

states approve such a plan, multiple taxation would still result. Perhaps the only feasible solution would be federal action, and this is currently being considered.¹⁷

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Contracts—Federal Arbitration Act—Severability of Arbitration Clause.—*El Hoss Engineering & Transport Co. v. American Independent Oil Co.*¹—El Hoss Engineering & Transport Co. (El Hoss), a Lebanese corporation with its principal place of business in Lebanon, entered into an agreement with American Independent Oil Co. (Aminoil), a Delaware corporation with its principal place of business in New York City. Under the terms of the agreement Aminoil was to sell to El Hoss automotive and construction equipment and El Hoss was to lease this same and other equipment to Aminoil, and furnish such transportation as Aminoil would need. Immediately preceding the signature of Aminoil's agent was the following clause:

"and accepted by the Company this 1st day of October, 1959, subject to compliance with the conditions of this agreement as to guarantees or endorsements by third parties in favor of the Company covering the unpaid installments on purchase price, performance bonds and insurance coverage, etc., not later than fourteen (14) days from the date of the acceptance by the Company."

The agreement included a standard arbitration clause.²

Aminoil extended the time for the posting of the performance bond and insurance from October 14 to November 1, and then to November 20, as it and El Hoss were negotiating with regard to same. Then in December, El Hoss filed a petition under Section 4 of the Federal Arbitration Act³ to compel arbitration as to the terms and suitability of the performance bonds and insurance which it was prepared to furnish. The petition was granted,⁴

¹⁷ Pub. L. No. 86-272, § 201, 73 Stat. 556 (Sept. 14, 1959). Congress directed the Senate Committee on Finance and the House Committee on the Judiciary to hold hearings and report proposed legislation to provide uniform standards to be observed by the states.

¹ 289 F.2d 346 (1961), petition for cert. filed, 30 U.S.L. Week 3026 (U.S. July 6, 1961) (no. 209).

² "11. In the event of any disagreement between the parties hereto as to the effectuation of this agreement, or performance thereof, or any part of the agreement, each party undertakes to use its best efforts to resolve said disagreement without submission to arbitration. However, should such solution be impossible, the parties hereto will select a mutually acceptable arbitrator whose decision as to the matters presented to him shall be final. If the parties cannot agree on such an arbitrator, each shall nominate an arbitrator of its choice and these shall in turn select a third, and the decision of a majority of this panel of three shall be final as to all matters submitted. This paragraph shall not effect the rights of the company to terminate this agreement under the provisions of paragraphs three (3) and four (4) of section one (1)" *Supra* note 1, at 348.

³ 61 Stat. 671 (1947), as amended, 9 U.S.C. § 4 (1958).

⁴ 183 F. Supp. 394 (S.D.N.Y. 1960).

but on appeal the Court of Appeals for the Second Circuit reversed the order and remanded the case to the District Court. HELD: The issue as to the performance bond and insurance is not arbitrable as the arbitration clause is not separable from the remainder of the agreement.

At common law, arbitration agreements were considered to be collateral to the main contract.⁵ The courts exemplified this position by allowing a party to avoid the agreement to arbitrate and proceed directly to an action on the contract itself—they were deemed severable at will.⁶ In order to overcome this judicial hostility to arbitration various jurisdictions passed arbitration laws.⁷ But even though the arbitration clauses by virtue of such statutes were deemed valid and irrevocable, judicial restraint remained evident. The generally accepted approach was for the courts to decide whether or not the main contract was entered into. Such a ruling was considered an indispensable prerequisite to an order compelling arbitration;⁸ the reason being that the agreement to arbitrate was considered a component part of the main contract. Thus, if the main contract failed for any reason, so too did the arbitration agreement.⁹

It was in this light that *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*¹⁰ was presented. The problem before the court in that case was whether or not an action could be brought for fraudulent inducement of a contract which contained an arbitration clause. It was there decided that the Federal Arbitration Act necessitated the application of federal rather than state law.¹¹

⁵ *Hamilton v. Home Insurance Co.*, 137 U.S. 370 (1890).

⁶ *United States Asphalt Refining Co. v. Trinidad Lake Petroleum Co.*, 222 Fed. 1006 (S.D.N.Y. 1915).

⁷ The Federal Arbitration Act was originally enacted in 1925. 43 Stat. 833 (1925), 9 U.S.C. §§ 1-15. It was repealed and substantially re-enacted in 1947. 61 Stat. 669 (1947), 9 U.S.C. §§ 1-14 (1958). N.Y. Civ. Prac. Act. §§ 1448-69. The New York Arbitration Act was originally enacted in 1925. L. 1925, c. 925. See also *Kulukundis Shipping Co., S/A v. Amtorg Trading Corp.*, 126 F.2d 978 (2d Cir. 1942).

⁸ *Heyman v. Darwin's Ltd.*, [1942] A.C. 356; *Fernandez v. Golodetz*, 148 F.2d 625 (2d Cir. 1945); *Seymour Grean & Co. v. Grean*, 274 App. Div. 898, 82 N.Y.S.2d 787 (1948).

⁹ "Even if, for some purposes, the provision for arbitration is declared to be independent and collateral, the factor that makes the rest of the transaction void or voidable would affect that transaction as a whole. If one party failed to express assent to the terms proposed by the other, no contract has been made. The proposal for arbitration lacks acceptance just as fully as do the other proposed terms."

⁶ *Corbin, Contracts* § 1444 (1951).

¹⁰ 271 F.2d 402 (2d Cir. 1959), cert. granted, 362 U.S. 909 (1960), dismissed, 364 U.S. 801 (1960).

¹¹ On this point there is disagreement among the federal courts. *Rose v. Twentieth Century-Fox Film Corp.*, 236 F.2d 632, 634 (9th Cir. 1956), and *Lummas v. Commonwealth Oil Refining Co.*, 280 F.2d 915, 924 (1st Cir. 1960), both hold that applicable state law must govern. *American Airlines, Inc. v. Louisville & Jefferson C.A.B.*, 269 F.2d 811 (6th Cir. 1959), takes an intermediate view, as there decided was the point that both state and federal law should apply. The source of this confusion lies with *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198 (1956); *Erie v. Tompkins*, 304 U.S. 64 (1938); and *Red Cross Line v. Atlantic Fruit Co.*, 264 U.S. 109 (1924). See also *Kochery, The Enforcement of Arbitration Agreements in the Federal Courts: Erie v. Tompkins*, 39 Cornell L.Q. 74 (1953); *Sturges, Some Confusing Matters Relating to*

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And as under federal law an arbitration clause is deemed separable, a general allegation of fraudulent inducement is not a sufficient basis for an action at law, if the arbitration clause is broad enough to encompass such a charge.¹² To reach this conclusion, as to the separability of the arbitration clause, reliance was placed on three points: (1) Section 2 of the Federal Arbitration Act made "valid, irrevocable, and enforceable" *only* the provision dealing with arbitration; it does not apply to the contract *in toto*;¹³ (2) at common law such clauses were treated as separable; and (3) public policy favored arbitration.¹⁴

It was this issue of separability which the court in the instant case met head on. *Robert Lawrence* was distinguished on the ground that there the allegation of fraud in the inducement applied only to the contract as a whole and not to the arbitration clause, whereas in the instant case enjoyment of the contractual rights and liabilities was subject to the posting of the performance bond and liability insurance. "Every clause including the arbitration clause was expressly so conditioned."¹⁵ What the court does not explain is why an allegation of fraudulent inducement of the whole contract tends to show that the arbitration clause is separable, when an allegation that a condition precedent to the contract was not met shows that the arbitration clause is not separable.

The decision of the court was characterized in the dissenting opinion as "an undesirable departure from the liberal arbitration policy enunciated by this court in *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*"¹⁶ What the court here did consider, and what it did not in *Robert Lawrence*, was the over all intent of the parties: does the tenor of the whole contract, including any part thereof should be treated as valid for any or all reasons? On the other hand, the court in *Robert Lawrence* held in effect that under federal law there is a presumption that the arbitration clause is separable.¹⁷

Arbitration Under the United States Arbitration Act, 17 Law & Contemp. Prob. 580 (1953); Note, 108 U. Pa. L. Rev. 915 (1960).

¹² The arbitration clause appearing in *Robert Lawrence* read as follows:

"Any complaint, controversy, or question which may arise with respect to this contract that cannot be settled by the parties thereto, shall be referred to arbitration. If the controversy concerns the condition or quality of merchandise it shall be referred to the Mutual Adjustment Bureau of the cloth and garment trades pursuant to the rules and regulations thereof. All other controversies shall be submitted to the American Arbitration Association."

Supra note 10, at 404.

¹³ 61 Stat. 670 (1947), 9 U.S.C. § 2 (1958). Section 2 reads as follows:

"... a written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction ... shall be valid, irrevocable and enforceable save on such grounds as exist in law or equity for the revocation of any contract."

¹⁴ Supra note 10, at 409-10.

¹⁵ Supra note 1, at 349. It should be again noted that the clause stating this condition appeared only once in the contract. The court also summarily stated that "here there is no likelihood of sham litigation to avoid submitting issues to arbitration." Ibid.

¹⁶ Id. at 351.

¹⁷ This approach was earlier proposed by Sturges, *Fraudulent Inducement as a*

In *Lummus v. Commonwealth Oil Refining Co.*,¹⁸ the court dismissed the contention of the plaintiff that, if it were to apply federal law, it would have to find that the agreement to arbitrate was an integral part of the whole contract. "We see no reason why parties should not agree, if they wish to, that if a question arises as to whether the principal agreement was obtained by fraud, that that question will be arbitrated. For a court then to hold that fraud which bore only upon the principal agreement automatically invalidated the arbitration contract would be to destroy precisely what the parties had sought to create. Moreover, any other approach sets the stage for delaying action"¹⁹ It would seem that here the court adopts a criterion similar to that of the instant case—the intent of the parties as exemplified by the tenor of the whole contract.²⁰

In *In re Exercycle Corporation and Maratta*,²¹ the New York Court of Appeals held that the question of whether or not a contract was illusory was arbitrable. It did not advert in any manner to the doctrine of separability, though by reason of its decision it had to find that the arbitration clause was separable.²² The court also stated that if the objection raised was one of fraud, duress, illegality, or failure of a condition precedent such would not be arbitrable.²³

Exercycle points up the problem presented by the court in the instant case. If the test of separability is the intent of the parties, will the result reached vary with the objection raised to the main contract? Do the objections of fraud in the inducement or lack of mutuality pose any greater reason to find that the clause is separable than if the objection raised is one of an unfulfilled condition precedent, lack of capacity or illegality? If uniformity of result is a worthy attribute when federal law is applied, then the approach of the court in *Robert Lawrence*, and not that in *El Hoss*, is to be favored.

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Defense to the Enforcement of Arbitration Contracts, 36 Yale L.J. 866, 873 (1927). See also Parsell, Arbitration of Fraud in the Inducement of a Contract, 12 Cornell L.Q. 351 (1927). In *Robert Lawrence* it was not alleged that the parties considered the arbitration clause as an inseparable part of the whole. It is submitted that such an allegation would have had no effect.

¹⁸ 280 F.2d 915 (1st Cir. 1960), cert. denied, 364 U.S. 911 (1960).

¹⁹ *Id.* at 924.

²⁰ The subjunctive mood was here used as the court did not apply federal law but rather state law (see note 11 *supra*) and according to its interpretation the doctrine of separability was not recognized in New York.

²¹ 9 N.Y.2d 329, 174 N.E.2d 463, 214 N.Y.S.2d 353 (1961).

²² If the court did not find first that the agreement to arbitrate was separable, it would in effect be saying that the arbitrators have exclusive jurisdiction to decide whether or not there was an agreement to arbitrate. Or put in another way, even if it is alleged that the agreement to arbitrate was void or voidable such would have to be decided by the arbitrators. Even *Robert Lawrence* denies the validity of this position. *Supra* note 10, at 411.

²³ *Supra* note 21, 174 N.E.2d at 465, 214 N.Y.S.2d at 356.