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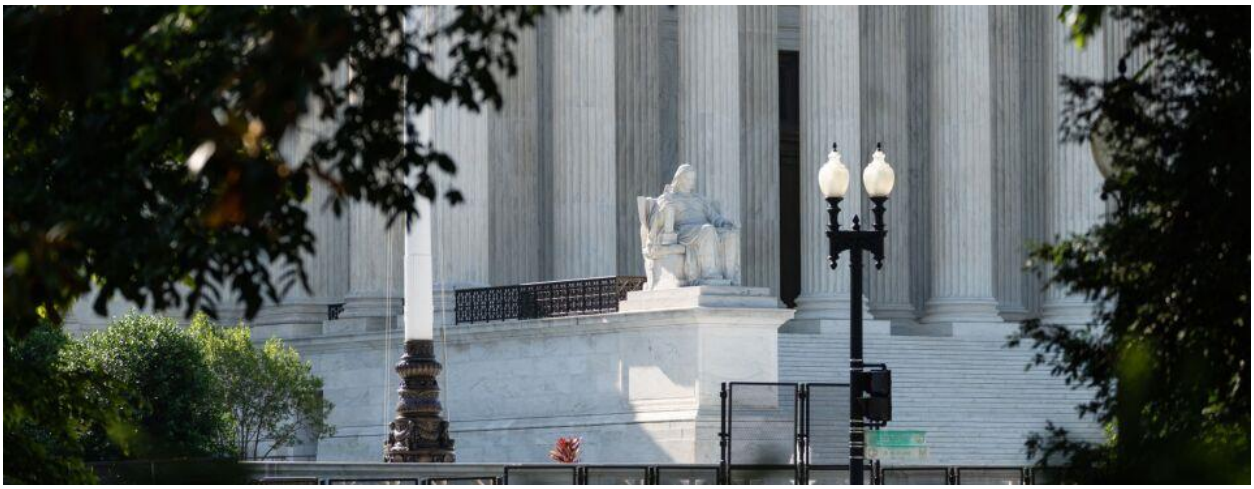

Is the Supreme Court Having Second Thoughts About Arbitration?

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The US Supreme Court's recent rulings in cases involving arbitration reinforce the core of its historic arbitration jurisprudence: the principle that an arbitration contract must be enforced like any other contract, Covington & Burling LLP attorneys Sonya Winner and Ashley Simonsen write. They examine the two rulings and conclude the high court's staunch defense of arbitration agreements is unlikely to change significantly in their wake.

One of the most valuable protections companies have against class actions is the ability to include provisions in their contracts with employees and consumers that require any disputes to be submitted to individual arbitration rather than pursued in class action litigation. This mechanism has been controversial, and many state courts and lower federal courts (as well as some state legislators and federal policymakers) have attempted to limit companies' ability to enforce such provisions.

For the past four decades, the US Supreme Court has consistently rejected such efforts, referring time and again to a federal "policy favoring arbitration" embodied in the Federal Arbitration Act. In its recent decision in *Morgan v. Sundance Inc.*, however, the Supreme Court made clear that the phrase has a significantly narrower meaning than what many have long thought.

Does this reflect a sea change in the Supreme Court's views on arbitration? Probably not, especially in light of the Supreme Court's more expansive statements about the FAA in another decision issued only three weeks later. But *Morgan* may require some reframing of the way issues under the FAA are addressed.

Two-Part Test Rejected

In *Morgan*, a unanimous Supreme Court rejected the two-part test applied by most circuits in evaluating whether a party has waived its right to compel enforcement of an arbitration agreement. Under that test, waiver would be found only if a party acted in a manner inconsistent with its arbitration rights and that inconsistency caused prejudice to the other side.

The principal justification for the prejudice requirement was the Supreme Court's oft-cited federal "policy favoring arbitration." Finding that the usual test for contractual waiver typically requires only

inconsistent conduct, the high court held it improper to graft an additional prejudice requirement onto the waiver analysis just for arbitration agreements.

Although the two-part test was the majority rule in the lower courts, its rejection is unlikely to have a major impact on decisions about waiver. The main effect will be an enhanced focus on exactly what conduct is sufficiently "inconsistent" with the arbitration right to create a waiver.

The Supreme Court offered no comment on that subject, but the answer is likely to leave the outcome in most cases the same as it would have been under the two-part test—inconsistent conduct that is significant enough to cause prejudice will typically create a waiver, while conduct so immaterial as to be wholly non-prejudicial will likely not be considered sufficiently "inconsistent" with arbitration rights to waive those rights.

What may be more significant is the basis for the decision in *Morgan*, where the Supreme Court explained that the "federal policy favoring arbitration" should not be interpreted as referring to anything more than confirmation that an agreement to arbitrate is just as enforceable as any other contract: "The federal policy is about treating arbitration contracts like all others, not about fostering arbitration."

Although the Supreme Court pointed to language from some prior decisions that was consistent with this narrower interpretation, one can hardly criticize lower courts for viewing the high court's prior decisions overall as suggesting that federal policy supports arbitration itself, not simply the enforcement of arbitration contracts as contracts.

As Justice Antonin Scalia observed in his groundbreaking opinion in *AT&T Mobility v Concepcion*, "our cases place it beyond dispute that the FAA was designed to promote arbitration."

Some may see *Morgan* as reflecting an important change in the Supreme Court's views about the FAA, but its broader significance is likely to be limited.

To be sure, the proposition that arbitration contracts should be treated "like all others" is often easier to state in the abstract than to apply in the context of specific situations that are inherently unique to arbitration agreements. Courts have found the "federal policy favoring arbitration" to play a useful gap-filling role in helping to resolve ambiguous situations. That said, nothing in *Morgan* implies reconsideration of any of the Supreme Court's prior pro-arbitration decisions.

***Viking River* Ruling**

Moreover, only three weeks after *Morgan*, the Supreme Court issued its decision in *Viking River Cruises Inc. v. Moriana*, in which it reversed a California court that refused to enforce an arbitration agreement against a plaintiff bringing a claim under California's Private Attorneys General Act.

Of particular note was the high court's explanation that FAA preemption is not limited to state rules that discriminate against arbitration on their face, such as rules that prohibit arbitration of certain kinds of claims.

The Supreme Court confirmed that the FAA also can preempt rules "that are generally applicable as a formal matter" but have the effect of making arbitration agreements ineffective because they are inherently inconsistent with arbitration. Such rules would include those that would require a party to

arbitrate on a class basis or not at all. Whatever else the high court may be thinking, it is still solidly behind its 2011 *Concepcion* decision.

Ultimately, *Morgan* reinforces the critical core of the Supreme Court's historic arbitration jurisprudence: the principle that arbitration contracts must generally be enforced, and that the FAA does not allow courts, policymakers, or legislators (other than Congress) to impose special limitations based on hostility to arbitration. So long as that principle remains solidly in place, the Supreme Court's staunch defense of arbitration agreements is likely to continue.

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