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Supreme Court Issues a Pair of Unanimous Arbitration Decisions

By Jordan Elias and Adam E. Polk

In two January 2019 opinions written by the two newest justices, the Supreme Court added to its ever-growing body of arbitration jurisprudence.

The unanimous decisions in *Henry Schein, Inc. v. Archer & White Sales, Inc.* and *New Prime Inc. v. Oliveira* address the threshold matter of "who decides who decides" the dispute when a litigant invokes an arbitration agreement. Although the decisions come at this "delegation" issue from different angles, each takes a strict constructionist approach.

Henry Schein: Refusing to Graft a "Wholly Groundless" Exception onto the Federal Arbitration Act

Justice Kavanaugh authored his first Supreme Court opinion in *Henry Schein*. The decision holds that a court lacks power to decide whether a dispute is covered by an arbitration clause—i.e., is arbitrable—even if the judge finds the argument for arbitrability "wholly groundless," where clear and unmistakable evidence shows that the parties intended to reserve that decision on applicability and scope to an arbitrator.

The decision invalidates a policy-based exception previously recognized by the Fourth, Fifth, Sixth, and Federal Circuits, under which courts could maintain jurisdiction by deeming a claim clearly outside the scope of the arbitration agreement. Under *Henry Schein*, a valid "delegation" clause must be enforced according to its terms, even if a judge thinks it is obvious that the dispute belongs in court. Like other of the Supreme Court's arbitration decisions premised on effectuating the mutual intent of contracting parties, *Henry Schein* coexists uneasily with the reality that most people who contract with businesses lack the ability or wherewithal to negotiate or opt out of arbitration agreements.

Henry Schein involves a dispute between businesses. The plaintiff distributor sought injunctive relief in part and argued that its claims were not covered by its agreement to arbitrate, which exempted actions for injunctive relief. The agreement also provided that "[a]ny dispute arising under or related to this Agreement . . . shall be resolved by binding arbitration in accordance with the arbitration rules of the American Arbitration Association." The defendant manufacturer, which had been supplying the distributor, argued that this language delegated questions of arbitrability to an arbitrator, given that the AAA rules empower an arbitrator to determine arbitrability, and that in any event the dispute was subject to arbitration. The district court

disagreed, holding the dispute not subject to arbitration and further characterizing the defendant's contrary argument as "wholly groundless" such that the court could decide arbitrability.

The Fifth Circuit affirmed, but the Supreme Court reversed because no "wholly groundless" exception to delegation appears in the Federal Arbitration Act (FAA). "We must interpret the Act as written," Justice Kavanaugh opined, "and the Act in turn requires that we interpret the contract as written."

The text of the statute defeated each of the plaintiff's arguments. The plaintiff argued, for instance, that the FAA allows a court to set aside an arbitral award by holding that the arbitrator exceeded his or her power, and if a court can find a dispute not arbitrable after arbitration, it should be able to do the same before any arbitral proceeding. But the Supreme Court found this logic unpersuasive because the statute provides for back-end, not front-end, review—"and it is not our proper role to redesign the statute." The Court likewise rejected the policy argument that the "wholly groundless" exception saves time and money by avoiding a round-trip to arbitration and back before the dispute can be litigated: "The short answer is that the Act contains no" such exception.

The Court left unaddressed whether incorporation of an arbitration association's rules, without more, amounts to "clear and unmistakable" evidence, under *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 944–45 (1995), that the parties intended to delegate arbitrability. Lower courts have expressed conflicting views on this question. *See generally Gilbert St. Developers, LLC v. La Quinta Homes, LLC*, 94 Cal. Rptr. 3d 918, 925–26 (Cal. Ct. App. 2009) (cataloguing split in federal authority).

For example, Judge Easterbrook wrote that arbitral rule incorporation is "not broad enough to compel the conclusion that arbitrability is itself an arbitrable issue." *Oblix, Inc. v. Winiecki*, 374 F.3d 488, 490 (7th Cir. 2004); *see also Gilbert*, 94 Cal. Rptr. 3d at 925–26 (labeling this the "majority rule" and criticizing contrary decisions on the basis that they "do not focus on what *First Options* made explicit . . . about the importance of the parties *specially focusing* on the [delegation] issue"). By contrast, in *PaineWebber Inc. v. Bybyk*, the Second Circuit held that a clause relegating "any and all claims" to arbitration was "elastic enough to encompass disputes over whether . . . a claim is within the scope of arbitration." 81 F.3d 1193, 1199 (2d Cir. 1996); *see also Contec Corp. v. Remote Solution Co., Ltd.*, 398 F.3d 205, 208 (2d Cir. 2005) (citing *PaineWebber* to hold that "when . . . parties explicitly incorporate rules that empower an arbitrator to decide issues of arbitrability, the incorporation serves as clear and unmistakable evidence of the parties' intent to delegate such issues to an arbitrator"). More recently, the Ninth Circuit and other courts of appeals have concluded that whether rule incorporation clearly and unmistakably establishes intent to delegate may depend on whether a party is unsophisticated.

See Ingalls v. Spotify USA, Inc., No. C 16-03533 WHA, 2016 WL 6679561, at *3–4 (N.D. Cal. Nov. 14, 2016) (gathering case law).

Given this unsettled landscape, one has to wonder: Will the Supreme Court eventually revisit the case and give birth to *Henry Schein II*?

***New Prime*: Preserving the FAA's Exemption for Transportation Workers**

Fresh off his consequential opinion in *Epic Systems Corp. v. Lewis*, 138 S. Ct. 1612 (2018), Justice Gorsuch lifted his pen once more to delineate the rights of workers faced with arbitration clauses waiving representative claims. Although *Epic Systems* is a 5–4 decision favoring arbitration and *New Prime* a unanimous decision limiting arbitration, the decisions follow the same guiding principle of strict adherence to the FAA's text.

Interpreting a statutory exemption, the Court in *New Prime* held that interstate truck drivers need not submit to arbitration even if they are independent contractors as opposed to employees.

Dominic Oliveira drove for New Prime, an interstate trucking company. On behalf of a proposed class of other independent trucking contractors, Oliveira sued New Prime for failure to pay lawful wages. He opposed New Prime's arbitration motion by arguing that the FAA exempts "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce."

The Supreme Court held that the lower courts correctly rejected New Prime's argument that this exemption does not apply to independent contractors like Oliveira. The Court explained that "[w]hile a court's authority under the Arbitration Act to compel arbitration may be considerable, it isn't unconditional" and is limited by various provisions. These include not only section 1's "contracts of employment" exclusion but also section 2's requirement of a "written provision" in a "maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction."

The Court emphasized that these limiting provisions are "antecedent" in the statutory scheme. Therefore, even if an arbitration agreement covers "every question under the sun," Justice Gorsuch wrote, borrowing from Ecclesiastes, the agreement may be unenforceable because the FAA does not apply to it. So even when a valid delegation clause exists, a court must first decide "whether §1's 'contracts of employment' exclusion applies before ordering arbitration. After all, to invoke its statutory powers under §§ 3 and 4 to stay litigation and compel arbitration according to a contract's terms, a court must first know whether the contract itself falls within or beyond the boundaries of §§ 1 and 2."

The Court went on to apply the plain meaning rule—under which words in a statute are "generally" interpreted as "taking their ordinary meaning at the time Congress enacted the

statute"—to hold independent contractors covered by the exemption at issue. Various sources (dictionaries, statutes, court decisions) demonstrate that in 1925, when Congress enacted the FAA, "contract of employment" simply meant an agreement to perform work, regardless of the employer's level of control over the work. Lending further support to this conclusion, the FAA's "contracts of employment" provision refers to "any other class of *workers*."

Just as the Court rejected a policy argument in *Henry Schein*, so did it reject New Prime's reliance on the FAA's general policy in favor of arbitration, which cannot displace the exceptions codified in the statute. Justice Gorsuch noted that "[i]f courts felt free to pave over bumpy statutory texts in the name of more expeditiously advancing a policy goal, we would risk failing to take account of legislative compromises essential to a law's passage and, in that way, thwart rather than honor the effectuation of congressional intent."

Justice Ginsburg concurred with a reminder that the plain meaning rule does not invariably call for a fossilized understanding of statutory terms. Instead, as with the Racketeer Influenced and Corrupt Organizations Act and the Sherman Act, Congress sometimes imbues legislation with flexibility through broad terms.

The ghost of Justice Scalia and the specter of constitutional challenges yet to come lurk in this debate.

Conclusion

Henry Schein and *New Prime*, issued in swift succession, represent minor additions to the Supreme Court's arbitration canon. Yet, their strict approach to interpreting statutes and contracts sounds a major theme in the Court's jurisprudence, arbitration-related and otherwise.

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