ALM | LAW.COM

New York Law Journal

Supreme Court's Trend in Ruling in Arbitration Topics Should Have Litigators Reflecting on Strategy

By Leslie A. Berkoff

March 15, 2024

Over the past several years, the Supreme Court has issued numerous decisions interpreting and enforcing various provisions of the Federal Arbitration Act (FAA). Whether the FAA has come before the court due to an ongoing rise and recognition of arbitration as an accepted clause in the underlying agreements or as an increasing form of dispute resolution adopted voluntarily by the parties is unclear, but certainly the use of dispute resolution as a tool in a litigator's toolbox is expanding at a great enough pace that splits in the circuits continue to arise with some degree of frequency and at a level to warrant the attention of our highest court.

This article touches on several decisions and the potential impact they have on the trajectory of a litigation and/or strategy of litigators.

In a unanimous decision in *Morgan v. Sundance,* 596 U.S. 411 (2022), the Supreme Court held that employers who do not act promptly to invoke an arbitration clause may be held to have waived the right to compel arbitration. This decision resolved a split in the circuits as to whether a party opposing a delayed motion to compel arbitration had to show that it had been prejudiced by such delay to support an argument of waiver.

Photo: Diego M. Radzinschi/ALM

The U.S. Supreme Court.

This decision is a significant departure from the pro-arbitration rulings issued by the court over recent years and has important implications for those who might have relied upon precedent in determining when to advance their contractual rights in this regard. In issuing this decision, the court specifically recognized that despite the clear policy underpinning the FAA favoring arbitration, federal courts may not simply interpret arbitration agreements with an unfettered bias towards arbitration.

As a general matter, when an action is commenced in state or federal court, a defendant has the right to file a motion to stay the litigation and seek to compel arbitration if the underlying dispute is governed by a contractual arbitration provision pursuant to Sections 3 and 4 of the FAA. Often, the question arises as to when to bring that motion and until this decision, even if there had been a significant delay in filing this motion, the majority of the circuits had often granted the motion as long as there has been no prejudice to the nonmoving party. However, outside of the arbitration context, prejudice is not typically considered when determining whether a party has waived its right.

While the Supreme Court recognized that an overarching federal policy favoring arbitration was intended to combat the judicial history of refusing to enforce arbitration agreements, it noted that this policy was only intended to "make arbitration agreements as enforceable as other contracts, but not more so." *Morgan*, 596 U.S. at 417 (quoting *Prima Paint v. Flood & Conklin Manufacturing*, 388 U.S. 395, 404, n. 12 (1967)). As such, the court determined that federal courts could not use this policy in a carte blanche fashion to create "special, arbitration-preferring procedural rules."

The takeaway from this decision is clear: parties should not wait to file motions to compel arbitration; rather it should be advanced as early as practicable to avoid having that motion denied based upon an argument of waiver.

The impact of a decision denying that motion could be on the trajectory of a litigation was further illuminated by another more recent decision. On June 23, 2023, in *Coinbase v. Bielski*, the court found that a litigation pending in the district court is automatically stayed pending an appeal of a decision by that court denying a motion to compel arbitration. 599 U.S. 736, 747 (2023). This decision resolved a circuit split between the U.S. Courts of Appeals for the Third, Fourth, Seventh, Tenth, Eleventh and D.C. Circuits, which held that the denial of a motion to compel divested the district court of jurisdiction thereby automatically staying proceedings, and the U.S. Courts of Appeals for the Second, Fifth and Ninth Circuits, which had left the decision to stay to the discretion of the district court judge.

The court determined that Section 16(a) of the FAA, which provides that a party seeking arbitration may file an immediate interlocutory appeal when a district court denies a motion to compel arbitration, had been enacted against "a clear background principle" that an appeal "divests the district court of its control over those aspects of the case involved in the appeal." The court did not find it to be persuasive that the absence of an explicit stay requirement in the FAA indicated other Congressional intent or that ordinary discretionary stay factors would adequately protect parties' rights. It reasoned that if the underlying proceedings were not stayed, certain benefits of arbitration, *i.e.* efficiency and cost reduction, would be lost.

The decision impacts those practicing in the minority courts whereas the litigants might have presumed they could move on parallel paths pending resolution of an appeal (which could take years). There is clearly an economic and strategic impact for those determining whether to appeal the denial of a motion as they are no longer spending dollars in both courts.

Of course, not all matters concerning arbitration belong in federal court just because the question is touching upon arbitration. In *Badgerow v. Walters et al.*, 596 U.S. 1 (2022), the Supreme Court restricted the ability of the federal courts to confirm or vacate arbitral awards under Sections 9 and 10 of the FAA. It determined that the "look through" approach previously endorsed by the court concerning Section 4 of the FAA does not apply for petitions to confirm or vacate an award under Sections 9 or 10 of the FAA. (The "look through" approach was developed in the case of *Vaden v. Discover Bank et al.*, 556 U.S. 49 (2009) and generally directs a court to look past the existence of an arbitration agreement and examine

the facts of an underlying dispute when determining whether it has jurisdiction to hear a motion to compel arbitration).

Specifically, Section 4 of the FAA only allows a party to compel arbitration in a "United States district court which, save for such [arbitration] agreement, would have jurisdiction." This has been interpreted to mean that if the facts and nature of the dispute would give rise to either a federal question or diversity jurisdiction, then a federal court could rule on a motion to compel.

By contrast, in this decision, the court recognized that Sections 9 and 10 of the FAA do not contain the same aforementioned textual language as Section 4 and there was no statutory basis to "look through" to the facts of the underlying dispute. As such, the court held that absent specific text, a federal court could not simply assume jurisdiction over such actions and instead a state court would need to rule on the award as the FAA does not in and of itself create subject matter jurisdiction.

The impact of this decision is clear: a party seeking to confirm, vacate or modify an award will now have to identify a separate grant of federal jurisdiction in its petition and not rely upon the FAA in order to seek relief from a federal court. In turn, courts will have to independently assess the existence of the same without relying on the "look through approach." Absent success in such an approach, parties will have to rely upon the state courts for the confirmation of arbitral awards in what may otherwise be potential federal question cases.

Recently, the Supreme Court granted a petition for certiorari in *Coinbase v. Suski* to review the question of whether the court or the arbitrator should determine whether an arbitration agreement containing a delegation clause can be narrowed by a subsequent agreement that does not contain clauses addressing arbitration or delegation. *Suski v. Coinbase*, 55 F.4th 1227, 1228 (9th Cir. 2022), *cert. granted*, *Coinbase v. Suski*, No. 23-3, 2023 WL 7266998 (U.S. Nov. 3, 2023).

There is currently a circuit split as to the enforceability of delegation clauses (clauses that dictate the arbitrator is authorized to determine threshold issues regarding the arbitration agreement). Currently, the First and Fifth Circuits recognize the enforceability of delegation clauses and would allow an arbitrator to decide whether a subsequent agreement narrows the arbitration agreement in a prior agreement, while the Third and Ninth Circuits refuse to enforce delegation clauses where a second agreement narrows an earlier arbitration agreement.

In denying the motion to compel arbitration, both lower courts determined that the question concerning the "scope of the arbitration agreement" referred to how widely it could be applied, and as such it was an issue for the court to decide unless the parties clearly and unmistakably provided otherwise.

In its petition for a writ of certiorari, petitioner *Coinbase* pointed to Supreme Court precedent requiring the enforcement of delegation clauses in arbitration agreements and argued that absent a meritorious challenge to these provisions, they must be enforced if the subsequent agreement does not other alter that provision and it was left for the arbitrator to determine this issue.

The case is scheduled for argument during the court's current term. Depending upon how the Supreme Court rules, corporate attorneys may need to reevaluate how supplemental agreements are drafted to ensure an intent to arbitrate/or delegate decisions is not lost down the line.

Leslie A. Berkoff *is a partner at Moritt Hock & Hamroff and chair of the Dispute Resolution Practice Group.* **Nicole Case**, *an associate at the firm, assisted in the preparation of this article.*

Reprinted with permission from the March 15, 2024 edition of the NEW YORK LAW JOURNAL © 2024 ALM Global Properties, LLC. All rights reserved. Further duplication without permission is prohibited, contact 877-256-2472 or asset-and-logo-licensing@alm.com. # NYLJ-3152024-55073