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# NOTES

## ARBITRATION AND FORUM SELECTION CLAUSES IN INTERNATIONAL BUSINESS: THE SUPREME COURT TAKES AN INTERNATIONALIST VIEW

### I. INTRODUCTION

In recent years, the tremendous increase in American participation in international commerce has led to ever-increasing commercial contacts between Americans and citizens of other nations. These multinational contacts have brought about complex legal relationships which have resulted in conflict of laws and jurisdictional problems, which in turn have generated unwelcome uncertainty in international business transactions. One response to this uncertainty has been the insertion in international business contracts of arbitration or forum selection clauses—both to invoke the parties' chosen place and manner of dispute resolution and, in some cases, to avoid the possible extraterritorial application of American law. But arbitration and forum selection clauses have not always been enforced. Two recent Supreme Court decisions<sup>1</sup> have addressed the use of such clauses in the international business environment. In these decisions, the Court has held that there are certain inherent limitations on the transnational application of American law and that judicial application of American law might vary in the international as opposed to the domestic context. One decision enforced an arbitration clause; the other enforced a forum selection clause. This Note will examine the development of extraterritorial application of American law; the use of arbitration and forum selection clauses in an international context; and the implications of the Supreme Court's two recent decisions in this field. Some particular attention will be given the Securities Exchange Act of 1934<sup>2</sup> since a number of the decisions in this field have involved that Act and it provides, therefore, a convenient and pertinent example for discussion.

### II. EXTRATERRITORIAL APPLICATION OF AMERICAN LAW

The jurisdiction of a state and its concurrent ability to apply its law to a particular situation<sup>3</sup> traditionally were based on a territorial principle—the state could impose its will on individuals for acts committed within its

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1. *Scherk v. Alberto-Culver Co.*, 94 S. Ct. 2449 (1974); *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972).

2. Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78hh (1970).

3. This section, in treating the extraterritorial application of American law, attempts to provide, very briefly, a legal background for the discussion that will follow on arbitration and forum selection clauses in an international context. The section does not purport to treat the closely related and very difficult subject of conflict of laws. The Byzantine complexities of that subject are treated, fully and with great erudition, in the following works. A. Ehrenzweig, *Private International Law* (1972); A. Ehrenzweig, *A Treatise on the Conflict of Laws* (1962); H. Goodrich & E. Scoles, *Conflict of Laws* (4th ed. 1964); R. Leflar, *American Conflicts Law* (rev. ed. 1968); R. Weintraub, *Commentary on the Conflict of Laws* (1971).

borders.<sup>4</sup> This basis subsequently has been expanded by the development of other grounds for the assertion of jurisdiction.<sup>5</sup> For example, the use of nationality as a basis for the application of domestic law is now well recognized. "A state has jurisdiction to prescribe a rule of law . . . attaching legal consequences to conduct of a national of the state wherever the conduct occurs . . ."<sup>6</sup> The national interest of the forum state also has been used as a basis for the extraterritorial application of its law. The national interest theory may be regarded as an outgrowth of a protective principle, which was traditionally restricted to activities that threatened the security of the state or its governmental functions<sup>7</sup> but which has expanded to include areas of law involving long standing public policy and overriding public interest.<sup>8</sup> American courts have given extraterritorial effect to the antitrust statutes, "cornerstones of this nation's economic policies,"<sup>9</sup> on such a rationale.

4. Committee on International Law, Report, 21 Record of N.Y.C.B.A. 240, 244-45 (1966); R. Leflar, *American Conflicts Law* 3-4 (rev. ed. 1968); Note, *Extraterritorial Application of the Securities Exchange Act of 1934*, 69 Colum. L. Rev. 94, 95-96 (1969).

5. Four principles have been used to describe these other grounds: (1) the nationality principle under which jurisdiction is based on the nationality of the person committing the offense; (2) the protective principle which is designed to protect national interests; (3) the universality principle which is based on having custody of the individual who committed the offense; and (4) the passive personality principle which uses the nationality of the person injured as the basis for jurisdiction. Committee on International Law, Report, 21 Record of N.Y.C.B.A. 240, 245 (1966).

6. Restatement (Second) of Foreign Relations Law of the United States § 30(1) (1965); see R. Leflar, *American Conflicts Law* 45-46 (rev. ed. 1968). The Supreme Court has recognized the use of nationality as a basis for the application of domestic law with the caveat that "the rights of other nations or their nationals . . . not [be] infringed." *Lauritzen v. Larsen*, 345 U.S. 571, 587 (1953), quoting *Skiriotes v. Florida*, 313 U.S. 69, 73 (1941).

Where corporations are involved the determination of nationality may be difficult. Place of incorporation is important, but not necessarily controlling. The corporation's principal place of business, as well as the nationality of its investors and management, may be considered. Vagts, *The Corporate Alien: Definitional Questions in Federal Restraints on Foreign Enterprise*, 74 Harv. L. Rev. 1489, 1490, 1526-50 (1961). See also Note, *The "Nationality" of International Corporations Under Civil Law and Treaty*, 74 Harv. L. Rev. 1429 (1961).

7. Restatement (Second) of Foreign Relations Law of the United States § 33 (1965).

8. *Joseph Muller Corp. Zurich v. Societe Anonyme de Gerance et D'Armement*, 451 F.2d 727, 729 (2d Cir. 1971), cert. denied, 406 U.S. 906 (1972).

9. *United States v. First Nat'l City Bank*, 396 F.2d 897, 903 (2d Cir. 1968); see *Pacific Seafarers, Inc. v. Pacific Far E. Line, Inc.*, 404 F.2d 804 (D.C. Cir. 1968), cert. denied, 393 U.S. 1093 (1969); Kintner & Hallgarten, *Application of United States Antitrust Laws to Foreign Trade and Commerce—Variations on American Banana Since 1909*, 15 B.C. Ind. & Com. L. Rev. 343 (1973).

An earlier case, *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945), gave extraterritorial effect to the American antitrust laws based on an objective territorial principle (discussed at note 10 infra and accompanying text). Said Judge Learned Hand: "Both agreements would clearly have been unlawful, had they been made within the United States; and it follows . . . that both were unlawful, though made abroad, if they were intended to affect imports and did affect them." *Id.* at 444.

In *Hellenic Lines Ltd. v. Rhoditis*, 398 U.S. 306 (1970), the Court held the Jones Act, 46 U.S.C. § 688 (1970), applicable in a personal injury action between a Greek seaman and his

The extraterritorial application of the securities laws has experienced a similar expansive development, albeit on a somewhat different rationale. In securities cases the courts have continued to rely on the old territorial principle, but have expanded it almost beyond recognition by applying it in its objective and subjective form. The objective territorial principle bases jurisdiction on acts commenced or committed outside the territory of a state but completed or having substantial effects therein.<sup>10</sup> The subjective territorial principle bases jurisdiction on some act committed within the state even though the activity is completed abroad.<sup>11</sup>

One of the earliest cases dealing with the extraterritorial application of the Securities Exchange Act of 1934 was *Kook v. Crang*.<sup>12</sup> In that case, an American purchased stock of a Canadian corporation traded on the Toronto Exchange through a Canadian broker. The only other connection with the United States was that the broker maintained an office in New York, but that office was not involved in the sale.<sup>13</sup> The American brought suit claiming a violation of the margin requirements under section 7(c) of the

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Greek corporate employer despite the fact that the contract of employment provided for the application of Greek law by a Greek court to any claims arising out of the employment. The seaman's injury occurred in American waters, but the Court did not rest its decision on that fact. Rather, the Court emphasized the operational contacts that the Greek corporation had with America (95% of its stock was held by a Greek citizen domiciled in America and its business in America was extensive) and the competitive advantage it would have over American corporations if held exempt from the Jones Act. *Rhoditis* is not an antitrust case, but the fundamental policy the decision purports to promote—economic competition—is an antitrust policy.

10. Committee on International Law, Report, 21 Record of N.Y.C.B.A. 240, 245 (1966); Note, The Extraterritorial Application of Rule 10b-5, 4 Cornell Int'l L.J. 81, 82 (1970); 10 Colum. J. Transnat'l L. 150, 152-53 (1971). The Restatement (Second) of Foreign Relations Law of the United States has incorporated the objective territorial principle. "A State has jurisdiction to prescribe a rule of law attaching legal consequences to conduct that occurs outside its territory and causes an effect within its territory, if either

(a) the conduct and its effect are generally recognized as constituent elements of a crime or tort under the law of states that have reasonably developed legal systems, or

(b) (i) the conduct and its effect are constituent elements of activity to which the rule applies; (ii) the effect within the territory is substantial; (iii) it occurs as a direct and foreseeable result of the conduct outside the territory; and (iv) the rule is not inconsistent with the principles of justice generally recognized by states that have reasonably developed legal systems." Restatement (Second) of Foreign Relations Law of the United States § 18, at 47 (1965); see text accompanying notes 17-21 *infra*. For an argument that territoriality principles should give way to interest-based analyses in transnational securities cases, see Comment, An Interest Analysis Approach to Extraterritorial Application of Rule 10b-5, 52 Texas L. Rev. 983 (1974).

11. Section 17 of the Restatement (Second) outlines the subjective territorial principle: "A state has jurisdiction to prescribe a rule of law (a) attaching legal consequences to conduct that occurs within its territory, whether or not such consequences are determined by the effects of the conduct outside the territory, and (b) relating to a thing located, or a status or other interest localized, in its territory." Restatement (Second) of Foreign Relations Law of the United States § 17, at 45 (1965); see text accompanying notes 22-27 *infra*.

12. 182 F. Supp. 388 (S.D.N.Y. 1960).

13. *Id.* at 389.

Securities Exchange Act.<sup>14</sup> The district court dismissed on the basis of section 30(b) which exempts "any person insofar as he transacts a business in securities without the jurisdiction of the United States . . . ."<sup>15</sup> The court specifically rejected the use of the telephone and mails within the United States as a basis of jurisdiction.<sup>16</sup>

Eight years later, however, the Second Circuit took a different view in *Schoenbaum v. Firstbrook*.<sup>17</sup> An American stockholder brought a derivative suit under section 10(b) and rule 10b-5<sup>18</sup> against a Canadian corporation and its directors. The stockholder alleged that the defendants had sold corporate treasury shares at market prices which, based on insider information, they knew did not represent the true value. All of the questionable transactions took place in Canada but, unlike *Kook*, the stock involved was traded on an American exchange.<sup>19</sup> Rejecting a section 30(b) defense,<sup>20</sup> the court held "that Congress intended the Exchange Act to have extraterritorial application in order to protect domestic investors who have purchased foreign securities on American exchanges and to protect the domestic securities market from the effects of improper foreign transactions in American securities."<sup>21</sup> The Second Circuit thus adopted the objective territorial principle by holding that an action consummated outside the United States will be subject to the jurisdiction of American courts if that action has significant adverse effects on American investors or exchanges.

In *Leasco Data Processing Equipment Corp. v. Maxwell*,<sup>22</sup> the Second Circuit was faced with a similar case which, however, appeared to lack the significant effect of *Schoenbaum*. In *Leasco*, the plaintiffs contended that the British defendants conspired to have Leasco purchase the stock of a British corporation at an artificially inflated price in violation of section 10(b) and rule 10b-5. Much of the negotiations had taken place abroad, and the claim of American jurisdiction was based on fraudulent statements made in New York and in transatlantic mail and telephone communications.<sup>23</sup> The court rejected the *Schoenbaum* objective territorial principle as factually inapplicable, doubting whether the "impact on an American company and its shareholders

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14. 15 U.S.C. § 78g(c) (1970).

15. *Id.* § 78dd(b).

16. 182 F. Supp. at 390.

17. 405 F.2d 200 (2d Cir.), *rev'd* on other grounds, 405 F.2d 215 (2d Cir. 1968) (en banc), cert. denied, 395 U.S. 906 (1969).

18. 15 U.S.C. § 78j(b) (1970); 17 C.F.R. § 240.10b-5 (1974).

19. 405 F.2d at 204-06.

20. The court construed section 30(b) as exempting only those who conduct a "business in securities" outside the United States and not "persons who engage in isolated foreign transactions." *Id.* at 207-08.

21. *Id.* at 206; see *Roth v. Fund of Funds, Ltd.*, 405 F.2d 421 (2d Cir. 1968), cert. denied, 394 U.S. 975 (1969). See generally Griffin, *The Power of Host Countries Over the Multinational: Lifting the Veil in the European Economic Community and the United States*, 6 *Law & Policy Int'l Bus.* 375, 398-401 (1974).

22. 468 F.2d 1326 (2d Cir. 1972).

23. *Id.* at 1330-31.

would suffice to make the statute applicable if the misconduct had occurred solely in England . . . ."<sup>24</sup> Instead, the court relied on section 17 of the Restatement (Second) of Foreign Relations Law of the United States<sup>25</sup> holding that when there was conduct within the United States, this "alone would seem sufficient from the standpoint of *jurisdiction* . . . ."<sup>26</sup> and that the making of substantial representations within the United States constituted such conduct.<sup>27</sup> Thus, whereas *Schoenbaum* had expanded the extraterritorial application of the Securities Act objectively through the significant effects test, *Leasco* did so subjectively utilizing the significant conduct test.

### III. FORUM SELECTION AND ARBITRATION AS ALTERNATIVES TO THE TRANSNATIONAL APPLICATION OF DOMESTIC STATUTES

To assure some degree of certainty regarding the legal implications of their international transactions, businessmen, as noted above, have often resorted to two devices—forum selection and arbitration clauses. These clauses have met with varying degrees of receptivity in American courts and occasionally have come into conflict with the extraterritorial application of United States law.

#### A. *The Forum Selection Clause*

Forum selection clauses historically have been frowned upon by the judiciary.<sup>28</sup> Reasons for this aversion generally include the fact that such clauses oust the court of jurisdiction,<sup>29</sup> "disturb the symmetry of the law" by

24. *Id.* at 1337. Judge Friendly also stated: "However, the language of § 10(b) of the Securities Exchange Act is much too inconclusive to lead us to believe that Congress meant to impose rules governing conduct throughout the world in every instance where an American company bought or sold a security. When no fraud has been practiced in this country and the purchase or sale has not been made here, we would be hard pressed to find justification for going beyond *Schoenbaum*." *Id.* at 1334.

25. See note 11 *supra*.

26. 468 F.2d at 1334.

27. *Id.* at 1337. In dictum, the court also stated that it saw "no reason why . . . making telephone calls and sending mail to the United States should not be deemed to constitute conduct within it." *Id.* at 1335. See *Travis v. Anthes Imperial Ltd.*, 473 F.2d 515 (8th Cir. 1973) where the court apparently followed this dictum as its basis for jurisdiction in a section 10(b) action. In *Travis*, although there was some conduct within the United States, all of the fraudulent misrepresentations were made in international mail and telephone communications. The court stated "that both the place of sending and place of receipt constitute locations in which conduct takes place when the mails or instrumentalities of interstate commerce are used to transmit communications." *Id.* at 524 n.16.

28. Judge Learned Hand told one commentator "that it was his guess that this judicial aversion dates from the time . . . judges were paid by the case and accordingly viewed arbitration and choice of forum provisions as devices that were likely to curtail their income." Reese, *The Contractual Forum: Situation in the United States*, 13 *Am. J. Comp. L.* 187, 189 (1964) [hereinafter cited as Reese].

29. *Hall v. People's Mut. Fire Ins. Co.*, 72 *Mass.* (6 Gray) 185, 192 (1856); Delaume, *Choice of Forum Clauses and the American Forum Patriae; Something Happened on the Way to the*

placing the will of the parties above that of the law,<sup>30</sup> tend to be found in adhesion contracts<sup>31</sup> and often lead to great inconvenience.<sup>32</sup> Advocates of forum selection clauses point out, however, that such clauses provide a degree of certainty required in international business dealings,<sup>33</sup> avoid many of the jurisdictional problems often found in multinational litigation,<sup>34</sup> and frequently are the result of extensive negotiations aimed at choosing a neutral forum.<sup>35</sup> Despite these latter arguments, judicial opposition to forum selection clauses has continued.<sup>36</sup>

Judge Learned Hand is given credit for adopting what is known as the modern view toward forum selection agreements. In *Krenger v. Pennsylvania R.R.*,<sup>37</sup> Judge Hand stated that there was no longer any "absolute taboo against such contracts" and that a test of reasonableness should be used in evaluating the effect to be given them.<sup>38</sup> This reasonableness test was reaffirmed by the Second Circuit in *Wm. H. Muller & Co. v. Swedish American Line, Ltd.*,<sup>39</sup> an admiralty case dealing with a choice of forum clause in a shipping contract. The case was brought under the Carriage of Goods by Sea Act,<sup>40</sup> but the court found no congressional intent to invalidate such clauses and concluded that enforceability depended on reasonableness.<sup>41</sup>

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Forum: Zapata and Silver, 4 J. Maritime L. & Com. 295, 296 (1973) [hereinafter cited as Delaume]; Reese 188.

30. *Nute v. Hamilton Mut. Ins. Co.*, 72 Mass. (6 Gray) 174, 180 (1856); Reese 188.

31. 25 Fordham L. Rev. 133, 137 (1956).

32. See Delaume 296.

33. See 25 Fordham L. Rev. 133, 136-37 (1956).

34. *Id.*

35. See Collins, Forum Selection and an Anglo-American Conflict—The Sad Case of the Chaparral, 20 Int'l & Comp. L.Q. 550, 556 (1971); Comment, The Transnational Reach of Rule 10b-5, 121 U. Pa. L. Rev. 1363, 1393-94 (1973) [hereinafter cited as The Transnational Reach of Rule 10b-5].

36. E.g., *Carbon Black Export, Inc. v. The S.S. Monrosa*, 254 F.2d 297 (5th Cir. 1958), cert. dismissed, 359 U.S. 180 (1959) (forum selection clauses against public policy).

37. 174 F.2d 556 (2d Cir.), cert. denied, 338 U.S. 866 (1949).

38. *Id.* at 561. Professor Weintraub indicates that the reasonableness test "appears to be the emerging consensus of United States courts." R. Weintraub, *Commentary on the Conflict of Laws* 163-64 (1971). The Restatement (Second) of the Conflict of Laws § 80, at 244 (1971) states: "The parties' agreement as to the place of the action cannot oust a state of judicial jurisdiction, but such an agreement will be given effect unless it is unfair or unreasonable." The official comment to this section points out that such a provision should be disregarded if there is overreaching, unequal bargaining power, or if the forum chosen would be seriously inconvenient.

39. 224 F.2d 806 (2d Cir.), cert. denied, 350 U.S. 903 (1955).

40. 46 U.S.C. §§ 1300-1315 (1970). Plaintiff alleged that § 1303(8) prohibited the enforcement of any forum selection clause. 224 F.2d at 807.

41. 224 F.2d at 807-08. Muller was subsequently overruled by *Indussa Corp. v. S.S. Ranborg*, 377 F.2d 200 (2d Cir. 1967). However, it appears that *Indussa* overruled Muller only insofar as it was in conflict with the Carriage of Goods by Sea Act (COGSA), 46 U.S.C. § 1303(8) (1970), and not in relation to its reasonableness test for forum selection clauses. Shipping contracts are usually of the adhesion variety and one of the purposes of COGSA was to prevent such contracts. *Standard Electrica, S.A. v. Hamburg Sudamerikanische Dampfschiffahrts-Gesellschaft*, 375 F.2d 943, 945 (2d Cir.), cert. denied, 389 U.S. 831 (1967); Delaume 298;

Judicial acceptance, however, was not uniform. The Fifth Circuit, in an almost identical case,<sup>42</sup> refused to enforce a forum selection clause indicating that the purpose of such clauses was to oust the court of its jurisdiction and, as such, was contrary to public policy.<sup>43</sup>

### B. *Arbitration Clauses*

Initially, the common law aversion to forum selection clauses was carried over to arbitration agreements, in some cases, with even greater vigor.<sup>44</sup> However, businessmen realized the many advantages of arbitration over traditional litigation<sup>45</sup> and, in 1925, Congress passed the Arbitration Act<sup>46</sup> with the partial intent of forcing the courts to accept the validity of agree-

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Nadelmann, *Choice-of-Court Clauses in the United States: The Road to Zapata*, 21 *Am. J. Comp. L.* 124, 134 (1973).

42. *Carbon Black Export, Inc. v. The S.S. Monrosa*, 254 F.2d 297 (5th Cir. 1958), cert. dismissed, 359 U.S. 180 (1959).

43. *Id.* at 300-01.

44. Judge Cardozo, in discussing forum selection clauses and arbitration agreements stated: "Indeed, the considerations adverse to the validity of the contract are more potent in the latter circumstances, for in the one case we yield to regular and duly organized agencies of the state and in the other to informal and in a sense irregular tribunals." *Meacham v. Jamestown, F. & C. R.R.*, 211 N.Y. 346, 353, 105 N.E. 653, 655 (1914). Critics of arbitration point out that there is little respect for precedent, with a consequent inconsistency of result; that there are fewer safeguards such as adherence to the rules of evidence; that there is no judicial review for errors of law or fact; and that there is a limited ability to appeal. *Burchell v. Marsh*, 58 U.S. (17 How.) 344, 349 (1854) (no judicial review for errors of law or fact); *American Almond Prods. Co. v. Consolidated Pecan Sales Co.*, 144 F.2d 448, 450-51 (2d Cir. 1944) (no need to follow the rules of evidence); *Mutual Benefit Health & Accident Ass'n v. United Cas. Co.*, 142 F.2d 390 (1st Cir.), cert. denied, 323 U.S. 729 (1944) (arbitration binding despite errors of law); *Lentine v. Fundaro*, 29 N.Y.2d 382, 385, 278 N.E.2d 633, 635, 328 N.Y.S.2d 418, 421 (1972) (arbitrators are not bound by substantive law or rules of evidence); see 1 J. Wigmore, *A Treatise on the Anglo-American System of Evidence in Trials at Common Law* § 4e (3d ed. 1940); Kawakami & Henderson, *Arbitration in U.S./Japanese Sales Disputes*, 42 *Wash. L. Rev.* 541, 543-44 (1967); Phillips, *A Lawyer's Approach to Commercial Arbitration*, 44 *Yale L.J.* 31, 36-37 (1934).

45. Arbitration is considered an efficient, informal, flexible, confidential, quick, and inexpensive manner of handling disputes. In addition, arbitral tribunals often utilize individuals who are familiar with the customs and practices of the trade. It is particularly well suited to the settlement of international disputes where the inconvenience, expense, and uncertainty caused by jurisdictional and conflict of laws problems often make multi-national litigation all but an impossibility. *American Almond Prods. Co. v. Consolidated Pecan Sales Co.*, 144 F.2d 448, 450 (2d Cir. 1944); Kawakami & Henderson, *Arbitration in U.S./Japanese Sales Disputes*, 42 *Wash. L. Rev.* 541, 542, 545 (1967); McMahon, *Implementation of the United Nations Convention on Foreign Arbitral Awards in the United States*, 2 *J. Maritime L. & Com.* 735 (1971). For a discussion of the rules and procedures used in international arbitration, see Cohn, *The Rules of Arbitration of the International Chamber of Commerce*, 14 *Int'l & Comp. L.Q.* 132 (1965); Eisemann, *Arbitrations under the International Chamber of Commerce Rules*, 15 *Int'l & Comp. L.Q.* 726 (1966).

46. Arbitration Act of 1925, 9 U.S.C. §§ 1 et seq. (1970). Sections 1 and 2 of the Act limit its scope to arbitration agreements in contracts or transactions which are either maritime or involve interstate or foreign commerce. See Evans & Ellis, *International Commercial Arbitration: A Comparison of Legal Regimes*, 8 *Texas Int'l L.J.* 17, 18-28 (1973).



ments to arbitrate.<sup>47</sup> Faced with such specific legislative action, the courts have given increasing support to arbitration agreements—so much so, that calls are now being heard to restrict the scope of the acceptance of such agreements.<sup>48</sup>

However, one significant exception was made to the judicial acceptance of arbitration agreements. In *Wilko v. Swan*,<sup>49</sup> the Supreme Court refused to enforce an arbitration clause in a securities contract (not involving any international aspects) holding that “the protective provisions of the Securities Act require the exercise of judicial direction to fairly assure their effectiveness . . . .”<sup>50</sup> *Wilko* involved an action brought against a brokerage firm under section 12(2) of the Securities Act of 1933.<sup>51</sup> *Wilko* claimed that he purchased stock on the basis of false representations made by the broker.<sup>52</sup> The defendant firm moved for dismissal pursuant to section 3 of the United States Arbitration Act<sup>53</sup> claiming that the agreement between the parties had specified arbitration as the method of settling disputes. *Wilko*, however, claimed that the arbitration agreement was void according to section 14 of the Securities Exchange Act of 1933,<sup>54</sup> since the arbitration agreement was a “condition, stipulation, or provision” which was designed to force him to waive his access to the courts which was guaranteed by section 22 of the

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47. See H.R. Rep. No. 96, 68th Cong., 1st Sess. (1925) which stated: “Arbitration agreements are purely matters of contract, and the effect of the bill is simply to make the contracting party live up to his agreement. He can no longer refuse to perform his contract when it becomes disadvantageous to him. An arbitration agreement is placed upon the same footing as other contracts, where it belongs.” (quoted in *Standard Magnesium Corp. v. Fuchs*, 251 F.2d 455, 457-58 (10th Cir. 1957)).

48. See Note, *The Consequences of a Broad Arbitration Clause Under the Federal Arbitration Act*, 52 B.U.L. Rev. 571 (1972).

49. 346 U.S. 427 (1953).

50. *Id.* at 437.

51. Section 12(2) provides: “Any person who—offers or sells a security . . . by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact . . . and who shall not sustain the burden of proof that he did not know . . . shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction . . . .” 15 U.S.C. § 77l(2) (1970).

52. The broker recommended the purchase of stock in a company on the basis of a supposed merger with a larger corporation and implied that there would be significant speculative profits. However, he failed to inform *Wilko* that some or all of the stock he was purchasing was being sold by a director of the subject corporation. 346 U.S. at 428-29.

53. Section 3 of the Arbitration Act, 9 U.S.C. § 3 (1970), provides: “If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement . . . .”

54. Section 14, 15 U.S.C. § 77n (1970), provides: “Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void.”

Act.<sup>55</sup> The Court recognized the conflict between the two congressional acts, pointing out that the purpose of the Arbitration Act was "to secure prompt, economical and adequate solution of controversies through arbitration"<sup>56</sup> whereas the Securities Act was "[d]esigned to protect investors" and "created a special right to recover for misrepresentation."<sup>57</sup>

The Court held that the agreement to arbitrate was a "stipulation" under section 14 of the Securities Act and, as such, was void.<sup>58</sup> Even though the arbitration agreement bound the arbitrators to adhere to the Securities Act,<sup>59</sup> the Court indicated that the effectiveness of the Act would be less "in arbitration as compared to judicial proceedings."<sup>60</sup> Arbitration of this type of fraud required "subjective findings" of fact on the part of the arbitrators without any "judicial instruction on the law."<sup>61</sup> Since arbitrators can make awards "without explanation of their reasons and without a complete record," the Court felt that there was no possible way to judicially review their interpretations of the law short of a "manifest disregard" of it.<sup>62</sup> Lacking such judicial review and feeling a need for judicial interpretation of the Securities Act provisions, the Court refused to enforce the arbitration agreement.<sup>63</sup>

*Wilko*, if read broadly to embrace the international context, thus added another facet to the extraterritorial application of American securities law. Not only did American law apply to international dealings in securities which produce "significant effects" within the United States or in which there was some "significant conduct" within our borders,<sup>64</sup> but it also precluded a foreign businessman from agreeing to arbitrate or choosing a neutral forum to settle disputes in which American securities laws might control.<sup>65</sup> American courts would not be "ousted" of their jurisdiction.

#### IV. *Zapata* AND *Scherk*: A REJECTION OF PAROCHIALISM

##### A. *Forum Selection*

In two recent decisions, the Supreme Court has taken a radically different view of forum selection clauses and arbitration agreements insofar as they

55. Section 22(a), 15 U.S.C. § 77v(a) (1970), provides in part: "The district courts of the United States . . . shall have jurisdiction . . . concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this subchapter."

56. 346 U.S. at 438.

57. *Id.* at 431.

58. *Id.* at 434-35.

59. *Id.* at 433-34.

60. *Id.* at 435.

61. *Id.* at 435-36.

62. *Id.* at 436-37.

63. *Id.* Justice Frankfurter pointed out that since failure to observe the law would constitute grounds for vacating the award, "appropriate means for judicial scrutiny must be implied, in the form of some record or opinion, however informal, whereby such compliance will appear, or want of it will upset the award." He went on to say that the majority ruling would be appropriate in a case of unequal bargaining power or over-reaching, but such was not the case in *Wilko*. *Id.* at 440 (Frankfurter, J., dissenting).

64. See notes 17-27 *supra* and accompanying text.

65. See *The Transnational Reach of Rule 10b-5*, at 1393-94.

apply to international transactions. In *The Bremen v. Zapata Off-Shore Co.*,<sup>66</sup> the Court was faced with an admiralty case involving a forum selection clause. Zapata, an American corporation, had contracted with Unterweser, a German corporation, to have Zapata's oceangoing oil drilling rig towed to Europe.<sup>67</sup> The contract contained a clause specifying that all disputes would be settled before the London Court of Justice and two exculpatory clauses relieving Unterweser of any liability for defects of navigation or damage to the drill.<sup>68</sup> The drill was damaged during a storm and towed to Tampa, Florida where Zapata instituted a suit for damages.<sup>69</sup> The district court<sup>70</sup> and the Fifth Circuit,<sup>71</sup> relying on *Carbon Black Export, Inc. v. The S.S. Monrosa*,<sup>72</sup> refused to dismiss the suit in favor of the British courts. The Fifth Circuit also relied on the fact that British courts would enforce the exculpatory clauses which, according to *Bisso v. Inland Waterways Corp.*,<sup>73</sup> were contrary to United States public policy.<sup>74</sup>

Chief Justice Burger, writing for the Court,<sup>75</sup> immediately rejected the "parochial concept that all disputes must be resolved under our laws and in our courts."<sup>76</sup> He went on to say:

[I]n an era of expanding world trade and commerce, the absolute aspects of the doctrine of the *Carbon Black* case have little place and would be a heavy hand indeed on the future development of international commercial dealings by Americans. We cannot have trade and commerce in world markets and international waters exclusively on our terms, governed by our laws, and resolved in our courts.<sup>77</sup>

The argument that forum selection clauses oust a court of jurisdiction was rejected as "hardly more than a vestigial legal fiction" designed to protect "the

66. 407 U.S. 1 (1972). For a discussion on the creation of a climate favorable to a Zapata ruling, see Nadelmann, Choice-of-Court Clauses in the United States: The Road to Zapata, 21 Am. J. Comp. L. 124, 127-34 (1973).

67. 407 U.S. at 2.

68. Id. at 2-3 & n.2.

69. Id. at 3-4.

70. 296 F. Supp. 733 (M.D. Fla. 1969), aff'd, 428 F.2d 888 (5th Cir. 1970), vacated, 407 U.S. 1 (1972).

71. 428 F.2d 888 (5th Cir. 1970), vacated, 407 U.S. 1 (1972).

72. 254 F.2d 297 (5th Cir. 1958), cert. dismissed, 359 U.S. 180 (1959); see notes 42-43 supra and accompanying text.

73. 349 U.S. 85 (1955).

74. 428 F.2d at 894-95. The Fifth Circuit's opinion was subject to severe criticism. One commentator viewed it as demonstrating "a total disregard for the necessities of international business relations and the principle of party autonomy." Delaume 301. A British writer decried the court for its "narrow nationalism" and went on to say: "The American federal court entirely failed to appreciate that choice of jurisdiction in an international commercial transaction is not a minor clause relating to machinery but very often a vital factor in negotiations. Every practitioner must know of cases where contracts would never have been entered into but for the choice of some particular law or jurisdiction. If such choices are to be so freely disregarded the whole point of having a rational system of private international law will have disappeared." Collins, Forum Selection and an Anglo-American Conflict—The Sad Case of the Chaparral, 20 Int'l & Comp. L.Q. 550, 557 (1971).

75. The decision was 8-1, Justice Douglas dissenting.

76. 407 U.S. at 9.

77. Id.

power and business of a particular court." Such arguments have "little place in an era when all courts are overloaded and when businesses once essentially local now operate in world markets."<sup>78</sup>

The Court declared that forum selection clauses are prima facie valid unless enforcement can be shown to be unreasonable.<sup>79</sup> Such agreements made "in an arm's-length negotiation by experienced and sophisticated businessmen" should be enforced "absent some compelling and countervailing reason."<sup>80</sup> The Court recognized that the acceptance of a neutral forum by both parties was the result of extensive negotiations aimed at the elimination of the uncertainties so often found in international business dealings and, as such, should be enforced.<sup>81</sup>

Perhaps even more significant than the strong language used by the Chief Justice was the manner in which the Court distinguished the *Bisso* doctrine that exculpatory clauses were against public policy.<sup>82</sup> The Court pointed out that *Bisso* dealt with a similar situation strictly within American waters and therefore was "not controlling in an international commercial agreement."<sup>83</sup> The Court implied that international commercial agreements would be placed on a footing different from those in a purely domestic context.<sup>84</sup> *Zapata*, however, was an admiralty case and it was not clear whether such an interpretation would be restricted to admiralty. It also was unclear whether the decision forecast a trend toward a more liberal approach to the enforceability of clauses in international contracts generally.

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78. *Id.* at 12.

79. *Id.* at 10. The Court analogized to *National Equip. Rental, Ltd. v. Szukhent* which held: "[I]t is settled . . . that parties to a contract may agree in advance to submit to the jurisdiction of a given court, to permit notice to be served by the opposing party, or even to waive notice altogether." 375 U.S. 311, 315-16 (1964). But see 8 Texas Int'l L.J. 85 (1973) where the author argued that, in *Szukhent*, "the real issue was the adequacy of service under Rule 4(d) of the Federal Rules of Civil Procedure" and that the *Zapata* reference to *Szukhent* was nothing more than "a questionable attempt to embellish the instant holding with a sense of continuity." *Id.* at 90.

80. 407 U.S. at 12. Such compelling reasons were described as "fraud, undue influence, or overweening bargaining power." The Court required the showing of one of these compelling reasons before the forum selection clause would be dishonored. *Id.* at 12-13, 15. Inconvenience was almost totally rejected as a compelling reason when the Court stated: "[I]t should be incumbent on the party seeking to escape his contract to show that trial in the contractual forum will be so gravely difficult and inconvenient that he will for all practical purposes be deprived of his day in court. Absent that, there is no basis for concluding that it would be unfair, unjust, or unreasonable to hold that party to his bargain." *Id.* at 18.

81. *Id.* at 13-14; see Collins, *Forum Selection and an Anglo-American Conflict—The Sad Case of the Chaparral*, 20 Int'l & Comp. L.Q. 550, 556-57 (1971). The author pointed out that businessmen who negotiated the *Zapata* type of contract "know their law" and "know their courts." *Id.* at 556.

82. See notes 73-74 *supra* and accompanying text.

83. 407 U.S. at 15-16.

84. See 58 Cornell L. Rev. 416, 421 (1973).

B. *Arbitration Clauses*

Two years later, the Supreme Court answered these questions in *Scherk v. Alberto-Culver Co.*<sup>85</sup> Alberto-Culver was an American corporation which entered negotiations with Scherk, a German national, regarding the purchase of three European business corporations and the licensing of certain trademarks associated with them. Negotiations extended over a period of three years and culminated in a purchase agreement which included express warranties that Scherk had sole and unencumbered rights to the trademarks.<sup>86</sup> The contract also contained a clause which provided for the settlement of all disputes by arbitration before the International Chamber of Commerce in Paris with the laws of the State of Illinois controlling.<sup>87</sup>

Approximately one year later, Alberto-Culver discovered that the trademarks were seriously encumbered and, as a result, offered to return the properties and rescind the contract. When Scherk refused, Alberto-Culver brought an action in a federal district court claiming that the fraudulent representations violated section 10(b) of the Securities Exchange Act of 1934.<sup>88</sup> Scherk responded by seeking a stay of the action pending arbitration; Alberto-Culver countered by seeking an injunction restraining arbitration. The Court of Appeals for the Seventh Circuit,<sup>89</sup> relying on *Wilko*,<sup>90</sup> decided in favor of Alberto-Culver and enjoined the arbitration.<sup>91</sup> The Supreme Court reversed, holding that an agreement to arbitrate disputes arising out of international commercial transactions "is to be respected and enforced by the federal courts in accord with the explicit provisions of the Arbitration Act."<sup>92</sup>

The Supreme Court initially ruled that, since the *Scherk* transactions involved commerce with foreign nations, the Arbitration Act of 1925<sup>93</sup> was applicable as it was in *Wilko*.<sup>94</sup> The Court also pointed out that since *Wilko* dealt with the Securities Act of 1933 and *Scherk* involved the Securities Exchange Act of 1934, "a colorable argument could be made that even the semantic reasoning of the *Wilko* opinion does not control . . ."<sup>95</sup> Nonethe-

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85. 94 S. Ct. 2449 (1974).

86. *Id.* at 2451-52.

87. *Id.* at 2452.

88. 15 U.S.C. § 78j(b) (1970).

89. 484 F.2d 611 (7th Cir. 1973), rev'd, 94 S. Ct. 2449 (1974).

90. See notes 49-63 *supra* and accompanying text.

91. The Seventh Circuit pointed out that Zapata would be controlling if the transaction did not come under the securities law. 484 F.2d at 614-15.

92. 94 S. Ct. at 2457 (footnote omitted).

93. 9 U.S.C. §§ 1 et seq. (1970). The Court placed emphasis on sections 2-4. 94 S. Ct. at 2453. Section 2 provides that arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2 (1970). *Id.* § 3 permits federal courts to stay any pending action until "such arbitration has been had . . ." *Id.* § 4 authorizes the court to issue "an order directing the parties to proceed to arbitration in accordance with the terms of the agreement." See notes 45 & 52 *supra*.

94. See notes 53-56 *supra* and accompanying text.

95. 94 S. Ct. at 2454. The Court did not rule on whether the purchase of Scherk's business was a security transaction under section 10(b) of the Securities Exchange Act of 1934 since that judgment of the Seventh Circuit was not appealed. *Id.* at 2455 n.8. Justice Douglas, in his

less, the Court decided, for purposes of this case, to treat the pertinent provisions of both acts in a similar manner<sup>96</sup> and distinguished *Wilko* on different grounds.

The "significant" and "crucial" difference between *Wilko* and *Scherk* was that the latter dealt with "a truly international agreement."<sup>97</sup> The Court listed the three factors which made the agreement "international." First, the parties to the agreement were of different nationalities with the bulk of their activities in their respective home countries. Second, the negotiations took place in three nations and involved legal and trademark experts from four nations. Finally, and most significantly, the "subject matter" involved the sale of businesses incorporated in Europe and their "activities were largely, if not entirely, directed to European markets."<sup>98</sup> In *Wilko*, on the other hand, the parties, negotiations, and subject matter were all situated in the United States, and "there was no question but that the laws of the United States generally, and the federal securities laws in particular, would govern disputes . . ."<sup>99</sup> In international agreements, however, there is always a great deal of uncertainty as to which country's law will be applicable to disputes. Echoing *Zapata*, the Court went on to say:

A contractual provision specifying in advance the forum in which disputes shall be litigated and the law to be applied is, therefore, an almost indispensable precondition to achievement of the orderliness and predictability essential to any international business transaction.<sup>100</sup>

The Court also pointed out that a "parochial refusal" to enforce international arbitration agreements could lead to "destructive jockeying" by the parties as each attempted to secure advantages from courts of various countries. The problems of conflicting judgments from different nations' courts would create a "dicey atmosphere" which "would surely damage the fabric of international commerce and trade, and imperil the willingness and ability of businessmen to enter into international commercial agreements."<sup>101</sup> This atmosphere would also make the *Wilko* rationale of protecting access to the courts "chimerical" since such access could easily be blocked or hindered by the opposing party's resort to foreign tribunals.<sup>102</sup> Describing an agreement to arbitrate as, "in effect, a specialized kind of forum-selection clause," the Court concluded by recognizing the need to reject parochialism while

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dissent, agreed with the Seventh Circuit that the Securities Exchange Act was controlling. *Id.* at 2458-59 (dissenting opinion). See generally *Movielab, Inc. v. Berkey Photo, Inc.*, 452 F.2d 662 (2d Cir. 1971); *Lawrence v. SEC*, 398 F.2d 276 (1st Cir. 1968).

96. 94 S. Ct. at 2455.

97. *Id.*

98. *Id.*

99. *Id.* The plaintiff in *Scherk* desired to limit *Wilko* to situations where there was unequal bargaining power since the arbitration clause in *Wilko* was contained in a standard form margin contract. The Court, however, pointed out that lack of choice had not been demonstrated in *Wilko* and proceeded to decide the case on other grounds. *Id.* at 2454 n.6.

100. *Id.* at 2455.

101. *Id.* at 2456.

102. *Id.*

encouraging the certainty which constitutes an "indispensable element" in international commerce.<sup>103</sup>

#### V. CONCLUSION

The holdings of *Zapata* and *Scherk* are quite clear. In international trade and commerce, "experienced and sophisticated" businessmen will no longer be able to depend on American law and American courts to protect them from unwise business dealings. If American businessmen agree to the settlement of disputes either in a foreign forum or through the process of arbitration, the expectations of the parties must be met. The requirements of international commerce and the degree of certainty required by businessmen in such a milieu necessitate a rejection of a "parochial" outlook toward foreign tribunals or arbitration boards. An American businessman will no longer be able to "repudiate his solemn promise."<sup>104</sup>

The *Zapata* and *Scherk* holdings, however, were not without qualifications. In both cases, the agreements in question were what the Court in *Scherk* described as "truly international."<sup>105</sup> Although somewhat vague as to which factors make an agreement truly international or essentially American, the Court did provide some general guidelines. To qualify as international, the parties, the negotiations, and the subject matter of the agreement must have a substantially international character as was demonstrated in *Scherk*.<sup>106</sup> Such agreements "touching" two or more countries almost inevitably result in considerable uncertainty as to which nation's substantive and conflict of laws rules will apply.<sup>107</sup> The purpose of the Court's rulings was to eliminate this uncertainty by providing judicial recognition to the parties' resolution of the problem through forum selection or arbitration agreements. Such a solution "obviates the danger" that the dispute will be submitted to a forum hostile to one of the parties and it also helps to avoid the "dicey atmosphere" which might result from conflicting rulings of courts of various nations.<sup>108</sup>

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103. *Id.* at 2457. Justice Stewart pointed out that the holding of the Court was confirmed by the rationale of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 10, 1958, [1970] 3 U.S.T. 2517, T.I.A.S. No. 6997, 330 U.N.T.S. 3, and the United States enabling legislation. 9 U.S.C. ch. 2 (1970). He stated that the goal of the Convention was "to encourage the recognition and enforcement of commercial arbitration agreements in international contracts and to unify the standards by which agreements to arbitrate are observed . . ." 94 S. Ct. at 2457 n.15. The Court did not use the Convention as a basis for its opinion and did not reach the question whether the Convention would have served as an alternate basis for enforcing the arbitration agreement. *Id.* at 2457-58 n.15. On the Convention and its enforcement, see *Island Territory of Curacao v. Solitron Devices, Inc.*, 489 F.2d 1313 (2d Cir. 1973), cert. denied, 94 S. Ct. 2389 (1974); *In re Fotochrome Inc.*, 377 F. Supp. 26 (E.D.N.Y. 1974); Firth, *The Finality of a Foreign Arbitral Award*, 25 *Arb. J.* 1 (1970); Quigley, *Convention on Foreign Arbitral Awards*, 58 *A.B.A.J.* 821 (1972); Quigley, *Accession by the United States to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards*, 70 *Yale L.J.* 1049 (1961).

104. 94 S. Ct. at 2457.

105. *Id.* at 2455.

106. *Id.*

107. *Id.*; see note 131 *infra*.

108. 94 S. Ct. at 2455-56.

What is essentially American is best illustrated by *Wilko*. In that case, both the parties were American; all of the negotiations took place domestically; the subject matter of the negotiations was American securities; and there was no doubt that American securities laws were the only ones applicable to the transaction.<sup>109</sup> Thus, the uncertainty as to conflict of laws, which was the primary variable in *Zapata* and *Scherk*, was not present and, consequently, there was no doubt that the transaction was "essentially American."

Obviously, these guidelines are not all-encompassing and, as the Court recognized in *Scherk*,<sup>110</sup> we will have to await future litigation for more precise rules. However, the Court did address certain problem areas. An agreement between two Americans to settle disputes before a foreign court or arbitrators will under *Zapata* suggest the question whether the agreement was of the adhesion variety.<sup>111</sup> Similarly, the selection of a foreign forum to settle disputes that are "essentially American" might contravene a public policy of the United States.<sup>112</sup> Justice Douglas, in his dissent in *Scherk*, expressed the fear that various multinational corporations might utilize the holding to circumvent American statutes which should control their actions.<sup>113</sup> However, the requirement that the agreements be truly international, the rejection of adhesion agreements and those contrary to public policy, as well as the ability of federal courts to pierce the nationality veil,<sup>114</sup> should be sufficient to prevent the abuse of the *Zapata* and *Scherk* rulings.

It has also been said that the relegation of an American to a foreign forum or arbitral tribunal could lead to a loss of substantive rights.<sup>115</sup> It is true that foreign courts may have different substantive and procedural rules; it is also true that arbitral awards are not subject to review for errors of law or fact and that a reasoned opinion is not required.<sup>116</sup> But these arguments are merely the traditional ones against forum selection and arbitration. In the case of arbitration awards, overly technical judicial review would defeat the primary purpose of arbitration—speed, efficiency, and informality.<sup>117</sup> The Court in *Zapata* and *Scherk* limited its rulings to experienced and sophisticated businessmen. The American parties in those cases were major corpora-

109. *Id.* at 2455.

110. *Id.* at 2456 n.11.

111. 407 U.S. at 17.

112. *Id.* Article V 2(b) of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards authorizes the courts of a participating country to reject an arbitration agreement if it is "contrary to the public policy of that country." [1970] 3 U.S.T. 2517, T.I.A.S. No. 6997, 330 U.N.T.S. 3, Article V, para. 2(b).

113. 94 S. Ct. at 2463-64 (Douglas, J., dissenting).

114. See *SEC v. Gulf Intercontinental Fin. Corp.*, 223 F. Supp. 987, 995 (S.D. Fla. 1963) (the court looked through the "transparent fabric" of the defendants' scheme to observe that a nominally Canadian corporate defendant was a mere conduit for the American corporate defendants); II A. Ehrenzweig & E. Jayme, *Private International Law* 128-29 (1973).

115. 407 U.S. at 23 (Douglas, J., dissenting).

116. *Kawakami & Henderson, Arbitration in U.S./Japanese Sales Disputes*, 42 Wash. L. Rev. 541, 543 (1967); see note 44 *supra*.

117. *Federal Commerce & Navigation Co. v. Kanematsu-Gosho, Ltd.*, 457 F.2d 387, 389 (2d Cir. 1972); see note 45 *supra*.



tions that had access to extensive legal advice before entering into contracts. Such businessmen (or businesswomen) must now consider the procedural and substantive limitations of a foreign forum or arbitral tribunal before entering into such a contract.

In addition, American courts still provide an adequate opportunity to be heard. In the case of arbitration, access to the courts is available through motions to compel or stay arbitration, to stay court proceedings pending arbitration or to confirm the award.<sup>118</sup> Similar access is available in the case of forum selection as was demonstrated in *Zapata*. At any of these points, an American party can show cause why the particular agreement should not be enforced, but he must show "compelling reasons" such as fraud, undue influence or overweening bargaining power.<sup>119</sup> Sophisticated businessmen will no longer be able to plead reasons such as inconvenience when these should have been considered at the time of the contract negotiations.<sup>120</sup> Businessmen have been put on notice that when negotiating contracts, they must be aware of forum selection or arbitration clauses and, if desired, expressly designate the laws which are to be controlling, the issues to be arbitrated, and the powers of the arbitrators.

One final question that should be addressed is the effect of *Zapata* and *Scherk* on the extraterritorial application of American securities law. *Scherk* arguably has removed any prohibition of arbitration agreements in international securities transactions that *Wilko* may have imposed—at least so far as experienced and sophisticated business executives are concerned. This permission of arbitration in "truly international" agreements is similar to the exemption permitting arbitration of disputes between various members of organized stock exchanges.<sup>121</sup> In the latter instance, the securities laws were construed as providing protection for individual investors and were not designed to protect "dealers from the improprieties of fellow dealers."<sup>122</sup> In essence, *Scherk* could be read as holding that the securities laws likewise were not designed to protect large multinational corporations. However, the question of the protection of the individual investor in such corporations would still remain. Justice Douglas described these "corporate giants" as "guardians of a host of wards unable to care for themselves,"<sup>123</sup> and it was these wards whom the securities laws were designed to protect. He also pointed out that these investors could be the victims of the actions of the multi-national corporations.<sup>124</sup> The majority opinion responded to such criticism by pointing out that *Scherk* had "no bearing on the scope of the

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118. Symposium—Arbitration and the Courts, 58 Nw. U.L. Rev. 466, 522 (1963).

119. See note 80 supra.

120. Id.

121. *Coenen v. R.W. Pressprich & Co.*, 453 F.2d 1209, 1213-14 (2d Cir.), cert. denied, 406 U.S. 949 (1972); *Axelrod & Co. v. Kordich, Victor & Neufeld*, 451 F.2d 838, 842-43 (2d Cir. 1971); *Brown v. Gilligan, Will & Co.*, 287 F. Supp. 766, 771-72 (S.D.N.Y. 1968).

122. 287 F. Supp. at 771-72.

123. 94 S. Ct. at 2461 (Douglas, J., dissenting).

124. Id. at 2464 (Douglas, J., dissenting).

substantive provisions of the federal securities laws,"<sup>125</sup> and by this seemed to imply that such questions would be answered on a case by case basis. Justice Douglas, in his dissent in *Zapata*, pointed out that the Court has "often adopted prophylactic rules rather than attempt to sort the core cases from the marginal ones."<sup>126</sup> It appears that the Court has rejected this prophylactic approach to the securities laws in international business transactions and implicitly has ruled that the impact of the transactions in *Scherk* on individual Alberto-Culver shareholders was insufficient to necessitate the application of American securities law.<sup>127</sup>

*Scherk* can also be analyzed in relation to the subjective territorial principle which provided the basis for the *Leasco* decision.<sup>128</sup> In *Scherk*, Justice Stewart pointed out that "[t]he only contacts between the United States and the transaction . . . [are] the fact that Alberto-Culver is an American corporation and the occurrence of some—but by no means the greater part—of the pre-contract negotiations [were] in this country."<sup>129</sup> These contacts were judged too insignificant to apply the *Wilko* rationale; yet, in *Leasco*, the Second Circuit found similar negotiations within the United States to be conduct sufficient to create jurisdiction.<sup>130</sup> In other words, contacts or conduct sufficient to create jurisdiction, under *Leasco*, may not be significant enough to require the application of American law, under *Scherk*.<sup>131</sup>

*Zapata* and *Scherk* place international business dealings on a plane different from domestic ones. If an American businessman agrees to submit to the jurisdiction of a foreign court or arbitration, American law and American courts will not provide the protection which the executive otherwise could have enjoyed. Businessmen and their attorneys must henceforth be conscious of the particular nuances of foreign law and arbitration rules and make an educated selection according to their particular needs and expectations. *Zapata* and *Scherk* hold that American courts cannot be relied upon to compensate for ignorance or carelessness. Such rulings are necessary "in the light of present-day commercial realities and expanding international trade"<sup>132</sup> if we wish to avoid imperiling "the willingness and ability of businessmen to enter into international commercial agreements."<sup>133</sup>

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125. Id. at 2456 n.12.

126. 407 U.S. at 24 n. (Douglas, J., dissenting).

127. The court in *Leasco* also doubted whether the impact on shareholders alone would suffice as a basis of asserting jurisdiction. See notes 24-27 *supra* and accompanying text. However, four Justices did dissent in *Scherk*.

128. See notes 11, 22-27 *supra* and accompanying text.

129. 94 S. Ct. at 2456 n.11.

130. 468 F.2d at 1334.

131. In *Scherk*, the arbitration agreement specified that the laws of the State of Illinois would apply. It is not clear whether an arbitral tribunal or a foreign court would construe this provision as requiring application of rule 10b-5 of the Securities Exchange Act of 1934. 94 S. Ct. at 2463 n.11 (Douglas, J., dissenting).

132. 407 U.S. at 15.

133. 94 S. Ct. at 2456 (footnote omitted).