Increasingly, many arbitration agreements include clauses that attempt to limit substantive rights and remedies that are otherwise afforded to parties by various federal and state statutes. For example, many employment, cable television subscriptions, or residential mortgage loan contracts contain arbitration clauses purporting to exclude or limit punitive or actual damages otherwise available under applicable remedial statutes. These clauses have been subject to varying degrees of judicial scrutiny, depending on the jurisdiction where the dispute is brought. One particular issue as to which the circuits are sharply divided is whether courts should adjudicate the enforceability of an arbitration clause before arbitration if the party opposing arbitration contends that public policy prohibits the waiver of the party’s statutory rights that the clause purports to effect.

The First, Fifth, Sixth, Ninth, Eleventh, and D.C. Circuits have held that an arbitration clause that is alleged to impermissibly preclude or limit statutorily authorized remedies is still a valid agreement to arbitrate, and that the arbitrator should decide the availability of remedies along with the other issues in the case. This article examines the different approaches courts have taken with regard to the enforceability of such clauses.

Introduction

The current split among the circuits has its genesis in a trilogy of U.S. Supreme Court opinions that have touched upon, but not resolved, the issue of enforceability of arbitration clauses that preclude or limit statutorily authorized remedies.

In *Gilmer v. Interstate/Johnson Lane Corp.*, the Supreme Court stated that “[b]y agreeing to arbitrate a statutory claim, a party does not forego the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than judicial forum.” The Court, however, did not analyze the issue of enforceability of the rights-restrictive agreements in more detail, as the facts in *Gilmer* did not involve limitations upon the types of relief that the arbitrator could award.

Subsequently, in *PacifiCare Health Systems, Inc. v. Book*, the Court held that when there is ambiguity about the scope of a remedies limitation in an arbitration agreement, an arbitrator must decide the issues of enforceability in the first instance. *PacifiCare* addressed the question of whether parties could be compelled to arbitrate claims arising under the Racketeer Influenced and Corrupt Organizations Act (RICO), notwithstanding the fact that the arbitration agreement’s bar of punitive damages could be construed to limit the arbitrator’s authority to award treble damages under the RICO statute. The Court concluded that it was unclear whether the arbitration agreement’s bar of punitive damages could be construed to limit the arbitrator’s authority to award treble damages under the RICO statute. The parties’ agreement was also subject to uncertainty surrounding the parties’ intent with respect to the contractual term “punitive.” The Court concluded that the case was not ripe for judicial determination, and that the arbitrator should decide the issue of the agreement’s enforceability in the first instance. The Court’s ruling, however, did not address the situation where there was not any ambiguity affecting the
scope of remedial limitations in the arbitration agreement.  

Most recently, in *Buckeye Check Cashing, Inc. v. Cardegna*, the Supreme Court held that a challenge to the validity of a contract as a whole, and not specifically to the arbitration clause within it, must be resolved by the arbitrator in the first instance.  

*Buckeye* involved a putative class action, in which plaintiffs challenged the validity of the entire contract between the parties, including the arbitration provision. The Court explained that federal courts may adjudicate only challenges that “go[] to the making of the agreement to arbitrate,” as the Federal Arbitration Act does not permit federal courts to consider challenges to contracts generally. Thus, unless the challenge is to the arbitration clause itself, the issue of the contract’s validity is to be considered by the arbitrator in the first instance.

The Supreme Court has not yet resolve definitively whether the issue of enforceability of an arbitration clause that limits a party's substantive remedies must be resolved by the courts or left for the arbitrators. The circuit courts currently are split on this issue, reflecting a divergence of views concerning the proper scope of judicial review regarding the enforceability of arbitration agreements. The prevailing tendency among the circuits has been to assign the issue to the courts. The majority of circuits hold that challenges to arbitration agreements based upon their remedial restrictions fall within the category of gateway matters to be decided by a court. Other circuits disagree, holding that challenges to the adequacy of arbitration remedies have nothing to do with whether the parties agreed to arbitrate, and that such challenges must first be considered by the arbitrator.

First, Fifth, Sixth, Ninth, Eleventh, and D.C. Circuits Adjudicate the Enforceability of Substantive Restrictions in Arbitration Agreements Prior to Arbitration

The First, Fifth, Sixth, Ninth, Eleventh, and D.C. Circuits have held a court’s determination of arbitrability encompasses the issue of enforceability of substantive restrictions contained in the arbitration agreement that allegedly conflict with state or federal statutes and public policy. Under this approach, a trial court can either invalidate the entire agreement to arbitrate and hear the merits of the case, or sever the offending provisions and require arbitration under the remainder of the contract. The differences in outcomes on the issue of severability reflect variations among different arbitration agreements.

Under the approach taken in these circuits, when a party challenges the validity of an arbitration clause on the ground that it contains unenforceable remedial restrictions, the court must first decide whether the restrictions are unenforceable because they defeat the remedial purpose of the state or federal statute. Courts will deny the motion to compel arbitration only where the invalid terms of the arbitration agreement render the entire arbitration clause void. If all provisions of the arbitration agreement are enforceable, the court must compel arbitration. If, however, some or all of the provisions in the agreement are unenforceable, then the court must determine whether the unenforceable provisions are severable. If the offending provisions are severable from the rest of the arbitration agreement, the court must compel arbitration according to the remaining, valid terms of the parties’ agreement.

The Eleventh Circuit also permits district courts to compel arbitration without first passing on the validity of remedial restrictions if the agreement contains an unambiguous severability clause, and there is no doubt that the dispute would wind up in the arbitration. A district court might then refrain from ruling on the validity of the challenged restrictions and direct the parties to proceed to arbitration because there is no longer any question as to whether the parties had a valid agreement to arbitrate.

The decisions striking arbitration clauses in their entirety most often involve agreements without a severability clause, and situations where the agreements are pervasively infected with illegality, particularly if “the offensive provisions clearly represent an attempt . . . to achieve through arbitration what Congress has expressly forbidden.” The decisions in which the courts
severed the offending provisions and compelled arbitration, on the other hand, typically involve agreements with discrete, readily separable provisions. In reviewing these agreements, the focus should be on the nature of the remedy sought and whether the remedy is of a similar nature to that available in court. If it is, the agreement may be enforceable; if not, the agreement may be invalid.

**Clauses Foreclosing Substantive Rights Might Invalidate an Otherwise Enforceable Agreement To Arbitrate**

In several instances, the circuit courts have invalidated entire arbitration agreements that foreclosed statutory remedies. In *Paladino v. Avnet Computer Technologies, Inc.*, for example, the Eleventh Circuit invalidated the entire agreement to arbitrate because the arbitration clause impermissibly restricted plaintiff’s statutory remedies under Title VII. The arbitration agreement in that case specified that “[t]he arbitrator is authorized to award damages for breach of contract only, and shall have no authority whatsoever to make an award of other damages.” *Id.*

Because Title VII damages are not contract damages, the Eleventh Circuit concluded that this arbitration clause denied the employee “the possibility of meaningful relief in an arbitration proceeding.” *Id.* As the court explained, the arbitration agreement defeated the statute’s remedial purposes by insulating defendant from Title VII damages and equitable relief a court could award, and “the arbitrability of [statutory] claims rests on the assumption that the arbitration clause permits relief equivalent to court remedies.” *Id.*

Similarly, in *Graham Oil Co. v. Arco Products*, the Ninth Circuit invalidated an arbitration clause that purported to forfeit plaintiff’s statutorily-mandated rights to exemplary damages, attorney’s fees, and one-year statute of limitations. The court refused to sever the offending provisions, instead concluding that the entire arbitration clause must be eliminated as it clearly purported to achieve through arbitration what Congress has expressly forbidden. The court concluded that severance is inappropriate when the entire clause represents an integrated scheme to contravene public policy.

*Paladino and Graham Oil* involved exceptional circumstances that presented several allegedly offending provisions. As the Eleventh Circuit later explained, “*Paladino* does not hold that any remedial restriction contained in an arbitration agreement is necessarily unenforceable or necessarily renders the agreement null and void in its entirety.” *Id.* Instead, when a party challenges the validity of an arbitration clause on the ground that it contains unenforceable remedial restrictions, the court must first determine whether those remedial restrictions are severable.

**Judicial Determinations of Severability of Allegedly Offending Provisions**

When the arbitration agreement includes a severability provision, courts will not lightly conclude that a particular provision of an arbitration agreement taints the entire agreement. Indeed, in *Buckeye*, the Supreme Court held that as a matter of substantive federal arbitration law, an arbitration provision is severable from the remainder of the contract. In general, the more one of the parties overreaches, the less a court is likely to sever the offending provisions and enforce the rest of the arbitration agreement. But when the agreement contains a severability clause and the offending provisions are discrete and separable, a court is likely to sever the unenforceable part and compel arbitration under the remainder of the agreement.

For example, in *Morrison v. Circuit City Stores, Inc.*, the Sixth Circuit held that the arbitration agreement’s provisions restricting an employee’s right to compensatory and punitive damages under Title VII were unenforceable but severable. The court emphasized that Circuit City’s arbitration agreement, which limited plaintiff’s compensatory and punitive damages under Title VII, contravened the remedial principles of the statute by preventing full compensation for any harms caused by wrongful discrimination, and by eviscerating Congress’ intent to utilize punitive damages as a tool for combating discrimination. Nonetheless, the court held that the offending provisions were severable from the arbitration agreement as a whole.

Likewise, in *Jackson v. Cintas Corp.*, the Eleventh Circuit upheld the trial court’s arbitration order severing the restrictions in the arbitration clause that purported to limit the time in which the employee could bring statutory claims. Similarly, in *Kristian v. Comcast Corp.*, the First Circuit held that arbitration agreements prohibiting
recovery of treble damages as applied to federal antitrust claims, attorney’s fees and costs, and the class arbitration bar were invalid, and severed the offending provisions from the arbitration agreements as applied to antitrust claims. With the offending provisions removed, the parties could proceed with the arbitration of the antitrust claims.

Third, Seventh, and Eighth Circuits Hold That Arbitrators, Not Courts, Should Adjudicate the Enforceability of Substantive Restrictions in Arbitration Agreements

The Third, Seventh, and Eighth Circuits hold that challenges to a provision restricting arbitration remedies must be determined by the arbitrator in the first instance. Under this approach, the court’s scope of review of an arbitration agreement is limited to the issues which are “essential to defining the nature of the forum in which the dispute will be decided.” Once a court determines that a valid agreement to arbitrate exists, the arbitrator should decide all remaining issues. Questions concerning public policy and remedies are outside the scope of that inquiry because these issues are considered not to affect the validity of an agreement to arbitrate.

A recent decision within the Eighth Circuit, by the Southern District of Iowa in Faust v. Command Center, Inc., provides a typical example of such limited judicial review. In Faust, a former employee sued her employer for sex discrimination, sexual harassment, and retaliation in violation of the Iowa Civil Rights Act. Plaintiff’s employment agreement contained an arbitration clause, which limited the arbitrator’s authority to award punitive damages. The employer moved to compel arbitration. Plaintiff opposed the motion to compel arbitration, contending that the punitive damages limitation in the arbitration agreement violated public policy. The district court compelled arbitration, holding that it is for the arbitrator, not the court, to decide whether the waiver of punitive damages is unenforceable.

Despite the limited scope of judicial inquiry in the Third, Seventh and Eighth Circuits, courts within these circuits still disfavor arbitration agreements that limit the relief an arbitrator may award, and these courts recognize that the arbitrators have power to fashion appropriate relief. For example, courts have allowed an arbitrator to award the party relief even in the face of contractual limitations, and may rule that certain arbitration awards are unenforceable. The narrow scope of the initial judicial review under the arbitration agreement does not foreclose a party from subsequently vindicating legal rights because “[b]y agreeing to arbitrate a statutory claim, a party does not forego the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than judicial forum.”

In Alexander v. Anthony International, L.P., for example, the Third Circuit found the agreement to arbitrate unenforceable under the doctrine of unconscionability because plaintiffs were not presented with any real opportunity to negotiate the terms of the arbitration agreement; the agreement provided one-sided time limitations and restrictions on the
relief available to plaintiffs, and the "loser pay" provisions for arbitrator’s fees and expenses unreasonably favored the defendant. The court concluded that those elements of illegality permeated the entire agreement to arbitrate, precluding severance of the offending provisions.

**Parties Also Can Contractually Submit the Issue of Arbitrability to the Arbitrator and Avoid Antecedent Judicial Review**

Even in jurisdictions where courts typically adjudicate enforceability of arbitration clauses in the face of allegations that the clauses contravene public policy, parties may avoid such adjudication by specifically addressing this topic in their arbitration clauses. In Terminix International Co. v. Palmer Ranch Limited Partnership, the Eleventh Circuit allowed the parties to contract around the default rule that requires antecedent enforceability assessment of the remedial restrictions in the arbitration agreement. The court instructed that when parties incorporate the Commercial Arbitration Rules of the American Arbitration Association (AAA) into their arbitration agreement, a court does not have to decide the antecedent question regarding the validity of the arbitration clause, and will order the parties to proceed to arbitration, leaving it to the arbitrator to decide whether the agreement unlawfully deprives the party of any statutory rights.

AAA Rule 8(a) provides that "[t]he arbitrator shall have the power to rule on his or her own jurisdiction, including any objections with respect to the existence, scope or validity of the arbitration agreement." Thus, by incorporating Rule 8 into their agreement, the parties consented that the arbitrator would decide whether the arbitration clause is valid. The court concluded that because the arbitrator is to decide the ultimate question of arbitrability, there is no reason for the court to decide the subsidiary, antecedent questions regarding the validity of the remedial restrictions, and the court therefore directed the case to arbitration.

**Conclusion**

Until the Supreme Court determines whether the issue of validity of an arbitration agreement that limits substantive remedies is to be resolved by the courts or left for the arbitrators, courts will continue to proceed with varying degrees of review of such agreements. As a general matter, however, agreements limiting the relief that an arbitrator may award are disfavored, and the ultimate effectiveness of such restrictions is uncertain. Parties drafting arbitration clauses therefore should be mindful of the risk that such clauses may be subject to review and possible unenforceability if the clauses encroach too far on substantive rights and remedies, particularly in those jurisdictions where courts have demonstrated a willingness to engage in this type of analysis in deciding a motion to compel arbitration.

**Endnotes**

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3 See, e.g., Booker v. Robert Half Intern., Inc., 413 F.3d 77 (D.C. Cir. 2005) (arbitration agreement purporting to limit punitive damages otherwise available under the D.C. statute); Hadnot v. Bay, Ltd., 344 F.3d 474 (5th Cir. 2003) (arbitration provision prohibiting punitive and exemplary damages otherwise available under Title VII of the Civil Rights Act); Kristian v. Comcast Corp, 446 F.3d 25 (1st Cir. 2006) (cable television subscriber agreements barring treble damages otherwise available under federal antitrust laws); Anders v. Hometown Mortgage Services, Inc., 346 F.3d 1024 (11th Cir. 2003) (arbitration agreement purporting to limit punitive and treble damages, penalties or attorney’s fees otherwise available under the Truth in Lending Act, and the Real Estate Settlement Procedures Act).


5 Id. at 32. In Gilmer, the Court rejected a general challenge to the arbitrability of a claim brought under the Age Discrimination in Employment Act (ADEA). Id. at 23. The Court concluded that the ADEA claim was subject to arbitration in the absence of showing that Congress intended to preclude a waiver of a judicial forum in the text of the ADEA, its legislative history, or as a result of an "inherent conflict" between arbitration and the underlying purposes of the statute. Id. at 27-29.


7 Id. at 402-03.

8 Id. at 405-06.

9 Id. at 406.

10 Id. 406-07.

11 See, e.g., Kristian, supra note 3, at 45 (PacifiCare does not apply where
“[There is nothing ambiguous about the remedies-stripping provision at issue.”].

12 546 U.S. 440, 445-46 (2006); see also Pleasant v. Houston Works USA, No. 06-20824 (5th Cir. June 7, 2007) (district court properly compelled arbitration where plaintiff conceded he agreed to arbitrate all employment disputes, and contended generally that arbitration clause was unenforceable due to the employer’s alleged breach of obligations under the entire Employment Dispute Resolution Program).


14 Compare with State ex rel. Vincent v. Schneider, 194 S.W.3d 853, 857 n. 1 (Mo. 2006) (Buckeye does not apply where plaintiff challenges arbitration clause directly and not the contract as a whole).

15 See, e.g., Kristian, supra note 3, at 45-46 (rejecting inconsistent dicta from MCI Telecomm. Corp. v. Matrix Communications Corp., 135 F.3d 27 (1st Cir. 1998), and holding that a court, not the arbitrator, should resolve claims of damages limitation which preclude plaintiffs’ federal antitrust claims). See also infra note 18.


17 See, e.g., Hawkins v. Aid Ass’n for Lutherans, 338 F.3d 801, 807 (7th Cir. 2003). The Seventh Circuit also held that Gilmer only applies to federal statutory claims if Congress has evinced its intention to preclude the waiver of statutory rights, and does not apply to state common-law claims. Id. at 807. See also infra note 43.

18 Kristian, supra note 3, at 45-46; Hadnot, supra note 3; Morrison v. Circuit City Stores, Inc., 317 F.3d 646, 670-74 (6th Cir. 2003); Graham Oil Co. v. Arco Prods., Co., 43 F.3d 1244, 1247-48 (9th Cir. 1995); Paladino v. Avnet Computer Techs., Inc., 134 F.3d 1054, 1057-60 (11th Cir. 1998); Booker, supra note 3, at 79. See also Cole v. Burns Int’l Security Services, 105 F.3d 1465, 1468 (D.C. Cir. 1997).

19 Booker, supra note 3, at 84-85.


21 Morrison, supra note 18, at 675.

22 Terminix, supra note 20, at 1331.

23 Anders, supra note 3; Terminix, supra note 20, at 1332 (quoting Green Tree Fin. Corp. v. Bazzle, 539 U.S. 444, 452 (2003)).

24 Graham Oil, supra note 18, at 1248-49.

25 Booker, supra note 3, at 84-85.

26 Paladino, supra note 18, at 1062.

27 Id. at 1062.

28 Id.

29 Graham Oil, supra note 18, at 1246.

30 Id.

31 Id.

32 Terminix, supra note 20, at 1331.

33 Id.

34 Morrison, supra note 18, at 675.

35 Buckeye, supra note 12.

36 Booker, supra note 3, at 85-86.

37 Morrison, supra note 18, at 670-75.

38 Id. at 672.

39 Id. at 675.

40 425 F.3d 1313, 1317 (11th Cir. 2005).

41 Kristian, supra note 3, at 64.

42 Id.

43 Bob Schulz Motors, Inc. v. Kawasaki Motors Corp., U.S.A., 334 F.3d 721 (8th Cir. 2002); Larry’s United Super, Inc. v. Werries, 253 F.3d 1083, 1085 (8th Cir. 2001); Matrix, supra note 15, at 33 n. 12 (issue of validity of arbitration agreement foreseeing statutory remedies “must be brought to the arbitrator because it does not go to the arbitrability of the claims but only to the nature of available relief”); Hawkins, supra note 17, at 807 (“Because the adequacy of arbitration remedies has nothing to do with whether the parties agreed to arbitrate or if the claims are within the scope of that agreement, these challenges must first be considered by the arbitrator”); Great Western Mortgage Corp. v. Peacock, 110 F.3d 222, 232 (3d Cir. 1997) (“The availability of punitive damages is not relevant to the nature of the forum in which the complaint will be heard. Thus, availability of punitive damages cannot enter into a decision to compel arbitration.”).

44 Larry’s United, supra note 43, at 1085; Great Western, supra note 43, at 230.

45 Great Western, supra note 43, at 231.

46 Arkcom Digital Corp. v. Xerox Corp., 289 F.3d 536, 539 (8th Cir. 2002).

47 484 F. Supp. 2d 953 (S.D. Iowa 2007).

48 Id. at 954.

49 Id.

50 Id. at 955.

51 Faber v. Menard, Inc., 367 F.3d 1048, 1052 (8th Cir. 2004).


53 Gilmer, supra note 4; Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 628 (1985); Arkom Digital, supra note 46, at 538.

54 Kawasaki Motors, supra note 43.


56 Id.

57 See, e.g., Doctor’s Assoc., Inc. v. Casarotto, 517 U.S. 681, 687 (1996) (“generally applicable contract defenses, such as fraud, duress, or unconscionability, may be applied to invalidate arbitration agreements without contravening § 2 of the FAA”); Cap Gemini Ernst & Young, U.S., L.L.C. v. Nackel, 346 F.3d 360, 364 (2d Cir. 2003) (questions of contractual validity relating to the unconscionability of the underlying arbitration agreement must be re-
solved first, as a matter of state law, before compelling arbitration).

58 *Prima Paint, supra* note 13, at 403-04 (fraud in inducement); *Alexander, supra* note 55, at 265 (unconscionability).

59 *Prima Paint, supra* note 13, at 403-04.

60 *Alexander, supra* note 55, at 264-70; *Cap Gemini, supra* note 57 at 364.

61 *Alexander, supra* note 55, at 263.

62 *Id.*

63 *Terminix, supra* note 20, at 1333.

64 *Id.* at 1332-33.