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Ala. Supreme Court Stance On Arbitrability

Law360, New York (October 19, 2009) -- The Alabama Supreme Court recently held that the arbitrator, not the court, is to determine whether conditions precedent have been met prior to the invocation of an arbitration provision.

In Brasfield & Gorrie LLC v. Soho Partners LLC, 2009 WL 2573919 (Ala., Aug. 21, 2009), the court made a clear distinction between "substantive arbitrability" and "procedural arbitrability."

Courts are required to determine matters of "substantive arbitrability," including whether a valid agreement to arbitrate exists and whether the specific dispute falls within the scope of that agreement.

The arbitrator, on the other hand, determines questions that grow out of the dispute and bear on its final disposition such as defenses of notice, laches, estoppel and other compliance defenses.

The dispute in Brasfield & Gorrie involved the amount owed to the general contractor under a construction contract.

The contract contained specific procedures requiring an initial decision by the architect and then mediation as conditions precedent before arbitration could be invoked.

The contractor submitted a demand for arbitration, and the owner filed a lawsuit to dismiss and to enjoin the arbitration proceeding based on the contractor's alleged noncompliance with the conditions precedent under the contract.

The contractor then filed a motion to dismiss or stay the lawsuit pending arbitration, contending that the conditions concerning the architect's decision and the mediation requirement had been satisfied or waived by the parties' conduct.

The trial court denied the contractor's motion to stay the proceeding pending arbitration, holding that the determination of whether conditions precedent had been satisfied was for the court to decide.

The trial court subsequently found that the contractor had failed to comply with the conditions precedent before invoking the arbitration clause by failing to make a written request for mediation.

On appeal, the Alabama Supreme Court — relying heavily on Howsam v. Dean Witter Reynolds Inc., 537 U.S. 79 (2002) — reversed the trial court and held that whether the contractor had complied with the contractual obligations before invoking arbitration was the type of condition precedent that ought to be decided by the arbitrator.

Unless the parties provide otherwise in their agreement, a court is empowered to determine only the narrow questions of substantive arbitrability.

The substantive threshold questions for a court are: (1) Whether parties are bound by a given arbitration agreement and (2) whether the arbitration clause applies to a particular type of controversy. See Howsam, 537 at 84.

The Federal Arbitration Act (FAA) mandates arbitration whenever a contract provides for claims to be submitted to arbitration and evidences a transaction involving interstate commerce. See 9 U.S.C. § 2.

In Allied-Bruce Terminix Companies v. Dobson, 513 U.S. 265 (1995), the U.S. Supreme Court held that as long as the contract at issue touches upon interstate commerce in any sense or context, the FAA applies so as to preempt state law and displace it with the strong federal policy favoring enforcement of arbitration agreements.

The phrase "involving commerce" in the FAA essentially means "affecting commerce," and therefore expresses legislative intent that the FAA apply to the fullest extent of the Commerce Clause. Allied-Bruce, 513 U.S. at 281.

It is well settled that there is a "liberal federal policy favoring arbitration agreements." Moses H. Cone Memorial Hospital v. Mercury Constr. Corp., 460 U.S. 1, 24-25 (1983).

Aside from those specifically defined substantive arbitrability questions for a court, all other "gateway questions" of procedural arbitrability and conditions precedent are the province of the arbitrator.

Examples of such procedural prerequisites would include time limits, notice, laches and estoppel, among others. The specific matter under the court's consideration in Howsaw was a limitations period.

The Alabama court's ruling that reiterates the U.S. Supreme Court's holding from Howsam has been applied in multiple jurisdictions.

See, e.g., Sleeper Farms v. Agway Inc., 506 F.3d 98, 103 (1st Cir. 2007) (claim of waiver was threshold issue for the arbitrator); United Steelworkers of Am. v. Saint Gobain Ceramics & Plastics, 505 F.3d 417, 421-22 (6th Cir. 2007) (rule is straightforward that a time limitation is a matter of procedure for an arbitrator).

Moreover, the Revised Uniform Arbitration Act of 2000, which seeks to "incorporate the holdings of the vast majority of state courts and the law that has developed under the [FAA]" expressly states that an "arbitrator shall decide whether a condition precedent to arbitrability has been fulfilled. RUAA § 6(c), and comment 2, 7 U.L.A. 12-13 (Supp. 2002) — a point recognized by the Supreme Court in Howsam. See Howsam, 537 U.S. at 85.

In a case with the exact same conditions precedent in the same construction contract language as was found in the Brasfield & Gorrie dispute, a Texas court ruled that "compliance with conditions precedent or prerequisites to the obligation to arbitrate ... are questions for the arbitrator, not questions for the trial court." In re Global Construction, 166 S.W.3d 795, 798 (Tex. App. 2005).

The one notable exception to the generally recognized division of labor between court and arbitrator emerges when the parties do not dispute or explicitly consent on the issue of whether the conditions precedent have been satisfied.

The commonly referred to John Wiley exception — from John Wiley & Sons Inc. v. Livingston, 376 U.S. 543 (1964) — allows a court to refuse to send a matter to arbitration when, among other things, "the breach of [a] procedural requirement was clear."

General Warehousemen & Helpers Local Union 767 v. Albertson's Distrib., 331 F.3d 485, 488 (5th Cir. 2003) (ultimately holding that this "rare exception" did not apply because there was a factual dispute as to whether the labor union had complied with the procedural requirements).

The exception will not apply where there are factual disputes as to whether a party complied with the procedural requirements for arbitration.

As the court in John Wiley put it: "doubt whether grievance procedures or some part of them apply to a particular dispute, whether such procedures have been followed or excused, or whether the unexcused failure to follow them avoids the duty to arbitrate" raise questions of "procedural arbitrability." John Wiley, 376 U.S. at 557.

A myriad of cases recognize the distinction between whether compliance was in dispute or not, and whether to apply the corresponding exception to the general rule of procedural arbitrability.

See, e.g., HIM Portland, LLC v. Devito Builders Inc., 317 F.3d 41 (1st Cir. 2003) (it was undisputed that the parties never requested mediation); Kemiron Atlantic Inc. v.

Aguakem International Inc., 290 F.3d 1287, 1290-91 (11th Cir. 2002) (party admitted that he did not give notice required under the arbitration agreement).

One other significant point is that cases which concern whether a binding arbitration clause has been waived by the parties' conduct in litigation may remain a matter for the trial court to decide.

See Brasfield, 2009 WL 2573919 *6 at n.1; Ocwen Loan Servicing LLC v. Washington, 939 So.2d 6, 14 (Ala. 2006) (arbitration can be waived if the party moving for arbitration substantially invoked the litigation process).

Other courts have held that questions as to potential waiver of arbitration by litigation conduct can be distinguished from Howsam.

See, e.g., Ehleiter v. Graptree Shores Inc., 482 F.3d 207, 219-21 (3d Cir. 2007) (whether a party waived right to arbitration through its conduct in litigation remains the determination of the court); American Gen. Home Equity Inc. v. Kestel, 253 S.W.3d 543 (Ky. 2008) (litigation-conduct waiver is for the court to decide as Howsam's language on that point was mere dicta); Good Samaritan Coffee Co., v. LaRue Distrib. Inc., 748 N.W.2d 367, 373 (Neb. 2008) (litigation-conduct waiver is for the court).

In the labor arena, arbitration clauses long have been the norm in collective bargaining agreements, but now they are quite common in individual employment agreements, noncompete agreements, severance agreements and many types of commercial agreements.

Such clauses can convey considerable benefits to both parties of any dispute to obtain a more timely, fair and less expensive resolution.

See Employment Arbitration: What Does the Data Show? by the National Workrights Institute at www.workrights.org/current/cd_arbitration.html (empirical studies revealing how employees fair in arbitration); Eric J. Mogilnick and Kirk D. Jensen, Arbitration and Unconscionability, 19 Ga. St. U. L. Rev. 761 (2003) (highlighting studies to indicate that arbitration is fair, less expensive, garners quicker results than civil litigation and provides overall benefits to individuals).

The Brasfield & Gorrie decision shows an increasing willingness by the courts in Alabama to enforce clauses as written.

It further demonstrates that when parties agree to arbitration, the courts are going to defer to the arbitrator's decision on as many issues as possible, including particular questions of procedural arbitrability.

Since many employment arbitrations simply do not have the issues or dollars at stake as do large commercial or construction arbitrations, any decisions like this which will cut

down on potential legal fees and expenses for protracted court battles are important and worthy of note by clients and litigators alike.

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