

Ascertaining the Parties' Intentions in Arbitral Design

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I. INTRODUCTION

Supreme Court case law teaches us that the federal interest in arbitration does not consist of enforcing agreements to arbitrate according to some sort of abstract or ideal arbitral model, but rather according to the particular arbitral model upon which the parties had agreed.¹ This body of law is driven by the same notions of party autonomy that underlie the law of arbitration generally.² That parties may agree to forego access to national courts in favor of arbitration is an initial manifestation of that attitude. By logical extension, the parties also enjoy extraordinary latitude in determining the features that “their” eventual arbitration should display.

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1. *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52 (1995); *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468 (1989).

2. *See generally* A. VAN DEN BERG, *THE NEW YORK ARBITRATION CONVENTION OF 1958*, at 144-45 (1981).

A legal system that elevates party autonomy in arbitration to such a high level of importance ought, at least in principle, to develop some consistent methodology for identifying the arbitral features that the parties intended for their arbitration. United States arbitration law simply has not done so, thus leaving arbitrators and courts alike somewhat at sea. For the arbitrators, there is more at stake than merely respecting party preferences, important though that is. A tribunal that deviates substantially from the procedures agreed upon by the parties, and insisted upon by one of them, risks finding its award vacated³ or denied recognition or enforcement.⁴ Of course, for any number of reasons, an award resulting from an arbitral process that deviated from party intentions may nevertheless survive and earn recognition or enforcement: the deviation may be regarded as insubstantial;⁵ the complaining party may be deemed to have waived its objections or otherwise acquiesced;⁶ or the general latitude that arbitrators enjoy in matters of procedure may operate to shield the award.⁷

The fault, if that is the right term, lies of course partly with the parties and their counsel. By virtue of the premises of party autonomy itself, the parties bear responsibility for making their intentions known, and they commonly could have done a much better job in that regard than they did. But that will always be the case to some degree.

It is courts, led by the United States Supreme Court, that have made fidelity to the parties' arbitral preferences a cardinal principle of arbitration law, and it is they that ultimately have responsibility for enforcing that principle. Yet, an examination of the multitude of cases in which the parties disagree over the ground rules governing their arbitration reveals that the courts do little better than improvise as they try to identify what in fact the parties intended by way of arbitral process. The contrast between the confidence with which the courts proclaim the principle of fidelity to party intention in arbitral design, on the one hand, and the precariousness of their conclusions as to what the parties actually intended by way of arbitral design, on the other, is nothing short of striking.

3. Federal Arbitration Act, 9 U.S.C. §§ 9-10.

4. United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 21 U.S. 2517, 330 U.N.T.S. 3, as implemented in the United States, 9 U.S.C. §§ 201-08. *See also* Yusuf Ahmed Alghanim & Sons v. Toys "R" Us, Inc., 126 F.3d 15 (2d Cir. 1997), *cert. denied*, 118 S. Ct. 1042 (1998).

5. *E.g.*, Fairchild & Co. v. Richmond, Fredericksburg & Potomac R.R. Co., 516 F. Supp. 1305 (D. D.C. 1981).

6. *E.g.*, Fortune, Alsweet & Eldridge, Inc. v. Daniel, 724 F.2d 1355 (9th Cir. 1983) (*per curiam*).

7. *E.g.*, Parsons & Whittemore Overseas Co. v. Société Générale de l'Industrie du Papier, 508 F.2d 969 (2d Cir. 1974).

To begin with, there is a greater diversity of arbitral process among the various institutional and other rules available to the parties for incorporation in their agreement than is commonly acknowledged. Moreover, the Federal Arbitration Act (FAA) is decidedly not preemptive, in the sense of “occupying the field,”⁸ so that state law may provide different or additional ground rules. The peculiarities not only differ from state to state, but may differ according to the particular body of law within any given state—the state law of contracts, the state law governing arbitration agreements, and the state law of arbitration itself—that one consults. The result is an environment in which, unanimity over the general principle of party autonomy notwithstanding, uncertainty and disagreement over the kind of arbitration the parties wanted easily arise. Courts need to face that reality and seek more effectively to close the intentions “gap.” This article aims to illustrate the nature and magnitude of the problem and begin an effort to mitigate it.

II. THE ORIGINS: *VOLT* AND *MASTROBUONO*

In a pair of seminal rulings, the Supreme Court defined the federal interest in arbitration as emphatically limited to effectuating the parties' intention to resolve future disputes according to the procedural design that the parties themselves selected, rather than according to some standard arbitral model. Thus, while federal law seeks to promote arbitration, the arbitration sought to be promoted is the arbitration that the parties intended.

In *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University*,⁹ the Court determined that the FAA permitted application of a California statute postponing the arbitration pending the outcome of related litigation involving persons not party to the agreement to arbitrate.¹⁰ Although the effect of the California law could be described in general terms as *not* pro-arbitration, it was deemed by the Court to be an integral part of the arbitral framework that the parties had bargained for and that the FAA requires courts to support. The Court reasoned that the parties, in choosing California law,¹¹ had adopted a procedural provision of California that permitted

8. *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468, 477 (1989).

9. *Id.*

10. California Arbitration Act, Cal. Civ. Proc. Code Ann. § 1280 *et seq.* (West 1982).

11. The contract did not name California law as such as the governing law. Rather, it provided that “[t]he Contract shall be governed by the law of the place where the Project is located,” and the project was located in California. *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 65 (1995)

postponement of arbitration under certain stated circumstances. Moreover, the Court believed that it was bound by the state courts' determination that the choice of law clause was to be interpreted as embracing the California statutory provision in question.¹²

In *Mastrobuono v. Shearson Lehman Hutton, Inc.*,¹³ decided several years later, the Court determined that the arbitration contemplated by the parties was one that permitted the arbitrators to award punitive damages in proper circumstances. This time, the Court did not base its conclusion on the law chosen by the parties to govern their contract, since that law—New York law—barred the award of such damages by arbitrators.¹⁴ Rather, the Court looked to the then-NASD rules of arbitration to which the parties had also made specific reference in their agreement and which, at the very least, did not foreclose the award of punitive damages.

This pair of cases represents only two of the innumerable scenarios in which private parties, even while giving signals indicating the type of arbitration they would want, leave the courts, and indeed the arbitrators, in genuine doubt as to the specific features they intended their arbitration to display.

The central problem in *Volt* was that the parties had incorporated into their agreement a body of state law that constrained the arbitration in ways that the state arguably could not have unilaterally imposed as a matter of state policy.¹⁵ However, the parties in *Volt* were deemed to have incorporated that law by reference into their agreement, thus making it an element of the arbitration meant to be championed by the FAA's pro-arbitration policy. The question that *Volt* clearly raised was whether and to what extent a policy that a state might not be permitted to dictate to the parties is one that the parties could nevertheless be deemed voluntarily to have embraced by electing that body of law.

The problems of party autonomy were compounded in *Mastrobuono*. Not only did the parties voluntarily embrace a body of law that restricted the arbitrators' powers of decision (much as in *Volt*), but they confused matters further by also specifically referencing in their arbitration agreement a body of procedural rules (the NASD Code of

12. Before the Supreme Court, *Volt* understandably argued that the state courts had erred in interpreting the choice-of-law clause as bringing California rules of arbitral procedure into their arbitration agreement, but the Supreme Court was unwilling to review the state courts' interpretation of the contract, which it considered to be strictly a question of state law. *Volt*, 489 U.S. at 474.

13. 514 U.S. 52 (1995).

14. The New York Court of Appeals had ruled that under New York law only judicial tribunals, and not arbitral tribunals, have the authority to award punitive damages. *Garrity v. Lyle Stuart, Inc.*, 353 N.E. 2d 793 (1976).

15. See *Allied-Bruce Terminix Co. v. Dobson*, 513 U.S. 265 (1995); *Southland Corp. v. Keating*, 465 U.S. 1 (1984).

Arbitration Procedure) that could be read as lifting that very restriction. The Code itself was silent on the subject of punitive damages, mentioning only “damages and other relief,”¹⁶ without more, and the Court chose to read such silence as tacitly preserving the possibility of an award of punitive damages. The Court drew support for this result from the manual that the NASD furnished to its arbitrators, which stated that “[t]he issue of punitive damages may arise with great frequency in arbitrations [and that p]arties to arbitration are informed that arbitrators can consider punitive damages as a remedy.”¹⁷ *Mastrobuono* thus involved not only a potential conflict between a state law rule and federal policy in matters of arbitration, as in *Volt*, but doubt as to whether the parties embraced that particular state law rule in the first place, when other language in the agreement suggested that they preferred a set of contrary ground rules. In other words, *Mastrobuono* was a case of “mixed signals.”

In fact, *Volt* and *Mastrobuono* entailed reference to only some, but not all, potential indicators of party intention as to arbitral design. The facts in *Volt* permitted the Court to focus on a California law providing for the deferral of arbitration, while the facts in *Mastrobuono* permitted the Court to consider the provisions of both New York law and the NASD Code on the arbitrators' authority to award punitive damages. In reality, there exists a much broader range of potential “extrinsic” sources of party intent.

III. THE LAW OF THE CONTRACT AND THE *LEX ARBITRI*

As noted, the Court in both *Volt* and *Mastrobuono* apparently looked to the substantive state law that the parties had chosen. Its decision to do so rests on debatable premises. It is useful, therefore, to examine more deeply the Court's assumptions and analyses.

A. *Applying the Substantive Law of the Chosen State*

Choice of law clauses come in various forms. In the great majority of cases, the provision represents what courts have come to call a “generic” choice of law clause,¹⁸ that is, a clause calling in general terms for application of the designated state's law, without further specification of any particular body of law within state law. Such was the case, for example, in *Volt*.¹⁹ The Supreme Court recognized the problem inherent

16. NASD Code of Arbitration Procedure, P3741(e).

17. *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 61 (1995).

18. *Roadway Package Sys. v. Kayser*, 257 F.3d 287, 296 (3d Cir. 2001).

19. *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468, 470 (1989).

in treating a generic choice of law clause as incorporating a state's law of arbitration, but it nevertheless chose to defer to the California courts' view that the choice of law clause should be construed to include California arbitration law.²⁰ Justice Brennan, dissenting, considered that the Court was not bound by the state courts' treatment of a generic choice of law clause as encompassing a state law provision on a narrow question of arbitral procedure.²¹

Fortunately, in the great majority of cases since *Volt*, the courts have rejected the notion that a generic choice of law clause should do anything more than import into the transaction the state's rules of substantive law—that is, the rules going to the merits of the underlying dispute.²² Of course, the *Mastrobuono* decision strongly promoted this development, since it rejected the idea that a generic choice of New York law imported into the parties' contract a New York rule disallowing an award of punitive damages by arbitrators. (In reaching this conclusion, the *Mastrobuono* Court chose to treat the New York law rule as if it were a rule of arbitral procedure rather than a substantive rule of law,²³ a characterization that is, however, debatable.) As a result, courts have mostly distanced themselves from the notion, to which *Volt* had lent at least some support, that issues of arbitration law should be regarded as falling within the ambit of a generic choice of law clause. For most courts, only a clause specifically designating a state law to govern the arbitration agreement has the effect of incorporating into the agreement that state's law of arbitration.²⁴

B. *The Often-Overlooked Lex Arbitri*

If the law designated in a generic choice of law clause is not ordinarily applicable to matters of arbitral procedure, then what law is applicable? One obvious possibility is to have the *lex arbitri*, *i.e.*, the law governing the arbitration, govern matters of arbitral procedure. Certainly, in international arbitration, the law of arbitration at the place of arbitration is considered to supply the rules governing the arbitral process itself.²⁵ That is to say, the parties are deemed, in designating an

20. *Id.* at 475.

21. *Id.* at 479 (Brennan, J., dissenting).

22. *See, e.g.*, *Sec. Ins. Co. of Hartford v. Trustmark Ins. Co.*, 283 F.Supp. 2d 602 (D. Conn. 2003); *Porush v. Lemiure*, 6 F. Supp. 2d 178 (E.D.N.Y. 1998); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Stephenson*, 822 F. Supp. 125 (S.D.N.Y. 1993).

23. *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 59-60 (1995).

24. *See, e.g.*, *Jacada (Europe) Ltd. v. Int'l Mktg. Strategies, Inc.*, 401 F.3d 701 (2005); *UHC Mgmt. Co., Inc. v. Computer Scis. Corp.*, 148 F.3d 992 (8th Cir. 1998); *Stone & Webster, Inc. v. Baker Process, Inc.*, 210 F.Supp. 2d 1177 (S.D. Cal. 2002).

25. GARY B. BORN, *INTERNATIONAL COMMERCIAL ARBITRATION* 1240ff. (2009).

arbitral seat, to have submitted their arbitration as such to that body of law, including its rules or presumptions as to arbitral design. Fortunately, most rules of the *lex arbitri* turn out to be default rules only (that is, rules from which the parties may agree to derogate), and few of them are mandatory. The parties remain free to structure their arbitration as they choose, with the *lex arbitri* supplying rules only to the extent the parties fail to do so.²⁶

Yet, in both *Volt* and *Mastrobuono*, the *lex arbitri* passed entirely unmentioned. The oversight is less remarkable in *Mastrobuono*, since the authority of arbitrators to award punitive damages could have been regarded as implicating the substance of the dispute (and thus properly governed by the substantive law chosen by the parties) rather than the arbitral procedure itself (and thus properly governed by the *lex arbitri*). More problematic is *Volt*, since the issue in question there—namely, the propriety of suspending an arbitration pending the outcome of litigation—relates chiefly to the conduct of the arbitration rather than to the substance of the dispute. Yet, in both cases, the Court paid regard to the substantive law of the contract and not to the law of the place of arbitration.²⁷

In *Volt*, at least, the error—if it was error—might be considered harmless. The place of arbitration in that case seems likely, given the contract's reference to the location of the parties and the construction project, to have been California. (It is nevertheless revealing that the Court nowhere indicates where the arbitration was to have taken place.) California law was accordingly not only the applicable substantive law, having been designated in the parties' choice of law clause, but in all likelihood also the *lex arbitri*. However, the same cannot be said of *Mastrobuono*, since the place of arbitration there appears to have been Illinois,²⁸ yet the substantive law chosen by the parties was the law of New York. Part of the autonomy parties in arbitration enjoy, after all, is the autonomy to pick different jurisdictions as place of arbitration and place of applicable law.

The two cases demonstrate that if, as *Volt* dictates, courts are to give effect to the parties' expectations in terms of arbitral procedure—and in so doing potentially consult both the chosen law and the *lex arbitri* as sources of presumed party intent—they need to delineate more clearly

26. *Id.* at 1241.

27. As noted, the Supreme Court did not seem entirely convinced that the California rule in question represented a rule of substantive law, as opposed to a rule of arbitral procedure. But, it felt bound to defer to the California courts' determination that the election by the parties of California law as the governing law included the election of this provision. *See supra* note 12.

28. *Mastrobuono*, 514 U.S. at 54.

than they often do the proper sphere of these two bodies of law. The *lex arbitri* has a wide scope of application. It has been understood as governing in principle both the *internal* and the *external* aspects of an arbitration.²⁹ “Internal” issues relate principally to procedural aspects of the arbitration, such as the required number of arbitrators, the availability of provisional relief in the arbitration, discovery, and arbitrator ethics. “External” issues, by contrast, concern the relationship between the arbitral proceedings and national courts, typically the courts of the place of arbitration, and thus entail such matters as judicial orders of provisional relief, judicial aid in the gathering of evidence, and judicial annulment of awards.

While the provision at issue in *Volt*, namely the “postponability” of the arbitration, seems to fit somewhat more comfortably into the external than the internal category of issues, it would appear, by any measure and in any event, to be properly subject to California law as the *lex arbitri*. What the California provision in question is *not* is a provision going to the substance of the dispute. Unlike questions such as the scope of the submission to arbitration or the forms of relief available to the arbitrators (as was the issue in *Mastrobuono*), the question that the California provision addresses does not even entail interpretation of the contract or the arbitration agreement. In other words, whether the “postponability” issue is characterized as internal or external, it cannot reasonably be said to come within the ambit of the substantive law governing the contract. It is a *lex arbitri* issue. In sum, the Court did not do an especially good job in these cases of delineating the respective spheres of a state’s substantive law, on the one hand, and its law of arbitration, on the other.

In point of fact, an examination of the domestic post-*Volt* cases finds that, even when courts properly refuse to apply a generic choice of law clause to an issue of arbitral process, they rarely turn to the law of the site of arbitration as a source.³⁰ In the majority of cases in which post-*Volt* courts decide whether to enforce a given provision of state law relating to arbitral design, they do not consult the law of the place of arbitration. As in *Volt* and *Mastrobuono* alike, the place of arbitration may not even be mentioned.

This finding is problematic for a number of reasons. First, disregarding the law of the arbitral situs on arbitration issues may, albeit

29. BORN, *supra* note 25, at 1241-43.

30. See, e.g., *H.D. Brous & Co., Inc. v. Mrzyglocki*, No. 03 CIV. 8385 (CSH), 2004 WL 1367451 (S.D.N.Y. June 16, 2004); *Arnold v. Goldstar Fin. Sys., Inc.*, No. 01 C 7694, 2002 WL 1941546 (N.D. Ill. Aug. 22, 2002); *Painewebber, Inc. v. Landay*, 905 F. Supp. 193 (D. Mass. 1995).

rarely, prejudice the validity of the award³¹ or its eventual recognition or enforcement.³² In addition, ignoring the *lex arbitri* in domestic FAA cases introduces a strange dissonance between the interstate and the international cases, for in international cases, courts do generally consider the arbitration law of the arbitral situs as the law providing the legal framework of the arbitration.³³ It is understandable that courts pay closer attention to the distinction between substantive law and the *lex arbitri* in international cases, but there is no principled reason why they should do so. Finally, not all contracts—not even all commercial contracts—contain a choice of law clause. In the absence of such a clause and of a role for the *lex arbitri*, courts have no choice but to embark on an inquiry into which jurisdiction has the closest connection with the contract or the greatest claim to have its rules of law apply.³⁴ Such a practice can only lead to uncertainty.

In fact, courts often (and especially when the choice of law clause is a generic rather than arbitration-specific one) apply some combination of FAA case law, including the FAA's so-called "pro-arbitration bias,"³⁵ on the one hand, and the judicial forum's own law of arbitration,³⁶ on the other. Note that the judicial forum will not necessarily be the same as the arbitral forum. The court that will hear an action to confirm or vacate an award will ordinarily be the court of the place of arbitration (*i.e.*, the place that furnished the *lex arbitri*),³⁷ but there is no guarantee that that

31. The Federal Arbitration Act authorizes vacatur of an award "3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced."

32. Article VI(d) of the New York Convention authorizes courts to refuse recognition or enforcement where "the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place." See also *Yusuf Ahmed Alghanim & Sons v. Toys "R" Us, Inc.*, 126 F.3d 15 (2d Cir. 1997), *cert. denied*, 118 S. Ct. 1042 (1998).

33. See BORN, *supra* note 25, at 1240ff.

34. See, for example, UNCITRAL Model Law of Arbitration: "[F]ailing any designation by the parties, the arbitral tribunal shall apply the law determined by the conflict of law rules which it considers applicable."

35. *E.g.*, *Progressive Casualty Ins., Co. v. CA Reaseguradora Nacional de Venezuela*, 991 F.2d 42, 48 (2d Cir. 1993).

36. In *CRS Serrine Eng'rs, Inc. v. Aetna Casualty & Surety Co.*, No. 96-11749-GAO, 1997 WL 136335 (D. Mass. Feb. 24, 1997), the federal district court sitting in Massachusetts looked not only to the federal policy favoring arbitration, but also to the Massachusetts Uniform Arbitration Act to determine the circumstances in which consolidation of separate arbitrations was proper. There is no indication in the case of what the place of arbitration was to be. The Court may have applied Massachusetts law on account of that state being the forum state. See also *Kilmer v. Flocar, Inc.*, 212 F.R.D. 66 (N.D.N.Y. 2002).

37. The New York Convention, Article VI(e) implies that an award may be vacated or confirmed not only by the courts of the place where the award was made, but, also, in

will be the case in an action to compel arbitration or to recognize or enforce an award. In the latter cases, application of forum law will often make little or no sense.

In sum, it is not enough for courts to distinguish between “generic” and “arbitration-specific” choice of law clauses, desirable as such a distinction may be. Courts should also seriously distinguish between the issues most properly determined by the chosen law and those most properly determined by the *lex arbitri*. Of course, consideration must always be given to the FAA and to FAA case law, since no body of state law may operate to frustrate the overriding federal policy in favor of arbitration of disputes where the parties have indeed agreed to arbitrate.³⁸

C. *Conflicts between State Law and the FAA*

Whether the intent of the parties as to a given issue of arbitral design is determined by reference to the law of the contract, the law of the arbitration agreement, or the *lex arbitri*, the question remains whether the parties may, through incorporation by reference, select a state law that is inconsistent with the FAA and its underlying policies.

On the one hand, Supreme Court rulings establish that the FAA’s pro-arbitration purposes, coupled with the Supremacy Clause, operate to bar States from enforcing laws that render certain causes of action non-arbitrable,³⁹ that treat agreements to arbitrate as any less enforceable than other private agreements,⁴⁰ or that otherwise impede the overriding federal policy in favor of arbitration as a method of dispute resolution.⁴¹ A State, therefore, may not create a cause of action and declare it to be non-arbitrable, impose conditions on the enforceability of an agreement to arbitrate that it does not impose on private agreements generally, or otherwise frustrate Congress’ pro-arbitration policy. That much seems clear.

On the other hand, if the parties are truly the architects of their arbitration, as *Volt* insists, then they are surely free to include in their arbitration agreement the language of a state statute that is, in itself, inhospitable to arbitration. Taking *Volt* again as an example, nothing would have prevented the parties from agreeing in their contract that any arbitration initiated pursuant to their agreement would be subject to stay

the rare case where the parties have agreed that the arbitration should be governed by an arbitration law of a state other than the place of arbitration.

38. *Doctor’s Assoc. v. Casarotto*, 517 U.S. 681 (1995).

39. *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265 (1995); *Southland v. Keating*, 465 U.S. 1 (1984).

40. *Casarotto*, 517 U.S. 681; *Perry v. Thomas*, 482 U.S. 483 (1987).

41. *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468, 477-78 (1989); *see also Casarotto*, 517 U.S. 681.

or suspension by a court in the event that the same or closely related dispute happened to be the subject of court proceedings involving a person who was not a party to the arbitration agreement. Indeed, they could have “cut and pasted” the California provision into the body of their arbitration agreement. Having expressed their preference as to arbitral procedure, the parties would be entitled, according to *Volt*, to have that preference respected. In other words, they would have effectively made that feature as much an element of their arbitration as any other one they built into their agreement. The same conclusion would follow if the parties merely referred to the specific state law provision, as by its title or section number. Whether the incorporation is achieved *in haec verba* or by specific identification, the parties would have acknowledged that the state statute had become part of their agreement to arbitrate.

In the great majority of cases, however, we find ourselves with neither a state law on its own impermissibly restricting the arbitration, nor an express incorporation of that law into the parties' arbitration agreement. All we have is a reference to a chosen substantive law and perhaps an indication of the intended place of arbitration. This is, of course, the scenario in *Volt*, except that there the Court avoided the difficulty by essentially finding no inconsistency between the California statute and the policies underlying the FAA. According to the *Volt* Court, the California statute merely addressed the sequence between arbitration and litigation,⁴² a determination upon which the federal policy favoring arbitration did not depend. The Court found that such a provision on timing was not capable of “undermin[ing] the goals and policies of the FAA.”⁴³

By determining in a conclusory fashion that the California law was not “arbitration-unfriendly,” the Court failed to probe meaningfully into the degree of dissonance between the California statute and the FAA's pro-arbitration philosophy. But, the question whether the required postponement of arbitration was sufficiently arbitration-unfriendly as to offend the FAA called for a more serious inquiry by the Court. Arguably, a postponement of arbitration affects a good deal more than mere timing. The point of postponing arbitration is to avoid an

42. “[W]e think the California arbitration rules which the parties have incorporated into their contract generally foster the federal policy favoring arbitration. . . . [T]he FAA itself contains no provision designed to deal with the special practical problems that arise in multiparty contractual disputes when some or all of the contracts include agreements to arbitrate. California has taken the lead in fashioning a legislative response to this problem by giving courts authority to consolidate or stay arbitration proceedings in these situations in order to minimize the potential for contradictory judgments.” *Volt*, 489 U.S. at 476 n.5.

43. *Id.* at 478.

inconsistency of result between the outcomes of the litigation and arbitration.⁴⁴ But, that objective can only be achieved by treating the parties to the later proceeding (the arbitration) as bound by the determinations reached in the prior proceeding (the litigation), and that in turn can only be achieved by depriving the arbitrators of the right to make the relevant determinations independently. Only with difficulty can such a result be regarded as arbitration-friendly. In short, the Court in *Volt* plainly missed an opportunity to clarify what it takes for a state law provision to thwart the substantive federal policy favoring the arbitration of disputes.

The courts would do well to confront this problem more squarely than the Supreme Court did in *Volt*. It is one thing for courts to impute to the parties default rules of arbitration contained in either the law governing the contract or in the *lex arbitri*. It is another thing to give effect to inhospitable state laws on the basis of a fiction that the parties knowingly made those laws a part of their contract and thereby part of the arbitration. A distinction should be drawn between state law provisions that the parties specifically acknowledged and those they did not—with the former, and only the former, deemed to reflect an expression of party intent as to arbitral design sufficient to overcome the presumption of inapplicability of state laws that are inconsistent with the FAA.

Not only did the Supreme Court fail seriously to consider whether application of the California law would undermine the federal policy favoring arbitration, but it failed even to consider how likely it was that the parties had any expectation, in selecting California law as the substantive law of the contract, of embracing a purely procedural rule that would effectively remove crucial issues from the arbitration and submit them to a litigation process that they had sought to avoid. In other words, the Court did a poor job of assessing the impact of the California law on the viability of the arbitration, and no job at all of assessing the likelihood that the parties meant to embrace California's postponement mechanism in the first place.

If the Court is serious about protecting arbitration from hostile state law, it has every reason to keep FAA-inconsistent state law from creeping too easily into the definition of the kind of arbitration for which the parties contracted. But it cannot possibly hope to succeed in that effort without giving greater and clearer content than it did in *Volt* to the notion of conflict between state law rules and mechanisms regarding arbitration, on the one hand, and the federal policy favoring arbitration, on the other.

44. *Id.*

IV. RULES OF ARBITRATION

Another obvious extrinsic source of party intention—in addition to the law governing the contract as a whole, the law governing the arbitration agreement, and the law of the place of arbitration—is the body of rules of arbitral procedure that the parties may have adopted in their arbitration agreement. It seems fair to suppose that the parties, in incorporating such rules into their arbitration agreement, mean for them to fill gaps in that agreement, subject to any mandatory rules of law of the place of arbitration that may apply.⁴⁵

A. *Rules of Arbitral Procedure*

To the extent that courts seek, as *Volt* requires, to determine the kind of arbitration the parties intended to have, rules of arbitral procedure designated in an arbitration agreement have a central role to play. Whether the parties specifically designated a set of procedural rules, or simply chose a specific administering arbitral institution that has promulgated procedural rules, those rules are properly considered as having been incorporated into the arbitration agreement.⁴⁶ Even if the parties were personally unfamiliar with the rules, they signed an arbitration agreement that specifically incorporated them, and may properly be treated as intending them to govern the arbitration. Obviously, such rules can be displaced by more specific terms in the arbitration agreement⁴⁷ and can also be supplanted by inconsistent mandatory rules of the arbitral forum.⁴⁸ Otherwise, they should be considered as elements of the arbitral design that the parties chose and that *Volt* expects the courts to enforce.

In some respects, imputing rules of arbitral procedure to the parties is a more reliable exercise than imputing to them provisions of the governing law or the *lex arbitri*. When parties make a generic choice of law to govern their contract, they contemplate that the chosen law will determine their respective rights and obligations and the relief to which they are entitled in the event of breach. Rarely will they be contemplating the rules of that jurisdiction concerning the arbitration of

45. *E.g.*, *Coastal Caisson Corp. v. E.E. Cruz/NAB/Frontier-Kemper*, Nos. 05 Civ. 7462(DLC), 05 Civ. 7466, 2007 WL 2285936 (S.D.N.Y. Aug. 10, 2007); *Williamson v. Public Storage, Inc.*, No. 3:03CV1242(RNC), 2004 WL 491058 (D. Conn. Mar. 1, 2004).

46. *E.g.*, *St. Lawrence Explosives Corp. v. Worthy Bros. Pipeline Corp.*, No. 96-7745, 1997 WL 187332 (2d Cir. Apr. 17, 1997).

47. *Szuts v. Dean Witter Reynolds, Inc.*, 931 F.2d 830, 831-32 (11th Cir. 1991).

48. *See* UNCITRAL Rules of Arbitration, Rule 2.1 (“These Rules shall govern the arbitration except that where any of these Rules is in conflict with a provision of law applicable to the arbitration from which the parties cannot derogate, that provision shall prevail. . .”).

eventual disputes. (The situation is obviously different when a choice of law clause states that it specifically governs the arbitration agreement or the arbitration itself.) It is true that parties contemplate arbitration more specifically when they designate a place of arbitration and, to that extent, the *lex arbitri* looks like a better indicator of party intent as to arbitral design than the body of substantive law chosen to govern the contract. However, parties select arbitral sites for many reasons having nothing to do with the rules of arbitral procedure at the situs. There is little reason to assume that the parties, in selecting a *lex arbitri*, considered every procedural prescription in the local law, however advisable it would have been for them to do so. By contrast, parties to a contract cannot reasonably suppose that, in designating specific rules of arbitral procedure, they are doing anything other than expressing their mutual preferences as to arbitral design.

Incorporation of rules of arbitral procedure in an agreement to arbitrate does not resolve all problems associated with determining arbitral design. The rules themselves may not speak with sufficient clarity to all procedural issues. More importantly, the rules of arbitral procedure adopted by the parties may point in a different direction than the *lex arbitri*, the law chosen to govern the contract, or the law chosen specifically to govern the arbitration agreement or the arbitration itself. Reconciling the diverse indications contained in the multiplicity of extrinsic sources referred to or implied in the arbitration agreement or main contract is not always a simple task.

B. *When Laws and Rules Collide*

The *Mastrobuono* case exemplifies the not uncommon situation in which an arbitration agreement refers to multiple extrinsic sources that may conflict with one another. It will be recalled that New York law, which the parties had selected as governing law, apparently precluded the award of punitive damages by arbitral tribunals,⁴⁹ whereas the NASD Code arguably authorized arbitrators to award them.⁵⁰ Clearly, the Court felt considerable tension between the two sources, and strove mightily to reconcile them.

Ultimately, the Court permitted the parties' designation of the NASD arbitral rules to carry the day. It reasoned that the only way to give effect both to the parties' choice of New York law and to their adoption of the NASD rules was to confine the designation of New York law to New York *substantive* law (which was proper) and to characterize

49. See *supra* note 14 and accompanying text.

50. See *supra* note 16 and accompanying text.

the question of the authority of arbitrators to award punitive damages as a *procedural* one (which was at the very least debatable).⁵¹ This reasoning resulted in permitting the NASD rules to control the punitive damages question, effectively putting an end to the conflict.⁵²

Once again, however, the Court showed little interest in gauging the likelihood that the parties to the arbitration agreement had contemplated (or would have contemplated if they thought about the matter) that the availability of damages in arbitration would be governed by a norm found in the NASD rules as opposed to one found in the substantive law of New York. On the one hand, the Court might have noted the greater specificity of New York law on the availability of punitive damages in arbitration, as compared to the at-best-oblique reference to the subject in the NASD rules. On the other hand, it is entirely possible that, if the parties had sought an answer to the punitive damages question, they would more likely have looked in the NASD rules governing the arbitration than in the body of substantive law to which they had subjected their contract as a whole. The likelihood was that the parties chose the NASD Code as the source of procedural rules of arbitration (including rules on available remedies) and New York law as governing the merits of any eventual dispute. In point of fact, the NASD Code said little that would have put the parties effectively on notice that punitive damages were off limits in an eventual arbitration.

The fact is that, notwithstanding their obvious relevance to the question of how the tension between New York case law and the NASD rules should be resolved, the Court in *Mastrobuono* did not make much of an inquiry into any of these considerations.⁵³ Arbitrators and courts alike need a surer basis than the one provided in *Mastrobuono* on which to sort out the “mixed signals” sent by the various extrinsic sources that the parties refer to in their agreement, directly or indirectly, as pertinent to arbitral design.

51. *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 63-64 (1995). The Court reinforced its position by positing that the choice of law clause was merely a substitute for the choice of law analysis that the forum would otherwise have had to conduct in deciding what law to apply. *Id.* The Court reasoned that, had there been no choice of law clause, but instead New York law had been indicated by the forum’s general choice of law principles, then New York law would still have been applicable, without there being in the contract anything (like the choice of law clause) that could be regarded as manifesting an intention to embrace New York law and thus to exclude the possibility of punitive damages. *Id.* In that event, absent an expression of party intention to embrace New York law, the FAA would govern and would preempt the New York courts’ prohibition on the award of punitive damages by arbitrators. *Id.* at 59.

52. To the extent that the availability of punitive damages is a matter of substantive rather than procedural law, the lower courts correctly understood it as subject to the choice of law clause.

53. *See Mastrobuono*, 514 U.S. 52.

V. CONCLUSION

The Supreme Court has emphatically stated that the parties are the masters not only of their private agreements, but also of the kind of arbitration they want, if and when disputes arise out of those agreements. In so doing, the Court rejected the notion that the Federal Arbitration Act, which recognizes arbitration in interstate and foreign commerce as a matter of genuine federal concern, imposes any particular arbitral model on the parties or the courts. It is true that the Court has recently suggested that the FAA curbs the parties' freedom to determine contractually the role and function that courts should play in determining whether an award merits confirmation or vacatur.⁵⁴ That decision, however, left party autonomy entirely intact insofar as the arbitral process itself, as opposed to judicial review of it, is concerned.

The Court's determination to rally behind party autonomy in arbitral design has not, however, been matched by a similar show of determination as to how the intended arbitral design is to be ascertained. Judicial shortcomings in this respect are several in number and important. First, the courts have been slow to circumscribe the role, if any, that generic choice of law clauses should play as an indicator of preferences in arbitral design. Fortunately, a distinction between generic and arbitration-specific choice of law clauses is coming into focus, though doubts persist over what is and what is not an arbitration-specific issue.⁵⁵ More generally, the respective spheres of a state's substantive law and its law of arbitration remain poorly delineated. Still more problematic is the unexplained neglect of the law of the place of arbitration as an extrinsic source of arbitral design in domestic FAA cases—a neglect that is all the more peculiar in light of the preponderant role of the *lex arbitri* as an indicator of party intent on such issues in international arbitration cases.

Whether courts derive indications of arbitral design from state substantive or state arbitration law, there remains the potential for conflict between such state law and the pro-arbitration bias that the FAA is said to embody as a matter of federal law. While the FAA certainly does not “occupy the field” of arbitration in the United States, it does bar the application of state law that is inimical to the federal policy. On the other hand, *Volt* plainly allows parties to adopt “arbitration-unfriendly”

54. *Hall Street Assocs., LLC v. Mattel, Inc.*, No. 06-989, 552 U.S. ___ (2008); *see also* 9 U.S.C. § 10.

55. Recall that in the *Mastrobuono* case, the Court determined that the availability of punitive damages in arbitration is an arbitration-specific issue, even though the availability of punitive damages, as such, is a matter of substantive law. *Mastrobuono*, 514 U.S. at 62.

provisions of state law as elements of their arbitration model, provided they do so clearly enough to indicate an intention to that effect. But courts should be more reluctant than they have been to interpret the mere inclusion in a contract of a choice of law clause—particularly a generic choice of law clause—as signaling a contractual embrace of every “arbitration-unfriendly” provision that the state law happens to contain, thereby unleashing *Volt*'s requirement of judicial support for them all. Once courts become more vigilant in this regard, they will be less able to avoid the difficult but essential task of determining where the line between “arbitration-neutral” and “arbitration-unfriendly” state law is to be drawn.

The trend in contemporary practice of drafting arbitration agreements toward selecting multiple extrinsic sources of arbitral design—including various bodies of law and various institutional and procedural regimes—makes the incidence of what I term “mixed signals” increasingly probable. *Volt* insisted that the FAA's core function is to ensure enforcement of the arbitration, and only the arbitration, for which the parties bargained. Fidelity to that idea requires a more principled methodology for sorting out the signals than cases such as *Mastrobuono* and its progeny have thus far yielded. That methodology should privilege those indications of party intention in matters of arbitral design that strike courts as most probative of the parties' actual or probable intentions. Otherwise, the principles for which *Volt* and *Mastrobuono* stand will simply not be realized.