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Takeaways From The Supreme Court's October 2021 Term Decisions Involving The FAA

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Commentary

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The Supreme Court heard three cases during the October 2021 term concerning the Federal Arbitration Act, 9 U.S.C. §§ 1 *et seq.* (“FAA”). Each opinion reinforced the principle that the Supreme Court will not expand the scope of the FAA despite the strong federal policy favoring arbitration; however, we anticipate the Supreme Court will continue to hear cases regarding the FAA's scope. Four key takeaways from these cases are:

1. Arbitration clauses should not be treated differently than any other written contractual agreement, and therefore, a party waives its right to arbitrate if it knowingly relinquishes the right to arbitrate by acting inconsistently with that right. There is no prejudice requirement in the waiver inquiry.

2. The exemption in Section 1 covers any “class of workers engaged in foreign or interstate commerce” based on the actual work performed by the class members, not based on the general line of work of their employer.
3. Arbitration is a matter of consent, and thus, a party may not be compelled to submit to class or representative arbitration.
4. All three decisions confirm the pattern of strongly enforcing the FAA's preference for arbitration over class actions except, of course, when the FAA explicitly exempts arbitration agreements from its coverage.

Morgan v. Sundance, Inc.

In Morgan v. Sundance, Inc.,¹ the Supreme Court resolved a circuit split concerning the test to be applied in determining whether a party waives its right to arbitrate. Nine circuits used a test that assessed whether the non-compelling party was prejudiced by the compelling party's inconsistent actions.² And, two circuits rejected the prejudice requirement.³

In an unanimous decision, the Supreme Court rejected the “prejudice” test, holding instead that the FAA does not authorize federal courts to create an arbitration-specific procedural rule. The Court concluded “the Eighth Circuit was wrong to condition a waiver of the right to arbitrate on a showing of prejudice.”⁴ In so holding, the Court noted that: “The policy is to make arbitration agreements as enforceable as other contracts, but not more so.”⁵ “Outside the arbitration context, a federal court assessing waiver does not

generally ask about prejudice. Waiver, we have said, 'is the intentional relinquishment or abandonment of a known right.' To decide whether a waiver has occurred, the court focuses on the actions of the person who held the right; the court seldom considers the effects of those actions on the opposing party."⁶

In short, to determine whether a party has waived its right to arbitrate (or any other right), the question is: Did that party knowingly relinquish its right to arbitrate by acting inconsistently with that right?

We believe this decision will likely result in an increase of waiving arbitration rights because parties who choose to wait to enforce a subject arbitration provision cannot rest on prejudice as an excuse. Therefore, a party should decide at the outset of the case whether to enforce an arbitration provision; otherwise the party risks waiving its right to do so.

Southwest Airlines Co. v. Saxon

The FAA has an exception that excludes from its scope "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce."⁷ In Southwest Airlines Co. v. Saxon,⁸ the Supreme Court analyzed the meaning of "any other class of workers engaged in foreign or interstate commerce." Looking at the precise words chosen by Congress, the Court found in a 8-0 decision that "any class of workers directly involved in transporting goods across state or international borders," such as airplane cargo loaders, falls within Section 1's exemption.⁹ The Supreme Court further held that the determination is based on the actual work carried out by "the members of the class, as a whole," not by what the company does generally.¹⁰ As such, the Court rejected an interpretation that would expand the scope of Section 1 to "virtually all employees of major transportation providers."¹¹

We believe this decision will likely result in fewer arbitration claims because the Court's more expansive interpretation of Section 1's exemption will exclude more workers from the FAA.

Viking River Cruises, Inc. v. Moriana

In Viking River Cruises, Inc. v. Moriana,¹² the Supreme Court in a 8-1 decision reaffirmed the principle that "arbitration is strictly a matter of consent." The Court stated that "state law cannot condition

the enforceability of an arbitration agreement on the availability of a procedural mechanism that would permit a party to expand the scope of the arbitration by introducing claims that the parties did not jointly agree to arbitrate."¹³ "A state rule imposing an expansive rule of joinder in the arbitral context would defeat the ability of parties to control which claims are subject to arbitration. Such a rule would permit parties to superadd new claims to the proceeding, regardless of whether the agreement between them committed those claims to arbitration."¹⁴

Consequently, the Court found that the FAA preempts the rule of Iskanian v. CLS Transportation Los Angeles, LLC,¹⁵ "insofar as it precludes division of [California's Labor Code Private Attorneys General Act of 2004 ("PAGA")] actions into individual and non-individual claims through an agreement to arbitrate."¹⁶ Pursuant to the rule of Iskanian, an aggrieved employee was permitted to abrogate his or her agreement to arbitrate 'individual' PAGA claims based on personally sustained violations "after the fact and demand either judicial proceedings or an arbitral proceeding that exceeds the scope jointly intended by the parties."¹⁷ This created a conflict between PAGA's procedural structure¹⁸ and the FAA, which could not stand.

The Court further noted that "the FAA does not require courts to enforce contractual waivers of substantive rights and remedies. The FAA's mandate is to enforce arbitration agreements, . . . [which] is a specialized kind of forum-selection clause that posits not only the situs of suit but also the procedure to be used in resolving the dispute. An arbitration agreement thus does not alter or abridge substantive rights; it merely changes how those rights will be processed."¹⁹

Because more individuals subject to arbitration clauses now lack statutory standing to bring PAGA claims, we believe this decision will likely result in fewer PAGA claims unless/until the California legislature amends PAGA or state judges interpret it differently.

Endnotes

1. Morgan v. Sundance, Inc., 142 S.Ct. 1708 (2022).
2. Id. at 1712.
3. Id.

4. Id. at 1712-13.
5. Id. at 1713.
6. Id. (citations omitted).
7. 9 U.S.C. § 1.
8. Southwest Airlines Co. v. Saxon, 142 S.Ct. 1783 (2022).
9. Id. at 1789.
10. Id. at 1788.
11. Id. at 1791.
12. Viking River Cruises, Inc. v. Moriana, 142 S.Ct. 1906 (2022).
13. Id. at 1923.
14. Id. at 1924.
15. Iskanian v. CLS Transp. Los Angeles, LLC, 59 Cal.4th 348 (Cal. 2014).
16. Viking River Cruises, Inc., 142 S.Ct. at 1924.
17. Id.
18. “An employee with statutory standing may ‘seek any civil penalties the state can, including penalties for violations involving employees other than the PAGA litigant herself.’ An employee who alleges he or she suffered a single violation is entitled to use that violation as a gateway to assert a potentially limitless number of other violations as predicates for liability.” Id. at 1915 (citations omitted).
19. Id. at 1919 (internal citations omitted). ■

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