴⁴ *See AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1745 (2011) (explaining that the Ninth Circuit held the arbitration provision was unconscionable (citing *Laster v. AT&T Mobility LLC*, 584 F.3d 849, 855 (9th Cir. 2009)); *see also, e.g., Lowden v. T-Mobile USA, Inc.*, 512 F.3d 1213, 1219 (9th Cir. 2008) (citation omitted) (applying Washington state law to find class action waivers unconscionable and unenforceable); *Thibodeau*, 912 A.2d at 886–87 (applying Pennsylvania and Massachusetts state laws to find a ban on class action suits unconscionable and unenforceable).

⁴⁵ *AT&T Mobility*, 131 S. Ct. at 1753 (citations omitted).

⁴⁶ *Id.* (quoting *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941)).

laws are preempted by the FAA and how far such preemption will go to preclude an invalidation of an arbitration agreement. The *Discover Bank* rule provides that arbitration provisions would be deemed unconscionable when one party is found to have superior bargaining power and has instituted an arbitration agreement to prevent class actions in cases that would not be economically beneficial to pursue for individuals (i.e., cases involving small amounts of damages).⁴⁷ The Court seemed to suggest that it is not established that bilateral arbitration (i.e., one-on-one) adequately substituted for the deterrent effects of class actions.⁴⁸ The *Discover Bank* rule deemed arbitration agreements that contain a prohibition on class actions—known as collective-arbitration waivers—unconscionable under California general law and under the state’s civil code.⁴⁹ However, the U.S. Supreme Court reversed the Ninth Circuit and held that “[w]hen state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA.”⁵⁰ Thus, a general state law that bans class action waivers in arbitration agreements would be unconscionable and unenforceable because, according to the U.S. Supreme Court, the ban would have a disproportionate impact on such agreements, and ultimately the FAA would preempt it.

The decision in *AT&T Mobility* raises more questions about the applicability of the ruling than it answers. Is the holding simply that this particular general law in California, namely the *Discover Bank* holding, was preempted and nothing more? Or are we to wait for more cases to test whether other general law defenses to contracts operate in a way that has a disproportionate impact on arbitration agreements? Is “disproportionate impact” now the test to be applied? Or has the *AT&T Mobility* decision already applied that test and indicated where the test

⁴⁷ *Id.* at 1746.

⁴⁸ *Id.* The reasoning of the *Discover Bank* rule, as stated by the California Supreme Court, was quoted by the U.S. Supreme Court as follows:

[W]hen the waiver is found in a consumer contract of adhesion in a setting in which disputes between the contracting parties predictably involve small amounts of damages, and when 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 becomes in practice the exemption of the party ‘from responsibility for [its] own fraud, or willful injury to the person or property of another.’ Under these circumstances, such waivers are unconscionable under California law and should not be enforced.

Id. (quoting *Discover Bank v. Superior Court*, 113 P.3d 1100, 1110 (Cal. 2005)) (alterations in original).

⁴⁹ *Discover Bank*, 113 P.3d at 1103.

⁵⁰ *AT&T Mobility*, 131 S. Ct. at 1747 (citation omitted).

has been met so as to preempt state law? These questions show that the future of the *AT&T Mobility* holding is uncertain.

Despite the last sentence in *AT&T Mobility* suggesting that the decision is applicable solely to the *Discover Bank* rule, it is necessary to look at the full body of the *AT&T Mobility* majority opinion, because the Court provided examples of applying general laws that would have a “disproportionate impact” on the FAA.⁵¹ Although some may view these examples as simply disingenuous dicta that muddied the water, others may argue that the Court’s examples operate as a binding preclusion of any lower courts’ review of the legality of arbitration agreements on general law principles. Enumerating the examples in the opinion thus nullifies the effectiveness of the *Buckeye* opinion.⁵² Lower courts are precluded from invalidating arbitration agreements based on substantive and, in some cases, procedural unconscionability.

Consequently, scholars and courts analyzing and applying the *AT&T Mobility* decision appear to disagree as to its scope and its effect on lower courts’ review of arbitration agreements, which is permitted by the *Buckeye* decision. Some argue that *AT&T Mobility* completely precludes

⁵¹ *Id.*

⁵² If the test of “disproportionate impact” is applicable to all of the examples given in the opinion, then there is nothing left for lower courts to review in consideration of the legality of provisions in arbitration agreements. Thus, the *Buckeye* decision essentially becomes ineffective. The Supreme Court gave the following examples in the *AT&T Mobility* case:

An obvious illustration . . . would be a case finding unconscionable or unenforceable as against public policy consumer arbitration agreements that fail to provide for judicially monitored discovery. . . . A [lower] court might reason that no consumer would knowingly waive his right to full discovery, as this would enable companies to hide their wrongdoing. Or the [lower] court might simply say that such agreements are exculpatory—restricting discovery would be of greater benefit to the company than the consumer, since the former is more likely to be sued than to sue. And, the reasoning would continue, because such a rule applies the general principle of unconscionability or public-policy disapproval of exculpatory agreements, it is applicable to “any” contract and thus preserved by § 2 of the FAA. In practice of course, the rule would have a *disproportionate impact* on arbitration agreements; but it would presumably apply to contracts purporting to restrict discovery in litigation as well.

Other examples are easy to imagine. The same argument might apply to a rule classifying as unconscionable arbitration agreements that fail to abide by the Federal Rules of Evidence, or that disallow an ultimate disposition by a jury (perhaps termed “a panel of twelve lay arbitrators” to help avoid preemption).

Id. (emphasis added) (citation omitted).

application of general law to arbitration agreements.⁵³ If so, then the *Buckeye* decision becomes a nullity. Others appear to be unconvinced.⁵⁴ Still others opine that dual readings of the decision exist and that the decision can be read narrowly even if the Supreme Court intended a broader interpretation.⁵⁵ Before the *AT&T Mobility* decision, however, there was a drastically different process for reviewing arbitration, which took general law into account.

IV. THE EVOLUTION OF ARBITRATION CLAUSES AND THE FINALITY OF THE ARBITRATION AWARD

To understand the irregularities in the present state of affairs, it is necessary to review the history of arbitration. Around the mid-twentieth century, there began an explosive expansion of the arbitral process, which was generally sanctioned by the courts.⁵⁶ In private arbitration,

⁵³ See, e.g., Mike Appleton, *AT&T Mobility v. Concepcion: Has Consumer Protection Law Been Preempted?*, JOHNATHAN TURLEY (July 3, 2011), <http://jonathanturley.org/2011/07/03/att-mobility-v-concepcion-has-consumer-protection-law-been-preempted/>.

⁵⁴ Recent decisions in cases demonstrate that lower courts continue to find exceptions to the preemption doctrine. *In re DirecTV Early Cancellation Fee Mktg. & Sales Practices Litig.*, 810 F. Supp. 2d 1060, 1072–73 (C.D. Cal. 2011) (holding that state law remains valid notwithstanding the *AT&T Mobility LLC* decision), *abrogated by* *Kilgore v. KeyBank, Nat'l Ass'n*, 673 F.3d 947, 960, 963 (9th Cir. 2012); *Plows v. Rockwell Collins, Inc.*, 812 F. Supp. 2d 1063, 1069 (C.D. Cal. 2011)).

⁵⁵ See Colin P. Marks, *The Irony of AT&T v. Concepcion*, 87 IND. L.J. SUPP. 31, 32 (2012) (discussing how the opinion is open to multiple interpretations and can be read narrowly and broadly); see also *Sanchez v. Valencia Holding Co.*, 135 Cal. Rptr. 3d 19, 31 (Cal. Ct. App. 2011) (striking down an arbitration agreement containing a class waiver clause on the ground of unconscionability and stating that the agreement was a contract of adhesion and unfairly one-sided); *Brown v. Ralphs Grocery Co.*, 128 Cal. Rptr. 3d 854, 860–61 (Cal. Ct. App. 2011) (invalidating a class-action waiver in an arbitration agreement as it was applied to a representative action under a state statute that allowed a plaintiff to bring an action on behalf of other employees to enforce the Labor Code, distinguishing the representative actions from class actions).

⁵⁶ Jay R. Sever, Comment, *The Relaxation of Inarbitrability and Public Policy Checks on U.S. and Foreign Arbitration: Arbitration out of Control?*, 65 TUL. L. REV. 1661, 1667–68 (1991).

American courts, led by recent landmark decisions of the U.S.

Supreme Court, have moved from a hostile and jealous attitude towards the institution of arbitration to allowing and enforcing almost any arbitration agreement or award of international commercial character, regardless of whether it comports with traditional arbitrability and public policy standards. The Court enunciated a major rationale for its liberal attitude in *The Bremen* when it noted that courts should honor the “ancient concepts of freedom of contract.” A more recent . . . undercurrent in the Court’s rationale is a nearly absolute deference to arbitration, apparently for purposes of judicial efficiency.

Id. (footnotes omitted).

980 VALPARAISO UNIVERSITY LAW REVIEW [Vol. 47]

disputing parties agree to arbitrate. Parties enter into these agreements either before any dispute arises or after a dispute begins. The pre-dispute agreements to arbitrate are usually clauses in larger contracts. Many arbitration clauses contain choice-of-law provisions designating the law of a particular state to govern disputes. Once an arbitration award is made, it is difficult to reverse it on appeal to a court. Nevertheless, the loser of the arbitration hearing may choose to appeal the decision to the courts or defy the arbitrator's decision.⁵⁷

Typically, a reviewing court can only reverse an arbitration award based upon very specific and limited reasons, such as when: (1) the award was maintained by corruption or fraud; (2) the arbitrator was not impartial; (3) the arbitrator exceeded his authority; (4) the arbitrator unreasonably refused to postpone the hearing or hear material evidence; or (5) there was no arbitration agreement.⁵⁸ The FAA does not allow for an appeal on the merits of an arbitration award but rather allows only judicial review of procedural errors.⁵⁹ In *Hall Street Associates, L.L.C. v. Mattel, Inc.*, the U.S. Supreme Court invalidated the expanding efforts of review by lower courts, holding that the grounds listed in the FAA are the exclusive grounds available for reviewing an arbitration award.⁶⁰ Yet, many federal appellate courts have pronounced additional grounds for review of arbitration decisions, including review for disregard of law, public policy, irrationality, and arbitrariness.⁶¹

In 1984, the U.S. Supreme Court essentially federalized arbitration in *Southland Corp. v. Keating*, finding that the FAA constituted substantive federal law, which thereby preempted any contradictory or conflicting state law from curtailing certain aspects of arbitration availability and procedures.⁶² The *Keating* decision served to close one more avenue of

⁵⁷ Stephen J. Ware, *Default Rules from Mandatory Rules: Privatizing Law Through Arbitration*, 83 MINN. L. REV. 703, 708 (1999). Should the loser choose the road of defiance, the winner must petition the court for an order confirming the award. *Id.*

⁵⁸ See, e.g., 710 ILL. COMP. STAT. ANN. 5/12(a) (West 2007) (providing the scenarios where the court will vacate an arbitration award).

⁵⁹ 9 U.S.C. § 10(a) (2006).

⁶⁰ *Hall Street Assocs., LLC v. Mattel, Inc.*, 552 U.S. 576, 590 (2008). The Court noted that there may be other ways for courts to review cases in other sections of the FAA, but for sections 9, 10, and 11, the FAA grounds listed for review are exclusive. *Id.*

⁶¹ Stephen L. Hayford, *A New Paradigm for Commercial Arbitration: Rethinking the Relationship Between Reasoned Awards and the Judicial Standard for Vacatur*, 66 GEO. WASH. L. REV. 443, 461-62 (1998). The courts rely on section 2 of the FAA to determine the enforceability of arbitration agreements "upon such grounds as exist at law or in equity for the revocation of a contract." *Revelation, Reaction and Reflection*, *supra* note 4.

⁶² *Southland Corp. v. Keating*, 465 U.S. 1, 12 (1984) ("We thus read the underlying issue of arbitrability to be a question of substantive federal law: 'Federal law in the terms of the Arbitration Act governs that issue in either state or federal court.'" (quoting *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983))).

protections within the private arbitration processes. Then, in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, the Court allowed for the arbitration of statutory rights, which was followed by *Circuit City Stores, Inc. v. Adams*, where the Court applied this analysis to the employment dispute arena.⁶³

As a result of the Court's decisions over the past fifty years, it has been said repeatedly that the process of arbitration, and the power afforded to that process, is lawless. The process itself has been described as a "legal black hole."⁶⁴ This notion of lawlessness becomes even more apparent when examining judicial review under the FAA.

V. ABROGATION OF JUDICIAL REVIEW OF THE FAA

Judicial review is one of the cornerstone principles of our legal system. In the United States, the courts serve as the supreme protector of the rights of individuals. Since the monumental case of *Marbury v. Madison*, the courts have reviewed the actions of the government to ensure that the rights of individuals are not improperly impaired.⁶⁵ Chief Justice John Marshall stated that "[i]t is emphatically the province and duty of the judicial department to say what the law is."⁶⁶

Arbitrators may substitute their concepts of fairness for the law, but they generally follow common law and statutory law in making their decisions. However, courts regularly emphasize that arbitrators are not obligated to follow the law when deciding a case or reaching an award.⁶⁷

⁶³ See *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985) (explaining that parties may choose the arbitration process over judicial review unless Congress says otherwise, because it is simplistic, informal, and expeditious); see also *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, 119 (2001) (stating that if Congress intended to exclude all employment contracts from the FAA, then Congress would include that language in the FAA). The Court found that § 1 of the FAA exempted only employment contracts of transportation workers, disagreeing with the Court of Appeals, which interpreted § 1 to exclude all employment contracts. *Id.*

⁶⁴ Appleton, *supra* note 53.

⁶⁵ *Marbury v. Madison*, 5 U.S. (1 Cranch) 137 (1803).

⁶⁶ *Id.* at 177.

⁶⁷ See Ware, *supra* note 57, at 720 n.82 (citing to New York cases finding that arbitrators are not bound by rules of law unless the arbitration agreement requires it); see also Kenneth S. Abraham & J.W. Montgomery, III, *The Lawlessness of Arbitration*, 9 CONN. INS. L.J. 355, 357 (2003) (noting that arbitration operates with a sort of "contractual lawlessness"); Richard M. Alderman, *Consumer Arbitration: The Destruction of the Common Law*, 2 J. AM. ARB. 1, 11 (2003) ("Even assuming an arbitrator is committed to following the law, however, he or she cannot make it. Therein lies the problem. . . . Arbitration eliminates litigation in a public forum, precedent-establishing decisions, and stare decisis.") (footnotes omitted); Barbara Black & Jill I. Gross, *Making It up as They Go Along: The Role of Law in Securities Arbitration*, 23 CARDOZO L. REV. 991, 1040 (2002) ("While it seems that an investor may have difficulty prevailing in court under the established law, arbitration panels, on more than an

982 VALPARAISO UNIVERSITY LAW REVIEW [Vol. 47]

For example, in *Perini Corporation v. Greate Bay Hotel & Casino, Inc.*, a dispute arose between a casino and its construction contractor regarding their contract.⁶⁸ The dispute went to arbitration, where a panel of arbitrators decided in favor of the casino and awarded it lost profits.⁶⁹ On appeal, the contractors argued that the parties did not contemplate lost profit damages in the contract, and thus the arbitrators did not follow existing law.⁷⁰ The court affirmed the arbitrator's decision and held that the asserted errors of law did not warrant judicial invalidation of the award, because they were not gross, unmistakable, or a manifest disregard of applicable law.⁷¹ In looking at the narrow grounds for overturning an arbitration decision, the court stated, "Obviously a mistake of law is not one of the stated grounds for vacating an award. Nor, indeed, is sufficiency of the evidence."⁷² The New Jersey Supreme Court upheld the arbitrator's award.⁷³

In a second case, *St. John's Mercy Medical Center v. Delfino*, the U.S. Court of Appeals for the Eighth Circuit held that a court could only overturn an arbitrator's award if the arbitrator was fully aware of the existence of a clearly defined governing legal principle and refused to apply it (known as the "manifest disregard doctrine").⁷⁴ The Eighth Circuit found that since the arbitrator, in the case at hand, clearly failed to cite the relevant contract law and then disregarded it, the manifest disregard doctrine did not apply.⁷⁵ Thus, the Eighth Circuit held that the lower court erred in substituting its remedial judgment for the arbitrator, because no contract law reason was actually cited by the court.⁷⁶

In a third case, the court reinforced the doctrine of *stare decisis*:

occasional basis, are reaching decisions favorable to investors even where the 'law is clear' that there is no basis for imposing liability on the broker."); Edward Brunet, *Toward Changing Models of Securities Arbitration*, 62 BROOK. L. REV. 1459, 1484 (1996) ("The arbitrator need not apply substantive legal principles. The old 'manifest disregard' of the law standard appears close to dead.") (footnotes omitted); Jennifer J. Johnson, *Wall Street Meets the Wild West: Bringing Law and Order to Securities Arbitration*, 84 N.C. L. REV. 123, 140 (2005) ("[T]here is no meaningful judicial oversight to ensure that arbitrators are applying the law, and limited evidence on the ground suggests that SRO ['Self Regulatory Organization'] panels may not in fact apply the law.") (footnotes omitted).

⁶⁸ *Perini Corp. v. Greate Bay Hotel & Casino, Inc.*, 610 A.2d 364, 366 (N.J. 1992).

⁶⁹ *Id.* at 368.

⁷⁰ *Id.*

⁷¹ *Id.* at 366, 368 ("[T]he arbitrators had not committed 'the kind of gross mistake or clear disregard of applicable law that is required to overturn an award.'").

⁷² *Id.* at 370.

⁷³ *Id.* at 384.

⁷⁴ *St. John's Mercy Med. Ctr. v. Delfino*, 414 F.3d 882, 884 (8th Cir. 2005).

⁷⁵ *Id.*

⁷⁶ *Id.* at 885.

At common law, the courts have almost uniformly refused to vacate an arbitrator's award because of an error of law or fact. It has been held that the arbitrator is the final judge of both law and facts, and that an award will not be set aside except upon a clear showing of fraud, misconduct or some other irregularity rendering the award unjust, inequitable, or unconscionable[] and that even a grossly erroneous decision is binding in the absence of fraud.⁷⁷

Much of the current discussion and criticism about arbitration concerns the absence of *stare decisis* principles in private arbitration decision-making. Attorney practitioners voice many concerns about this situation:

One of the most distinguishing characteristics of an arbitration proceeding is the absence of *stare decisis*, meaning "the policy of the court to stand by precedent." Instead, a decision made during one proceeding will not affect the decision in a following, similar proceeding. In other words, arbitration lacks the deterrent of an unfavorable court decision having been issued. Thus, even if a managed care company is proven wrong in one hearing, it may not alter its practice, since a future arbitration will begin with a clean slate.⁷⁸

Arbitration is a confidential process. Due to this, arbitration decisions do not establish case precedent.⁷⁹ This concern becomes particularly troublesome when an arbitrator's case is one of first impression, or the lower courts have conflicted over it.⁸⁰ Further, arbitration awards are generally not published. In fact, in many arbitration proceedings, the parties have an obligation to keep both the proceedings and final outcome of the arbitration confidential.⁸¹ As such, the decision of one

⁷⁷ Goodyear Tire & Rubber Co. v. Local Union No. 200, 330 N.E.2d 703, 708 (Ohio 1975) (citations omitted).

⁷⁸ Maria Pepe VanDerLaan & David G. Jordan, *Modern Arbitration Clauses Place Health Care Providers into Unanticipated Corner*, SAXE DOERNBERGER & VITA, P.C., http://www.sdvlaw.com/images/Arbitration_Pitfalls__SDV.Unabridged.pdf (last visited May 16, 2013).

⁷⁹ Abraham & Montgomery, *supra* note 67, at 360.

⁸⁰ *Id.* at 363.

⁸¹ See Alderman, *supra* note 67, at 11 ("Even when published and made available to the public, the decision of one arbitrator, or a panel of arbitrators, is in no way binding on any other arbitrator or panel."); Charles L. Knapp, *Taking Contracts Private: The Quiet Revolution*

arbitration panel has no binding or precedential effect on other arbitration panels, nor should it.

Recent cases from the Supreme Court have further complicated the issue concerning arbitration in its interpretation of the FAA's authority over state and common law.

VI. RECENT POSTURING OF THE SUPREME COURT TOWARDS TOTAL PREEMPTION

States have continuously struggled with the idea of replacing traditional litigation with alternative dispute resolution, particularly arbitration.⁸² Some states, in response to the increase in the use of arbitration, have enacted laws regulating arbitration; however, the FAA has preempted many of these laws.⁸³ The concept of federal preemption is derived from the U.S. Constitution:

This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.⁸⁴

The U.S. Supreme Court has used this provision to hold any state law unconstitutional that conflicts with a federal law.⁸⁵ In the case of private arbitration, judicial decisions and state arbitration statutes act as the state law that conflicts with the FAA, the applicable federal law.⁸⁶ In determining whether a particular federal law preempts state law, the U.S. Supreme Court examines legislative intent.⁸⁷

In the case of *Southland Corp. v. Keating*, the U.S. Supreme Court held that the FAA was not only applicable in state court proceedings, but also

in Contract Law, 71 FORDHAM L. REV. 761, 785 (2002) ("[O]nce the case is decided by the arbitrators, it will furnish no precedent by which future decision-makers—whether judges or other arbitrators—will be guided. Past decisions in arbitration furnish no reliable guide to the present and present decisions serve as no reliable guide to the future.").

⁸² See Christopher R. Drahozal, *Federal Arbitration Act Preemption*, 79 IND. L.J. 393, 394 (2004) (noting the ongoing struggle states are having as they adapt to using arbitration rather than litigation).

⁸³ *Id.* at 395.

⁸⁴ U.S. CONST. art. VI, cl. 2.

⁸⁵ Drahozal, *supra* note 82, at 397.

⁸⁶ See *id.* (explaining how conflict preemption operates between state and federal law).

⁸⁷ *Id.*

held that § 2 of the FAA preempted conflicting state law.⁸⁸ This California case involved convenience store franchisees who alleged that the franchisor violated the California Franchise Investment Law by seeking to compel arbitration of the contract dispute.⁸⁹ After this case, states could no longer require a judicial forum for the resolution of disputes, and, pursuant to the opinion of the Court, arbitration offered an equally valid forum for the resolution of disputes.⁹⁰ The Court justified preemption by finding that it helped reverse long-time judicial hostility towards arbitration and reaffirmed the right of individuals to contract without court interference.⁹¹

The U.S. Supreme Court has in its decisions consistently reaffirmed its commitment to arbitration and the preemption of the state statutes by the FAA. In the case of *Buckeye Check Cashing, Inc. v. Cardegna*, the Court upheld the enforceability of an arbitration clause in a contract, despite the claim that the underlying contract was both illegal and void.⁹² Buckeye, the check cashing company, sought to compel arbitration, but the trial court held that a court rather than an arbitrator should decide if the underlying contract was illegal.⁹³ On appeal, the decision was reversed, because the Cardegnas were not actually challenging the arbitration clause; rather, they had challenged the high interest rates of the contract.⁹⁴ The U.S. Supreme Court held that the arbitrator was empowered to decide the validity of the entire contract, and a court would only be necessary if the parties challenged the arbitration clause itself.⁹⁵ Justice Thomas dissented in the *Buckeye* case:

I remain of the view that the Federal Arbitration Act (FAA), 9 U.S.C. § 1 *et seq.*, does not apply to proceedings in state courts. Thus, in state-court proceedings, the FAA cannot be the basis for displacing a state law that prohibits enforcement of an arbitration clause contained in a contract that is unenforceable under state law. Accordingly, I would leave undisturbed the judgment of the Florida Supreme Court.⁹⁶

⁸⁸ *Southland Corp. v. Keating*, 465 U.S. 1, 16 (1984).

⁸⁹ *Id.* at 3–4.

⁹⁰ Lawrence Waddington, *Federalizing Arbitration*, L.A. LAW., Sept. 2003, at 30, 31.

⁹¹ *Id.*

⁹² *Buckeye Check Cashing v. Cardegna*, 546 U.S. 440, 449 (2006).

⁹³ *Id.* at 443.

⁹⁴ *Id.*

⁹⁵ *See id.* at 449 (holding that a challenge on the whole of the contract must go to the arbitrator).

⁹⁶ *Id.* (Thomas, J., dissenting) (citations omitted).

986 VALPARAISO UNIVERSITY LAW REVIEW [Vol. 47]

More recently, in *AT&T Mobility, LLC v. Concepcion*, the Court struck down a California Supreme Court decision that found an arbitration clause unconscionable under state law.⁹⁷ The Concepcions received a free telephone from AT&T, but AT&T required them to pay a California tax in the amount of \$30.22.⁹⁸ AT&T's consumer contract contained an arbitration clause.⁹⁹ With this decision by the Court, it seems as if the *Buckeye* decision allowing for courts to review the legality of arbitration clauses has been nullified.

The 5–4 decision authored by Justice Scalia, held that, pursuant to the FAA, California must enforce arbitration agreements even when the agreement requires consumers to arbitrate their complaints individually, instead of as a class.¹⁰⁰ According to the Court, the test used by California state courts to determine the unconscionability of an arbitration clause, requiring waiver of a class-action, was preempted by the FAA even if the underlying contract was potentially fraudulent or was related to false advertising.¹⁰¹ The Court found that the FAA preempted the state law because the state law singled out arbitration agreements, and the standard allowed them to find an arbitration agreement unconscionable more frequently than other contracts.¹⁰² The Court found that “[a]rbitration is a matter of contract, and the FAA requires courts to honor parties’ expectations.”¹⁰³ It reasoned,

The overarching purpose of the FAA, evident in the text of §§ 2, 3, and 4, is to ensure the enforcement of arbitration agreements according to their terms so as to facilitate streamlined proceedings. Requiring the availability of classwide arbitration interferes with fundamental attributes of arbitration and thus creates a scheme inconsistent with the FAA.¹⁰⁴

The Court found that California’s statute containing the no-class-waiver rule does not apply to “any contract” because it impedes the purpose of the FAA.

⁹⁷ *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1753 (2011).

⁹⁸ *Id.* at 1744.

⁹⁹ *Id.*

¹⁰⁰ *Id.*

¹⁰¹ *See id.* at 1753 (“States cannot require a procedure that is inconsistent with the FAA, even if it is desirable for unrelated reasons.”).

¹⁰² *Id.* at 1746, 1753.

¹⁰³ *Id.* at 1752 (citing *Rent-A-Center, West, Inc. v. Jackson*, 130 S. Ct. 2772, 2774 (2010)).

¹⁰⁴ *Id.* at 1748 (Breyer, Ginsburg, Sotomayor, Kagan, J.J., dissenting).

The dissent in this case identified an important principle missed by the majority opinion—state sovereignty. They noted,

By using the words “save upon such grounds as exist at law or in equity for the revocation of any contract,” . . . Congress reiterated a basic federal idea that has long informed the nature of this Nation’s laws. . . . Here, recognition of that federalist ideal, embodied in specific language in this particular statute, should lead us to uphold California’s law, not to strike it down. We do not honor federalist principles in their breach.¹⁰⁵

It would seem that the *AT&T Mobility* case has now removed the courts from conducting such a review of arbitration clauses for unconscionability and has essentially nullified the *Buckeye* holding. Not only do recent cases present uncertainty as to the reviewability of arbitration clauses, but the interpretation of § 2 of the FAA also raises questions for the future of arbitration.

VII. THE MEANING OF § 2 OF THE FAA AND THE PHRASE “GENERAL LAW”

Section 2 of the FAA states that arbitration clauses or agreements “shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.”¹⁰⁶ The Supreme Court has further noted that “[s]ection 2 embodies the national policy favoring arbitration and places arbitration agreements on equal footing with all other contracts[.]”¹⁰⁷ As such,

[a] written provision in . . . a contract . . . to settle by arbitration a controversy thereafter arising out of such contract . . . or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.¹⁰⁸

¹⁰⁵ *Id.* at 1762.

¹⁰⁶ Federal Arbitration Act, 9 U.S.C. § 2 (2006).

¹⁰⁷ *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 443 (2006).

¹⁰⁸ *Id.* at 443–44 (quoting 9 U.S.C. § 2).

988 VALPARAISO UNIVERSITY LAW REVIEW [Vol. 47]

Courts have used general contract defenses, such as fraud, duress, or unconscionability, to invalidate arbitration agreements without conflicting with § 2 of the FAA.¹⁰⁹

From the *Buckeye* case, the Court set out that challenges to the validity of arbitration agreements, “upon such grounds as exist at law or in equity for the revocation of any contract,” include two sets of cases.¹¹⁰ One type specifically challenges the validity of the agreement to arbitrate.¹¹¹ The other challenges the contract underlying the arbitration as a whole, either on a basis that directly affects the entire agreement (e.g., the agreement was fraudulently induced) or on the ground that the illegality of one of the provisions of the contract renders the whole contract invalid.¹¹² The question remains as to whether the *Buckeye* decision remains applicable. Historically, the doctrine has stated that the law of a particular state governs contract law while stipulating the grounds that may invalidate a contract. Additionally, one of the main purposes of the FAA is “to overcome courts’ refusals to enforce agreements to arbitrate.”¹¹³ What remains unclear is whether there is any state law or general law that can be relied on for a court to invalidate an arbitration agreement.

VIII. CONCLUSION

“Arbitration is power, and courts are forbidden to look behind it.”¹¹⁴ The protection of arbitration awards against judicial interference and the development of organized arbitration have established “judicial powers” other than those provided in both the federal and state constitutions. “It is not possible to maintain any legally established policy or order in domestic and international trade, whether it is an order of free competition protected by antitrust legislation or any other type of economic order provided by law, if courts abdicate their power in favor of private tribunals serving private interests.”¹¹⁵ American courts are presently conflicted with such private tribunals. “In the face of the

¹⁰⁹ *Doctor’s Assocs., Inc. v. Casarotto*, 517 U.S. 681, 686–87 (1996).

¹¹⁰ *Buckeye Check Cashing, Inc.*, 546 U.S. at 444 (quoting 9 U.S.C. § 2).

¹¹¹ *See, e.g., Southland Corp. v. Keating*, 465 U.S. 1, 10 (1984) (challenging the agreement to arbitrate as void under California law insofar as it purported to cover claims brought under the state’s Franchise Investment Law).

¹¹² *Id.* The claim is the second type in this case. The crux of the complaint is that the contract as a whole, including its arbitration provision, is rendered invalid by the usurious finance charge. *Id.*

¹¹³ *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 270 (1995) (citing *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468, 474 (1989)).

¹¹⁴ Heinrich Kronstein, *Arbitration Is Power*, 38 N.Y.U. L. REV. 661, 699 (1963).

¹¹⁵ *Id.* at 700.

current trends in our society, the central concept of a social regime whose exclusive ordering is the totality of legislative and judicial mandates[] has been weakened by the cession of segments of the law to organized arbitration.”¹¹⁶ As one scholar has explained,

[D]enial of access to a court of law in most cases means exactly that—denial of access not merely to a court, or even to a jury, but to the law itself. . . . [A]rbitrators in most cases are not bound to follow the law, nor are their decisions appealable to a court of law for any but the most egregious of defects. Mere failure to follow the law is not such a defect. The result is that whatever the rules of law may be, arbitrators are not bound to follow them, and their handiwork is subject to only the most perfunctory of judicial oversight. Arbitrators of course may choose to follow the law—nothing requires them *not* to—but if they do, it’s not because they have any obligation to do so, and it’s not something that a litigant or her attorney can count on going in. Knowledgeable attorneys may have some sense of the approach that an arbitration panel is likely to take to a given type of case. Still, the arbitrators bring their own “law” with them, and they take it with them when they leave.¹¹⁷

It would seem that the *AT&T Mobility* case now prevents courts from conducting such a review of arbitration clauses. The teetering of the seesaw on the playground continues.

There are renewed suggestions that arbitration decisions should undergo a process of judicial review. First, and seemingly most simply, an arbitration agreement can include a provision that the award will be subject to judicial review. Of course, this may be an unlikely measure for both parties to agree on. But, if the arbitration agreement includes a requisite that the arbitrator follow the law, then it would seem that courts become empowered to review the award to assure that such has been done.¹¹⁸ Second, there is a growing call for a return to the process of judicial review by the courts, especially in view of the recent decisions

¹¹⁶ *Id.*

¹¹⁷ Knapp, *supra* note 81, at 782–83 (footnote omitted omitted).

¹¹⁸ See Christopher R. Drahozal, *Contracting Around RUAA: Default Rules, Mandatory Rules, and Judicial Review of Arbitral Awards*, 3 PEPP. DISP. RESOL. L.J. 419, 431–33 (2003).

990 VALPARAISO UNIVERSITY LAW REVIEW [Vol. 47]

of federal circuit courts regarding the scope of judicial review of arbitration awards.¹¹⁹

If there is a reversal of the current favoritism toward the finality of arbitration awards, that reversal must come from the legal system—either by the courts or through legislative action. It remains to be seen whether the judiciary is willing to take on a task that it seems to be diligently avoiding, or whether Congress is willing to meet the financial demands of returning to greater judicial involvement. The legal system must play together on the playground to protect the rights of the people. As it stands now under recent rulings by the U.S. Supreme Court, privatization is the name of the game, and fairness, it appears, be damned. The best take-away conclusion that can be offered at this point is this: Congress could seriously reconsider the FAA so as to preclude pre-dispute arbitration agreements, or the newly created Consumer Czar could propose administrative rules to be enacted by the Consumer Financial Protection Bureau that potentially may curb practices that adversely affect consumers.¹²⁰

The legal profession recognizes the need for safeguards in this unregulated dispute resolution arena called arbitration and has devised procedures to introduce a protective process so as to avoid a complete disregard of judicial review. The American Bar Association, National Association of Arbiters, and the American Arbitration Association have established protocols for arbitration, which could help with the privatization of dispute issues. Both the American Arbitration Association¹²¹ and the National Academy of Arbiters have annunciated due process procedures to be incorporated into the arbitration process.¹²² If properly implemented, these procedures will call into question certain unfair clauses in arbitration agreements, such as prohibitions on class actions, punitive damages, the admissibility of evidence, and publication of arbitration awards.

¹¹⁹ See generally Sarah Rudolph Cole, *Revising the FAA to Permit Expanded Judicial Review of Arbitration Awards*, 8 NEV. L.J. 214, 214 (2007).

¹²⁰ See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 2003-04 (2010) (to be codified at 12 U.S.C. § 5518(b) (2012)) (noting the congressional intent to restrict mandatory pre-dispute arbitration, among other things, under the Dodd-Frank Act).

¹²¹ The American Arbitration Association is a not-for-profit, private, public service organization that offers a broad range of dispute resolution services across the United States. *Why AAA/ICDR Administered Alternative Dispute Resolution*, AM. ARBITRATION ASS'N, www.adr.org (last visited Apr. 23, 2012).

¹²² The protocol can be found at the National Association of Arbiters. *A Due Process Protocol for Mediation and Arbitration of Statutory Disputes Arising out of the Employment Relationship*, NAT'L ACAD. OF ARBITRATORS, www.naarb.org/protocol.asp (last visited Apr. 23, 2012).

2013]

The Arbitration Seesaw

991

If the situation is left unaddressed, then we have returned to the days of fragmented law created by private arbitrators with nothing “common” about each decision. The current state of arbitration in the law is becoming more likened to that found before the creation of the Kings Bench, with local customs deciding civil disputes in complete disregard to uniformity or reliability. Until we are able to establish tangible and consistent protocol for arbitration clauses, all we can do is ask: King Henry II, where are’t thou?