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CPLR 7501: Broad Arbitration Clause Compels Submission of Question of Recovery of Consequential Damages to Arbitrator Notwithstanding Damage Limitation Clause

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Arbitration Act was modelled specifically on the New York arbitration statute. The corresponding provisions should be interpreted similarly.[178] Furthermore, the New York courts, in *Rederi* and *Aerojet*, voluntarily followed the *Prima Paint* holding in maritime and interstate commercial transactions and considered an arbitration clause as distinct from the underlying contract. It is anomalous, therefore, to reject the separability approach when confronted with wholly intrastate activities, there being no compelling public interest requiring a different standard for intrastate commercial dealings.

New York, historically the leader in encouraging arbitration and developing a sophisticated arbitration jurisprudence, should clarify the present confusion as to its treatment of the question of fraudulent inducement and adopt the progressive separability approach of the federal courts. It should no longer remain the only state with a modern arbitration statute to follow a non-separability rule.[179]

CPLR 7501: Broad arbitration clause compels submission of question of recovery of consequential damages to arbitrator notwithstanding damage limitation clause.

In *Allen Knitting Mills v. Dorado Dress Corp.*,[180] the appellant, a textiles seller, applied to stay arbitration on the ground that the respondent, who sought consequential damages, was barred from such recovery by clauses in their contracts limiting the appellant's liability to the difference in value between goods ordered and goods actually received. Each of the arbitration clauses encompassed "[a]ny controversy or claim arising out of or relating to this contract, any interpretation thereof or breach thereof. . . ." The Appellate Division, First Department, affirmed the lower court's denial of a stay, noting that the arbitrator derives his authority from the scope of the arbitration clause,[181]

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178 *See* Aksen at 10. The adoption of CPLR 7501, deleting the terminology declaring arbitration agreements to be "valid, enforceable and irrevocable," which was found in CPA 1448 and is currently found in § 2 of the federal statute, should not be viewed as a modification of New York's traditional approach favoring arbitration. It is the better view that this expression has been deleted as unnecessary. *See* 7B McKINNEY'S CPLR 7501, commentary at 433 (1963); 8 WK&M ¶ 7501.03.

179 "[N]either New Jersey nor Maryland nor any [of the other twenty-one states] with a modern arbitration law — with the possible exception of New York — has formulated a rule of non-separability." Aksen at 9. The separability approach is also widely followed in Europe. *See* Nussbaum, *The "Separability Doctrine" in American and Foreign Arbitration*, 17 N.Y.U.L.Q. REV. 609 (1940).

180 39 App. Div. 2d 286, 333 N.Y.S.2d 848 (1st Dep't 1972) (per curiam).

181 The Court of Appeals, in Exercycle Corp. v. Maratta, 9 N.Y.2d 329, 336, 174 N.E.2d 463, 466, 214 N.Y.S.2d 353, 357 (1961), noted: "Where there is a broad provision for arbitration, . . . arbitration may be had as to all issues arising under the contract."

and holding that, notwithstanding the clause limiting liability, the issue of consequential damages constituted a controversy or claim within the purview of the arbitration clause. The court concluded that the broad clause entitled the arbitrator to determine the applicability, enforceability, and validity of the damage limitation clause,[182] stating that "[w]here as here there is a broad grant of power, we may not curtail the submission on a matter well within that grant of power."[183]

The *Allen Knitting Mills* court relied on *Granite Worsted Mills v. Aaronson Cowen, Ltd.*,[184] in which the Court of Appeals held that an arbitrator need not enforce a damage limitation clause in a contract, but a court may vacate an award unless the arbitrator indicates the basis on which he disregarded the clause.[185] The *Allen Knitting Mills* decision is a logical extension of *Granite Worsted Mills* since to stay arbitration in the face of a broad arbitration clause would be to determine the merits of the case, which the court may not do.[186]

Granite Worsted Mills, which expanded the scope of judicial review of arbitration awards, has been criticized as encouraging unnecessary litigation;[187] but it provides an additional protection for parties, *e.g.*, the appellant in *Allen Knitting Mills*, who must arbitrate a question of damages when liability for such damages was expressly disclaimed in the agreement itself.

See also Terminal Auxiliar Maritima v. Winkler Credit Corp., 6 N.Y.2d 294, 160 N.E.2d 526, 189 N.Y.S.2d 655 (1959); Paloma Frocks, Inc. v. Shamokin Sportswear Corp., 3 N.Y.2d 572, 147 N.E.2d 779, 170 N.Y.S.2d 509 (1958); Lipman v. Haeuser Shellac Co., 289 N.Y. 76, 43 N.E.2d 817 (1942).

182 39 App. Div. 2d at 287-88, 333 N.Y.S.2d at 850. Absent the clause limiting liability there is little question that an arbitrator has the power to award consequential damages. *See* Publishers' Ass'n v. New York Stereotypers' Union No. 1, 8 N.Y.2d 414, 171 N.E.2d 323, 208 N.Y.S.2d 981 (1960); United Buying Serv. Int'l Corp. v. United Buying Serv. of Northeastern New York, Inc., 38 App. Div. 2d 75, 327 N.Y.S.2d 7 (1st Dep't 1971).

183 39 App. Div. 2d at 289, 333 N.Y.S.2d at 851.

184 25 N.Y.2d 451, 255 N.E.2d 168, 306 N.Y.S.2d 934 (1969), *discussed in The Quarterly Survey*, 45 St. John's L. Rev. 145, 175 (1970).

185 The Court argued:

> There is no doubt that an arbitrator, if he so decides, may indeed refuse to enforce such a damage limitation clause on the ground of unconscionability or on other grounds and today's decision does not in any way limit that power. What is required, however, is that the award indicate that he has in fact deliberately and intentionally exercised that power so that judicial review can proceed without the need for speculation as to what in fact occurred in the arbitral tribunal.

Id. at 457, 255 N.E.2d at 171, 306 N.Y.S.2d at 939.

186 39 App. Div. 2d at 288, 333 N.Y.S.2d at 850, *citing* CPLR 7501 *and* Vogel v. Lewis, 25 App. Div. 2d 212, 268 N.Y.S.2d 237 (1st Dep't 1966), *aff'd*, 19 N.Y.2d 589, 224 N.E.2d 738, 278 N.Y.S.2d 236 (1967).

187 One can but regret the majority opinion for it is bound to generate a host of unnecessary litigation. It is particularly unfortunate in light of the fact that the enervating conflict between the courts and the arbitration tribunals had appeared at an end.

Greenberger, *Contracts*, 22 Syracuse L. Rev. 187, 193 (1971).