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Sailing Around *Erie*: The Emergence of a Federal General Common Law of Arbitration

Professor Kenneth F. Dunham*

INTRODUCTION

Some legal scholars opine that the current law on arbitration agreements is a natural evolution of American contract law, while others are of the opinion that binding contractual arbitration is a violation of existing federal law.¹ The positions taken by the academic and the legal communities on arbitration have developed from the same factual events, case law, and statutes. This raises a question over how so many people could examine the same material and defend positions which are polar opposites? Paradise for some, yet purgatory for others, the binding pre-dispute arbitration clause evokes a night and day reaction depending upon who is polled.

Few legal scholars would argue that arbitration law in the United States today is totally different from arbitration law in the United States prior to 1925.² From colonial times until the passage of the United States Arbitration Act (USAA) in 1925, binding pre-dispute arbitration agreements

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1. For example, the work of two legal scholars yields opposite results. Professor Stephen Ware makes the evolution of law argument and has voiced his support of binding contractual arbitration in numerous law review and journal articles. STEPHEN WARE, *ALTERNATIVE DISPUTE RESOLUTION* (2001). He has also voiced his support of binding contractual arbitration in numerous law review and journal articles. Professor Jean Sternlight has written numerous articles criticizing the effects of binding contractual arbitration, especially in consumer cases. See Jean Sternlight, Address at the Roscoe Pound Institute 2003 Forum for State Court Judges: The Rise and Spread of Mandatory Arbitration as a Substitute for the Jury Trial (July 19, 2003). Professor Sternlight argues that arbitration is becoming a substitute for jury trials and interferes with access to justice by depriving claimants of their Seventh Amendment rights. *Id.*

2. Both of the above listed professors in their works and numerous other legal scholars in their contributions to the field agree that the American arbitration landscape in 1924 bore little resemblance to today's broadened picture of enforcement of nearly every kind of arbitration agreement. See WARE, *supra* note 1; Sternlight, *supra* note 1.

were considered unenforceable in most United States courts.³ One of the chief arguments against binding contractual arbitration is that Congress never intended the USAA to be more than a federal procedural act applicable only in the federal court system.⁴ Supporters of binding contractual arbitration argue that Congress actually intended the USAA to be substantive law applicable in all courts.⁵ Therefore, a historical perspective is critical when developing a position on this issue.

The USAA became codified in 1947, as Title 9 U.S.C. § 1, known as the Federal Arbitration Act (FAA).⁶ The federal cases in which the FAA is scrutinized may be placed into two general categories. Category one includes cases prior to the Supreme Court's 1984 decision in *Southland Corp. v. Keating*, which consistently held that the FAA was to be applied as a federal procedural act with judicial preference for its use.⁷ *Southland* held that the FAA was applicable in all courts as substantive law. Prior to *Southland*, the FAA was generally understood to be a federal procedural act applicable only in the federal courts.⁸

3. Prior to the enactment of the United States Arbitration Act in 1925, the vast majority of states followed the old common law arbitration doctrine of revocability. See IAN R. MACNEIL, *AMERICAN ARBITRATION LAW* (Oxford Univ. Press 1992). Professor MacNeil describes the American arbitration scene prior to 1925 in great detail. *Id.*

4. David H. Taylor and Sara M. Cliffe, *Civil Procedure by Contract: A Convoluted Confluence of Private Contract and Public Procedure in Need of Congressional Control*, 35 U. RICH. L. REV. 1085, 1098-1103 (2002). See also Justice O'Connor's dissent in *Southland Corp. v. Keating*, 465 U.S. 1 (1984).

5. See Chief Justice Burger's majority opinion in *Southland Corp. v. Keating*, 465 U.S. at 1.

6. Federal Arbitration Act, 9 U.S.C. §§ 1-14 (1947).

7. *Southland Corp. v. Keating*, 465 U.S. 1, 12 (1984). This case held that the FAA should no longer be considered a procedural act applicable only in federal courts, but was substantive law applicable in all courts. *Id.* at 16. Justice Burger opined in *Southland*,

In enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration. . . . The Federal Arbitration Act rests on the authority of Congress to enact substantive rules under the Commerce Clause Although the legislative history is not without ambiguities, there are strong indications that Congress had in mind something more than making arbitration agreements unenforceable only in the federal courts.

Id. at 10-12. Justice O'Connor dissented and argued that the FAA was a procedural act applicable only in federal courts. *Southland*, 465 U.S. at 25 (O'Connor, J., dissenting). Justice Rehnquist joined with Justice O'Connor in the dissent which stated in part, "[i]n 1925 Congress emphatically believed arbitration to be a matter of 'procedure' Today's decision is unfaithful to congressional intent, unnecessary, and in light of the FAA's antecedents and the intervening contraction of federal power, inexplicable." *Id.* at 36. The intervening contraction of federal power likely referred to the Court's presumed power to decide general law before *Erie*. *Southland* became the seminal case on federal preemption of state law by the FAA under the Supremacy Clause.

8. *Southland*, 465 U.S. at 25-26 (O'Connor, J., dissenting).

Thus, category two includes cases decided after 1984, in which the federal courts consistently held that the FAA is substantive law and therefore preempts contrary state law under the Supremacy Clause.⁹

Southland's critics have charged that it has led to a body of federal general common law of arbitration which is theoretically prohibited by the holding in *Erie Railroad Co. v. Tompkins*.¹⁰ The view by proponents of binding contractual arbitration is that *Southland* was not a 180 degree turn from the high court's prior opinions on the effect of the FAA. *Southland* was the first case which clearly set forth the Commerce Clause position the Court had endeavored to take in earlier cases.¹¹ *Southland*, according to its supporters, was not an end run around the *Erie* principle, but a result of the *Erie* principle's application to existing federal law.¹²

This article postulates that reinterpretation of statutes from the bench is a not so rare an occurrence, especially in federal courts. The United States Constitution Article III, § 2 grants the Supreme Court and inferior federal courts the power to interpret federal statutes.¹³ The federal courts regularly interpret the intent of Congress in federal statutes; even though the statutes subject to judicial interpretation may have been in place for decades. Obviously, *Southland's* interpretation of the intent of Congress in 1925, when it passed the USAA/FAA, was not based on a consultation with the deceased original sponsors of the legislation, but rather on a careful examination of statutory language.¹⁴ Some of *Southland's* dissenters argue that the real harm in *Southland* lies in the fact that the Court changed

9. Perry v. Thomas, 482 U.S. 483 (1987).

10. *Southland*, 465 U.S. at 25-26 (O'Connor, J., dissenting). Justice O'Connor opined that the Court reinterpreted an existing procedural act (i.e., the FAA) to create substantive law, in order to usurp the *Erie* Doctrine. See also *Erie R.R. Co. v. Tompkins*, 304 U.S. 64, 80 (1938). The principle holding in *Erie* was that in federal courts except when a matter is governed by the U.S. Constitution or a federal statute, the law to be applied is the law of the state. *Id.* at 78. The rationale behind the holding was that federal courts lacked the power to declare substantive rules through case law. *Id.* Hence, the conclusion reached in *Erie* was that federal general common law does not exist. *Id.*

11. In earlier cases the Supreme Court wrestled with the relationship between state law and the FAA, but never concluded that the FAA was substantive law. The Supreme Court's struggle with the federalism suggested by *Erie* is illustrated in *Bernhardt v. Polygraphic Co. of Am.*, 350 U.S. 198 (1956). The Supreme Court in *Bernhardt* made references to the federal law of arbitration, but declined to rule that the FAA preempted state law. *Id.* at 205; see also JOHN S. MURRAY, ALAN SCOTT RAU & EDWARD F. SHERMAN, *ARBITRATION* 55-56 (1996).

12. The supporters of arbitration have argued that *Erie* actually helped the Supreme Court to move toward the holding in *Southland*. See WARE, *supra* note 1, at 28-30.

13. U.S. CONST. art. III, § 2.

14. *Southland*, 465 U.S. at 10-14.

existing law from the bench.¹⁵ Some of these dissenters were on the *Southland* Court and voiced their opposition in *Southland*.¹⁶

The following pages contain a brief discussion of the history of arbitration in the United States, followed by a history of the FAA, and a discussion of the intent behind the original USAA in 1925. This article postulates that the Court opinions prior to *Southland* in favor of arbitration allowed the Court majority in *Southland* to avoid the limitations of the *Erie* principle against creating a body of federal general common law through interpretation and clarification of the intent of Congress. Although prior federal court decisions did not hold that federal procedural law was substantive law applicable in state courts, the language in several older Supreme Court opinions indicates the high court has been troubled for many years by such issues as state court forum shopping.¹⁷ Through analysis of *Southland's* progeny, this article contends that *Southland* was not a surprise holding, but a holding consistent with a pattern of movement by federal courts away from federal procedure status toward substantive law status for the FAA.

I. ADDRESSING THE *ERIE* PROBLEM

There is a handlebar shaped pile of rocks at the entrance to the Marina Del Rey yacht basin not shown on most Los Angeles city maps. At the ocean end of the Marina Del Rey channel a massive collection of boulders serves as a breakwater jetty. Yachtsmen sailing into or out of Marina Del Rey must sail around this barrier in order to arrive at their destination. The skilled sailor does not sail into the rocks, but tacks to change direction thereby avoiding them. Established legal principles are sometimes like this jetty, because rock solid legal principles sometimes act as barriers to progress. When progress is needed, those outdated principles can be sailed around by skilled members of the judiciary employing analytical tools to interpret old statutes in a new light. This is not an unfair or even unusual method of gaining access to the desired destination.

15. *Southland*, 465 U.S. at 33-36 (O'Connor, J., dissenting).

16. *Id.* at 21-36.

17. *Guaranty Trust Co. v. York*, 326 U.S. 99, 104-05 (1945). This case held that federal courts cannot "create" substantive rights denied by state courts in diversity cases, and cannot deny substantive rights created by state law in accordance with *Erie*. *Id.* at 106. The outcome in federal court or in state court should be the same under *Erie*; federal courts cannot allow plaintiffs to forum shop between courts depending upon the outcome they desire. *Id.* at 109. In diversity cases the same outcome must be available in state courts and federal courts, and this is accomplished by following the state statutes. *Id.*

In 1938, the Supreme Court held in *Erie Railroad Co. v. Tompkins* that “[e]xcept in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the state.”¹⁸ *Erie* was intended to act as a complete barrier to federal courts from attempting to legislate from the bench when navigating diversity cases.¹⁹ *Erie* allegedly forced those courts to follow state law.²⁰ Prior to *Erie*, federal courts were free to chart their own course in diversity cases, even if that course ignored the public policies of the states.²¹ Post *Erie*, federal courts, at least theoretically, could no longer craft decisions that ignored state law principles in diversity cases to create a body of federal general common law in a subject area.²²

Erie's purpose was to force federal courts to consistently apply state substantive law and federal procedural law in diversity removal cases.²³ However, the *Erie* principle has never been an ironclad doctrine applicable in all cases at all times.²⁴ The survival of removal actions in federal courts usually depends upon state law principles,²⁵ but federal common law controls the interpretation of federal statutory intent.²⁶ *Erie* was never intended to bar federal courts in diversity cases from interpreting existing federal statutes. Its purpose was to stop federal courts from creating new federal law that ignored existing state law principles when the case was based upon state law. A general state choice-of-law clause within an arbitration agreement does not force FAA mandates to yield to state law, because agreements to arbitrate are controlled by a federal statute not state law.²⁷ Therefore, even under the *Erie* principle, state law cannot bar binding arbitration under the FAA.²⁸

18. *Erie R.R. Co.*, 304 U.S. at 78.

19. *Id.*

20. *Id.*

21. *Id.*

22. *Erie R.R. Co.*, 304 U.S. at 78.

23. *Gasperini v. Ctr. for Humanities, Inc.*, 518 U.S. 415, 426 (1996). Under the *Erie* doctrine, federal courts sitting in diversity apply state substantive and federal procedural law.

24. *Hill v. Martinez*, 87 F. Supp. 2d 1115 (Colo. 2000) (State law controls in federal diversity cases unless it is inconsistent with the U.S. Constitution).

25. *Caine v. Hardy*, 943 F.2d 1406 (5th Cir. 1991) (en banc), cert. denied, 112 S. Ct. 1474 (1992). Survival of some federal actions depends upon the state laws of the state in which the federal court sits. *Id.*

26. *United States v. NEC Corp.*, 11 F.3d 136 (11th Cir. 1993).

27. *Sovak v. Chugai Pharm. Co.*, 280 F.3d 1266 (9th Cir. 2002).

28. *Mago v. Shearson Lehman Hutton, Inc.*, 956 F.2d 932 (9th Cir. 1992). State adhesion laws cannot nullify an agreement to arbitrate under the FAA. *Id.*

Southland and subsequent, opinions interpreting the FAA have resulted in a body of federal substantive law regarding arbitrability.²⁹ This body of federal law preempts state law even if the contract containing the arbitration clause purports to be governed by state law. Thus, for all practical purposes, state law has been ousted from the arbitration arena by coupling the FAA with the Commerce Clause. It is necessary to understand the history of binding arbitration agreements in the United States and additionally understand the history of the FAA in order to understand the current state of arbitration law in the United States.

II. THE HISTORY OF PRE-DISPUTE BINDING ARBITRATION IN THE UNITED STATES

The idea of a general common law developed early in the recorded history of England.³⁰ It was brought to the colonies by the English, and this common law was incorporated into the body of United States law.³¹ Common law probably originated from the solidification of customs into case law.³² English monarchs were not concerned with the needs and interests of commoners, so the common law served as a safety net for public freedom.³³ Under King Henry II, court decisions were written down and filed under various categories for future reference.³⁴ A filing system allowed future judges to review prior decisions in the same category of law, and the case collection developed into binding precedents, or *stare decisis*. English courts rarely reconsidered issues of a similar nature.³⁵ Once a recognized case set forth a principle to be followed, most judges followed the *stare decisis*, even if they might personally wish to do otherwise.³⁶

Common law and arbitration have a long and somewhat adversarial relationship.³⁷ In fact, the purpose of the FAA as set forth in *Southland* was to overcome judicial hostility to arbitration as a process of resolving

29. *Hatzlachh Supply Inc. v. Moische's Elecs., Inc.*, 828 F. Supp. 178 (S.D.N.Y. 1993). Although state law applies to contracts to arbitrate to determine if the parties agreed to arbitrate, there is a body of federal substantive law created by the FAA governing arbitrability of disputes.

30. Julie S. Rial, *Origins of Common Law*, *International Encyclopedia of Justice Studies* (Dec. 2002) available at http://www.iejs.com/Law/origins_of_common_law.htm.

31. *Id.*

32. *Id.*

33. Edward L. Glasser & Andrei Shleifer, *Legal Origins*, Yale Law School, Economics and Organization Workshop, 23 (2002).

34. *Understanding Common Law, Sovereign Services* (1994), <http://www.buildfreedom.com>.

35. *Id.*

36. *Id.*

37. *EEOC v. Waffle House, Inc.*, 534 U.S. 279 (2002). There has been a long standing hostility between courts and arbitration. *Id.*

disputes.³⁸ Until recent years, American courts generally viewed arbitration with suspicion.³⁹ Federal decisions ordering arbitration to replace jury trials, when an underlying contract contains a pre-dispute contractual arbitration clause, have resulted in negative feelings about the use of arbitration in consumer cases within the plaintiff's bar.⁴⁰ Some consumer groups have purchased billboards and personified arbitration as an evil personage that robs average consumers of their due.⁴¹

Arbitration is not a thief. Arbitration is not a person. Arbitration is a conflict resolution process used to resolve disputes that resembles a bench trial. There is not much mystery in the process. Arbitration has been around for centuries and has been used all over the world to resolve conflicts.⁴² In the 17th Century, English courts held arbitration was a non-binding process.⁴³ The English courts became concerned that arbitration had the potential to displace or oust the court's role in society.⁴⁴ Through a series of court decisions limiting the effect of arbitration, the English courts began to view arbitration as a non-binding process based upon the principle of agency revocability.⁴⁵ The English reversed their position on binding arbitration in 1889, but American courts continued down the old common law path.⁴⁶ The

38. *Id.*

39. *Id.*

40. *See id.* Jere Beasley, an Alabama trial attorney, publishes a monthly newsletter in which he uses a negative traffic symbol to portray arbitration. The Jere Beasley Report, *available at* http://www.beasleyallen.com/jlb_report/arbitration.htm. The symbol is a circle containing the word "arbitration" with a line drawn through it diagonally. *Id.*

41. Alabama highway billboards sponsored by a "grass roots" consumer movement against arbitration personify arbitration as a thief who steals rights: "Arbitration Steals Your Right To A Jury Trial."

42. LEONARD L. RISKIN, *DISPUTE RESOLUTION AND LAWYERS* 503 (1997). Nearly all-ancient civilizations record the use of arbitration. Moses used arbitration during the Exodus. The Romans and Greeks used the process in connection with their court systems. In the Middle Ages it was used in the European guild system to resolve disputes. Arbitration was present in English common law and was brought to America by the colonists. George Washington used arbitration to resolve Virginia land. In *Vynior's Case*, 77 Eng. Rep. 595 (K.B. 1609), Lord Coke opined that the English court's views of arbitration as revocable at will by the parties who had contracted to use it. *Id.* The rule set forth in *Vynior's Case* was that the arbitrators were agents of the parties, and the arbitrator's agency could be revoked by the parties at any time until an arbitration hearing had been held. *Id.* This became known as the revocability doctrine. A second reason to make arbitration revocable was the "ouster doctrine." Courts were afraid that arbitration would oust them from their jurisdiction over legal matters. *Id.*

43. *Id.*

44. *Id.*

45. *Id.*

46. The English Arbitration Act of 1889 made arbitration agreements irrevocable.

common law doctrine of revocability was followed by American courts until the enactment of the FAA in 1925.⁴⁷ The doctrine of revocability was grounded in the public law courts fear that they might be displaced by a private process of dispute resolution and thereby be put out of work.

The American judiciary's view of arbitration prior to the FAA was that the parties' pre-dispute contract to use arbitration, instead of the public courts, to resolve the dispute would result in an improper removal or ouster of the court's jurisdiction.⁴⁸ Some state statutes still follow the old common law view of arbitration. For example, Alabama's anti-pre-dispute arbitration statute, Ala. Code § 8-1-41 (3), follows the common law view of arbitration from the 18th and 19th centuries.⁴⁹ After the passage of the FAA in 1925, many states adopted modern arbitration statutes in order to align their state law with current federal law on arbitration, but other states like Alabama hung on to its old laws. From American Colonial times until 1925, several state statutes and the greater body of American case law held binding pre-dispute contractual arbitration agreements to be unenforceable and revocable at will by the parties who contracted for arbitration.⁵⁰

III. THE HISTORY OF THE FEDERAL ARBITRATION ACT: NEW YORK ARBITRATION ACT TO *SOUTHLAND* AND BEYOND

On April 19, 1920, the State of New York enacted section 2386(f) Code of Civil Procedure, the New York Arbitration Act (NYAA). Today the NYAA has been expanded into Consolidated Laws of New York, which makes contractual arbitration agreements binding in New York.⁵¹ In 1924, the United States Supreme Court decided *Atlantic Fruit Co. v. Red Cross Line*. The Court held that the New York Arbitration Act could be used to

47. *Tobey v. County of Bristol*, 23 Fed. Cas. 1313 (No. 14065) (C.C.D. Mass. 1845). A Massachusetts court refused to order specific performance of an arbitration agreement contained in a public works contract. *Id.* The *Tobey* court stated it was impractical to use equity to order arbitration and the plaintiff should exercise the legal remedies available. *Id.* In *Home Insurance Company of New York v. Morse*, 87 U.S. 445 (1874), the United States Supreme Court held pre-dispute agreements to arbitrate were invalid due to the common law revocability of such agreements. *Id.*

48. KATHERINE V.W. STONE, *ARBITRATION LAW* 2-3 (Foundation Press 2003); KATHERINE V.W. STONE, *PRIVATE JUSTICE, THE LAW OF ALTERNATIVE DISPUTE RESOLUTION* 305 (Foundation Press) (2003); *Vynior's Case*, 77 Eng. Rep 595.

49. ALA. CODE § 8-1-41(3) (1975).

50. *The Birmingham News Co. v. Horn*, 901 So. 2d 27 (Ala. 2004). Under common law pre-dispute and post-dispute arbitration agreements were considered revocable at will by the parties involved, if either desired to back out of the agreement prior to an arbitration hearing. The FAA makes such agreements enforceable.

51. N.Y., C.P.L.R. 7500 *et. seq.* The consolidated laws of New York are the latest version of the New York Arbitration Act.

enforce specific performance of a contract to arbitrate, but it could not be used as a complete bar to litigation.⁵²

Following hearings that hashed and re-hashed the nature of the FAA, the United States Congress failed to vote on the first version of a federal arbitration statute in 1922. The proposed statute was withdrawn and amended by its supporters and the American Bar Association and resubmitted to Congress in 1924.⁵³ It was enacted as the United States Arbitration Act (USAA) on February 12, 1925.⁵⁴ The language of the USAA was principally patterned after the language of the NYAA, but contained some significant changes.⁵⁵ The USAA was eventually codified as the United States Federal Arbitration Act (FAA), Title 9 of the United States Code, on July 30, 1947. The hearings held prior to the original enactment of the USAA in 1925, did not indicate that the act would be binding on state courts.⁵⁶ In fact, the FAA did not contain so much as a sentence fragment granting federal jurisdiction in arbitration cases.⁵⁷

According to Professor Ian MacNeil's book, *American Arbitration Law: Reformation-Nationalization-Internationalization*, there were a number of organizations across the United States that endeavored to promote binding arbitration in the late 1800s and early 1900s.⁵⁸ The American Bar Association (ABA) got behind these efforts and spear-headed the movement to get a national arbitration act to Congress.⁵⁹ However, due to some objections to the first draft of the USAA, the ABA withdrew and revised the

52. DONALD J. KENNEDY, *MARITIME ARBITRATION 1899-1999* (2003). Although the New York Arbitration Act promised to overcome the longstanding judicial hostility regarding arbitration, its initial test in the court, *Atlantic Fruit Co. v. Red Cross Line*, 264 U.S. 109 (1924), held that the New York statute was an available remedy to enforce a contract, but not a bar to litigation.

53. IAN R. MACNEIL, *AMERICAN ARBITRATION LAW: REFORMATION, NATIONALIZATION, INTERNATIONALIZATION* 42 (1992). Professor MacNeil traces the history of arbitration in America through the 19th and 20th Centuries. *Id.* He includes the beginning of the movement to change arbitration law from holding arbitration agreements unenforceable to holding them enforceable in federal courts. *Id.* He traces the history of the FAA from the efforts of a few to the push by the ABA to get the act through Congress. *Id.* He discusses the impact of *Southland* and moves on to discuss international arbitration and the New York Convention. *Id.* MacNeil criticizes the *Southland* Court for ignoring the history of the FAA and transforming the act into a different kind of law than the one envisioned by its drafters. *Id.* Although MacNeil's conclusions about the FAA have been challenged by some scholars, his historical digest of the FAA's early years is without equal. *Id.*

54. *Id.* at 47.

55. *Id.* at 52.

56. *Id.* at 117-18.

57. 9 U.S.C.A. § 1 et. seq.

58. MACNEIL, *supra* note 53.

59. *Id.* at 48.

USAA and resubmitted it to Congress.⁶⁰ The revised draft was eventually passed in virtually the same form as it exists today.⁶¹

Following its passage in 1925, the USAA was used in federal courts, if a binding pre-dispute arbitration contract clause was present in a federal case.⁶² Federal courts refused to order arbitration under the USAA if the matter was litigated in a state court, before being removed to the federal court on diversity grounds.⁶³ This was due at least in part to the *Erie* doctrine's state law application mandates. Following *Southland* the references in the case law to *Erie* all but disappeared, and federal courts now routinely cite section two of the FAA, placing arbitration agreements in any court "upon the same footing as other contracts."⁶⁴

There is no specific language in the FAA that states there is a federal policy in favor of arbitration which preempts contrary state law.⁶⁵ The federal policy favoring arbitration language came from *Moses H. Cone Memorial Hospital v. Mercury Construction Company* and was confirmed and expounded upon by the United States Supreme Court in *Southland*.⁶⁶

Southland, using the Commerce Clause and the Supremacy Clause as bridges, harmonized the outcome of arbitration under the FAA with the outcome of arbitration under state law.⁶⁷ While the *Erie* doctrine was discussed in arbitration cases prior to *Southland*, such as *Bernhardt v. Polygraphic Company of America*, federal courts declined to disturb the perceived procedural status of the FAA until *Southland*.⁶⁸ Although the

60. *Id.* at 91-101.

61. *Id.*

62. *Id.* at 107.

63. MACNEIL, *supra* note 53.

64. *HIM Portland, LLC v. DeVito Builders, Inc.*, 317 F.3d 41, 43 (2003) (Justice Torruella wrote, "Congress enacted the FAA to place arbitration agreements upon the same footing as other contracts and to render them valid, irrevocable and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.")

65. 9 U.S.C.A. § 1 et. seq.

66. *See Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1 (1983); *see also Southland*, 465 U.S. at 1 ("In enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration. . . . The Federal Arbitration Act rests on the authority of Congress to enact substantive rules under the Commerce Clause. . . . Although the legislative history is not without ambiguities, there are strong indications that Congress had in mind something more than making arbitration agreements enforceable only in the federal courts.")

67. *Id.*; Justice Brennan cited "the statutory policy of rapid and unobstructed enforcement of arbitration agreements." *Id.* at 22-23. He further stated "any doubts should be resolved in favor of arbitration." *Id.*

68. *Bernhardt v. Polygraphic Co. of Am, Inc.*, 350 U.S. 198 (1956). *Bernhardt* entered into an employment contract containing an arbitration clause in New York. *Id.* *Bernhardt* later moved to Vermont, and performed his duties under the employment contract in Vermont. *Id.* *Bernhardt* was

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early arbitration cases acknowledged the problem of state versus federal court forum shopping, they did not correct the problem because they viewed the FAA as procedural.⁶⁹

The state court ruling in *Southland* followed the general understanding of the time between state law and the FAA.⁷⁰ The California Supreme Court's ruling in *Southland* closely followed the principles enunciated by the United States Supreme Court in 1956, in *Bernhardt*.⁷¹ *Bernhardt* viewed the FAA as a procedural statute.⁷² *Bernhardt* confirmed the principle of eliminating forum shopping by stating the same result should be obtained in state and federal courts as had been previously enunciated in *Guaranty Trust Co. v. York*.⁷³ Therefore, the trial court's ruling in *Southland* followed the prevailing law in pre-*Southland* arbitration cases, but treated the FAA as a substantive law act using a broad interpretation of "affecting commerce."

IV. LOCATING THE ORIGINAL INTENT OF CONGRESS: COUPLING THE FAA AND THE COMMERCE CLAUSE AND ATTACHING BOTH TO THE SUPREMACY CLAUSE

At the time *Southland* was decided, some states had statutes making the enforcement of arbitration agreements illegal as a matter of public policy.⁷⁴ Since *Southland*, the United States Supreme Court has consistently held that the Commerce Clause, as it applies to FAA sanctioned arbitrations, must be interpreted broadly so as to apply to state court actions affecting

fired by Polygraphic Company of America, Inc., while working in Vermont. *Id.* He brought a lawsuit against Polygraphic in a Vermont state court, and Polygraphic removed it to federal district court. *Bernhardt*, 350 U.S. at 198. The U.S. District Court denied Polygraphic's motion to compel arbitration due to the *Erie* doctrine requirement of following state law in cases removed on diversity grounds. *Id.* at 200. Justice Douglas wrote the majority opinion which remanded the case to the federal district court in Vermont to determine which state law, Vermont or New York, applied to *Bernhardt*'s case. *Id.* at 199. Justice Douglas opined that *Erie R.R. Co. v. Tompkins* required the case to be decided by local law. *Id.* Justice Douglas based the court's treatment of *Bernhardt* on principles set forth in *Guaranty Trust Co. v. York*, 326 U.S. 99 (1945), and stated "If the federal court allows arbitration where the state court would disallow it, the outcome of the litigation might depend on the courthouse where suit is brought." *Id.* at 203.

69. *Bernhardt*, 350 U.S. at 206-08 (Frankfurter, J., concurring) Justice Frankfurter's concurring opinion in *Bernhardt* concluded that the FAA was tied to U.S. Constitution Article III, Section 2 and "does not obviously apply to diversity cases." *Id.* at 208.

70. *Id.*

71. Compare *Bernhardt*, 350 U.S. at 204, with *Southland*, 465 U.S. at 1.

72. *Bernhardt*, 350 U.S. at 203.

73. *Guaranty Trust Co.*, 326 U.S. at 99.

74. See ALA. CODE 8-1-41(3); see also WARE, *supra* note 1.

interstate commerce.⁷⁵ The United States Supreme Court has also made it clear that the Supremacy Clause preempts any contrary state statute that conflicts with the FAA, because the FAA clearly expresses the intent of Congress to enforce arbitration agreements to the full reach of the Commerce Clause.⁷⁶

For nearly sixty years the United States Supreme Court, in apparent compliance with *Erie*, held that state law should be applied to arbitration agreements in state courts.⁷⁷ Cases prior to *Southland* narrowly construed the meaning of interstate commerce, and thus narrowly construed the applicability of the FAA. This narrow view of commerce coupled with the *Erie* doctrine forced federal courts to apply state law in diversity cases like *Bernhardt*. *Erie* was pure federalism. Therefore, *Southland* was seen as inconsistent with federalism, although it was rendered by a Court supportive of federalism principles.⁷⁸ Justice O'Connor and Justice Rehnquist's dissenting opinion is indicative of the federalist's critique of *Southland*.

Professor Stephen Ware opines that the federal courts were able to separate the procedural from the substantive when applying the *Erie* doctrine.⁷⁹ The Supreme Court then took a serious look at upholding arbitration clauses through a series of cases.⁸⁰ Federal courts used their own rules and procedures, if a case was removed from a state court to a federal court, but avoided using their decisions to create federal substantive law in state court cases.⁸¹ The problem with this approach was that if various state arbitration laws were applied in removal cases it could encourage forum shopping.⁸²

Southland addressed the forum shopping problem by preempting state law. The United States Supreme Court in *Southland* interpreted the statutory intent of *Southland* under the Commerce Clause and enforced arbitration agreements in state courts with a Supremacy Clause argument.⁸³ When *Southland* interpreted the FAA as a substantive law act which furthered the Congressional intent of the Commerce Clause, it extended the reach of the

75. *Citizens Bank v. Alafabco, Inc.*, 539 U.S. 52, 56-58 (2003).

76. *Perry v. Thomas*, 482 U.S. 483 (1987).

77. David S. Schwartz, *Mandatory Arbitration: Correcting Federalism Mistakes in Statutory Interpretation: The Supreme Court and the Federal Arbitration Act*, 67 LAW & CONTEMP. PROBS. 5 (2004). Professor Schwartz addresses the impact of *Southland* on *Erie*. He concludes that *Southland* was not a good decision when it was made, but the Supreme Court has been unwilling to overrule its own precedent in *Southland*. *Id.*

78. *Id.* at 54.

79. WARE, *supra* note 1, at 54.

80. *Id.*

81. *See Bernhardt*, 350 U.S. at 198.

82. *Id.*

83. *Southland*, 465 U.S. at 1.

FAA into state courts.⁸⁴ State law could never be preempted by a federal procedural law, but state law could be preempted by a federal substantive law act under the Supremacy Clause.

V. PRECEDING CASES THAT SET THE STAGE FOR *SOUTHLAND*

The first significant departure from ordinary contract law governing contractual arbitrations came in the 1967 case of *Prima Paint v. Flood & Conklin Manufacturing Co.*⁸⁵ *Prima Paint* required federal courts to give special consideration to pre-dispute arbitration clauses in regular contracts.⁸⁶ The requirement of a special examination of arbitration clauses became known as the separability doctrine.⁸⁷ It required federal courts to separate the arbitration clause from its so-called container contract for examination.⁸⁸ Arbitration clauses were to be carved out and examined on their own merits.⁸⁹ *Prima Paint* required courts to determine if the arbitration clause itself was under attack or if the contract as a whole was being challenged. If the contract as a whole was alleged to be void *ab initio*, then the case would be sent to arbitration where the arbitrator(s) would decide the issues.⁹⁰ If the arbitration clause itself was challenged, then courts would decide if the parties had agreed to arbitrate, and if arbitration was appropriate.⁹¹ This

84. *Id.*

85. *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967). *Prima Paint* filed suit to rescind the entire contract with Flood & Conklin, including the arbitration clause, based on fraud in the inducement of the contract as a whole. *Id.* at 399. The federal district court stayed the case and sent the matter to arbitration. The United States Supreme Court affirmed. *Id.* Tying the contract to interstate commerce instead of state contract law, the United States Supreme Court expressed what has become known as the “separability doctrine.” An allegation of fraud in the inducement of the contract as a whole will be decided by the arbitrators, unless the parties specifically withheld that issue from arbitration. *Id.* The *Prima Paint* Court ruled that arbitration clauses are separable from the contract in which they are embedded. *Id.* Citing Section 4 of the arbitration clause, the courts may adjudicate it, but if there is a claim of fraud against the contract as a whole that claim will be arbitrated. *Prima Paint*, 388 U.S. at 399. In a motion opposing a stay, a federal court may only examine issues relating to the arbitration clause itself to determine the validity of the stay. *Id.*

86. *Id.* at 395-402.

87. *Id.* at 402-03, 411.

88. *Id.* at 402-03.

89. *Id.* at 403.

90. *Prima Paint*, 388 U.S. at 403.

91. *Id.* at 404.

“special” analysis went well beyond placing arbitration clauses on the same footing as other contracts.⁹²

This case was the beginning of elevated status in federal courts for contractual pre-dispute arbitration clauses, because *Prima Paint* gave pre-dispute arbitration agreements a unique status in contract law.⁹³ Pursuant to *Prima Paint*, federal courts allow immediate review of orders denying arbitration, but disallow immediate appellate review of orders granting arbitration.⁹⁴ Federal courts therefore treat arbitration agreements differently from other contracts.⁹⁵ Courts that review arbitration awards do not review the awards based upon general contract principles, but the standards of review are limited to those set forth in the FAA.⁹⁶

The second major step on the path to *Southland* came in the 1983 United States Supreme Court case of *Moses H. Cone Memorial Hospital*.⁹⁷ In *Moses H. Cone*, the Court declared a “liberal federal policy” favoring arbitration, holding that §2 of the FAA created a body of “federal substantive law of arbitrability.”⁹⁸ Although *Moses H. Cone* involved a controversy over the issuance of a stay in a federal lawsuit until the state law claims had been resolved, its language regarding arbitration would resurface

92. CHRISTOPHER R. DRAHOZAL, COMMERCIAL ARBITRATION: CASES AND PROBLEMS, 54 (2002).

93. *Id.* at 403-04.

94. *South Louisiana Cement, Inc. v. Van Aalst Bulk Handling, B.V.*, 383 F.3d 297, 300-01 (La. 2004). Interlocutory appeals from an order denying arbitration are “final” and thus appealable, but appeals from an order compelling arbitration are not appealable on an interlocutory basis.

95. *Caley v. Gulfstream Aerospace Corp.*, 333 F. Supp. 2d 1367, 1374 (N.D. Ga. 2004). Motion to compel arbitration in a class action based upon Fair Labor Standards Act was granted. Arbitration clauses are not reviewed using the same standards as other contracts.

96. *Wyman-Gordon Co. v. United Steel Workers of America*, 337 F. Supp. 2d 241, 244 (Mass. 2004).

97. *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 1. *Moses H. Cone Memorial Hospital*, a North Carolina medical facility, contracted with Alabama contractor Mercury Construction Corporation for additions to its physical plant. *Id.* The hospital drafted the contract between the two businesses, and the contract contained an arbitration clause. *Id.* Following disagreements over construction delays and money issues, unsuccessful attempts at negotiation were followed by a declaratory judgment action filed by the hospital in a North Carolina state court. *Id.* The state court issued an injunction against arbitration, but rescinded the order upon protest by Mercury Construction. *Id.* After the stay was lifted, Mercury Construction filed a lawsuit in federal district court and moved to compel arbitration the federal district court stayed the federal case until resolution of the state court case. *Id.* The U.S. Court of Appeals for the Fourth Circuit reversed the federal district court and remanded the case for arbitration. *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 1-2. The United States Supreme Court affirmed the Fourth Circuit, and in doing so used the language that would soon become commonplace in federal arbitration cases. *Id.* at 2. Relying on the Commerce Clause argument for enforcement of arbitration, and citing both FAA Section 2 and *Prima Paint*, the Court spoke of a “federal policy favoring arbitration.” *Id.* at 24.

98. *Id.* at 24.

in *Southland* as explaining the federal policy in favor of arbitration.⁹⁹ *Moses H. Cone* also paved the way for the holding in *Southland* because it enunciated a federal policy in favor of arbitration by using a Commerce Clause argument.¹⁰⁰ The special contract analysis required under *Prima Paint* and the favoritism enunciated in *Moses H. Cone*, in some ways “telegraphed the punch” of the Supreme Court in *Southland*.¹⁰¹

VI. THE ACADEMY SPEAKS OUT ON *SOUTHLAND*: WHAT OTHERS HAVE SAID

The shift in the High Court’s preference for arbitration did not go unnoticed by legal scholars.¹⁰² While there is no general consensus among legal scholars on the rationale or effect of *Southland*, legal scholars appear to locate themselves within or near two distinct camps regarding the *Southland* opinion: *Southland* is good law or *Southland* is bad law. Some scholars, like Professor Jean Sternlight have questioned the Supreme Court’s reasoning in *Southland*,¹⁰³ while others like Professor Richard Reuben have explored the impact of this shift on the way state courts treat contractual arbitration clauses.¹⁰⁴ Professor Stephen Ware and others have defended *Southland* and the United States Supreme Court’s current position on arbitration.¹⁰⁵ One of the leading critics of *Southland* has been Professor Ian MacNeil, whose book *American Arbitration* provides an in-depth analysis of the legislative history of the FAA.¹⁰⁶ Professor Christopher Drahozal,

99. Schwartz, *supra* note 77, at 35.

100. *Id.* at 35-37.

101. *See id.* at 35-37.

102. See Jean R. Sternlight, *Rethinking the Constitutionality of the Supreme Court’s Preference for Binding Arbitration: A Fresh Assessment of Jury Trial, Separation of Powers and Due Process Concerns*, 72 TUL. L. REV. 1 (1997). See also Jean R. Sternlight, *Mandatory Binding Arbitration and the Demise of the Seventh Amendment Right to a Jury Trial*, 16 OHIO ST. J. ON DISP. RESOL. 669 (2001), and Jean R. Sternlight, *Panacea or Corporate Tool?: Debunking the Supreme Court’s Preference for Binding Arbitration*, 74 WASH. U.L.Q. 637 (1996). Professor Sternlight remains one of binding arbitrations most vocal critics regarding access to justice issues.

103. *See id.*

104. See Richard C. Reuben, *Public Justice: Toward a State Action Theory of Alternative Dispute Resolution*, 85 CAL. L. REV. 577 (1997). Professor Reuben has questioned the impact of binding arbitration under the FAA on other areas of law.

105. Stephen J. Ware, *Contractual Arbitration, Mandatory Arbitration, and State Constitutional Jury Trial Rights*, 38 U.S.F. L. REV. 39 *passim* (2003). Professor Ware defends arbitration clauses because people have a right to contract, and that right should not be denied. *Id.*

106. MACNEIL, *supra* note 53.

supports *Southland's* outcome as the correct decision, even though the Court's reasoning may have been flawed.¹⁰⁷ In Professor Drahozal's view, the majority in *Southland* may have used weak analysis, but the correct conclusion was reached.¹⁰⁸ Still other scholars like Professor Reuben question the long-term impact of *Southland* on other areas of the law like individual rights.

VII. THE PRIMARY EFFECT OF *SOUTHLAND* ON THE LEGAL SYSTEM: PREEMPTION OF STATE ANTI-ARBITRATION LAWS

Federal courts rely on the Supremacy Clause to preempt state anti-arbitration laws and uphold the power of Congress under the Commerce Clause to enforce the mandates of the FAA.¹⁰⁹ In *Southland*, the Supreme Court held that Congress in 1925 had intended that the FAA be a substantive law act enforcing the Commerce Clause in all courts, and had never intended the FAA to be limited to Article III procedural matters.¹¹⁰ *Southland* resolved the continuing conflict between state and federal arbitration law by using the Supremacy Clause and the Commerce Clause as applied to the FAA to nullify the effect of state anti-arbitration laws.¹¹¹

Although the *Southland* argument under Commerce Clause was persuasive for a majority of the court, the dissenting opinions of Justice Stevens, Justice Rehnquist and Justice O'Connor in *Southland* pointed out the fact that the FAA's history was purely procedural.¹¹² Justice Rehnquist and Justice O'Connor's review of congressional hearings preceding the FAA concludes that Congress never intended for the FAA to become a substantive law act.¹¹³ Since members of Congress who held these hearings prior to the FAA's passage can no longer be called upon to explain their intent in passing the FAA, because they died years ago, there is a presumption argument on both sides of the issue.

The dissenting opinions in *Southland* seem to suggest *Southland's* true purpose was to establish a stare decisis favoring the use of arbitration

107. Christopher R. Drahozal, *In Defense of Southland: Re-examining the Legislative History of the Federal Arbitration Act*, 78 NOTRE DAME L. REV. 101 (2002) *passim*. See also Christopher R. Drahozal, *Revisiting Southland*, 10 No. 3 DISP. RESOL. MAG., 24 (Spring 2004)

108. *Id.*

109. Nathan E. Ross, *Federalism v. The Greater Good... Should Powerful Franchisors be Allowed to Contract for the Home Court Advantage Through Forum Selection Clauses?*, 2000 J. DISP. RESOL. 199, 212 (2000). The power given to Congress under the Constitution allows federal law to preempt contrary state law.

110. *Southland*, 465 U.S. at 11.

111. *Id.* See also *Guaranty Trust, Co.*, 326 U.S. at 99.

112. *Southland*, 465 U.S. at 17 (Stevens, J., concurring in part and dissenting in part).

113. *Southland*, 465 U.S. at 21-36 (O'Connor, J., dissenting).

agreements in contracts nationwide, rather than offering an interpretation of Congress' true intent, to enforce the Commerce Clause using the FAA.¹¹⁴ Perhaps the majority's interpretation of Congressional intent in *Southland* stretches the interpretative envelope, but it also accomplishes the goal of harmonizing the approach to arbitration in all American courts. Two of the major effects of *Southland* on the legal system have been to eliminate state court forum shopping in arbitration cases and uniting the legal system on a divisive issue.

Justice Stevens' dissent in *Perry v. Thomas* revisited the *Southland* opinion:

Even though the Arbitration Act had been on the books for almost 50 years in 1973, apparently neither the Court nor the litigants even considered the possibility that the Act had pre-empted state-created rights. It is only in the last few years that the Court has effectively rewritten the statute to give it a pre-emptive scope that Congress certainly did not intend.¹¹⁵

Justice Stevens viewed *Southland* as a rewriting of the FAA to make the statute substantive law so as to preempt state arbitration law.¹¹⁶ The *Southland* opinion thus created uniformity in the treatment of arbitration clauses, no matter which type of court was presented with a motion to compel arbitration.¹¹⁷

Southland led to cheers from the business community and jeers from the plaintiff's bar and consumer advocacy groups.¹¹⁸ The long-term effects of *Southland* on Constitutional issues such as access to justice and the waiver of the Seventh Amendment right to a jury trial are still in the refinement stage. However, there is no question that *Southland* has resulted in residual

114. *Id.*

115. *Perry v. Thomas*, 482 U.S. 483 (1987) (Stevens, J., dissenting). Justice Stevens' dissent in *Perry v. Thomas* compared the 1973 case of *Merrill Lynch, Pierce, Fenner & Smith v. Ware*, to *Perry*. *Id.*; see also *Merrill Lynch, Pierce, Fenner & Smith v. Ware*, 414 U.S. 117 (1973). He concluded that in those two cases, the same facts yielded different results, due to the Supreme Court's rewriting of the FAA in *Southland*. *Id.*

116. *Id.* at 493-94.

117. Schwartz, *supra* note 77, at 53.

118. See, e.g., Jean Sternlight, *Rethinking the Constitutionality of the Supreme Court's Preference for Binding Arbitration: A Fresh Assessment of Jury Trial, Separation of Powers, and Due Process Concerns*, 72 TUL. L. REV. 1 (1997) (exploring the issue of whether "arbitration agreements may unconstitutionally deprive persons of their right to a jury trial, to a judge and to due process of law"); see also Margaret L. Moses, *Privatized "Justice"*, 36 LOY. U. CHI. L.J. 535 (2005) ("depriving large numbers of consumers of access to our court system without their consent could not have been the intent of the drafters of the FAA.").

effects reaching across several areas of the law. The clarification of these effects will take time to fully develop.

VIII. THE *SOUTHLAND* PROGENY: STATE ARBITRATION LAWS DIE HARD

The next major state law preemption case following *Southland* was *Allied-Bruce Terminix Cos. v. Dobson*.¹¹⁹ Alabama Code section 8-1-41(3) declared pre-dispute arbitration clauses could not be specifically enforced in Alabama. In *Terminix*, the Supreme Court of Alabama interpreted *Southland* to hold that Congress' power to enforce the Commerce Clause under the FAA was limited to situations where the parties contemplated that interstate commerce would be substantially affected by their transaction.¹²⁰ After weighing the facts of *Terminix*, the Supreme Court of Alabama determined that the parties did not contemplate that interstate commerce would be substantially affected by a termite bond issued on Dobson's residence, and that the state anti-arbitration statute, Alabama Code section 8-1-41(3), applied.¹²¹ On appeal, the United States Supreme Court found the Supreme Court of Alabama's reasoning was based on too narrow an interpretation of term "affecting commerce," and held that the words "affecting commerce" should receive a very broad interpretation. The United States Supreme Court held that the transaction's actual effect on commerce, rather than the contemplation of the parties should determine whether the FAA applied.¹²² In *Terminix*, the United States Supreme Court held that pest control chemicals shipped across state lines to treat an individual's home substantially affected interstate commerce.¹²³

In addition to the language of FAA § 2, the language from *Southland* was generously used in *Terminix*. Justice Breyer stated in *Terminix* that "Nothing significant has changed in the 10 years subsequent to *Southland*; no later cases have eroded *Southland's* authority."¹²⁴ It is interesting that Justice Breyer referred to *Southland's* authority rather than the authority of the FAA. Justice O'Connor wrote in her concurrence, "Today's decision caps this Court's effort to expand the Federal Arbitration Act. Although each decision has built logically upon the decisions preceding it, the initial building block in *Southland* laid a faulty foundation."¹²⁵ Although *Terminix* may have presented the Court with a significant opportunity to limit or even

119. *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 282 (1995).

120. *Allied-Bruce Terminix Cos. v. Dobson*, 628 So. 2d 354 (Ala. 1993).

121. *Id.* at 357.

122. *Terminix*, 513 U.S. at 272-77.

123. *Id.* at 280-81.

124. *Id.* at 272.

125. *Id.* at 272.

overturn *Southland*, due to the head-on collision between the FAA and Alabama Code section 8-1-41(3) occurring in a state court, the United States Supreme Court stood by *Southland* and strengthened the federal policy favoring arbitration in *Terminix*.¹²⁶

There are at least two schools of thought regarding the impact of *Terminix* on state anti-arbitration laws: (1) the line of reasoning followed by the United States Supreme Court, and (2) the line of reasoning followed by the Supreme Court of Alabama. The *Terminix* opinion by the United States Supreme Court did not deter the Alabama Supreme Court from attempting to find some other way to uphold Alabama's public policy on pre-dispute arbitration agreements. In *Sisters of the Visitation v. Cochran Plastering Company, Inc.*, the Supreme Court of Alabama reasoned that Alabama Code section 8-1-41(3) was not declared unconstitutional by *Terminix*, but the application of the FAA to the facts in *Terminix* resulted in a transaction that substantially affected interstate commerce.¹²⁷ This interpretation led the Supreme Court of Alabama to devise a five-prong test to determine when commerce is substantially affected.¹²⁸ The test created a line of state-commerce-only cases governed by Alabama's anti-arbitration statute, and a parallel line of cases held to be substantially affecting interstate commerce governed by the FAA.¹²⁹

Part of the Alabama court's reasoning may have been a misunderstanding of the intent of the *Terminix* decision, but the public policy of Alabama, as expressed in Alabama Code section 8-1-41(3), probably played a major role in the establishment of the two streams of cases. Unlike federal judges who are appointed, Alabama's Supreme Court justices are elected. State Supreme Court justices answer in the ballot box to the citizens' assessment of their performance in upholding Alabama's laws.¹³⁰ They have a moral and ethical duty to follow the wishes of their constituency, but they also have a duty to follow the rule of law in their

126. *Id.*

127. *Sisters of the Visitation v. Cochran Plastering Co.*, 775 So. 2d 759 (2000). This case explains that in *Terminix*, "the United States Supreme Court held that for an arbitration clause to be enforceable under the FAA the transaction to which the contract relates must turn out, in fact, to involve interstate commerce, regardless of the contemplation of the parties." *Id.* at 760; *see also* *U.S. v. Lopez*, 514 U.S. 549 (1995) (a criminal case which extracted limiting language concerning the coverage of the Commerce Clause.)

128. *Sisters of the Visitation*, 775 So. 2d at 761.

129. *Id.*

130. *See* Stephen J. Ware, *The Alabama Story: Arbitration Shows Law's Connection to Politics and Culture*, DISP. RESOL. MAG., Summer 2000, at 24.

decisions. The Alabama Supreme Court endeavored to do both things with a new line of reasoning.

The Supreme Court of Alabama explained their new line of reasoning in *Sisters of the Visitation v. Cochran Plastering Company, Inc.*,¹³¹ an Alabama case which utilized the Commerce Clause limitation language contained in *United States v. Lopez*.¹³² The United States Supreme Court held in *Lopez* that Congress' power to enforce the Commerce Clause was not unlimited. *Lopez* was a school zone gun case that had nothing to do with arbitration, but everything to do with limiting the power of Congress under the Commerce Clause. In *Sisters of the Visitation*, the Supreme Court of Alabama used the holding in *Lopez* to construct a five-prong test to determine if the underlying transaction leading to the contract containing the pre-dispute arbitration clause substantially affected interstate commerce, thereby activating the FAA mandate to arbitrate.¹³³ If the facts of each case met all five-prongs of the *Sisters* substantial interstate commerce contracts test it was said to fall under the mandate of the FAA to arbitrate.¹³⁴ However, if the facts met only one or two of the prongs of the *Sisters* test it was governed by Alabama Code section 8-1-41(3), because the power of Congress to control commerce was not unlimited.¹³⁵

The second school of thought regarding the effect of *Terminix* on Alabama Code section 8-1-41(3) was enunciated in *Citizens Bank v. Alafabco, Inc.* by the United States Supreme Court.¹³⁶ *Alafabco* held that the words "involving commerce" should be given the broadest possible reading.¹³⁷ The interpretation of "involving commerce" set forth in *Alafabco* is the equivalent of "affecting commerce," and this definition does not allow the states much "wobble room" in drafting anti-arbitration statutes.¹³⁸ It is clear from *Alafabco* that the federal courts will enforce almost any arbitration clause under the FAA's mandate to arbitrate, and any contrary state law will be preempted.¹³⁹ In fact, *Alafabco* held that "Congress' Commerce Clause power 'may be exercised in individual cases without showing any specific effect on interstate commerce.'"¹⁴⁰

131. *Sisters of the Visitation*, 775 So. 2d at 761-65.

132. *United States v. Lopez*, 514 U.S. 549 (1995). A criminal case regarding the use of a gun within a prohibited zone. The case used limiting language under the Commerce Clause.

133. *Sisters of the Visitation*, 775 So. 2d at 774-79.

134. *Id.*

135. *Id.*

136. *Alafabco*, 539 U.S. at 56-59.

137. *Id.*

138. *Id.*

139. *Id.*

140. *Id.*

Alabama has been at the forefront of the *Southland* controversy, but other states have also failed to accept the FAA mandates until a few struggles highlighted the tension between state public policy and the FAA. Some states have attempted to limit or eliminate arbitration altogether, if certain conditions are not met.¹⁴¹ A Montana statute, for example, required any contract containing an arbitration clause to post a notice of the arbitration clause in bold letters on the front page of the contract to protect the unwary.¹⁴² However, the United States Supreme Court held in *Doctor's Associates, Inc. v. Casarotto*, the statute's notice requirement was unconstitutional because it placed arbitration on a different footing from other contracts.¹⁴³ A New York statute disallowed punitive damages in arbitration based upon a public policy against punitive damages in contract cases.¹⁴⁴ A contract containing an arbitration clause also contained choice of law language selecting New York law to govern the contract in *Mastrobuono v. Shearson Lehman Hutton, Inc.*¹⁴⁵ The arbitrators returned an award containing punitive damages contrary to New York law. Thereafter, the United States Supreme Court upheld the arbitrator's award of punitive damages based upon the contract itself not excluding punitive damages.¹⁴⁶ Thus, parties to an arbitration agreement may contract for potential arbitration awards that are contrary to state law.¹⁴⁷

Federal courts generally enforce state laws that support arbitration, even if those laws are not worded exactly like the FAA.¹⁴⁸ The federal courts

141. California and Montana have statutes that limit the use of arbitration, while Alabama Code section 8-1-41(3) prohibits enforcement of pre-dispute arbitration clauses.

142. MONTANA CODE ANN. 27-5-114(4).

143. *Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 687-89 (1996). The United States Supreme Court held that courts cannot enforce a state policy that places arbitration clauses on unequal footing with other contracts. Special notice requirements do not apply to other contracts in Montana, so special notice requirements could not be applied to arbitration clauses.

144. New York Civil Practice Act, as interpreted by *Garrity v. Lyle Stuart, Inc.*, 353 N.E. 2d 793 (N.Y. 1976).

145. *Mastrobuono v. Shearson Lehman Hutton Inc.*, 514 U.S. 52 (1995). The arbitrators granted punitive damages and the respondent appealed citing New York law's prohibition on punitive damages in arbitration awards. The United States Supreme Court allowed the punitive damages based upon the language of the underlying contract not excluding punitive damages.

146. *Id.* at 58.

147. *Id.*

148. *See Volt Info. Sciences, Inc. v. Bd. of Trs.*, 489 U.S. 468 (1989). The United States Supreme Court upheld that opinion of the California Court of Appeal that California's arbitration law, although much different from the FAA, did not conflict with the FAA because a contract to arbitrate would be enforceable under California arbitration law. *Volt* involved a construction

have made it clear that state laws eliminating arbitration will be preempted by the FAA, and only generally recognized state law contract defenses will be allowed to overcome the federal presumption in favor of arbitration.¹⁴⁹ The federal presumption is that arbitration clauses should be enforced, and any doubts should be resolved in favor of arbitration.¹⁵⁰ District courts should not only stay litigation until the arbitration is completed, but also should stay litigation in the event a denied motion to compel arbitration has been appealed.¹⁵¹ The federal judiciary has made its point vividly clear with regard to state laws limiting or eliminating contractual binding arbitration. Any state law which allows state courts to by-pass the mandates of the FAA will be pre-empted. There are no exceptions.

IX. THE PREEMPTION OF FEDERAL LAW BY THE FAA: WAIVER OF THE SEVENTH AMENDMENT RIGHT TO A JURY TRIAL IN ARBITRATION

At the time *Southland* was decided, it was understood that in order to waive the constitutional right to a jury trial, a person had to knowingly and intelligently waive that right by signing an agreement. This was not a major problem prior to *Southland*, but it became a sticky issue in some of *Southland's* progeny. Does a waiver require signatures to be held valid? What standards of assent will be applied? The so-called “shrink wrap” cases allowed the enforcement of pre-dispute arbitration clauses even when the parties had not signed an arbitration agreement. In *Hill v. Gateway* a federal court held, consumers were required to arbitrate their claim against a computer manufacturer because the computer-shipping box contained not only a computer, but also a package of shrink-wrapped documents notifying the consumers of an arbitration requirement.¹⁵² Thus, under a contractual

contract, containing an arbitration clause, but with a California choice of law provision. California law requires arbitration to be stayed until pending related litigation is resolved.

149. See *Alafabco*, 539 U.S. at 56.

150. *Masco Corp. v. Zurich Am. Ins. Co.*, 382 F.3d 624 (2004). A general presumption in favor of arbitration exists “and any doubts are to be resolved in favor of arbitration ‘unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute.’” *Id.* (quoting *AT&T Techs., Inc. v. Comm’ns Workers of Am.*, 475 U.S. 643, 650 (1986)). A general arbitration clause is enforceable, even if contained in a contract that is voidable unless the arbitration clause is challenged. *Id.* at 628 (citing *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967)).

151. *Blinco v. Green Tree Servicing LLC*, 400 F.3d 1308 (11th Cir. 2005).

152. *Hill v. Gateway 2000, Inc.*, 105 F.3d 1147, 1148 (7th Cir. 1997). Judge Easterbrook opined that the consumers who purchased a computer were bound by the terms of a contract to arbitrate contained inside the computer’s shipping box, because the terms of the contract required the consumer to return the computer within 30 days or be bound by the terms of the contract, including the arbitration clause. *Id.* at 1147-48. Although initially questioned on grounds of warranty laws, *Hill* is still considered good law in many federal courts. In *Falbe v. Dell, Inc.*, 2004 U.S. Dist. Lexis

assent standard, assent to use arbitration as an alternative forum to courts can be found by action or non-action.

However, not all federal courts follow the contractual assent rule. Some federal courts have held that consumers may not be held to a waiver of their rights by contractual assent, but require actual notice and a written waiver, evidenced by a signature.¹⁵³ The United States Supreme Court has not dealt with this waiver issue so as to clear up the divergent paths taken by federal courts in this area of constitutional law.

A non-signatory party may also be held to assent to waiver by endeavoring to use the contract containing the arbitration clause to their advantage. Beneficiaries who did not sign a contract have also been held to the terms of arbitration clauses when they seek to enforce the contract terms against a signatory to the contract.¹⁵⁴ For instance, Dobson, the Plaintiff in *Terminix*, was a third-party beneficiary to the termite bond containing the arbitration agreement.¹⁵⁵ Therefore, the Supreme Court seems willing to accept contractual assent by third parties.

X. THE PANDORA'S BOX OF *SOUTHLAND'S* PROGENY: CLASS ACTIONS AND PUNITIVE DAMAGES

Southland opened the door to creative thinking by some members of the plaintiffs' bar. Courts have been divided for years over the appropriateness of class actions and punitive damages in arbitration. Some courts have ruled out class actions in arbitration, while other courts have left the class action determination to the arbitrators.¹⁵⁶ In *Green Tree Financial Corporation v. Bazzle*, one of *Southland's* progeny, the United States Supreme Court opened the door to class actions in arbitration by holding that arbitrators, not

13188, the U.S. District Court used *Hill* to analyze a Dell computer case and order it to arbitration. No. 04-C-1425, 2004 U.S. Dist. LEXIS 13188, at *11 (N.D. Ill. July 12, 2004). Judge Grady stated in the *Falbe* case that the court's analysis "began and ended" with the 7th Circuit's decision in *Hill*. *Id.*

153. *Klocek v. Gateway, Inc.*, 104 F. Supp. 2d 1332, 1339-41 (D. Kan. 2000).

154. *Philadelphia Flyers, Inc. v. Trustmark Ins. Co.*, No. 04-2322, 2004 U.S. Dist. LEXIS 12772, at *10 (E.D. Pa. 2004). The court held that principles of equitable estoppel may require a non-signatory to be bound by the terms of a contract, including an arbitration clause, if the non-signatory attempts to enforce the terms of the contract. *Id.* at *11-12.

155. *Terminix*, 513 U.S. at 268.

156. *Bazzle v. Green Tree Fin. Corp.*, 569 S.E. 2d 349, 361-62 (S.C. 2002) *vacated in Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444 (2003).

courts, may determine whether a class action can be arbitrated.¹⁵⁷ Like the punitive damages issue presented in *Mastrobuono*, the holding in *Bazzle* can be interpreted to take a permissive approach if the contract language is silent on class actions.¹⁵⁸ The holding in *Bazzle* was notice to contract drafters that remedies not excluded in the contract language may be included in the arbitration.¹⁵⁹ This situation caused many contract drafters to reexamine their standard arbitration clauses and shore up traditional boiler plate language.¹⁶⁰ Some businesses may decide to litigate instead of arbitrate if class actions and punitive damages are allowed by the arbitrators in cases where the contract is silent; but they can only do so if they prove the contract is not subject to the enforcement provisions of the FAA.¹⁶¹ While it is not clear how courts will treat future class action cases due to the far-reaching implications of *Bazzle*, but the decision has certainly caused the business

157. *Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444, 451-55 (2003). Class actions in arbitration have always presented problems for courts. Should the court interpret the contract to determine if a class action is permissible, or should the arbitrators determine this issue? State and federal courts have argued this issue for years, but the United States Supreme Court held in *Bazzle* that arbitrators have the authority to allow or prohibit a class action. *Bazzle* puts contract drafters on notice to include preclusion against class actions in arbitration or leave their clients at the mercy of the arbitrators. Due to the holding in *Bazzle*, silence regarding arbitration class actions in ordinary arbitration clauses leaves the client exposed to the potential of a class action. *Bazzle* is consistent with prior holdings allowing courts to determine the existence of an agreement to arbitrate and its applicability to the parties and the facts, while allowing the arbitrators to determine all other issues related to the arbitration.

158. *Mastrobuono*, 514 U.S. at 56-64.

159. See Stephen K. Huber, *The Arbitration Jurisprudence of the Fifth Circuit*, 35 TEX. TECH. L. REV. 497, 539 (2004). Supporting that arbitration is here to stay and class arbitration is coming. See *id.* at 498. Although *Bazzle* did not produce a unanimous decision, Huber points out that all the Justices seem willing to accept the idea of a class action in arbitration. *Id.* at 538. The decisions of arbitrators are set aside only on rare occasions. *Id.* at 529.

160. Alan S. Kaplinsky, & Mark J. Levin, *Arbitration Update: Green Tree Financial Corp. v. Bazzle-Dazzle for Green Tree, Fizzle for Practitioners*, 59 BUS. LAW. 1265 (2004). The disagreements over the meaning of *Bazzle* continue. Does silence on class action mean there is a green light or a red light to class actions in arbitration? No one really knows, but these two practitioners argue that it is only a matter of time before the United States Supreme Court will clarify this issue.

161. Stephen J. Ware, *Arbitration Clauses, Jury-Waiver Clauses, and Other Contractual Waivers of Constitutional Rights*, 67 LAW & CONTEMP. PROBS. 167 (2004). Professor Ware concludes a pre-dispute binding arbitration clause merely replaces the jury trial with arbitration. *Id.* at 170-73. He points out that general contract defenses may be used against arbitration clauses, but state anti-arbitration clauses may not be used to set aside arbitration. *Id.* at 170. Professor Ware states that the FAA requires a contract law standard of consent, but many critics of the FAA wish to apply a knowing consent standard. *Id.* at 181-83. The knowing consent standard was rejected in favor of contract law standard of consent in *Doctor's Associates, Inc. v. Cassarotto*. Professor Ware does not accept the argument that consumer arbitration clauses should be treated differently from contracts between businesses. *Id.* at 182. Professor Ware contrasts criminal and civil waivers and concludes the contractual consent waiver rather than the knowing consent waiver will likely prevail in future Supreme Court cases. *Id.*

community a great deal of concern.¹⁶² Arbitration clauses were presumed to have protected business' exposure to class actions, but *Bazzle* raises substantial doubt as to arbitration's ability to eliminate class actions.¹⁶³ *Mastrobuono* opened the door to the possibility of punitive damages in a contract containing an arbitration clause, if the arbitration clause was silent on the applicability of such damages, even if punitive damages were not allowed by the state law governing the contract.

XI. TAKING CONTRACTUAL ARBITRATION TO WORK AFTER *SOUTHLAND*: THE ALL POWERFUL AGREEMENT TO ARBITRATE IN EMPLOYMENT CASES

The supporters of arbitration under the FAA point out that constitutional rights and statutory rights are not inalienable and can be waived by contract.¹⁶⁴ An argument has arisen over the type of consent needed for waiver in employment cases and the results are mixed. While some of arbitration's supporters want a contractual standard of consent, opponents want a knowing standard of consent.¹⁶⁵ Contractual assent does not require an employee to be given an explanation of arbitration, while knowing assent requires evidence in writing of consent to arbitrate.¹⁶⁶ It may well be that the federal presumption in favor of arbitration has virtually eliminated knowing consensual waiver as a defense in contractual arbitration cases where the employee is a party to the contract.¹⁶⁷ Employees are not generally held to contractual waiver Title VII claims in union arbitration contracts, because

162. Robert J. Herndon, *Mistaken Interpretation: The American Arbitration Association, Green Tree Financial Corporation v. Bazzle, and the Real State of Class-Action Arbitration in North Carolina*, 82 N.C.L. REV. 2128 (2004). Herndon begins this article by pointing out *Bazzle* was a consolidation of two South Carolina class action suits involving a state consumer protection code. *See id.* A divided United States Supreme Court heard the case, vacated the South Carolina decisions, and remanded the matter back to South Carolina's Supreme Court. *See id.* at 2129. The interpretation of *Bazzle* is important. *See id.* at 2129. Some view *Bazzle* as allowing arbitrators to examine if a contract is silent as to class actions, while others contend that *Bazzle* allows arbitrators to determine if a class action is allowed if the contract is silent. *Id.*

163. Herndon, *supra* note 162 at 2129.

164. Jeffery W. Stempel, *Symposium Securities Arbitration: A Decade After McMahon: Bootstrapping and Slouching Toward Gomorrah: Arbitral Infatuation and the Decline of Consent*, 62 BROOK. L. REV. 1384 (1996). Professor Stempel points out that consent is a thing of the past, and quoting Professor Speidel, he summarizes that consent is lately a legal fiction. *See id.* at 1387. Professor Stempel makes a case for court determination of consent. *See id.* at 1388.

165. *See id.* at 1381-82.

166. *See id.* at 1391.

167. *Id.*

the employee plays no role in the formation of the contract, and the employee's interests are not always synonymous with those of the union.¹⁶⁸

Drafters of arbitration clauses may not receive a totally unencumbered path to arbitration in statutory rights cases in the employment area. Although a contracting party may have waived statutory rights by signing an arbitration agreement, federal agencies may still have a cause of action on behalf of the aggrieved party that is not subject to arbitration.¹⁶⁹ For example, in *Equal Employment Opportunity Commission (EEOC) v. Waffle House*, the Court held that although an employee had waived statutory rights claims, the EEOC had not been estopped from pursuing those claims under the federal statute.¹⁷⁰ Employers who choose to insert arbitration agreements into employment contracts can force the employee into arbitration but may not be able to use the FAA to force a federal agency out of public law courts.¹⁷¹ Following *Gilmer v. Interstate/Johnson Lane Corp.*, the green light was given to employers to use arbitration agreements in employment contracts to force employees to arbitrate all claims, including statutory claims.¹⁷² Today, there exists a serious debate over whether employees should be forced to sign a contract waiving their constitutionally guaranteed rights in order to obtain employment.¹⁷³

XII. DEFENSES AGAINST THE FAA MANDATE TO ARBITRATE UNDER STATE CONTRACT LAW AND DEFENSES TO AWARDS RENDERED

Defenses to arbitration agreements and avoidance of arbitration are dependent upon state contract law defenses. All of the normal state law defenses to contracts such as mutual mistake, detrimental reliance, and unconscionability are available to a party seeking to avoid arbitration on the grounds that the arbitration agreement is flawed.¹⁷⁴ Mutual mistake is not often used as a defense to the arbitration contract, although it is conceivable if the party seeking to set aside the arbitration agreement could prove the

168. See *McDonald v. City of West Branch*, 466 U.S. 284 (1984).

169. See *Waffle House, Inc.*, 534 U.S. at 297-98 (holding that government agencies can enforce federal statutory claims in court, even when the employee has agreed to arbitrate those claims. The employee is estopped, but the EEOC may proceed); see also *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991) (opening the door for effective arbitration in employment disputes); see also *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105 (2001) (expanding the use of arbitration agreements in employment contracts).

170. *Id.*

171. *Id.*

172. *Id.*

173. Kristin McCandless, Comment, *Circuit City Stores, Inc. v. Adams: The Debate Over Arbitration in the Employment Context Rages On*, 80 DENV. U. L. REV. 225, 228 (2002).

174. See *Terminix*, 513 U.S. 265, 281 (1995).

parties agreed to different terms when forming the agreement to arbitrate.¹⁷⁵ Detrimental reliance on terms that were fraudulently induced can serve as grounds to rescind a contract.¹⁷⁶ The fundamentals of this defense are that one party lied, the lie was intentional and was told for purposes of inducing the other party to contract, the other party relied on the lie to enter the contract and damages resulted.¹⁷⁷ Courts have also sustained breach of contract claims against the drafters of contracts of adhesion when the arbitration process contained in the contract lacked “the rudiments of even-handedness.”¹⁷⁸ Courts have held that contracts that are constructed as one-sided in favor of the drafter are unconscionable and are subject to rescission.¹⁷⁹ These cases are, however, the exception to the reality of arbitration agreements. In the vast majority of cases, agreements to arbitrate are upheld and enforced by the courts.¹⁸⁰

Georgia was the first state to recognize manifest disregard of the law by the arbitrator(s) as a ground for vacating an arbitration award.¹⁸¹ While there is growing interest in manifest disregard of the law as a vehicle for challenging arbitration awards, the definition of “manifest disregard of the law” is still in the developmental stages.¹⁸² Another area of keen interest is the potential of award challenges based on arbitrator bias. California has passed new ethical standards for arbitrators requiring disclosure of past

175. See GRANT GILMORE, DEATH OF CONTRACT 40-41 (1974).

176. See *Engalla v. Permanente Medical Group, Inc.*, 938 P. 2d 903, 925 (Cal. 1997). A cancer victim sued an HMO for fraudulent misrepresentation of the terms of the arbitration agreement. *Id.* The court allowed the revision of the contract to arbitrate due to the misrepresentations. *Id.*

177. See *id.* at 908.

178. *Hooters of Am., Inc. v. Phillips*, 173 F.3d 933, 935 (4th Cir. 1999). The arbitration panel was composed of employer’s managers in deciding an employee’s claim. See *id.*

179. See *id.* at 940.

180. MACNEIL, *supra* note 53, at 148-50.

181. See Brent S. Gilfedder, “A Manifest Disregard of Arbitration?” *An Analysis of Recent Georgia Legislation Adding “Manifest Disregard of the Law” to the Georgia Arbitration Code as a Statutory Ground for Vacatur*, 39 GA. L. REV. 259, 260 (2004). Mr. Gilfedder points out that Georgia became the very first state to add “manifest disregard of the law” as an additional ground to vacate arbitration awards in 2003. See *id.* He points out that manifest disregard of the law usually means the award conflicts with public policy or it is arbitrary or capacious. See *id.* As federal courts have discovered, this standard for vacatur is difficult because it is ill defined. See *id.* He contends “manifest disregard of the law” is an “illusory” concept so it cannot be applied on a consistent basis. See *id.* at 276. He cites cases in which federal courts have interpreted manifest disregard of the law in various ways, but the central theme of these seems to be the arbitrators knew the law and ignored it. See *id.* at 278-81.

182. Gilfedder, *supra* note 181, at 278-81.

dealings between arbitrators and the parties.¹⁸³ Although arbitrators and arbitration providers oppose these new standards of disclosure, the opponents of arbitration hope to prove arbitration bias through the information obtained through these standards.¹⁸⁴ Arbitrator bias can also be a ground upon which to assert a contract defense of unconscionability against the arbitration process.¹⁸⁵ If the opponents of arbitration can demonstrate financial ties to one of the parties by the arbitrators, they may have grounds for setting aside any award rendered based on bias,¹⁸⁶ or challenging the process on grounds of unconscionability.¹⁸⁷ Financial consequences of the arbitration on the challenging party appear to be a more difficult defense, unless there is proof on record of the financial inequities of the process on one of the parties.¹⁸⁸

In addition to the state law contract defenses to the arbitration agreement, parties also have defenses to the arbitration award. 9 U.S.C. § 10 lists the following grounds for vacating an arbitration award:

- (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.
- ...
- (b) If an award is vacated and the time within which the agreement required the award to be made has not expired the court may, in its discretion, direct a rehearing by the arbitrators.¹⁸⁹

183. Jaimie Kent, *The Debate in California Over and Implications of New Ethical Standards for Arbitrator Disclosure: Are the Changes Valid or Appropriate?*, 17 GEO. J. LEGAL ETHICS 903, 913 (2004). This article discusses the new rules for arbitrators in California regarding disclosure of repeat customers. *Id.* Forcing arbitrators to disclose their financial dealings with repeat players is causing major controversy in California. *Id.* at 913-14. Several courts, state and federal, have disallowed the applications of the new rules for various reasons. *Id.* at 916-18. Obviously, large corporations, arbitrators whose incomes are largely derived from repeat business, and arbitration providers like AAA oppose the new rules. *Id.* at 914. Kent concludes that some ethical disclosure standards for arbitrators are necessary. *Id.* at 926.

184. Kent, *supra* note 183 at 912.

185. *Id.* at 911 n. 64.

186. *Id.* at 925.

187. *Id.* at 911 n. 64.

188. See *Hooters*, 173 F.3d at 939. The arbitrator panel had members with connections to the business party. *Id.* at 938-39

189. 9 U.S.C. § 10.

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All but one of the grounds involves arbitrator misconduct and all are exceptionally difficult to prove.¹⁹⁰

9 U.S.C. § 11 provides the following grounds for modifying or correcting a flawed arbitration award:

- (1) Where there was an evident material miscalculation of figures or an evident material mistake in the description of any person, thing, or property referred to in the award.
- (2) Where the arbitrators have awarded upon a matter not submitted to them, unless it is a matter not affecting the merits of the decision upon the matter submitted.
- (3) Where the award is imperfect in matter of form not affecting the merits of the controversy.¹⁹¹

CONCLUSION

Prior to *Southland*, the chief problem for federal courts in diversity cases containing arbitration clauses was that not all state arbitration laws were the same. For example, New York promoted the use of pre-dispute contractual arbitration,¹⁹² Alabama prohibited the use of pre-dispute contractual arbitration¹⁹³ and California allowed pre-dispute contractual arbitration in some cases, while prohibiting it in others.¹⁹⁴ Therefore, depending upon the state law to be applied by the federal courts under the *Erie* principle to the facts of the cases, the outcomes could be radically different. Such state-to-state variances could lead to forum shopping in arbitration cases, which was troubling to the United States Supreme Court.¹⁹⁵ The cases prior to *Southland* offered little help in resolving the forum shopping dilemma, because the FAA's language did not grant federal jurisdiction in arbitration cases.¹⁹⁶ The FAA had been written like a federal procedural act and it lacked the trappings of a substantive law act. Although

190. These grounds require the party seeking to set aside the award to submit proof of wrongdoing by the arbitrators. However, no standard for submission of proof of wrongdoing is set forth in the FAA.

191. 9 U.S.C. § 11.

192. N.Y., C.P.L.R. 7501 (McKinney 1998).

193. ALA. CODE § 8-1-41(3).

194. *Compare* Volt Info. Sciences, Inc. v. Bd. of Trs., 489 U.S. 468, 470 (1989) (noting that California denied use of pre-dispute arbitration where there was litigation with a third party under a California statute) with *Southland*, 465 U.S. 5 (noting that the California Supreme Court refused to enforce the arbitration agreement pursuant to California law, but allowed other claims to be arbitrated).

195. See, e.g., *Bernhardt*, 350 U.S. at 202-03.

196. *Id.* at 200-02.

the dilemma was addressed in early federal cases involving the FAA, there appeared to be little the courts could do about the problem, due to the application of the *Erie* principle.¹⁹⁷

Southland addressed the problem and resolved the dilemma by converting a procedural FAA into a substantive law act by placing a new interpretation on the intent of Congress regarding the FAA.¹⁹⁸ The majority in *Southland* cited some of the testimony from the Congressional hearings leading up to the FAA, and concluded that Congress had intended the FAA to be substantive using a Commerce Clause argument.¹⁹⁹ The minority in *Southland* also cited testimony from the Congressional hearings leading up to the FAA, and their conclusion was that the FAA was never intended to apply in state courts.²⁰⁰ *Southland's* progeny share the theme of expansion of the FAA's reach with their common ancestor. *Circuit City Stores, Inc. v. Adams* held that the Congressional intent behind the FAA was to regulate commerce and preempt contrary state laws.²⁰¹ *Geier v. American Honda Motor Co.* held that state law must yield if it stands in the way of the accomplishment of the purposes and objectives of Congress.²⁰² Contractual arbitration agreements will be enforced unless state law contract defenses apply.²⁰³ The point of these cases seems to be that state contract law cannot bring federal commerce to a halt by prohibiting the use of arbitration and insisting upon litigation in every contracts case.

The progeny contain language from both the FAA and *Southland* and usually a dissent or two stating the FAA was never intended to apply to the state courts. Although the United States Supreme Court has had numerous opportunities to limit or reverse its holding in *Southland* over the past twenty-one years, it has declined to change its direction. *Southland* has successfully sailed around the rocks of *Erie*, but the question remains, where is arbitration going now that *Southland* has cleared the jettys?

Opponents of arbitration continue to attack the fairness of the process and point out access to justice problems created by the contractual waivers of rights contained in arbitration clauses.²⁰⁴ Their argument is in essence a repackaging of the old ouster doctrine under the common law, preferring litigation over arbitration in consumer and employment cases. The common

197. *Id.* at 202.

198. *Southland*, 465 U.S. at 10-11.

199. *See id.* at 12-14.

200. *See id.* at 25-28.

201. *Circuit City Stores*, 532 U.S. at 112.

202. *Geier v. Am. Honda Motor Co.*, 529 U.S. 861, 884-85 (2000).

203. *See Iberia Credit Bureau, Inc. v. Cingular Wireless, LLC*, 379 F.3d 159 (5th Cir. 2004).

204. Jean R. Sternlight, *Mandatory Binding Arbitration and the Demise of the Seventh Amendment Right to a Jury Trial*, 16 OHIO ST. J. ON DISP. RES. 669, 70 (2001).

law view of pre-dispute contractual arbitration as a revocable process, was dealt a death blow by *Southland*. The question of whether *Southland* and its progeny have resulted in legislation from the bench, or simply a more accurate interpretation of Congressional statutory intent, becomes a moot question in light of current federal law. *Southland* does not represent the first case to reinterpret the intent behind existing statutory law, and it is unlikely that *Southland* will be the last such case.²⁰⁵ Current federal case law favors the enforcement of binding pre-dispute arbitration clauses, and there is no indication by the courts or Congress that the rule of law in this area is likely to change anytime soon. Arbitration's opponents appear to be fighting a losing battle in their efforts to limit or eliminate the FAA and reverse the holding in *Southland*. Perhaps their time would be better spent in finding creative ways to use the FAA to benefit their clients, like the claimants in *Bazzle*.²⁰⁶

Southland's progeny are continuing to define the length and width of arbitration's reach under the FAA. No doubt, some members of the legal profession long for the days of yesteryear when the law was more static in this area. However, the full effect of *Southland* and its progeny has yet to be realized. The initial issues of binding agreements to arbitrate and preemption of state anti-arbitration laws have been resolved. The law in this field has now moved on to address new issues like the availability of punitive damages and class actions. It is likely to be some time before the law is settled in those areas. *Southland* removed the lid from a Pandora's Box of possibilities for enforcement of arbitration under the FAA because it created a federal common law with regard to arbitration. The only organization that can replace that lid is the United States Congress, which has not given the slightest indication of any impending efforts to limit or eliminate the FAA.

205. *Wilko v. Swan*, 346 U.S. 427 (1953); *Ludwig Honold Mfg. Co. v. Fletcher*, 405 F.2d 1123, 1128 (3rd Cir. 1969); *Perry v. Thomas*, 482 U.S. 483 (1987).

206. *Bazzle*, 539 U.S. at 451-55.

