DECISION BY DIVISION: THE CONTRACTARIAN STRUCTURE OF COMMERCIAL ARBITRATION

Steven Walt

In commercial arbitration, two decision makers, the arbitrator and the court, have authority over different aspects of the arbitrated dispute. The distribution of decision making, while not inevitable, is a persistent and prevalent part of the law of domestic and international commercial arbitration.

Professor Walt's article analyzes this allocation. Professor Walt criticizes contractual and regulatory accounts as unable to explain or justify it. He defends a contractarian analysis, based on the distribution of decision making as a choice of a specified group under specified conditions of choice. In doing so Professor Walt justifies each of four decision-making allocations recognized in commercial arbitration. He then uses the contractarian approach described to evaluate a sample of court decisions.

TABLE OF CONTENTS

Introduction ......................................................... 370
I. Decisional Allocations in Commercial Arbitration ......................................................... 374
   A. Competence-Competence and the Existence Issue ....................................................... 375
   B. Competence-Competence and the Scope Issue ............................................................ 379
   C. The Doctrine of Separability and the Contract Issue .................................................... 381
   D. The Review Issue ......................................................... 384
II. The Defects of Contractual and Regulatory Approaches ................................................ 385

* Professor of Law, University of Virginia School of Law. I thank Clayton Gillette, Jack Goldsmith, John Jeffries, Jody Kraus, Saul Levmore, William W. Park, George Triantis, Amy Wax, and participants in the University of Virginia Legal Theory Workshop for comments or discussion on earlier drafts of this paper. The usual disclaimer applies.

369
INTRODUCTION

Nonmandatory commercial arbitration contains a set of persistent statutory and doctrinal components. Arbitral tribunals issue awards; courts can review them on a very limited statutory basis.\(^1\) Arbitrators interpret the terms of the main agreement; courts can assess the validity of the arbitration agreement and, with some variance, its scope.\(^2\) Arbitrators decide issues the parties have agreed to submit to them; courts decide whether the issues submitted can be arbitrated.\(^3\) Statutory and case law are not uniform and resist exceptionless generalization, but the components identified describe a stable pattern. Given their relative invariance across legal systems, these components create a structure of nonmandatory commercial arbitration.

Described abstractly, the components identified differ in their content. Some concern the mandatory terms of an arbitration agreement, treating a range of issues as nonarbitrable. Others concern the content of an agreement containing an arbitration clause, distinguishing between the arbitration agreement and the main agreement of which it is often a part. Yet other components address a condition

---

1. See infra text accompanying notes 48-53.
2. See infra text accompanying notes 33-39.
3. See infra text accompanying notes 11-33.
of the enforcement of a binding resolution of a dispute, limiting the grounds upon which a court can overturn an arbitral award. Although different, the components identified share an important feature: all allocate different sorts of issues between arbitrators and courts. The elements identified do not set default or mandatory standards for contractual performance, but rather assign particular issues to particular decision makers. Once assigned, arbitrators and courts resolve these different issues. Arbitrators, for instance, test the terms of the main agreement against standards of contractual performance, while courts determine the validity and scope of the arbitration agreement.

Division of decision making is certainly not unique to commercial arbitration. Decision making is allocated among governmental bodies, as between courts and administrative agencies, different courts, and state and local governments. Division also can occur via the terms of an agreement between contracting parties. For instance, the parties’ agreement can give one party the right to set the contract price. A liquidated damages clause can be fashioned to allow the victim of a breach to specify its damages ex post. Decision making can also be divided between courts via a contractual forum selection clause. The court seized with a case determines the validity of the clause selecting a different forum. If valid, the case is dismissed, and the forum selected determines the terms of the agreement of which the clause is a part. The division of decision making in commercial arbitration is not just an artifact of private ordering achieved by contract, because it is not confined to deciding issues facing only contracting parties. It also applies in determining whether someone is a party to an arbitration agreement in the first place. This makes the division of decision making in commercial arbitration distinctive.

Why does commercial arbitration have this structure? Two familiar but different questions are being asked here. One question is normative: What legitimates allocating particular decisions to courts and others to arbitrators? The other question is positive in nature: What explains the allocation of decision making between courts and arbitrators exhibited by the structure of commercial arbitration identified above? Traditional treatments of both questions, when offered, are of two sorts—contractual or regulatory. Either facts about contracting parties’ actual or hypothetical preferences are offered or a variety of public policy concerns are introduced to explain or justify the division of decision making between arbitrators and courts.

Contractual and regulatory treatments are unconvincing. They do not fail only on their own terms. Standard tropes such as “the actual

or presumed intent of the contracting parties," or "the brute need to assume the feature being justified or explained," are either unexplained or questionable (or both). Traditional treatments also consist of an unsatisfactory blend of contract-based considerations and vague considerations of public policy favoring arbitralion. In addition, they fail to connect the justification or explanation offered to other functionally similar decision-allocating devices in contract law such as the treatment of judicial forum selection clauses.

This Article describes and defends the contractarian structure of commercial arbitration. The components of commercial arbitration are best explained and justified as the decisional allocations we prefer, given our knowledge about arbitrators, courts, and the markets in which arbitrators' services are offered and purchased. Who "we" are varies. The appropriate group to consider differs according to the issue raised. The preferences are for particular decision makers to decide particular sorts of matters, not only for resolution of those matters themselves. We may or may not be parties to a contract containing an arbitration clause. Where a party to an arbitration agreement disputes its validity or scope, the allocation of decision making looks to the preferences of contracting parties. Theirs are the relevant interests to consult.

Because commercial arbitration's structure allocates decision making by the interests of different groups, and because only sometimes are those interests those of contracting parties, it cannot be based in contract alone. This structure cannot be a set of majoritarian, penalty default, or mandatory rules, even tailored to the particular needs of the contracting parties. Nor can it be based on vague standards of public policy favoring arbitralion. In particular, commercial arbitration's structure is not based on a statutory or political bias favoring arbitralion as a mechanism of dispute resolution. Carefully considered, the Federal Arbitration Act (FAA) and decisional law do not underwrite a pro-arbitralation policy at all. Rather, the basis of commercial arbitration is contractarian. It relies on the preferences of those affected by an issue to have the issue decided by a particular decision maker, given what they know about the likely incentives and market constraints under which decision makers act.

To be sure, not all features of commercial arbitration have a contractarian source. Restrictions on subject matter arbitrability, for instance, although increasingly limited under domestic law, may

5. See infra Part II.A-B.
6. See, e.g., Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 35 (1991) (holding that an Age Discrimination in Employment Act (ADEA) employment discrimination claim is not exempt from mandatory arbitralion); Rodriguez de Quijas
resist such treatment. My claim is more modest. The main components of commercial arbitration, I contend, have a contractarian basis, not a contractual or regulatory basis. Getting clear on its contractarian basis, I also contend, has practical consequences for the judicial handling of arbitration agreements.

I need to make a terminological point at the outset. "Contractarianism" has a varied use within contract law theory, political and moral philosophy, and financial economics. Some of its uses correspond to the idea of "contractual approaches." This paper will also describe an approach which is recognizably contractarian. The approach judges decisional allocations by the interests of persons affected by them. Of course, a "person's interests" is a notoriously vague notion, and more refined discussion would distinguish interests, preferences, and individual welfare as well as their relations to each other. Since Part III.A assesses rules by their effect on what matters to an individual, without deciding foundational questions of value and assessment, a precise analysis of an individual's interests is unnecessary here. Accordingly, the account refers to interests generically, without distinguishing carefully among an individual's

v. Shearson/American Express, Inc., 490 U.S. 477, 483 (1989) (holding that an agreement to arbitrate under the Securities Act is enforceable); Shearson/American Express, Inc. v. McMahon, 482 U.S. 220, 242 (1987) (holding that an agreement to arbitrate under the Racketeer Influences and Corrupt Organizations Act (RICO) is enforceable); Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 640 (1985) (holding that an agreement to arbitrate antitrust claims under the Arbitration Act is enforceable); Scherk v. Alberto-Culver Co., 417 U.S. 506, 519-20 (1974) (holding that an agreement to arbitrate an international commercial transaction dispute is enforceable); Pritzker v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 7 F.3d 1110, 1122 (3d Cir. 1993) (holding that an agreement to arbitrate Employee Retirement Income Security Act (ERISA) claims is enforceable); Saturday Evening Post Co. v. Rumbleseat Press, Inc., 816 F.2d 1191, 1199 (7th Cir. 1987) (permitting arbitration in copyright infringement cases); Rhone-Poulenc Specialites Chimiques v. SCM Corp., 769 F.2d 1569, 1572 (Fed. Cir. 1985) (upholding an arbitration agreement that controlled resolution of patent infringement suits); Albert v. National Cash Register Co., 874 F. Supp. 1328, 1331-32 (S.D. Fla. 1994) (holding that sex, race, and national origin discrimination claims are subject to arbitration when such claims are terms of a valid contract); cf. infra Part III.C (discussing types of matters contracting parties have referred to arbitration).


8. See discussion infra Part III.A.
interests, preferences, and welfare. Most important, Part III.A's approach is called "contractarian" primarily for easy reference. Nothing significant depends on the choice of terminology. The account described is central, not the term describing it.

The Article proceeds as follows. Part I describes in brief detail the main components of commercial arbitration, emphasizing their division of decision making. Part II outlines and criticizes contractual and regulatory treatments of several of the components by focusing on the doctrine of separability. It argues that separability cannot be justified by regulatory treatments in part because the pro-arbitration policy underlying the treatments does not exist. Part III justifies the components of commercial arbitration detailed in Part I in precisely characterized contractarian terms. In doing so it distinguishes contractarian from contractual and regulatory accounts. Determining the basis of the main features of commercial arbitration is not just a matter of labeling. It has practical implications for case outcomes and evaluating case law. Part IV enumerates some of the case law implications of a contractarian approach in two areas: the application of the doctrine of separability and the interpretation of the scope of arbitration clauses. The Conclusion summarizes the argument animating the article.

I. DECISIONAL ALLOCATIONS IN COMMERCIAL ARBITRATION

Consider a dispute between two parties. One party alleges that the other party breached a contract containing an arbitration clause. The party submits the dispute to arbitration and the arbitrators issue an award. Subsequently the party seeks to have it enforced. If the other party resists arbitration initially or enforcement of the arbitral award later, it can do so on at least four grounds. First, it can deny that it was a party to a valid arbitration agreement covering the contract alleged to have been breached. Second, it can deny that the dispute is within the scope of an arbitration agreement to which it is a party. Third, the party resisting enforcement can deny that it breached the contract in dispute. Fourth, it can assert that the arbitral tribunal, in issuing the award, exceeded the scope of its authority or otherwise acted improperly. In principle, arbitration can be enjoined or the award vacated or its enforcement refused if any of the party's allegations prove to be true. 9

Each of the four grounds for refusal of enforcement presents a jurisdictional issue that a court or arbitrator could resolve. Call the first issue the “existence issue,” the second the “scope issue,” the third the “contract issue,” and the fourth the “review issue.” The predominant law of domestic and international commercial arbitration distributes decision making differently according to the issue presented. Statutory and predominant decisional law denies arbitrators the unreviewable jurisdictional competence to decide the existence issue: whether someone is a party to a valid arbitration agreement. Although confused and confusing in terminology, the denial is a rejection of the doctrine of arbitral competence-competence. Resolution of the scope issue, whether the dispute falls within the scope of a valid arbitration clause, is allocated to courts by predominant black-letter law as a consequence of the denial of competence-competence. But the judicial standard for resolution, and often the issue itself, is so deferential that the scope issue is in effect assigned to arbitrators. The contract issue, whether a breach of contract occurred, is delegated to arbitrators under the doctrine of separability. The review issue, whether the arbitral tribunal exercised its powers improperly, is allocated to the courts by statute and decisional law.

A. Competence-Competence and the Existence Issue

The doctrine of competence-competence allocates to arbitrators the power to determine their own jurisdiction. Although not frequently distinguished, the doctrine comes in strong and weak forms. The strong form of competence-competence gives to arbitrators the unreviewable jurisdiction to determine their own jurisdiction. Competence-competence, according to the weak form, allows arbitrators to exercise jurisdiction over a dispute without requiring prior jurisdic-

of contract, the third ground, is not a recognized basis for vacating or refusing to enforce an arbitration award. The first, second, and fourth grounds can also be raised prior to the issuance of an arbitral award, to resist arbitration.

10. See discussion infra Part I.A-B.


entional determination by a court. Judicial determination of arbitral jurisdiction is either always permitted or is prohibited at some point before or after arbitration has begun. If X alleges that Y is a party to a valid arbitration agreement to be decided by arbitrator A, the strong form of competence-competence allows A to determine whether Y is a party to such an agreement. A’s decision is not reviewable by a court. The weak form of competence-competence also allows A to make the same determination, but A’s decision may be reviewable by a court only at particular points over the course of the arbitration.

Judicial review might be prohibited before, during, or after completion of arbitration. Institutional arbitration rules typically allow arbitrators to initially determine their own jurisdiction. Since those rules are silent about judicial review, typical institutional arbitration rules are silent about the doctrine of competence-competence. Legal regimes, however, reject it. They either deny the doctrine entirely or adopt the weak form of competence-competence. In either case, legal regimes allocate the existence issue ultimately to courts.

Domestic law, while not using the label, adopts a weak form of competence-competence. Section 3 of the Federal Arbitration Act expressly requires a federal court to stay litigation upon a party’s request when “satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement” (i.e., under a written agreement calling for arbitration). The requirement necessarily allocates the issue of the arbitrator’s jurisdiction to federal courts to resolve. No restriction is placed on when the court can review an arbitrator’s assertion of jurisdiction over a dispute. Section

13. See id. at 180-81.
15. See SAMUEL, supra note 11, at 181.
16. See id.
17. See id. at 180-81.
18. See, e.g., UNCITRAL ARBITRATION RULES, supra note 14, art. 21(1); UNCITRAL MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION, supra note 14, art. 16(1); AMERICAN ARBITRATION ASS’N, supra note 14, art. 15(1) (arbitral tribunal has power to rule on its own jurisdiction); INTERNATIONAL CHAMBER OF COMMERCE, supra note 14, art. 8(3) (arbitrator has power to rule on her own jurisdiction if ICC Court of Arbitration finds prima facie existence of arbitration agreement).
4 of the Federal Arbitration Act requires a federal court to compel arbitration upon a party's request when "satisfied that the making of the agreement for arbitration . . . is not in issue."\(^{20}\) The requirement presupposes that the court determine the arbitrator's jurisdiction arising from an arbitration agreement.\(^{21}\) Judicial determination of arbitral jurisdiction therefore is permitted at any point before or after arbitration has been requested by a party.

Decisional law makes the same allocation in cases not governed by the Federal Arbitration Act.\(^{22}\) State arbitration acts modeled on the Uniform Arbitration Act also make the same allocation to state courts.\(^{23}\) Some recent Supreme Court dicta do not alter domestic law's rejection of the doctrine of competence-competence. In *First Options of Chicago, Inc. v. Kaplan*\(^{24}\) the Court noted in passing that parties by contract could opt out of judicial review of an arbitrator's exercise of jurisdiction.\(^{25}\) They could do so if done in "clear and unmistakable" language.\(^{26}\) The dictum does not reflect an acceptance of competence-competence even in limited circumstances. Allowing parties to contract out of judicial review of arbitrability still requires a court to determine whether the parties have opted out in the first place. *First Options* only sets an enhanced evidentiary standard that parties doing so have to meet "clear and unmistakable evidence." A court still has to find both that the parties entered into an arbitration agreement and that the standard is satisfied in any particular

\(^{20}\) *Id.* § 4.

\(^{21}\) See, e.g., *Three Valleys Mun. Water Dist. v. E.F. Hutton & Co.*, 925 F.2d 1136, 1140-41 (9th Cir. 1991) ("[B]ecause an 'arbitrator's jurisdiction is rooted in the agreement of the parties,' a party who contests the making of a contract containing an arbitration provision cannot be compelled to arbitrate the threshold issue of the existence of an agreement to arbitrate.") (citations omitted).


\(^{25}\) See *id.* at 944 ("Courts should not assume that the parties agreed to arbitrate arbitrability unless there is 'clear[r] and unmistakable[]' evidence that they did so.").

\(^{26}\) *See id.*
case. The Supreme Court therefore is not endorsing a strong form of competence-competence.

Other legal regimes also at most adopt weak forms of competence-competence. French law, for example, allows arbitrators to determine their own jurisdiction. At the same time it allows courts to pass on arbitral jurisdiction prior to arbitration only if the arbitration agreement is manifestly void. In other cases a court can determine the matter at the time the arbitral award is to be enforced. English law also allows arbitrators to determine their own jurisdiction. Parties may by agreement appeal the decision to a court during the arbitration or, in any event, when enforcement of the award is sought. Courts retain the power to refuse to stay litigation in a nonarbitral forum if it considers the arbitration agreement void or otherwise ineffective. Both French and English law therefore restrict, while not eliminating, judicial determination of the existence issue over the course of arbitration. Other legal regimes have similar rules. Limiting when courts can decide the existence issue can have allocative effects on the rate of arbitration and settlement of


28. See NOUVEAU CODE DE PROCÉDURE CIVILE [N.C.P.C.] art. 1466 (Fr.).

29. See id. art. 1458.


33. See id. § 9(4), in 36 I.L.M. 165, 168 (1997) (“[T]he court shall grant a stay unless satisfied that the arbitration agreement is null and void, inoperative, or incapable of being performed.”).

34. For example, some state arbitration laws also allow arbitral determination of jurisdiction. Cf. CAL. CIV. PROC. CODE § 1297.161 (West Supp. 1998) (stating that “[t]he arbitral tribunal may rule on its own jurisdiction”); FLA. STAT. ANN. § 684.06(2) (West 1996) (“The arbitral tribunal shall have the power to rule on all challenges to its jurisdiction.”); see also SAMUEL, supra note 11, at 180-81 (comparing English and continental law on competence-competence); Park, supra note 27, at 150-51 (comparing German and Swiss law on competence-competence); Peter Schlosser, The Competence of Arbitrators and of Courts, 8 ARB. INT’L 189, 190-204 (1992) (comparing German and French law on competence-competence).
disputes. But weak forms of competence-competence still allow courts to decide the existence issue at some point. Hence, both legal regimes that deny all forms of competence-competence and those that adopt a weak form of competence-competence allocate the existence issue to courts. They differ only as to when the existence issue is presented to the courts.

B. Competence-Competence and the Scope Issue

Denying the doctrine of competence-competence in allocating the existence issue does not require denying it in allocating the scope issue. The decision as to whether \( X \) is a party to an arbitration agreement can be allocated to courts. Whether the arbitration agreement covers a particular matter—the issue of scope—is a decision that still can be delegated to arbitrators. The two allocations are not inconsistent. In fact, despite some black-letter law to the contrary, domestic law in effect does this.

Judicial practice differs significantly from some judicial gloss on the allocation of the scope issue, but the judicial gloss is deceptive. Courts sometimes state, with some statutory support, that they are to pass on the scope of an arbitration agreement as well as on its existence.\(^{35}\) Most courts, however, hold that the scope of the agreement is to be determined by arbitrators.\(^{36}\) Even courts that delegate the scope issue to the courts in effect allocate the decision to arbitrators by allowing them to decide the matter as long as there is “clear

---


36. See, e.g., Republic of Nicaragua v. Standard Fruit Co., 937 F.2d 469, 478 (9th Cir. 1991) (holding that the court’s “role is strictly limited to determining arbitrability and enforcing agreements to arbitrate”); Teledyne, Inc. v. Kone Corp., 892 F.2d 1404, 1410 (7th Cir. 1990) (requiring “that cases be submitted to arbitration unless there is a challenge to the arbitration provision” itself); Appollo Computer, Inc. v. Berg, 886 F.2d 469, 473-74 (1st Cir. 1989) (finding that the parties “clearly and unmistakably” contracted to send all disputes to arbitration); Conticommodity Servs. Inc. v. Philipp & Lion, 613 F.2d 1222, 1225 (2d Cir. 1980) (concluding that unless the agreement to arbitrate itself or its enforcement is in question, “the court must compel arbitration”); RPJ Energy Fund Management, Inc. v. Collins, 552 F. Supp. 946, 950 (D. Minn. 1982) (explaining that an “arbitrator may be called upon to determine the scope of the arbitration clause”); BORN, supra note 11, at 397.
and unmistakable evidence” that the parties so intended.37 The question then becomes the sort of evidence needed to satisfy the heightened standard of proof seemingly demanded. Here, rules of contract construction, a presumption of arbitrability, inferences drawn from the parties’ course of dealing, or pro-arbitration policy operate to determine party intent. As applied, these devices can provide the needed “clear and unmistakable” evidence. Rules of construction, presumptions of arbitrability and the like therefore work to allocate the scope issue to arbitrators.38 Initially assigning the scope issue to courts while allowing it to shift to arbitrators, conjoined with liberal evidence as to when the scope issue is shifted, amounts to assigning the matter ultimately to arbitrators. In practice, in the

37. Compare Smith Barney Shearson, Inc. v. Boone, 47 F.3d 750, 754 (5th Cir. 1995) (holding “that the timeliness issues raised in this case are issues of procedural arbitrability and must be decided by the arbitrator”), and FSC Sec. Corp. v. Freel, 14 F.3d 1310, 1312-13 (8th Cir. 1994) (noting that the National Association of Securities Dealers (NASD) Rule 15 “clearly and unmistakably” leaves to arbitrators the question of whether the claim is time barred), with Cogswell v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 78 F.3d 474, 481 (10th Cir. 1996) (holding that the “courts, not the arbitrators” decide the time-bar issue under NASD Rule 15), Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Cohen, 62 F.3d 381, 383 (11th Cir. 1995) (concluding “that the court decides whether claims are timely” under NASD Rule 15), Dean Witter Reynolds, Inc. v. M.C. McCoy, 995 F.2d 649, 651 (6th Cir. 1993) (holding that the court decides what issues the parties intended to arbitrate), aff’d, 70 F.3d 1271 (6th Cir. 1995), and Edward D. Jones & Co. v. Sorrells, 957 F.2d 509, 514 (7th Cir. 1992) (holding that NASD Rule 15 does not “clearly and unmistakably” assign time bar disputes to arbitrators).

38. See, e.g., Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52, 57 (1995) (explaining that federal pro-arbitration policy underwrites resolving ambiguities in an arbitration clause in favor of arbitration); United Paperworkers Intl Union v. Misco, Inc., 484 U.S. 29, 38 (1987) (stating that in labor arbitration “as long as the arbitrator is even arguably construing or applying the contract and acting within the scope of his authority,” the arbitrator’s decision will be upheld); Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24-25 (1983) (“The Arbitration Act establishes that . . . any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration . . . .”); Elahi, 87 F.3d at 599 (“[T]he signing of a valid agreement to arbitrate the merits of the subject matter in dispute presumptively pushes the parties across the ‘arbitrability’ threshold . . . . ”); Flexible Mfg. Sys., Ltd. v. Super Prods. Corp., 86 F.3d 96, 99 (7th Cir. 1996) (stating that where the issue involves the scope of the agreement, “the rule requiring any doubts concerning the scope of arbitration to be resolved in favor of arbitration comes into play”); Schulze & Burch Biscuit Co. v. Tree Top, Inc., 831 F.2d 709, 715-16 (7th Cir. 1987) (finding that contractual clause stating that disputes should be arbitrated “in the usual manner” clearly forces the parties to arbitrate any disputes); Genesco, Inc. v. T. Kakiuchi & Co., 815 F.2d 840, 847 (2d Cir. 1987) (explaining that federal pro-arbitration policy results in a presumption that arbitrators acted within their authority); Howard Elec. & Mechanical Co. v. Frank Briscoe Co., 754 F.2d 847, 850 (9th Cir. 1985) (quoting Moses H. Cone Mem’l Hosp., 460 U.S. at 24-25); infra text accompanying note 136.
range of cases, the scope issue therefore is decided by arbitrators.\textsuperscript{39} Hence, the predominant result is that courts allocate the scope issue to arbitrators, if not initially, then ultimately. Other legal regimes make the same allocation.

C. The Doctrine of Separability and the Contract Issue

The doctrine of separability provides that an arbitration agreement is separate from the main contract of which it is a part, even if the arbitration clause is included in or related to the main contract.\textsuperscript{40} Separability divides the agreement into two distinct bargains: the arbitration agreement and the rest of the agreement. Absent contrary intent, the doctrine treats the arbitration and main agreements as if each were entered into independently of the other.\textsuperscript{41} Domestic federal and state law, other legal regimes, and insti-

\textsuperscript{39} \textit{AT&T Technologies, Inc. v. Communications Workers of America}, 475 U.S. 643 (1986), is a well-known labor arbitration case illustrating this point. At issue was whether a court or an arbitrator is to determine whether “layoffs” were an arbitrable subject matter under a collective bargaining agreement containing an arbitration clause. \textit{See id.} at 644. The question therefore concerned the allocation of the scope issue. The Court held that the issue was one for the court. \textit{See id.} at 651. At the same time it reaffirmed its earlier holding that an arbitration clause covers a matter unless it can be said “with positive assurance” otherwise. \textit{Id.} at 650 (quoting \textit{Warrior & Gulf}, 363 U.S. at 582-83). The second holding creates a strong presumption of arbitrability, decisive in most cases, which can extend to the choice of who is to interpret the arbitration clause. \textit{Cf. id.} at 654-55 (Brennan, J., concurring). Hence, when conjoined, the two holdings effectively allocate the scope issue to the arbitrator. The arbitrator decides whether a dispute falls within the scope of an arbitration agreement.


\textsuperscript{41} \textit{See Nussbaum, supra} note 40, at 610-11.
tutional rules of arbitration incorporate a doctrine of separability. The doctrine is pervasive.

The consequences of separability are significant. They include contractual performance, arbitral jurisdiction, and defects in contract formation. Performance of the main agreement does not discharge the duty to arbitrate. An arbitration clause survives even if the agreement of which it is a part is found to be nonexistent, invalid, or voidable. Moreover, the arbitration clause is ineffective only if nonexistent, invalid, or voided by the party urging nonenforcement. Relatedly, the arbitrators selected under the contract continue to retain jurisdiction over the contract even if it is found to be nonexistent, invalid, or voidable. More generally, formational challenges to the main agreement do not alone challenge the validity or enforceability of an arbitration clause in it. Each of these consequences is realized only if the arbitration agreement is considered separable from the main agreement.

42. See Arbitration Act, 1996, ch. 23, § 7 (Eng.), in 36 I.L.M. 165, 168 (1997). Unless otherwise agreed by the parties, an arbitration agreement which forms or was intended to form part of another agreement . . . shall not be regarded as invalid, non-existent or ineffective because that other agreement is invalid, or did not come into existence or has become ineffective, and it shall for that purpose be treated as a distinct agreement. *Id.; see also* Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395, 401-03 (1967) (holding that separability is a matter of substantive federal law under the Federal Arbitration Act in diversity cases); Flower World of Am., Inc. v. Wenzel, 594 P.2d 1015, 1018-19 (Ariz. Ct. App. 1979); Nelley v. Mayor of Baltimore City, 166 A.2d 234, 238-40 (Md. 1960); Quirk v. Data Terminal Sys., Inc., 400 N.E.2d 858, 860-61 (Mass. 1980); Jackson Mills, Inc. v. BT Capital Corp., 440 S.E.2d 877, 879 (S.C. 1994) (recognizing separability under state law); UNCITRAL MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION, supra note 14, art. 16; United Nations Convention on Contracts for the International Sale of Goods, art. 81(1), U.N. Doc. A/Conf.97/18 (1980), reprinted in 19 I.L.M. 668, 690 (1980); DOMKE, supra note 40, at 89-90; SAMUEL, supra note 11, at 155, 162-64 (arguing that separability is accepted in most legal systems of Western Europe); Alejandro M. Garro, *Enforcement of Arbitration Agreements and Jurisdiction of Arbitral Tribunals in Latin America*, 1 J. INT'L ARB. 293, 306-07 (1984) (demonstrating that some Latin American legal systems recognize separability).


44. See, e.g., Prima Paint Corp., 388 U.S. at 400 ("[A] claim of fraud in the inducement of the contract generally—as opposed to the arbitration clause itself—is for the arbitrators and not for the courts . . .").

45. Another consequence bears on choice of law. The law applicable to the arbitration clause can be different from that applicable to the main agreement. Since choice of law doctrine based on dépêçage can consider the arbitration clause and the main agreement as presenting different issues calling for different applicable law, matters concerning applicable law do not follow from separability. Separ-
To be sure, the doctrine of separability alone does not determine which decision makers pass on the arbitration clause and the main contract. Separability itself only distinguishes into two components what are usually elements of a single contract. Hence the choice of decision maker and the contractual elements allocated to her are independent matters. Although no legal regime has done so, in principal it is possible for the same decision maker to vet both the arbitration clause and main agreements without treating the two as inseparable. Conversely, it is possible for different decision makers to pass on the arbitration clause and main agreements while considering the two as separable. Therefore the doctrine of separability does not by itself allocate to arbitrators the contract issue—whether X breached an obligation under a validly concluded and otherwise enforceable agreement. However, the doctrine of separability, combined with the denial of the strong form of competence-competence, does allow arbitrators to decide on the contract issue. The denial of the strong form of competence-competence requires courts to pass on the existence and validity of the arbitration clause. Separability distinguishes between the validity of the arbitration clause and the main

46. The independence of separability and the choice of the appropriate decision maker sometimes is wrongly ignored in discussions of the relation between the doctrines of separability and competence-competence. See, e.g., ALAN REDFERN & MARTIN HUNTER, LAW AND PRACTICE OF INTERNATIONAL COMMERCIAL ARBITRATION 177 (2d ed. 1991) ("There is a direct connection between the autonomy of the arbitration clause and the power (or competence) of an arbitral tribunal to decide upon its own jurisdiction (or competence."); Rosen, supra note 11, at 609 (explaining that the doctrine of competence-competence is a "corollary" of separability). For instances in which institutional arbitration rules and case law conflate separability and competence-competence, see UNCITRAL MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION, supra note 14, article 16(1), which states: "The arbitral tribunal may rule on its own jurisdiction. . . . For that purpose, an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract." For instances of the confusion of the two notions in recent case law, see BERGER v. CANTOR FITZGERALD SECURITIES, 942 F. Supp. 963, 965 (S.D.N.Y. 1996), and MAYE v. SMITH BARNEY, INC., 897 F. Supp. 100, 106 n.3 (S.D.N.Y. 1995).

47. An example of the possibility of not involving arbitration is the doctrine of divisibility under general contract law. Divisibility allows the court to enforce part of an agreement when other parts of the agreement are unenforceable, if the unenforceable parts are not considered "essential parts" of the agreement. See, e.g., Technical Aid Corp. v. Allen, 591 A.2d 262, 271-72 (N.H. 1991); RESTATEMENT (SECOND) OF CONTRACTS § 184(1) (1981). By allowing a court to enforce only part of an agreement, the doctrine allows the same decision maker to treat one agreement as if it consisted of two separate agreements.
agreement. Given the distinction and a desire to honor arbitration clauses, the validity and terms of the main agreement are left to arbitrators. Domestic and international law exhibit this allocation; to different extents, the existence issue is delegated to courts, the contract issue to arbitrators.

D. The Review Issue

Judicial review of arbitral awards is extremely limited. In general, the grounds for annulling an arbitral award or refusing its enforcement or recognition are restricted to procedural irregularities or an excess of arbitral authority. Under the Federal Arbitration Act, for instance, fraud, palpable bias, or misconduct by an arbitrator during the arbitration are bases for vacating an award. Excess of arbitral authority includes the nonexistence or unenforceability of an arbitration clause. Misapplication of law, or misinterpretation of the contract, without more, are not grounds for vacatur. Nor are bases that fall outside the few judicial enlargements of enumerated statutory grounds of review. Other legal regimes restrict judicial review of an arbitral award in the same way. There is some variation here in the grounds of review. English law allows a court to review the award for errors of law unless the parties’ arbitration agreement


49. See id. § 10(a)(4) (proclaiming vacatur on grounds that the award is in excess of arbitral authority); accord Comprehensive Accounting Corp. v. Rudell, 760 F.2d 138, 140 (7th Cir. 1985); cf. Wiepking v. Prudential-Bache Sec., Inc., 940 F.2d 996, 998-99 (6th Cir. 1991) (allowing review under § 10(a)(4) to determine existence of arbitration clause).


provides otherwise. French and Swiss law allow vacation of an arbitral award when it violates public policy. Variation in the grounds of review does not affect the point; judicial review of arbitral awards remains limited in scope.

The consequence for the review issue is obvious. Limited judicial review of an arbitral award allocates final decision making concerning the contract between courts and arbitrators. Courts decide only issues presented by the award which bear roughly on procedural irregularities, arbitral misconduct, or excess authority. Judicial review to determine an excess of arbitral authority includes the presence and enforceability of the arbitration clause—the existence issue. Arbitrators determine the parties’ rights and obligations under the main contract—the contract issue. Absent procedural irregularities and misconduct, their determinations are final, even if mistaken. True, maintaining the division of decision making between courts and arbitrators sometimes can be difficult. For instance, it can be hard to determine whether the arbitrator exceeded her authority (a judicial issue) without interpreting the terms of the parties’ main agreement (an arbitral issue). In this way judicial review of arbitral awards sometimes requires a court to independently resolve the contract issue too. Again, reviewing an award to determine arbitral authority (a judicial issue) requires a court to resolve the scope issue (in practice an arbitral issue). Still, in most cases the issues decided are clearly allocated to different decision makers.

II. THE DEFECTS OF CONTRACTUAL AND REGULATORY APPROACHES

The structure of commercial arbitration allocates the existence and review issues to courts, and the scope and contract issues to arbitrators. The question is why commercial arbitration exhibits this structure. Its allocation of decision making is not inevitable. The existence issue, for example, could be delegated to arbitrators instead of the courts. There is nothing incoherent about such a possibility. Municipalities are not given the authority to determine whether a matter is of purely local concern; the state is given that authority. Courts, on the other hand, are given the jurisdiction to rule on their own jurisdiction, even if their determination is reversible upon appeal. Courts

do so by virtue of a legal norm that allocates to them the decision over their own jurisdiction. There is no conceptual impossibility in a legal norm allocating the same capacity to arbitrators. Again, a legal norm is possible that gives courts the authority to decide the sort of disputes covered by an arbitration clause. As some case law demonstrates, the scope issue could be allocated to courts instead of arbitrators. Since the distribution of issues between courts and arbitrators is a contingent feature of commercial arbitration, it has to be explained and justified.

Traditional approaches to the structure of commercial arbitration are either contractual or regulatory in nature. Under a contractual approach, the allocation of existence, scope, contract, and review issues is based upon the contractual intent of the parties to an arbitration agreement. Slightly extended, the above approach treats the allocation as a set of default or mandatory rules based on the majoritarian preferences of contracting parties. A regulatory approach looks to a set of concerns independent of contract which justifies a distribution of adjudicative power between courts and arbitrators. A prominent animating concern is an assumed federal policy, evident in case law and commentary, favoring arbitration. In practice, traditional accounts of commercial arbitration often are a hybrid of the two. In this Part of the Article, I argue that contractual approaches do not explain or justify the allocation of all issues exhibited by commercial arbitration. I also argue that regulatory approaches fail, in part because there is no pro-arbitration policy animating federal law. I will later describe and defend a suitably specified contractarian account of commercial arbitration.

A. Contractual Approaches

A contractual approach is based either on the arbitration agreement or the actual or hypothetical preferences of the parties to it. The approach can be extended to take into account the preferences of most parties to arbitration agreements. So considered, the decision of decision making resolved by commercial arbitration is treated as a set of default or mandatory rules allocating decisions. In either case the allocation is based on the actual or hypothetical preferences of all or a majority of contracting parties to an arbitration agreement. The

55. See cases cited supra note 35.
56. See infra Part II.A.
57. See infra Part II.B.
58. See infra Part III.
approach is attractive because contract is the source of nonmandatory arbitration: the contractual choice of parties to have a range of disputes submitted to a third party of their selection for binding resolution. Parties may contract for arbitration rather than litigation because of reductions in delay and expense, arbitral expertise in adjudication, neutrality, and legal uncertainty. Accordingly, a respect for private ordering maximizes welfare by reducing total contracting costs to parties selecting an arbitration clause. Case reporters are full of opinions that, in giving effect to the terms of an arbitration agreement, closely track the contractual approach.

However, contractual approaches cannot explain the structure of commercial arbitration. Two features remain unaccounted for: the mix of mandatory and default rules allocating decision making, and particular allocations of decision making. Consider these features in turn. The allocations of scope and contract issues to arbitrators are in the nature of default rules. Contracting parties can alter the former rule by providing that courts are to determine the scope of the arbitration clause. The latter rule can be altered by a contractual provision stating that the arbitration clause and the rest of the contract are inseparable. Opting out obviously also can occur by not selecting arbitration in the first place. The allocation of the existence and review issues to courts are mandatory decisional rules, as are the increasingly limited sorts of disputes that cannot be decided by arbitration. Parties to an arbitration agreement cannot by contract


61. Cf. Arbitration Act, 1996, ch. 23, § 7 (Eng.) (explaining that unless parties otherwise agree, an arbitration agreement shall not be considered invalid because the main agreement is invalid); First Options, 514 U.S. at 942-45; Prima Paint v. Flood & Conklin Mfg. Co., 388 U.S. 395, 402 (1967) ("[E]xcept where the parties otherwise intend—arbitration clauses as a matter of federal law are 'separable' from the contracts in which they are embedded.").

62. See DOMKE, supra note 40, at 155-56.
allocate these decisions to an arbitrator. Contractual approaches cannot plausibly justify this pattern of mandatory decisional allocations.

To understand this point, recognize that mandatory rules can be justified in four ways. First, a default rule may impose negative externalities on other contracting parties. For instance, if X and Y can alter an allocation of decision making, a third party has to determine whether they have in fact done so. The third party’s determination may increase contracting party A and B’s uncertainty that they have retained the default allocation of decision making to govern their contract. A and B might have to incur contracting costs to reduce this uncertainty. Second, a default rule obviously may impose negative externalities on noncontracting parties. Third, the justification may be paternalistic: allowing contracting parties X and Y to alter an allocation of decision making diminishes their welfare, whatever X and Ys’ preferences and information may be. Fourth, “self-paternalism” may justify a mandatory rule: allowing X and Y to alter an allocation of decision making at a point after they have contracted might diminish their welfare, as judged by X and Y’s preferences at the time they contracted. Strictly, the first justification does not appeal only to the interests of the parties to an arbitration agreement, and the second appeals entirely to the interests of noncontracting parties. Since both justifications in different ways consider the costs contracting imposes on other parties, contractual approaches cannot invoke them. Given the different sorts of contracts that contain arbitration clauses, paternalistic and “self-paternalistic” justifications do not account for the range of mandatory terms. It is therefore an implausible article of faith that contractual approaches can explain or justify the pattern of commercial arbitration’s mandatory rules.

Consider next a particular decisional allocation within commercial arbitration, for example, the distribution of the existence issue to courts and the contracts issue to arbitrators. Contractual approaches to the allocation are weak because they rely on restrictive assump-

---

tions. The following account illustrates this phenomenon. Parties to
an arbitration agreement select an arbitration clause presumably
because it reduces net contracting costs compared to litigation. An
element of cost is the risk of adjudicatory error accompanying arbi-
tration. Assume that arbitration increases the risk of adjudicatory
error above that of litigation. The risk of arbitral error can be re-
duced in two ways. The parties may make ex ante investments to
avoid arbitral error, such as taking greater care in selecting an arbit-
trator or increasing their care in performance of the contract. The
parties may also allocate different decisions to different decision
makers. Assuming that the costs associated with the allocation are
less than the ex ante investment, contracting parties will prefer the
allocational device to reduce the risk of arbitral error.

Allocating the existence and contract issues to different decision
makers can reduce the risk of arbitral error. This is primarily be-
because the allocation makes an arbitrator's determination of liability
binding only if two findings are also made: that a valid arbitration
agreement exists, and that a valid agreement exists. Since it is possi-
ble to find that a valid arbitration agreement exists but that a valid
agreement does not, and vice versa, the arbitrator's determination of
liability is binding only when both the agreement and the main con-
tract are valid. Error can occur in making both findings. Where both
findings are probabilistically independent of each other, expected risk
is lower than when the findings are correlated. By allocating the
existence issue to a court and the contract issue to the arbitrator,
probabilistic independence of outcomes is achieved. Since the court
finds whether a valid arbitration agreement exists and the arbitrator
finds whether a valid agreement exists, the errors in findings are
likely to be uncorrelated. The expected risk of error to a party in
determining liability, a cost, therefore is reduced. Hence, parties can
prefer the allocation, especially when the cost of allocating decisions
is less than precaution costs.

To see this, let \( p \) describe the probability of whether a valid arbi-
tration agreement is made, and \( q \) the probability of whether a valid
agreement is made. Since the arbitrator's finding of liability depends
on a finding that both the arbitration clause and the rest of the
agreement are valid, a party's expected liability depends on the val-
ues of \( p \) and \( q \). Where \( p \) and \( q \) are probabilistically independent
of each other, the probability that both findings will be made is a pro-
duct of \( p \) and \( q \). (If liability only depended on either one of the find-
ings being made, the probability of liability would be the sum of the
two probabilities.) For values above zero, the product of \( p \) and \( q \) is
smaller than the sum. Hence, given a party's loss upon a finding of
liability, the party's expected liability under the arbitral doctrine
assures that $p$ and $q$ are probabilistically independent. The denial of the strong form of the doctrine of competence-competence allocates the existence issue to courts. The doctrine of separability divides the agreement into an arbitration agreement and the main agreement. The denial and doctrine combine to allocate the contract issue to arbitrators.\textsuperscript{64} Since different decision makers pass on the validity of different agreements, the probability that one decision maker finds the arbitration agreement invalid is independent of the probability that the main agreement will be deemed invalid. Absent any information about the decision makers or the process of decision, the outcomes of the decision are uncorrelated. In this way the expected exposure to a finding of liability by an arbitrator is reduced.

There is a parallel here with the independence principle in letter of credit law. It too assures probabilistic independence where otherwise there might be correlation. By doing so, the independence principle serves a cost-reducing function, making a letter of credit a more attractive financial instrument. According to the principle, the issuer's obligation of payment runs directly to the beneficiary and is unaffected by performance of the underlying contract between the beneficiary and the customer.\textsuperscript{65} There are two separate obligations corresponding to two distinct contracts. Therefore the beneficiary will not receive payment only if both the issuer and the customer default on their payment obligations to it. Since the issuer can be (and usually is) a distinct entity from the customer with independent obligations running to the beneficiary, the issuer's default risk is independent of the default risk presented by the customer. The risk that the beneficiary will not receive payment therefore is the product of the issuer and the customer's default risks. Accordingly, this risk of non-payment is lower than the default risk presented by the customer. A reduction in the beneficiary's risk of nonpayment reduces the expected cost of a letter of credit to the beneficiary. The instrument is thereby made a more attractive financial device for it than alternative devices (e.g., a guarantee).

The parallel with commercial arbitration obviously is not perfect. The independence principle operates to reduce a risk of nonpayment. In the case of commercial arbitration, a risk of a binding determination of liability is allocated between courts and arbitrators. But in

\textsuperscript{64} See supra text accompanying notes 46-47.

\textsuperscript{65} The independence principle is subject to a fraud exception, the scope of which is debatable and debated within letter of credit law. Since the exception affects only the size, not the existence, of the cost-reducing consequence of the independence principle, it is unimportant here.
both instances cost-reduction is achieved by creating probabilistic independence between events.

The above contractual account of the division of existence and contract issues is weak. It relies on two restrictive assumptions: that arbitration has a higher rate of adjudicatory error than litigation, and that the cost of ex ante investment is higher than the costs of allocating the issues between courts and arbitrators. If either assumption is unsound, parties to an arbitration clause will not prefer an allocational device for reducing the risk of arbitral error. The increased informality of arbitral proceedings might increase the risk of arbitral error. Arbitral expertise in the subject matter of the dispute, on the other hand, diminishes that risk as compared to a counterpart judicial proceeding.66 The net effect of these two factors on arbitral accuracy is indeterminate, hence, arbitral error in adjudication cannot be supposed to be systematically higher than its judicial counterpart. The assumption that the decisional allocation has a cost-advantage over ex ante investment in risk-reduction strategies is similarly questionable. A distribution of issues among a court and arbitrator often requires the parties to prove some of the same facts to both tribunals ex post. It also requires expenditures on legal advice appropriate to each forum. These ex post costs can exceed the cost of ex ante investments in arbitral risk-reduction strategies. The point here is not the unexciting truth that both assumptions rely on empirical matters. It is that they are unlikely to be satisfied in sufficiently many circumstances to justify the prevalence of commercial arbitration’s allocation of existence and contract issues. Therefore, the contractual approach is weak.

B. Regulatory Approaches

A regulatory approach is based on a set of concerns partially or entirely independent of the preferences of the contracting parties. Commercial arbitration’s allocation of issues among courts and arbi-

trators then is explained or justified by these concerns. The concerns identified can vary. They may encompass a desire to reduce the dockets of the courts, a concern that arbitrators are likely to be systematically biased in a way not exhibited by courts, a stated public interest in having social norms articulated in a public forum, or a brute public policy favoring arbitration. Although different in kind, these concerns all allocate decision making without exclusively taking into account the interests of contracting parties. Regulatory accounts at a minimum control the contracting practices of parties without regard to their welfare. Of course, by effecting the cost of arbitration, regulation affects the incentives of parties to enter into arbitration agreements. But the effect on cost is not the explanation or justification of commercial arbitration’s structure, according to regulatory approaches.

A prominent instance of a regulatory approach is the appeal to a supposed public policy favoring arbitration. Judicial opinions are full of dicta to the effect that the Federal Arbitration Act underwrites a general pro-arbitration policy. If true, a preference for arbitration might explain or justify the distribution of decision making exhibited by commercial arbitration. I argue that this approach fails because it rests on the mistaken belief that there is a general federal policy favoring arbitration. There are specific legislative biases in favor of arbitration, such as, for instance, in labor arbitration under the National Labor Management Act. But no sufficiently general federal preference for arbitration exists under the Federal Arbitration Act.

68. Cf. Robert Hale, Law Making By Unofficial Minorities, 20 Colum. L. Rev. 451, 454-55 (1920) (stating that the rich and powerful of society usually have the upper hand in arbitration hearings because they can dictate certain terms of the hearing); Heinrich Kronstein, Business Arbitration—Instrument of Private Government, 54 Yale L.J. 36, 53 (1944) (commenting on the increasing power of arbitration tribunals to be independent of municipal law).
70. See infra Part II.B.2-3.
None, therefore, can justify commercial arbitration’s structure. Judicial pro-arbitration dicta at most account for only part of this arbitration preference.

1. The Range of Pro-Arbitration Dicta

Pro-arbitration dicta include a range of attitudes toward agreements to arbitrate, all of which can be said to favor arbitration. Whether federal law exhibits a general policy favoring arbitration obviously depends on what is meant by favoring arbitration as a device for dispute resolution. Simple contract enforcement is the weakest relevant sense. There is a Pickwickian sense in which enforcing an agreement to arbitrate favors arbitration. Such a practice specifically enforces a right to arbitrate rather than not enforcing that right. Section 2 of the Federal Arbitration Act, for instance, provides that “[a] written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration . . . shall be valid, irrevocable, and enforceable.” The Act “favors” arbitration in the sense that a contractually created entitlement is enforced. Judged by a baseline of nonenforcement, the Act “favors” arbitration. However, it does not favor arbitration in the sense that it indicates an extra-contractual (Congressional) preference for arbitration as a means of dispute resolution. When the Supreme Court and lower federal courts find a pro-arbitration policy based on section 2 of the Act, the policy endorsed is one of contract

73. Cf. Sverdrup Corp. v. WHC Constructors, Inc., 989 F.2d 148, 152-55 (4th Cir. 1993) (stating that although several remedies exist outside the Federal Arbitration Act’s power to enforce rulings, arbitration is still a highly favored form for dispute resolution); Kulukundis Shipping Co., S/A v. Amtorg Trading Corp., 126 F.2d 978, 985 (2d Cir. 1942); H.R. REP. No. 68-96, at 1-2 (1924). For arguments that pre-Federal Arbitration Act law did not reflect a baseline of unqualified or predominant nonenforcement, see MacNeil, supra note 67, at 15-24, and Bruce L. Benson, An Exploration of the Impact of Modern Arbitration Statutes on the Development of Arbitration in the United States, 11 J.L. ECON. & ORG. 479, 485-90 (1995). Benson cites evidence that arbitration and the trend to accept arbitration rulings was established long before arbitration statutes were passed. See Benson, supra.
enforcement. In this attenuated sense of the term, there is a pro-enforcement policy toward all contractual entitlements.

Other sorts of attitudes toward arbitration are more serious. A second sense of favoring arbitration is neutrality: arbitration clauses are to be enforced or not enforced in the same way, and to the same extent, as other sorts of contractual provisions. Nonmandatory arbitration is favored by subjecting arbitration agreements to the same grounds of enforcement as other contracts. The "savings clause" of section 2 of the Act exhibits neutrality toward arbitration; roughly, arbitration clauses in written agreements in contracts "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or equity for the revocation of any contract."75 Another sense in which arbitration can be favored is by way of a presumption of contractual intent in the case of ambiguity. A pro-arbitration policy can create a presumption that, absent indications to the contrary, parties to an arbitration agreement want an issue to be resolved by arbitration. Arbitration is favored by stating a default rule of contract interpretation based on the likely preferences of the majority of contracting parties. A fourth sense of policy favoring arbitration is as a substitute for contractual intent. There might be good reasons for arbitrating disputes independent of the preferences of contracting parties. A policy might prefer arbitration when the parties' agreement is otherwise ambiguous on the matter or even when parties prefer not to arbitrate. By serving as a substitute for contractual intent, arbitration is favored for dispute resolution in spite of the preferences the parties may have. The Supreme Court's pro-arbitration dicta ranges from simple contract enforcement, to neutrality, to a presumption of contractual intent.76 Some lower federal courts invoke the dicta also as a substitute for contractual intent. The Act at most favors arbitration in the sense of simple contract enforcement, neutrality, or a presumption of intent.

2. A Brief History of Pro-Arbitration Dicta

The Supreme Court's pro-arbitration dicta vary in meaning. The variation does not reflect a change in the way the Court reads the Federal Arbitration Act to favor arbitration. Rather, its use of pro-arbitration dicta shows that simple contract enforcement, a presumption of contractual intent, and neutrality are recurring senses in which arbitration is "favored." All of these elements may sometimes

76. See infra Part II.B.2. For a less charitable view, finding that the Court sometimes invokes pro-arbitration as a substitute for contractual intent, see MACNEIL, supra note 67, at 172.
figure in the same opinion. Beginning in 1974, the dicta appear in a set of well-known cases. Simple contract enforcement came first, obliquely in Scherk v. Alberto-Culver Co. The Scherk Court had to decide whether to compel arbitration under an arbitration agreement when the issue to be arbitrated was considered nonarbitrable under then existing securities laws. The international commercial nature of the underlying contract, uncertainty in applicable law, and the prospective of transnational forum shopping convinced the Court to order arbitration by applying the Federal Arbitration Act. Congressional policy, it noted in passing, supported arbitration given the circumstances. A pro-arbitration policy of contract enforcement in Scherk, therefore, is invoked to allow enforcement of an arbitration clause in limited circumstances when it otherwise would be unenforceable. Contract enforcement reappears in later cases to eliminate restrictions on arbitrability based on state and federal law.

Pro-arbitration policy in the form of a presumption of contractual intent came next. In Moses H. Cone Memorial Hospital v. Mercury Construction Corp., the issue facing the Court concerned the scope of an arbitration clause: whether a tardy prosecution of a claim between an owner and contractor was to be arbitrated. In this case, the arbitration clause needed to be interpreted by the Court. To do so, the Court invoked a policy favoring arbitration in the form of a presumption:

[T]he Courts of Appeals have since consistently concluded that questions of arbitrability must be addressed with a healthy regard for


79. See id. at 519-20.
80. See id. at 521 n.15.
81. See, e.g., Allied-Bruce Terminex Cos. v. Dobson, 513 U.S. 265, 277-81 (1995) (citing Alabama law treating arbitration clause as unenforceable that is preempted by the Federal Arbitration Act); see also Perry, 482 U.S. at 490 (stating that the Act's reach is expansive); Southland Corp., 465 U.S. at 10 (explaining that state law, which restricted the arbitrability of franchise disputes, is held preempted by the Act based on "national policy favoring arbitration").
82. See Shearson/American Express, Inc. v. McMahon, 482 U.S. 220, 226 (1987) (stating that federal policy favoring arbitration requires arbitration of securities claims); Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 631 (1985) ("Here, as in Scherk, that presumption [i.e., in favor of enforcing bargained-for choice of forum clauses] is reinforced by the emphatic federal policy in favor of arbitral dispute resolution.").
the federal policy favoring arbitration. We agree. The Arbitration Act establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability.84

Since the presumption of arbitrability is based on section 2 of the Federal Arbitration Act, and the latter in turn requires the enforcement of arbitration agreements, the presumption goes to the contracting parties' intent. Later cases preserve the presumption of arbitrability while also invoking the policy of contract enforcement. Volt Information Sciences v. Leland Stanford Junior University,85 for instance, finds that favoring arbitration requires both that ambiguities in the scope of an arbitration agreement be interpreted in favor of arbitration and that arbitration agreements be enforced.86

Finally, arbitration is also favored in the sense of neutrality: agreements to arbitrate are subject to no greater restrictions than other sorts of contracts. A policy of neutral enforcement is mentioned in passing in Scherk as placing arbitration agreements on the "same footing" as other contracts.87 Southland Corp. v. Keating reads section 2 of the Act as imposing only two limitations on their enforcement. One limitation is that the agreement to arbitrate be written and "evidence a transaction involving commerce."88 The other limitation is that the enforcement becomes valid according to the same grounds applicable to other sorts of contracts.89 The second limitation states a policy of neutral enforcement. Its consequences are drawn by the Court in Southland and subsequent cases. Southland invalidates state laws which restrict the arbitrability of franchise disputes.90 Perry v. Thomas invalidates state laws allowing judicial determination of wage claims covered by an arbitration agreement.91

84. Id. at 24-25 (citations omitted).
86. See id. at 475-76; cf. Mastrobuono, 514 U.S. at 62 (citing Volt Info. Sciences, 489 U.S. at 476).
87. See 417 U.S. at 511 (citations omitted).
89. See id. at 11; cf. Allied-Bruce Terminex Cos., 513 U.S. at 281 ("What States may not do is decide that a contract is fair enough to enforce all its basic terms (price, service, credit), but not fair enough to enforce its arbitration clause.").
Doctor's Associates, Inc. v. Casarotto voids state laws requiring that arbitration clauses be displayed in a manner not required of other contract terms. In each case, the Court invokes a policy of neutrality to invalidate law placing enhanced burdens on agreements to arbitrate.

3. Pro-arbitration Dicta in the Courts

Lower courts sometimes invoke pro-arbitration dicta in another way: as a preference for arbitration independent of contracting parties’ preferences. Case citations to authority are deceptive. They mask a different use of Supreme Court dicta favoring arbitration. To be sure, the predominant use of pro-arbitration dicta by lower courts is consistent with the use by the Supreme Court. If an agreement to arbitrate otherwise subject to the Federal Arbitration Act is at issue, a policy of simple contract enforcement is given as a reason for compelling arbitration. If the arbitrability of a matter under the agreement is in question, the presumption of a contractual intent is used to answer the question. If limitations to enforcement presented by federal or state law restrictions on arbitrability are in play, a policy of neutrality is invoked to compel arbitration nonetheless. Pro-arbitration dicta in each case can serve either as a consideration or sufficient condition for compelling arbitration.

However, lower courts sometimes put the dicta to at least three additional uses. One is as a device for interpreting provisions of the Federal Arbitration Act itself. If the question concerns the

93. See id. at 687.
94. See Mitsubishi Motors Corp., 473 U.S. at 627.
96. A fourth use, tried but later rejected by some courts, is to compel consolidation of arbitrations. If A and B have different valid arbitration agreements with X, can a court order A and B to arbitrate with X in a single proceeding? Some courts have employed pro-arbitration dicta to order consolidation. See, e.g., Government of United Kingdom v. Boeing Co., 998 F.2d 68, 71 n.1 (2d Cir. 1991) (collecting cases); Compania Espanola de Petroleos, S.A. v. Nereus Shipping, S.A., 527 F.2d 966, 975 (2d Cir. 1975); P/R Clipper Gas v. PPG Indus., 804 F. Supp. 570, 573-75 (S.D.N.Y. 1992); Rio Energy Int'l v. Hilton Oil Transp., 776 F. Supp. 120, 122 (S.D.N.Y. 1991); cf. Baesler v. Continental Grain Co., 900 F.2d 1193, 1196 (8th Cir. 1990) (Brown, J., dissenting). The use of the dicta has later been rejected as a reason for ordering consolidation. See Boeing Co., 998 F.2d at 71 (“[R]ecent Supreme Court case law has undermined our previous conclusion that the FAA's 'liberal purposes' and the Federal Rules of Civil Procedure allow us to consolidate arbitration proceedings absent consent.”).
97. See Snyder v. Smith, 736 F.2d 409, 417 (7th Cir. 1984) (“evidencing a
scope of section 2 of the Act, for instance, policies of contract enforcement, a presumption of contractual intent or neutral enforcement obviously cannot answer it. This is because the question is one of statutory interpretation, not contract interpretation or enforcement. A second use of pro-arbitration dicta is to decide whether someone is a party to an arbitration agreement.98 Since the question here is whether X is a party to an arbitration agreement, policies based on contract enforcement, contractual intent, or neutrality are irrelevant. Pro-arbitration dicta is relevant in each of these three uses only if there exists a freestanding policy favoring arbitration which serves as a substitute for contractual intent. The third use of the dicta is to allow nonparties to an arbitration agreement to compel parties to arbitrate with them.99 If A and B are parties to an enforceable arbitration agreement, may X, a nonparty to it, force A or B to arbitrate with her? Conversely, may A or B force X to arbitrate? Again, considerations restricted to contract enforcement, a presumption of contractual intent, or neutrality cannot alone answer the question. Only a freestanding policy preferring arbitration can do so. Pro-arbitration dicta, when used to interpret the Federal Arbitration Act, decide who can take advantage of an arbitration agreement, or determine whether someone is a party to one, functions as a replacement for contractual intent. The dicta states an additional policy.

For example, Latifi v. Sousa100 illustrates the third use of pro-arbitration dicta. Axion Corporation entered into a joint venture with Boserup Corporation and Samson Bankers.101 The joint venture agreement included an arbitration clause requiring arbitration of


98. See, e.g., Republic of Nicaragua v. Standard Fruit Co., 937 F.2d 469, 477-79 (9th Cir. 1991); Teledyne, Inc. v. Kone Corp., 892 F.2d 1404, 1410-11 (9th Cir. 1989); see also infra Part IV.A.2.

99. See, e.g., Letizia v. Prudential Bache Sec., Inc., 802 F.2d 1185, 1187 (9th Cir. 1986) ("[N]onsignatories of arbitration agreements may be bound by the agreement."); see also Roby v. Corporation of Lloyd's, 996 F.2d 1353, 1360 (2d Cir. 1993); Arnold v. Arnold Corp.—Printed Communications for Bus., 920 F.2d 1269, 1281-82 (6th Cir. 1990) (citing Letizia with regard to nonsignatories of an arbitration agreement being able to force parties to arbitrate with them). But cf. Grunstad v. Ritt, 106 F.3d 201, 205 n.5 (7th Cir. 1997) (stating that federal policy favoring arbitration does not extend to parties who never agreed to arbitration in the first place); McCarthy v. Azure, 22 F.3d 351, 355 (1st Cir. 1994) (finding that requiring that arbitration rely on the consent of both or all parties is "wholly consistent with federal policy").

101. See id.
disputes arising from “any aspect of this agreement . . . with resulting damages to the other party.”\textsuperscript{102} Axion filed suit against Sousa, Boserup’s employee, and a nonsignatory to the joint venture agreement, alleging that Sousa committed fraud in connection with the agreement.\textsuperscript{103} Sousa moved to compel arbitration of the allegation.\textsuperscript{104} The \textit{Latifi} court decided that a nonparty to an arbitration agreement, when acting in his representative capacity, can compel arbitration against himself.\textsuperscript{105} The court’s reasoning appears in the following argument:

A number of federal courts have concluded that employees of an entity that signs an arbitration agreement are entitled to the protection of their employer’s arbitration provision. Agents and employees are bound under traditional agency law principles, and the availability of arbitration to non-signatory employees \textit{also} serves the strong federal policy favoring arbitration: it precludes plaintiffs from evading their obligations to arbitrate by suing individuals rather than the signatory entities.\textsuperscript{106}

The \textit{Latifi} court’s route to its decision is questionable. Principles of agency law do not allow Sousa to compel arbitration because Sousa was an agent for a fully disclosed principle. As such, Sousa was not a party to the joint venture agreement and therefore not bound by it. Traditional principles of contract interpretation do not allow an arbitration clause signed on behalf of Sousa’s principle, Boserup, to protect him. By its terms, the arbitration clause extended to disputes with the “other party,” i.e., Boserup. Axion’s dispute was with Sousa, allegedly for his having defrauded Axion. In any case, the court does not employ principles of contract interpretation to extend the arbitration clause to Sousa. Only the “strong federal policy favoring arbitration” mentioned by the court allows it to conclude that a nonparty to an arbitration agreement can enforce it. The “strong federal policy” here serves as a substitute for the joint venturers’ contractual intent,

\textsuperscript{102} Id.
\textsuperscript{103} See id.
\textsuperscript{104} See id.
\textsuperscript{105} See id. at *2.
\textsuperscript{106} Id. (emphasis added) (citations omitted); cf. \textit{Letizia}, 802 F.2d at 1187-88 (“Other circuits have held consistently that nonsignatories of arbitration agreements may be bound by the agreement under ordinary contract and agency principles. The rule is an outgrowth of the strong federal policy favoring arbitration.”) (citations omitted); \textit{Scher v. Bear Stearns & Co.}, 723 F. Supp. 211, 217 (S.D.N.Y. 1989) (“If this Court were to allow plaintiff to avoid arbitration of claims arising out of the customer agreement, simply by naming individual agents of the institutional party as defendants, it would in effect ignore both the particular arbitration clause and the explicit federal policy in favor of arbitration.”).
an independent policy favoring arbitration. Without it, the Latifi
court’s reasoning contains a non-sequitur. With the policy, there
might be good reason for allowing nonparties to take advantage of an
agreement to arbitrate. The argument below shows that no federal
policy favoring arbitration in the requisite sense exists.

4. Why Pro-Arbitration Policy Does Not Exist

An initial consideration suggests that there is no policy favoring
arbitration. Judicial treatment of judicial forum selection clauses is
the same as arbitral forum selection clauses. Predominant judicial
practice gives effect to valid clauses selecting judicial fora. This is so
even when the contract of which the forum selection clause is a part
is later found to be invalid.107 In other words, a doctrine of separa-
bility is in effect applied to judicial forum selection clauses. The fo-
rum selected by the contract determines whether the forum selection
clause is enforceable. In doing so, it does not pass on the enforceabili-
ty of the rest of the contract. If the forum selection clause is enforce-
able, the forum dismisses the case. The enforceability of the rest of
the contract is left to the forum selected by the parties. This judicial
treatment of judicial forum selection clauses mimics the allocation of
decision making between courts and arbitrators. This is not surpris-
ing since an arbitration agreement is a type of forum selection
clause. The treatment of judicial forum selection clauses does not de-
pend on a policy “favoring” forum selection clauses.108 It suggests,
without proving, that the judicial treatment of arbitration agree-
ments also does not depend on a policy favoring arbitration.

The argument that no pro-arbitration policy exists is straightfor-
ward. It can be stated in the form of a dilemma: Either the policies
identified in the Federal Arbitration Act or in the federal jurispru-
dence do not favor arbitration over other sorts of agreements or,
while favoring arbitration, are not accepted pro-arbitration poli-
cies.109 If the former, then the policies identified do not prefer arbi-

---

107. See Frietsch v. Refco Inc., 56 F.3d 825, 829-30 (7th Cir. 1995); AVC
Nederland B.V. v. Atrium Inv. Partnership, 740 F.2d 148, 158 (2d Cir. 1984);
Enviroilite Enters. v. Glastechnische Industrie Peter Lisec Gesellschaft M.B.H., 53
Inc., 747 F. Supp. 552, 553-54 (W.D. Mo. 1990); Gaskin v. Stumm Handel GmbH,

1990) ("We are persuaded that the only good reason for treating a forum selection
clause differently from any other contract . . . is the possibility of adverse effects
on third parties. Where that possibility is slight, the clause should be treated like
any other contract.").

109. See MACNEIL, supra note 67, at 72-77.
tration over other ways of resolving disputes. If the latter, then the preference for arbitration is not recognized in law. Hence, dicta notwithstanding, in both cases there is no policy favoring arbitration.

To see this, consider the policies identified above. Simple contract enforcement and neutrality only justify treating arbitration agreements in the same way as other types of agreement. In those senses, arbitration is no more (or less) favored than agreements to sell widgets. A presumption of contractual intent is a default rule for deciding which issues fall within the scope of an otherwise unspecific arbitration clause. Whether understood as a majoritarian or penalty default, it is selected to effectuate or elicit the preferences of contracting parties. In this respect, the rule is the same as the default rules for price or delivery terms in a contract. It does not replace contractual intent and is not selected to serve other goals. Therefore, simple contract enforcement, neutrality, and presumptive contractual intent cannot serve as policies favoring arbitration over other sorts of agreements. To describe them as pro-arbitration policies is a misnomer.

Consider next arbitration as a substitute for the contractual intent of the parties. A policy that prefers arbitration independently of contractual intent obviously favors arbitration over other ways of resolving disputes. But arbitration as a substitute for contractual intent is not a policy recognized in statute or case law. At most, policies of contract enforcement, neutrality, and a presumption of contractual intent are frequently invoked and they do not underwrite arbitration as a substitute for contractual intent. True, courts sometimes apply pro-arbitration dicta in this way, as noted above. But the application is infrequent and goes beyond the support the dicta provides. Therefore, a preference for arbitration independent of contractual intent is not accepted in statute or case law. A policy favoring arbitration in this sense does not exist. The conclusion is not surprising. Since the statutory provisions of the Federal Arbitration Act give effect to the parties' agreement to arbitrate, the Act cannot exhibit a preference for arbitration independent of the parties' intent. And since the structure of commercial arbitration allocates to courts and arbitrators some issues concerning noncontracting parties, a pro-arbitration policy supposedly exhibited by the Act cannot explain or justify it. For instance, the doctrine of separability treats the existence and validity of an arbitration clause as independent of the validity of the main agreement. Because the arbitration clause

110. Cf. U.C.C. § 2-305(1)(a) (1991) (price); § 2-308(a) (place of delivery).
111. See supra text accompanying notes 71-73.
112. See supra text accompanying notes 40-42.
might not exist, and the Act does not prefer arbitration independent of the contracting parties' intent, the doctrine cannot be explained or justified.

An objection might be made here. A bit of legal realism, it might be said, shows judicial acceptance of a policy favoring arbitration. The application of pro-arbitration dicta by some courts as a substitute of contractual intent indicates a recognition of the policy. After all, if courts sometimes employ pro-arbitration dicta to attain results reachable only by considering arbitration as a substitute for party intent, the better inference is that they endorse a policy favoring arbitration. Invoking pro-arbitration dicta to do so merely shows that the dicta are an inaccurate indication of that endorsement. Judicial application is a better indication. As put, the objection fails. For one thing, it overstates the extent to which arbitration has been imposed as a substitute for contractual intent. Some lower courts have done so, but the practice is infrequent, and increasingly rejected.\[13\] The frequency of reliance on arbitration as a replacement for contractual intent therefore is insufficient to find judicial acceptance of the policy.

Furthermore, even if sufficiently frequent, the policy endorsed cannot explain or justify the structure of commercial arbitration. This is because it is too broad to account for the pattern of allocations of issues to courts and arbitrators. A policy preferring arbitration independent of contractual intent does not explain or justify allocating the existence and review issues to courts and the scope and contract issues to arbitrators. It has nothing to do with why some decisional allocations are mandatory and others are only default allocations. In other words, the policy is too coarse-grained to account for the structure of commercial arbitration. The same point applies to regulatory approaches in general. Docket-clearing, the communitarian value that social norms be expressed in a public form, or a brute preference for arbitration, may be the bases for un-

\[13\] The case law concerning consolidation of arbitrations is an example. The Second Circuit relied upon arbitration as a substitute for contractual intent in Compañía Española de Petróleos, S.A. v. Nereus Shipping, S.A., 527 F.2d 966 (2d Cir. 1975), and its progeny. See supra note 96 and accompanying text. In doing so it invoked the pro-arbitration policy expressed in Robert Lawrence Co. v. Devonshire Fabrics, Inc., 271 F.2d 402, 410 (2d Cir. 1959), stating that "any doubts as to the construction of the [Federal Arbitration Act] ought to be resolved in line with its liberal policy of promoting arbitration." The Second Circuit overruled Nereus Shipping in part by rejecting Robert Lawrence's characterization of the Act's pro-arbitration policy. See Boeing Co., 998 F.2d at 72. Boeing Co. found the Act's pro-arbitration policy to be one of simple contract enforcement. See id. Taken as a whole, these cases indicate a rejection of a policy which treats arbitration as a substitute for contractual intent.
articulated attitudes toward commercial arbitration. But the approaches fail to explain or justify commercial arbitration's pattern of decisional allocations. Regulatory approaches do not therefore account for its structure.

III. THE CONTRACTARIAN STRUCTURE OF COMMERCIAL ARBITRATION

Neither contractual nor regulatory approaches can account for the allocation of issues between courts and arbitrators. Contractual approaches are incomplete in part because they focus only on contracting parties and ignore the effects of decisional allocations on noncontracting parties. Regulatory approaches fail because the existing law exhibits no general, freestanding preference for arbitration over other means of dispute resolution. Since a contractarian approach need not consider only the interests of contracting parties or rely on an independent (and vague) policy preference for arbitration, it can do better. This Part describes and applies a contractarian approach to the allocation of issues that define the structure of commercial arbitration.

A. A Contractarian Approach

Contractarian accounts treat rules as the object of choice by a suitably specified group of persons under specified conditions of choice. The approach requires stipulation of three elements: the persons choosing, the rules chosen, and the conditions under which the choice is made. Since the persons selecting rules need not be only parties to a contract, contractarian and contractual approaches are distinct. Contractarian political theories are the most familiar. Here, the stipulation of choosing persons, rules, and conditions of choice are distinctive. Rawls, for instance, has members of a constitutional democracy selecting principles governing its basic institutions when deprived of information about their abilities and individual circumstances. Eliminating information about abilities and individual circumstances is meant to achieve impartiality in choosing the principles. The exercise's purpose is to select rules for evaluating the legitimacy of fundamental social arrangements. Although well-known in political and moral theory, contractarian approaches need not be

confined to those domains. They can be used to evaluate the legitimacy of specific legal rules. In particular, a contractarian approach can be used to assess commercial arbitration's allocation of issues between courts and arbitrators.

To assess commercial arbitration's allocation, begin with several easy distinctions. One distinction concerns the objects of choice. Suitably specified parties can select either an entire set of rules or discrete rules. Rawls's exercise calls for the choice of principles governing basic institutions, an entire set of rules. But there is nothing to prevent the choice of particular rules, such as the allocative rules applicable to commercial arbitration.

Another distinction concerns the circumstances in which parties select rules. The distinction is between the choice of a rule under ideal circumstances and its choice under actual circumstances. Rawls, for example, has parties choosing principles of justice to further their self-interest, when deprived of information about themselves and their circumstances. Given Rawls's parties' stipulated motivations and information available to them, they choose principles of justice under ideal circumstances.

Another example of choice under ideal circumstances is the selection of terms by contracting parties given full information and zero transaction costs. It is possible to stipulate the actual circumstances in which a rule is chosen. Parties can choose particular legal rules to further their self-interest without limitations on their use of information available to them, whatever background principles of justice obtain. Consulting informed self-interest might be objectionable as part of an exercise in moral theory. However, it is not subject to the same objections when particular rules of commercial law are at


stake. A final distinction is between parties to a contract and parties otherwise affected by a rule selected. There is no need to restrict consideration to contracting parties; the preferences or judgments of persons affected by a rule can be taken into account.

Accordingly, contractarian accounts can select particular rules by the choice of informed, self-interested parties. This exercise has been used to select standards of contractual performance—for instance, the fiduciary duties of a trustee to her beneficiary or the duties of corporate managers to shareholders. It can also be used to choose a "second order" standard for allocating particular issues to decision makers for their decision. Used in this way, the account abstracts from the operation of background principles of justice applicable to basic social institutions. Because the exercise selects a particular legal rule under actual circumstances of choice, all other legal rules are taken as given. It assumes that parties lack complete information about future states of the world but know the likely incentives of decision makers in existing institutions. In the law of commercial arbitration, the decision makers are courts and arbitrators, and the existence, scope, contract, and review issues are to be allocated between them.

Which allocation of issues would parties prefer in light of information available to them about the likely behavior of courts and arbitrators? It depends on which parties' preferences are considered. Where the allocation induces few externalities, contracting parties' preferences are decisive. All affected parties' preferences are relevant when externalities are significant. The distribution of the contract issue to arbitrators is straightforward. Use of an arbitration clause as an express contract term indicates a preference among contracting parties for the arbitrator selected to pass on the underlying contract. Other allocations require further justification. In the next two sections, I justify the allocation of the existence issue to courts by considering the preferences of all affected parties and the allocation of the scope issue to arbitrators by considering the preferences of the contracting parties. I then describe the mandatory nature of the distribution of the existence and review issues to courts.

B. Allocation of the Existence Issue

The existence issue asks whether an agreement to arbitrate is enforceable against a particular party. Its enforceability in turn requires that the party is bound by a valid arbitration agreement. In

principle, if the party resists arbitration, either a court or arbitrator could have final say in the matter. 118 Since the party might be a stranger to the arbitration agreement, the favored decision maker cannot be determined by consulting only the preferences of contracting parties, for whether someone is a party to an arbitration agreement is the issue that needs to be decided in the first place. In fact, anyone could be alleged to be a party to an enforceable agreement to arbitrate and there need not even be prima facie evidence of an arbitration agreement. Hence, the preferences of all those who might be alleged to be a party to an arbitration agreement must be considered, not just the interests of contracting parties. Assuming that the only issue is whether or not an enforceable agreement to arbitrate exists, the question is one of the choice of decision maker. Since an arbitrator is selected by agreement of contracting parties, and a party might be a stranger to an arbitration agreement, a nonjudicial decision maker is a private judge who may or may not be an arbitrator. If an enforceable arbitration agreement exists, the private judge is an arbitrator; otherwise, she is not. The choice of decision maker therefore is between a court and a private judge. Would parties prefer a court or a private judge to decide the existence issue finally, given an allegation that they are bound by an enforceable arbitration agreement?

Parties presumably want to minimize the sum of costs to them of the issue being decided. Since, again, a party might be a stranger to a commercial arbitration agreement, the relevant parties cannot be restricted to contracting parties. The choice of decision maker therefore turns on the respective costs to parties of courts and private judges deciding the existence issue. A salient cost variable is the parties’ decision costs, principally litigation or arbitration expenses. Decision costs can be ignored for two reasons. First, the little impressionistic empirical evidence available suggests that commercial arbitration costs are no lower systematically than litigation costs. 119

118. See supra text accompanying notes 9-10. In principle, the existence issue could further be disaggregated into further issues, such as whether the arbitration agreement exists, its validity, and whether someone is a party to it. Allocations of these further issues then could be made between courts and arbitrators. For case law allocating the existence issue depending on whether the existence of the arbitration agreement or being a party to it is disputed, see cases cited infra notes 157-58.

119. See Charles N. Brower & Abby Cohen Smutny, Arbitration Agreements Versus Forum Selection Clauses: Legal and Practical Considerations, in INTERNATIONAL DISPUTE RESOLUTION: THE REGULATION OF FORUM SELECTION 37, 41-43 (Jack L. Goldsmith ed., 1997) (noting that the evidence is the same regarding international commercial arbitration); Park, supra note 59, at 4 (noting that arbitration costs are no lower generally than litigation costs); Thomas J. Stipanowich,
Second, and more important, because the resolution of the existence issue by private judges is only a possibility, the needed cost comparison is counterfactual. That is, the question is: what would be the size of parties' litigation and arbitration expenses if courts or private judges decided the existence issue? Such a cost estimate is too speculative to be the decisive variable in the choice of decision maker. Two other familiar sorts of cost variables are apparent: an incorrect finding that a party is bound by an enforceable arbitration agreement, and the precautions undertaken by a party to reduce the likelihood of the finding being made. Call the first sort of cost an "error cost" and the second sort a "precaution cost." Estimates of these costs favor allocating the existence issue to courts. Both error and precaution costs are likely to be lower when courts decide the matter than when private judges do so.

Error costs can result either from simple mistake or bias. There is no reason to believe that private judges make more mistakes in resolving the existence issue than courts, or vice versa. This is because the same information and expertise can be available to both sorts of decision makers. Judges' salaries are fixed while private judges' fees vary according to market demand, so it might seem that judges lack the incentive arbitrators have not to make errors of law or fact. But the inference is weak since judges' concern for their judicial reputation or a desire not to be reversed concentrates the judicial mind. Put more carefully, nothing suggests that private judges

Rethinking American Arbitration, 63 IND. L.J. 425, 461-62 (1987) (summarizing ABA survey of members of its construction litigation division; although responses indicate that arbitration is "somewhat less costly" than litigation, evidence suggests that direction of response might depend on size of case); cf. 1 IAN R. MACNEIL ET AL., FEDERAL ARBITRATION LAW § 3.2.2.2 (1995) ("There is as much or more uncertainty about the costs of arbitration relative to the costs of litigation as there is respecting their relative speeds.").

120. Even when different information or expertise is available, arbitrators are no more mistake-prone than courts. To resolve the existence issue in any particular case, both law and facts are needed. Mistake can occur in determining either law or facts. For instance, in order to determine whether an arbitration agreement was entered into, the legal standard for acceptance of an offer has to be known. Whether a response operated to conclude the agreement also depends on the circumstances in which the response occurred. An arbitrator expert in a particular industry might have more knowledge about the facts than a court. At the same time the court might have more knowledge about the operative legal standards. Private judges do not therefore know less (or more) than courts of what is needed to resolve the existence issue. Hence, if less knowledge makes for a heightened risk of mistake, private judges are no more (or less) likely to make mistakes than courts in deciding the existence issue.

are systematically more mistake-prone in a matter than courts, or vice versa. Nor is the range of matters in which they make mistakes greater than that of courts. Private judges, however, are more likely than courts to be biased with respect to the existence issue. The bias has supply and demand side components. On the supply side, the compensation schedule for private judges gives them an incentive to find jurisdiction in any particular dispute. This is because they receive at least as high fees when an enforceable agreement is found as when none is found. On the demand side, the means by which private judges can be selected to decide the existence issue allows a party to control its resolution. If a private judge has final say over the existence issue, a party need only allege that the other party agreed to have a particular private judge decide the dispute. The named private judge then would pass on the enforceability of the agreement. The private judge's favorable decision could be assured by a side payment and the possibility of recovering her fees from the other party. Systematically biased decision makers therefore could be selected if private judges decide the existence issue. A similar mechanism is not present in the selection of courts.

Compare the situation in the case of private judges and courts. The benefits from arranging for an inaccurate arbitral decision are greater than those from a judicial decision. And, correspondingly, the costs of doing so are lower than for a favorable judicial decision. Since the private judge's decision would be final, the benefits of a

(arguing that judicial reputation and concern for reversal affect judges' utility function); Thomas J. Miceli & Metin M. Coggel, Reputation and Judicial Decision-making, 23 J. ECON. BEHAV. & ORG. 31 (1994).

122. Institutional arbitration rules typically require a party filing a claim to deposit amounts as an advance on prospective arbitration costs. See, e.g., AMERICAN ARBITRATION ASS'N, supra note 14, art. 34(1); INTERNATIONAL CHAMBER OF COMMERCE, ICC RULES OF ARBITRATION AND ICC RULES OF CONCILIATION, art. 30(1) (1998). The arbitrator receives its fee no matter how it resolves the existence issue. Since fees plausibly increase with the parties' use of the arbitrator, fees also increase if the existence issue is resolved in favor of an enforceable agreement and the parties do not settle. (In that case the parties will require more of an arbitrator's services.) The size of the increase depends on the probability of settlement. Given a nonzero probability of nonsettlement, the arbitrator's expected fees are higher when it finds an enforceable agreement than when none is found. Since arbitral bias is present if expected arbitral fees are at least as high if arbitral jurisdiction is found as when it is not found, the text only makes the weaker claim.


124. Some institutional arbitral rules allow for limited review of arbitral
favorable decision are assured. A "bounty" need only be promised to the private judge by a party. Because of the possibility of appellate review, a favorable judicial decision cannot be assured by a single judge. The benefits of such a decision therefore are reduced. Correspondingly, in order to obtain a favorable decision on the existence issue from a private judge, a party need only compensate an arbitrator or arbitration panel. Lack of docket control and the presence of appellate review increase the cost of assuring that a court makes the same decision. Assuming that the required "bounty" increases with the number of necessary favorable decisions, the costs of assuring a favorable decision are lower with arbitration than with litigation. The greater benefits and lower costs of assuring a favorable decision increase the demand for biased arbitrators. Since that bias is not present when judges pass on the existence issue, error costs are likely to be higher when arbitrators pass on the matter.

Consider now the precaution costs borne by parties. Their size is affected by the presence of error costs. Where error costs are positive, a party will incur precaution costs that optimally minimize them. Precaution costs are measures undertaken by a party to reduce the likelihood of a decision maker making an inaccurate finding against her. They can range from a preemptive offer of a "bounty" to a private judge for a favorable decision to controlling one's underlying activities in a jurisdiction that might result in a demand for arbitration. Since error costs are likely to be higher when a private judge rather than a court decides the existence issue, a party's precaution

jurisdiction and awards by the sponsoring arbitral institution. See, e.g., INTERNATIONAL CHAMBER OF COMMERCE, supra note 122, art. 6(2) (challenge to jurisdiction can be submitted to "Arbitral Tribunal"); id. art. 27 (court scrutiny of award). Where such arbitral review is possible, the arbitrator's decision is not final, and assurance of a favorable decision would require compensating those arbitral administrators reviewing the award. Since arbitral review is limited and a party need not select institutional arbitration in the first place, I ignore the possibility. My claim is only that, if arbitrators passed finally on the existence issue, a party could select a person willing to decide in its favor.

125. The cost of compensation in effect can be shared by the other party, since part or all of the arbitrator's fees can be recovered from the other party. Some institutional arbitral rules provide for this. See, e.g., AMERICAN ARBITRATION ASS'N, COMMERCIAL ARBITRATION RULES, Administrative Fee Schedule (1996) ("Unless the parties agree otherwise, arbitrator compensation and administrative fees are subject to allocation by the arbitrator in the award."); id. art. 49 ("Expenses"); INTERNATIONAL CHAMBER OF COMMERCE, supra note 122, art. 31(3) (arbitrator's award "shall fix the costs of the arbitration and decide which of the parties shall bear them or in what proportion they shall be borne by the parties"); LONDON COURT OF INTERNATIONAL ARBITRATION RULES, art. 18.2 (1985) ("Unless the parties shall agree otherwise, the Tribunal shall determine the proportions in which the parties shall pay all or part of them to the Court.").
costs also will be higher. Again, the estimation of the size of precaution costs is comparative only. Courts can make inaccurate findings, either from bias or simple mistake, and parties incur cost-justified expenses in reducing their expected error costs. The claim is only that, given a likely systematic bias by selected private judges, the corresponding expense incurred by a party is likely to be higher than that induced by judicial error. Because the sum of error and precaution costs are higher when private judges rather than courts finally decide the existence issue, parties favor allocating the decision to courts.

C. Allocation of the Scope Issue

The scope issue requires a determination of the matters contracting parties have referred to arbitration. It concerns the breadth of an arbitration clause or agreement to arbitrate a range of items. Since the existence and scope issues are distinct, the choice of decision maker does not have to be the same. I have justified allocating the existence issue to courts. The next question therefore is whether parties prefer to allocate the scope issue to courts or arbitrators, given that they prefer to have courts decide the existence issue. Because the scope issue only concerns the range of issues contracting parties have agreed to be submitted to arbitration, the preferences of contracting parties alone are relevant. Estimates of the respective size of costs to the parties associated with courts and arbitrators deciding the scope issue therefore are needed.

Two sorts of costs can be considered: the cost of resolving the scope issue and error costs associated with the decision. The cost of resolving the issue is likely to be lower when an arbitrator rather than a court decides. This is because the parties have allocated to the arbitrator selected matters concerning the interpretation of the underlying contract. Given that the matters allocated to the arbitrator are determined by the arbitration clause, the arbitrator has to decide that a particular matter is within the arbitration clause. In doing so, she therefore has to pass on its contours. Hence the marginal cost of determining the scope of the arbitration clause is low. Allocating the determination to a court, another decision maker, requires an additional transaction and an extra cost. The marginal costs associated with its determination therefore are likely to be higher than with its arbitral counterpart.

Error costs associated with an arbitral determination of scope are distinct. They are likely to be no greater than with a judicial determination of scope. Here, as with the existence issue, arbitrators are
no more mistake-prone than courts. Unlike the existence issue, however, error costs resulting from arbitral bias are unlikely to be higher too. They may even be lower than with courts. Arbitrators' income depends on the fees received from parties to an arbitration agreement. Maximizing their income requires arbitrators to in turn maximize the contracting parties' demand for their services. Doing so requires an arbitrator to satisfy the preferences of the contracting parties. Otherwise, a competing private judge could offer to decide disputes in a way that would maximize the parties' joint satisfaction for the same fee. The arbitrator who decides disputes at variance with the wishes of the contracting parties loses future customers. Competition for fees therefore favors arbitrators whose decisions maximize satisfaction of the contracting parties' ex ante preferences.

The scope of an arbitration clause is an indication of these preferences, for while an arbitrator's decision might be unfavorable to one party ex post, scope authorizes the arbitrator to make a decision on particular matters. Scope therefore indicates the contracting parties' ex ante preference that the arbitrator do so. Accordingly, competition for fees among arbitrators favors arbitrators who decide matters within the scope of an arbitration clause. A priori there is no reason to believe that market discipline among arbitrators produces more bias than is produced by judicial decision. Hence, error costs resulting from bias are likely to be no higher if arbitrators decide the scope issue than if courts decide the matter.

The competitive mechanism which eliminates arbitral bias deserves emphasis. It can be described informally. For arbitrators to compete for fees, prospective customers need information in order to select among available private judges. The information has to concern the quality of a judge's decisions. It can come from observing previous arbitral decisions of candidates or from their reputation as arbitrators. Once informed, customers are able to make reliable predictions about a candidate's likely resolution of a scope issue. In this way, arbitrators can compete by price and the quality of their decision. All else being equal, arbitrators who make decisions outside of the scope of their authority probably will do the same in other cases. The cost of such decisions is the loss of arbitral fees of future customers.

126. See supra notes 66 & 120 and accompanying text.
about arbitral performance is produced. Some arbitral decisions are published, in varying degrees of detail. Publication produces some information for prospective customers about the quality of an arbitral decision, possibly including its resolution of scope issues. Informal survey data also suggests that reputation operates in the selection of an arbitrator. Publication and reputation are both devices for transmitting information about an arbitrator's performance. Both devices raise the cost to an arbitrator of making decisions that violate the scope of the parties' arbitration agreement. Given the availability of information about past arbitral performance and reputation, arbitrators therefore have an incentive to be unbiased in their resolution of the scope issue. Systematic error costs resulting from arbitral bias therefore are unlikely to be present.

The preferred allocation of the scope issue has a counterpart in administrative law. Under the Chevron doctrine, federal courts de-
fer to an administrative agency’s interpretation of its own statute. In reviewing the agency’s interpretation, if Congress has clearly addressed the matter, the court gives effect to its directive. Otherwise, courts must follow the agency’s interpretation if the interpretation is reasonable. The *Chevron* doctrine therefore allocates to administrative agencies the reasonable interpretation of Congressional statutory directives. Part of the justification for this doctrine is apparent. Executive agencies, at least, are agents of a politically responsive agent, the executive. As subagents, agencies are therefore indirectly responsive to control by a principal in the form of the popular will. Accordingly, they are unlikely to systematically misinterpret statutory directives through political bias.

Arbitrators can be considered agents of the contracting parties. The competition for fees makes them responsive to the scope of the arbitration agreement set by the parties. Scope is a term in an arbitration agreement. As with the interpretation of any contract term, an arbitrator’s incentive to be biased in interpreting a scope term is controlled. Hence, both the interpretation of other contract terms—a contract issue—and the scope issue are allocated to arbitrators. Pecuniary “accountability” here replaces political accountability, but otherwise the mechanism is the same—error costs are unlikely to be greater when an arbitrator decides the scope issue than when a court decides it.


132. See id. at 843-44.
133. See id. at 842-43.
134. See id. at 844.
135. Cf. id. at 865-66 (stating that it is appropriate for administrative agencies to make policy choices because the chief executive to whom they report is “directly accountable to the people”). For a sample of arguments to the effect that judicial review of agency rulemaking in practice is less deferential than *Chevron* requires, see Thomas W. Merrill, *Judicial Deference to Executive Precedent*, 101 YALE L.J. 969, 970 (1992), and Russell L. Weaver, *Some Realism about Chevron*, 58 Mo. L. REV. 129, 130-32 (1993). But cf. Peter H. Schuck & E. Donald Elliot, *To the Chevron Station: An Empirical Study of Federal Administrative Law*, 1990 DUKE L.J. 984, 1058-59 (arguing, based on the authors’ statistical analysis, that *Chevron* “reinforced” the deference courts give to administrative agencies). Since the above parallel depends on the *Chevron* doctrine, not the frequency of its application, the actual practice of judicial review of agency rulemaking is irrelevant here.

136. Park invokes the *Chevron* doctrine to argue, in effect, that arbitrators should not decide the existence issue. See Park, *supra* note 27, at 155-56. He does not notice that the same parallel justifies allocating the scope issue to arbitrators.
D. Mandatory Decisional Allocations and Terms

Both mandatory decisional allocations and mandatory contract terms restrict distributions of risk in arbitration agreements. Mandatory decisional allocations do so by requiring that courts and arbitrators decide different sorts of issues. They assign particular types of decisions to particular decision makers. Alteration by contract is not possible. Mandatory contract terms, understood broadly, restrict either the enforceability of a contract or the standards of its performance. Formation rules, definiteness requirements, and writing requirements in the nature of the statute of frauds, for example, state substantive conditions that must be satisfied for an agreement to be enforceable. A nondisclaimable implied warranty is an example of a contractual standard of performance. Since decisional allocations distribute decision making while contract terms allocate incidents of contractual performance, their justifications need not be the same.

The contractarian approach accounts for important mandatory decisional allocations. The existence issue is a mandatory decisional allocation; parties cannot contract around courts passing on the enforceability of their arbitration agreement. Allocating the issue to arbitrators imposes error costs on third parties—all those who might be alleged to be parties to an arbitration agreement. Because error costs in deciding the existence issue systematically are likely to be higher when arbitrators rather than courts decide the matter, parties prefer that courts decide the existence issue. The preference, once given effect, does not allow parties to contract for arbitrators to decide the matter, for the decisional allocation has courts yet an arbitration agreement containing such a clause to determine its enforceability. In determining the clause's validity, the contracting parties' preferences as to decision maker are not honored. Judicial determination of the agreement's enforceability, therefore, does not give effect to the parties' attempt to opt out of the allocation. It could not be otherwise. Either courts or arbitrators have to pass on the enforceability of an alleged arbitration agreement against a party. Once the decision is allocated to either decision maker, she decides whether to give effect to an agreement containing a choice of an alternative decision maker. In doing so, the parties' choice of an alternative decision maker to resolve the same issue is frustrated. Contracting around the existence issue therefore is not possible.

The review issue also is a mandatory decisional allocation with a contractarian basis. Parties cannot opt out of limited judicial review

137. See supra text accompanying notes 24-33.
of some aspects of an arbitral award.\textsuperscript{138} Externalities in the form of error costs associated with arbitrators deciding the existence issue indirectly account for the mandatory allocation. Arbitrators can issue an award after determining their own jurisdiction. Given arbitral bias in making the determination, the bias carries over to the resulting award. The award and its enforcement, therefore, can impose error and precaution costs on noncontracting parties. Error and precaution costs are lower when courts review an award than when the final decision on the existence issue is left to arbitrators. Accordingly, parties prefer that courts review arbitration awards. Limited review of the arbitration award when confirmation or enforcement is sought is a consequence of the allocation of the existence issue to courts. Parties might by contract try to opt out of judicial review of an arbitration award. But opting out is restricted because courts pass on the enforceability of their agreement to contract out of judicial review. Judicial review of an award, therefore, is not eliminated. Swiss law, for instance, allows parties, under restricted conditions, to contract around judicial review of arbitral awards.\textsuperscript{139} Even here, however, courts still pass on the enforceability of the agreement excluding or limiting review. Current law therefore does not allow parties to opt out of the allocation of the review issue to courts.

A contractarian approach does not account for all mandatory decisional allocations and terms. Subject matter arbitrability, an increasingly limited allocation in domestic law,\textsuperscript{140} is an unexplained mandatory decisional allocation. If $X$ is a subject that cannot be arbitrated according to statute or decisional law, $X$'s resolution is assigned to courts. Parties, of course, can settle a matter involving $X$, here as elsewhere, but they cannot enforceably provide by contract that an

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{138} See supra note 50.
\item \textsuperscript{139} See Federal Statute on Private International Law, SR art. 192(1), \textit{translated in Switzerland's Private International Law Statute 1987, supra} note 51, at 165 (parties to arbitration agreement may exclude judicial review of issuance of award when all are nondomiciles or residents of Switzerland); \textit{cf. id.}, art. 191(2) (notwithstanding exclusion agreement, judicial review of enforcement of award under New York Convention on Recognition and Enforcement of Foreign Arbitral Awards).
\item \textsuperscript{140} See 1 \textit{MacNeil et al.}, \textit{supra} note 119, § 15.3.7 (noting that there are few nonarbitral issues under the Federal Arbitration Act). Subject matter arbitrability is more important in other legal systems. \textit{See M. Sornarajah, International Commercial Arbitration} 166-67 (1990) (noting that the American trend is "without parallel" in other legal systems); \textit{William Grantham, The Arbitrability of International Intellectual Property Disputes, 14 Berkeley J. Int'l L.} 173 (1996); \textit{Christopher B. Kuner, The Public Policy Exception to the Enforcement of Foreign Arbitral Awards in the United States and West Germany Under the New York Convention, J. Int'l Arb.}, Dec. 1990, at 71, 73-77.
\end{enumerate}
\end{footnotesize}
arbitrator resolve it. In excluding selected topics from arbitral decision, subject matter arbitrability therefore functions as an inalienability decisional rule, to adapt Calabresi and Melamed’s familiar term. The contractarian account leaves the range of nonarbitrable subjects indeterminate. In deciding particular sorts of substantive matters, the existence, direction, and size of error costs imposed on third parties from arbitral bias is unclear. There is no straightforward connection between the type of decision maker and its propensity for bias, for instance, in vetting antitrust claims, awarding punitive damages; copyright infringements, or statutory rights. Rather, the connection, if any, will be at a retail level, as it were, topic by topic. Mandatory contract terms also are left unexplained. Since the contractarian account looks to the preferences of parties for decision makers, not contractual standards for enforceability or performance, it has nothing to say about mandatory contract terms. This is unsurprising. Courts and arbitrators are unlikely to make systematically inaccurate judgments about substantive rules of enforceability or contractual performance. So different error costs associated with decisions by courts and arbitrators are unlikely to be present. Even if they were, the phenomenon does not underwrite making some contractual terms mandatory. At most, a mandatory allocation of decision-making authority is justified.

Even when indeterminate, a contractarian approach can be useful because it disciplines arguments for recommended mandatory allocations and contract terms. In allocating matters between courts and arbitrators, the contractarian approach looks to the interests of parties, given the likely behavior of courts and arbitrators in making particular sorts of decisions. It therefore requires identification of affected parties, their preferences for decision maker, and the comparative size of arbitral error costs. The requirement excludes recourse to vaguely stated and question-begging values such as the production of public norms by courts or the importance of specific norms. The contractarian approach insists on an argument connecting parties, the comparative decision-making biases of courts and arbitrators, and particular decisions. Judged by this standard, some arguments for specific mandatory decisional allocations fail. An example is the arbitrability of nonunion employees’ statutory rights, a chestnut of the law of commercial arbitration. Gilmer v. Interstate/Johnson Lane Corp held that arbitration of an employee’s rights under the Age Discrimination in Employment Act is enforceable under the Federal Arbitration Act when covered by an arbitra-

141. See supra notes 66 & 120-21 and accompanying text.
tion agreement. The holding safely can be generalized to all statutory rights, absent legislative prohibition of arbitrability. The debate is whether this is a good thing.

At bottom, the debate is about a mandatory decisional allocation. If employees' statutory rights can be arbitrated, their determination by courts is only a default allocation of decision making and can be altered by contract. If statutory rights cannot be decided by arbitration via contract, their determination is distributed to courts. An inalienable decisional rule is being mandatorily allocated by subject matter. The question is what can be said in favor of a mandatory allocation. A contractarian case for a mandatory decisional allocation looks to the existence and size of externalities induced by arbitrators vindicating statutory rights. This approach requires arguments connecting arbitral decision and affected parties' preferences.

Judged by this standard, some familiar arguments are unsuccessful. None identify the error costs that arbitration clauses impose on noncontracting parties. The asserted importance of statutory rights is insufficient even to allocate the forum in which they are vindicated. By itself, their claimed importance, therefore, does not select between a default and mandatory decisional allocation. Positive externalities produced by litigation, such as precedent and publicity, also are not determinative. Settlement is a missed opportunity for the production of a publicly announced norm. Yet private settlements are enforceable and encouraged, and they do not produce precedent and publicity. Current law aside, the social costs of litigation have to be taken into account, so the optimal rate of settlement is greater than zero. Put simply, precedent production and publicity are not costless public goods. Hence, the value of vindicating statutory rights in a public forum is not enough to make the case for nonarbitrability.

Arguments which look to employee and employers' preferences alone are even weaker. A nonnegotiable arbitration clause in an otherwise negotiated employment contract cannot be unenforceable

143. See id. at 35.
144. See id. at 26.
145. For an undefended assertion of the comparative importance of select statutory entitlements, see G. Richard Shell, ERISA and Other Federal Employment Statutes: When Is Commercial Arbitration an "Adequate Substitute" for the Courts?, 68 Tex. L. Rev. 509, 570 (1990), stating that "Title VII claims deal with rights to personal dignity and equal protection, not economic rights such as those embodied in the securities laws, RICO and ERISA."
just because it was not negotiated.\textsuperscript{147} The reason is familiar. Nonnegotiable terms can reduce transaction costs: the costs of negotiating the term might exceed the associated benefit to the employee of doing so. Because the nonnegotiable term is part of the employment contract, it does not therefore mean that the term is not bargained for. It only means that the bargain reflects adjustments in other terms. More important, if the arbitration clause is not enforced, a court has to substitute a term to maximize the joint value of the contract to the parties. An arbitration clause in a bargained-for agreement arguably is a better gauge of joint value than a judicially substituted term.\textsuperscript{148} The weakness of the argument from nonnegotiability is simpler. Even if successful, the argument at most shows that nonnegotiated arbitration clauses should not be enforced. The argument does not justify treating statutory rights as nonarbitrable when covered by a negotiated arbitration clause in an employment contract.

The case for nonarbitrability is equally weak when based on arbitral error. Claims of arbitral error in determining statutory rights resulting from mistake or bias are controversial. The slight empirical evidence supporting the claim is inconclusive.\textsuperscript{149} Even if true, arbitral bias does not justify a mandatory allocation of decision making to courts. It only justifies a default allocation. Assume that arbitrators inaccurately determine employees' statutory rights against employer's interests more frequently than courts do. Assume also that the employer's liability from violating them increases the employer's costs. Adverse arbitral error is a cost to the employee. On the employer's part, error reduces exposure to liability and therefore the employer's costs of respecting its employees' statutory rights. An

\textsuperscript{147} For criticism of this argument, see Stone, supra note 146, at 1037.

\textsuperscript{148} Cf. Richard Craswell, Property Rules and Liability Rules in Unconscionability and Related Doctrines, 60 U. CHI. L. REV. 1, 51 (1993) ("[I]f invalidating Y's consent triggers a liability rule then Y's consent should be invalidated only if there is some reason to think courts can do better than X in selecting reasonable terms.").

\textsuperscript{149} Compare William M. Howard, Arbitrating Claims of Employment Discrimination: What Really Does Happen? What Really Should Happen, 50 Disp. Resol. J. 40, 45 (Oct.-Dec. 1995) (finding that the rate of employer liability in sample employer discrimination cases is not significantly greater in litigation than in arbitration; mean and median recovery is greater in litigation than in arbitration, although the source of difference is inconclusive), with Stuart Bompey & Michael Pappas, Compulsory Arbitration in Employment Discrimination Claims: The Impact of Gilmer v. Interstate/Johnson Lane Corp., 1993 A.B.A. SEC. ON EMPLOYMENT & LAB. LAW EEO COMM. PAPER, cited in Stone, supra note 146, at 1040 n.162 (survey data showing differences in rates of liability and damages as between arbitration and litigation). Neither study controls for differences in types of case, contractual provisions, or the accuracy of arbitral or judicial findings.
arbitration clause covering statutory rights therefore could reduce the value of the employment contract to the employee more than it reduces the employer's costs. If so, most employees would "pay" employers not to include the arbitration clause in their employment contract. A majoritarian default rule would replicate the predominant preference of employees and employers: that courts pass on the employees' statutory rights under the employment contract. Employees could contract around the allocation, however, when judicial determination was not cost-justified. When arbitral error is comparatively low, the likelihood of statutory rights being violated remote, or litigation costs comparatively high, employees might prefer arbitration. Hence the existence of arbitral error does not make the case for mandatory nonarbitrability.

My point is not that nonarbitrability cannot be justified. It is only that some familiar arguments for nonarbitrability violate constraints set by a contractarian approach. Roughly, the contractarian approach requires justification of nonarbitrability by the preferences of affected parties, taking into account the likely incentives of courts and arbitrators in passing on statutory rights. The above arguments in their different ways fail to connect the incentives of decision makers, decisions, and the preferences of affected parties. Claims about the comparative importance of statutory rights, positive externalities produced by adjudication, and arbitral error do not link them to party preferences in a convincing manner.

IV. CASE LAW IMPLICATIONS

The contractarian approach explains the division of decision making settled on by statute and case law. Because significant externalities in the form of error costs resulting from bias can be present when arbitrators pass on the existence issue, its resolution is allocated to courts. Where the confirmation or enforcement of an arbitral award depends on resolution of the existence issue, the review issue also is allocated to courts. Where arbitral resolution of the scope issue does not induce systematic error costs resulting from arbitral bias, it is allocated to arbitrators. Preferences of affected parties, given the likely behavior of courts and arbitrators, account for these allocations. The persistent pattern of the domestic and comparative law of commercial arbitration reflects these allocations.150 Although the account is consistent with statute and case law, it does not explain the entire structure of commercial arbitration. When the direction and size of externalities resulting from arbi-

150. See supra p. 372.
tral bias in deciding substantive matters is unclear, there is room for disagreement. In these instances, a case based on the preferences of affected parties is indeterminate. Subject matter arbitrability is a prominent example. Whether antitrust regulations, awards of punitive damages, trademark or patent infringement, or statutory rights are at issue, the contractarian approach does not allocate the decision maker by subject matter. The result is consistent with the variety of subject matters considered nonarbitrable within legal systems across time and between legal systems. The extent and judicial review of arbitral awards is another example.

The contractarian approach also has consequences for case law. If issues are allocated to arbitrators and courts based on party preference, the approach states a standard by which case outcomes and reasoning can be evaluated. Accordingly, there are two sorts of implications for case law. One implication concerns the evaluation of case outcomes—application of arbitral doctrine in a way that allocates to arbitrators (courts) issues that are properly allocated to courts (arbitrators). The other implication concerns the justification of results reached in cases. The contractarian approach supports some case outcomes in a more convincing way by reference to party preference given the presence or absence of arbitral bias. This Part illustrates both sorts of case implications, evaluates prominent applications of the doctrine of separability, and justifies case outcomes that allocate to arbitrators the scope issue in securities arbitrations. The following section justifies the standard judicial reliance in commercial arbitration on labor arbitration precedent concerning scope allocations.

A. Separability Applied

1. Timing Decisions and the Existence Issue

The doctrine of separability divides the arbitration clause and the main agreement into two agreements. It treats the arbitration clause as an independent contract. Since separability alone says nothing about who passes on the enforceability of the arbitration clause and main agreement, it does not allocate the choice of decision maker. In applying the separability doctrine, case law has allocated the choice in two different ways. Some courts assign the decision to enforce both the arbitration clause and the main contract to arbitrators, unless there are facts alleged that specifically challenge the enforceability of the arbitration clause. If such facts are alleged, the court passes on it. If not, the arbitrator passes on both the arbitra-

---

151. See supra note 140 and accompanying text.
152. See supra text accompanying note 46.
tion clause and the main contract. For example, Prima Paint Corp. v. Flood & Conklin Manufacturing Co.\(^{153}\) states that requirement: "if the claim is fraud in the inducement of the arbitration clause itself... the federal court may proceed to adjudicate it."\(^{154}\) Section 4 of the Federal Arbitration Act, according to Prima Paint, does not allow courts to consider claims of fraud not directed specifically at the arbitration clause.\(^{155}\) Courts following Prima Paint have extended its holding. Claims directed at the entire contract, when based on unconscionability, duress, mistake, and frustration of purpose, for instance, are for the arbitrator to decide.\(^{156}\) In deciding, the arbitrator passes on the enforceability of the arbitration clause as well as the main contract.

Other courts assign the decision to enforce the arbitration clause differently. They follow Prima Paint and allocate to the court the decision about enforceability when facts are alleged which go specifically to the arbitration clause. But these courts also allocate the decision according to whether the existence of an arbitration agreement or being a party to it is disputed. Claims denying the existence of an arbitration agreement, whether directed at the arbitration clause or the entire contract, are for the court to decide.\(^{157}\) Addition-

---

154. Id. at 403-04.
156. Cf. Union mutual Stock, 774 F.2d at 529 (mutual mistake, frustration of purpose); Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Haydu, 637 F.2d 391, 398 (5th Cir. 1981) (duress, unconscionability); 1 MacNeil et al., supra note 119, § 15.3.2 (collecting cases).
157. See, e.g., Three Valleys Mun. Water Dist. v. E.F. Hutton & Co., 925 F.2d 1136, 1140-42 (9th Cir. 1991) (holding plaintiffs were not required to submit to arbitration when they contested the agreement to arbitrate); Jolley v. Welch, 904 F.2d 988, 994 (5th Cir. 1990) (affirming the district court's referral of dispute to the magistrate where a possibility of forgery of signatures on the arbitration agreement existed); Cancanon v. Smith Barney, Harris, Upham & Co., 805 F.2d 998, 1000 (11th Cir. 1986) (stating that "where the allegation is one of... ineffective assent to the contract, the issue [of arbitrability] is not subject to resolution pursuant to an arbitration clause contained in the contract documents"); Par-Knit Mills, Inc. v. Stockbridge Fabrics Co., 636 F.2d 51, 55 (3d Cir. 1980) (holding that the determination as to whether there is a "meeting of the minds" as to contract formation should be left to the finder of fact); Dougherty v. Mieczkowski, 661 F. Supp. 267, 275 (D. Del. 1987) (holding an arbitration clause to be not enforceable when the signatures to the agreement were forged); Kyung In Lee v. Pacific Balloon, Inc., 788 F. Supp. 155, 158 (E.D.N.Y. 1992) (holding that a dispute over the validity of an arbitration agreement should be resolved at trial where the
ally, the courts decide claims that a person is not a party to an arbitration agreement.\textsuperscript{158} \textit{Jolley v. Welch} is representative when it states that the “first task” of a court under the Federal Arbitration Act “is to determine whether the parties agreed to arbitrate [their] dispute.”\textsuperscript{159} Because an allegation of nonexistence need not go just to the arbitration clause, \textit{Prima Paint} and \textit{Jolley} sometimes assign the decision as to its enforceability to different decision makers. The statutory language of the Federal Arbitration Act does not settle the disagreement. Section 4 of the Act, for instance, requires that a court compel arbitration “upon being satisfied that the making of the agreement for arbitration . . . is not in issue.”\textsuperscript{160} It says nothing about when a court is “satisfied”—whether an allegation of unenforceability is directed at the arbitration clause is needed or whether it is enough to dispute the existence of an arbitration agreement.\textsuperscript{161}

plaintiff has raised a bona fide claim of fraud in the action). \textit{But see} Timberton Golf, L.P. v. McCumber Constr., Inc., 788 F. Supp. 919, 924-25 (S.D. Miss. 1992) (compelling an arbitration clause despite finding that the underlying contract was void).

\textsuperscript{158} See, e.g., Chastain v. Robinson-Humphrey Co., 957 F.2d 851, 854-55 (11th Cir. 1992) (requiring the district court to determine the validity of an arbitration clause where the plaintiff never personally signed the agreement); Tehran-Berkeley Civil & Envtl. Eng'ts v. Tippetts-Abbett-McCarthy-Stratton, 816 F.2d 864, 868 (2d Cir. 1987) (noting that the question of whether the plaintiff was a party to the contract was too “ambiguous” to allow the court to enforce the arbitration agreement); I.S. Joseph Co. v. Michigan Sugar Co., 803 F.2d 396, 400 (8th Cir. 1986) (holding that when the plaintiff denies a contractual relationship with the defendant, the court should decide on the enforceability of the arbitration clause); Interocean Shipping Co. v. National Shipping & Trading Corp., 462 F.2d 673, 678 (2d Cir. 1972) (allowing a trial where there is “sufficient uncertainty” as to whether the plaintiff is a party to the contract).

\textsuperscript{159} 904 F.2d at 994 (quoting Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 626 (1985)); cf. Republic of Nicaragua v. Standard Fruit Co., 937 F.2d 469, 475 (9th Cir. 1991) (quoting Howard Elec. & Mechanical Co. v. Frank Briscoe Co., 754 F.2d 847, 849 (9th Cir. 1985)).


\textsuperscript{161} The Court in \textit{Prima Paint} found that the “plain meaning” of section 3 and the language of section 4 of the Federal Arbitration Act required that facts alleged go to the arbitration clause specifically. \textit{See Prima Paint}, 388 U.S. at 404. The Court’s plea of statutory compulsion is exaggerated. Section 3 requires a court to stay suit pending arbitration “upon being satisfied that the issue involved . . . is referable to arbitration.” 9 U.S.C. § 3. Section 4 requires a court to compel arbitration when it is “satisfied that the making of the agreement for arbitration . . . is not in issue.” 9 U.S.C. § 4. Since neither section says when the court is to be “satisfied,” neither section’s language states the requirement that courts pass on enforceability of the arbitration clause only when a claim alleges facts going to the arbitration clause itself.
The fight between *Prima Paint* and *Jolley* is over the point in a dispute at which a court should pass on the existence issue. The fight is not over whether, but only when, the existence issue is to be decided by courts. In other words, although not usually understood in these terms, the disagreement is really one about timing. For a court decides the existence issue either initially or in reviewing the award, when called upon to confirm, enforce, or vacate it. Section 10(a)(4) of the Act assures, under the excess of authority standard, that the court decides the existence issue in reviewing the award. 162 *Prima Paint* and *Jolley* therefore disagree only about when the issue is initially allocated to the court. Both allow a court to pass on the enforceability of an arbitration clause when the challenge goes to the clause itself. But *Prima Paint*'s requirement that facts alleged go specifically to the arbitration clause means that the arbitrator often initially decides the matter. The court initially decides the existence issue more often under *Jolley*’s exception for allegations of no agreement or being a nonparty to an arbitration agreement. Because judicial review of the initial decision is allowed in both cases, the existence issue ultimately is allocated to courts. *Prima Paint* and *Jolley* therefore do not disturb the decisional allocation.

The contractarian case described previously does not favor *Prima Paint* over *Jolley*, or vice versa. 163 This is because it has nothing to say about the matter of timing. The case only accounts for the allocation of the existence issue to courts at some point. Because arbitral decision of the existence issue induces error and precaution costs resulting from bias, contracting costs are reduced by allocating the existence issue to courts. Parties affected by the allocation therefore prefer that courts pass on the issue. 164 The particular point in time during a dispute at which affected parties prefer courts to decide is left open. This is not a defect in a contractarian account, for the timing of judicial determination is a general question in litigation, not peculiar to commercial arbitration. Doctrines of standing, case and controversy requirements, mootness, and some restrictions on available remedies each operate to restrict the point in time at which courts decide matters. They also apply independently of the preferences of affected parties. Because the timing of judicial determination is not peculiar to commercial arbitration, it is not part of commercial arbitration’s structure. The contractarian approach does not therefore have to account for timing of decision of the existence issue. 165

162. *See supra* text accompanying note 49.
163. *See supra* Part III.A.
164. *See supra* Part III.B.
165. *See supra* Part III.B. Some argue for the initial allocation of the existence
2. Standard Fruit: Deciding the Existence Issue

An obvious implication of the assignment of the existence issue to the court is that it actually decides the matter. The court must determine whether an arbitration agreement exists. If it does not do so, the determination in effect is being made by the arbitrator in exercising arbitral jurisdiction. Republic of Nicaragua v. Standard Fruit Co.\textsuperscript{166} nicely illustrates the point. To settle a dispute under a buy-sell agreement for bananas between the Standard Fruit Company ("SFC") and the government of Nicaragua, SFC's parent companies, Steamship Company and Castle and Cooke, executed a document with Nicaragua.\textsuperscript{167} The document was termed a "memorandum of intent" and contained a clause calling for arbitration of "[a]ny and all disputes arising under the arrangements contemplated hereunder."\textsuperscript{168} SFC did not sign the document, and when Nicaragua alleged that SFC breached the agreement and sought arbitration, SFC resisted.\textsuperscript{169} Three questions were presented to the court. First, was there an arbitration agreement or merely an agreement to agree? Second, was there a buy-sell agreement for bananas or merely an agreement to agree? Third, if there was an arbitration agreement, was SFC a party to it or otherwise bound by it?\textsuperscript{170} The second question concerns the buy-sell agreement between SFC and Nicaragua, the main contract. Accordingly, the court left its resolution to the arbitrator.\textsuperscript{171} Because the third question concerns whether SFC was a party to an arbitration agreement or bound by it, the existence

\begin{footnotesize}
\begin{enumerate}
\item See id. at 472.
\item Id. at 473.
\item See id. at 471-72.
\item See id. at 471.
\item See id.
\end{enumerate}
\end{footnotesize}
issue is present. The court therefore rightly remanded the matter to
the district court to decide the question on the basis of agency
principles. The first question also concerns the existence issue: whether
the arbitration clause evidenced an agreement to arbitrate or only an
intention to enter into an arbitration agreement in the future. The
question concerns contractual intent, and the evidence was mixed.
Against the finding of an arbitration agreement was the language of
the memorandum containing the arbitration clause, which described
the document as a “memorandum of intent” subject to “arrangements
contemplated hereunder.” In favor of finding an agreement was
the subsequent conduct of SFC and Nicaragua in recognizing a buy-
sell agreement. The court did not rely only on the available evidence
to determine the parties’ contractual intent, but also on a federal
policy favoring arbitration. Under that policy, according to the
court, “the most minimal indication of the parties’ intent to arbitrate
must be given full effect.”

The court’s determination is wrong for two reasons. First, the pro-
arbitration policy relied upon by the court does not exist. As previ-
ously discussed, there is no freestanding policy preferring arbitration
to other sorts of dispute resolution. At most, the policy favoring arbi-
tration is one of simple contract enforcement, neutrality, and a pre-
sumption of contractual intent. Second, pro-arbitration policies
cannot decide the question of whether an arbitration agreement ex-
ists. Pro-arbitration policies determine whether and how such agree-
ments, once found, are to be enforced. They are of no help in deter-
mning whether the parties have manifested their assent to arbitrate
in the first place. Even the presumption of contractual intent applies
only when, on independent grounds, the parties have been found to
have agreed to arbitrate. Since the central question in Standard
Fruit is whether there existed an arbitration agreement, pro-arbitra-
tion policy is irrelevant to its answer. Hence, pro-arbitration policy
does not justify a finding of contractual intent on the “most minimal”
evidence. In invoking pro-arbitration policy to justify the finding, the
Standard Fruit court wrongly leaves the existence issue to arbitra-
tors. The court should answer the question in the same way that it
answers any question of contract formation.

172. See id. at 480-81.
173. Id. at 473.
174. See id. at 478 (quoting Mitsubishi Motors, 473 U.S. at 631).
175. Id.
176. See supra Part II.B.1-2.
177. See supra text accompanying notes 75-76.
B. Scope Allocations in Securities Arbitration

The scope issue asks whether a particular dispute is within the scope of an arbitration clause. Cases concerning securities arbitration have disagreed about whether a court or an arbitrator decides the scope issue. The disagreement appears in connection with arbitration agreements covering all disputes arising between customers and brokerage firms. A standard arbitration clause incorporates by reference the procedures for arbitration of the National Association of Securities Dealers (NASD). Section 15 of the NASD Code of Arbitration Procedure provides that "[n]o dispute, claim, or controversy shall be eligible for submission to arbitration under this Code where six (6) years have elapsed from the occurrence or event giving rise to the act or dispute, claim or controversy."178 Whether a customer's particular claim against a brokerage firm can be arbitrated depends on whether it is time-barred under section 15. Because the time-bar requires dating the "occurrence or event" resulting in the customer's claim, the question goes to section 15's scope. Who decides whether the customer's claim is time-barred under section 15 depends on the allocation of the scope issue. Courts are almost evenly split as to whether an arbitrator or a court is to decide the matter.179 Usually

179. Compare Cogswell v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 78 F.3d 474, 481 (10th Cir. 1996) (holding that courts rather than arbitrators must decide whether a claim is time-barred absent clear and unmistakable evidence that the parties intended the arbitrator to decide the issue), Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Cohen, 62 F.3d 381, 383 (11th Cir. 1995) (holding that the court should decide the timeliness of claims under the NASD Code of Arbitration), Smith Barney, Inc. v. Schell, 53 F.3d 807, 809 (7th Cir. 1995) (holding that arbitrability is an issue for the court to decide when the claims were filed outside the six-year eligibility period), Dean Witter Reynolds, Inc. v. McCoy, 995 F.2d 649, 651 (6th Cir. 1993) (holding that the court must decide whether time-barred claims were eligible for arbitration), and Painewebber Inc. v. Hofmann, 984 F.2d 1372, 1383 (3d Cir. 1993) (holding that the court is obligated to determine the scope of the arbitration agreement when some of the plaintiff's claims arise from occurrences or events outside the six-year time bar), with Painewebber, Inc. v. Elahi, 87 F.3d 589, 600-01 (1st Cir. 1996) (holding that the arbitrability question is to be determined by the arbitrator absent an express intent by the parties for judicial determination when the claim is time-barred), Smith Barney Shearson, Inc. v. Boone, 47 F.3d 750, 754 (5th Cir. 1995) (holding that the timeliness issue was for the arbitrator to decide unless the claim was to bar the arbitration altogether), FSC Sec. Corp. v. Frei, 14 F.3d 1310, 1312 (8th Cir. 1994) (holding that the time limitation was a procedural and not a substantive issue for the arbitrator to interpret), and O'Neal v. National Ass'n of Sec. Dealers, Inc., 667 F.2d 804, 807 (9th
cast in terms of the "arbitrability" of scope, the dispute is over the preferred default decisional allocation.

Arguments offered on both sides are unpersuasive. First, some courts read section 15 to limit the jurisdiction of arbitration. Customers' claims are not "eligible for submission" to arbitration if time-barred under section 15. They conclude that courts therefore are to determine whether a claim is time-barred.\textsuperscript{180} The conclusion, however, does not follow. It is one thing to limit by agreement the matters that an arbitrator decides. Section 15 does this. But the limitation says nothing about who decides whether a particular dispute falls within those matters. Hence the "eligibility" limitation in section 15 does not allocate the scope issue to a court or an arbitrator. Second, other courts characterize section 15 as stating a statute of limitations for otherwise arbitrable claims, procedural in nature.\textsuperscript{181} They conclude that arbitrators therefore are to pass on whether a claim is time-barred under section 15. This conclusion does not follow even if the "procedural" label is taken seriously. Again, the question is who decides the question of "eligibility" for arbitration—the proper decision maker. Even if a customer's particular claim is otherwise arbitrable, section 15 does not determine who decides whether it is time-barred. Labeling section 15 as "procedural" does not decide the matter. Third, some courts simply assign to courts the issue of "eligibility" under section 15 as a default rule while finding that the parties have opted out of the assignment. They do so by finding that other provisions of the parties' agreement indicate that they have "clearly and unmistakably" agreed that section 15's scope is for the arbitrator to decide.\textsuperscript{182} The default assignment itself is unsupported by argument.\textsuperscript{183} An opposite allocation could just as well have been to arbitrators. Evidence of opting out is also

\textsuperscript{180} See, e.g., Cohen, 62 F.3d at 383; McCoy, 995 F.2d at 651; Hofmann, 984 F.2d at 1379; Edward D. Jones & Co. v. Sorrells, 957 F.2d 509, 513 (7th Cir. 1992) (interpreting section 15's time limitation to be removed only if the court orders the matter to be submitted to arbitration).

\textsuperscript{181} See, e.g., Boone, 47 F.3d at 754; O'Neal, 667 F.2d at 807.

\textsuperscript{182} See, e.g., Painewebber, Inc. v. Bybyk, 81 F.3d 1193, 1196 (2d Cir. 1996) (holding that a broad arbitration clause is "clear and unmistakable" evidence of same party intent); FSC Sec. Corp., 14 F.3d at 1312 (holding that section 35 of NASD Code, providing that "arbitrators shall be empowered to interpret and determine the applicability of all provisions under this Code," is a "clear and unmistakable" expression of intent to leave section 15's applicability to arbitrators).

\textsuperscript{183} See, e.g., Elahi, 87 F.3d at 599 (assigning the default allocation to the arbitrator with no supporting argument).
questionable, and other courts have disagreed as to the "clarity and unmistakable" nature of the same evidence. Since all three arguments are unpersuasive, the dispute among the courts is inconclusive.

The contractarian approach supports case law which assigns the scope issue in section 15 to arbitrators. Under the contractarian approach, the scope issue is allocated to courts or arbitrators by the preferences of affected parties, taking into account the likely incentives of courts' and arbitrators to make unbiased decisions. Since the only parties affected by a determination of the scope of an arbitration agreement are parties to the agreement, the preferences of the customer and brokerage firm are considered. Market competition for fees among arbitrators and arbitral organizations reduces arbitral error resulting from bias in deciding the scope issue. Competition among arbitrators, combined with information about previous decisions, reduces systematically biased arbitral decisions that violate the terms of the arbitration clause. There is no reason to believe that residual arbitral bias is greater than bias present in judicial decisions. In securities arbitration, the competitive mechanism is indirect. Standard brokerage agreements allow customers to elect to arbitrate under the rules of one of several self-regulating organizations, including the NASD and the major securities exchanges.

The rules of self-regulating organizations give the director of the organization the power to appoint an arbitrator, unless the parties provide otherwise. Although customers do not therefore usually select arbitrators directly, they do so indirectly by choosing to arbitrate among self-regulating organizations. Systematic arbitral bias is reduced in the competition among self-regulating organizations for the customer's business. Given that the parties have the arbitrator deciding the contract issue, contracting costs are lower when an arbitrator, rather than a court, also decides the scope issue. Hence, parties prefer to allocate the issue to arbitrators, unless they indicate otherwise.

184. See, e.g., Cogswell, 78 F.3d at 481.
185. See supra text accompanying notes 126-28.
188. See supra text accompanying note 64.
The contractarian approach provides strong arguments for some otherwise indefensible case law. It gives reasons for the default allocation of the scope issue, rather than simply asserting that the assignment is proper. The approach also avoids inconclusive or question-begging considerations. For instance, considering the question of section 15’s time bar as an issue of “arbitrability” is unhelpful because the results are indeterminate. Given a typically broad arbitration clause covering “all disputes” concerning investment securities, the customer’s particular claim against the brokerage firm is “arbitrable.” The dispute is not “arbitrable” when described as a “dispute involving an investment more than six years old.”

Because the contractarian approach allocates decision makers by their comparative incentive to make a biased decision concerning particular issues, not by the rules to be applied by decision makers, section 15’s time-bar is irrelevant to the allocation. Whether section 15 states a “procedural” or “substantive” rule also is irrelevant for the same reason. A contractarian approach determines arbitrability directly after the parties choose a decision maker, based on the likely incentives of arbitrators and courts in deciding the scope issue. Here the market mechanism by which arbitrators of securities disputes compete for fees is decisive.

C. Labor and Commercial Arbitration: The Charge of Conflation

Standard judicial practice now applies doctrines developed in labor arbitration to commercial arbitration. Commentators lament courts’ failure to keep the corpus of doctrine in the two areas distinct. The criticism is that labor and commercial arbitration are so different that indiscriminate use of doctrine is a mistake. At bottom, the charge is one of illegitimate conflation. The rationale for the allocation of the scope issue to arbitrators shows that the charge is overstated, for the allocation of the scope issue in commercial arbitration.

189. The Elahi court recognizes the point. See 87 F.3d at 596.
190. See, e.g., First Options of Chicago v. Kaplan, 514 U.S. 938, 946 (1995); National Union Fire Ins. Co. v. Belco Petroleum Corp., 88 F.3d 129, 133 (2d Cir. 1996) (presumption in favor of arbitration applies in commercial and labor contexts); Elahi, 87 F.3d at 594 n.6 (“Earlier, one might have doubted whether appellate decisions concerning labor arbitration would apply to commercial arbitration. Today, there is little question.”); cf. MACNEIL, supra note 67, at 57-58.
191. For a sampling of commentary noting and criticizing the phenomenon, see Shell, supra note 145, at 572-73, noting the courts’ misinterpretation of congressional intent regarding differences between commercial arbitration and labor arbitration, and Sternlight, supra note 77, at 653-54, 661 n.129, citing cases that fail to distinguish between labor and commercial arbitration.
192. See supra Part III.C.
cases is the same as its allocation in labor arbitration. Borrowing precedent on the matter found in labor arbitration therefore is appropriate. Conflation, where it occurs here, is justified.

Consider the matter of scope in labor arbitration. The law of labor arbitration combines two doctrines that in effect allocate the scope issue to the arbitrator. One doctrine is that courts determine the "arbitrability" of a dispute under an arbitration agreement. The other is that all doubts about an arbitration clause are to be resolved in favor of coverage. In combination, as a matter of labor arbitration, the doctrines effectively allocate the scope issue to the arbitrator. Since the same allocation is justifiably made in commercial arbitration, case support drawn from labor arbitration is unobjectionable. To be sure, labor and commercial arbitration have different salient characteristics. Labor arbitration typically involves collective bargaining agreements governing recurrent interactions between management and a union during the life of the agreement. Given the wide range of details covered by a collective bargaining agreement, it has the features of a relational contract. Labor arbitration also presents the prospect of agency costs induced by a divergence of interests between the employee and its representative. Commercial arbitration typically lacks the same salient features. But the question is not whether the two sorts of arbitration have different features. They clearly do. The question instead is whether mechanisms exist in both labor and commercial arbitration which control arbitral error based on bias in determining scope. There arguably are.

In commercial arbitration, competition for fees disciplines arbitrators. Parties purchase arbitrators’ services with some information about reputation and prior performance in dealing with arbitration clauses. Arbitrators failing to maximize the joint interests of the parties by exhibiting bias in deciding scope risk losing fees in the future. Here, arbitral reputation and some publication of arbitral awards are vehicles which transmit information about systematic arbitral bias. Such bias therefore is reduced. The comparable mechanism in labor arbitration may well be different. Given the length of a contract and the continuing relationship of the parties under it, arbitra-

193. See, e.g., supra text accompanying note 35. But see United Steelworkers v. Enterprise Wheel & Car Corp., 363 U.S. 593, 599 (1960) ("[The question of interpretation of the collective bargaining agreement is a question for the arbitrator."); United Steelworkers v. Warrior & Gulf Navigation Co., 363 U.S. 574, 585 (1960) (stating that "only the most forceful evidence of a purpose to exclude the claim from arbitration can prevail" where the arbitration clause is broad).

194. See Warrior & Gulf, 363 U.S. at 582-83 ("An order to arbitrate . . . should not be denied unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute.").
Central services can be required over the life of the contract. The risk of losing arbitral fees when administering the contract or a diminished reputation, or some combination of both, induces the arbitrator to maximize the gain to both parties over a lengthy period of time.\textsuperscript{195} The precise mechanism by which arbitral bias is controlled is not important here. The point is that, whatever the mechanism, arbitral bias is controlled in commercial arbitration as well. Moreover, it is the comparative absence of systematic arbitral bias, rather than a reduction by mechanism, that is important. Since systematic arbitral bias in deciding the scope issue is reduced in both labor and commercial arbitration, relevant doctrine in labor arbitration can be used in commercial arbitration. The migration of doctrine in judicial practice therefore is unobjectionable.

CONCLUSION

Nonmandatory commercial arbitration is governed by a stable and pervasive set of "second order" rules. They function to allocate decision-making authority over particular issues between courts and arbitrators. Discussion of the domestic and comparative law of commercial arbitration has centered on discrete substantive rules and mostly ignored the division of decision making at work in commercial arbitration. The concern mainly has been with standards of contractual performance, not the distribution of decisional authority between courts and arbitrators. Once put in focus, the division of decisional authority in commercial arbitration needs to be accounted for.

Contractual and regulatory approaches fail to explain the pattern of decisional allocations in commercial arbitration. Most of these decisional allocations can be accounted for in a recognizably contractarian fashion: as the allocation of issues to courts and arbitrators that affected parties prefer, given the likely incentives of courts and arbitrators. In commercial contexts, parties presumably prefer to minimize costs, including error costs resulting from decisional bias. This Article accounts for the allocation of existence, scope, and review issues on this basis.\textsuperscript{196} Of course, in noncommercial contexts, where concerns other than costs can dominate, party preference might dictate different decisional allocations. A different

\textsuperscript{195} Cf. Estreicher, supra note 69, at 759-60 (noting the need of a labor arbitrator to resolve disputes in a manner acceptable to parties in order to "keep busy in this field"); Julius G. Getman, Labor Arbitration and Dispute Resolution, 88 Yale L.J. 916, 929 (1979) ("Arbitrators whose decisions over time accurately reflect the priorities of the parties are [more] likely to maintain and enhance their acceptability.").

\textsuperscript{196} See supra Part III.
contractarian account, with a different specification of the selection of decision maker, might be needed. The contractarian approach is limited to commercial settings. The important point throughout obviously is not lexicographic: whether the approach is properly labelled as "contractarian." It is that the approach described is defensible and illuminates statutory and doctrinal rules, and case law results.