

The Scope of the Federal Arbitration Act's Preemption Power: An Examination of the Import of *Saturn Distribution Corp. v. Williams*

On June 6, 1990, the United States Court of Appeals for the Fourth Circuit held that portions of the Virginia Motor Vehicle Dealer Licensing Act, prohibiting the use of nonnegotiable arbitration agreements in automobile franchise agreements, were preempted by the Federal Arbitration Act (FAA). This case was the latest in a series of cases dealing with the scope of the Federal Arbitration Act's preemption power. Because the FAA does not contain an explicit preemption provision, there has been much confusion over the years concerning the scope of FAA preemption power and exactly when a state law will be preempted.

This Note will attempt to provide order to the various cases dealing with the scope of the Federal Arbitration Act's preemption power. Part I of this Note is a discussion of the history of arbitration, leading up to and including, the enactment of the FAA, the purposes of the FAA, and the United States Supreme Court's and other federal courts' changing view of arbitration as a form of dispute resolution. Part II is a detailed discussion of the facts of the *Saturn Distribution* case and examine both the majority and the dissenting opinions. Part III is an analysis of both the majority and dissenting opinions in light of the prior case law, the purposes behind the FAA and certain public policy considerations. Finally, this Note will conclude that the Fourth Circuit's opinion in *Saturn Distribution* was incorrectly decided in light of the Dealers' Day in Court Act, which equalizes the economic advantages manufacturers have over their dealers. As a result of the Act, dealers are provided with an opportunity for judicial determination of disputes.¹

I. GENERAL BACKGROUND

A. *The History of Arbitration*

Arbitration is not a recent development. It has existed as a form of dispute resolution almost as long as humankind itself. One of the earliest examples of the use of arbitration as a form of dispute resolution comes from ancient Greece and Israel where traveling wise men, for a

1. *Hanley v. Chrysler Motors Corp.*, 433 F.2d 708 (10th Cir. 1970); *Barney Motor Sales v. Cal Sales, Inc.*, 178 F. Supp. 172 (S.D. Cal. 1959).

fee, would act as *ad hoc* arbitrators.² Despite its long history as a form of dispute resolution, arbitration faced a considerable amount of judicial hostility from the early English and American courts. In *Vynior's Case*,³ Lord Coke held that agreements to arbitrate were revocable at will, prior to the issuance of an award. Despite arguments advanced by commentators that *Vynior's Case* was incorrectly decided,⁴ it quickly became firmly entrenched in English and American courts. The common law rule regarding agreements to arbitrate quickly grew to stand for the proposition that such agreements are not enforceable because they are viewed as an attempt to deprive the courts of their jurisdiction.⁵ Thus, prior to the adoption of the Federal Arbitration Act, courts generally looked with disfavor on arbitration agreements, holding that public policy forbade the specific performance of such agreements.⁶

The common law rule remained unaltered by American courts until the late 1800's. Fueled by the English decision of *Scott v. Avery*,⁷ American courts began to hold that agreements to arbitrate were enforceable.⁸ The change in the American position is thought to be a result of the increased industrialization at the turn of the century and the increased frequency of labor and business disputes.⁹ The acceptance of arbitration as an alternative form of dispute resolution took a giant step forward in 1920 with New York's adoption of the first "modern" arbitration statute. The statute generally permitted parties to include binding agreements to arbitrate in their contracts.¹⁰

2. THOMAS H. OEHMKE, COMMERCIAL ARBITRATION § 2.3, at 19 (1987).

3. 4 Eng. Rep. 302 (1609).

4. It has been argued by author Julius Cohen that the rule of *Vynior's Case* was wrongly formulated and improperly emphasized by later courts.

It was wrongly formulated because, at that time, the law of binding contracts was just emerging and because Lord Coke confused the *Vynior* facts with situations where a person grants a power which is revocable by the grantor; [it] was improperly emphasized because, first, the rule was dictum and, second, because there were other cases, some earlier, upholding the enforceability of arbitration.

OEHMKE, *supra* note 2, at 21.

5. OEHMKE, *supra* note 2, at 19. See also *Robert Lawrence Company v. Devonshire Fabrics, Inc.*, 271 F.2d 402, 406 (2d Cir. 1959), *cert. granted*, 362 U.S. 909, and *cert. dismissed*, 364 U.S. 801 (1960).

6. *Petition of Pahlberg*, 43 F. Supp. 761 (S.D.N.Y. 1942), *appeal dismissed*, In re *Pahlberg Petition*, 131 F.2d 968 (2d Cir. 1942).

7. 5 H.L. Cas. 811 (1856) (holding that agreements to arbitrate future disputes which were limited to specific matters, did not displace the court's jurisdiction and were valid and enforceable as to those specific matters only).

8. *Snodgrass v. Gavit*, 28 Pa. 221 (1857) (holding that an agreement to arbitrate future disputes was enforceable).

9. OEHMKE, *supra* note 2, at 19.

10. N.Y. CIV. PRAC. LAW § 7501 (1980). See OEHMKE, *supra* note 2, at 19.

SCOPE OF FAA'S PREEMPTION POWER

B. *The Federal Arbitration Act*

In 1925, Congress followed New York's lead and enacted the Federal Arbitration Act.¹¹ The passage of this act was an indication of a "growing national policy favoring arbitration as an alternative form of dispute resolution permitting parties to submit their disputes to a private arbitrator rather than pursuing litigation, thus reducing the number of cases tried in the courts."¹² The FAA was enacted to combat the judicial hostility faced by arbitration at common law and to reverse the common law rules that arbitration agreements were revocable by either party at any time prior to the issuance of an arbitration award.¹³ In addition to reversing the common law rules, the FAA was enacted "to ensure that courts would honor the contractual agreements of parties who choose to resolve their disputes by means of the informal arbitration procedure"¹⁴ and "to make it possible for parties who agreed to arbitrate to avail themselves of the same legal and equitable sanctions as could parties to any other valid contract."¹⁵ Thus, under the provisions of the FAA, arbitration agreements which come within its scope are as effectively enforceable as any other contract provision.¹⁶

While the purpose of the FAA has been made relatively clear by the courts, the scope of the FAA was anything but clear until recently. In order to effectuate fully the congressional intent behind the enactment of the FAA,¹⁷ the FAA must apply equally in both state and federal courts.¹⁸ However, there was a substantial split of authority regarding the applicability of the FAA in state courts:

Many early commentators concluded that the FAA was enacted by Congress as a procedural statute applicable only in federal courts

11. 9 U.S.C. §§ 1-14 (1947). Previously known as the United States Arbitration Act.

12. ROBERT MELVIN RODMAN, *COMMERCIAL ARBITRATION WITH FORMS* § 3.9, at 70 (1984).

13. *Id.*

14. *New England Energy, Inc. v. Keystone Shipping Co.*, 855 F.2d 1, 3 (1st Cir. 1988), *motion denied*, 489 U.S. 1007, *and cert. denied*, 489 U.S. 1077 (1989)(citing *Mitsubishi Motors, Inc. v. Soler Chrysler-Plymouth*, 473 U.S. 614, 625-26 (1985); *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 219-20 (1985)).

15. Laura A. Kaster, Note, *The Consequences of a Broad Arbitration Clause Under The Federal Arbitration Act*, 52 B.U. L. REV. 571 (1972).

16. *Global Maritime Leasing Panama, Inc. v. M/S North Breeze*, 349 F. Supp. 779, 784 (D.R.I. 1972). *See also* *Scherk v. Alberto-Culver*, 417 U.S. 506, *reh'g denied*, 419 U.S. 885 (1974).

17. *See infra* notes 108-113 and accompanying text.

18. *See* *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402 (2d Cir. 1959), *cert. granted*, 362 U.S. 909, *cert. dismissed*, 364 U.S. 801 (1960). *See generally* Linda R. Hirshman, *The Second Arbitration Trilogy: The Federalization of Arbitration Law*, 71 VA. L. REV. 1305 (1985).

and that the Act, therefore, did not displace state authority in the field of arbitration. Other commentators have concluded that the FAA created a body of federal substantive law applicable in both federal and state courts.¹⁹

The majority of courts addressing this issue have held that the FAA creates a "body of federal substantive law of arbitrability, applicable to any arbitration agreements within the coverage of the Act."²⁰

The FAA was conclusively classified as substantive by the United States Supreme Court in *Southland Corp. v. Keating*.²¹ In *Keating*, the Court dealt with a dispute between the Southland Corporation, the owners and franchisors of a chain of convenience stores, and a number of their California franchisees. The franchisees filed an action in California state court alleging a laundry list of causes of action, including a violation of the California Franchise Investment Law (FIL).²² Pursuant to an arbitration clause contained in the franchise agreement,²³ the Southland Corporation moved the court to compel arbitration of the matter. The state court granted Southland's motion as to all causes of action except the violation of the FIL. The court read the FIL as requiring a judicial forum for resolution of disputes arising under it.²⁴

The United States Supreme Court held that the portion of the FIL requiring a judicial forum was in direct conflict with Section 2 of the FAA and was therefore void under the Supremacy Clause of the United States Constitution.²⁵ The Court stated that the FAA was enacted pursuant

19. Carlos R. Carrasquillo, Note, *Commercial Arbitration: Southland Corp. v. Keating — Section 2 of the Federal Arbitration Act Preempts State Law in the Field of Commercial Arbitration*, J. CORP. L., Spring 1985, at 767. See also Julius H. Cohen & Kenneth Dayton, *The New Federal Arbitration Law*, 12 VA. L. REV. 265, 275-76 (1926); Note, *Erie, Bernhardt & Section 2 of the United States Arbitration Act: A Farrago of Rights, Remedies and a Right to a Remedy*, 69 YALE L.J. 847, 863 (1960); Note, *Scope of the United States Arbitration Act in Commercial Arbitration: Problems in Federalism*, 58 NW. U. L. REV. 468, 492 (1963).

20. *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983). See also *El Hass Eng'g & Transport Co. v. American Indep. Oil Co.*, 183 F. Supp. 394 (S.D.N.Y. 1960), *rev'd on other grounds*, 289 F.2d 346 (2d Cir. 1961), and *cert. denied*, 368 U.S. 837 (1961); *Pinkis v. Network Cinema Corp.*, 512 P.2d 751 (Wash. App. 1973); *Paine, Webber, Jackson & Curtis, Inc. v. McNeal*, 239 S.E.2d 401, 403 (Ga. App. 1977); *Episcopal Hous. Corp. v. Federal Ins. Co.*, 239 S.E.2d 647, 649 (S.C. 1977); *Mamlin v. Susan Thomas, Inc.*, 490 S.W.2d 634, 636 (Tex. Civ. App. 1973).

21. 465 U.S. 1 (1984).

22. CAL. CORP. CODE §§ 3000-516 (West 1977).

23. *Southland Corp. v. Keating*, 465 U.S. 1, 3. The arbitration clause at issue in *Keating* provided: "[a]ny controversy or claim arising out of or relating to this Agreement . . . shall be settled by arbitration . . ."

24. *Id.* See generally Carrasquillo, *supra* note 19, at 773-74.

25. *Keating*, 465 U.S. 1.

SCOPE OF FAA's PREEMPTION POWER

to the Commerce Clause²⁶ and was a body of substantive law enforceable in both state and federal courts.²⁷ "In enacting [Section] 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."²⁸ "In creating a substantive rule applicable in state as well as federal courts, Congress intended to foreclose state legislative attempts to undercut the enforceability of arbitration agreements."²⁹ The Court saw nothing in the FAA indicating that the broad principle of enforceability is subject to any additional limitations under state law.³⁰ Thus, after *Keating*, it was clear that the FAA was applicable in both state and federal courts, and the states had no power to limit the use of arbitration agreements in transactions falling within the scope of the FAA. "The Supreme Court's decisions support a conclusion that all state laws seeking to *limit* the use of the arbitral process are superseded by federal law."³¹

Since the FAA does not have an explicit preemption provision, courts have come to rely on Section 2 of the FAA to implement fully the congressional intent behind the enactment of the FAA. Section 2 provides that "a written provision in any maritime transaction or a contract evidencing commerce to settle by arbitration a controversy . . . arising out of such contract or transaction, . . . shall be valid, irrevocable and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."³² "Section 2 embodies a clear federal policy

26. "The Congress shall have power . . .

[3] To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes" U.S. CONST. art. I, § 8, cl. 3.

27. *Keating*, 465 U.S. 1, 11-12. See also *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 405 (1967); *Moses H. Cone*, 460 U.S. 1, 25 n.32 (1983).

28. *Keating*, 465 U.S. 1, 10.

29. *Id.* at 16.

30. *Id.* at 11.

31. *Keystone Shipping*, 855 F.2d 1, 4 (1st Cir. 1988), *motion denied*, 489 U.S. 1007, and *cert. denied*, 489 U.S. 1077 (1989).

32. Section 2 of the FAA provides:

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon grounds as exist at law or in equity for the revocation of any contract.

9 U.S.C. § 2 (1947).

of requiring arbitration unless the agreement to arbitrate is not part of a contract evidencing interstate commerce or is revocable 'upon such grounds as exist at law or equity for the revocation of any contract.'³³ Thus, courts no longer have the power to decide matters subject to a valid arbitration agreement where that agreement is within the scope of Section 2 of the FAA. Under the FAA, the courts have been assigned the limited role of ascertaining whether the party seeking arbitration is making a claim which, on its face, is governed by the agreement to arbitrate.³⁴

C. Courts' Changing View of Arbitration

During the past two decades, the increase in the use of arbitration in the resolution of commercial disputes, tort actions, and insurance claims in the United States has been phenomenal.³⁵ This increase has been due to many factors, none of which is more influential than the fact that arbitration as a form of dispute resolution is quickly gaining acceptance among the various courts in the country. In fact, public policy now favors the enforcement of agreements to arbitrate without regard to the justiciability of underlying claims. It is no longer of any consequence that a court, otherwise competent to hear a dispute, is deprived of its jurisdiction by the arbitration process.³⁶ A survey of relatively recent Supreme Court and other federal court decisions clearly demonstrates a strong national policy favoring arbitration and requiring the enforcement of arbitration agreements.³⁷

There are several reasons for the courts' departure from the common law judicial hostility towards arbitration. One of the most apparent reasons is that the competence of arbitral tribunals is much higher today than it has ever been.³⁸ So many cases today deal with such highly technical areas that the arbitral tribunal is almost better suited to

33. *Perry v. Thomas*, 482 U.S. 483, 489 (1987) (quoting 9 U.S.C. § 2 1947).

34. Benjamin Suckewer and Thomas E. Hefler, *Disputes Among Shareholders and Directors in Closely Held Corporations in ARBITRATION: COMMERCIAL DISPUTES, INSURANCE AND TORT CLAIMS* 11, 64 (Alan I. Widiss ed., 1979).

35. Alan I. Widiss, *Introduction, in ARBITRATION: COMMERCIAL DISPUTES, INSURANCE AND TORT CLAIMS I* (Alan I. Widiss ed., 1979).

36. *Pettinaro Constr. Co. v. Harry C. Partridge & Sons, Inc.* 408 A.2d 957, 961 (Del. Ch. 1979).

37. *See Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989); *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1986), *reh'g denied*, 483 U.S. 1056 (1987); *Keating*, 465 U.S. 1 (1984); *Moses H. Cone*, 460 U.S. 1 (1983); *Prima Paint.*, 388 U.S. 395 (1967); *Necchi S.P.A. v. Necchi Sewing Machine Sales Corp.*, 348 F.2d 693 (2d Cir. 1965), *cert. denied*, 383 U.S. 909 (1966).

38. *See Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 233-34.

SCOPE OF FAA's PREEMPTION POWER

resolve the dispute than is the judicial forum.³⁹ If the parties are forced into pursuing their rights in a judicial forum, they may very well end up appearing before a judge with little or no knowledge in the area from which the dispute arose. If the parties are permitted to submit their dispute to arbitration, they can select an arbitrator who has a substantial degree of expertise in the applicable area, thus, in all probability, facilitating a more just resolution.

Speed in settling a case which could have dragged through the courts for years is another principal reason why arbitration is becoming an increasingly popular way to resolve a dispute. In a study done in the securities context, "the average elapsed time to the termination of a case through litigation was 599 days, whereas the average elapsed time for cases referred to arbitration was 434 days."⁴⁰ The reduction in the amount of time required to resolve a dispute through arbitration also results in lower costs to the parties, thereby providing more people with the opportunity to pursue their rights. Thus, it is clear that commercial arbitration is favored as a speedy and cost efficient method of dispute resolution.⁴¹

II. DISCUSSION OF *Saturn Distribution Corp. v. Williams*

A. *Facts of the Case*

Saturn Distribution Corporation (Saturn) is a wholly-owned subsidiary of Saturn Corporation, which is a wholly-owned subsidiary of General Motors Corporation. Saturn was created to design, manufacture, and market motor vehicles under the "Saturn" nameplate. Saturn sets itself apart from other manufacturers of motor vehicles by using a slightly different "Mission and Philosophy" of manufacturing and marketing automobiles.⁴² This "Mission and Philosophy" is reflected in the Saturn Distribution Corporation Dealer Agreement (Dealer Agreement). To further implement its philosophy, Saturn concluded that an alternative

39. This is because the parties may seek out a specialist in the field to act as an arbitrator if proceeding to arbitration, while in a judicial forum they may be assigned to a judge with no understanding of the area.

40. See William C. Hermann, *Arbitration of Securities Disputes: Rodriguez and New Arbitration Rules Leave Investors Holding a Mixed Bag*, 65 IND. L.J. 697, 707 (1990).

41. *Ohio Casualty Insurance Co. v. Benson*, 432 A.2d 905 (N.J. 1981).

42. *Saturn Distribution Corp. v. Williams*, 905 F.2d 719, 721 (4th Cir. 1990), cert. denied, 111 S. Ct. 516, and reh'g denied, en banc, 1990, U.S. App. LEXIS 22948.

system of dispute resolution should be a core element of its Dealer Agreement. That system includes binding arbitration which is mandatory under the agreement.⁴³

Under Saturn's Dealer Agreement, if a dispute arises, either party, Saturn or the dealer, may file a request for mediation. The dispute is then forwarded to a mediation panel, which recommends a consensus solution. If either party rejects the panel's solution, the dispute then proceeds to binding arbitration, which provides for discovery and a hearing. The arbitration panel, composed of two Saturn representatives and two dealers, must reach a consensus decision. This decision is final and unappealable, except as provided by the Federal Arbitration Act.⁴⁴ This arbitration procedure is considered by Saturn as central to the structure of its Dealer Agreement, and Saturn, therefore, refuses to contract with any dealer who will not consent to the mandatory arbitration provision.⁴⁵

This case arose because of two conflicting provisions of the Virginia Motor Vehicle Dealer Licensing Act. The first of which,⁴⁶ provides:

It is unlawful for any manufacturer, factory branch, distributor or distributor branch, or any field representative, officer, agent or any representative whatsoever of any of them:

10. To fail to include in any franchise with a motor vehicle dealer the following language: "If any provision herein contravenes the valid laws or regulations of any state or other jurisdiction wherein this agreement is to be performed, or denies access to the procedures, forums, or remedies provided for by such laws or regulations, such provision shall be deemed to be modified to conform to such laws or regulations, and all other terms and provisions shall remain in full force and effect," or words to that effect."⁴⁷

The other provision⁴⁸ is primarily an enforcement provision requiring a manufacturer to submit its standard franchise agreement to the

43. *Id.*

44. *Id.* at 721 n.1.

45. *Id.* It is for this reason that the Fourth Circuit's opinion refers to the arbitration clause as "nonnegotiable."

46. VA. CODE ANN. § 46.1-550.5:27 (1989 Supp.).

47. *Id.*

48. VA. CODE ANN. § 46.1-550.5:24 (1988 Supp.).

SCOPE OF FAA'S PREEMPTION POWER

Commissioner of the Department of Motor Vehicles for his approval prior to offering it to the dealer.⁴⁹

When Saturn submitted its Dealer Agreement to the Commissioner, David E. Williams, he rejected it on the basis of the "nonnegotiable" arbitration clause. The Commissioner "also made it clear that he would not approve the Agreement unless it included an 'opt-out' provision to the binding arbitration provisions" allowing dealers to escape being forced into arbitration.⁵⁰ Saturn brought this action for declaratory and injunctive relief against the Commissioner alleging that the provisions of the Virginia Motor Vehicle Dealer Licensing Act, as applied by the Commissioner, were preempted by the FAA.⁵¹ The United States District Court for the Eastern District of Virginia held that the FAA did not preempt the Virginia provisions and granted summary judgment to the Commissioner.⁵²

B. The Majority Opinion

On appeal, the United States Court of Appeals for the Fourth Circuit reversed the district court's granting of summary judgment and held that Section 46.1-550.5:27 of the Virginia Motor Vehicle Dealer Licensing Act, as applied by the Commissioner, does conflict with the Federal Arbitration Act and is therefore preempted under the Supremacy Clause of the United States Constitution.⁵³ Thus, the "nonnegotiable" arbitration provision in Saturn's Dealer Agreement is enforceable in Virginia and the Commissioner may not prohibit or discourage the use of "nonnegotiable" arbitration provisions in contracts between Saturn and its dealers in Virginia.⁵⁴

The first step in the Fourth Circuit's reasoning was to determine if the scope of the FAA encompasses state laws governing the formation of arbitration agreements. The Fourth Circuit reasoned that pursuant to Section 2 of the FAA, arbitration agreements must be placed on the same enforceability level as other contracts. "The language of the FAA requires that states place no greater restrictions upon arbitration provisions than they place upon other contractual terms."⁵⁵ Therefore, if a state law singles out arbitration agreements and limits or restricts their

49. *Saturn Distribution*, 905 F.2d 719, 721.

50. *Id.*

51. *Id.*

52. *Saturn Distribution Corp. v. Williams*, 717 F. Supp. 1147 (E.D. Va. 1989).

53. U.S. CONST., art. VI.

54. *Saturn Distribution*, 905 F.2d 719, 722.

55. *Id.*

enforceability, it will be preempted.⁵⁶ The majority relied on a number of cases expressing the liberal federal policy favoring arbitration and the enforcement of agreements to arbitrate.⁵⁷

The majority next considered whether the Virginia statutes at issue were preempted by the FAA. The majority closely examined the wording of the Virginia provision at issue,⁵⁸ and determined that while the Virginia statute appeared to void all arbitration agreements in automobile franchise agreements, the Commissioner's interpretation that only nonnegotiable arbitration agreements are prohibited by this section would be considered controlling.⁵⁹ The majority stated that since the general common and statutory law of Virginia enabled contracting parties to make the terms of their contract nonnegotiable, the Virginia provision in question unjustifiably singled out arbitration agreements and therefore was preempted.⁶⁰ The majority found the reasoning in *Securities Industry Ass'n v. Connolly*⁶¹ persuasive. *Connolly* held that Massachusetts regulations prohibiting securities brokerage firms from including nonnegotiable arbitration provisions in their customer agreements were preempted by the FAA.⁶²

Finally, the majority refused to adopt the position of the district court that the Virginia statute could be harmonized with the FAA because it only ensures "consensual rather than forced arbitration."⁶³ The majority argued that the district court's reliance on statements made during the legislative hearings, to the effect that the Act would not apply to standardized contracts, was misplaced. The majority felt that these statements "should not be overemphasized due to the absence of limiting language in the FAA and the fact that the Act has often been applied to standardized contracts."⁶⁴ The majority further declined to accept that the United States Supreme Court's decision in *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University*,⁶⁵ mandated a contrary result. In *Volt*, the Court stated that "[a]rbitration under the Act

56. *Id.*

57. See *Dean Witter Reynolds v. Byrd*, 470 U.S. 213 (1985); *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985); *Moses H. Cone*, 460 U.S. 1 (1983).

58. VA. CODE ANN. § 46.1-550.5:27 (1988 Supp.).

59. *Saturn Distribution*, 905 F.2d 719, 724.

60. *Id.*

61. 883 F.2d 1114 (1st Cir. 1989), *cert. denied*, 110 S. Ct. 2559 (1990).

62. *Saturn Distribution*, 905 F.2d 719, 724.

63. *Id.* at 726.

64. *Id.* at 726 (citing *Rodriguez de Quijas*, 490 U.S. 477, 478 (1989)); *Perry*, 482 U.S. 483, 485; *Mitsubishi Motors Corp.*, 473 U.S. 614, 617.

65. 489 U.S. 468, 475 (1989).

SCOPE OF FAA'S PREEMPTION POWER

is a matter of consent, not coercion.⁶⁶ The Fourth Circuit argued that the Supreme Court's statement in *Volt* required that the FAA not impose arbitration on unwilling parties, but allowed the parties to agree to submit their disputes to arbitration.⁶⁷ Thus, since the dealers were not required to agree to the terms of the Dealer Agreement,⁶⁸ the arbitration involved in this case was still a matter of consent and not one of coercion.

C. *The Dissenting Opinion*

In his dissenting opinion, Circuit Judge Widener presented a relatively compelling argument challenging the majority's reasoning. He argued that the majority abandoned the proper and appropriate preemption analysis and failed to take into consideration Virginia's inherent right to protect its own citizens.⁶⁹ The dissent contended that the majority employed the "frustrate the federal policy" theory of preemption⁷⁰ which is the most difficult preemption theory to establish.⁷¹ Judge Widener argued that this category of preemption is "in the face of congressional silence" and therefore the analysis must start with a "presumption against preemption."⁷² Thus, Widener argued that since "statutes that regulate the relationship between dealers and manufacturers in an attempt to equalize the parties' respective bargaining power are a legitimate exercise of a state's police powers,"⁷³ the analysis must "start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress."⁷⁴ Thus, according to Widener, the appropriate starting point for analyzing the Virginia statute is the presumption against preemption, absent a clear and manifest congressional intent to the contrary.⁷⁵

66. *Id.* at 475.

67. *Saturn Distribution*, 905 F.2d 719, 727.

68. *Id.* The majority argued that becoming a Saturn dealer was a matter of choice and if the dealer strongly objected to the terms of the Saturn Dealer Agreement, it could choose not to become a dealer and thus not have to agree to the arbitration provisions.

69. *Saturn Distribution*, 905 F.2d 719, 727 (Widener, J., dissenting).

70. This theory essentially states that a state statute is preempted when compliance with it would frustrate the policy behind a federal statute.

71. *Saturn Distribution*, 905 F.2d 719, 728 (Widener, J., dissenting).

72. *Id.* (quoting *Abbot v. American Cyanamid Co.*, 844 F.2d 1108, 1112 (4th Cir. 1988), *cert. denied*, 488 U.S. 908 (1988)).

73. *Id.* (quoting *Boatland, Inc. v. Brunswick Corp.*, 558 F.2d 818, 823 (6th Cir. 1977)).

74. *Id.* at 728 (quoting *California v. ARC Am. Corp.*, 490 U.S. 93, 100 (1989) quoting *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947)).

75. *Id.* at 728.

Widener then applied this analysis to the Virginia statute and argued that it requires a different result than that reached by the majority. Since the FAA contains no explicit preemptive provision and does not reflect a congressional intent to occupy the entire field of arbitration,⁷⁶ in order to support a finding of preemption, the majority must find that the Virginia statute is in direct conflict with the FAA.⁷⁷ Widener argued that there is no direct conflict and that because there is no conflict, the analysis should end there and the Virginia provisions should be enforceable.

However, Widener did not end his dissent there. He went on to argue that the majority failed to recognize the significance of the Dealers' Day in Court Act (DDCA).⁷⁸ The ultimate purpose of the DDCA is to curtail the effects of any coercion and intimidation which automobile manufacturers may be able to impose on their retail dealers by virtue of the manufacturers' superior economic position.⁷⁹ The DDCA, Widener claimed, shows a clear congressional intent to override the FAA in this area by indicating its intent to preclude waiver of a judicial forum.⁸⁰ By essentially ignoring the DDCA, the majority had overlooked the reasons behind the enactment of that statute which, Widener argued, are essentially the same reasons behind the Virginia statute at issue.⁸¹ Thus, Widener concluded that where a "presumptively valid state statute is in general tension with a federal statute of general application, and yet furthers precisely the same goals as another federal statute dealing precisely with the specific subject in issue, the state enactment should stand until Congress says otherwise."⁸² Thus, in light of the purpose behind the DDCA, Widener argued that the Virginia provisions should stand until Congress specifically addresses this issue.

Finally, Widener found *Securities Industry Ass'n v. Connolly*,⁸³ unpersuasive for two reasons. First, Widener argued, the "underlying

76. *Id.* (citing *Volt Info. Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 471 (1989)).

77. *Id.* at 728.

78. 15 U.S.C. §§ 1221-25 (1982).

79. *De Cantis v. Mid-Atlantic Toyota Distributors, Inc.*, 371 F. Supp 123 (E.D. Va. 1974).

80. *Saturn Distribution*, 905 F.2d 719, 729 (Widener, J., dissenting). Widener relies on a portion of the legislative history of the DDCA which states: "The bill creates a cause of action where none previously existed in that, *irrespective of contractual provisions*, it grants a right of review in the Federal courts between automobile manufacturers and their dealers" H.R. REP. NO. 2850, 84th Cong., 2d Sess. 3, *reprinted in* 1956 U.S.C.C.A.N. 4596.

81. *Saturn Distribution*, 905 F.2d 719, 729 (Widener, J., dissenting).

82. *Id.* at 730.

83. 883 F.2d 1114 (1st Cir. 1989).

SCOPE OF FAA'S PREEMPTION POWER

reasoning of *Connolly* is its concern with [the] '[i]ncreased resort to the courts, and the consequent tumefaction of already-swollen court calendars.'"⁸⁴ Widener did not believe that this concern should enter into the court's decision because the court's job is to do justice between the parties, and not to keep their dockets clear.⁸⁵ Second, Widener argued that *Connolly* is a securities case, and securities regulation is an area where the Supreme Court has addressed the applicability of the FAA.⁸⁶ Another distinguishing point is that the regulations at issue in *Connolly* arose from the states' concurrent power to regulate the area of securities, while the Virginia statute arises from Virginia's inherent police power to protect its citizens.⁸⁷ Widener concluded by stating that "[b]y precluding Saturn from making arbitration clauses nonnegotiable, Virginia is merely seeking to ensure that arbitration 'is a matter of consent, not coercion'"⁸⁸

III. ANALYSIS

A. *Intended Scope of the Federal Arbitration Act*

The majority's conclusion that the arbitration agreement contained in Saturn's Dealer Agreement was within the intended scope of the Federal Arbitration Act was definitely in accord with the prior case law dealing with the scope of the FAA and the legislative history of the FAA. From the language of the FAA itself, it is apparent that the FAA applies to maritime transactions and any contract evidencing interstate commerce.⁸⁹ As stated previously, the FAA enunciates a clear "congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary."⁹⁰ Furthermore, the FAA was enacted to promote the enforceability of agreements to arbitrate and to make arbitration a more

84. *Id.* at 1116.

85. *Saturn Distribution*, 905 F.2d 719, 731 (Widener, J. dissenting) (quoting *Connolly*, 883 F.2d 1114, 1116 (1st Cir. 1989)).

86. *Id.* at 730 (citing *Rodriguez de Quijas*, 490 U.S. 477 (1989), *Shearson/American Express, Inc.*, 482 U.S. 220 (1986)).

87. 905 F.2d 719, 730 (4th Cir. 1990). Here, Virginia is trying to protect its automobile dealers from the disparity of bargaining power between the dealers and auto manufacturers.

88. *Id.* at 730 (Widener, J., dissenting), (quoting *Volt Info. Science*, 489 U.S. 468, 471 (1989)).

89. 9 U.S.C. § 1 (1947).

90. *Moses H. Cone*, 460 U.S. 1, 24 (1983).

viable option to parties who would have trouble affording the costs and delays of ordinary litigation.⁹¹

The Saturn Dealer Agreement was clearly one involving interstate commerce and thus is covered by the FAA. However, the Commissioner argued that the scope of the Federal Arbitration Act's preemption power is limited to laws covering existing arbitration agreements and does not extend to laws that prohibit or regulate the formation of arbitration agreements.⁹² The majority properly disagrees with this proposition. The mere fact that the majority of cases dealing with the scope of the FAA have arisen in the context of existing arbitration agreements does not, by any means, limit the Federal Arbitration Act's preemption power to existing agreements. By enacting the FAA, "Congress intended to foreclose state legislative attempts to undercut the enforceability of arbitration agreements."⁹³ The majority correctly stated that if it were to restrict the Federal Arbitration Act's preemption power to existing arbitration agreements it would, in effect, allow the states to "wholly eviscerate congressional intent to place arbitration agreements 'upon the same footing as other contracts.'"⁹⁴

A diligent search has failed to produce a single case which adopts the narrow interpretation of the Federal Arbitration Act's preemption power advanced by the Commissioner. However, as the majority stated, the Commissioner's interpretation was rejected by the First Circuit in *Securities Industry Ass'n v. Connolly*.⁹⁵ Despite the arguments expressed by Judge Widener in his dissent that *Connolly* is unpersuasive in this case, *Connolly* appears to be applicable here. *Connolly* dealt with state regulations concerning predispute arbitration agreements. Specifically, the regulations barred firms from requiring, as a nonnegotiable condition precedent to account relationships, that customers agree to predispute arbitration agreements; they required that the arbitration agreement be brought "conspicuously" to the attention of prospective customers, and they required the brokers to make written disclosure of the effect of the agreement.⁹⁶ One of the main reasons behind the First Circuit's decision that the regulations were preempted by the FAA was that the regulations singled out arbitration agreements, thus they conflicted with the federal

91. *Byrd*, 470 U.S. 213, 220 (1985); H.R. REP. NO. 96, 68th Cong., 1st Sess. 2 (1924).

92. *Saturn Distribution*, 905 F.2d 719, 723.

93. *Keating*, 465 U.S. 1, 16.

94. *Saturn Distribution*, 905 F.2d 719, 723 (quoting *Keating*, 465 U.S. 1, 16-17 (quoting H.R. REP. NO. 96, 68th Cong., 1st Sess. 1 (1924))).

95. 883 F.2d 1114, 1123-24 (1st Cir. 1989).

96. *Id.* at 1117.

SCOPE OF FAA'S PREEMPTION POWER

policy of placing arbitration agreements on equal footing with other contracts.⁹⁷ "A state law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with [the equality] requirement of [Section 2]."⁹⁸ Applying this principle to the Virginia statute at issue dictates that it too, must be preempted. Even though the Virginia statute does not explicitly mention arbitration agreements, its effect is to undercut the enforceability of such agreements and it is therefore in direct conflict with the "congressional intent to foreclose all state legislative attempts to undercut the enforceability of arbitration agreements."⁹⁹

B. Applicability of Federal Arbitration Act's Preemptive Power to the Virginia Motor Vehicle Dealer Licensing Act

While the thrust of the majority's opinion appears to be based on the need to further the liberal federal policy favoring arbitration through the enforcement of agreements to arbitrate and the preemption of state laws hindering such agreements, the majority's lack of discussion of the effect of the Dealers' Day in Court Act (DDCA)¹⁰⁰ is somewhat troublesome. The majority dealt with the DDCA briefly in a footnote¹⁰¹ by stating that the text of the DDCA does not demonstrate a clear congressional intent to override the FAA, and that it was not deciding whether all DDCA claims could be arbitrated.¹⁰² The majority rationalized its refusal to deal with the DDCA issue by referring to another Fourth Circuit case which stated, "[c]ourts cannot determine whether arbitration agreements are to be enforced by making subjective judgments as to the relative importance of various federal statutes."¹⁰³ The majority stated that clear guidance from Congress was required before federal courts should refrain from enforcing arbitration agreements.¹⁰⁴

While the majority does have a point that clear guidance is required from Congress on this issue, the legislative history of the DDCA

97. *Dean Witter Reynolds, Inc.*, 470 U.S. 213, 219 (quoting H.R. REP. NO. 96, 68th Cong., 1st Sess. 1 (1924)). See also *Prima Paint Corp.*, 388 U.S. 395, 404 n.12 (1967).

98. *Connolly*, 883 F.2d 1114, 1123 (quoting *Perry*, 482 U.S. at 492 n.9).

99. *Keating*, 465 U.S. 1, 16.

100. 15 U.S.C. §§ 1221-25.

101. *Saturn Distribution*, 905 F.2d 719, 722 n.2.

102. *Id.*

103. *Id.* (quoting *Gilmer v. Interstate/Johnson Lane Corp.*, 895 F.2d 195, 203 (4th Cir. 1990), *reh'g denied en banc*, No. 88-1796, 1990 U.S. App. LEXIS 7370 (4th Cir. Mar. 28, 1990), and *cert. granted in part*, 111 S. Ct. 41 (1990), and *aff'd*, 111 S. Ct. 1647 (1991)).

104. *Id.*

seems to indicate the required congressional intent needed to override the FAA. "An exception to federal preemption exists if Congress has overridden the FAA by indicating its intent to preclude waiver of a judicial forum for a particular statutory right."¹⁰⁵ As Judge Widener argued in his dissent, "[a] congressional intent to preclude waiver of a judicial forum for a particular statutory right 'will be deducible from text or legislative history.'"¹⁰⁶ The legislative history of the DDCA states: "The bill creates a cause of action where none previously existed in that, *irrespective of contractual provisions*, it grants a right of review in the federal courts of disputes between automobile manufacturers and their dealers"¹⁰⁷ The legislative history also states that Section 2 of the DDCA:¹⁰⁸

authorizes a franchised dealer to bring suit against the manufacturer in an appropriate United States district court, without respect to the amount in controversy, to recover damages by reason of the manufacturer's failure . . . to act in good faith in the performance of the franchise or in terminating, canceling or not renewing the franchise.¹⁰⁹

This language, written some thirty years after the enactment of the FAA,¹¹⁰ does seem to indicate Congress' intent to override the FAA with regard to disputes between automobile manufacturers and their dealers.

Furthermore, one of the purposes behind the DDCA is to assure a dealer an opportunity to secure a judicial determination, *irrespective of contractual terms*, as to whether the automobile manufacturer has failed to act in good faith in performing or complying with any provisions of the franchise agreement.¹¹¹ Thus, from the use of the phrase "irrespective of contractual provisions" (or "terms") in both the legislative history of the DDCA and the Fifth Circuit's interpretation of the statute in *Marquis v. Chrysler Corp.*, it seems apparent that Congress intended a dealer to have an opportunity to seek a judicial determination of any conflicts arising between the dealer and the manufacturer, despite any contractual provision denying the dealer this opportunity.

105. *Id.*

106. *Id.* at 729 (Widener, J., dissenting) (quoting *Mitsubishi Motors*, 473 U.S. 614, 628 (1985)) (emphasis added).

107. *Id.* (quoting H.R. REP. NO. 2850, 84th Cong., 2d Sess. 3, reprinted in 1956 U.S.C.C.A.N. 4596).

108. 15 U.S.C. § 1222.

109. H.R. REP. NO. 2850, 84th Cong., 2d Sess., reprinted in 3 U.S. CODE & ADMIN. NEWS 4596, 4602 (1956).

110. This language was written in 1956. The FAA was enacted in 1925.

111. *Marquis v. Chrysler Corp.*, 577 F.2d 624 (9th Cir. 1978).

SCOPE OF FAA'S PREEMPTION POWER

Another purpose behind the DDCA is "to remedy the manifest disparity in the ability of the franchised dealers of automotive vehicles to bargain with their manufacturers."¹¹² "A primary source of the manufacturer's power over their dealers stems from the unilateral nature of the franchise agreements."¹¹³ The nonnegotiable nature of the arbitration clause in Saturn's dealer agreement operates in direct conflict with the purposes behind the DDCA. Moreover, Saturn's refusal to negotiate with regard to the arbitration clause is an example of the type of disparity in bargaining power and coercion employed by manufacturers against dealers at which the DDCA was aimed. In order to become a Saturn dealer, a person must fully consent to the binding arbitration clause, thereby foregoing his opportunity and right to secure a judicial determination of any later arising conflict between himself and the manufacturer. This result is contrary to the purposes and rationales behind the DDCA.

IV. CONCLUSION

While the majority's opinion seems to be in accord with the majority of cases dealing with the scope of the Federal Arbitration Act's preemption power, the majority appears to have erred in failing to examine fully the effect of the Dealers' Day in Court Act on the issue in front of it. The majority's decision would, in essence, be correct if the same issue arose out of a different factual setting. However, because *Saturn Distribution Corp. v. Williams* involved a dispute over a proposed arbitration agreement between an automobile manufacturer and prospective dealers, the majority should have considered the impact of the DDCA. If the majority would have done so, it would have held that the Virginia statute was not preempted because Congress, through the DDCA, expressed its intent to override the FAA with regard to disputes between automobile manufacturers and their dealers.

The only ways this issue can be finally resolved are for the Supreme Court to address it or for Congress to provide some guidance and clearly indicate its intent on this issue. Thus, at the very least, the

112. H.R. REP. NO. 2850, *supra* note 109, at 4596-97.

113. *Id.* at 4599.

majority's decision in this case strengthens the cries for congressional guidance on this issue.

John C. Norling