Against the Tide: The Role of "Commerce" in the Applicability of the FAA

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Over the past few years, the buzz in the arbitration world has been the Supreme Court's expansive view of the preemptive reach of section 2 of the Federal Arbitration Act. Most recently, as anyone who follows trends in this area knows, the Court all but did away with the notion of "effective vindication" of a plaintiff's statutory rights. *See American Express Co. v. Italian Colors Restaurant*, 2013 WL 3064410, *5 (June 20, 2013). *Italian Colors* is the latest in a long line of decisions beginning with *Southland Corp. v. Keating*, 465 U.S. 1 (1984), in which the Supreme Court held that the FAA mandate to undo the judicial prejudice to arbitration applies to state as well as federal courts. Before *Italian Colors*, the Court's last major decision, *AT&T Mobility v. Concepcion*, 131 S.Ct. 1740 (2011), held that the FAA preempts state laws that presumptively invalidate arbitration agreements.

Given the Court's expansive view of the FAA's scope, the recent decision from a New York state court in Nassau County – *Schiffer v. Slomin's Inc*. – comes as a surprise. S.C.-003102-12, 2013 WL 23214 (Nassau Cty 1st Dist., June 26, 2013). In that decision, the court held that an arbitration provision in a contract for an alarm and security system was *not* enforceable because it conflicts with New York's General Business Law § 399-c, which prohibits the use of arbitration clauses in contracts for the sale or purchase of consumer goods.

The *Schiffer* court was fully cognizant of the Supreme Court's teachings on the subject of FAA preemption, citing *Concepcion* and *Italian Colors* as well as two *per curiam* decisions, *Marmet Health Care Center, Inc. v. Brown*, 132 S.Ct. 1201 (2012), and *Nitro-Lift Tech. LLC v. Howard*,[1] 133 S.Ct. 500 (2012), in which the Supreme Court remanded decisions denying motions to compel arbitration in light of *Concepcion*. In *Marmet*, the West Virginia Supreme Court of Appeals refused to enforce an arbitration agreement that required claimants to arbitrate personal injury and wrongful death claims against nursing homes. According to the West Virginia court, state law invalidated pre-dispute arbitration agreements in such cases. The nursing home appealed to the United States Supreme Court, which vacated and remanded the decision. In doing so, the Court admonished the West Virginia court, noting that "[w]hen this court has fulfilled its duty to interpret federal law, a state court may not contradict or fail to implement the rule so established." *Marmet*, 132 S.Ct. at 1202 (internal citation omitted).

Despite the Supreme Court's reproval in Marmet and its unequivocal mandate that the FAA preempts state law, the Nassau County court nonetheless bucked the tide by refusing to enforce an arbitration

[1] In *Nitro-Lift*, the Supreme Court held, *inter alia*, that the Oklahoma Supreme Court, in reversing a decision dismissing an action against an employer on the ground that noncompetition agreements at issue were null and void, had usurped the arbitrator's jurisdiction.

provision based on state law grounds. The court's rationale is a thoughtful one, although likely quixotic. It harkens back to the principles articulated in 1995 in *Allied-Bruce Terminix, Cos., Inc. v. Dobson*, 513 U.S. 265 (1995).[2] In that case involving a termite prevention agreement for a residence, the Supreme Court held that an arbitration provision was enforceable because it "involved" commerce and thus fell under section 2 of the FAA, which enforces arbitration provisions in any "contract evidencing a transaction involving commerce . . . ." *Id*. at 273. In reaching its decision, the Supreme Court held that the phrase "involving commerce" should be given the broadest possible meaning, "indeed the functional equivalent of 'affecting'" commerce. *Id*.

The agreement at issue in *Schiffer* for a residential security system would seem to be analogous to the termite prevention agreement in *Allied-Bruce Terminix*; both agreements were sold by companies with a national presence; both were for a residence; and both were for a one-time installation by a local provider that would require ongoing service by the parent company. Indeed, in the case of Slomin's, the provider in *Schiffer*, in all likelihood the security monitoring would occur at a phone center outside New York state, although the decision does not address this issue. Nonetheless, the court in *Schiffer* held that the arbitration provision in the Slomin's agreement was unenforceable in light of New York's General Business Law because the agreement did "'not affect interstate commerce' as that term has been defined and applied by the United States Supreme Court and the New York Court of Appeals . . . ." 2013 WL 3285605 at * 7. Indeed, the court found that this was a local transaction:

> The singular transaction here of a Nassau County homeowner/consumer, and who purchases goods which will be installed and utilized in a security system for his or her protection personal and property at the residence, is not a transaction within the flow of interstate commerce.

Although the *Schiffer* decision is unlikely to withstand scrutiny if appealed it raises an interesting issue: are there some contracts that are of such local origin that they are *not* within the FAA's reach? The core issue, of course, is whether consumer contracts are exempt from arbitration on these grounds. In all likelihood they are not given the global nature of consumer goods. At minimum, however, the decision raises a possible ground for plaintiffs' counsel to consider when trying to find a way to escape the long arm of arbitration that the Supreme Court has found to exist in the FAA.

[2] Justice Scalia vigorously dissented from the majority's opinion in *Allied-Bruce,* but warned that he would "not in the future dissent from judgments that" were founded on *Southland*. *Allied-Bruce*, 513 U.S. at 285. He has been true to his word as seen in *Italian Colors*, which Justice Scalia drafted for the majority.

About the Author

Ms. McCallion is partner in the firm's Litigation and Arbitration practice group. She has substantial trial and arbitration experience and has litigated a broad array of complex commercial disputes, with an emphasis on products liability, patent and trademark litigation, and international arbitration. Ms. McCallion is a member of the firm's Diversity Committee. She formerly practiced with the Debevoise & Plimpton LLP. She is a graduate of Yale Law School, where she served as a Lead Editor of the Yale Journal on Regulation.

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