Arbitration

CASES, PROBLEMS, AND PRACTICE

2019 Letter Update/Supplement

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Dear Professor,

I am hard at work on a second edition of the book, so I can tell you now, and quite specifically, where the book will change, and as a result, how the teaching of the book will change from as recently as last Fall.

Class Action and Arbitration

The most significant developments in the law since the book's publication in 2017 will be in Chapter 4, "Arbitration and Class Action". This reflects the continued SCOTUS emphasis on this particular area. The Court has issued roughly one opinion per year on this subject since *Concepcion* in 2010, a pace that continued in the two years since publication of my first edition. In 2018 the Court issued *Epic Systems* and in 2019 the Court issued *Lamps Plus*.

In *Epic Systems*, the Court held that an arbitration clause overcame concerns that single-employer arbitration conflicted with employee protections under the Federal Labor Relations Act, *Epic* was therefore another case in the "effective vindication" line of cases treated in the book in which the court has rejected arguments that arbitration clauses interfere with the pursuit of otherwise valid statutory remedies. For example, in the *Italian Colors* case at page 182, the Court upheld a clause that required each individual claimant to arbitrate on its own, even though they argued that individually they would never be able to afford an economics expert which in turn was necessary for their "effective vindication" of their antitrust case. *Epic* flows directly from the *Concepcion* line of cases addressed in the book. It is notable that it was written by Justice Gorsuch, who continues the late Justice Scalia's aggressive upholding of arbitration clauses in the face of challenges on access to justice grounds, and that it comes over an impassioned dissent from Justice Ginsburg. Justice Gorsuch stated expressly that Concepcion governs the holding. I think *Epic* is the most interesting and important arbitration case of the last five years, and I would encourage you to read and teach it if you teach this unit.

Lamps Plus is more recent, not quite as critical as *Epic*, but still in my view worth teaching in the class action unit. The underlying facts involved a data breach which resulted in the publication of tax returns of employees of the "breached" employer. The employees each had an employment agreement with an arbitration clause. One employee brought a claim but argued that he was entitled to class rather than individual arbitration. The language in the employment agreement was arguably ambiguous as to whether it permitted/prohibited class arbitration. Because the clause was drafted by the employer, the 9th Circuit ruled that class arbitration was permissible under the contract interpretation maxim "construe against the drafter." By a 5-4 majority, again over a vigorous Ginsburg dissent and an equally strong dissent by Justice Kagan, the Supreme Court held that the "pro-arbitration" policy of the Federal Arbitration Act overcame the contract interpretation argument and so class arbitration was impermissible. The dissents are valuable for articulating the view, which I have personally come to hold, that Congress in passing the Federal Arbitration Act in 1924 meant arbitration to be an efficient means of deciding commercial issues between merchants, and never meant arbitration to have its contemporary reach to consumer vs. business issues. I usually engage the students on that debate after we get through these cases – of which, as seen, there are now two more.

That takes us to the failure of administrative reforms in the class action/arbitration area. I plan to make substantial changes to the material at page 207. By coincidence, the last chance I had to make revisions to the first edition was just after the 2016 election. At that point, the Obama Administration had promulgated regulations by the Consumer Financial Protection Bureau that would have dramatically affected the reach of arbitration to consumer vs. business cases. Employers, since *Concepcion*, had perfected what I call the "one-two punch": first, requiring employees to agree to resolve any disputes through arbitration and second, inserting class action bans into these clauses. This has had the predictable impact of making these cases unattractive to the plaintiff's bar and thus cutting down substantially on the number of consumer cases. The Bureau promulgated a regulation that would have made illegal class action bans in consumer contracts. At the time the book went to press it seemed unlikely that this regulation would survive the Trump election, and that is precisely what happened: the regulations were killed by the new Administration before they ever took effect. *See* https://www.consumerfinance.gov/policy-compliance/rulemaking/final-rules/arbitration-agreements/

I plan on adding an expanded section on this development. I suggest that teaching of the Obama-era regulations as promulgated, and then the Trump Administration's rescinding of them, is valuable from several respects. First, it shows how much arbitration has risen from a dry dispute resolution subject to a hotly contested issue of social policy. Second, it allows coverage of administrative law in what up to this point has been a case-driven approach. Third, it frames the debate going forward as to how far the pendulum will and should swing toward arbitration and away from any class action rights for consumers.

Section 2 Savings Clause

The new SCOTUS class action cases also caused me to reassess the book's treatment in Chapter 2 on the so-called "Savings Clause" in section 2 of the FAA. Section 2 recognizes that arbitration clauses must be enforced just like any other contract, unless there are reasons that – again, just as with any other contract – the agreement should not be upheld. These reasons can include classic contract defenses such as fraud, invalidity and lack of capacity. In recent years, during the class action debate discussed above, parties challenging arbitration agreements have argued that it is "fraud", or a violation of social policy, to insert arbitration clauses into consumer or other individual agreements, and that this triggers a section 2 defense. Most courts have responded that a section 2 challenge based solely on the clause calling for arbitration, without otherwise showing a more general contract defense, is an improper reading of Congress's intent in enacting the "savings clause." The recent cases contain extensive discussion of section 2 and I am therefore going to rework the treatment of this subject in the "Formation and Federalism" portion of Chapter 2, starting at page 37.

Delegation Clauses

At pages 112-116 and especially in the *First Options* case, the book covers "delegation clauses", where parties delegate to arbitrators issues such as arbitration jurisdiction which would otherwise be left to the courts. Justice Kavanaugh's first reported decision upheld delegation clauses over a "wholly groundless" objection. *Schein v. Archer & White*, Jan. 8, 2019. The

decision was not that controversial or groundbreaking, as reflected by its 9-0 margin. It is, however, worth a brief reference both as to the continued validity of delegation clauses, their insulation from most attacks, and, on a broader level and here again, the continued high level of attention this Court pays to arbitration. On that last point, and as a gentle pushback to *Schein* on the deference paid to delegation clauses, *see* yet another 2019 Term arbitration SCOTUS decision, the January 15, 2019 9-0 Gorsuch opinion in *New Prime v. Oliviera*. There, the Court ruled that the section 1 FAA exemption for transportation workers is a threshold determination to be made by the court, even with a delegation clause. I then plan on addressing this at what is now the text at 116-117.

Diversity in Arbitrator Selection (Chapter 5)

There is substantial debate in the arbitration bar about diversity in arbitrator selection. Both domestic and (in my view especially) international arbitration have drawn arbitrators consistently from an old boys network. That has been slowly changing but not at a pace that reflects the makeup of our profession. There are substantial movements afoot to increase diversity. This took a dramatic and highly publicized turn last year when the entertainer Jay-Z brought a collateral challenge in New York state court to the lack of diversity of a AAA panel hearing an arbitration he had brought. That case, captioned Shawn C. Carter v. Iconix Brand Group, and its aftermath will be part of a new section on arbitrator diversity that I will add to Chapter 5. I will cover as well efforts at increasing diversity in international arbitration, spearheaded by my friend Professor Catherine Rogers. Professor Rogers has a number of speeches and articles on this point and, for what I plan to receive particular emphasis in the book, a website that promotes diversity by making arbitrator statistics and experience accessible so that parties can choose up-and-coming arbitrators who may not have gotten visibility through the old networks. See https://arbitratorintelligence.com/ai-news I plan to introduce excerpts from this site.

Manifest Disregard

Chapter 14 is entitled "The Rise, Fall and Uncertain Life of Manifest Disregard". It covers what in my view is the single most unresolved important subject in arbitration practice: merits review of arbitration awards. Merits are intentionally *not* listed as a ground for review of arbitration awards in section 10 of the FAA, nor are the words "manifest disregard of the law" in the Act. Nevertheless, the term "manifest disregard" crept into appellate practice, with the result that there is a sharp difference between courts as to its reach and meaning. In a 2008 case called *Hall St. Assocs. v. Mattel* covered at page 516, the Supreme Court refused to clarify the limits of the doctrine, a point the book addresses at length. This has had significant practical effects since many challengers now to arbitration awards include attacks on the merits captioned as "manifest disregard."

In 2017, a lower NY court breathed substantive life into the manifest disregard standard and made it appear that merits challenges were now available under New York law. That decision caused substantial concern in the NY arbitration bar, who feared that it would drive arbitrations out of NY. The Appellate Division reversed that award in 2018, after the book was published. *Daesang Corp. v. Nutrasweet Co*., 2018 WL 4623562. The decision merits study as courts continue to struggle with the reach, if any, of manifest disregard and the extent that any merits review survives or should survive.

Injunction carveouts

Chapter 10 covers those situations in which parties subject to arbitration clauses sue initially in court, claiming that there is an emergency that leaves no time to institute an arbitration. Most modern arbitration contracts have so-called "injunction carve-outs" that permit judicial intervention to preserve the status quo until the arbitration determines the merits. There is also a common law doctrine that permits this even without a carve-out clause.

I have found in my own cases that parties can abuse this commonly understood exception and attempt to avoid arbitration when pursuing *any* kind of equitable relief rather than just emergency equitable relief. It is one thing to rush to court to prevent the bleeding of a trade secret, and quite another to argue that the "equitable" exception means that one does not have to arbitrate a specific performance (equitable) claim that arises under a contract subject to arbitration. Since the first edition, I published an article on this entitled "Injunction Curve – Outs in Arbitration: Emergency Only, or All Equity Claims?", in the AAA arbitration section's house organ, *Alternatives*. See htpps://doi.org/10.1002/alt.21713. The article explores whether courts faced with plain language that applies the carve-out to all equitable claims should limit the carve-out to emergency situations.

Evidence from Third Parties

Chapter 9 covers the circuit split as to when and whether third parties can be compelled to give evidence in arbitration. Like manifest disregard, this is another area that cries out for Supreme Court clarification and resolution, because it is a practice point that arises in virtually every complex case where a witness is located outside of the jurisdictional "seat" of the arbitration. Under Section 7 of the FAA, as addressed at length in the book, the arbitrators can compel a witness to attend and bring documents to the hearing. Since, however, section 7 is silent as to pre-hearing powers, the circuits have split as to what arbitrators can require of third-party and in particular extra-jurisdictional witnesses during the discovery stage. In 2018 I participated in an arbitration in which the determining factor in the case was my client's ability to access third-party information from a party in Minnesota before an arbitrator sitting in New York. The options available to counsel and the ways in which we had to address different state laws caused me to publish another *Alternatives* piece on the subject, "When, Where and Whether: The Confusing Law of Third Party Evidence" found at https://doi.org/10.1002/alt.21780. I plan to introduce excerpts from this article and to devote a practical unit to accessing third party evidence in arbitration.

International Arbitration (Chapter 15)

While the book is largely devoted to domestic arbitration and what amounts to the law and practice of the FAA, my editor did suggest that we add one chapter on international arbitration. The chapter is by necessity a broad overview of a subject that has its own full casebooks and full semester courses. That said, one of the subjects covered in this broad overview is the institutional rules that govern international arbitrations. In the past several years and culminating early this year, a new set of rules has been urged on the international arbitration community by practitioners and scholars from non-common law countries and in particular from Russia and Eastern Europe. These have been called the "Prague Rules." They de-emphasize discovery and elevate the role of the arbitrator over that of the parties, in clear contravention to the common

law-favored doctrine of "party autonomy" in arbitration. The new rules may be found at www.praguerules.com.

The rules have received extensive coverage in the arbitration community and in academic commentary. The open question now is the extent to which they will be adopted in arbitrations, especially in ones concerning parties from the countries who most pushed for these new rules. The adoption of any rules still requires consensus and there is, to date, a sharp lack of consensus in the overall community as to the wisdom of these rules. Following this will be interesting, timely, and will present a cross-cultural look at arbitration, and so I plan to include a new unit within chapter 15 that addresses this development.

I hope this overview is useful and I of course welcome any comments, suggestions or critiques. I greatly appreciate your using my book.

Sincerely,

Matthew H. Adler