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Arbitration of Claims of Contract Unconscionability

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ARBITRATION OF CLAIMS OF CONTRACT UNCONSCIONABILITY

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SYNOPSIS

Q: There is a strong public policy against enforcement of unconscionable contracts and contractual provisions. There is a strong public policy favoring arbitrability of commercial disputes. Should a party to a contract providing for arbitration of all disputes arising out of the contract or relating thereto be compelled to arbitrate a claim that the contract or any provision thereof is unconscionable?

A: If the parties knowingly and willingly agreed to arbitrate any dispute arising out of or relating to their contract, any claim that the contract or any provision thereof is unconscionable should be determined by the arbitrators and not the courts.

PREFACE

In 1969 the New York Court of Appeals unanimously held that an arbitrator has the power, analogous to the power of a court acting pursuant to U.C.C. §2-302, to decline to enforce a provision he deems unconscionable even though that provision is contained in the contract from which he derives his jurisdiction.[1] Indeed, while the majority of four judges held that in such circumstances the arbitrator must indicate in his award that he has deliberately

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1. Granite Worsted Mills, Inc. v. Aaronson Cowen, Ltd., 25 N.Y.2d 451, 255 N.E.2d 168, 171, 306 N.Y.S.2d 934, 939 (1969).

ignored a contractual provision on grounds of unconscionability, the three-judge minority thought that even that requirement constituted unwarranted interference with the arbitrator's authority.

This decision seemed consistent with a general trend of increasing judicial hospitality towards arbitration of commercial disputes. Thus, only two years earlier the United States Supreme Court had held that where a valid agreement to arbitrate exists, all other issues, even a claim that the contract containing the arbitration clause (but not the arbitration clause itself) was induced by fraud, are for the arbitrators to determine.[2]

On August 16, 1978, however, the United States Court of Appeals for the Second Circuit held that where a party to a contract claims that one of its clauses is unconscionable, the court must first receive evidence and determine the issue of unconscionability before it can give effect to the arbitration clause contained in the contract.[3] This decision naturally caused wide consternation within the arbitration bar, since it seemed to signal a possible return to an earlier age marked by judicial hostility to arbitration. This concern was heightened by the fact that only one month earlier the New York Court of Appeals, the highest court of the state which has traditionally been most hospitable to arbitration, rendered a decision holding that "the inclusion of an arbitration agreement materially alters a contract for the sale of goods, and thus, pursuant to [U.C.C.] Section 2-207(2)(b), it will not become a part of such a contract unless both parties explicitly agree to it."[4] It seemed as if the Dark Ages were about to return.

The New York Court of Appeals "material alteration" decision has in fact had a widespread and deleterious effect on arbitration practice, compelling many parties to go to court with disputes which had theretofore been arbitrable.[5] The Second Circuit opinion cited above has not had a similar effect for the reason that on July 19, 1979, the Second Circuit had second thoughts and, on reargument, reversed and held (2-1) that the issue of unconscionability should be sent to the arbitrators.[6] The majority adopted the procedure which had been mandated by the

2. Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395, 402 (1967). The New York Court of Appeals brought New York into line with this principle in Weinrott v. Carp, 32 N.Y.2d 190, 298 N.E.2d 42, 47, 344 N.Y.S.2d 848, 855-56 (1973). *Accord,* Stateside Machinery Co., Ltd. v. Alperin, 591 F.2d 234 (3d Cir. 1979).

3. Farkar Co. v. R.A. Hanson Disc, Ltd., 583 F.2d 68, 72 (2d Cir. 1978).

4. Marlene Indus. Corp. v. Carnac Textiles, Inc., 45 N.Y.2d 327, 333, 380 N.E.2d 239, 242, 408 N.Y.S.2d 410, 413 (1978).

5. *See* Houston, *A Barrier to Arbitration in the Textile Industry,* 34 Arb. J. 9 (1979).

6. Farkar Co. v. R. A. Hanson Disc, Ltd., 604 F.2d 1 (2d Cir. 1979).

New York Court of Appeals in 1969 and instructed the District Court to "direct the arbitrators to be bound by the limitation of damages provision unless in a separate determination expressed in the award they find the provision to be unconscionable within the meaning of U.C.C. §§2-302, 2-719."[7] Circuit Judge Moore would not even go that far and strongly dissented on the ground that U.C.C. § 2-302 commences: "if the court as a matter of law finds. . . ."[8] Judge Moore also noted that "[b]efore a contract is submitted to arbitration the nature and the extent of the contract must be known. These cases are uniform in holding that this determination must be made by the court."[9]

As the synopsis of this article suggests, it is here submitted that the New York Court of Appeals in 1969 was correct in holding that a claim of unconscionability should be determined by the arbitrators appointed under a broad arbitration clause and that the United States Court of Appeals for the Second Circuit was correct in 1979 in reconsidering and reversing its 1978 decision.

I. THE PUBLIC POLICY AGAINST ENFORCEMENT OF UNCONSCIONABLE CONTRACTS

A. COMMON LAW BACKGROUND

At common law, notwithstanding universal support for "freedom of contract," courts sometimes found ways of declining to enforce contracts which were so onesided as to "offend the conscience." Inadequacy of consideration was naturally the most obvious indication of unfairness, but the courts usually required some additional element showing unfair dealing by a party with overwhelming strength on one side against a party suffering from debilitating weakness on the other. For example, during the first generation of our independent jurisprudence Chancellor Kent, one of the greatest of our legal theoreticians, held "[t]here is no case where mere inadequacy of price, independent of other circumstances, has been held sufficient to set aside a sale made between parties standing on equal ground, and dealing with each other without any imposition or oppression."[10]

A century and a quarter later the fifth edition of Pomeroy's

7. *Id.* at 2.
8. *Id.* at 3.
9. *Id.*
10. Osgood v. Franklin, 2 Johns. Ch. 1, 23 (new York 1816), *aff'd.* 14 Johns. 527 (1817).

classic EQUITY JURISPRUDENCE merely elaborated upon Kent's formulation:

> If there is nothing but mere inadequacy of price, the case must be extreme, in order to call for the interposition of equity. . . . When the accompanying incidents are inequitable and show bad faith, such as concealments, misrepresentations, undue advantage, oppression on the part of the one who obtains the benefit, or ignorance, weakness of mind, sickness, old age, incapacity, pecuniary necessities, and the like, on the part of the other, these circumstances, combined with inadequacy of price, may easily induce a court to grant relief, defensive or affirmative.[11]

By these formulations, two elements must be present before a court will relieve a party from his contractual commitments: (1) gross inadequacy of consideration and (2) unfairness in dealing. The first element, which has been called "substantive unconscionability," did not suffice without the presence also of the second element, "procedural unconscionability."[12] The New York Court of Appeals in this regard has held as follows:

> Ordinarily, the signer of a deed or other instrument, expressive of a jural act, is conclusively bound thereby. That his mind never gave assent to the terms expressed is not material [citation omitted]. If the signer could read the instrument, not to have read it was gross negligence; if he could not read it, not to procure it to be read was equally negligent; in either case the writing binds him. . .
>
> [However,] [i]f the signer is illiterate, or blind, or ignorant of the alien language of the writing, and the contents thereof are misread or misrepresented to him by the other party, or even by a stranger, unless the signer be negligent, the writing is void.[13]

Examples of similar statements by the most impressive authorites could be multiplied almost without end. But in fact, it was always the inadequacy of consideration which shocked the

11. 3 C. POMEROY, EQUITY JURISPRUDENCE § 928 at 639-42 & nn.1-3 (5th ed. 1941).
12. *See, e.g.*, Christianson Bros., Inc. v. State of Washington, 90 Wash.2d 782, 586 P.2d 840 (1978); Schroeder v. Fageol Motors, Inc., 86 Wash.2d 256, 544 P.2d 20 (1975).
13. Pimpinello v. Swift & Co., 253 N.Y. 159, 162-63, 170 N.E. 530, 531 (1930).

conscience of a court willing to relieve a party of his contractual commitments. After all, if the price were fair, the inequality of the parties' bargaining position would not matter. By the same token, if the price were grossly disproportionate to the thing being exchanged, why should the apparent positions of the parties matter? At civil law, indeed, there developed a doctrine called *laesio enormis* whereby a party could rescind a contract which gave him less than half of the value of his property being exchanged.[14]

At common law, however, "freedom of contract" was accorded great rhetorical respect. Therefore, a court could not decline to enforce a contract "merely" because it was grossly unfair. There had to be some additional element, some aspect of procedural unfairness, of bad faith in dealing. In practice, this put a great premium on judicial creativity, what Karl Llewellyn called "intentional and creative misconstruction."[15] The result, according to Llewellyn, was that the courts failed to:

> face the issue, they fail[ed] to accumulate either experience or authority in the needed direction: that of marking out for any given type of transaction what the *minimum decencies* are which a court will insist upon as essential to an enforceable bargain of a given type, or as being inherent in a bargain of that type.[16]

The author of a recent treatise on the Uniform Commercial Code stated that "[f]or better or for worse, the court loath to limit the exercise of freedom [of contract] directly did so by engaging in a dangerous word game to achieve the same result. The objective was laudable; the method of achieving it, deplorable."[17] A good example of this practice is the leading modern pre-Code case, *Campbell Soup Co. v. Wentz.*[18] It is cited in every discussion of the pre-Code doctrine of unconscionability for the proposition that more than mere inadequacy of consideration was necessary. But in fact, notwithstanding what the *Campbell* court *said,* nothing but inadequacy of consideration was present.

The defendant-farmer had sold to Campbell his entire crop of a certain type of carrots for future delivery. The contract price was

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14. *See,* Dawson, *Economic Duress and the Fair Exchange in French & German Law,* 11 TUL. L. REV. 345, 364-70 (1937).
15. Llewellyn, Book Review, 52 HARV. L. REV. 700, 703 (1939).
16. *Id.*
17. I. QUINN, UNIFORM COMMERCIAL CODE COMMENTARY & LAW DIGEST 2-96 (1978).
18. 172 F.2d 80 (3rd Cir. 1948).

$30 a ton but at the time delivery was due the market price had risen to $90 a ton. The farmer thereupon sold the carrots to someone else and Campbell sued for specific performance. The court agreed that Campbell was entitled to equitable relief (it found that Campbell needed the carrots and that they were unobtainable in the market) except for one thing - "the sum total of its provisions [referring to the contract between the parties, which was on Campbell's standard printed form] drives too hard a bargain for a court of conscience to assist."[19]

But the "hard" provisions cited by the court, such as one restricting the farmer's disposition of carrots which might be rejected by Campbell's, had nothing to do with the case, which involved nothing more than one party's refusal to deliver goods for an agreed price after the market for that commodity had risen substantially above what it had been on the day of contracting. The court did not even find that the price was unreasonable when the contract was entered into. Nor did it condone the farmer's breach. Nevertheless, the court held as follows:

> We are not suggesting that the contract is illegal. Nor are we suggesting any excuse for the grower in this case who has deliberately broken an agreement entered into with Campbell. We do think, however, that a party who has offered and succeeded in getting an agreement as tough as this one is, should not come to a chancellor and ask court help in the enforcement of its terms. That equity does not enforce unconscionable bargains is too well established to require elaborate citation.[20]

It seems clear that the conscience of the *Campbell* court was shocked by the inadequacy of the consideration (one-third of the actual value of the goods being exchanged) but felt obliged to indulge in "creative misconstruction" to satisfy the judicial proprieties.

B. THE UNIFORM COMMERCIAL CODE

According to a New York appellate court "the conclusion is inescapable that the Uniform Commercial Code [§2-302] simply codified the doctrine [of unconscionability], which was used by the

19. Campbell Soup Co. v. Wentz, 172 F.2d 80, 84 (3rd Cir. 1948).
20. *Id.* at 83.

commonlaw courts to invalidate contracts under certain circumstances."[21] That was very true. Moreover, the drafters of the Code cut through the rhetoric of the judicial doctrine of unconscionability and focused on what the courts actually *did.* Thus the drafters of the Code virtually ignored procedural unconscionability and made the only test the fairness of the bargain itself. Indeed, procedural unconscionability is not even mentioned in U.C.C. §2-302, which provides in full as follows:

> (1) If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid an unconscionable result.
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> (2) When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose and effect to aid the court in making the determination.

Nevertheless, the courts continued to talk about unequal bargaining power, unfair dealing, and the like. A comparison of a case decided immediately prior to passage of the U.C.C. with two cases decided after adoption of the U.C.C., is revealing. In *Williams v. Walker-Thomas Furniture Co.,*[22] the plaintiff-customer was a woman on relief, separated from her husband, with seven children. The retailer-defendant belonged to that all too numerous species known as the common ghetto parasite. Mrs. Williams had purchased *and paid for* a considerable quantity of furniture over several years but when she defaulted on a payment for a stereo set, the store took *everything* back under an add-on provision in the sales contract for the stereo set. The trial court expressed its condemnation of the store's conduct but thought that it had no power to refuse to enforce even "such exploitative contracts."[23] The Circuit Court disagreed and held the following:

> But when a party of little bargaining power, and hence

21. Matter of Friedman, 64 A.D.2d 70, 84, 407 N.Y.S.2d 999, 1007 (1978).
22. 198 A.2d 914 (D.C. Ct. App. 1964), *remanded,* 350 F.2d 445 (D.C. Cir. 1965).
23. Williams v. Walker-Thomas Furniture Co., 198 A.2d 914, 916 (D.C. Ct. App. 1964), *remanded,* 350 F.2d 445 (D.C. Cir. 1965).

> little real choice, signs a commercially unreasonable contract with little or no knowledge of its terms, it is hardly likely that his consent, or even an objective manifestation of his consent, was ever given to all the terms. In such a case the usual rule that the terms of the agreement are not to be questioned should be abandoned and the court should consider whether the terms of the contract are so unfair that enforcement should be withheld.[24]

In *Frostifresh Corp. v. Reynoso,*[25] decided less than two years after the U.C.C. became effective in New York, the court declined to enforce a retail installment contract requiring the purchaser to pay a total of $1,145.88 for a refrigerator which had cost the dealer $348.00, where the customer spoke only Spanish and was tricked into signing an English-language contract by a Spanish-speaking salesman.[26] Similarly, in *Jones v. Star Credit Corp.*[27] the court held that an installment sales contract calling for payment of a total of $1,439.69 for a freezer having a maximum *retail* value of $300.00 was unconscionable where the purchasers were welfare recipients who had already paid $619.88 for the $300.00 freezer. The court held the following:

> On the one hand it is necessary to recognize the importance of preserving the integrity of agreements and the fundamental right of parties to deal, trade, bargain, and contract. On the other hand there is the concern for the uneducated and often illiterate individual who is the

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24. 350 F.2d at 449-50. Before the circuit court rendered its decision, Congress passed the U.C.C. for the District of Columbia. However, the circuit court held that the common law was adequate to the task and enunciated the applicable common law principles in the language quoted above. *Id.* at 448-49.

25. 52 Misc.2d 26, 274 N.Y.S.2d 757 (1966), *rev'd on other grounds,* 54 Misc.2d 119, 281 N.Y.S.2d 964 (App. Term 1967).

26. Frostifresh Corp. v. Reynoso, 52 Misc.2d 26, 274 N.Y.S.2d 757 (1966), *rev'd on other grounds,* 54 Misc.2d 119, 281 N.Y.S.2d 964 (1967). The trial court gave the dealer only $348 but its decision was modified to add reasonable profit and freight and finance charges, 54 Misc.2d 119, 281 N.Y.S.2d 964 (App. Term 1967). *See also,* Brooklyn Union Gas Co. v. Jimeniz, 82 Misc.2d 948, 371 N.Y.S.2d 289 (Civil Ct. 1975); Graziano v. Tortora Agency, Inc., 78 Misc.2d 1094, 359 N.Y.S.2d 489 (Civil Ct. 1974); Albert Merrill School v. Godoy, 78 Misc.2d 647, 357 N.Y.S.2d 378 (Civil Ct. 1974); Educational Beneficial, Inc. v. Reynolds, 67 Misc.2d 739, 324 N.Y.S.2d 813 (Civil Ct. 1971); Milford Finance Corp. v. Lucas, 8 U.C.C. Rep. 801 (Mass. App. Div. 1970). *Cf.,* Johnson v. Mobil Oil Corp., 415 F. Supp. 264 (E.D. Mich. 1976) (a "practically illiterate" party was permitted to avoid a contractual exclusion of consequential damages, even though he had never advised Mobil that he couldn't read). In reaching this decision the court took note of Mobil's "immense bargaining power." *Id.* at 269.

27. 59 Misc. 2d 189, 298 N.Y.S.2d 264 (Sup. Ct. 1969).

> victim of gross inequality of bargaining power, usually the poorest members of the community.[28]

But was the status and condition of the disadvantaged party really necessary to the decision in any of these three cases — the one decided without benefit of UCC § 2-302 and the two with? Are not the courts really holding only that a gross discrepancy in the value of things exchanged creates a *presumption* of unfair dealing and-or unequal bargaining power? The Surrogate of New York County was surely correct when he noted the following:

> The courts do, however, look to the adequacy of the consideration in order to determine whether the bargain provided for is grossly unreasonable or unconscionable [citation omitted]. Thus, where inequality of the bargain is so gross there is an inference that it was in some way improperly obtained and is unconscionable [citations omitted].[29]

C. APPLICABILITY TO COMMERCIAL TRANSACTIONS

The cases mentioned above involved retail consumer transactions where the retailer was in effect charged with quasi-fiduciary obligations to his customers.[30] This of course raises a different issue — indeed, virtually a diametrically opposite issue — from a commercial transaction between business entities

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28. Jones v. Star Credit Corp., 59 Misc. 2d 189, 190, 298 N.Y.S.2d 264, 265. (Sup. Ct. 1969). *See also* Steiner v. Mobil Oil Corp., 20 Cal. 3d 90, 569 P.2d 751, 141 Cal. Rptr. 157, (1977); Christiansen Bro., Inc. v. State of Washington, 90 Wash. 2d 872, 586 P.2d 840 (1978); Schroeder v. Fageol Motors, Inc., 86 Wash. 2d256, 544 P.2d 20 (1975); Toker v. Perl, 103 N.J. Super. 500, 247 A.2d 701 (Law Div. 1968); *aff'd,* 108 N.J. Super. 129, 260 A.2d 244 (App. Div. 1970); Toker v.-Westerman, 113 N.J. Super. 452, 274 A.2d 78 (Dist. Ct. 1970); Walsh v. Ford Motors Co., 59 Misc. 2d 241, 298 N.Y.S.2d 538 (Sup. Ct. 1969); Central Budget Corp. v. Sanchez, 53 Misc. 2d 620, 279 N.Y.S.2d 391 (Civil Ct. 1967); Electronics Corp. of America v. Lear Jet Corp., 55 Misc. 2d 1066, 286 N.Y.S.2d 711 (Sup. Ct. 1967). *Cf.* Matter of Anna D., N.Y.L.J., Sept. 5, 1979, at 11, col. 2 [not officially reported] (New York City Family Court) where the Department of Social Services sought to transfer the custody and care of a minor child under a "Voluntary Placement Agreement" written in the English language and signed by parents who read only Italian. Moreover, to the extent that a department agent attempted to explain the effect of the document to the parties (in English, the agent spoke no Italian) the court found that her explanations were probably misleading. Under these circumstances, the court held that no binding contract existed.

29. In Re Estate of Vought, 70 Misc. 2d 781, 788, 334 N.Y.S.2d 720, 728 (Surr. Ct. 1972. *But see* Mandel v. Liebman, 303 N.Y. 88, 100 N.E.2d 149 (1951).

30. *Cf.* State of New York v. ITM, Inc., 52 Misc. 2d 39, 275 N.Y.S.2d 303 (Sup. Ct. 1966) where the state succeeded in enjoining retailers from selling appliances at unconscionable prices and by deceptive means. *See also* M. BENFIELD, NEW APPROACHES IN THE LAW OF CONTRACTS (1970) and the burgeoning materials on consumer law. It will be recalled that Dante assigned violators of fiduciary obligations to the lowest circle of his Inferno.

presumably dealing at arms length. But the courts also apply the unconscionability doctrine to commercial transactions.

For example, in *Electronics Corp. of America v. Lear Jet Corp.*[31] Lear's local distributor sold an aircraft to Chandler Leasing Corp., which financed the purchase by mortgaging the aircraft to an insurance company and also assigning to the insurance company the lease between Chandler and plaintiff. The aircraft did not work and the plaintiff returned it to Lear, which retained possession. The lease contained an express exclusion of all warranties. The court, noting an apparent close relationship between Lear and Chandler, held that the warranty exclusion provision might be unconscionable and denied Chandler's motion for summary judgment.[32] Similarly, in *Industralease Automated & Scientific Equip. Corp. v. R.M.E. Enterprises, Inc.*[33] the defendant operated a picnic grove and leased from plaintiff two incinerators which never worked. Plaintiff sued for lease payments and invoked the warranty disclaimer contained in the lease. The court held that the disclaimer was unconscionable in the circumstances of the case and affirmed a defendant's verdict.[34]

In *Sinkoff Beverage Co., Inc. v. Jos. Schlitz Brewing Co.*[35] the court denied relief, not on the ground that the unconscionability defense was not available to a business entity, but rather on the ground that the contract provision was not unconscionable.[36] Sinkoff had been the exclusive distributor for Schlitz beer in Suffolk County, New York, for six years under a contract permitting either party to cancel at any time. Schlitz cancelled on short notice and Sinkoff moved to enjoin it from selling beer to anyone else in Suffolk County, claiming that the termination-at-will provision was unconscionable. The court reviewed the background of the relationship between the parties, held that the termination was not unconscionable, and denied Sinkoff's motion for a preliminary injunction.[37]

A recent case in the United States District Court for the Southern District of New York does indicate that the courts may

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31. 55 Misc. 2d 1066, 286 N.Y.S.2d 711 (Sup. Ct. 1967).

32. Electronics Corp. of America v. Lear Jet Corp., 55 Misc. 2d 1066, ____, 286 N.Y.S.2d 711, 714 (Sup. Ct. 1967).

33. 58 A.D.2d 482, 396 N.Y.S.2d 427 (App. Div. 1977).

34. Industra lease Automated & Scientific Equip. Corp. v. R.M.E. Enterprises, Inc., 58 A.D.2d 482, ____, 396 N.Y.S.2d 427, 427-28 (App. Div. 1977).

35. 51 Misc. 2d 446, 273 N.Y.S.2d 364 (Sup. Ct. 1966).

36. Sinkoff Bev. Co., Inc. v. Jos. Schlitz Brewing Co., 51 Misc. 2d 446, ____, 273 N. Y.S. 2d 364, 367 (Sup. Ct. 1966).

37. *Id. See Also* County Asphalt, Inc. C. Lewis Welding & Eng'r Corp., 444 F.2d 372 (2d Cir), *Cert. denied,* 404 U.S. 939 (1971).

require a more egregious violation of contractual morality where the complaining party is a large corporation. In *Fleischmann Distilling Corp. v. Distillers Co., Ltd.*[38] the plaintiffs were parties to distributor contracts with defendants, United Kingdom corporations which controlled the applicable markets for Scotch whiskey. Plaintiffs complained that the termination provisions in the distributor contracts were unreasonably short and resulted from the defendant's overwhelmingly superior bargaining power (if plaintiffs wanted to deal in Scotch, they had to deal with defendants).[39] The court denied relief, in holding "'[t]hough a commercial setting does not necessarily bar a claim of procedural unconscionability, 'it is the exceptional commercial setting where a claim of unconscionability will be allowed' [citation omitted], particularly where the cries of unconscionability are made by large corporations [citations omitted].'"[40]

In any event, it is clear that the defense of unconscionability[41] is available to business entities engaged in commercial transactions.

II. ARBITRATION OF CLAIMS OF CONTRACT UNCONSCIONABILITY

A. INTRODUCTION TO COMMERCIAL ARBITRATION

Commercial arbitration involves the resolution of business-related disputes outside the regular judicial structure by lay judges who are not bound by the forms of law and whose decisions are generally non-reviewable (except where corruption exists or as a result of certain procedural errors).[42]

Arbitration is almost always a creature of contract.[43] It is

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38. 395 F. Supp. 221 (S.D.N.Y. 1975).

39. Fleischmann Distilling Corp. v. Distillers Co. Ltd., 395 F. Supp. 221, 229 (S.D.N.Y. 1975).

40. *Id.* at 233. *Cf.* the refusal to let corporations assert the defense of usury, which comparison was made by the court in Whitestone Credit Corp. v. Barbory Realty Corp., 5 U.C.C. Rep. 176 (N.Y. Sup. Ct. 1968). It is interesting to note that Art. 138,2 of the German Civil Code, the counterpart to U.C.C. §2-302, is commonly referred to as the usury provision of the Code although like U.C.C. §2-302 it is much broader than the traditional concept of usury. Dawson, *Unconscionable Coercion: The German Version,* 89 HARV. L. REV. 1041, 1053 (1976).

41. It should be noted that U.C.C. §2-302 is purely defensive; restitution cannot be ordered by the Court under that section. *See* Von Lehn v. Astor Art Galleries, Ltd., 86 Misc. 2d 1, 380 N.Y.S.2d 532 (Sup. Ct. 1976). Similarly, no damages are recoverable by the injured party under U.C.C. §2-302. *See* Pearson v. National Budgeting Systems, Inc., 31 A.D.2d 792, 297 N.Y.S.2d 59 (1969).

42. The fullest survey of the law of commercial arbitration is M. DOMKE, COMMERCIAL ARBITRATION (1968 & Supp.). For a discussion of the law and practice of commercial arbitration, see G. GOLDBERG, A LAWYER'S GUIDE TO COMMERCIAL ARBITRATION (ALI 1977). *See also* AMERICAN MANAGEMENT ASSOCIATION, RESOLVING BUSINESS DISPUTES (1965).

43. There are a few mandatory arbitration statutes, and an experimental program in the federal

possible to agree to arbitrate existing disputes in 48 states.[44] Agreements to arbitrate future disputes are enforceable under the laws of 35 states.[45] Where interstate, international or maritime commerce is involved, it may also be possible to enforce an agreement to arbitrate under the United States Arbitration Act.[46] However, certain categories of commercial disputes have been held to be non-arbitrable, regardless of any agreement between the parties. For example, a claim that a contract is void for usury raises an issue for courts and not arbitrators regardless of any arbitration clause contained in the agreement claimed to be usurious.[47] Similarly, where performance is rendered illegal by federal regulation, such as price controls, arbitration is barred.[48] Particularly pertinent to our inquiry are those circumstances where a contract is not claimed to be illegal but the dispute raises issues which so impinge upon important public policies that the courts have insisted that they retain exclusive jurisdiction over them. Thus a serious defense under the federal securities laws[49] or the antitrust laws[50] removes a case from arbitration, as does a claim of patent invalidity;[51] and where the welfare of children is concerned the courts will not relinquish their role as *parens patriae* to any

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courts for compulsory (but non-binding) arbitration of certain disputes, but these need not concern us here.

44. The two states which do not allow such arbitration agreements are Oklahoma and Vermont.

45. In North Dakota an agreement to arbitrate is not specifically enforceable. N.D. CENT. CODE § 32-04-12(3) (1976). In the following states an agreement to arbitrate can be enforced specifically: ALASKA STAT. §09.43.010 (1973); ARIZ. REV. STAT. ANN. §12-1501 (1962); ARK. STAT. ANN. §34-502 (1962); CAL. CIV. PRO. CODE §1281 (West 1972); COLO. REV. STAT. ANN. §13-22-201 (1975);- CONN. GEN. STAT. REV. §52-408 (1960); DEL. CODE ANN. tit. 10, §5701 (1974); FLA. STAT. ANN. §682.02 (Supp. 1979); HAWAII REV. STAT. §658-1,2 (1976); IDAHO CODE §7-901 (1979); ILL. ANN. STAT. Ch. 10, §101 (Smith-Hurd 1975); IND. CODE §34-4-2-1 (Burns 1973); KAN. STAT. ANN. §5-401 (1975); LA. REV. STAT. ANN. §9:4201 (West 1951); ME. REV. STAT. ANN. tit. 14 §5927 (Supp., 1979); MD. CTS. & JUD. PRO. CODE ANN. §3-206 (1974); MASS. ANN. LAWS ch. 251, §1 (Supp. 1979); MICH. STAT. ANN. §600.5001 (1968); MINN. STAT. ANN. §572.08 (Supp. 1979); NEV. REV. STAT. §38.035 (1973); N.H. REV. STAT. ANN. §542:1 (1974); N.J. STAT. ANN. §2A:24-1 (1952); N.M. STAT. ANN. §44-7-1 (Supp. 1978); N.Y. CIV. PRAC. §7501 (McKinney 1963); N.C. GEN. STAT. §1-567.1,2 (Supp. 1975); OHIO REV. CODE ANN. §2711.01 (Anderson Supp. 1978) formerly OHIO REV. CODE ANN. §2711.01 (Anderson 1953); ORE. REV. STAT. §33.210,220 (1977); PA. STAT. ANN. tit. 5, §161 (1963); R.I. GEN. LAWS ANN. §10-3-2 (Supp. 1978), *Amending* R.I. GEN. LAWS ANN. §10-3-2 (1970); S.D. COMPILED LAWS ANN. §21-25A-1, 3 (Interim Supp. 1978); TEX. REV. CIV. STAT. ANN. art. 224 (1973); VA. CODE ANN. §8-503(b) (Supp. 1979); WASH. REV. CODE ANN. §7.04.010 (1961); WIS. STAT. ANN. §298.01 (1958); WYO. STAT. ANN. §1-36-101 (Interim Supp. 1977).

46. 9 U.S.C. §§ 1-14 (1978).

47. Durst v. Abrash, 22 A.D.2d 39, 253 N.Y.S.2d 351 (1964), *aff'd,* 17 N.Y.2d 455, 213 N.E.2d 887, 266 N.Y.S.2d 806 (1965).

48. Kramer & Uchitelle, Inc. v. Eddington Fabrics Corp., 288 N.Y. 467, 43 N.E.2d 493, *reh. denied.,* 289 N.Y. 649, 44 N.E.2d 622 (1942).

49. Wilko v. Swan, 346 U.S.427 (1953). But if the securities transaction involved international commerce, arbitration may be appropriate. Scherk v. Alberto-Culver Co., 417 U.S. 506, *reh. denied,* 419 U.S. 885 (1974).

50. Power Replacements, Inc. v. Air Preheater Co., 426 F.2d 980 (9th Cir. 1970); American Safety Equip. Corp. v. J.P. Maguire & Co., 391 F.2d 821 (2d Cir. 1968); Aimcee Wholesale Corp. v. Tomar Products, Inc., 21 N.Y.2d 621, 237 N.E.2d 223, 289 N.Y.S.2d 968 (1968).

51. Foster Wheeler Corp. v. Babcock & Wilcox Co., 440 F.Supp. 897 (S.D.N.Y 1977).

private forum.[52]

Arbitration may be conducted on an ad hoc basis, or before special arbitration tribunals connected with certain industries (such as securities and commodities), or under the auspices of the American Arbitration Association and its subsidiary tribunals (hereinafter referred to collectively as "AAA"). It is assumed in this article that the subject dispute is arbitrable under the Commerical Arbitration Rules of the AAA, although the same considerations will often apply to arbitration before other domestic arbitration tribunals.[53]

Under the Commercial Arbitration Rules of the AAA most disputes are heard by three arbitrators selected by the AAA in consultation with the parties. Normally one of the arbitrators will be selected from the claimant's industry division, one of the arbitrators will be selected from the respondent's industry division, and the third arbitrator will be selected from some other industry division. In any event, all three arbitrators are deemed and expected to be wholly impartial.[54]

After hearing all of the evidence submitted by the parties, usually at an oral hearing (although provision is made for written submission),[55] the arbitrators render a written award. The award identifies the parties and the contracts from which the arbitrators derive their jurisdiction and sets forth the relief, if any, granted to each of the parties. Written opinions giving reasons for the award are actively discouraged by the AAA and are very rarely rendered.

Most arbitration awards are complied with voluntarily by the parties who, after all, agreed to submit their disputes to arbitration. Where a party refuses to comply voluntarily with the award, or where it is desired for some other reason to reduce the award to judgment, provision is made for the confirmation of the award in a court of competent jurisdiction. While procedures for confirmation vary from state to state and court to court, in general some procedure akin to a motion for summary judgment is made available.

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52. Schneider v. Schneider, 17 N.Y.2d 123, 216 N.E.2d 318, 269 N.Y.S.2d 107 (1966); Agur v. Agur, 32 A.D.2d 16, 298 N.Y.S.2d 722 (1969), *appeal dismissed,* 27 N.Y.2d 643, 261 N.E.2d 903, 313 N.Y.S.2d 866 (1970); Sheets v. Sheets, 22 A.D.2d 176, 254 N.Y.S.2d 320 (1964); Lasek v. Lasek, 13 A.D.2d 242, 215 N.Y.S.983 (1961); Fence v. Fence, 64 Misc. 2d 480, 314 N.Y.S.2d 1016 (Family Ct. 1970); Michelman v. Michelman, 5 Misc. 2d 570, 135 N.Y.S.2d 608 (Sup. Ct. 1954).

53. No consideration is given here to arbitrations conducted under the auspices of the International Chamber of Commerce or any other international tribunal.

54. There is some question as to the impartiality of party-appointed arbitrators, an early form of arbitrator-selection still commonly used in maritime charter party contracts. *See, e.g.,* Petrol Shipping Corp. v. Kingdom of Greece, 360 F.2d 103 (2d Cir.), *cert. denied,* 385 U.S. 931 (1966).

55. Commercial Arbitration Rules of the AAA §36 as set out in G. GOLDBERG, A LAWYER'S GUIDE TO COMMERCIAL ARBITRATION, Appendix A (ALI 1977).

In any event, the scope of judicial review of arbitration awards is very limited. For example, in 1854 the United States Supreme Court held "[i]f the award is within the submission, and contains the honest decision of the arbitrators, after a full and fair hearing of the parties, a court of equity will not set it aside for error, either in law or fact."[56]

A myriad of courts, federal and state, have expressed similar opinions,[57] and indeed, the grounds for judicial vacatur of an arbitration award are extraordinarily uniform throughout the United States. There are in essence only four grounds for vacating an arbitration award:

(1) There was an undisclosed relationship between an arbitrator and a party or his counsel affecting the arbitrator's impartiality or appearance of impartiality;

(2) An arbitrator was corrupt;

(3) The arbitrators did not schedule or conduct the hearing in a fair and judicious manner;

(4) The arbitrators granted relief they were not authorized to grant under the contract pursuant to which the arbitration was held.

In other words, the only question the courts ask is: Were the procedural decencies respected? If the answer is yes, the award will usually be confirmed.

B. THE POWER OF THE ARBITRATORS

It is obvious that, if the courts are to defer the consideration of a claim of unconscionability to arbitrators, arbitrators must have the power to decline enforcement of unconscionable contracts or contract provisions. There is little question that arbitrators have such power.

Section 42 of the Commercial Arbitration Rules of the AAA provides in pertinent part that "[t]he Arbitrator may grant any remedy or relief which he deems just and equitable and within the

56. Burchell v. Marsh, 58 U.S. 344, 349 (1854).

57. *E.g.*, Newark Stereotypers' Union No. 18 v. Newark Morning Ledger Co., 397 F.2d 594 (3d Cir.), *cert. denied*, 393 U.S. 954 (1968); I/S Stavborg v. National Metal Converters, Inc., 500 F.2d 424 (2d Cir. 1974); Federal Commerce & Navigation Co. v. Kanematsu-Gosho, Ltd., 457 F.2d 387 (2d Cir. 1972); University of Alaska v. Modern Constr., Inc., 522 P.2d 1132 (Alaska Sup. Ct. 1974); Smitty's Super-Valu, Inc. v. Pasqualetti, 22 Ariz. App. 178, 525 P.2d 309 (1974); Verdex Steel & Constr. Co. v. Board of Supervisors, 19 Ariz. App. 547, 509 P.2d 240 (1973); Atlas Floor Covering v. Crescent House & Garden, Inc., 166 Cal. App. 2d 211, 333 P.2d 194 (Dist. Ct. App. 1958); Trustees of Boston & Maine Corp. v. Massachusetts Bay Transp. Auth., 363 Mass. 386, 294 N.E.2d 340 (1973); Wilkins v. Allen, 169 N.Y. 494, 62 N.E. 575 (1902); Fudickar v. Guardian Mut. Life Ins. Co., 62 N.Y. 392 (1873); Barlow v. Todd, 3 Johns. 367 (N.Y. Sup. Ct. of Judicature 1808).

scope of the agreement of the parties, including, but not limited to, specific performance of a contract."[58]

This has likewise been the holding of the courts. In a leading 1961 case the New York Court of Appeals held "[o]nce it be ascertained that the parties broadly agreed to arbitrate a dispute 'arising out of or in connection with' the agreement, it is for the arbitrators to decide what the agreement means and to enforce it according to the rules of law which they deem appropriate in the circumstances."[59]

Moreover, the courts have made it clear that arbitrators have inherent power to decline to enforce provisions they deem unconscionable, such as a contractual exclusion of consequential damages in a sales transaction. Indeed, this was the opinion of all seven judges of the New York Court of Appeals in the leading case in point.[60] Further, the courts have refused to limit the scope of an on-going arbitration and have refused to preclude arbitrators from considering a claim for a measure of damages expressly excluded by the subject contract. Thus it has been held that "parties, although purporting to be ready to proceed to arbitration, have been insistent upon obtaining review from the court, in advance of arbitration, of the area in which the arbitrators are to exercise their jurisdiction. This is improper."[61]

In essence, arbitrators can award virtually any kind of damages they deem appropriate, even where a court would be reversed for granting such relief. Thus it has been held "it begs the question to say that the arbitrators may award 'non-allowable' damages. 'Non-allowable' in this context means not allowable in an action at law as determined by the law of sales. Arbitrators are not so confined."[62]

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58. Commercial Arbitration Rules of the AAA § 42. *See supra* note 55.

59. Exercycle Corp. v. Maratta, 9 N.Y.2d 329, 334, 174 N.E.2d 463, 464, 214 N.Y.S.2d 353, 355 (1961). *See also* Spectrum Fabrics Corp. v. Main St. Fashions, Inc., 285 A.D. 710, 139 N.Y.S.2d 612, *aff'd* 309 N.Y. 709, 128 N.E.2d 416 (1955); Shevell v. Besen, 29 A.D. 2d 751, 287 N.Y.S.2d 340 (1968); Colletti v. Mesh, 23 A.D.2d 245, 260 N.Y.S.2d 130, *aff'd*, 17 N.Y.2d 460, 213 N.E.2d 894, 266 N.Y.S.2d 814 (1965); Bay Iron Works, Inc. v. Eisenstein, 17 A.D.2d 804, 232 N.Y.S.2d 746 (1962); Transpacific Transp. Corp. v. Sirena Shipping Co., 9 A.D.2d 316, 193 N.Y.S.2d 277 (1959), *aff'd*, 8 N.Y.2d 1048, 170 N.E.2d 391, 207 N.Y.S.2d 70 (1960).

60. Granite Worsted Mills, Inc. v. Aaronson Cowen, Ltd., 25 N.Y.2d 451, 255 N.E.2d 168, 306 N.Y.S.2d 934 (1969). Four of the judges thought the arbitrator should say in his award that he was deliberately disregarding the exclusionary provision on grounds of unconscionability while the other three judges thought he shouldn't have to say anything, but all seven judges agreed that the arbitrator had the power to refuse to enforce the provision excluding consequential damages if he found it unconscionable in the circumstances of the case before him. *Id.* at 457, 255 N.E.2d at 171, 306 N.Y.S. at 939.

61. Vogel v. Simon, 13 A.D.2d 725, ____, 214 N.Y.S.2d 36, 37 (1961).

62. Transpacific Transp. Corp. v. Sirena Shipping Co., 9 A.D.2d 316, 322, 193 N.Y.S.2d 277, 284 (1959), *aff'd*, 8 N.Y.2d 1048, 170 N.E.2d 391, 207 N.Y.S.2d 70 (1960).

It is thus clear that arbitrators have the power to decline to enforce a contractual provision, even though it is contained in the contract from which they derive their jurisdiction, if they find it unconscionable. The question then remains: Should a party to an arbitration agreement be *compelled* to submit a claim of unconscionability to arbitration?

C. ARBITRATION OF CLAIMS OF CONTRACT UNCONSCIONABILITY

CASE NO. 1:

Eden Textiles, Inc. and Berkshire Sportswear Co., Inc. were parties to two contracts pursuant to which Eden sold and Berkshire purchased 15,100 yards of cotton fabric at a total price of $17,365.00. The contracts covering this transaction provided for arbitration of "any controversy arising out of or relating to this contract." Nevertheless, Berkshire commenced an action in the New York Supreme Court against Eden claiming damages of $35,000.00 for alleged late delivery.[63] Eden promptly moved to stay the action and compel arbitration of the subject dispute.

In resisting arbitration, Berkshire argued that the contracts between the parties contained a clause excluding consequential damages; that Berkshire's damages were essentially consequential (clearly they were so on their face, since they equalled almost exactly twice the total purchase price of the merchandise); that in the circumstances of the case such exclusion left Berkshire virtually without remedy and was therefore unconscionable; that it is against the public policy of New York State to enforce unconscionable contract provisions; that arbitrators are not bound to follow the law; and that, *therefore,* the court should first resolve the claim of unconscionability before permitting the case to go to the arbitrators.

The New York Supreme Court rejected this argument and granted Eden's motion to stay the action and compel arbitration, holding "whether or not the limitation of damages provided for is in fact unconscionable is, to some degree, dependent upon proof of trade usage [citations omitted]. *This is an area particularly appropriate for determination by the arbitrator.*"[64]

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63. *Berkshire Sportswear Co. v. Eden Textiles, Inc.*, in which the author represented the prevailing party, was not officially reported. The decision was unofficially reported at N.Y.L.J., March 30, 1970, at 15, col. 1F.

64. *Id.* (emphasis added).

CASE NO. 2:

Lumbrazo v. Woodruff[65] did not involve arbitration — that is, there was no arbitration clause in the contract between the parties pursuant to which a quantity of Japanese onion sets were sold. What the contract did contain was a disclaimer of any and all warranties, including the warranty that the seeds in fact constituted Japanese onion sets.[66] The question confronting the court was whether such a total disclaimer was unconscionable.

It may be suspected that the trial judge who heard the evidence and decided that the disclaimer was not unconscionable was obliged to gain a quick education in the idiosyncracies of Japanese onion sets, a subject which his legal training might perhaps not have focused upon. It is likely that the five justices of the Appellate Division who reversed (3-2) and found that the disclaimer was unconscionable, likewise were charged with the acquisition of new knowledge. Finally, the seven judges of the Court of Appeals who unanimously reversed the Appellate Division and reinstated the trial judge's decision also had to spend some time on what to them could only have been an esoteric body of knowledge.

Familiarity with the peculiarities of Japanese onion sets was essential to the decision in this case for the issue turned on the extent to which identification of Japanese onion sets could be made through a physical inspection of the seeds.[67] If the seeds could readily be identified as to their anticipated progeny, then it should be unreasonable for a seller thereof to decline to be responsible for variant progeny. If it was all guesswork, as eleven of the thirteen judges who participated in the case evidently concluded it was, then the seller would have been exceedingly imprudent not to disclaim all warranties.

Commercial arbitration was not widely used a half century ago when this case arose. Had it been, thirteen highly salaried government officials might have been able to find a better use for their time than studying the proclivities of Japanese onion sets for genetic secrecy. Arbitrators, selected from among sellers, buyers and other persons familiar with vegetable gardening would of course have had a much easier and unquestionably less time-consuming task.

These two cases demonstrate rather vividly the obvious

65. 256 N.Y. 92, 175 N.E. 525 (1931).
66. Lumbrazo v. Wood ruff, 256 N.Y. 92, ____, 175 N.E. 525, 527 (1931).
67. *Id.* at____, 175 N.E. at 526.

advantage of having claims of contract unconscionability determined by arbitrators familiar with the practices and usages of the pertinent trade. This conclusion is reinforced by the Official Comment to U.C.C. § 2-302 which states the basic test as "whether, *in the light of the general commercial background and the commercial needs of the particular trade or case,* the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract."[68]

It would thus appear that arbitrators are uniquely well-situated and equipped to determine claims of contract unconscionability. As already noted,[69] some courts have evinced uneasiness about entrusting to arbitrators the determination of issues involving significant public policies. Since U.C.C. § 2-302 certainly represents a legislative determination of a significant public policy, it might be argued that this is another area, like usury, antitrust and patents, where enforcement must be implemented by the courts. But the rationale for excluding arbitrators from certain categories of disputes was clearly stated by the New York Court of Appeals in a leading case staying arbitration of an alleged violation of New York's antitrust statute. The court stated as follows:

> Arbitrators are not bound by rules of law and their decisions are essentially final. . . . Even if our courts were to review the merits of the arbitrators' decision in antitrust cases, errors may not even appear in the record which need not be kept in any case. More important, arbitrators are not obliged to give reasons for their rulings or awards. Thus our courts may be called upon to enforce arbitration awards which are directly at variance with statutory law and judicial decision interpreting that law. Furthermore, there is no way to assure consistency of interpretation or application. The same conduct could be condemned or condoned by different arbitrators.
>
> If the arbitrators here should decide wrongly that the goods were or were not defective, the injustice done is essentially only to the parties concerned. If, however, they should proceed to decide erroneously that there was or was not a violation of the Donnelly Act, the injury extends to the people of the State as a whole. . . .

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68. U.C.C. § 2-302, Comment 1 (emphasis added).
69. *See* text accompanying notes 47-52 *supra.*

> Thus the issue which the arbitrators will be called upon to decide transcends the private interests of the parties. It is not simply that arbitrators can impose unnecessarily restrictive or lenient standards. The evil is that, if the enforcement of antitrust policies is left in the hands of arbitrators, erroneous decisions will have adverse consequences for the public in general, and the guardians of the public interest, the courts, will have no say in the results reached. . . .[70]

The same rationale has been enunciated by courts staying arbitration of claims of patent invalidity.[71] However, it is interesting to note that this view is not universally held. For example, of 120 federal circuit and district court judges who answered a questionnaire, 88 judges (73.3 percent of the total responding) said that they would be in favor of allowing disputes over patent infringement and validity to be determined by arbitration.[72] Of particular significance is the following statement of then Chief Judge Friendly of the United States Court of Appeals for the Second Circuit: "This patent appeal is another illustration of the absurdity of requiring the decision of such cases to be made by judges whose knowledge of the relevant technology derives primarily, or even solely, from explanations by counsel. . . ."[73]

Perhaps the distinction between the usury, anti-trust, securities fraud and patent validity cases on the one hand, and the unconscionability cases on the other hand, is that the former tend to involve injury to the general public while the latter usually are limited in their impact to the parties directly involved in the case. Where the antitrust laws are concerned, this is clearly the case, since the satisfaction of the parties to a contract which unreasonably restrains trade is scarcely a ground for approving it. Removing claims of securities fraud and patent invalidity from the scope of arbitration seems to have less justification, but it may be argued that the public has an extraordinary interest in the integrity of the securities markets and in the limitation of the legal monopoly granted by patents.

Where usury is concerned a different rationale seems to be

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70. Aimcee Wholesale Corp. v. Tomar Prod., Inc., 21 N.Y.2d 621, 626-27, 237 N.E.2d 223, 225-226, 289 N.Y.S.2d 968, 971-972 (1968).

71. *See, e.g.,* Diematic Mfg. Corp. v. Packaging Indus., Inc., 381 F.Supp. 1057 (S.D.N.Y. 1974), *appeal dismissed,* 516 F.2d 975 (2d Cir.), *cert. denied,* 423 U.S. 913 (1975).

72. Goldsmith, *The Arbitration of Patent Disputes,* 34 ARB. J. 28, 29 (1979).

73. General Tire and Rubber Co. v. Jefferson Chemical Co., 182 U.S.P.Q. 70 (2d Cir. 1974).

present. As stated in the leading case on point:

> Moreover, any one desiring to make a usurious agreement impenetrable need only require the necessitous borrower to consent to arbitration and also to arbitrators by name or occupation associated with the lending industry [citation omitted]. . . .
>
> If the arbitration clause device could be thus used, all the complicated legislative distinctions in the statutes, civil and criminal, as well as the authority of the administrative regulating agencies, would be avoided by the simplest draftsmanship. The welter of legislation in this area makes clear that the concern is one of grave public interest and not merely a regulation with respect to which the immediate parties may contract freely.[74]

There are several reasons why this rationale is either inapplicable to claims of unconscionability or actually supports the arbitrability of claims of unconscionability. First, the quoted language reminds one that usury is an unusual doctrine, really *sui generis.* There are indeed "complicated legislative distinctions" and a "welter of legislation," both civil and criminal, concerning usurious transactions. None of this pertains where the doctrine of unconscionability is concerned.

Still more important, and indeed of the utmost significance to our inquiry, is the concern of the court with the oppression of a "necessitous borrower," presumably by a powerful lending institution able to dictate terms. Obviously this takes us back to the traditional claim of procedural unconscionability — to the welfare recipient whose poor credit rating obliges her to do business with a ghetto predator or the little carrot farmer obliged to do business with the giant Campbell Soup Company and accept its preprinted contract form or the gasoline station operator obliged to do business with Mobil.

What the court seems to be suggesting is that the "necessitous borrower" never gave free, knowing consent to the arbitration clause contained in the contract claimed to be usurious. Put another way, the court is suggesting that the "necessitous borrower" might have been inveigled or tricked into executing the agreement containing the arbitration clause. But if such be the

74. Durst v. Abrash, 22 A.D.2d 39, 44, 253 N.Y.S.2d 351, 355-356 (1964), *aff'd,* 17 N.Y.2d 445, 213 N.E.2d 887, 266 N.Y.S.2d 806 (1965).

case, there is no reason to reach the issue of usury, for it is universally held that a party will not be compelled to arbitrate unless he has knowingly and explicitly agreed to arbitrate.[75] Where a party freely gave his consent to arbitration of all disputes "arising out of or relating to" the subject contract (the standard language for arbitration clauses), it is destructive of the arbitral process for the courts to become involved in delineating the issues and deciding which should go to the arbitrators and which should first be determined by the courts. The duplication of effort, with the attending ills of added delay and expense, is obvious. Even more important is the undermining of the authority of the arbitrators whose function may well be reduced to mere calculators of damages. This was expressly recognized by the dissenting judges in the *Durst* case, who wrote the following:

> In very many instances the question of whether the instrument is legally enforcible or not depends on the interpretation to be put on it and this, in turn, depends most frequently on subsidiary issues of fact. The resolution of these issues determines the right to recovery. It is just those issues that the parties agreed to submit to arbitrators. If these issues are to be determined by the court, the role of the arbitrators is written out of the contract, or at least reduced to a calculation of damages.[76]

There is another very good reason why the courts should not become involved in claims of contract unconscionability as a preliminary to compelling arbitration of a dispute under a contract providing for arbitration of all disputes. A claim that a contract is usurious can normally be assessed with relative ease. Whether a contract is violative of the anti-trust laws is admittedly more complicated. However, in response to that very fact, the courts have required a rather conspicuous antitrust violation before permitting a party to avoid his contractual commitments on that account. Thus the United States Court of Appeals for the First Circuit has held that "antitrust defenses are allowed only in cases where the intrinsic illegality of the contract is so clear that enforcement would make a court party to the precise conduct forbidden by the law."[77]

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75. *See, e.g.*, Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395 (1967); Doughboy Industries, Inc. v. Pantasote Co., 17 A.D.2d 216, 233 N.Y.S.2d 488 (1962). *Cf.*, Marlene Industries Corp. v. Carnac Textiles, Inc., 45 N.Y.2d 327, 380 N.E.2d 239, 408 N.Y.S.2d 410 (1978).

76. 22 A.D.2d at 46, 253 N.Y.S.2d at 357-358.

77. Dickstein v. du Pont, 443 F.2d 783, 786 (1st Cir. 1971).

For the same reason, courts should be loath to go behind the contract and hear evidence of the specific circumstances of the parties as well as trade usage in order to determine, as a preliminary to arbitration, whether any of the provisions in the contract providing for arbitration might be unconscionable. As recently stated by the New York Court of Appeals, "the courts must be able to examine an arbitration agreement or an award on its face, without engaging in extended factfinding or legal analysis, and conclude that public policy precludes its enforcement."[78] This quote is taken from a case in which the court upheld an arbitrator's enforcement of a restrictive covenant in an employment agreement although the court clearly implied that it disagreed with the result and might even reverse a comparable judicial determination.

One final consideration. In the preface to this article it is noted that a judge of the United States Court of Appeals for the Second Circuit dissented from a decision sending the issue of unconscionability to an arbitration panel on the ground that U.C.C. § 2-302 begins "If the court as a matter of law finds. . . ." This dissenting judge also noted that the issue could not be submitted to a jury.[79] The answer to this objection is that the judge seems to be misconstruing the role of the arbitrator as analogous to that of a civil jury. In fact, as a myriad of cases make clear, an arbitrator's function is rather analogous to that of a judge sitting without a jury. Thus it is regularly held that "[b]oth questions of fact and law are for the arbitrators."[80]

CONCLUSION

The inadequacy of court litigation for the resolution of commercial disputes is a reality known to most businessmen. Long delays are common, great expense is inevitable. Every successful litigator has heard a client express admiration for his advocacy skills while remarking that one additional such victory will find him in the bankruptcy courts.

Commercial arbitration holds out to the businessman the possibility of an expeditious and relatively inexpensive resolution of his disputes with his suppliers and his customers. He can expect, for example, that a dispute over the ownership of seasonal

78. Sprinzen v. Nomberg, 46 N.Y.2d 623, 631, 389 N.E.2d 456, 460, 415 N.Y.S.2d 974, 978 (1979).

79. *See,* n. 6 *supra.*

80. Spectrum Fabrics Corp. v. Main St. Fashions, 285 A.D. 710, 139 N.Y.S.2d 612, 617, *aff'd,* 309 N.Y. 709, 128 N.E.2d 416 (1955). *And see* case cited *supra* note 65.

merchandise will be resolved while that merchandise is still merchantable. And he may anticipate that the successful prosecution of his claim, or the successful interposition of a defense to a claim brought against him, will not be so expensive as to make a victory Pyrrhic or a defense uneconomical.

But the advantages of arbitration will be dissipated or even wholly lost if the parties become embroiled in preliminary or ancillary judicial proceedings. Indeed, if the courts are going to receive evidence and make factual determinations and legal conclusions which will be binding upon the arbitrators, one might just as well dispense with the arbitrators and let the courts finish the job they have begun. Indeed, a proceeding which involves an initial court determination of such an issue as whether a contract provision is unconscionable, followed by an arbitration hearing to determine whatever there is still left over to determine, followed by a contested motion to confirm the award, may well be more consuming of time and money than a straightforward litigation would be. Combining litigation and arbitration generally accords one the major disadvantages of both.

There may be certain areas where matters of such immense public importance are at stake that their resolution cannot be left to tribunals not bound to follow the rules of law. Antitrust enforcement is the most obvious such area and perhaps the courts are correct that issues of usury, securities fraud, and the validity of patents must likewise be determined by judges bound to follow the law and subject to judicial review of their decisions. But if the arbitration of commercial disputes is to be encouraged — and everyone who speaks on the subject, from the Chief Justice of the United States on down, has said that it should be — then it is extremely important to keep the non-arbitrable categories as limited and narrow as possible. For the reasons adumbrated in this article a claim of contract unconscionability should certainly not be included within the non-arbitrable categories; rather, it constitutes precisely the kind of dispute which arbitrators are ideally situated to resolve quickly and fairly.