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COMMERCIAL ARBITRATION: ENFORCEMENT OF AN AGREEMENT TO ARBITRATE FUTURE DISPUTES

By PETER R. SONDERBY*

INTRODUCTION

Arbitration is a procedure whereby parties, by voluntary agreement, submit a dispute for binding determination to private unofficial persons of their own choice rather than to the regularly established tribunals of justice.¹ Commercial arbitration is a specialized branch of arbitration dealing with disputes arising under sales, construction, shipping and a wide variety of other types of agreements.²

According to its proponents, arbitration as a method of dispute settlement has a number of significant advantages over ordinary litigation. Those most commonly mentioned are: (1) it is faster and less expensive; (2) the availability of expert decision makers; (3) privacy, since arbitration proceedings are not a matter of public record; and (4) the avoidance of the hostility which destroys business and other intimate relationships when a dispute is litigated in the courts.³

For these and other reasons, the parties to commercial and other types of contracts frequently include as part of their

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¹ See M. DOMKE, COMMERCIAL ARBITRATION 1 (1968) [hereinafter cited as DOMKE]; F. KELLOR, AMERICAN ARBITRATION 4 (1948); K. Carlston, *The Theory of the Arbitration Process*, 17 LAW & CONTEMP. PROB. 631 (1952); W. Sturges, *Arbitration — What Is It?*, 35 N.Y.U.L. REV. 1031 (1960).

² DOMKE §1.01 at 3. For detailed discussions of some of the specific uses of commercial arbitration, see *Symposium: Arbitration and Antitrust*, 44 N.Y.U.L. REV. 1069 (1969); G. Asken, *Resolving Construction Contract Disputes Through Arbitration*, 23 ARB. J. 116 (1969); C. Bridge, Jr., *Arbitration of Accident Claims*, 54 ILL. B.J. 334 (1965); D. Collins, *Arbitration and the U.C.C.*, 41 N.Y.U.L. REV. 736 (1966); R. Coulson, *Family Arbitration — An Exercise in Sensitivity*, 3 FAM. L.Q. 22 (1969); J. Dobkin, *Arbitrability of Patent Disputes Under the United States Arbitration Act*, 23 ARB. J. 1 (1968); M. Domke, *Foreign Trade Arbitration*, 46 CHI. B. REC. 65 (1964); L. Kovin, *Uninsured Motorist Arbitration Under the Illinois Statute*, 21 ARB. J. 229 (1966); H. Rudnick, *Arbitration of Disputes Between Franchisors and Franchisees*, 55 ILL. B.J. 54 (1966); J. Sembower, *Landlord-Tenant Arbitration*, 24 ARB. J. 35 (1969); note, *The Validity of Arbitration Provisions in Trust Instruments*, 55 CALIF. L. REV. 521 (1967); note *Arbitration as a Means of Settling Disputes within Close Corporations*, 63 COLUM. L. REV. 267 (1963); note *Mandatory Arbitration as a Remedy for Intra-Close Corporate Disputes*, 56 VA. L. REV. 271 (1970).

³ S. Mentschikoff, *Commercial Arbitration*, 61 COLUM. L. REV. 846, 848-49 (1961); see C. Tausch, *Extra-judicial Settlement of Controversies*, 83 U. PA. L. REV. 147 (1934).

agreement a provision requiring arbitration of future disputes which may arise thereunder.⁴ However, when a dispute does in fact arise, it is not uncommon that one of the parties (usually the one against whom a claim is asserted) decides that perhaps arbitration was not such a good idea after all and that the delays and uncertainties of litigation would be more desirable. In such a situation the party who wishes to arbitrate must find a means to compel the recalcitrant party to live up to the arbitration agreement. The purpose of this article is to provide a general survey of the formal legal means which are available to compel arbitration pursuant to an agreement to arbitrate future disputes and to point out some of the problems which may be encountered in attempting to utilize those means.

HISTORICAL BACKGROUND

A. *At Common Law*

At common law arbitration was viewed with disfavor and this attitude persists today in some jurisdictions.⁵ The origin of the common law attitude is generally attributed to a dictum of Lord Coke in 1609 in *Vynior's Case*.⁶ Involved there was an action of debt on a penal bond by Vynior against Wilde for the latter's breach of the bond for failing to submit a dispute to arbitration. At that time it was customary for the parties to arbitration agreements to post such bonds to insure compliance with the agreement and in accordance with the rule then prevailing, a judgment was awarded to the plaintiff for the full amount of the bond.⁷ Although entirely unnecessary to anything decided in the case Lord Coke nevertheless pointed out in his opinion that:

If I submit myself to an arbitrament . . . yet I may revoke it for my act or my words cannot alter the judgment of the law to make *that* irrevocable, which is of its own nature revocable.⁸

The impact of this dictum was not felt for 78 years until 1687 when Parliament enacted the statute of Fines and Penalties.⁹ This legislation provided that execution on a judgment entered upon a bond given for the performance of an agreement

⁴ The following is an example of a contract provision for the arbitration of future disputes. It is recommended by the American Arbitration Association for insertion in all commercial contracts:

Any controversy or claim arising out of or relating to this contract, or the breach thereof, shall be settled by arbitration in accordance with the Rules of the American Arbitration Association, and judgment upon the award may be entered in any Court having jurisdiction thereof.

1 MODERN LEGAL FORMS §594 (1963).

⁵ *E.g.*, *Green v. Wolff*, 140 Mont. 413, 372 P.2d 427 (1962).

⁶ 8 Coke Rep. 81b, 77 Eng. Rep. 597 (K.B. 1069); *see generally* Wolaver, *The Historical Background of Commercial Arbitration*, 83 U. PA. L. REV. 132, 138-39 (1934).

⁷ 5 W. HOLDSWORTH, *HISTORY OF ENGLISH LAW*, 293 (1924).

⁸ 8 Coke Rep. at 82a, 77 Eng. Rep. at 599-600.

⁹ 8 & 9 Will. 3, ch. 2, §8.

would issue only for the amount of damages actually sustained rather than the entire amount of the bond. According to Lord Coke's dictum in *Vynior's Case* an arbitration agreement was revocable at any time, and this was construed to mean, under the statute of Fines and Penalties, that the breach of an arbitration agreement could give rise only to an action for nominal damages.¹⁰ Moreover, since an agreement to arbitrate future disputes was revocable at law, it could not be enforced in equity by means of specific performance under commonly accepted equitable principles.¹¹

For a number of years, this rationale was applied by the English courts in refusing to enforce agreements to arbitrate future disputes.¹² Several rationalizations were devised for this rule of non-enforceability, the most popular being that arbitration agreements were against public policy because they "ousted the jurisdiction of the courts."¹³ Finally, in *Scott v. Avery*,¹⁴ what came to be known as the rule of *Vynior's Case* was significantly modified. There it was held that although the parties may not oust the courts from jurisdiction, they could agree that no cause of action would arise until their dispute had been submitted to arbitration. On the basis of *Scott v. Avery* and later English decisions and legislation, the hostile attitude of the English courts towards arbitration gradually dissipated and today agreements to arbitrate future disputes are fully enforceable in England.¹⁵

The English "ouster of jurisdiction" concept based on *Vynior's Case* was adopted at an early stage in this country.¹⁶ However, most courts here did not follow *Scott v. Avery* and later modifications of the English rule and continued to apply the rule of *Vynior's Case* long after it had generally been abandoned in England. Thus, for many years the state and federal courts almost uniformly held that executory arbitration agreements

¹⁰ See Sayre, *Development of Commercial Arbitration Law*, 37 YALE L. J. 595, 604 (1927).

¹¹ Simpson, *Specific Enforcement of Arbitration Contracts*, 83 V. PA. L. REV. 160 (1934).

¹² E.g., *Kill v. Hollister*, 1 Wilson 129, 95 Eng. Rep. 532 (K.B. 1746); *Wellington v. Mackintosh*, 2 Atk. 569, 26 Eng. Rep. 741 (Ch. 1743); see generally E. Wolaver, note 6 *supra* at 138-44.

¹³ *Kill v. Hollister*, note 12 *supra*.

¹⁴ 25 L.J.Ex. 308; 5 H.L. Cas. 811; 10 Eng. Rep. 1121 (1856). In *Scott v. Avery*, Lord Campbell claimed that the hostile attitude of the English courts towards executory arbitration agreements was based primarily upon the judges' desire to protect their incomes, since at that time there were no fixed salaries and the judges were dependent almost entirely on fees for their compensation. *Id.* at 313, quoted in *Kulukundis Shipping Co. v. Amtorg Trading Co.*, 126 F.2d 978, 983 n. 14 (2d Cir. 1942).

¹⁵ G. Ellenbogen, *English Arbitration Practice*, 17 LAW & CONTEMP. PROB. 656 (1952).

¹⁶ See, e.g., *Tobey v. County of Bristol*, 23 F. Cas. 1313 (No. 14065) (C.C. Mass. 1845); *Greason v. Keteltas*, 17 N.Y. 491, 496 (1858).

would neither be granted specific performance nor form the basis of a stay in an action at law¹⁷ and this rule still obtains today in some jurisdictions where the common law has not been modified by statute.¹⁸

B. Statutory Modifications

The courts' hostility towards executory arbitration agreements came under increasing judicial criticism in the 20th century¹⁹ but for the most part the courts continued to apply the common law rule.²⁰ The commercial interests of the country were also quite dissatisfied with the common law rule and as a result of increasing pressure from this sector,²¹ the New York Arbitration Act of 1920 was finally enacted.²² This legislation was the first of what may be termed the modern arbitration statutes, providing, contrary to the common law rule, that agreements to arbitrate future disputes were irrevocable and setting forth a procedure whereby a reluctant party could be compelled to arbitrate in accordance with an arbitration agreement.²³

The New York Act provided the pattern and impetus for the Federal Arbitration Act of 1925,²⁴ the Uniform Arbitration Act

¹⁷ *E.g.*, *Red Cross Line v. Atlantic Fruit Co.*, 264 U.S. 109 (1924); *Haskell v. McClintic-Marshall Co.*, 289 F. 405 (9th Cir. 1923); *Cotalis v. Nazides*, 308 Ill. 152, 139 N.E. 95 (1923); *Meacham v. Jamestown F. & C. R.R.*, 211 N.Y. 346, 105 N.E. 653 (1914); *contra*, *Park Constr. Co. v. Independent School Dist.*, 209 Minn. 182, 296 N.W. 475 (1941); *see generally*, Annot., 135 A.L.R. 79 (1941).

¹⁸ *E.g.*, *Green v. Wolf*, note 5 *supra*; see notes 30-31 and accompanying text, *infra*.

It should be noted that the courts' unfriendly attitude towards arbitration extended only to executory agreements to arbitrate and that from an early date the courts in both this country and England were willing to enforce executed arbitration agreements *i.e.* ones which had ripened into awards. *See, e.g.*, *Hall v. Hardy*, 3 P. Wms. 187, 24 Eng. Rep. 1023 (Ch. 1733); *Ballance v. Underhill*, 4 Ill. 453, 459 (1842); *see generally*, Simpson, note 11 *supra*, at 160. It has been argued that since the courts did enforce arbitrators' awards, they were not really unfriendly towards arbitration, but the truth seems to be that they were in fact unfriendly but simply did not carry their hostility to its logical conclusion. *Kulukundis Shipping Co. v. Amtorg Trading Corp.*, 126 F.2d 978, 983 n. 11 (2d. Cir. 1942).

¹⁹ *See, e.g.*, *Atlantic Fruit Co. v. Red Cross Line*, 276 F. 319 (S.D.N.Y. 1921); *United States Asphalt Refining Co. v. Trinidad Petroleum Co.*, 222 F. 1006 (S.D.N.Y. 1915) (Hough, J.); *Park Constr. Co. v. Independent School Dist.*, note 17 *supra*.

²⁰ *See* authorities cited, note 17 *supra*.

²¹ Note, *Judicial Control of the Arbitrators Jurisdiction: A Changing Attitude*, 58 Nw. U.L. REV. 521 (1963).

²² N.Y. Sess. Law 1920, c. 275, originally in N.Y. CIV. PRACT. ACT §1448-69, now in N.Y. CIV. PRACT. LAW & RULES §§7501-14. (McKinney 1963).

²³ The essential aspects of a modern arbitration act are (1) irrevocability of an agreement to submit future disputes to arbitration, (2) power of a party to invoke the assistance of a court to compel a recalcitrant party to arbitrate, (3) power of a party to stay an action at law instituted in violation of an arbitration agreement, (4) authority of a court to appoint arbitrators or fill vacancies when the parties fail to do so, (5) restriction on the courts' ability to review the findings of fact and application of law by the arbitrator, (6) specifications of a limited number of grounds upon which an arbitrator's award may be attacked. DOMKE §4.01, at 20.

²⁴ 9 UNIFORM LAWS ANNOTATED 76.

of 1955,²⁵ which has been enacted in several states²⁶ and a number of other state arbitration acts.²⁷

Today there are 23 states in addition to New York with modern arbitration acts providing for the enforcement of agreements to arbitrate future disputes. Of these, seven have adopted the Uniform Act in its entirety or with minor changes²⁸ and the other 16 have adopted some other form of act containing some or all of the essential elements of a modern arbitration statute.²⁹

In the remaining 26 states a modern arbitration statute has not been enacted. In 22 of these the statutes in existence permit only the arbitration of present disputes.³⁰ In the remaining four states there are no statutes at all concerning arbitration and the common law rule applies.³¹

PROCEDURE UNDER MODERN STATE ARBITRATION STATUTES

Generally an agreement to arbitrate future disputes may be enforced under state law only in those states where a modern arbitration statute has been enacted.³² Because of the many variations which exist, a comprehensive review of the procedure

²⁵ 28 U.S.C. §§1-14 (1947).

²⁶ See statutes cited, note 28 *infra*.

²⁷ See statutes cited, note 29 *infra*.

²⁸ ARIZ. REV. STAT. ANN. §§12-1501 to 1517 (Supp. 1969); FLA. STAT. ANN. §§682.01-22 (1969); ILL. REV. STAT. ch. 10, §§101-23 (1969); MAINE REV. STAT. ANN. ch. 706, §§5927-49 (1964); MD. ANN. CODE, art. 7, §§1-23 (1965); MASS. GEN. LAWS ANN. ch. 251, §§1-19 (1960); MINN. STAT. ANN. §§572.01-30 (Supp. 1963), WYO. STAT. ANN. §§1-1048 to 1048.21 (Supp. 1969).

²⁹ CAL. CODE CIV. PRAC. tit. 9, §§ 1280-94 (West Supp. 1969); CONN. GEN. STAT. ANN. §§52-408 to 424 (1968); HAWAII REV. LAWS §§658-1 to 15 (1968); KY. REV. STAT. ANN. §§417.010 to .040 (1969); LA. REV. STAT. ANN. §§9:4201-17 (1967); MICH. STAT. ANN. §27A.5001-5035 (1962); N.H. REV. STAT. ANN. §§542:1-10 (1955); N.J. REV. STAT. §§2A:24-1 to 11:24-11 (1962); OHIO REV. CODE ANN. §2711.01-15 (Supp. 1968); ORE. REV. STAT. §§3.210-340 (1964); PA. STAT. ANN. tit. S §§1-181 (1969); R.I. GEN. LAWS ANN. §§10-3-1 to 20 (1956); TEX. REV. STAT. art. 224, 238-6 (1969 Supp.); REV. CODE WASH. ANN. §7.04-010 to 220 (1961); WIS. STAT. ANN. §298.01-18 (1957).

³⁰ ALA. CODE tit. 7 §§829-44 (1967); ARK. STAT. ANN. §34-501 to 510 (Supp. 1967); COLO. RULES OF CIV. PROC., ch. 16, R. 109 (1963); DEL. CODE ANN. tit. 10 §§5701-06 (1953); GA. CODE ANN. §§7-101 to 111, 7-201 to 224 (1969); IDAHO CODE ANN. §§7-901 to 910 (1963); IND. STAT. ANN. §§3.201-220 (1968); IOWA CODE ANN. §679.1-19 (1964); KAN. REV. STAT. §§5-201 to 213 (1969); MISS. CODE ANN. §§279-97 (1956); MO. REV. STAT. §§435.011-280 (1952); MONT. REV. CODES ANN. §§93.201-1 to 10 (1947); NEB. REV. STAT. §§25.2103 to .2120 (1964); NEV. REV. STAT. §§38.010-240 (1969); N.M. STAT. ANN. §§2-3-1 to 8 (1953); N.C. GEN. STAT. §§1-544 to 567 (1969); N.D. CENT. CODE §§32-29-01 to 21 (1959); CODE OF LAWS OF S.C. §§10-1901-1905 (1962); TENN. CODE ANN. §§23.501-519 (1955); UTAH CODE ANN. §§78-31-1 to 22 (1953); VA. CODE ANN. §§55-10-1 to 8 (1965).

³¹ These states are Alaska, Oklahoma, South Dakota and Vermont. There is no arbitration statute specifically applicable to the District of Columbia, however, the Federal Arbitration Act applies there. 9 U.S.C. §§1-2 (1947).

³² Green v. Wolf, note 5 *supra*; *contra* Park Constr. Co. v. Independent School Dist., note 17 *supra*.

in all states having such statutes will not be attempted. Instead, the focus will be on the procedure followed in Illinois where the Uniform Act with minor modifications has been adopted,³³ and where the procedure is typical of that utilized in other states having modern arbitration statutes.

Section 1 of the Illinois Act³⁴ declares, contrary to the common law rule, that:

[A] provision in a written contract to submit to arbitration in controversy thereafter arising between the parties is valid, enforceable and irrevocable save upon such grounds as exist at law or in equity for the revocation of any contract.

In Section 2 the Act provides for the enforcement of the contracts specified in Section 1.³⁵ Where a party has refused to arbitrate in accordance with an agreement, the other may apply for an order compelling arbitration. The application is made by motion and is heard in the manner provided for the making and hearing of motions in civil cases.³⁶ Notice of the initial application is served in the same manner as a summons in a civil case.³⁷

The initial application must show an agreement to arbitrate of the type made valid by Section 1 and the opposing party's refusal to arbitrate in accordance with the agreement. Upon making such a showing, "the court shall order the parties to proceed with arbitration."³⁸ However, if the party against whom an order is sought denies the existence of the agreement to arbitrate, the court summarily determines that issue. If it is found that there was no agreement to arbitrate, the moving party's order is denied. So that judicial involvement in the arbitration process is minimal, the court is specifically directed not to consider the merits of the dispute itself.³⁹

The same procedure is followed where a party breaches an arbitration agreement by bringing the court action relating to a dispute covered by the arbitration agreement. If the suit is brought in a court which would have jurisdiction to hear an initial application, the order for arbitration is sought there. Otherwise, subject to venue requirements, the application may be brought in any other court having jurisdiction. Upon the filing

³³ See generally, *Introductory Note*, ILL. ANN. STAT. ch. 10 (Smith-Hurd 1966).

³⁴ ILL. REV. STAT. ch. 10 §101 (1969).

³⁵ *Id.* at 102.

³⁶ *Id.* 115.

³⁷ *Id.*

³⁸ *Id.* at §102(a).

³⁹ "An order for arbitration shall not be refused on the ground that the claim in issue lacks merits or bona fides or because of any fault or grounds for the claim sought to be arbitrated have not been shown." ILL. REV. STAT. ch. 10, §102(a) (1969).

of the application, the pending court action is stayed, and if the application is granted, the stay continues.⁴⁰

Subsequent provisions of the act deal with various aspects of the arbitration proceeding itself. The manner of selecting arbitrators is specified,⁴¹ and the notice and manner of holding the arbitration hearing is set forth where these matters are not covered by the arbitration agreement.⁴² In addition, the parties' right to representation by an attorney is guaranteed.⁴³ The arbitrators are authorized to issue subpoenas, administer oaths and authorize the taking of depositions.⁴⁴ Upon application of a party the arbitrator's award is confirmed by court and thereafter may be enforced in the same manner as a judgment or decree in a civil case.⁴⁵ Upon application of a party, an arbitrator's award may be vacated but only for limited and specific causes.⁴⁶

PROCEDURE UNDER THE FEDERAL ARBITRATION ACT

Another modern arbitration statute which provides for the enforcement of agreements to arbitrate future disputes is the United States Arbitration Act of 1925.⁴⁷ For a number of reasons a party seeking arbitration may find it necessary⁴⁸ or de-

⁴⁰ *Id.* at §102(c).

⁴¹ *Id.* at §103. This provision differs from the Uniform Act in that it provides that the entire arbitration agreement terminates when the arbitration agreement does not provide for a method of choosing arbitrators and the parties cannot agree upon the appointment of arbitrators. Under the Uniform Act, the court chooses arbitrators in such a case. *Introductory Note ILL. ANN STAT.* ch. 10 (Smith-Hurd, 1966).

⁴² ILL. REV. STAT. ch. 10, §105(a) (1969).

⁴³ *Id.* at §106.

⁴⁴ *Id.* at §107.

⁴⁵ *Id.* at §114.

⁴⁶ An arbitrator's award may not be set aside or reviewed on the basis of an erroneous determination of law or fact but only for fraud, partiality and other specified procedural grounds. ILL. REV. STAT. ch. 10, §112 (1969).

⁴⁷ 9 U.S.C. §§1-14 (1970) (hereinafter referred to as the *Federal Act*); see generally, DOMKE §4.03.

⁴⁸ A modern state arbitration statute may be unavailable because the state in which the party wishes to compel arbitration may not have enacted such a statute. See notes 30-31, *supra*, and accompanying text. In some instances even if a modern arbitration statute has been enacted in the state, it still may not be available. For example, the Illinois Act is expressly applicable only to agreements made after its effective date, before which time agreements to arbitrate future disputes were unenforceable. ILL. REV. STAT. ch. 10, §119 (1969). Thus, an agreement to arbitrate future disputes made before 1961 presumably could not be enforced in the Illinois courts under the Illinois Act. *But see* the court's dictum in *R.E.A. Express v. Missouri Pac. R. Co.* 447 S.W.2d 721, 726 (Tex. Civ. App. 1969) to the effect even though an arbitration agreement is unenforceable under state law, it can be enforced in the state courts under the Federal Arbitration Act.

Even if the applicable state act covers the arbitration agreement involved, there may be some additional barrier precluding its use. For example, by statute in New York, agreements to arbitrate claims barred by the statute of limitations will not be enforced by the New York state courts. N.Y. CIV. PRAC. §7502(b). There is no comparable federal statute and under federal decisional law, the statute of limitations is not in itself a bar to arbitration. *E.g.*, *Reconstruction Finance Corp. v. Harrison and Crosfield, Ltd.* 204 F.2d 366 (2d Cir. 1953) *cert. denied*, 346 U.S. 854 (1953).

sirable⁴⁹ to utilize this rather than one of modern state acts discussed in the preceding section. But before he can do so, certain jurisdictional requirements must be met.

First, as under the modern state acts, the arbitration agreement must be in writing.⁵⁰ Secondly, the moving party must show that the United States District Court where arbitration is sought would have jurisdiction of the subject matter of a suit arising out of the controversy between the parties, absent the arbitration agreement.⁵¹ In the usual non-admiralty case involving private parties, this requirement will be satisfied by showing that jurisdiction based on diversity of citizenship exists.⁵²

Finally, the arbitration agreement must be contained either in a contract involving a "maritime transaction" or a "contract evidencing a transaction involving commerce."⁵³

Generally in a non-admiralty case the focus of the parties'

⁴⁹ The party may simply prefer to litigate in the federal court rather than in the state court. Also, it may be that the decisional law under the Federal Act favors the moving party on a point which he anticipates might be raised. For example, a defense frequently asserted to an action to compel arbitration is that the contract containing the arbitration clause was fraudulently induced. The decision under the *Federal Act* hold that such a claim is to be decided by the arbitrator rather than the court while in some states it is held that such a claim must be decided by the court before arbitration will be ordered. Compare *Prima Paint Corp. v. Flood and Conklin Mfg. Co.*, 388 U.S. 395 (1968) with *Murphy v. Morris*, 12 N.J. Super. 544, 80 A.2d 128 (1951); see generally Annot., 91 A.L.R.2d 936 (1963). Since the party seeking arbitration generally prefers to have the leverage of an order compelling arbitration as soon as possible, he would most likely choose to move for an order compelling arbitration in the federal court rather than a state court in which the opposing party could delay matters by raising the fraudulent inducement defense. See e.g. *Prima Paint Corp. v. Flood and Conklin Mfg. Co.*, *supra*; *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402, 409 (2d Cir. 1959), *cert. dismissed*, 364 U.S. 801 (1960) (holding that since the *Federal Act* is based on the commerce power, federal rather than state law governs proceedings under the *Act* even though jurisdiction may be based upon diversity of citizenship).

⁵⁰ 9 U.S.C. §2 (1947); see note 53, *infra*.

⁵¹ 9 U.S.C. §§3-4 (1947), see 28 U.S.C. §§1331-62 (1947) (jurisdiction of district courts).

⁵² 28 U.S.C.A. §1332 (1970) (citizens of different states; citizens of a state or different states and foreign states; amount in controversy exceeding \$10,000); see generally 1 J. MOORE, FEDERAL PRACTICE ¶¶0.76-78 (1964).

⁵³ This requirement is found in Section 2 of the Act which specifies the types of agreements to which the Act is applicable and contains the general declaration of the policy of the Act:

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 such grounds as exist at law or in equity for the revocation of any contract.

9 U.S.C.A. §2 (1970).

The terms "maritime transactions" and "commerce" are defined and the exceptions to the Act are set forth in Section 1:

'Maritime transactions', as herein defined, means charter parties, bills of lading of water carriers, agreements relating to wharfage, supplies furnished vessels or repairs to vessels, collisions, or any other

and the court's attention will be on the question of whether the latter requirement can be met. On its face, the statutory language — "a contract evidencing a transaction involving commerce" — does not appear to involve the full scope of Congress' power over commerce.⁵⁴ In other acts Congress has defined commerce to include activity which merely "affects" commerce.⁵⁵ Here, of course, commerce is not so broadly defined. Furthermore, the Federal Act contains no declaration of a national interest to be served or a national regulatory scheme to be created. Finally the quoted language appears to establish a formalistic test whereby the sole determinant of whether commerce is present is the face of the contract itself. For these and other reasons, it has been asserted that the Federal Act was intended to be of limited scope, for example, applicable only to contracts between merchants for the interstate shipment of goods,⁵⁶ and completely inapplicable in diversity of citizenship cases.⁵⁷

However, these arguments favoring a restrictive interpretation have not generally prevailed and the trend of the decisions has been to broadly construe the commerce requirement. Particularly pertinent in this regard is the recent Supreme Court decision in *Prima Paint Corp. v. Flood and Conklin Mfg. Co.*⁵⁸ In that case, Prima had purchased the business of F.&C. Co., a New Jersey paint company serving customers in various states, and, as a result of the purchase, F.&C.'s business operations were moved to Maryland. The purchase contract did not contain an arbitration clause. Rather, this was contained in a re-

matters in foreign commerce which, if the subject of controversy, would be embraced within admiralty jurisdiction; 'commerce', as herein defined, means commerce among the several states or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any state or foreign nation, or between the District of Columbia and any State or Territory or foreign nation, but nothing herein contained, shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce.

9 U.S.C.A. §1 (1970).

⁵⁴ See generally Note, *Scope of the United States Arbitration Act in Commercial Arbitration: Problems in Federalism*, 58 NW. U.L. REV. 468, 476, n. 43 (1963); Note, *Commercial Arbitration in The Federal Courts*, 20 VAND. L. REV. 607 (1967).

⁵⁵ E.g., Federal Employers Liability Act, 45 U.S.C.A. §51 (1954); National Labor Relations Act, 29 U.S.C.A. §152 (7) (1965); Civil Rights Act of 1964 (public accommodations), 42 U.S.C.A. §2000a.(b) (1970); see *Pawgan v. Silverstein*, 265 F. Supp. 898, 901 (S.D.N.Y. 1967) where it was stated that the operation of a motel in one state involved "commerce" for the purposes of the federal securities laws but not for the purposes of the United States Arbitration Act.

⁵⁶ *Prima Paint Corp. v. Flood and Conklin Mfg. Co.*, 388 U.S. 395, 409 (1967) (dissenting opinion).

⁵⁷ *Bernhardt v. Polygraphic Co.*, 350 U.S. 198, 208 (1956) (Frankfurter, J., concurring opinion).

⁵⁸ Note 56 *supra*.

lated consulting agreement whereby F.&C. and its principal officer were to furnish consulting services to Prima. There was no indication that these services were to be furnished at any other place than Prima's offices in Maryland. Nevertheless, the court held that since the consulting agreement was tied to the transfer of F.&C.'s business to Maryland and the operations of an interstate business, there "could not be a clearer case of a contract evidencing a transaction in interstate commerce."⁵⁹ In addition, the court noted that the application of "commerce" in the arbitration act was not limited merely to contracts between merchants for the interstate shipment of goods but that the legislative intent was that it reached not only physical interstate shipment of goods but "also contracts relating to interstate commerce."⁶⁰

The decisions of the lower courts are generally consistent with the Court's broad definition of commerce in *Prima Paint* and it appears that even if all acts under a contract take place in one state an arbitration agreement contained therein will nevertheless come within the coverage of the Federal Arbitration Act as long as some relationship to interstate commerce can be shown.⁶¹

Assuming that the jurisdictional requirements are met, the procedure followed for compelling arbitration under the Federal Act⁶² is quite similar to that followed under the Uniform and other state acts.

Under Section 4 a party seeking arbitration may petition a United States district court in the district where arbitration is sought for an order compelling arbitration. Written notice of the application for an order to compel arbitration must be served upon the party in default at least five days in advance of the hearing, in the same manner as a summons is served in a civil case. At the hearing, the party seeking arbitration must show that neither the agreement for arbitration nor the failure to comply therewith is in issue and upon such a showing the court

⁵⁹ 388 U.S. 395, 401 (1967).

⁶⁰ *Id.* at 401, and n. 7.

⁶¹ *E.g.*, *Metro Indus. Painting Co. v. Terminal Const. Co.*, 287 F.2d 382 (2d Cir. 1961), *cert. denied*, 368 U.S. 817 (1961); *Garfield & Co. v. Wiest*, 308 F. Supp. 1107 (S.D.N.Y. 1970); *Yunker Bros., Inc. v. Standard Const. Co.*, 241 F. Supp. 17 (S.D. Iowa 1965); *O'Meara v. Texas Gas Transmission Corp.*, 230 F. Supp. 788 (N.D. Ill. 1964).

⁶² The language of the enforcement and other provisions of the Federal Act would appear to require that any proceedings thereunder be held in a United States district court. However, it has been suggested that the Federal Act constitutes a declaration of national policy as to the validity and enforceability of the agreements specified in Section 2 (quoted in footnote 53, *supra*) and as such, is equally applicable in state or federal courts. *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, footnote 49, *supra*; *REA Express Co. v. Missouri Pac. R. Co.*, footnote 48, *supra*.

will order arbitration. Where those issues are raised, the party in default may demand a jury trial of them.⁶³

Where a suit is filed in connection with a dispute covered by an arbitration agreement a defendant who wishes to arbitrate may, under Section 3, move in the district court in which the suit is pending for a stay pending arbitration, provided that he can show that the issues involved are referable to arbitration and that he is not himself in default under the arbitration agreement.⁶⁴

The remaining sections of the Federal Act are similar to the Uniform Act, providing for the appointment of arbitrators and other remedies designed to insure compliance with the arbitration agreement.⁶⁵

⁶³ Section 4 provides as follows:

A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. Five days' notice in writing of such application shall be served upon the party in default. Service thereof shall be made in the manner provided by the Federal Rules of Civil Procedure. The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. The hearing and proceedings, under such agreement, shall be within the district in which the petition for an order directing such arbitration is filed. If the making of the arbitration agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof. If no jury trial be demanded by the party alleged to be in default, or if the matter in dispute is within admiralty jurisdiction, the court shall hear and determine such issue. Where such an issue is raised, the party alleged to be in default may, except in cases of admiralty, on or before the return day of the notice of application, demand a jury trial of such issue, and upon such demand the court shall make an order referring the issue or issues to a jury in the manner provided by the Federal Rules of Civil Procedure, or may specially call a jury for that purpose. If the jury find that no agreement in writing for arbitration was made or that there is no default in proceeding thereunder, the proceeding shall be dismissed. If the jury find that an agreement for arbitration was made in writing and that there is a default in proceeding thereunder, the court shall make an order summarily directing the parties to proceed with the arbitration in accordance with the terms thereof.

9 U.S.C.A. §4 (1970).

⁶⁴ Section 3 provides as follows:

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, providing the applicant for the stay is not in default in proceeding with such arbitration. 9 U.S.C.A. §3 (1970).

⁶⁵ 9 U.S.C.A. §§5-14 (1970).

ISSUES WHICH MAY ARISE IN CONNECTION
WITH A PROCEEDING TO COMPEL ARBITRATION

The Federal Act and the typical modern state arbitration acts discussed in the preceding sections strictly prescribe the issues which may be considered in a proceeding to compel arbitration or to stay a court action pending arbitration. Generally these include only the questions of whether (1) there was an agreement to arbitrate and, (2) whether there was a refusal to arbitrate under the agreement.⁶⁶ Once the party seeking arbitration has met these prerequisites, the typical statute leaves the court no discretion as to whether an order compelling arbitration should issue.

The purpose of these limitations is to keep judicial involvement in the arbitration process at a minimum,⁶⁷ but despite them, a number of defenses can be raised by the party resisting arbitration and a proceeding to compel arbitration can become a rather involved affair. The following is an illustrative review of cases dealing with some of the defenses commonly raised.

A. *Absence of Agreement to Arbitrate*

A defense specifically authorized by statute is that there was no agreement to arbitrate. This defense is generally raised in cases where the arbitration clause is contained, not in the parties' contract, but instead in some document referred to or mentioned therein.⁶⁸ In general, if under accepted principles of contract law, the requirements for incorporation by reference have been met,⁶⁹ arbitration generally will be ordered even though the party resisting arbitration may claim that he was unaware of the existence of the incorporated arbitration provision or that he did not intend the arbitration provision to be incorporated.

Illustrative in this regard is *Level Export Corp. v. Wolz, Aiken & Co.*⁷⁰ There the parties entered into two identical contracts whereby the petitioner agreed to purchase a quantity of cotton from the respondent. Each contract contained the following provision:

This Salesnote is subject to the provisions of Standard Cotton Textile Salesnote which, by this reference, is incorporated as a part of this agreement and together herewith constitutes the entire contract between buyer and seller. No variation therefrom shall be valid unless accepted in writing.⁷¹

⁶⁶ *E.g.*, 9 U.S.C.A. §§3, 4 (1970); ILL. REV. STAT. ch. 10, 102 (1969).

⁶⁷ *Trafalgar Shipping Co. v. International Milling Co.*, 401 F.2d 568 (2d Cir. 1968); *Layne-Minnesota Co., v. Regents of the Univ. of Minnesota*, 266 Minn. 284, 123 N.W.2d 371 (1963).

⁶⁸ See generally Annot. 41 A.L.R.2d 863 (1955).

⁶⁹ 17A C.J.S., CONTRACTS §299 (1963).

⁷⁰ 305 N.Y. 82, 111 N.E.2d 218 (1953).

⁷¹ *Id.* at 84, 111 N.E.2d at 219. (Emphasis supplied by the court.)

The Standard Cotton Textile Salesnote which was referred to in quoted language contained a provision requiring that any controversy arising under or relating to contract be settled by arbitration. A dispute subsequently arose under the contract and the respondent instituted arbitration proceedings; however the buyer refused to appoint an arbitrator and moved for a stay of the arbitration on the ground that no arbitration agreement existed between the parties, and this motion was granted by the lower court.

Petitioner admitted that it executed the contracts but claimed that it was at no time informed that the Standard Cotton Textile Salesnote referred to contained any provision requiring arbitration and that it was not a member of any textile trade association and was not familiar with the provision referred to. It further claimed that it was unaware that any arbitration clause existed until the controversy arose and that at no time did the respondent call the arbitration provision to its attention.

However, according to the court, "difficult it would be to find words more clearly to express the contractual intent of the parties."⁷² Moreover, the court noted that there was no claim in that the petitioner was misled by the words or conduct of the respondent that disputes between the parties would be settled other than by arbitration. The court thereupon remanded the cause with instructions that arbitration be ordered, relying upon the contract principal that a party to a written contract is bound by the provisions thereof whether he reads them or not and that ignorance through negligence will not relieve a party from his contractual obligations.⁷³

A similar result was reached in *Brown v. Gilligan, Will & Co.*,⁷⁴ which involved a dispute between stock exchange members. A lawsuit was pending between them and one moved for an order staying the action until arbitration had been had between them pursuant to the Constitution and Rules of the American Stock Exchange which contained provisions requiring arbitration. The party resisting arbitration claimed that arbitration was not required inasmuch as there was no agreement between the parties to arbitrate the dispute in question. After noting that both the party seeking arbitration and the party resisting arbitration were member firms of the American Stock Exchange, the court pointed out that:

Most exchanges require applicants for membership, as a prerequisite to admission, to sign the constitution of the exchange or an agreement to be bound by its provisions. But whether or not ex-

⁷² *Id.* at 86, 111 N.E.2d at 220.

⁷³ *Id.* at 86-88, 111 N.E.2d at 220-21.

⁷⁴ 287 F. Supp. 766 (S.D.N.Y. 1968).

press written assent is demanded, every member, by virtue of his admission, contracts to be governed by the conditions of membership which the exchange has imposed. These conditions are, therefore, binding on the members, and constitute virtually a body of law by which the members are governed in their dealings with the exchange and with each other.

* * *

Since the rules of the exchange 'constitute a contract between the members, the arbitration provisions which they embodied have contractual validity.'⁷⁵

But where the intention to incorporate an arbitration provision is not clearly expressed or where it appears that injustice might result, the courts have refused to compel arbitration. One such example is *In re American Rail & Steel Co.*⁷⁶ There the parties entered into a contract for the purchase of a quantity of used steel rails and bars. The purchase order contained the language:

This Contract is placed in accordance with the conditions of contracts Form ISM 826 Rev. Copy attached and can be modified or supplemented only in writing and signed by both parties hereto.⁷⁷

One of the paragraphs of the above-mentioned form provided that disputes arising in connection with the contract should be submitted to arbitration.

When a dispute arose under the contract, the purchaser, who had provided the purchase order, demanded that it be settled by arbitration. The seller then moved for a stay of arbitration, defending on the grounds that arbitration was not called for inasmuch as the purchase order did not expressly mention it, the form referred to in the order was not attached and its contents were not otherwise brought to the seller's attention. It was not clear whether the form was in fact attached but the purchaser contended that its omission would not change the situation. However, the court reversed the order below and ordered that arbitration be stayed on the basis that:

. . . a court cannot say that the intent to arbitrate was so clearly expressed as to warrant a direction that the parties proceed to settle their dispute by arbitration.⁷⁸

Another such case is *Northridge Cooperative Section No. 1 Inc. v. 32nd Ave. Construction Corp.*,⁷⁹ where the court held that an arbitration clause contained in a printed document and referred to in the parties' brief construction contract was not incorporated therein where it appeared that the true principals were not shown or aware of the arbitration clause and the per-

⁷⁵ *Id.* at 769-70.

⁷⁶ 308 N.Y. 577, 127 N.E.2d 562 (1955).

⁷⁷ *Id.* at 579, 127 N.E.2d at 563.

⁷⁸ *Id.* at 580, 127 N.E.2d at 563.

⁷⁹ 207 Misc. 327, 139 N.Y.S.2d 37 (1955).

sons who executed the contract on their behalf were apparently nominees of the other party to the contract and derelict in their fiduciary duty to the party resisting arbitration.

B. *Dispute Not Covered By the Parties Arbitration Agreement*

A defense sometimes raised is that the dispute in question does not fall within the terms of the parties' arbitration agreement. In other words, the existence of an arbitration agreement is admitted, but it is claimed that the dispute is not within its scope. This defense was often successful in the cases decided during the early days of the modern arbitration acts when the courts retained much of their traditional hostility towards arbitration.⁸⁰ However, over the years, the courts' views as to their role in the arbitration processes has changed, and today, questions as to the scope of the parties' arbitration agreement are generally left, at least initially, for the arbitrators.

The present view was well expressed in *Layne-Minnesota Co. v. Regents*,⁸¹ one of the leading cases construing the Uniform Arbitration Act.⁸² *Layne* involved a dispute between an owner and contractor as to whether their contract required them to submit to arbitration a dispute arising over a claim for additional compensation occasioned by unanticipated difficulties in completing the work. According to the court, the language of the contract did not clearly express the intention of the parties as to whether such disputes would be covered by the arbitration provisions contained therein. Further, the court noted that the language of the contract provided a reasonable basis to support

⁸⁰ For example, in *Young v. Crescent Dev. Co.*, 240 N.Y. 244, 148 N.E. 510 (1925) a contract between the parties for the construction of a number of houses contained the seemingly broad arbitration provision that: "All questions that may arise under this contract and in the performance of the work thereunder shall be submitted to arbitration." *Id.* at 247, 148 N.E. at 510.

Disputes arose between the parties which included a claim by the contractor that it was entitled to damages from the owner because the owner had delayed it in the performance of the contract. The contractor's application for an order requiring arbitration of this claim was granted by the courts below. However, the New York Court of Appeals reversed, adopting what would appear to be a highly technical and strained interpretation of the above quoted arbitration clause. According to the court, the acts of the owner occasioning the delay:

. . . were not done under and in performance of the contract, but in violation of it and in repudiation of its provisions. There is involved no interpretation of [the contract's] meaning, but a willful refusal to be bound by it and, as it seems to me, [the arbitration] clause was intended to cover controversies which do not deny but seek an interpretation of and submission to its provisions; an attitude which seeks action under the contract and not one outside and in denial of it.

Under this view, it appears that any time a dispute could be characterized as involving a "violation" of the contract, arbitration could be resisted.

⁸¹ 266 Minn. 284, 123 N.W.2d 371 (1963).

⁸² See generally M. Pirsig, *Arbitrability and the Uniform Act*, 19 ARB. J. 154 (1964).

both defendants' contention that the dispute in question was not covered as it did for the plaintiff's contention that it was.⁸³

The court refused to decide on the merits of the opposing contentions of the parties. Instead, based on the language of the Uniform Act,⁸⁴ the court felt that:

. . . where upon application to compel arbitration the court is unable to ascertain the clear intent of the parties as to the scope of the arbitration clause in a contract, *the sole issue is whether or not an agreement to arbitrate exists.*

* * *

Where the parties are in conflict as to the scope of the provision for arbitration, and the question of the parties' intention as to such scope is reasonably debatable, the problem arises as to whether the court or the arbitrator shall decide the question. We believe in such cases the rule should be, and we hold, that the issue of arbitrability be initially determined by the arbitrators subject to a party's right reserved in [UNIFORM ARBITRATION ACT §12] to challenge such determination subsequent to any award. Such a rule is consistent with the purpose and objectives of the Uniform Act. It would also be more likely to coincide with the intent of the parties who, by failing to precisely delineate the controversies to be arbitrated, probably chose broad language for the purpose of extending arbitration to unforeseeable disputes. To construe [UNIFORM ARBITRATION ACT §2] to authorize a preliminary judicial determination of whether or not the applicant presented an issue referable to arbitration would be to add non-existent language. Such construction, in many instances, might be destructive of the arbitration clause itself. The contents of the written request for arbitration would take on the aspects of a pleading; and where no evidence was submitted to the court, technicalities never intended to be used in arbitration proceedings could be controlling.⁸⁵

This reasoning has been adopted in other states where the Uniform Act has been adopted⁸⁶ and is the same reasoning applied by the federal courts in their interpretation of the Federal Act.⁸⁷ Thus, at the present, it can be expected that, in most cases, arbitration will be ordered as long as it is shown that an arbitration agreement exists between the parties and that it has some arguable relationship to the dispute in question.

C. Arbitration Agreement Based Upon Invalid Contract

In order to be enforceable, an arbitration agreement must, of course, be valid as a contract.⁸⁸ Consequently, a party resisting

⁸³ 266 Minn. 284, 289, 123 N.W.2d 371, 375.

⁸⁴ MINN. STAT. §572.09 (1971); UNIFORM ARBITRATION ACT §2.

⁸⁵ 266 Minn. 284, 289, 291-92, 127 N.W.2d 371, 375-77. (Emphasis added.)

⁸⁶ *E.g.*, Flood v. Country Mut. Ins. Co., 41 Ill. 2d 91, 242 N.E.2d 149 (1968).

⁸⁷ *E.g.*, Galt v. Libbey-Owens-Ford Glass Co., 376 F.2d 711 (7th Cir. 1967); Metro Indus. Painting Corp. v. Terminal Constr. Co., 287 F.2d 382 (2d Cir. 1961).

⁸⁸ DOMKE §1.01.

arbitration may raise in a proceeding to compel arbitration fraud, duress, failure of consideration, cancellation, rescission or other recognized defenses to the enforcement of a contract.⁸⁹ Once such a defense is raised, what has been termed the problem of "separability" may be presented.⁹⁰

At first glance it would appear that since an arbitration clause is almost invariably a part of a larger contract, any claim made as to the invalidity of the entire contract would naturally go to the validity of the arbitration provision contained in the contract and that the court would thus be required to determine the question of the validity of the arbitration provision. The state courts which have considered the question have generally adopted this view.⁹¹ The federal courts, however, have adopted what is known as the "separability doctrine"⁹² whereby an arbitration provision may be "separable" from the remainder of the contract in which it is contained for the purpose of determining contractual validity. In other words, if an issue is raised which goes to the validity of the entire agreement, those issues will be resolved by the arbitrator,⁹³ and only if an issue as to the validity of the making of the arbitration clause itself is raised, will the court consider the issue of validity.

In *Prima Paint Corp. v. Flood and Conklin Mfg. Co.*,⁹⁴ the Supreme Court explicitly recognized and applied the doctrine of "separability," thus resolving a conflict among the circuits on the question⁹⁵ and eliminating any doubts there may have been as to the applicability of the doctrine in the federal courts in proceedings under the Federal Act.

In that case, Prima entered into a contract with F.&C. to purchase an interstate paint business. In connection with the purchase contract, the parties also entered into a consulting agreement which contained a broad arbitration agreement covering "[a]ny controversy or claim arising out of or relating to this

⁸⁹ See 17 C.J.S. *Contracts* §§132-88 (1963).

⁹⁰ See generally Comment *Federal Arbitration Act and Application of the "Separability Doctrine" in the Federal Courts*, 1968 DUKE L.J. 588 (1968).

⁹¹ E.g., *Wrap-Vertiser Corp. v. Plotnick*, 3 N.Y.2d 17, 143 N.E.2d 366, 163 N.Y.S.2d 623 (1957); *Finsilver, Still & Moss, Inc. v. Goldberg, Maas & Co.*, 253 N.Y. 382, 389, 171 N.E. 579, 581 (1930); see generally, DOMKE §§8.03-.05.

⁹² See note 90 *supra*.

⁹³ Assuming, of course, that the arbitration clause covers "all disputes" or contains similar language broad enough to cover matters such as contract validity. See note 4 *supra*.

⁹⁴ 388 U.S. 395 (1967) (discussed in Section IV hereof *supra* in connection with the "commerce" requirement of the *Federal Act*).

⁹⁵ Compare *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) with *Lummus Co. v. Commonwealth Oil Ref. Co.*, 280 F.2d 915, 923-24 (1st Cir. 1960), *cert. denied*, 364 U.S. 911 (1960).

agreement." A controversy thereafter arose between the parties under the consulting agreement and F.&C. sought arbitration pursuant to the agreement. Prima then instituted an action in the federal court seeking rescission of the consulting agreement on the grounds that it had been induced to enter into the consulting agreement on the basis of fraudulent representations by Prima as to Prima's financial condition. F.&C. moved for a stay of the suit under Section 3 of the Federal Act pending arbitration and in opposition to the motion for a stay, Prima argued that there was no agreement to arbitrate inasmuch as the entire consulting agreement had been fraudulently induced.

The district court granted F.&C.'s motion for a stay of Prima's action for rescission pending arbitration and the Court of Appeals denied leave to appeal.

In affirming the Court of Appeals, the Court pointed out that the central issue in the case was "whether a claim of fraud in the inducement of the entire contract is to be resolved by the federal court, or whether the matter is to be referred to the arbitrators."⁹⁶ After noting that the Courts of Appeals had reached different results on the question, the Court concluded that:

With respect to cases brought in federal court involving maritime contracts or those evidencing contracts in 'commerce,' we think that Congress has provided an explicit answer. That answer is to be found in §4 of the Act, which provides a remedy to a party seeking to compel compliance with an arbitration agreement. Under §4, with respect to a matter within the jurisdiction of the federal court save for the existence of an arbitration clause, the federal court is instructed to order arbitration to proceed once it is satisfied that 'the making of the agreement for arbitration or the failure to comply [with the arbitration agreement] is not in issue.' Accordingly, if the claim is fraud the inducement of the arbitration clause itself — an issue which goes to the 'making' of the agreement to arbitrate — the federal court may proceed to adjudicate it. *But the statutory language does not permit the federal court to consider claims of fraud in the inducement of the contract generally. . . .* We hold, therefore, that in passing upon a §3 application for a stay while the parties arbitrate, a federal court may consider only issues relating to the making and performance of the agreement to arbitrate. In so concluding, we not only honor the plain meaning of the statute but also the unmistakably clear congressional purpose that the arbitration procedure, when selected by the parties to a contract, be speedy and not subject to delay and obstruction in the courts.⁹⁷

* * *

The same rationale would be applicable to claims other than fraud in the inducement *i.e.*, duress, lack of consideration and the

⁹⁶ 388 U.S. at 402.

⁹⁷ *Id.* at 403-04. (Emphasis added.)

other defenses going to the validity of a contract.⁹⁸ Thus under *Prima*, it is clear that the party who wishes to raise such a defense in a proceeding to compel arbitration under the Federal Act must specifically allege that the arbitration provision is invalid and not merely that the entire agreement is invalid. As indicated previously, the state courts apparently have not generally recognized the doctrine of "separability" or have not considered the question. Nevertheless, it would appear wise to specifically allege invalidity of the arbitration clause even in the state courts since the reasoning of the Supreme Court in *Prima* might well prove persuasive to a state court.

D. Arbitration Agreement Unenforceable for Reasons of Public Policy

Another defense which has been successfully asserted is that the dispute in question, for reasons of public policy is not one that should be determined by arbitration. For example, in *Wilko v. Swan*⁹⁹ a customer brought an action for monetary damages against a securities brokerage firm under the Civil Liabilities Provision of the Security Act of 1933,¹⁰⁰ alleging that defendant had made various misrepresentations in connection with the sale of securities. The defendant brokerage firm moved to stay the trial pursuant to Section 3 of the Federal Act until arbitration was had in accordance with terms of a margin agreement between the parties. The stay was denied by the district court but the Court of Appeals reversed, holding that the matter was arbitrable. Relying upon Section 14 of the Securities Act of 1933¹⁰¹ and the basic policy of the Securities Act, the protection of investors, the Supreme Court reversed the Court of Appeals and held that under the circumstances arbitration would be inappropriate. In reaching its conclusion, the Court pointed out that:

While a buyer and seller of securities, under some circumstances, may deal at arms length on equal terms, it is clear that the Securities Act was drafted with an eye to the disadvantages under which buyers labor. Issuers of and dealers in securities have better opportunities to investigate and appraise the prospective earnings and business plans affecting securities than buyers. It is therefore reasonable for Congress to put buyers of securities covered by that Act on a different basis from other purchasers.

* * *

When the security buyer, prior to any violation of the Securities Act, waives his right to sue in courts, he gives up more than would a participant in other business transactions. The security buyer

⁹⁸ *Id.* at 402 n. 8.

⁹⁹ 346 U.S. 427 (1953).

¹⁰⁰ 15 U.S.C.A. §§77a-77aa (1970).

¹⁰¹ 15 U.S.C.A. §77n (1970).

has a wider choice of courts in venue. He thus surrenders one of the advantages the Act gives him and surrenders it at a time when he is less able to judge the weight of the handicap the Securities Act places upon his adversary.¹⁰²

In addition, the Court felt that valuable substantive advantages to the customer as well as procedural advantages would be lost in the arbitration process if arbitrators were permitted to apply the provisions of the Securities Act to the parties' dispute. According to the court:

This case requires subjective findings on the purpose and knowledge of an alleged violator of the Act. They must be not only determined but applied by the arbitrators without judicial instruction on the law. As their award may be made without explanation of their reasons and without a complete record of their proceedings, the arbitrators' conception of the legal meaning of such statutory requirements as 'burden of proof', 'reasonable care' or 'material fact', . . . cannot be examined. Power to vacate an award is limited. . . . In unrestricted submissions, such as the present margin agreement envisage, the interpretations of the law by the arbitrators in contrast to manifest disregard are not subject, in the federal courts, to judicial review for error in interpretation.¹⁰³

A similar result was reached in *American Safety Equip. Corp. v. J. P. Maguire & Co.*¹⁰⁴ where one of the parties sought arbitration, pursuant to a trademark license agreement between them, of claims of federal antitrust violations. In reversing the district court's order staying a court action between the parties pending arbitration, the court stated:

A claim under the antitrust laws is not merely a private matter. The Sherman Act is designed to promote the national interest in a competitive economy; thus, the plaintiff asserting his rights under the Act has been likened to a private attorney-general who protects the public's interest. Antitrust violations can affect hundreds of thousands — perhaps millions — of people and inflict staggering economic damage. . . . We do not believe that Congress intended such claims to be resolved elsewhere than in the courts.¹⁰⁵

In addition, the court found, as did the Court in *Wilco*, that the arbitration process was not appropriate for the type of dispute involved. According to the Court:

[T]he issues in antitrust cases are prone to be complicated, and the evidence extensive and diverse, far better suited to judicial than to arbitration procedures. Moreover, it is the business community generally that is regulated by the antitrust laws. Since

¹⁰² 346 U.S. at 435-37.

¹⁰³ *Id.* at 437. Compare the decision in *Wilco* with *Brown v. Gilligan Will & Co.*, note 74 *supra* where the court held that the policy of the Securities Act would not prevent the arbitration of a dispute between two *members* of an exchange as opposed to a dispute between a member and an individual customer inasmuch as members were not within the class of persons the Securities Act was designed to protect.

¹⁰⁴ 391 F.2d 821 (2d Cir. 1968).

¹⁰⁵ *Id.* at 826-27.

commercial arbitrators are frequently men drawn for their business expertise, it hardly seems proper for them to determine these issues of great public interest.¹⁰⁶

E. Waiver of Right to Demand Arbitration

The party seeking arbitration may, by his own acts prior to the filing of a petition to compel arbitration or a motion to stay a proceeding pending arbitration, provide his opponent with a defense. This defense is commonly known as "waiver"¹⁰⁷ and generally arises where the parties seeking arbitration either filed a lawsuit in violation of the arbitration agreement or participates in a lawsuit initiated by his opponent without raising the arbitration agreement as a defense. As the court stated in *Cornell & Co., Inc. v. Barber & Ross Co.*:

The right to arbitration, like any other contract right, can be waived. A party waives his right to arbitrate when he actively participates in a lawsuit or takes other action inconsistent with that right. Once having waived the right to arbitrate, that party is necessarily 'in default in proceeding with such arbitration'.¹⁰⁸

Where the party seeking arbitration has, prior to that time, himself instituted a lawsuit in violation of the arbitration agreement, it is generally been held that this is an unequivocal manifestation of an intention not to arbitrate and a repudiation of the arbitration agreement.¹⁰⁹ Thus, in *Sussman v. Goldberg*¹¹⁰ plaintiff filed suit alleging the breach of a contract to purchase stock. When defendants served their answer, plaintiff served upon one of the defendants a demand for arbitration in accordance with the parties' agreement. Plaintiff thereafter moved for a stay of the court proceeding he had instituted pending arbitration. In denying plaintiff's motion, the court stated that:

By bringing suit, a plaintiff generally irrevocably waives and abandons any right to arbitration. Unless compelled to do so, he cannot later change his mind and compel arbitration once he has waived it by bringing the action.¹¹¹

Where a defendant who has filed a counterclaim and other-

¹⁰⁶ *Id.* at 827.

¹⁰⁷ The term "waiver" is used herein in its literal sense *i.e.* the intentional relinquishment of a know right or such conduct as warrants an inference of the relinquishment of such right. BLACK'S LAW DICTIONARY 1751 (4th Ed. 1957). The term, however, is sometimes used more broadly by the courts to include what is commonly thought of as "laches" or an unreasonable and prejudicial delay in asserting a right. *See Neechi Sewing Mach. Sales Corp. v. Carl*, 260 F. Supp. 665 (D.C.N.Y. 1966). The concept of laches as applied to an action to compel arbitration is treated separately below.

¹⁰⁸ 360 F.2d 512, 513 (D.C. Cir. 1966).

¹⁰⁹ *E.g.*, *Zimmerman v. Cohen*, 236 N.Y. 15, 19, 139 N.E. 764, 765 (1923) *Young v. Crescent Dev. Co.*, 240 N.Y. 244, 251, 143 N.E. 510, 511 (1925); *Annot.*, 161 A.L.R. 1426 (1946); *but see Chatham Shipping Co. v. Fertax S.S. Corp.* 352 F.2d 291, 293 (2d Cir. 1965).

¹¹⁰ 28 Misc. 2d 1070, 210 N.Y.S.2d 912 (1960).

¹¹¹ *Id.* at 1071, 210 N.Y.S.2d at 913.

wise participates in a lawsuit later seeks a stay pending arbitration, a waiver is generally found.¹¹²

Thus, in *Radiator Specialty Co. v. Cannon Mills, Inc.*¹¹³ the defendant, who was sued for breach of a contract containing an arbitration clause, filed an answer and also a counterclaim. The case was set for trial but later postponed on the motion of defendant and on the condition that the case would be tried on the adjourned date. When the case was called on the adjourned date both parties answered ready for trial and defendant then moved for the first time for a stay of the trial pending arbitration. Under the circumstances, the court found that defendant had waived his right to arbitration.

In *Cornell and Co. Inc. v. Barber & Ross Co.*¹¹⁴ the defendant first sought to stay the court action pending arbitration after he had moved for a change of venue, filed an answer to the complaint and a counterclaim and had taken depositions and had successfully sought production of records and documents. Under the circumstances, the court found that the defendant had waived the right to seek arbitration.

However, where the defendant does not file a counterclaim, he is generally in a better position to seek a stay pending arbitration.

In *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*,¹¹⁵ the defendant did not move for a stay pending arbitration pursuant to the parties' agreement until almost nine months after the complaint was filed and after it had consented to the taking of the deposition of its president, obtained information from plaintiff, apparently through discovery processes, and had discussed settlement with plaintiff and tested the goods whose quality was the subject of the parties' dispute. Despite this, the court found that there was no waiver of arbitration, since defendant had demanded arbitration in its answer and that the intervening steps taken by defendant were not inconsistent with its right to demand arbitration.

In *G. H. & J. T. Kelly, Inc. v. Lorson Elect. Co.*¹¹⁶ defendant, in its answer to plaintiff's complaint in a suit containing an arbitration clause, failed to set up the arbitration clause as a defense or seek arbitration. After plaintiff served a notice of deposition on defendant, defendant then moved for a stay of the action pending arbitration. On the grounds that defendant's delay in seeking arbitration was neither an unequivocal act constituting a

¹¹² See generally *Annot.* 161 A.L.R. 1426 (1946).

¹¹³ 97 F.2d 318 (4th Cir. 1938).

¹¹⁴ 360 F.2d 512 (D.C. Cir. 1966).

¹¹⁵ 271 F.2d 402 (2d Cir. 1959), *cert. denied*, 364 U.S. 801 (1960).

¹¹⁶ 51 Misc. 2d 655, 273 N.Y.S.2d 694 (1966).

waiver of arbitration nor prejudicial to plaintiff, the court granted defendant's motion for arbitration.

F. *Delay in Seeking Arbitration*

1. *Statute of Limitations*

In the absence of a statute to the contrary,¹¹⁷ the cases generally hold that the Statute of Limitations is not a bar to an order compelling arbitration.

In *Son Shipping Co. v. DeVosse & Tanghe*,¹¹⁸ plaintiff sought to enjoin arbitration pursuant to a charter party containing an arbitration provision and which also reserved to plaintiff all the rights it would have under the Carriage of Goods by Sea Act.¹¹⁹ Plaintiff argued that, since the parties' dispute had arisen almost two years before arbitration was demanded, the arbitration proceeding was barred by virtue of the one year statute of limitations for suits contained in the Carriage of Goods by Sea Act. This argument was rejected by the court, which held that:

[A]rbitration is not within the term 'suit' as used in that statute. Instead, it is the performance of a contract providing for the resolution of a controversy without suit.¹²⁰

Skidmore, Owings & Merrill v. Connecticut General Life Insurance Co.,¹²¹ involved a declaratory judgment action by the plaintiff architect for determination that a demand for arbitration made by the defendant building owner was barred by both a three-year property damage and six-year contract statute of limitations. In May, 1953 plaintiff and defendant had entered into a written contract whereby plaintiff was to render architectural supervisory services in connection with the design and construction of a home office building for defendant. The contract provided for arbitration of "all questions in dispute under this agreement." Defendant occupied the building in early 1957 and in early June, 1960, defendant became aware of defects in the air conditioning system. Shortly thereafter plaintiff was notified. Meetings were held to determine the cause of the defects and necessary remedial measures but a mutually satisfactory resolution of the problem was not reached and in July, 1962, defendant demanded arbitration.

In finding for defendant and dissolving plaintiff's temporary injunction, the court held first that arbitration is not a common law action and the institution of an arbitration proceeding is not

¹¹⁷ N.Y. CIV. PRAC. LAW §7502(b) (McKinney 1962) provides that if an action at law is barred, arbitration cannot be compelled.

¹¹⁸ 199 F.2d 687 (2d Cir. 1952).

¹¹⁹ 46 U.S.C.A. 1300 *et seq.* (1970).

¹²⁰ 199 F.2d at 689.

¹²¹ 25 Conn. Supp. 76, 197 A.2d 83 (Sup. Ct. Hartford Cty. 1963).

the "bringing of an action" under the various statutes of limitation. Further, the court held that even if a statute of limitations was applicable to an arbitration proceeding, the applicability of the statute and its effect was a matter to be determined by the arbitrators rather than by the court. Finally, the court held that the alleged breach continued until 1957 and that the demand for arbitration was timely within the six-year contract statute of limitations.

In *Reconstruction Finance Corp. v. Harrison & Crossfield, Ltd.*,¹²² a government corporation entered into a contract in 1941 with defendant for a shipment of crude rubber from the East Indies to the United States. One provision of the contract obligated the government corporation to take out insurance, but it did not do so. Some of the shipments were sunk by enemy action in 1942 and as a result, defendant suffered a loss due to the failure to take out insurance. However, defendant did not serve a demand for arbitration under the arbitration clause of the shipment contract until 1951, nine years after the loss had occurred. The demand was made on RFC, the statutory successor to the government corporation which had made the contract. RFC then filed suit to enjoin defendant from arbitrating and defendant crossclaimed to compel arbitration.

Plaintiff claimed that the New York six year statute of limitations was applicable and that under that statute, defendants demand for arbitration was three years late. However, the court differentiated between the performance of the obligation involved on the merits, the obligation to obtain insurance, and the performance the obligation to arbitrate. It held that with the question of the nine year time lapse between the failure to obtain insurance and the demand for arbitration was a question for the arbitrators to decide. The court held that the only period that it could be concerned with was the one covering the time period between the refusal of RFC to arbitrate pursuant to the arbitration clause after demand had been made and the bringing of the court action to compel arbitration, since, according to the court, the cause of action before it did not accrue until there had been a refusal to arbitrate. Since the time lapse between the refusal to arbitrate and the bringing of a court action was substantially less than six years, the court found that the statute of limitations was not a bar to arbitration.

2. Laches

The equitable doctrine of laches has generally been recognized as a defense to an action to compel arbitration. However,

¹²² 204 F.2d 366 (2d Cir.), cert. denied, 346 U.S. 854 (1953).

a recent Second Circuit decision indicates that the scope of the court's inquiry into this question on a petition to compel arbitration under the Federal Act is quite limited. In *Trafalgar Shipping Co. v. International Milling Co.*,¹²³ an action to compel arbitration was brought in 1967 pursuant to an arbitration provision contained in the charter party for damages to a vessel resulting from an incident in 1961. The defendant claimed that plaintiff's right to arbitrate was barred by laches and in support thereof argued that plaintiff's long delay in asserting its claim had left it powerless to defend itself before the arbitrators due to the death of witnesses, loss of evidence and other difficulties. The district court held that the question of laches was a matter to be decided by the court rather than the arbitrators in a petition to compel arbitration under the Federal Act, and that under the circumstances plaintiff was barred by laches from seeking arbitration due to its prejudicial delay in demanding arbitration. In reversing the district court, the Court of Appeals drew a distinction between laches pertaining to the issues which must be decided by the arbitrators on the merits and laches as it pertains to the limited issues which must be decided by the court in a petition to compel arbitration under the Federal Act. According to the court, it could consider only those questions of delay which relate to and affect the limited issues the court is called upon to decide under the Federal Act, namely, "the making of the arbitration agreement or the failure, neglect or refusal to perform the same."¹²⁴ Thus, in the court's view, if it were asserted that the agreement for arbitration was procured through fraud or duress, thus raising the issue of the "making of the arbitration agreement" the court could consider whether evidence pertaining to this defense had become lost or unavailable due to the unexcused delay of the moving party. However, with respect to a claim that moving the party's delay would prejudice its opponent's defense on the merits, the court held that that is an issue for the arbitrators to decide. According to the court:

This conclusion is consistent with the policy of the Arbitration Act to eliminate the expense and delay of extended court proceedings preliminary to arbitration. Evils which surely would be promoted by a rule which made all questions of laches for the court especially where a full hearing is required [citation omitted] and where, as here, an appeal is taken from the decision of the District Court. Moreover, in our view, laches is not a technical legal issue which only a judge is competent to decide. Rather, in the often esoteric field of commercial dealings, and in admiralty, it would seem that the severity of prejudice suffered through delay and the reasonableness of excuses offered by the dilatory party, the ele-

¹²³ 401 F.2d 568 (2d Cir. 1968).

¹²⁴ 9 U.S.C. §4 (1970).

ments of laches, might be resolved better where resort is had to the expertise of the arbitrators.¹²⁵

However, in a number of earlier federal cases¹²⁶ and in cases arising under the state arbitration acts,¹²⁷ the courts have generally been willing to consider the question of laches as it relates both to the issues which the court must decide and the merits of the dispute.

For example, in *Sociedad Armadora Aristomenis Panama*,¹²⁸ the court denied petitioner's motion to compel arbitration under the Federal Act on the grounds that its unexcused delay in filing the petition seriously prejudiced respondent in defending the merits of the claim. The dispute there involved a claim that stevedores had damaged a chartered vessel sometime prior to April, 1957. The petitioner was aware of the claim in 1957 and there was correspondence between the parties concerning it in 1959 and 1960. In 1960, after respondent had lost its right to recover from the stevedores, respondent advised petitioner that it was respondent's position that petitioner's claim was barred. Petitioner did not answer respondent's last letter for three years and did not demand arbitration until September, 1964. When respondent declined to arbitrate, petitioner filed its petition to compel arbitration. According to the court, petitioner was barred by laches from seeking arbitration since:

. . . the petitioner comes forward with no explanation for the long delay in demanding arbitration, while the respondent has lost, as a result of it, the right to seek indemnity from the stevedores, the party allegedly at fault. The respondent also notes the unavailability of documents and the difficulty of unearthing witnesses who, at this late date, had any knowledge of the events. Under these circumstances, there has been substantial prejudice to the respondent, and the doctrine of laches bars the petitioner from compelling arbitration.¹²⁹

CONCLUSION

As a result of legislation and a change in the attitude of the courts over the past 50 years, the machinery for enforcing an agreement to arbitrate future disputes is now generally available. It is intended to further the goals of arbitration itself —

¹²⁵ 401 F.2d at 572. *Contra*, *Sussleaf-Flemington, Inc. v. Bruce*, 84 N.J. Super. 599, 203 A.2d 131 (1964).

¹²⁶ *E.g.*, *Reconstruction Finance Corp. v. Harrison and Crosfield, Ltd.*, 204 F.2d 366 (2d Cir.) *cert. denied*, 346 U.S. 854 (1953); *World Brilliance Corp. v. Bethlehem Steel Co.*, 342 F.2d 362 (2d Cir. 1965); *Nortuna Shipping v. Isbrandtsen Co.*, 231 F.2d 528 (2d Cir.), *cert. denied*, 351 U.S. 964 (1956).

¹²⁷ *E.g.*, *Sussleaf-Flemington v. Bruce*, note 125 *supra*.; *New York Central R.R. v. Erie R.R.*, 30 Misc. 2d 362, 213 N.Y.S.2d 15.

¹²⁸ 244 F. Supp. 653 (S.D.N.Y. 1965).

¹²⁹ 244 F. Supp. at 654-55.

the simple and inexpensive resolution of disputes. But as demonstrated by the cases in the immediately preceding section, those goals may not be realized if one of the parties refuses to submit to arbitration and this is one of the factors which must be considered in deciding whether to include an arbitration provision in a contract.