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Frequently Arising Issues in Arbitration

# Speakers

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# Overview

- Background of Federal Arbitration Law / The FAA
- Frequently Arising Issues In Arbitration
- Significant Recent Decisions and Other Developments
- Practical Tips and Takeaways



# Background of Federal Arbitration Law / The FAA

Federal Arbitration Act, 9 U.S.C. Chapter 1 (“FAA”) (1925):

1. Provides that arbitration agreements are enforceable
2. Provides for confirmation of arbitration awards
3. Provides that an award procured by corruption fraud or undue means may be vacated.



# The meat of the FAA (Section 2):

“A written provision in any ... contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract ..., 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 contract ..., or refusal, shall be valid, irrevocable, and enforceable, save upon grounds as exist at law or in equity for the revocation of any contract ...”



# Key Elements of Section 2

1. Written provision of a contract
2. Involving commerce
3. Invoking arbitration as a mechanism for dispute resolution; is
4. Valid, irrevocable and enforceable; except
5. On the grounds that other contracts are held revokable



# What does the FAA not specifically address?

1. State Courts
2. Statutory Claims
3. Delegation of Determination of Issue of Arbitrability
4. Countervailing State Law
5. Economic Inequities Addressed by Class Actions



# State Courts

*Southland v. Keating*, 465 U.S. 1 (1984)

Holding: The FAA applies to State cases by virtue of the preemption doctrine.



# Statutory Claims

*Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985)

Holding: The FAA, by default, covers virtually all types of non-criminal statutory claims.



# Delegation of Determination of Issue of Arbitrability

*Rent-A-Center, West v. Jackson*, 561 U.S. 63 (2010)

Holding: Delegation clauses, whereby the parties delegate to the arbitrator the decision regarding the enforceability and formation of the arbitration agreement, are fully enforceable, unless a party can demonstrate fraud in the making of the delegation clause.



# Countervailing State Laws

*AT&T Mobility LLC v. Concepcion*, 563 U.S. 333 (2011)

Holding: The FAA has broad preemptive powers that can override state laws having a “disproportionate impact on arbitration.” The Court held that the FAA preempted a California law precluding arbitration class action waivers.



# Economic Inequities Addressed by Class Actions

*American Express, Co. v. Italian Colors Restaurant*, 570 U.S. 228 (2013)

Holding: The FAA does not permit courts to invalidate a contractual waiver of class arbitration on the ground that the plaintiff's cost of individually arbitrating a federal statutory claim exceeds the potential recovery.



# Why does the U.S. Supreme Court love arbitration so much?

You tell me.



# Is Congress Paying Attention?

The Ending Forced Arbitration of Sexual Assault and Sexual Harassment Act, 9 U.S.C.A. section 401, et seq. (March 3, 2022)

Amends FAA to allow persons asserting claim of sexual assault or sexual harassment to bring claims in court even if they previously agreed to arbitrate.



# Who Decides Whether Claims Will Be Arbitrated Or Litigated?

- Under the FAA, courts generally determine the threshold arbitrability issues of: (1) whether a valid agreement to arbitrate exists between the parties; and (2) whether the specific dispute falls within the scope of the agreement.
- However, when the parties clearly and unmistakably provide otherwise, the question of arbitrability can be delegated to the arbitrator.



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# Who Decides Whether Claims Will Be Arbitrated Or Litigated?

- Arbitration provisions are severable from the broader contract
  - *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967).
  - *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440 (2006).
- The delegation doctrine
  - *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995).
  - *Rent-A-Ctr., W., Inc. v. Jackson*, 561 U.S. 63 (2010).



# Who Decides Whether Claims Will Be Arbitrated Or Litigated?

The incorporation of AAA, JAMS, or other such rules into the arbitration provision is generally accepted by courts as evidence that the parties agreed to have the arbitrator, and not the court, decide the scope of the arbitrator's authority.

- *Doctor's Assocs., LLC v. Tripathi*, 794 F. App'x 91 (2d Cir. 2019)
- *Midwest Air Techs., Inc. v. JC US Inc.*, No. 21 C 337, 2021 WL 1688154 (N.D. Ill. Apr. 29, 2021)

Does “sophistication” of the parties matter?

- *Chong v. 7-Eleven, Inc.*, No. CV 18-1542, 2019 WL 1003135 (E.D. Pa. Feb. 28, 2019)



# Enforceability Of Agreements To Arbitrate

## **Substantive Unconscionability**

Unfairness in the terms of the contract itself; arises when a contract term is so one-sided that it has an overly harsh effect on the disadvantaged party.

Factors to consider include:

- commercial reasonableness of the contract terms
- the purpose and effect of the terms
- the allocation of the risks between the parties
- public policy concerns

## **Procedural Unconscionability**

A contract term is so difficult to find, read, or understand that the disadvantaged party cannot fairly be said to have been aware he was agreeing to it.



# Enforceability Of Agreements To Arbitrate

Unconscionability can be argued relative to various contract provisions, and largely turns on the facts.

## Example - Forum Selection Clauses:

- *VieRican, LLC v. Midas Int'l, LLC*, No. CV 19-00620 JAO-RT, 2020 WL 4430967 (D. Haw. July 31, 2020)
- *Escobar v. Nat'l Maint. Contractors, LLC*, No. 21-35765, 2022 WL 17830001 (9th Cir. Dec. 21, 2022)



# Enforceability Of Agreements To Arbitrate

## Fraud

- *Fritschler v. Draper Mgmt., LLC*, 203 A.D.3d 623 (N.Y. App. Div. 2022)

## Other Arguments

- Lack of Consideration

*Doctor's Assocs., Inc. v. Alemayehu*, 934 F.3d 245 (2d Cir. 2019)

- Lack of Mutuality

*Stowe v. Big Sky Vacation Rentals, Inc.*, 454 P.3d 655 (Mont. 2019)



# Do The Claims Fall Within The Scope Of The Arbitration Provision?

## Broad Clause

- A clause encompassing “all disputes between the parties” or “all disputes arising out of the contract”
- A presumption of arbitrability applies and only the most forceful evidence of a purpose to exclude the claim from arbitration can prevail
- Even matters tangential to the subject agreement will be arbitrable under a broad provision

## Narrow Clause

- A clause limiting the arbitrator's scope of authority by either including specific disputes or excluding other identified issues



# Do The Claims Fall Within The Scope Of The Arbitration Provision?

## Collateral Matters

As even matters tangential to the subject agreement can be arbitrable under a broad provision, questions frequently arise concerning the arbitrability of collateral issues that are somehow connected to the main agreement that contains the arbitration clause.

- *Choice Hotels Int'l, Inc. v. TK Hosp. Grp., LLC*, No. GJH-18-3364, 2019 WL 6324523 (D. Md. Nov. 26, 2019)
- *Imagetec, L.P. v. Lexmark Int'l, Inc.*, No. 5:18-CV-011-CHB, 2019 WL 4739686 (E.D. Ky. Sept. 27, 2019)



# Preliminary Injunctive Relief in Arbitration

- Several principal differences from seeking such relief in court:
  1. Court procedures are well-defined; not so in arbitration
  2. Enforcement issues
  3. Standards of proof
  4. Nature of arbitration
- Be aware of carveouts that allow a party to seek preliminary injunctive relief in court.



# Class/Multi-Claimant Waivers

- Provisions that prohibit individuals from joining together to file or participate in a class action lawsuit.
- Subject of significant debate
  - Pros: ensuing that disputes are handled in a private and efficient manner and limiting potential liability.
  - Cons: without the ability to aggregate claims, it may be difficult to enforce rights that are associated with lower-value claims.
- Generally enforceable in the franchise context



# Forum Issues

- Forum selection provisions are generally enforceable.
- Some state franchise laws/rules restrict forum selection provisions
  - Laws that restrict forum
  - Administrative rules that restrict forum
    - *Taylor v. Rothschild*, No. C18-5863 BHS, 2019 WL 3067255 (W.D. Wash. July 12, 2019)



# Waiver

- *Morgan v. Sundance, Inc.*, 142 S. Ct. 1708 (2022)
  - No arbitration-specific rules conditioning waiver on a showing of prejudice.
  - “Policy favoring arbitration” = arbitration contracts are on par with other types of contracts
- Highly factual analysis



# Non-Signatory Issues: Signatory enforcing arbitration provision against non-signatory

- General reluctance by courts
- Several exceptions:
  1. Incorporation by reference
  2. Agency
  3. Estoppel
  4. Third-party beneficiary
  5. Closely related companies under common ownership
- Frequently arises when a non-signatory family member of franchisee is involved in dispute



# Non-Signatory Issues: Non-signatory enforcing arbitration provision against signatory

- Non-signatories can seek to enforce arbitration provisions against signatories on several grounds, including as an express third-party beneficiary of the franchise agreement, as an employee, or as a disclosed agent of an entity that is a party to an arbitration agreement.
  - *Fritschler v. Draper Mgmt., LLC*, 203 A.D.3d 623 (N.Y. App. Div. 2022)
  - *Mayer v. Soik*, 970 N.W.2d 572 (Wis. Ct. App. 2021)
- Principles of estoppel also allow an agreement to be enforced by or against non-parties.



# Confirmation and Vacatur

- Section 9 of FAA: process for confirming arbitration award
  - Generally straightforward and summary; court's discretion is limited
- Sections 10 and 11 of FAA: grounds to vacate and/or modify and/or correct an arbitration award
- Recent development: *Badgerow v. Walters*, 142 S. Ct. 1310 (2022)



# Res Judicata / Preclusive Effect

- When award is confirmed, it is considered final and binding on the parties
- *Res judicata* (“already judged”) with respect to the issues or claims decided in the arbitration.
  - Examples:
    - *Rudell v. Comprehensive Acct. Corp.*, 802 F.2d 926 (7th Cir. 1986)
    - *Hill-Harriss v. Gingiss Int'l, Inc.*, No. 91 C 6682, 1992 WL 22705, at \*6 (N.D. Ill. Feb. 5, 1992)



# Significant Recent Decisions and Other Developments

## *Coinbase, Inc. v. Bielski, No. 22-105*

- The Supreme Court will decide whether a non-frivolous appeal of a denial of a motion to compel arbitration divests a district court's jurisdiction to proceed with litigation pending appeal

## *ZF Automotive US, Inc. v. Luxshare, LTD. 142 S.Ct. 2078 (2022).*

- The Supreme Court held that 28 U.S.C. § 1782(a) (authorizing a district court to order the production of evidence "for use in a proceeding in a foreign or international tribunal") does not apply to arbitration panels

## *Air-Con, Inc. v. Daikin Applied Latin America, LLC, 21 F.4th 168 (1st Cir. 2021)*

- The First Circuit joined the majority of other circuits in deciding to apply a summary judgment standard to evaluate motions to compel under the FAA.



# Significant Recent Decisions and Other Developments

## The Ending Forced Arbitration of Sexual Assault and Sexual Harassment Act

- The Act amends the FAA to give individuals asserting sexual assault or sexual harassment claims under federal, state, or tribal law the option to bring those claims in court even if they had agreed to arbitrate such disputes before the claims arose. In addition, those individuals (or representative of a class / collective action) bringing sexual assault or sexual harassment claims may choose to proceed via a class or collective action even if they had waived the right to proceed collectively before the claims arose.

## 2022 Amendments to AAA Commercial Arbitration Rules



# Practical Tips and Takeaways

## **For parties seeking to enforce arbitration clauses**

- Ensure that the arbitration provision is valid and enforceable under applicable law.
- Initiate arbitration promptly.
- Consider all the parties that you wish to name as respondents and analyze whether they are bound by the arbitration provision.
- Consider forum issues vis-à-vis state franchise laws.
- Consider the types of relief you want to seek and the best way to obtain that relief.



# Practical Tips and Takeaways

## **For parties seeking to oppose arbitration**

- Determine whether the threshold issue of arbitrability will be decided by the court or arbitrator in order to potentially prevent the dispute from reaching an arbitrator in the first place.
- If there is any question over a dispute's arbitrability, raise the issue in court as an arbitrator may not be so quick to issue a decision relinquishing his or her jurisdiction.
- Determine whether there is a basis to argue that the arbitration agreement (not the entire contract) is unenforceable because it was the product of fraud, unconscionability, or on a similar basis.



# Questions?

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