# 2 High Court Cases That Can Alter Arbitration Playing Field

By **Kevin O'Brien, Joshua Dille and Katharine Walton** (February 17, 2022)

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Each year, the U.S. Supreme Court faces a large number of certiorari petitions seeking review of a wide variety of civil disputes.

The court in recent years has consistently found room on its docket to address disputes regarding the Federal Arbitration Act, which sets out the statutory scheme for the judicial facilitation of dispute resolution through arbitration. Two matters currently pending before the court have the potential to change the playing field for attorneys counseling clients whose employment or business contracts contain arbitration clauses.

**Badgerow v. Walters**

Badgerow v. Walters presents an issue regarding the scope of federal court jurisdiction to confirm or vacate an arbitration award under the FAA. While the federal jurisdictional questions in Badgerow v. Walters may mainly interest those analyzing the varying responsibilities of federal and state courts, the case may hold a greater practical impact on arbitrating parties' ability to enforce or vacate an arbitration award.

The petitioner, Denise Badgerow, worked as a financial adviser for a Louisiana financial advising practice, REJ Properties Inc. Soon after Badgerow raised concerns about workplace harassment and reported several of her employer's alleged violations of securities laws, REJ Properties terminated her.

The respondents were the three principals of REJ Properties. Badgerow's employment with REJ Properties was subject to a Financial Industry Regulatory Authority arbitration agreement, so she entered a FINRA arbitration proceeding against the respondents. Her arbitration complaint asserted violations of both state and federal law. The FINRA arbitration panel sided with the respondents, issuing an award that dismissed Badgerow's claims with prejudice.[1]

But Badgerow was not finished yet. She filed a petition in Louisiana state court seeking to vacate the arbitration award, asserting that the respondents had obtained the award by fraud. The respondents removed the case to federal court, citing federal question jurisdiction over Badgerow's underlying claims and moving to confirm the award under Section 9 of the FAA. Badgerow sought remand to state court, which the district court denied.[2]

In finding that it had jurisdiction over the case, the district court applied the look-through approach that was developed by the Supreme Court in 2009 in Vaden v. Discover Bank, in which the court held that federal courts have jurisdiction over motions to compel arbitration under Section 4 of the FAA if the court would have had jurisdiction over the underlying controversy save for the arbitration agreement.[3]

The district court in Badgerow applied the Vaden look-through approach to the respondents' motion to confirm the award under Section 9, asserted jurisdiction because the underlying

controversy between the parties involved a federal question, and confirmed the award.[4]

On appeal, a divided panel on the U.S. Court of Appeals for the Fifth Circuit affirmed, holding that federal courts must determine their jurisdiction over petitions to confirm or vacate arbitral awards under Section 9 or 10 by "'looking through' to the claims involved in the underlying dispute (in this case, the claims brought in the FINRA arbitration proceeding)."[5]

The Supreme Court granted certiorari to resolve a circuit split on the question: "Whether federal courts have subject-matter jurisdiction to confirm or vacate an arbitration award under Sections 9 and 10 of the FAA where the only basis for jurisdiction is that the underlying dispute involved a federal question."[6]

Badgerow argued in her Supreme Court brief that the FAA's plain text does not support an application of Vaden's look-through approach to motions under Sections 9 and 10. Unlike Sections 9 and 10, Section 4 of the FAA has a prominent save for clause that requires courts to determine their jurisdiction over a petition to compel arbitration save for the arbitration agreement, which originally drove the Vaden Court to adopt the look-through approach.

Given the differences between the sections, Badgerow maintained, the court should enforce the plain text of the statute and treat motions to confirm/vacate awards differently than motions to compel arbitration.[7]

In contrast, the respondents argued that each of the FAA's various procedural provisions function as motions in a dispute, not as independent controversies, so federal courts should look through a Section 9 or 10 motion at the underlying controversy to determine if they have jurisdiction over the entire dispute.

Rarely would a motion under Section 9 or 10 present a federal question with its own jurisdictional basis, so these sections would be effectively nullified if federal courts cannot look through a petition to establish jurisdiction. The respondents interpreted Section 4's save for clause as a venue provision that explains which district courts may enforce an arbitration agreement, rather than a jurisdictional provision.[8]

The Supreme Court held oral argument on Nov. 2, 2021. Much of the discussion centered on whether to interpret the save for clause in Section 4 as a jurisdictional provision or a venue provision and whether using a "look-through" approach for Sections 9 and 10 is consistent with the text and purpose of the FAA.[9]

No one position seemed to command a majority of the justices during oral argument, so the outcome of this case is difficult to predict. The present court may be sympathetic to a more formalistic reading of the FAA's text and may hesitate to interpret the statute in a way that renders Section 4's save for clause superfluous. But the court also faces several powerful arguments for treating FAA petitions to confirm or vacate an award as motions rather than independent controversies that require their own jurisdictional analysis.

If the court sides with Badgerow, the look-through approach would apply to motions to compel arbitration under Section 4 but not to motions to confirm or vacate an arbitration award under Sections 9 and 10. This result would be analogous to enforcing a settlement after a voluntary dismissal — enforcing the settlement in federal court requires an independent jurisdictional basis apart from the underlying controversy that caused the settlement.[10]

The ability to confirm or vacate an arbitral award in federal court is arguably just as important as the ability to compel arbitration in federal court. Badgerow's position would shift petitions to confirm or vacate an award to state courts when the underlying dispute is based on a federal question.

As the respondents argued in their brief, this "relegate[s] many parties to using state procedural mechanisms that conflict with the FAA's streamlined approach, even when the claims involved are exclusively federal," noting that "several States' laws allow for vacating an arbitral award based [on] a court's reassessment of the legal and factual issues decided by arbitrators" as opposed to the specific grounds permitted in Section 10 of the FAA.[11]

If the court sides with the respondents, it could go as far as applying the look-through approach to all of the provisions of the FAA, not just Sections 9 and 10. Such a ruling for the respondents, however, would federalize more FAA litigation in a manner not contemplated by the statute.

Even if the look-through approach is just applied to motions under Sections 9 and 10, federal courts would have jurisdiction over any motion to confirm or vacate an arbitration award whenever the underlying controversy involves a federal question.

While the increased workload for federal courts would not be too overwhelming, as many Section 9 and 10 motions involve summary proceedings, some argue that state courts are equally competent to adjudicate these motions and that the statute's text suggests the FAA's drafters contemplated such a result.

Whichever route the court takes, its ruling will hold important consequences for attorneys and parties contemplating arbitration and could potentially limit access to the federal courts for parties seeking to confirm or vacate an arbitration award.

**Morgan v. Sundance Inc.**

In contrast, Morgan v. Sundance Inc. presents the issue of whether and under what circumstances a contractual right to arbitrate a dispute may be waived. Under the FAA, courts are required to place arbitration agreements "on an equal footing with other contracts."[12]

The Supreme Court outlined this position in 2010 in AT&T Mobility LLC v. Concepcion, stating that Section 2 of the FAA reflects that arbitration is a matter of contract.[13] In theory, this principle should prevent courts from treating cases involving arbitration agreements differently than cases involving other contractual disputes. In practice, several courts have constructed additional arbitration-specific rules.

Under the common-law doctrine of waiver, contractual rights "can be waived unilaterally by actions of the waiving party that are inconsistent with an intention of asserting those rights."[14]

However, many state and federal courts have an additional requirement in cases involving an agreement to arbitrate under which the party asserting waiver must demonstrate not only inconsistent actions by the waiving party, but also prejudice stemming from those inconsistent actions. The U.S. Court of Appeals for the Eighth Circuit is one of the courts to require prejudice when determining waiver.

On March 21, the Supreme Court will hear argument in Morgan v. Sundance Inc. to address

whether "the arbitration-specific requirement that the proponent of a contractual waiver defense prove prejudice" violates the Court's instruction in AT&T that arbitration agreements are on equal footing with other contracts.[15]

Petitioner Robyn Morgan worked at a Taco Bell franchise in Osceola, Iowa — one of 150 stores owned by Respondent Sundance. Morgan had signed an agreement that included a provision requiring arbitration of all disputes arising out of her employment.

On Sept. 25, 2018, Morgan instead filed a nationwide collective action against Sundance under the Fair Labor Standards Act in the U.S. District Court for the Southern District of Iowa.[16] She alleged Sundance did not properly pay its employees and shifted hours so that no employee logged over 40 hours in any given work week.

On Nov. 11, 2018, Sundance filed a motion to dismiss or stay Morgan's collective action, arguing it should be dismissed or stayed pursuant to the first-to-file rule, as a collective action against Sundance was ongoing in the U.S. District Court for the Eastern District of Michigan.[17] Sundance did not raise its right to compel arbitration under Morgan's employment agreement.

After the district court denied its motion to dismiss or stay, Sundance filed its answer, raising 14 affirmative defenses. None mentioned its right to compel arbitration of Morgan's claims. After unsuccessful settlement negotiations, Sundance filed a motion to compel individual arbitration on May 3, 2019.

The Southern District of Iowa denied Sundance's motion, but on appeal, the Eighth Circuit reversed and remanded for further proceedings.

Both courts had applied the Lewallen waiver test, which provides that a party waives its right to arbitration if it "(1) knew of an existing right to arbitration; (2) acted inconsistently with that right; and (3) prejudiced the other party by these inconsistent acts."[18]

The Eighth Circuit disagreed with the lower court's findings on the second and third elements. It found that in the eight months before Sundance filed its motion to compel, the parties had spent very little time arguing the merits of the case, and as a result, moving to arbitration would not "duplicate the parties' efforts."[19]

Turning to step three, the court found the record lacked evidence demonstrating Morgan would be prejudiced, as she had not lost evidence, nor, as the court had already pointed out, would she have to duplicate efforts. As a result, the totality of the circumstances demonstrated Morgan was not prejudiced.

Morgan obtained certiorari on the basis of her contention that requiring a showing of prejudice "[grafted] an additional requirement onto the waiver analysis" when arbitration is involved, placing the arbitration contract on an unequal footing with other contracts in violation of the Supreme Court's ruling in AT&T.

The outcome in Morgan v. Sundance will establish important guidelines for practitioners in the arbitration arena. If the court decides to affirm the Eighth Circuit's decision that a showing of prejudice is necessary to establish waiver of an arbitration right, a party could elect strategically to delay compelling arbitration — keeping a motion to compel arbitration in its back pocket and only asserting that right later if it is disappointed by the results of the litigation.

Of course, depending on the scope of the court's ruling, this approach would still entail significant risk. A court assessing prejudice under the Lewallen test would consider the totality of the circumstances in a specific case. If a party exchanges discovery or addresses the merits of the case before invoking its right to arbitration, a court may still find prejudice to the other party and thus a waiver of the contractual right to arbitrate.

Eighteen states and District of Columbia filed an amicus brief in support of Morgan, aiming to prevent parties, particularly corporate parties, from taking this approach.[20] These states contend that by allowing litigants to game the system, they tie up judicial resources and generate litigation costs, only to later compel arbitration.

For its part, Sundance maintains that there are numerous reasonable explanations for a party to engage initial defensive filings on jurisdictional or statutory grounds without having any intention to waive its right to arbitrate.[21] Moreover, Sundance argues, the waiver analysis is inappropriate as Section 3 of the FAA requires courts to stay litigation and compel arbitration unless the requesting party is in default.[22]

If the court rejects the Eighth Circuit's decision and rules that engaging in litigation constitutes a waiver of the right to arbitrate, the strategic ramifications would be more straightforward — a party to an agreement to arbitrate should file to compel arbitration when a dispute arises or waive that right.

In its amicus brief, the National Academy of Arbitrators supports this position, noting that when a party fails to compel arbitration, and instead waits to see if litigation offers a better outcome, arbitration "becomes a tactical device and simply serves to evade prompt and efficient resolution of the case — while flouting the prior commitment to resolve the dispute only in arbitration."[23]

Whatever the result of these two cases, attorneys counseling clients about arbitration clauses in their contracts will be well-advised to study not only the disposition of the cases but the specific reasoning of the court when the opinions are eventually issued.

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[1] Badgerow v. Walters , 975 F.3d 469, 470 (5th Cir. 2020).

[2] Badgerow v. Walters, No. 19-cv-10353, 2019 U.S. Dist. LEXIS 106832, at *6 (E.D. La. June 26, 2019).

[3] Vaden v. Discover Bank , 556 U.S. 49, 62 (2009),

[4] Badgerow v. Walters, 2019 U.S. Dist. LEXIS 106832, at *6.

[5] Badgerow v. Walters, 975 F.3d 469, 470 (5th Cir. 2020).

[6] Brief for Petitioner at I, Badgerow v. Walters, No. 20-1143 (U.S. petition for cert. filed Feb. 12, 2021).

[7] Reply of Petitioner at 2-3, Badgerow v. Walters, No. 20-1143 (U.S. petition for cert. filed Feb. 12, 2021).

[8] Brief for Respondent at 23-25, Badgerow v. Walters, No. 20-1143 (U.S. petition for cert. filed Feb. 12, 2021).

[9] Transcript of Oral Argument, Badgerow v. Walters, No. 20-1143 (U.S. petition for cert. filed Feb. 12, 2021).

[10] Kokkonen v. Guardian Life Ins. Co ., 511 U.S. 375 (1994).

[11] Brief for Respondent at 14, 46, Badgerow v. Walters, No. 20-1143 (U.S. petition for cert. filed Feb. 12, 2021)

[12] AT&T Mobility LLC v. Concepcion , 563 U.S. 333, 339 (2011).

[13] Id.

[14] Brief for Petitioner at 3, Morgan v. Sundance, Inc., No. 21-328 (U.S. petition for cert. filed Aug. 27, 2021).

[15] Id. at i.

[16] Id. at 9.

[17] Morgan v. Sundance, Inc ., No. 4:18-cv-316, 2019 U.S. Dist. LEXIS 177824, at *1 (S.D. Iowa Mar. 5, 2019).

[18] Lewallen v. Green Tree Servicing, L.L.C. , 487 F.3d 1085, 1090 (8th Cir. 2007).

[19] Morgan v. Sundance, Inc., 992 F.3d 711, 714 (8th Cir. 2021).

[20] Brief of Minnesota, Maryland, et al. as Amici Curiae in Support of Petitioner at 19-20, Morgan v. Sundance, Inc., No. 21-328 (U.S. petition for cert. filed Aug. 27, 2021).

[21] Brief for Respondent at 34, Morgan v. Sundance, Inc., No. 21-328 (U.S. petition for cert. filed Aug. 27, 2021).

[22] Id. at 15.

[23] Brief of the National Academy of Arbitrators as Amici Curiae in Support of Petitioner at 2, Morgan v. Sundance, Inc., No. 21-328 (U.S. petition for cert. filed Aug. 27, 2021).