Schein v. Archer: U.S. Supreme Court Again Reinforces Arbitration Agreements

Once again, United States Supreme Court has continued with its line of cases confirming the enforceability of arbitration in the United States. [1]

Adding to those precedents supporting arbitration, on January 8, 2019, the Supreme Court issued its decision in *Henry Schein, Inc. v. Archer and White Sales, Inc*.[2] In the case, respondent Archer & White Sales, a small distributor of dental equipment, had brought suit against petitioner Henry Schein, a dental equipment manufacturer, claiming that petitioner had violated federal and state antitrust law. The suit sought money damages as well as injunctive relief. The contract between the parties contained an arbitration clause which provided that any dispute "arising under or related to [the] Agreement (except for actions seeking injunctive relief…), shall be resolved by binding arbitration in accordance with the arbitration rules of the American Arbitration Association [(AAA)]."

In the District Court, petitioner had requested that the matter be referred to arbitration based on the Federal Arbitration Act (FAA); respondent, however, argued that because the complaint was seeking injunctive relief, even if only in part, the claim could not be subject to arbitration.[3] Petitioner countered by arguing that arbitrators have the authority to resolve arbitrability questions, and as such, the arbitrator (rather than the court) should be the one to decide whether the case would proceed in arbitration.[4]

In response to this contention, respondent pointed to the "wholly groundless" exception adopted by several lower courts, which essentially held that if a claim of arbitrability is wholly groundless, it would be a waste of time to send a case to an arbitrator, and thus a court has the authority to decide a threshold question of arbitrability.[5] The District Court accepted respondent's argument, finding that because petitioner's complaint sought (in part) injunctive relief, and because the contract provided that suits seeking injunctive relief were not subject to arbitration, any claim of arbitrability was wholly groundless.[6] Therefore, the District Court refused to compel arbitration, and the United States Fifth Circuit affirmed.[7]

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[1] One example is *Hall Street Associates, L.L.C. v. Mattel, Inc.* There, toy manufacturer Mattel was sued by its landlord, Hall Street Associates. The arbitration agreement contained an uncommon provision stating that "if the arbitrator's conclusions of law are erroneous," a District Court had the authority to overturn the arbitrator's decision. This provision was questionable in that it would grant a court considerable supervisory authority over arbitrators that was not granted by the FAA. The FAA only provides for narrow circumstances in which a court can override an arbitration decision. The Supreme Court invalidated the contractual provision at issue, holding that the FAA's provisions are exclusive and not susceptible to contractual expansion or modification by the parties to an agreement.

[2] 139 S. Ct. 524 (2019)

[3] *Archer & White Sales, Inc. v. Henry Schein, Inc.*, No. 2:12-CV-572-JRG, 2016 WL 7157421, at *1, *4 (E.D. Tex. Dec. 7, 2016), *aff'd*, 878 F.3d 488 (5th Cir. 2017), *vacated and remanded*, 139 S. Ct. 524 (2019).

[4] *Id.* at *4.

[5] *Id.* at *6.

[6] *Id.* at *9.

[7] *See Archer & White Sales, Inc. v. Henry Schein, Inc.*, 878 F.3d 488 (5th Cir. 2017), *cert. granted*, 138 S. Ct. 2678, 201 L. Ed. 2d 1071 (2018), and *vacated and remanded*, 139 S. Ct. 524 (2019)

The United States Supreme Court granted certiorari to determine whether the "wholly groundless" exception is consistent with the FAA.[8] In a unanimous opinion authored by Justice Kavanaugh, the Court held that the exception is inconsistent with both the FAA and with Supreme Court precedent.[9] The Court reasoned that, pursuant to the FAA, courts are bound to enforce arbitration contracts according to the terms of the contracts themselves. Under the FAA and Supreme Court precedent, "the question of who decides arbitrability is itself a question of contract."[10] If the a contract calls for an arbitrator to decide "gateway questions of arbitrability," a court may not override the contract, even if the court determines that the claim of arbitrability may be "wholly groundless."[11] To do so, the Court reasoned, would be to "short-circuit the process" of arbitration called for by the contract.[12] The Court noted that the FAA contains no such exception, and that it is not the Court's role to rewrite the statute.[13] The Court vacated the judgment of the lower courts and remanded the case to the Fifth Circuit to address the issue of whether the relevant contract delegated the question of arbitrability to an arbitrator.[14]

In formulating its holding, the Court first looked to the express language of the FAA, which provides, in relevant part:

> A written provision in…a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract…shall be valid, irrevocable, and enforceable, save upon any grounds as exist at law or in equity for the revocation of any contract.[15]

The Court looked to its own precedent, which held that "parties may agree to have an arbitrator decide not only the merits of a particular dispute but also gateway questions of arbitrability, such as whether the parties have agreed to arbitrate or whether their agreement covers a particular controversy."[16] This agreement regarding questions of arbitrability is treated just like any other contract to arbitrate, and thus, the Court reasoned, it should be upheld under the FAA.

The Court then turned to a discussion of the "wholly groundless" exception itself, addressing some Court of Appeals' reasoning that "the 'wholly groundless' exception enables courts to block frivolous attempts to transfer disputes from the court system to arbitration." The Court rejected this argument, positing that it is the province of the courts to "interpret the [FAA] as written," which "requires that we interpret the contract as written." In cases where the parties' contract provides that arbitrability questions be delegated to the arbitrator, the court cannot decide that issue, "even if the court thinks that the argument that the arbitration agreement applies to a particular dispute is wholly groundless." The Court looked to its ruling in *AT&T Technologies, Inc. v. Communications Workers*, 475 U.S. 643 (1986), in which it held that a

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[8] *Henry Schein, Inc.*, 139 S. Ct. at 528.
[9] *Id.* at 531.
[10] *Id.* at 527.
[11] *Id.* at 529.
[12] *Id.* at 527.
[13] *Id.* at 528.
[14] *Id.* at 531.
[15] 9 U.S.C. § 2.
[16] *Henry Schein, Inc.*, 139 S. Ct. at 529 (citing *Rent–A–Center, West, Inc. v. Jackson*, 561 U.S. 63, 68–69 (2010)) (internal quotations omitted).

court "may not rule on the potential merits of the underlying claim that is assigned by contract to an arbitrator, even if it appears to the court to be frivolous." The Court stated that this principle from AT&T Technologies "applies with equal force to the threshold issue of arbitrability."

Following its overview of the FAA and the Court's precedent, the Court addressed and rejected each of respondent's four principal arguments. First, respondent pointed to § 3 and 4 of the FAA, arguing that they signified that "a court must always resolve questions of arbitrability and that an arbitrator may never do so."[17] The Court rejected this, noting that "that ship has sailed," since the Court has consistently held that so long as the parties' agreement delegates threshold arbitrability questions to an arbitrator by "clear and unmistakable" evidence, then such an agreement will be upheld.[18] Next, respondent pointed to § 10 of the FAA, which provides for "back-end judicial review" of an arbitrator's ruling if the arbitrator has "exceeded" his or her "powers." Respondent argued that if a court has this authority on the back end, then the court should also have the authority on the front end to say that an underlying dispute is not arbitrable. The Court rejected this, noting that "Congress designed the Act in a specific way, and it is not [the Court's] proper role to redesign the statute."

Respondent's third argument centered on policy and practicality: "it would be a waste of the parties' time and money," respondent posited, "to send the arbitrability question to an arbitrator if the argument for arbitration is wholly groundless." The Court quickly disposed of this argument, noting that the FAA contains no such exception, and that courts are without authority to create their own exceptions. Moreover, the Court continued, "it is doubtful that the 'wholly groundless' exception would save time and money systemically even if it might do so in some individual cases."[19] Instead, the Court reasoned, the exception would likely ignite a host of collateral litigation "over whether a seemingly unmeritorious argument for arbitration is *wholly* groundless, as opposed to groundless." Finally, respondents asserted that, as a matter of policy, the "wholly groundless" exception is needed in order to prevent frivolous motions to compel arbitration. The Court reiterated that it "may not rewrite the statute simply to accommodate that policy concern," and chided respondent for overstating the problem: "We are not aware the frivolous motions to compel arbitration have caused a substantial problem in those Circuits that have not recognized a "wholly groundless" exception."

The Supreme Court's holding in this case can be seen as the resolution of nearly a decade of judicial uncertainty regarding threshold questions of arbitrability. In its 2010 decision in *Rent-A-Center, West, Inc. v. Jackson*, the Court considered whether the FAA applied to the gateway question of arbitrability.[20] There, the Court held that parties could contractually agree to delegate the decision of this threshold question to an arbitrator. Even so, some lower courts such as the ones discussed above, opted to create and follow the "wholly groundless" exception, rationalizing that "courts would conduct a more-efficient threshold inquiry and that judicial

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[17] "Section 3 provides that a court must stay litigation 'upon being satisfied that the issue' is 'referable to arbitration' under the 'agreement.' Section 4 says that a court, in response to a motion by an by the aggrieved party, must compel arbitration 'in accordance with the terms of the agreement' when the court is 'satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue."

[18] *Henry Schein, Inc.*, 139 S. Ct. at 530 (citing *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 944 (1995) and *Rent-A-Center*, 561 U.S. at 69, n.1).

[19] *Id.* at 530-31.

[20] 561 U.S. 63 (2010).

efficiency outweighed the parties' contractual agreement to delegate arbitrability questions to an arbitrator if the controversy was frivolous."[21] The Court's decision in *Henry Schein, Inc.*, sends an unequivocal message to parties that such an exception is inconsistent with the FAA and Supreme Court precedent, and thus that its application is no longer permissible.

This opinion is the most recent in a series of opinions in which the Court has confirmed the force of the FAA and overturned lower court decisions that invalidated agreements to arbitrate. Many commentators awaited this decision, hoping that it would indicate whether Justice Kavanaugh's appointment to the Court would support the Court's strong stance on arbitration. However, this opinion did not indicate shift and it signaled that none of the justices voted to open the floodgates of collateral litigation over threshold questions of arbitrability.

This decision is consistent with prior decisions of the court over recent years also supportive of arbitration have been, to name just a few: *Buckeye Check Cashing, Inc. v. Cardegna*[22]; *Oxford Health Plans LLC v. Sutter*[23]; *Rent-A-Center, West v. Jackson*[24]; *AT&T Mobility L.L.C. v. Concepcion*[25]; and *Epic Systems Corp v. Lewis*[26].[27]

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[21] Peter "Bo" Rutledge and Amanda W. Newton, *SCOTUS Loves Arbitration? – It's Not That Simple*, Daily Report (Feb. 14, 2019), https://www.law.com/dailyreportonline/2019/02/14/scotus-loves-arbitration-its-not-that-simple/.

[22] 546 U.S. 440 (2006). There, the plaintiff claimed that a loan contract was illegal and that, as a result, the arbitration clause was unenforceable. The Court granted certiorari to determine whether, under the FAA, a party to a contract can avoid arbitration by claiming that the overall contract is illegal. The Court held that unless an arbitration clause is itself directly and independently challenged as unenforceable, the validity of the contract as a whole a matter for the arbitrator, rather than the courts, to decide.

[23] 569 U.S. 564 (2013). In that case, a primary care doctor had a contract with a care network; the doctor later initiated a class action, on behalf of himself and other medical providers, arguing that the care network had breached their contract and broken New Jersey law. The contract had contained an arbitration clause which stated that "[n]o civil action concerning any dispute arising under this Agreement shall be instituted before any court." The arbitrator found that the clause was general enough to encompass any conceivable action, including class actions. The defendant moved to vacate that decision, arguing that the arbitration clause was not intended to include class actions, and thus that the arbitrator had exceeded his authority. The Court held unanimously that an arbitrator does not exceed his authority by deciding that the parties agreed to class arbitration based on general contractual language requiring arbitration of any dispute. More broadly, the court signaled that under the FAA, a court cannot overrule an arbitrator even if the arbitrator's interpretation was likely erroneous.

[24] 561 U.S. 63 (2010). There, an employee sued his employer for race discrimination and retaliation in Nevada federal district court. The employer moved to compel arbitration. On appeal, the Ninth Circuit held that the district court should have determined whether the provisions of the agreement to arbitrate were unconscionable. The Court granted certiorari to determine whether all district courts must first determine whether an arbitration agreement is unconscionable, even if the agreement clearly reflects that the parties have assigned that question to arbitration. The court held that when a party challenges a provision stating that the arbitrator will determine the enforceability of the agreement, the district court will determine that challenge, but when the party challenges the arbitrability of the agreement as a whole, the arbitrator will determine that challenge.

[25] 563 U.S. 333 (2011). Customers of AT&T brought a class action lawsuit against the telecommunications company alleging a relatively small fraud: that the company was charging sales tax on the retail value of allegedly "free" phones. AT&T moved to compel arbitration, which would effectively bar the action based on the contract's no-class action clause. California had a conflicting law that provided that arbitration clauses were only enforceable if they allowed for class actions. In a 5-4 ruling, the Court upheld the mandatory arbitration clause in the AT&T consumer contracts barring customers from bringing class actions, even though this effectively negated relief for consumers bringing claims for small amounts. The Court's holding also signified that the FAA preempted any state law that ran contrary to the objectives of the FAA.

[26] 138 S. Ct. 1612 (2018) Epic, a software company, had an arbitration agreement in its employee contracts that reqired individualized arbitration for any employment-based dispute. The clause also waived the employees' right to participate in or benefit from class or collective proceedings. An employee sued Epic in federal court under the Fair Labor Standards Act as a representative of a class., and Epic moved to dismiss the complaint. The district court held that the arbitration clause was unenforceable because it violated the employees' right to engage in "concerted activities" under the National Labor Relations Act (NLRA). The Seventh Circuit affirmed, and the Court granted certiorari to determine whether such a clause did violate the NLRA. The Court held 5-4 that arbitration agreements in employment contracts requiring individualized proceedings were indeed enforceable and were not a violation of the NLRA.

[27] These decisions are of importance in Louisiana because the Louisiana Supreme Court has ruled that Louisiana courts are governed by them. *Aguillard v. Auction Management Corp.*, 908 So.2d 1, 40 (La. 2005), superseded by La. C.C.P. art. 2083, as amended by 2005 La. Acts, No. 205 § 1, effective Jan. 1, 2006, with respect to the right to interlocutory appeal (adopting the Supreme Court's interpretation of federal arbitration law and holding that a "strong presumption of arbitrability" exists in Louisiana). The Louisiana Binding Arbitration Law, La. R.S. 9:4201, largely tracks the language of the FAA.