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CASE NOTES

ADVANCED MICRO DEVICES v. INTEL: DO YOU REALLY WANT TO ARBITRATE?

Advanced Micro Devices, Inc. v. Intel Corp., 16 Cal. App. 4th 346; 20 Cal. Rptr. 2d 73 (1993)

Donna M. Sadowy†

On June 4, 1993, the California Sixth District Court of Appeals ruled that an arbitrator had "exceeded his powers" and thus overturned a substantial portion of the remedies awarded to Advanced Micro Devices (AMD) in a dispute involving a 1982 technology exchange contract between AMD and Intel.¹ Earlier, a superior court judge had upheld the arbitration award. The arbitration which occurred from 1987 to 1992, involved 355 days of hearings, 47,000 pages of reporter's transcripts, and 2,500 exhibits.² Perhaps realizing the importance of this decision to companies agreeing to settle disputes by alternative dispute resolution (ADR), on September 2, 1993, the California Supreme Court agreed to hear AMD's appeal.³ The supreme court's decision is expected sometime in 1994 and should answer questions raised by this case concerning the scope of an arbitrator's powers in dealing with intellectual property rights and in granting remedies.

Advanced Micro Devices is one of a triad of recent and seemingly contradictory California cases dealing with arbitration powers and limits. In the other two cases, *Moncharsh v. Heily & Blase*⁴ and *Pacific Gas and Electric v. Superior Ct.*,⁵ the arbitrator's decisions were

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1. *Advanced Micro Devices v. Intel Corp.*, 16 Cal. App. 4th 346, 348 (6th Ct. App., 1993) (as modified July 2, 1993).

2. Steve Albert, *ADR Not Always Fast, Cheap; Even Some of the Lawyers in AMD and PG&E Cases Says Traditional Litigation Would Have Been Better*, THE RECORDER, Sept. 3, 1993, at 1.

3. *Advanced Micro Devices, Inc. v. Intel Corp.*, 858 P. 2d 567 (Cal. 1993).

4. 3 Cal. 4th 1 (1992).

5. 15 Cal. App. 4th 576 (1993).

upheld at the final level of appellate review.⁶ In the *Moncharsh* decision, the California Supreme Court stated that "[t]he arbitrator's decision should be the end, not the beginning of the dispute."⁷ In most cases, by agreeing to arbitrate, the parties are agreeing to the finality of the arbitrator's decision *without* the multiple layers of appeal possible in litigation. Therefore, what happened in *Advanced Micro Devices* to return this dispute to the courts after such a considered and protracted arbitral proceeding?

In 1982, AMD and Intel signed a contract to exchange for the next 10 years "technical information so that each party acquire[d] the capability to develop products suitable for sale as an alternate source for products developed by the other party."⁸ Essentially, the purpose was to set up a second-source arrangement for both companies. AMD could "earn" rights to manufacture Intel products and to receive a "Manufacturing Package" from Intel, by developing its own products that Intel in turn wanted to manufacture. Licensing rights were also included, coupled with an obligation to pay royalties for each sale of an exchanged product.⁹ The contract also contained an agreement that the two companies would arbitrate any disputes which might "arise under this Agreement."¹⁰

Unhappy with the progress of the contract, AMD initiated arbitration in 1987. The arbitrator, retired Superior Court Judge J. Barton Phelps, was to decide whether Intel had breached contractual obligations of good faith and fair-dealing.¹¹ Secondly, the arbitrator was called on to decide whether Intel should be compelled to provide AMD with the Manufacturing Package as well as licensing rights for its highly successful 80386 (or "386") microprocessor.¹² With regard to remedies, the two parties stipulated that "[t]he Arbitrator may grant any remedy or relief which the Arbitrator deems just and equitable and within the scope of the agreement of the parties, including, but not limited to, specific performance of a contract," and that the arbitrator

6. *Moncharsh*, 3 Cal. 4th at 33; *Pacific Gas and Electric*, 15 Cal. App. 4th at 612.

7. *Moncharsh*, 3 Cal. 4th at 10.

8. *Advanced Micro Devices*, 16 Cal. App. 4th at 348-49. Unless otherwise noted, the facts of *Advanced Micro Devices* are discussed in the unanimous three-judge appellate court decision authored by Judge P.J. Cottle.

9. *Id.* at 349.

10. *Id.* at 355.

11. *Id.* at 349.

12. While there were multiple semiconductor products at issue, most of the debate concerned the 80286 and 80386 microprocessors utilized in IBM and IBM-compatible personal computers.

could grant remedies "as he may in his discretion determine to be fair and reasonable but not in excess of his jurisdiction."¹³

In 1990, Judge Phelps issued his opinion on liabilities. He found that Intel had breached the 1982 contract by delaying the exchange of information, by providing AMD with erroneous information on its 80286 chip, and by failing to transfer its 8087 math coprocessor to AMD.¹⁴ Based on a review of internal Intel documents, he felt that these acts were the direct result of policy decisions made by Intel to frustrate the contract, to reject any products from AMD, and to keep this intent secret from AMD.¹⁵ Intel's actions were described as "a classic example of a breach of the covenant of good faith and fair dealing, preaching good faith but practicing duplicity."¹⁶ In turn, Judge Phelps stated that AMD had failed to provide Intel with acceptable products under the technology exchange agreement, and had harmed itself by failing to keep up with changing technology.¹⁷ He likewise found that AMD breached the covenant of good faith and fair dealing by providing Intel with a modem circuit while subsequently selling an updated version of the product.¹⁸ In 1990, AMD began selling the AM386, its version of the 386 microprocessor.¹⁹

The separate hearing on remedies was completed in 1992.²⁰ Judge Phelps concluded that it was Intel's intent to withhold its 386 chip from AMD, to pressure AMD to renegotiate the contract, and to delay AMD's production of a competing product.²¹ However, AMD was not entitled to the Intel 386 chip technology because AMD had not developed any acceptable products to exchange with Intel. Therefore, harm suffered by AMD was both a result of AMD's own "inertia" in developing products that it could have exchanged for the 386 technology and AMD's delay in seeking arbitration.²² The arbitrator awarded AMD over \$15 million for Intel's delay in sending AMD updated information on the 80286, and for the failure of Intel to deliver promised product information, as well as the Manufacturing

13. *Advanced Micro Devices*, 16 Cal. App. 4th at 349.

14. *Intel/AMD Dispute Developments*, 7 COMPUTER LAW., Nov. 1990, at 30.

15. *Id.*

16. Robert Ristelhueber, *Intel, AMD Scored by Arbitrator; AMD's Rights to 80386 Still Not Decided; Advanced Micro Devices' Suit for Rights to Intel's 80386 Microprocessor*, 36 ELECTRONIC NEWS, Oct. 15, 1990, at 1.

17. *Id.*

18. *Id.*

19. *Advanced Micro Devices*, 16 Cal. App. 4th at 350.

20. *AMD/Intel Arbitration Ends as Arbitrator Awards AMD Damages*, 9 COMPUTER LAW., Apr. 1992, at 34.

21. *Id.*

22. *Id.*

Package for the Intel 8087 chip.²³ For breach of the covenant of good faith and fair dealing, AMD was awarded nominal damages of \$1 plus the following remedies, contained in paragraphs five and six of the award:

¶ 5. AMD is hereby awarded a permanent, royalty-free, non-exclusive, non-transferrable, worldwide right (but not the right to assign, license or sublicense such right to any other party) under any and all Intel copyrights, patents, trade secrets and maskwork rights contained in the current versions of AMD's reversed-engineered 80386 family of microprocessors, to make, have made by a third party solely for AMD, use and sell the prior, and current future revisions and modifications of those products. . . . The intent of this paragraph is to provide a complete and dispositive defense to AMD as the Intel claims against AMD regarding the technology and intellectual property used in AMD's current versions of the 80386 in such lawsuits as *Intel Corp. v. Advanced Micro Devices, Inc.* . . . and to preclude and defeat other potential Intel intellectual property infringement claims with respect to the technology used in AMD's aforescribed past and current versions, and future revisions and modifications, of the 80386. . . .

¶ 6. In addition to the nominal damages awarded AMD for Intel's breaches as set forth . . . it is ordered that the rights conferred upon AMD under the 1982 AMD/Intel Agreement (which extended until 1995 the patent and copyright licenses originally granted by an agreement between the parties in 1976) are hereby extended two years from their present date of expiration only insofar as they relate to or concern the AMD 80386 and its revisions or modifications, if any.²⁴

The arbitrator explained the award in paragraphs five and six as an "attempt to abort the incessant warfare which has gone on between these companies Each of them has attempted to use the court system as a means of corporate strategy."²⁵ Moreover, he authorized AMD to initiate "its production and sale of the reverse engineered 80386 without harassment from Intel from any further law suit . . . because of the manner in which Intel to some extent lulled AMD into some sense of well-being about the continuation of the relationship and to some extent contributed to AMD's delay in reverse engineering the 80386" ²⁶ He also found that the two year extension of the

23. *Id.*

24. *Advanced Micro Devices*, 16 Cal. App. 4th at 350.

25. *Id.* at 350-51.

26. *Id.* at 351.

licenses granted to AMD under the contract was just and equitable.²⁷ Judge Phelps refused AMD's request to award attorney's fees.²⁸

Intel appealed the award, claiming a lack of power on the arbitrator's part to award the remedies discussed in paragraphs five and six. AMD argued that the scope of powers with respect to remedies was for the arbitrator to determine, and was not appealable.

California's private arbitration statute is located in its Code of Civil Procedure, §§ 1280-1294.2. It contains provisions for both vacating an award, in § 1286.2, and correcting an award, in § 1286.6. Courts have the power to correct an award under § 1286.6(b) if "[t]he arbitrators exceeded their powers but the award may be corrected without affecting the merits of the decision upon the controversy submitted."²⁹

The appeals court found that the scope of the arbitrator's remedial powers was a question of law, up to the courts to decide "except where the parties have unambiguously and expressly given such power to the arbitrator."³⁰ Judge Cottle found that this was not such an "exceptional" case, based on the jurisdictional hearings.³¹ He quoted AMD from the record of the hearing: "[i]n the event either party believes that any relief awarded is beyond the jurisdiction of the arbitrator, that is a specific ground upon which to challenge its confirmation or to appeal from the Arbitrator's award."³² Similarly, he quoted the arbitrator as deciding to make each award severable "in the event the Arbitrator's conclusion in respect to a particular issue or issues be deemed to be in violation of Code of Civil Procedure section 1286.2 . . . [or] 1286.6" ³³

Judge Cottle found support for the court's limitations on remedial power in case law, starting with the test enunciated by the U.S. Supreme Court: "an arbitrator is confined to interpretation and application of the . . . agreement; . . . his award is legitimate only so long as it draws its essence from the . . . agreement."³⁴ In addition, the court discussed two California Appellate Court cases. In the first case, an arbitrator's award of damages rather than real property was overturned because the original agreement specified a transfer of real property in

27. *Id.* at 351.

28. *AMD/Intel Arbitration Ends as Arbitrator Awards AMD Damages*, *supra* note 20.

29. CAL. CODE CIV. PROC. §§ 1280-1294.2 (West 1982 & Supp. 1993).

30. *Advanced Micro Devices*, 16 Cal. App. 4th at 352.

31. *Id.* at 353.

32. *Id.*

33. *Id.*

34. *Id.* (quoting *United Steelworkers v. Enter. Wheel & Car Corp.*, 363 U.S. 593, 597 (1960)).

consideration for performance of services.³⁵ In the second case, an arbitrator's award of vacation pay, according to one classification of labor, for an employee temporarily working in another classification, was overruled because it violated the basic contractual agreement.³⁶

As mentioned previously, AMD and Intel's stipulated terms were that the arbitrator could grant any remedy believed to be just and equitable, within the scope of their contract, and not outside of his jurisdiction. Thus, the language of the stipulation was not specific on what remedies could be granted. AMD argued that since nothing in the agreement expressly prohibited the remedies granted, it was within the arbitrator's powers to grant them. AMD used as the basis for this argument a California Court of Appeal case that held that the only remedy an arbitrator in a labor contract dispute was prohibited from granting was money damages; therefore, "any other remedy not inconsistent with the collective bargaining agreement" could be ordered.³⁷

Judge Cottle did not agree with AMD's interpretation of this case, using as the basis for his decision the U.S. Supreme Court's direction that a remedy must "draw its essence from the agreement."³⁸ He stated a two-part test for the granting of remedies: a remedy must be rationally related to the meaning and purpose of an agreement (there must be a "rational nexus"), and it can not be expressly prohibited by the agreement.³⁹ As mentioned previously, AMD and Intel agreed in their 1982 contract to arbitrate disputes that might arise under the agreement. While Judge Cottle felt that it was within the arbitrator's power to provide contract remedies, "the arbitrator granted to AMD rights which exceeded those it could have obtained from Intel under the contract."⁴⁰ The arbitrator decided that AMD had not earned rights to the Intel 386 chip technology under the contract, therefore Judge Cottle did not believe it was possible to award AMD any rights to Intel intellectual property contained in the AM386. Furthermore, the AM386 was not a product AMD could ever have earned under the 1982 contract. The court held that the arbitrator "rewrote

35. *Drake v. Stein*, 116 Cal. App. 2d 779 (1953).

36. *Firestone Tire & Rubber Co. v. United Rubber Workers of America, Local Union 100*, 168 Cal. App. 2d 444 (1959). In *Posner v. Grunwald-Marx Inc.*, 56 Cal. 2d 169 (1961), the California Supreme Court disapproved that part of the opinion that held that when the language of a collective bargaining agreement is "unambiguous" there is no need for any contractual interpretation by the arbitrator.

37. *Southern Cal. Rapid Transit Dist. v. United Transp. Union*, 5 Cal. App. 4th 416, 424 (1992). Judge Cottle did not identify any cases cited by Intel.

38. *Steelworkers*, 363 U.S. at 597.

39. *Advanced Micro Devices*, 16 Cal. App. 4th at 355.

40. *Id.*

the parties' agreement" by giving AMD rights to sell the AM386 without any exchange of products under the contract.⁴¹

Judge Cottle also found that the right to have the AM386 manufactured by a third party was specifically withheld.⁴² Likewise, the fact that AMD was not required to pay royalties to Intel on the AM386 was cited as contrary to the 1982 contract.⁴³ Finally, the fact that the arbitrator extended the patent and copyright licensing agreement for two years was also considered outside the scope of the contract.

Because these remedies were adjudged outside of the scope of the original contractual terms, the appellate court found that the arbitrator had exceeded his power. Since the court felt that the award could be corrected under California Code Civil Procedure § 1286.2 without affecting the merits of the case, only the remedies granted in paragraphs five and six were struck down. The other remedies were considered to be within the scope of the agreement and were ruled valid.

ANALYSIS:

Advanced Micro Devices will ultimately be decided by the California Supreme Court on the issue of whether the arbitrator exceeded his statutory grant of powers. The most recent state supreme court case dealing with arbitral powers, *Moncharsh*, was decided in 1992. In that case, the California Supreme Court affirmed an appellate court decision upholding an arbitral award in a dispute between an attorney and his former law firm.⁴⁴ The court in *Moncharsh* found that the basis for the arbitrator's power was a legislative scheme with a "strong public policy in favor of arbitration."⁴⁵ The general rule is that the arbitrator's decision is final, even if this is not expressly stated in the agreement, because parties assume this risk when agreeing to arbitration.⁴⁶ The trade-off for this risk is that arbitration saves time and money. Also, arbitrators need not make their award on principles of law alone, "but may decide on principles of equity and good conscience, and make their award . . . [according to what is just and good]."⁴⁷ Because the parties intend that the award be final and be-

41. *Id.* at 356.

42. *Id.*

43. *Id.* These final conclusions seems somewhat contradictory to the previous reasoning since the arbitrator's decision to award the AM386 under the AMD/Intel contract was described as having "rewrote the parties' agreement."

44. *Moncharsh*, 3 Cal. 4th at 33.

45. *Id.* at 9.

46. *Id.*

47. *Id.* at 11.

cause the arbitrator has freedom to go beyond the rules of law, courts are not to review the validity of an arbitrator's reasoning.⁴⁸

Moncharsh also held that the arbitrator's decision cannot be reviewed for either errors of fact or law, subject to narrow exceptions. It cannot even be reviewed "for errors on the face of the arbitration award causing substantial injustice" because of legislative intent to reject this basis.⁴⁹ Exceptions to these general rules include the statutory exceptions contained in §§ 1286.2 and 1286.6, including "when the arbitrators exceeded their powers," illegality, or a legislative expression of public policy.

The *Moncharsh* court made a brief, but specific pronouncement in regards to arbitrators exceeding their powers. Arbitrators do not exceed their powers "merely because they assign an erroneous reason for their decision."⁵⁰ Arbitrators *do* exceed their powers when they attempt to resolve issues the parties never agreed to arbitrate.⁵¹

In 1993, the California Supreme Court refused to review a Third District Appellate Court decision upholding an arbitration award in *Pacific Gas & Electric*.⁵² The appellate court reversed a superior court decision which had vacated the arbitrator's award. The court cited *Moncharsh*, in finding that arbitrators do not exceed their powers "merely" by reaching a wrong decision—"[t]he test is one of arbitrariness, not correctness."⁵³ Arbitrariness is created by an "egregious mistake" that arbitrarily remakes the contract.⁵⁴ As in *Moncharsh*, arbitrators were found to have substantial power to resolve disputes concerning the meaning, interpretation, and application of contract clauses. A "completely irrational" legal conclusion is required to find that arbitrators have exceeded their powers.⁵⁵

In *Pacific Gas & Electric*, the court also rejected the contention that there can be no reformation of the contract by an arbitrator. Reformation by an arbitrator can occur because of a mistake in the writing, or when contract language is "so ill-chosen as to mislead third persons, and to enable one of the parties to take an unjust advantage of

48. *Id.* at 11. As the court notes, parties entering a private arbitration agreement can specifically require the arbitrator to reach a decision based on rules of law.

49. *Moncharsh*, 3 Cal. 4th at 25.

50. *Id.* at 28.

51. *Id.*

52. *Pacific Gas & Electric Co. v. Superior Ct.*, 15 Cal. App. 4th 576. This case was referenced in *Advanced Micro Devices*, 16 Cal. App. 4th at 356 n.2, where it was described as "not inconsistent" with that court's opinion.

53. *Pacific Gas & Electric*, 15 Cal. App. 4th at 594.

54. *Id.* at 592-93.

55. *Id.* at 592.

the other.”⁵⁶ Such a broad arbitral power to reform a contract appears contrary to the Sixth District decision in *Advanced Micro Devices*.

Another difference between the two appellate cases was the amount of discussion concerning the significance of a breach of the covenant of good faith and fair dealing. The Sixth District in *Advanced Micro Devices* provided little, if any, discussion of the arbitrator’s finding that one party had intentionally frustrated performance of the contract. The arbitrator involved in the dispute in *Pacific Gas & Electric* ruled that no breach of the implied covenant of good faith and fair dealing had occurred. The Third District upheld the arbitrator’s decision, finding that the arbitrator can be reversed not on mere error of law, but on an “error of law that discards an unmistakable expectation of an implied covenant under the contract.”⁵⁷

Despite any possible contradictions, a review of *Advanced Micro Devices*, *Moncharsh*, and *Pacific Gas & Electric* makes it clear that there are key issues to be considered by any party agreeing to arbitrate. Paramount among these is that the contract terms detailing the arbitration agreement will rule the arbitration.⁵⁸

Arbitration agreements can restrict remedies, address discovery and evidentiary rules, describe how much written documentation is required to support the award, the number of arbitrators, arbitrators background or expertise, and arbitrator selection.⁵⁹ Alternatively, parties can agree to use guidelines developed by the American Arbitration Association, the International Chamber of Commerce, or other bodies. Parties should also be aware that their disputes may be governed by federal, rather than state arbitration statutes if their dispute is one involving interstate commerce.

A party agreeing to arbitration needs to decide beforehand the degree to which they want to restrict the arbitrator’s powers. Clearly, this will not always be an easy decision. A contract that was good business strategy ten to fifteen years previously may become hard to live with as a company’s fortune changes over the years.

If an arbitration agreement states that it is binding, the chances that there will be any judicial review are slim. Even if this is not addressed in the contract, there is a presumption that the parties intended a binding arbitration, as stated in *Moncharsh*. If the finality of

56. *Id.* at 593, quoting 3 ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 540, at 92 (1962).

57. *Pacific Gas & Electric*, 15 Cal. App. 4th at 609.

58. *See, e.g., Moncharsh*, 3 Cal. 4th at 8.

59. *See generally* Kenneth B. Clark & William A. Fenwick, *Structuring an Arbitration Agreement for High Technology Disputes*, 9 COMPUTER LAW., Sept. 1992, at 22. One additional issue to be considered is how likely experts in a particular field are to have preconceived opinions and biases. This may be one trade-off for obtaining the benefit of their knowledge.

an arbitration decision is not acceptable, a party should clearly state this in the agreement or not enter arbitration at all.

If parties agree to arbitrate "any dispute arising out of" the contract, they are agreeing to much greater arbitral power than if they narrowly define arbitration issues. If two parties disagree on any issue or interpretation under the contract, then there is a dispute that developed out of the contractual arrangement. Such broad language was cited as a reason behind the court's decision to uphold the arbitral award in *Moncharsh*.⁶⁰

Parties can agree to put limitations on remedies. If no limits are agreed upon, a party should realize that the statutory underpinnings of California contractual law are that "[f]or the breach of an obligation arising from contract, the measure of damages, except where otherwise expressly provided by this [California Civil] Code, is the amount which will compensate the party aggrieved for all the detriment proximately caused thereby, or which, in the ordinary course of things, would be likely to result therefrom."⁶¹ In other words, the basic idea behind awarding contract damages is that "the party injured by breach should receive as nearly as possible the equivalent of the benefits of performance."⁶² Considering that the arbitrator is not bound solely by principles of law but can also provide equitable remedies, this is an open-ended invitation for the arbitrator to create remedies.

Complex disputes, such as the one involved in *Advanced Micro Devices*, are less likely to achieve the twin goals of arbitration — the reduction of time and the reduction of costs required to settle a dispute. On the other hand, it is impossible to know how quickly the dispute would have been resolved if it had been litigated. In any case, arbitration may not be appropriate for all disputes. For example, if an extensive discovery process is required by a party to develop their evidence, arbitration is not the appropriate method of dispute resolution.

While ADR, including arbitration, may appear to be an attractive alternative to litigation, contracting parties should understand its ramifications before signing on. Additionally, parties should be aware of recent state or federal decisions in their jurisdiction defining arbitral powers. The upcoming California Supreme Court decision in *Advanced Micro Devices*, which should define the scope and finality of an arbitrator's decisions, will generate strong emotions among at least

60. *Moncharsh*, 3 Cal. 4th at 28.

61. CAL. CIV. CODE § 3300 (West 1970 & Supp. 1993).

62. 1 B.E. WITKIN, SUMMARY OF CALIFORNIA LAW, § 813 (1987 & Supp. 1993).

two Silicon Valley companies. It should be reviewed by any California high tech company considering arbitration.

