

Supreme Court Confirms Arbitrators Decide Gateway Arbitrability

January 9, 2019

On January 8, 2019, the United States Supreme Court held that the “wholly groundless” exception to arbitrators’ powers to decide questions of arbitrability otherwise contractually committed to them that had been developed by some federal courts is inconsistent with the Federal Arbitration Act (the “FAA”). The Court held that where an arbitration agreement delegates questions of arbitrability to an arbitrator, a court may not override the agreement, even if it determines that the claim that the dispute is subject to arbitration is “wholly groundless.” The Court found that this conclusion is consistent with both the text of the FAA and the Court’s precedents, reinforcing the principles that arbitration is a matter of contract and that contracts must be construed and enforced according to their terms.

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Background

The Supreme Court has consistently found that arbitration is a matter of contract, and that an arbitrator should decide gateway issues of arbitrability – *i.e.*, under a given arbitration agreement, whether a particular dispute must be arbitrated (sometimes couched as issues of arbitral “jurisdiction”) – provided that there is “clear and unmistakable evidence” of the parties’ intent for these issues to be resolved by the arbitrator.¹ However, it has remained an open question at the Supreme Court level as to what constitutes “clear and unmistakable” evidence and, until today’s decision, whether there may sometimes be an exception to the principle that arbitrability is for the arbitrator to decide where there is such evidence.

Background to *Henry Schein v. Archer and White Sales*

In *Henry Schein v. Archer and White Sales*, a dental equipment distributor, Archer and White Sales, Inc., sued Henry Schein, Inc. and other dental equipment distributors and manufacturers for allegedly conspiring to exclude lower cost distributors from the market in violation of U.S. antitrust laws. Archer and White Sales sought damages and an injunction to enjoin these distributors’ allegedly illegal conduct. After Archer and White Sales filed suit, Henry Schein sought to compel arbitration based on the wording of a distribution agreement, which stated that disputes would be resolved through arbitration “except for actions seeking injunctive relief.” Archer and White Sales countered that because it sought an injunction (in addition to damages), the dispute was not subject to arbitration.

Although a Texas magistrate judge granted the motion to compel arbitration,² the District Court for the Eastern District of Texas disagreed, finding the court could and should decide the question of arbitrability

and that the claims at issue were not arbitrable.³ The district court determined that the question of arbitrability should be decided by the court, instead of an arbitrator, for two reasons: “(1) the Parties did not clearly and unmistakably agree to arbitrate the arbitrability of actions seeking injunctive relief; and (2) Defendants’ argument that Plaintiff’s claims fall within the scope of the arbitration clause is wholly groundless.”⁴ In analyzing whether there was clear and unmistakable evidence of an agreement to arbitrate, the district court found that the arbitration clause’s reference to the rules of the American Arbitration Association (“AAA Rules”) – which provide for arbitrability to be decided by the arbitrator – constituted the parties’ agreement to arbitrate arbitrability, but that the express carve-out of claims for injunctive relief from arbitration meant that the parties had not agreed to arbitrate such claims.⁵ Therefore, there was no “clear and unmistakable” evidence that the parties intended to arbitrate the question of arbitrability in these circumstances.⁶ As a second rationale, the district court determined that the plain language of the contract’s carve-out clause excluded the action from arbitration, rendering Henry Schein’s argument that the action should be referred to the arbitrator to determine arbitrability “wholly groundless,”⁷ and thereby empowering the court to determine arbitrability.

The Fifth Circuit affirmed the district court, holding that the matter was not arbitrable.⁸ Although Henry Schein argued that the inclusion of the AAA Rules in the parties’ arbitration agreement indicated a clear and unmistakable intent to delegate the question of arbitrability to the arbitrator, the Fifth Circuit relied on its previous decision in *Douglas v. Regions Bank*⁹ to

¹ See *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 945 (1995).

² Mem. Or., *Archer and White Sales, Inc. v. Henry Schein, Inc.*, No. 2:12-CV-572-JRG-RSP, 2013 WL 12155243 (E.D. Tex. May 28, 2013).

³ *Archer and White Sales, Inc. v. Henry Schein, Inc.*, No. 2:12-cv-572-JRG, 2016 WL 7157421, at *9 (E.D. Tex. Dec. 7, 2016).

⁴ *Id.* at *6.

⁵ *Id.* at *7.

⁶ *Id.*

⁷ *Id.* at *9.

⁸ *Archer and White Sales, Inc. v. Henry Schein, Inc.*, 878 F.3d 488, 498 (5th Cir. 2017).

⁹ 757 F.3d 460, 463-64 (5th Cir. 2014).

“provide[] a narrow escape valve” and relied on the “wholly groundless” exception to find that the court could determine arbitrability because the claim for arbitration was “wholly groundless.”¹⁰

While the Fifth, Sixth and Federal Circuits have adopted the “wholly groundless” exception, the Tenth and Eleventh Circuits have expressly rejected it.¹¹ Henry Schein’s petition for *certiorari* provided the Supreme Court with the opportunity to resolve this circuit split and further refine the circumstances under which a court or an arbitrator should decide the gateway issue of arbitrability – *i.e.*, the existence of an agreement to arbitrate and what issues should and can be arbitrated under a particular arbitration agreement.

The Supreme Court’s Decision

The Supreme Court vacated and remanded the Fifth Circuit’s decision. In a unanimous decision written by Justice Kavanaugh (his first for the Court), the Court held that the “wholly groundless” exception to arbitrability is foreclosed by the plain text of the FAA and the Court’s precedent. The Court rejected the argument that such an exception should be recognized because the exception “confuses the question of who decides arbitrability with the separate question of who prevails on arbitrability.”¹²

Adopting a textual approach, the Court determined that the Federal Arbitration Act “does not contain a ‘wholly groundless’ exception, and we are not at liberty to rewrite the statute passed by Congress and signed by the President.”¹³ In addition to relying on the text of the FAA, the Court noted that it had “consistently held that parties may delegate threshold arbitrability questions to the arbitrator, so long as the parties’

agreement does so by ‘clear and unmistakable’ evidence.”¹⁴

The Court additionally rejected the argument that the “wholly groundless” exception advances the purpose of Section 10 of the FAA, which provides for “back-end judicial review” in the event an arbitrator exceeds her powers.¹⁵ The Court found that neither Section 10 nor any other provisions of the FAA provides “front end” powers to courts to “say that the underlying issue is not arbitrable,” and is again foreclosed by precedent.¹⁶

The Court also was not persuaded by Archer and White Sales’s policy arguments, which had contended that it would be contrary to the parties’ intent in executing an arbitration agreement to waste time having arbitrators decide whether they have the authority to hear a claim that clearly belongs in court. The Court expressed skepticism that it would be “easy” for a court “to tell when an argument for arbitration of a particular dispute is wholly groundless,” and noted that the exception may “spark collateral litigation.”¹⁷ The Court also rejected the claim that the “wholly groundless” exception could successfully deter frivolous motions to compel arbitration. The Court reiterated that it could not “rewrite the statute simply to accommodate that policy concern,” and also indicated that arbitrators could rule as quickly as courts to dispose of frivolous demands for arbitration by ruling there was no agreement to arbitrate the dispute in question.¹⁸

The Court remanded to the Fifth Circuit to determine whether the contract at issue in this particular case delegated the threshold arbitrability question to the arbitrator.

Conclusion

This decision supports previous holdings that it is up to arbitrators to determine issues of arbitrability when that authority has been unmistakably delegated to them

¹⁰ *Archer and White Sales, Inc. v. Henry Schein, Inc.*, 878 F.3d at 495-96.

¹¹ *Compare Simply Wireless, Inc. v. T-Mobile US, Inc.* 877 F.3d 522 (4th Cir. 2017); *Turi v. Main Street Adoption Servs., LLP*, 633 F.3d 496 (6th Cir. 2011); *Qualcomm, Inc. v. Nokia Corp.*, 466 F.3d 1366 (Fed. Cir. 2006) with *Belnap v. Iasis Healthcare*, 844 F.3d 1272 (10th Cir. 2017); *Jones v. Waffle House*, 866 F.3d 1257 (11th Cir. 2017).

¹² *Henry Schein, Inc. v. Archer and White Sales, Inc.*, 585 U.S. __ (2019) (slip op., at 8).

¹³ *Id.* at 2.

¹⁴ *Id.* at 6 (citing *First Options*, 514 U.S. at 944).

¹⁵ *Id.*

¹⁶ *Id.* at 6-7.

¹⁷ *Id.* at 7.

¹⁸ *Id.* at 8.

by the parties. However, it does not answer what might constitute unmistakable evidence of delegation.

Indeed, by remanding the case to the Fifth Circuit to resolve the question of whether the arbitration agreement in this case gives the arbitrator power to decide questions of arbitrability, the Court declined to reach the issue of whether the incorporation of institutional arbitral rules – here, the AAA Rules – constitutes “clear and unmistakable evidence” that the parties intended to arbitrate arbitrability, an issue the Fifth Circuit had not addressed. Although there was some discussion by the Justices during oral argument regarding this issue, the Supreme Court left it open to be decided another day. The Fifth Circuit will now consider whether the incorporation of the AAA Rules (which provide, like most institutional arbitral rules, that the arbitrator has the power to determine her own jurisdiction) in the parties’ arbitration agreement evidences the parties’ unmistakable intent for an arbitrator to determine the threshold issue of arbitrability. Many courts, including the Fifth Circuit, have held that this is indeed the case, but the current draft Restatement rejects that position, and the Supreme Court has never weighed in on this issue. It will be interesting to see what conclusion the Court reaches if the issue is squarely presented to it.

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