ISSUES FOR COURTS VS. ISSUES FOR PANELS

SUPREME COURT CLAIRIFICATION?

by

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I. Introduction

The distinction between issues properly addressed by the courts as opposed to arbitration panels has been a bit opaque in the past. This has led to uncertainty by both counsel and arbitrators as to the proper venue for a dispute. In 2010 the U.S. Supreme Court issued opinions on two non-reinsurance matters that may help clarify this distinction. The purpose of this article is to examine these two cases highlighting the distinction drawn by the Court over the issues properly addressed by the court vs. those properly addressed by arbitration panels.

II. Granite Rock Co. v. International Brother of Teamsters et al., 130 S.Ct. 2772 (2010)

This case involved a labor dispute. A union local was on strike until July 2, 2004 when it voted to accept a collective bargaining agreement ("CBA") with the employer, Granite Rock. At the time of the vote, the Local did not have a hold harmless agreement that would protect it from damages suffered by Granite Rock during the strike. The International Union advised the Local not to return to work without the hold harmless and the Local reversed its position and did not return to work. Granite Rock sued for damages and an injunction against the strike. On August 22, 2004, the Local again voted to accept the CBA and returned to work, thus mooting the injunction issue, but Granite Rock continued to seek damages.

Since the CBA contained a no-strike clause, the effective date of its ratification became an issue with respect to the calculation of damages. The Local argued that the effective date of the ratification should be determined by the arbitrator pursuant to the CBA and Granite Rock argued that it should be determined by a court. The district court held in favor of Granite Rock (*i.e.* that the court should determine the issue). The Court of Appeals reversed on the bases that the dispute was covered by the arbitration clause of the CBA and the national policy in favor of arbitration. The Supreme Court reversed with Mr. Justice Thomas writing the opinion for seven members of the court with two members concurring in part and dissenting in part.

The majority opened its opinion with the observation that prior caselaw indicates that the following issues generally are for determination by the courts: whether (a) a contract was formed between the parties that contains an arbitration clause ("Formation Issue"); and (b) the dispute in question falls within the ambit of the arbitration clause. Since arbitration is a creature of contract, there must be a contract between the parties that gives an arbitration panel the power to resolve disputes and the dispute in question must fall within the range of issues the parties have empowered the panel to decide.

The majority criticized the Court of Appeals for over-reliance on the presumption of arbitrability which applies to whether or not the dispute falls within the arbitration clause but does not apply to the Formation Issue. This presumption, or other policy considerations, can never override the principle that a court can submit to arbitration "only those disputes . . . which the parties have agreed to submit."[1] The majority ruled that the issue in this case was a Formation Issue which required:

> [J]udicial resolution of two questions central to Local's arbitration demand: when the CBA was formed and whether its arbitration clause covers the matters that Local wishes to arbitrate.[2]

As additional reasons to overturn the lower court decision, the majority observed that the dispute over the ratification date, which went to the very existence of the CBA, could not "arise under" the "relatively narrow" arbitration clause of the CBA. Also, the arbitration clause made it clear that labor disputes were to be arbitrated rather than disputes about the ratification of the CBA.[3]

The dissent observed that after the strikes were concluded, the parties made the CBA retroactive to May 1, 2004 (*i.e.* before either of the ratification votes) so that the Formation Issue was moot.[4] In addition, the dissenters re-defined the issue in the case as whether or not the no-strike clause prescribed the work stoppage and were of the opinion that this issue plainly "arose out of" the CBA and was subject to arbitration.

III. *Rent-a-Center, West, Inc. v. Jackson*, 130 S.Ct. 2772 (2010)

The issue in this case was the arbitrability of an employment discrimination action. As part of a larger employment arrangement, the employee signed an Arbitration Agreement by which he agreed to arbitrate, among other things, the enforceability of the Arbitration Agreement. The employer sought to enforce the Arbitration Agreement and the employee challenged it as unconscionable. The district court

held for the employer ruling that the Arbitration Agreement clearly gave the arbitrator the power to decide enforceability issues. The Court of Appeals reversed ruling that the enforceability of the Arbitration Agreement was a matter for the courts. Mr. Justice Scalia, writing for a five member majority, reversed the court of appeals and ruled that enforceability of the Arbitration Agreement was for the arbitrator to decide.

The majority first addressed the provision delegating the issue of enforceability of the Arbitration Agreement to the arbitrator ("Delegation Provision"). It ruled that gateway issues, such as that of arbitrability, which would usually be handled by the courts, may properly be addressed by the arbitrator as long as the delegation to the arbitrator is clear. Next, the Court dealt with challenges to the validity of the contract under § 2 of the Federal Arbitration Act. The Court observed that challenges to the arbitration clause of a contract are for the courts to determine but challenges to other clauses or the contract generally are for the arbitrator:

> If a party challenges the validity under § 2 of the precise agreement to arbitrate at issue, the federal court must consider the challenge before ordering compliance with that agreement under § 4. . . .
>
> But even where . . . the alleged fraud that induced the whole contract equally induced the agreement to arbitrate which was part of that contract – we nonetheless require the basis of challenge to be directed specifically to the agreement to arbitrate before the court will intervene.[5]

Arbitration clauses are severable in that they may be enforced by the courts while the arbitrator addresses the rest of the contract.

In this case, the employer was seeking enforcement of the Delegation Provision which gave the arbitrator the authority to decide the enforceability of the contract. Regardless of the fact that the remainder of the contract was an agreement to arbitrate, the majority ruled that the employee's unconscionability challenge had to be addressed to the Delegation Provision specifically, and not the Arbitration Agreement generally, for it to be a matter for the court to decide. In reviewing the record, the majority concluded that the unconscionability challenge was to the Arbitration Agreement generally and not to the Delegation Provision specifically. Therefore, the enforceability issue was for the arbitrator to decide.[6]

Mr. Justice Stevens wrote an articulate dissent for four members of the court. He focused on the fact that this was a challenge, general as it might be, to an agreement to arbitrate and that prior precedent had assigned challenges to arbitration provisions (*i.e.* in broader contracts) to the courts. The minority also dissented on the Delegation Provision arguing that the unconscionability defense undermined the employees consent to it. Finally, the dissenters objected to the narrowness of the challenge necessary to require resolution of the issue by the courts:

> Today the Court adds a new layer of severability – something akin to Russian nesting dolls – into the mix: Courts may now pluck from a potentially invalid *arbitration*

> *agreement* even narrower provisions that refer particular arbitrability disputes to an arbitrator. . . .
>
> [B]ecause we are dealing in this case with a challenge to an independently executed arbitration agreement – rather than a clause contained in a contract related to another subject matter – any challenge to the contract itself is also, necessarily, a challenge to the arbitration agreement.[7]

IV. COMMENTARY

Trying to interpret a trend in Supreme Court cases is a tricky business, particularly when only two cases are involved. Differences in facts, issues and the respective records may explain more than judicial philosophy.

Nonetheless, these cases seem to cut in opposite directions despite apparent agreement as to the legal principles behind the court vs. panel issue. These principles are:

A. The courts determine whether a contract has been formed between the parties that contains an arbitration clause (formation) and whether or not the dispute falls within the arbitration clause (arbitrability);

B. The parties may contract to delegate certain threshold issues, such as arbitrability, to the arbitrator so long as the delegation is clear; and

C. The arbitrator determines challenges to the contract even if the problem that allegedly infects the contract infects the arbitration clause as well.

In *Granite Rock*, the majority found a waiver of an argument which the dissent argued should have been considered to do justice to the Local. Relying on this waiver, the majority found an issue with the formation of contract that required resolution by the court.

In *Rent-a-Center*, five members of the *Granite Rock* majority took an extremely narrow view of the type of challenge to the arbitration agreement necessary for the court to resolve this issue. On this narrow view, the majority reached a conclusion opposite from that in *Granite Rock*, *i.e.* that the arbitrator should decide the issue.

Given the unusual facts involved in these cases, it may be difficult to take much more from these rulings than apparent agreement on the legal principles on which they are based.

ENDNOTES

[1] 130 S.Ct. 2847 at 2860 quoting *First Options of Chicago, Inc. v. K*aplan, 514 U.S. 938 (1995) at 943.
[2] *Id.*
[3] *Id. at 2862.*
[4] The majority ruled that the Local had waived this argument. *Id.* at 2861.
[5] 130 S.Ct. 2272 (2010) at 2278.
[6] *Id.* at 2780-1.
[7] *Id.* at 2786-7.