U.S. Supreme Court Rules on Threshold Issues of Arbitrability

Earlier this year, the U.S. Supreme Court (the ***Supreme Court*** or the ***Court***) handed down two interesting decisions on the question of who, between a judge and an arbitrator, was properly positioned to answer the threshold question of whether a specific dispute is subject to arbitration and whether the parties are entitled to delegate that issue to arbitrators.

Henry Schein, Inc. v. Archer & White Sales, Inc.: Supreme Court Rejects "wholly groundless" doctrine

In U.S. jurisprudence, questions relating to the existence, validity, and scope of an arbitration agreement go to the heart of consent to arbitration. As a result, these questions are, as a general rule, left to courts to decide. Nevertheless, parties to an agreement are entitled to leave those questions to the discretion of arbitrators if they have "*clearly and unmistakably*" agreed to that end (see: *First Options of Chicago, Inc. v. Kaplan*).

Although parties are entitled to empower arbitrators to decide

on the existence, validity, and scope of an arbitration agreement, some Courts of Appeals have derogated from this rule and have instead entertained the question of an arbitration agreement's validity when the arguments in favour of arbitration are "wholly groundless" (the ***"wholly groundless" doctrine***).

In an opinion delivered on 8 January 2019, the Supreme Court unanimously held that this "wholly groundless" doctrine was incompatible with the Federal Arbitration Act (the ***FAA*** or the ***Act***).

In that case, the plaintiff, *Archer & White Sales, Inc.*, (***Archer & White***), a distributor of dental equipment, had contracted with a dental equipment manufacturer, *Henry Schein, Inc.*, (***Schein***). In the course of the execution of the contract, however, Archer & White sued Schein in federal court in Texas for violations of federal and state antitrust law, seeking damages and injunctive relief. The contract between Schein and Archer & White provided that any dispute between them – except those seeking injunctive relief – should be resolved by arbitration, and that any arbitration proceedings would comply with the rules of the American Arbitration Association (***AAA***).

In light of that arbitration agreement, Schein asked the court to compel arbitration under the FAA, while Archer & White contended that their dispute, which sought injunctive relief in part, was exempt from the arbitration clause.

As a result, the district court had to decide who, between a judge and an arbitrator, was properly positioned to decide whether the parties' dispute was subject to arbitration at all. Schein pointed to the contract's incorporation of the AAA rules, which provide that an arbitrator should resolve threshold questions of arbitrability[1]. Archer & White, in turn, invoked the "wholly groundless" doctrine to argue that courts may address the predicate question of a dispute's

eligibility for arbitration when the defendant's argument for arbitration is entirely without justification.

The District Court for the Eastern District of Texas denied Schein's motion to compel arbitration, agreeing with Archer & White both that a "wholly groundless" doctrine existed and that Schein's argument lacked such grounds. The Fifth Circuit Court of Appeals agreed.

However, as seen above, the "wholly groundless" doctrine is a judge-made exception (originating particularly from the Courts of Appeals). It does not exist in the FAA and had never received the express approval and assent of the Supreme Court. As a result, the Supreme Court granted *certiorari* in this case.

Before the Supreme Court, Archer & White proposed four arguments to convince the Court of the validity of the "wholly groundless" doctrine.

First, Archer & White cited §3 and §4 of the FAA, which empower courts to compel arbitration based on the terms of the parties' agreement. Archer & White contended that these provisions essentially reserve the question of arbitrability to courts alone. "*But that ship has sailed*", according to the Court. The Supreme Court recalled its opinion in *First Options of Chicago, Inc. v. Kaplan* (see above) where it found that the FAA did not purport to categorically delegate the arbitrability question to courts to the exclusion of arbitrators.

Archer & White turned next to §10 of the FAA, which permits courts to conduct "*back-end judicial review*" of an arbitration decision in the event that an arbitrator exceeds his powers. Working backwards through this provision, Archer & White argued that if courts can apply back-end judicial review to an arbitrator's decision, they should be able to act at the front end and rule on the question of arbitrability. The Court

rejected this argument, noting that it is not their role to refashion legislation.

Archer & White's third and fourth arguments departed from the text of the FAA, relying on policy in its stead. Third, allowing an arbitrator to decide arbitrability is inefficient and unnecessarily expensive if the claim for arbitration lacks merit; fourth, the "wholly groundless" exception serves the necessary function of discouraging unjustified motions for arbitration. The Court doubted Archer & White's claims that obliging a court to decide arbitrability questions would be significantly more expeditious than permitting an arbitrator to do so, and was similarly skeptical that frivolous motions for arbitration are sufficiently problematic to warrant judicial measures.

Having dismissed all of Archer & White's arguments, the Supreme Court effectively eliminated the "wholly groundless" doctrine and held that the judiciary has no role to play if a contract clearly designates questions of arbitrability to an arbitrator.

It is, however, noteworthy to highlight that the Supreme Court did not take any explicit position as to whether the contract's incorporation of the AAA rules constituted language sufficiently "*clear and unmistakable*" to justify submitting arbitrability questions to an arbitrator. Instead, the Supreme Court remanded the case to the Fifth Circuit Court of Appeals to decide that issue.

New Prime Inc. v. Oliveira – Supreme Court Denies Motion to Compel Arbitration of Disputes with Independent Contractors

As a follow-up to *Henry Schein, Inc. v. Archer & White Sales, Inc.*, the Supreme Court addressed, on 15 January 2019, the question of whether a court must leave questions of arbitrability to an arbitrator even when the FAA explicitly excludes the type of dispute at hand from compulsory

arbitration.

In *New Prime Inc. v. Oliveira*, the plaintiff Mr. Dominic Oliveira worked as an independent contractor for the defendant New Prime Inc. (***New Prime***), a trucking company. Oliveira's contract with New Prime provided that all disputes should be resolved by an arbitrator, including disputes "*over the scope of the arbitrator's authority*".

Oliveira filed a class action lawsuit in Massachusetts federal court, alleging that New Prime treated their independent contractors like employees and thus owed them statutorily-mandated minimum wage. New Prime asked the court to invoke its authority under the FAA to compel arbitration, per the terms of its contract with Oliveira.

In response, Oliveira noted that the FAA does not unconditionally direct courts to compel arbitration. The FAA contains certain exceptions, and according to Oliveira, one such exception applied here: "*contracts of employment of* […] *workers engaged in foreign or interstate commerce*" are exempt from the FAA under §1. Oliveira argued that his employment arrangement with New Prime qualified under this exception and that, as a result, the court was without authority to compel arbitration.

New Prime argued that the applicability of the §1 exception was a question for the arbitrator, not the court, to decide. Even if the court had the authority to decide this issue, according to New Prime, the §1 exception would not apply to Oliveira anyway: it refers to "*contracts of employment*", to the exclusion of arrangements with independent contractors.

Both the District Court for the District of Massachusetts and the First Circuit Court of Appeals sided with Oliveira, agreeing that courts should decide as a preliminary matter whether the parties' contract falls within the §1 exception and that the language of §1 is not so narrow as to exclude

independent contractors.

Given the lack of consensus on these issues among the different circuits, the Supreme Court granted *certiorari* of the case.

In the opinion, authored by Justice Neil Gorsuch, the Supreme Court agreed with Oliveira, that courts – not arbitrators – should decide whether an agreement is excluded by §1.

The Supreme Court first looked to the terms and structure of the statute, noting that the provisions permitting courts to compel arbitration (§3 and §4) are found *after* the provision exempting from the FAA's coverage certain kinds of contracts (§1). This sequence suggests that for an agreement to provide the basis for arbitration under §3 and §4, it must first meet the requirements outlined in §1.

New Prime countered the Court's reasoning by pointing to the contract's delegation clause (*i.e.*, that the parties had specifically delegated to the arbitrator the power to resolve any questions regarding the scope of the arbitrator's authority). In particular, New Prime relied on the Supreme Court's previous decision in *Rent-A-Center West, Inc. v. Jackson*, which allows – in cases where the party resisting arbitration did not challenge the specific delegation clause – an arbitrator to decide predicate questions of whether a dispute is subject to arbitration at all. According to New Prime, since Oliveira did not separately challenge the parties' delegation clause in the case at hand, any disputes should be resolved in arbitration.

The Supreme Court disagreed. Irrespective of the fact that New Prime and Oliveira had "*clearly and unmistakably*" (see: *First Options of Chicago, Inc. v. Kaplan)* agreed to delegate to an arbitrator the power to answer questions regarding the scope of his own authority, the Supreme Court found that "[a] *delegation clause is merely a specialized type of arbitration*

agreement, and the [FAA] *'operates on this additional arbitration agreement just as it does on any other'*" (quoting *Rent-A-Center, West, Inc. v. Jackson*). As such, the Supreme Court found that §1 limits the power of the courts under the FAA. Consequently, before compelling arbitration, courts must answer the threshold question of whether the dispute falls within the scope of the FAA.

Having found that the lower courts were authorized to assess the applicability of §1 to Oliveira's contract, the Supreme Court then turned to the question of whether the FAA's language ("*contracts of employment*") encompasses agreements with independent contractors.

The Supreme Court began by recalling the foundational principle of statutory interpretation, that words should be construed according to their ordinary meaning at the time of the statute's enactment, and by expressing their commitment to judicial restraint to avoid "*upsetting reliance interests in the settled meaning of a statute*".

A "*contract of employment*" would have had an expansive meaning at the time the FAA was adopted in 1925, including not only formal employment contracts but independent contractor relationships as well. The Supreme Court looked to legal dictionaries from the early 1900s, and noted that the term's absence in these dictionaries is indicative that the phrase had not yet become a term-of-art, as it is today, signifying a formal employment relationship. Dictionaries from the period did, furthermore, define "*employment*" broadly to mean any kind of work.

Legal authorities from the early twentieth century similarly construed "*contract of employment*" broadly. Case law from the early 1900s, at both the state and federal levels, used the term to refer to agreements with independent contractors.

Significantly, even the text of the FAA uses varied language

when referring to the notion of "*employment*": §1's exception applies to "*contracts of employment of* […] *any* […] *workers engaged in foreign or interstate commerce*". The word choice of "*workers*" is a noteworthy one. It is broader than "*employees*" and "*easily embraces independent contractors*".

New Prime argued that "*employee*" and "*independent contractor*" had acquired different meanings by 1925. However, the Supreme Court found unconvincing the few cases cited by New Prime, especially when compared to the ample evidence on record that "*contracts of employment*" enjoyed a broad meaning in 1925. As a last resort, New Prime turned to policy arguments and contended that the Supreme Court should order arbitration in this case to serve the FAA's original aim of diminishing judicial aversion to arbitration. The Supreme Court disagreed, seeing its role better fulfilled by respecting the limits of the FAA.

The FAA requires courts to enforce arbitration agreements according to their terms. With the opinion's close analysis of the FAA's language, the Supreme Court in *New Prime* enforced the FAA according to *its* terms, albeit with the result that the parties' dispute will ultimately be settled through litigation, rather than arbitration. *New Prime* illustrates that the generally pro-arbitration Supreme Court may not always, in fact, compel arbitration.

This article was kindly drafted with the assistance of Emily Snow (intern at Van Bael & Bellis).

[1] Although, admittedly, the term "*arbitrability*" is widely used to describe the question of whether the legislature authorised the adjudication of a particular cause of action by an arbitral tribunal, in the present context, the term "*arbitrability*" describes all conditions or requirements that must be met in order for an arbitration to go forward. For further information, see: G. Bermann, *The "Gateway" Problem in International Commercial Arbitration*, The Yale Law Journal of

International Law, 2012, vol. 37.
