

## CHAPTER 1

# A BRIEF PRIMER ON THE HISTORY OF ARBITRATION

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### **I. Introduction**

Arbitration has been used as a dispute resolution tool for thousands of years. It has deep roots in a variety of settings, particularly in international and commercial contexts, and counts luminaries from King Solomon and George Washington to Rodger Goodell among its proponents. For much of this time it existed in an uneasy tension alongside courts of law, which were generally slow to embrace—and sometimes outwardly hostile to—the concept of a private party dispute resolution. However, beginning sometime in the early 20th century, countries around the world started to embrace arbitration, enacting laws requiring their courts to enforce arbitration agreements and severely circumscribing judicial review of arbitrators’ awards. Over the past 100 years a strong, pro-arbitration policy has emerged and it has become prevalent in commercial, consumer, and even professional sports disputes. Indeed, some would argue that arbitration has come to resemble traditional litigation, losing some of the time and cost savings that make it appealing to its proponents. This article explores these trends and provides a high-level overview of how the “law of arbitration” came to exist in its modern form.

### **II. Roots / History of Arbitration**

Arbitration is not a modern tool employed to avoid certain disadvantages associated with contemporary litigation; rather, the roots of arbitration can be traced through history to the most primitive societies as a

preferred method of dispute resolution. As set forth below, many legal fields that favor arbitration today—family, property, commercial transactions, trust and estates, and labor—have ancient arbitration roots.

One of arbitration's earliest family law decisions is King Solomon's infamous "judgment" in the Old Testament. Two mothers each claimed a child as her own and King Solomon asked for a sword to split the child in half. One woman protested that she would rather the other woman raise the living child while the second woman preferred the sword so that neither woman could raise the child. King Solomon's judgment was to give the child to the woman who was concerned for the child's best interest and would rather the child live with another than be divided.<sup>1</sup> Greek mythology even references arbitration. When Juno, Pallas Athene, and Venus dispute who is the most beautiful, the parties agreed to name Paris, the royal Shepherd, as arbitrator when all other methods of dispute resolution have failed.<sup>2</sup>

Arbitration to resolve property disputes has roots in Philip the II of Macedonia, father of Alexander the Great who often used arbitration in Ancient Greece, to resolve territorial disputes based on a peace treaty.<sup>3</sup>

Resolution of disputes arising out of commercial transactions spans across many nations and ancient peoples. Arbitration was used to resolve early commercial disputes in Marco Polo's desert caravans and between Greek and Phoenician traders.<sup>4</sup> In the middle ages of England, merchant disputes were viewed as better suited to arbitration type tribunals rather than the royal courts. Arbitration agreements in commercial contracts were first referred to as early as 1224.<sup>5</sup> Merchants traveled to different towns and fairs and needed expedited decisions on commercial and contractual disputes. The royal courts were more focused on land disputes rather than the issues that arose between merchants in financing commercial transactions.<sup>6</sup>

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1. Frank D. Emerson, *History of Arbitration Practice and Law*, 19 CLEV. ST. L. REV. 155, 155–56 (1970).

2. *Id.* at 156.

3. RICHARD BALES, *COMPULSORY ARBITRATION: THE GRAND EXPERIMENT IN EMPLOYMENT* 5 (Cornell University Press 1997).

4. Emerson, *supra* note 1, at 156.

5. Marvin F. Hill, Jr. & Anthony V. Sinicropi, *Improving the Arbitration Process: A Primer for Advocates*, 27 WILLAMETTE L. REV. 463, 465 (1991).

6. KYRIAKI NOUSSIA, *CONFIDENTIALITY IN INTERNATIONAL COMMERCIAL ARBITRATION* 11 (Springer-Verlag Berlin Heidelberg 2010).

Arbitration has long been used in estate management as well. Upon his death on December 14, 1799 (well before the American Arbitration Association implemented the Wills and Trusts Arbitration Rules and Mediation Procedure), it was revealed that George Washington had included an arbitration clause in his will:

But having endeavoured to be plain, and explicit in all Devises—even at the expence of prolixity, perhaps of tautology, I hope, and trust, that no disputes will arise concerning them; but if, contrary to expectation, the case should be otherwise from the want of legal expression, or the usual technical terms, or because too much or too little has been said on any of the Devises to be consonant with law, My Will and direction expressly is, *that all disputes (if unhappily any should arise) shall be decided by three impartial and intelligent men, known for their probity and good understanding; two to be chosen by the disputants – each having the choice of one – and the third by those two. Which three men thus chosen, shall, unfettered by Law, or legal constructions, declare their sense of the Testator’s intention; and such decision is, to all intents and purposes to be as binding on the Parties as if it had been given in the Supreme Court of the United States.*<sup>7</sup> (Emphasis added).

Clearly, Mr. Washington foresaw the benefits of avoiding expense and expediting the probate of wills in the realm of estate management.

### III. Judicial Attitudes Toward Arbitration

As reflected above, the concept of arbitration is deeply rooted across the globe. As formal courts of law began to develop, a perhaps uneasy tension resulted between courts, legislators, and arbitration, as evident in some early reported decisions from England and France. Interestingly, some observers have remarked that while arbitration as an institution precedes formal courts of law, upon the appearance of the latter arbitration immediately assumed a “backseat” role, subject to perhaps unwarranted oversight by the courts and viewed by many courts as lacking

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7. George Washington, The Will of George Washington Transcription (Mount Vernon, July 9, 1799), available at <https://trans-lex.org/files/george-washington-will.pdf>.

legitimacy.<sup>8</sup> (One notable exception to that rule is in the international trade context, as discussed *infra*.)

English law has long since recognized the use of arbitration as a dispute resolution mechanism, permitting the issuance of penal bonds to ensure compliance with arbitration agreements and adherence to decisions of arbitrators. See *Kulukundis Shipping Co., S.A. v. Amtorg Trading Corp.*<sup>9</sup> However, notwithstanding the above, some jurists viewed arbitration agreements as revocable by either party<sup>10</sup> and English courts throughout the 19th century and through a good part of the 20th century were generally hesitant to embrace arbitration agreements, perhaps for fear they would “oust” the jurisdiction of the courts.<sup>11</sup> The English courts would therefore not order specific performance of arbitration agreements, instead imposing relatively nominal penalties for breach of the agreement to arbitrate and then proceeding to judicial review of the claim on the merits.

French courts seemed to grapple with some of the same concerns. As early as 1790, the Constituent Assembly called arbitration “the most reasonable method for terminating disputes between citizens.”<sup>12</sup> Indeed, the French Civil Code had provisions recognizing and enforcing arbitration provisions in international trade disputes so long as certain safeguards prescribed by the legislature were adhered to. *L’Alliance v. Prunier*, Cour de cassation, Chambre civile, 10 July 1843. While France was quick to embrace on an international level, it was slower in the domestic context.<sup>13</sup> Nonetheless, a commentator has observed that the French jurisprudence was particularly important in developing consistency with respect to arbitration on the international level.<sup>14</sup>

In the United States, the roots of arbitration can be traced back before colonization as Native Americans used arbitration to settle disputes

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8. Tibor Varady, *The Standing of Arbitration Within the Legal System*, in LAW AND REALITY: ESSAYS ON NATIONAL AND INTERNATIONAL PROCEDURAL LAW 351–52 (Sumampouw et al. eds., 1995).

9. 126 F.2d 978 (2d Cir. 1942). See also TIBOR VARADY, ET AL., INTERNATIONAL COMMERCIAL ARBITRATION 45–50 (3d ed. 2006).

10. See *Vynor’s Case*, 77 Eng. Rep. 597 (1609).

11. See VARADY, *supra* note 9; see also Arthur Von Mehren, *A General View of Contract*, 7 INT’L ENCYCLOPEDIA OF COMP. L. 52–56 (1982).

12. *Id.*

13. *Id.* at 53.

14. Arthur Taylor von Mehren, *International Commercial Arbitration: The Contribution of the French Jurisprudence*, 46 LA. L. REV. 1045 (1986).

within and between tribes.<sup>15</sup> As early as 1632, the Commonwealth of Massachusetts had passed laws in support of arbitration. In one such private dispute, the wife of a prominent Boston resident used arbitration to resolve a private commercial dispute. Mrs. Hibbens contracted with Mr. Crabtree to perform carpentry services on her home but they could not agree on a price. They arbitrated the dispute, each choosing a qualified arbitrator—another carpenter. The carpenter arbitrators awarded a revised fee but Mrs. Hibbens refused to pay even after a second arbitration. Eventually, the church reverend presided over the final hearing.<sup>16</sup>

However, while arbitration may have been recognized during the early days of the United States, it was not preferred. Prior to the enactment of the Federal Arbitration Act (discussed *infra*), arbitrators' statutory authority to resolve a dispute was often limited to specific contexts, such as bankruptcy and admiralty.<sup>17</sup> Generally, American courts adopted the English common law approach, refusing to order specific performance of agreements to arbitrate and instead awarding only nominal damages for a party's breach of that agreement. See *Kulukundis Shipping Co., S.A. v. Amtorg Trading Corp.*<sup>18</sup> The Federal Arbitration Act (FAA) was enacted in 1925 to alter the judicial climate. As the legislative history quoted by the Second Circuit in *Kulukundis* reflects, "the effect of the bill is simply to make the contracting party live up to his agreement. . . . An arbitration agreement is placed on the same footing as other contracts, where it belongs." That legislative history specifically noted English hostility to arbitration agreements, referring to it as "jealousy" due to concern of having their jurisdiction ousted, and further expressed the desire to reject that view which had been adopted at common law by American courts.

The Federal Arbitration Act recognized, and perhaps attempted to bridge, the foregoing disconnect upon its passing in 1925. The Act gave a nod to the binding nature of arbitration by requiring federal courts to refer parties upon presentation of an agreement to arbitrate, and requiring

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15. Liliana Burnett, *The Current State of Arbitration Clauses Within Native American Tribal Contracts: An Examination of Binding Arbitration Contracts*, in NATIVE AMERICAN PAYDAY LENDING, THE ARBITRATION BRIEF 4, no. 1 142, 144 (2014).

16. Steven Certilman, *A Brief History of Arbitration in the United States*, NEW YORK DISPUTE RESOLUTION LAWYER (Spring 2010), available at <http://ssrn.com/abstract=1690512>.

17. VARADY, *supra* note 9, at 50 nn.28, 56.

18. 126 F.2d 978 (2d Cir. 1942).

courts to confirm and enforce those awards as judgments so long as there were not tainted by some narrow set of irregularities.

As jurisprudence interpreting the act developed, it became clear that arbitrators were vested with significant power—to determine whether a dispute fell within their jurisdiction to arbitrate, whether the contract at issue containing the arbitration agreement was even valid, and so on. State laws undermining the broad scope of the powers granted under the FAA were repeatedly held unenforceable. The use of arbitration as a broad dispute resolution mechanism became more and more prevalent as a result. Far from declining to enforce arbitration agreements voluntarily entered into between parties as was the case a mere 100 years ago, courts today now find that even non-parties to agreements may be required to arbitrate under an estoppel theory. *See, e.g., Sokol Holdings, Inc. v. BMB Munai, Inc.*<sup>19</sup> This is somewhat common in the surety context, where sureties have been required to arbitrate disputes under the construction contract where the surety bond in dispute incorporates an underlying contract that requires arbitration. *See, e.g., St. Paul Fire & Marine Insurance Co. v. Wooley/Sweeney Hotel #5.*<sup>20</sup>

#### **IV. The Rise of Institutional Arbitration**

The enactment of the FAA undoubtedly led to an increase in the sheer number of arbitrations, as the reliability of agreements to arbitrate, and the ability to rely upon courts to enforce awards issued therein, gave contracting parties more confidence in the system.<sup>21</sup> As set forth below, this confidence was further increased by the so-called “institutionalization” of arbitration, whereby private entities promulgated rules, regulations and procedures that parties could rely upon to further standardize the process.

To that end, obviously one of the hallmarks of arbitration is the parties’ ability to choose the parameters that will apply to resolve their disputes. In some respects, this likely proved easier said than done, as parties lacked the time and motivation to specify in detail the various rules that would govern theoretical disputes that could arise. Accordingly, around the same time as the Federal Arbitration Act was passed, the American Arbitration Association (“AAA”) was formed via the

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19. 542 F.3d 354 (2d Cir. 2008).

20. 545 So. 2d 958 (Fla. App. 1989).

21. *See* Von Mehren, *supra* note 11, at 56.

consolidation of three smaller arbitration societies. Drawing from the collective knowledge of participating legislators, practitioners, jurists, academics and industry leaders, sets of model rules were created that, via simple incorporation by reference in the applicable agreement to arbitrate, could provide a principled mechanism for resolving parties' disputes, and by 1931 the AAA published its "First Code of Arbitration Practice and Procedure."<sup>22</sup>

The AAA model also administered arbitrations, providing parties with easier access to qualified, neutral arbitrators who had experience administering the AAA's rules. By 1966, the AAA alone administered approximately 13,000 cases per year.<sup>23</sup> By 1979, the demand for such institutional models had continued to rise to the point that two other institutions—"Judicial Arbitration and Mediation Services" (now known simply as "JAMS") and "Conflict Prevention and Resolution ("CPR")—were also formed.<sup>24</sup> As with the AAA, both of these entities promulgate their own sets of rules and procedures, and JAMS actually employs a network of full-time neutrals to resolve disputes, both nationally and internationally. As the demand for arbitrators grew, further subspecialties were developed. For example, the National Association of Securities Dealers (NASD) and New York Stock Exchange (NYSE) devolved their own framework for administering disputes in the securities industry. When these two agencies merged to create Financial Industry Regulatory Authority (FINRA), that entity became the largest dispute resolution forum in the securities industry field. With the Supreme Court's blessing in *Shearson/American Express v. McMahon*<sup>25</sup> today nearly all disputes (with the notable exception of securities class actions) involving brokerage firms are resolved in arbitration.

The evolution and prominence of institutionalized arbitration has also reached surety companies in the payment and performance bond context. As mentioned above, sureties may be bound to arbitration because of owners, architects, contractors, and subcontractors' frequent use of the American Institute for Architects (AIA) forms as the basis for the

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22. The 'Lectric Law Library, History of the AAA and Alternative Dispute Resolution, <http://www.lectlaw.com/files/adr07.htm>

23. *Id.*

24. David McLean, *US Arbitral Institutions and Their Rules*, LEXISNEXIS FOR LEXISPSL ARBITRATION, <https://www.lw.com/thoughtLeadership/us-arbitral-institutions-and-their-rules>.

25. 482 U.S. 220 (1987).

construction contract. Specifically, Form AIA – A201™, the General Conditions of the Contract for Construction is regularly incorporated into the construction contract. Both the 2007 and recently revised 2017 versions of this form include arbitration clauses which name the American Arbitration Association as the forum for arbitration. Section 15.4, titled Arbitration of AIA, A201™ – 2007 and A201™ – 2017 states:

§15.4.1 If the parties have selected arbitration as the method for binding dispute resolution in the Agreement, any Claim subject to, but not resolved by, mediation shall be subject to arbitration which, unless the parties mutually agree otherwise, shall be administered by the American Arbitration Association in accordance with its Construction Industry Arbitration Rules in effect on the date of the Agreement.<sup>26</sup>

International arbitrations have evolved along similar lines. In 1958, the United States passed the “New York Convention,” which recognizes agreements to arbitrate that were entered into in foreign nations that were also signatories to the Convention, and also provides a mechanism for recognizing and enforcing awards made by tribunals in those countries. Moreover, in 1976 the United Nations Commission on International Trade Law (“UNCITRAL”) adopted a “Model Law” applicable to international commercial arbitrations. These rules, known as the UNCITRAL Rules, are specifically developed to apply internationally and are tailored to meet the needs of the UN’s various member States: “the establishment of rules for ad hoc arbitration that are acceptable in countries with different legal, social and economic systems would contribute to the development of harmonious international economic relations.”<sup>27</sup>

## V. Arbitration Pitfalls: Have the Stated Goals of Arbitration Proven Elusive?

One of the obvious benefits of arbitration is its finality and promotion of expeditious, and less expensive, decisions. The early presumption was

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26. A201™—Compared to A201™—2007, 35 *available at* <http://content.aia.org/sites/default/files/2017-08/A201%202017%20Comparative%20and%20A101%20Exhibit%20New.pdf>.

27. United Nations Commission on International Trade Law (UNCITRAL), ARBITRATION RULES, General Assembly Resolution 31/98, *available at* [www.uncitral.org/pdf/english/texts/arbitration/arb-rules/arb-rules.pdf](http://www.uncitral.org/pdf/english/texts/arbitration/arb-rules/arb-rules.pdf).



that parties to an arbitration agreement would be willing to trade-in some of the safeguards afforded by the courts in exchange for these considerations. *American Almond Products Co. v. Consolidated Pecan Sales Co.*<sup>28</sup>

Some may question whether these goals are still met in the arbitration context, or whether arbitration has simply become another, perhaps more expensive, form of traditional litigation. As one practitioner has remarked, “[w]hat started as a relatively swift and economical process for a . . . claimant to seek justice has evolved into a costly extended adversarial proceeding dominated by trial lawyers and the usual litigation tactics.”<sup>29</sup>

Some of the most visible examples of this paradigm shift are found in professional sports disputes, which generally involve challenges to discipline meted out to individual players and, on occasion, teams. These proceedings, followed by the judicial challenges thereto, involve dozens of lawyers from preeminent firms and routinely stretch far beyond the length of the suspension or other penalty being appealed.

Even smaller disputes are trending more toward the standard courtroom model. By way of example, the AAA rules permit extensive discovery where the parties agree or the arbitrator otherwise orders. Likewise, UNCITRAL Rules were “updated” in 2010 to reflect modern challenges like multi-party practice and expert discovery.

More discovery equates to more legal fees, and the involvement of experts can cause these costs to increase exponentially. Beyond that, the caliber of arbitrator required to resolve many technical or high-dollar disputes does not come cheap, and indeed, where a three-arbitrator panel is chosen (or required—for example, FINRA rules mandate three arbitrators in certain scenarios, as do AAA), the arbitrator costs alone can easily creep into the six-figures. Against this backdrop, one cannot help but wonder if some of the advantages originally intended by the arbitration framework are becoming illusory. Nonetheless, it is clear that arbitration is here to stay, and most litigators will be well-served to familiarize themselves with the concepts discussed in the coming pages.

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28. 144 F.2d 448, 450 (2d Cir. 1944).

29. Gretchen Morgenson, *Is This Game Already Over?*, N.Y. TIMES, June 18, 2006.