The U.S. Supreme Court and Arbitration: Their Love Is Here to Stay

This short article summarizes five opinions that impact the shape and direction of arbitration in the United States. New Jersey has tried to chip away at mandatory arbitration, but SCOTUS has made clear that unless federal law is changed, mandatory arbitration is here to stay.

By **Jed Marcus** | August 09, 2019

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There is no livelier topic in the labor and employment eco-sphere than the enforceability of arbitration agreements. The United States Supreme Court recently issued several vitally important opinions involving their scope and enforceability, including the enforceability of class action waivers, the preemption of state laws and rules, and the jurisdiction of arbitrators to resolve “gateway issues” of arbitrability. This short article summarizes five opinions that impact the shape and direction of arbitration in the United States.

The court recently issued two important decisions enforcing class action waivers in

arbitration agreements. In *Epic Systems Corp. v. Lewis*, 138 S.Ct. 1612 (2018), it held that class action waivers do not violate the National Labor Relations Act (NLRA), rejecting the argument that the NLRA overrides the Federal Arbitration Act (FAA). According to the court, there exists no "clear and manifest" congressional intention to displace one act with another. First, class and collective actions are not "concerted activities" protected by the NLRA because it focuses only on the right to organize unions and bargain collectively without ever mentioning class or collective action procedures or hinting at a clear and manifest wish to displace the FAA. Second, the NLRA, while establishing a detailed regulatory regime for the protection of "concerted activities," contains no rules, either expressly or implicitly, governing the adjudication of class or collective actions in court or arbitration. Third, the employees' underlying causes of action arise under the Fair Labor Standards Act, which permits collective actions but also does not prohibit individualized arbitration proceedings. Fourth, the National Labor Relations Board is not entitled to deference because it sought not simply to interpret just the NLRA, "which it administers," but to interpret the NLRA in a way that limits the work of the FAA, which it does not administer.

In *Lamps Plus v. Varela*, No. 17-988, 2019 U.S. LEXIS 2943 (April 24, 2019), the court ruled that class-wide arbitration may not be compelled where the arbitration agreement is "ambiguous" as to whether class arbitration is permitted, reversing the district court and the Court of Appeals for the Ninth Circuit below, both of which held that because the arbitration agreement was ambiguous, the ambiguity should be held against the drafter, in this case, the employer. In reversing, the court noted that because "arbitration 'is a matter of consent, not coercion'" *id*. at *11, and it is the intention of the parties that is critical, the identity of the drafter is irrelevant. *Id*. at *15. Class arbitration is different from traditional individualized arbitration, and "undermines the most important benefits of that familiar form of arbitration." *Id*. at *8. Under the FAA, "ambiguity does not provide a sufficient basis to conclude that parties to an arbitration agreement agreed to 'sacrifice[] the principal advantage of arbitration.'" *Id*. at *13.

Two recent cases show how the court views the preemptive effect of the FAA. In *Lamps Plus* (discussed above), the court found that the doctrine of contra proferentem (ambiguities are to be construed against the drafter) was not, in fact, an interpretative tool designed to find the intentions of the parties, and, therefore, cannot form the basis for striking down an arbitration agreement. This default rule "is by definition triggered only after a court determines that it cannot discern the intent of the parties." 2019 U.S. LEXIS 2943 at *16. Thus, "courts may not rely on state contract principles to 'reshape traditional individualized arbitration by mandating classwide arbitration procedures without the parties' consent.'" *Id*.

In *Kindred Nursing Ctrs. v. Clark*, 137 S.Ct. 1421 (2017), the court held that application of a Kentucky state rule that compelled an individual to explicitly waive a right to trial when

executing a power of attorney agreement violated the FAA because it "singles out arbitration agreements for disfavored treatment." *Id.* at 1425. The court rejected Kentucky's attempt to subject arbitration agreements to a heightened "clear statement" standard, thus emphasizing that the FAA will preempt not only a state law that "discriminat[es] on its face against arbitration," but also a state law that "covertly accomplishes the same objective by disfavoring contracts that have the defining features of arbitration agreements." *Id*. at 1426. Thus, a court may not invalidate an arbitration agreement based on legal rules that "apply only to arbitration or that derive their meaning from the fact that an agreement to arbitrate is at issue." The state court's "clear statement" rule ran afoul of the FAA because it "flouted the FAA's command to place [arbitration] agreements on an equal footing with all other contracts." *Id*. at 1429.

The *Kindred* decision may play a role in determining whether the FAA preempts state laws banning mandatory arbitration of discrimination cases. Proponents of New Jersey's ban claim that the FAA is inapplicable because, inter alia, the law concerns contract formation rather than contract enforcement. However, the court specifically rejected this argument, stating that the FAA's direction that arbitration agreements be treated as "valid" means that "[a] rule selectively finding arbitration contracts invalid because improperly formed fares no better under the Act than a rule selectively refusing to enforce those agreements once properly made." *Id*. at 1428. Placing contract-formation rules wholly outside the ambit of FAA preemption "would make it trivially easy for States to undermine the [FAA]—indeed, to wholly defeat it." *Id*.

Finally, the court addressed exactly who gets to decide whether a dispute is arbitrable and under what circumstances. The issue before the court in *Henry Schein v. Archer & White Sales*, 139 S.Ct. 524 (2019), was whether or not a court had the authority to deny a motion to compel arbitration even though the arbitration agreement delegated the question of arbitrability to an arbitrator because the movant's argument for arbitration was "wholly groundless." The court held that it could not, reasoning that "a court may not decide an arbitrability question that the parties have delegated to an arbitrator," and observing that "[t]he ['wholly groundless'] exception is inconsistent with the statutory text and with our precedent. It confuses the question of who decides arbitrability with the separate question of who prevails on arbitrability. When the parties' contract delegates the arbitrability question to an arbitrator, the courts must respect the parties' decision as embodied in the contract." *Id*. at 529.

Interestingly, the court did not decide whether or not the parties, having expressly agreed to incorporate the arbitration rules of the American Arbitration Association (AAA), "clearly and unmistakably" delegated the issue of arbitrability to the arbitrator. The court noted that "[w]e express no view about whether the contract at issue in this case delegated the arbitrability question to an arbitrator. The Court of Appeals did not decide that issue." *Id*. at 530-31.

This unanswered question has practical import for both advocates and arbitrators, because many agreements incorporate the AAA rules by reference. AAA Rule 6(a) provides that "the 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," and Rule 6(b) provides, inter alia, that "the arbitrator shall have the power to determine the existence or validity of a contract of which an arbitration clause forms a part." Does such incorporation "clearly and unmistakably" evince an intent to arbitrate arbitrability? Here, the courts are split. The Tenth and Eleventh Circuits concluded that the incorporation of AAA rules was "clear and unmistakable" evidence that the parties intended to delegate gateway issues to the arbitrator. *Spirit Airlines v. Maizes*, 899 F.3d 1230 (11th Cir. 2018); *Dish Network v. Ray*, 900 F.3d 1240 (10th Cir. 2018). While the Third Circuit has held that the incorporation of AAA rules alone is not a "clear and unmistakable" delegation of authority to the arbitrator. *Chesapeake Appalachia v. Scout Petroleum*, 809 F.3d 746, 758 (3d Cir. 2016).

The most recent case is *New Prime v. Oliveira*, 139 S. Ct. 532 (2019), where the court, while finding that certain interstate transportation workers are exempt under §1 of the FAA, held that it is for the court to decide whether the exemption applies, even if the parties' agreement otherwise delegates questions of arbitrability to an arbitrator. *Id*. at 538.

In *New Prime*, a group of drivers for an interstate trucking company, whose operating agreements referred to them as independent contractors, filed a class action lawsuit for alleged wage violations. When the company moved to compel arbitration, the drivers resisted, pointing out that because they were "workers engaged in foreign or interstate commerce," they were exempt from the act pursuant to §1 of the FAA, which, inter alia, exempts from coverage "contracts of employment of … workers engaged in foreign or interstate commerce." 9 U.S.C. §1. In response, the employer argued that the arbitrator should decide that issue based on the parties' delegation clause, and that the exemption applies only to employees, not to independent contractors. *Id*. at 541-542.

The court affirmed both the district court and the First Circuit Court of Appeals, emphasizing that if the workers in question are indeed engaged in interstate commerce and thus exempt from the FAA's coverage, §§2, 3 and 4, which authorize the court to stay a case and compel arbitration, do not apply. *Id*. at 537. Thus, when the question is whether the FAA applies at all, the parties' delegation clause is unenforceable.

New Jersey has tried to chip away at mandatory arbitration, but the court has made clear that unless federal law is changed, mandatory arbitration is here to stay. Can New Jersey's ban on mandatory arbitration of discrimination disputes survive an attack under the FAA? That remains to be seen, although a recent case out of the Southern District of New York held that the FAA preempted New York's ban on mandatory arbitration of sex harassment disputes. *Latif v. Morgan Stanley & Co.*, Civ. No. 18-11528, 2019 U.S. Dist.

LEXIS 107020 (S.D.N.Y. June 26, 2019). Stay tuned.

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