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SCOTUS Grounds the "Wholly Groundless" Exception: Parties Can Delegate Arbitrability to Arbitrators

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On January 8, 2018, the U.S. Supreme Court issued a unanimous decision holding that federal courts must categorically enforce a contractual provision delegating to an arbitral tribunal the question of whether the dispute must be arbitrated. *Henry Schein, Inc. v. Archer and White Sales, Inc.*, 586 U.S. ___ (2019). In doing so, the Court resolved a deep split among the federal courts of appeals. Reversing the position adopted by the majority of the circuits, the Supreme Court held that when a contract expressly delegates to the arbitral tribunal the question of "arbitrability"—that is, whether an arbitration agreement applies to a particular dispute—courts may not resolve that question themselves, even if the underlying arbitrability argument is allegedly "wholly groundless." The Supreme Court's decision is significant for parties who are drafting, or who might litigate the scope of, arbitration agreements in their commercial contracts.

The Underlying Litigation

In the underlying litigation, dental equipment distributor Archer and White Sales Inc. sued competing distributor Henry Schein Inc. in the Eastern District of Texas, alleging that Schein had conspired to limit Archer and White's sales territories under various distribution agreements between them. In response, Schein invoked the Federal Arbitration Act (the "FAA") and moved to compel Archer and White to arbitration.

Archer and White objected, arguing that a carve-out in the arbitration agreement precluded arbitration of disputes seeking injunctive relief. Archer and White further asserted that, where the argument in favor of compelling arbitration is "wholly groundless"—as Archer and White argued was the case—the district court should itself resolve the threshold question of arbitrability. Applying circuit precedent, the district court agreed, and denied Schein's motion to compel arbitration. The Fifth Circuit affirmed. Schein then sought certiorari from the Supreme Court to resolve the issue of whether the "wholly groundless" exception exists under the FAA.

The Supreme Court's Holding

In his first authored opinion since joining the Supreme Court, Justice Kavanaugh, writing for a unanimous Court, vacated the Fifth Circuit's decision. The Court emphasized that the FAA requires arbitration agreements, like any other contracts, to be enforced according to their terms. In accordance with that precept, not only may parties to an arbitration clause agree to have an arbitral

tribunal decide the merits of their particular dispute, they may also agree to have an arbitrator decide the "gateway question of arbitrability." Where the parties have "clearly and unmistakably" done so, the Court observed, an "'agreement to arbitrate a gateway issue is simply an additional, antecedent agreement the party seeking arbitration asks the federal court to enforce, and the FAA operates on this additional arbitration agreement just as it does on any other.'" Slip Op. at 4 (quoting *Rent-A-Center, West, Inc. v. Jackson*, 561 U.S. 63, 70 (2010)).

Because the FAA sets forth no express exception to that general rule, the Court concluded that the "wholly groundless" exception is inconsistent with the text of the FAA and Supreme Court precedent: "Just as a court may not decide a merits question that the parties have delegated to an arbitrator, a court may not decide an arbitrability question that the parties have delegated to an arbitrator." Slip Op. at 5. As the Court noted, this would be the case even if the court were otherwise to believe that the underlying arbitrability argument was wholly groundless.

In striking down the "wholly groundless" exception, the Supreme Court rejected reliance on several policy-based principles, including the contention that the exception enables courts to block frivolous efforts to transfer disputes from the court system to arbitration. The Court found this potential problem to be of no moment, as any such efforts did not appear to have caused a problem in those circuits opting not to recognize the "wholly groundless" exception. Slip Op. at 8. The Court added that arbitral tribunals are already capable of efficiently disposing of frivolous cases and deterring frivolous motions to compel, including by imposing fee-shifting and cost-shifting sanctions.

What the Supreme Court Did Not Decide

As important as the *Schein* decision is to eliminating certain challenges to a motion to compel arbitration, it is equally important to recognize what the Supreme Court in *Schein* did not hold.

The Court did ***not*** conclude that an arbitral tribunal ***always*** has the authority to decide its own jurisdiction to resolve a particular dispute. Rather, the Court ruled only that the judge-made "wholly groundless" exception cannot be invoked to deprive an arbitral tribunal of the ability to make that gateway decision, where there exists an otherwise valid delegation. Whether, pursuant to a valid arbitration agreement, the parties have "clearly and unmistakably" chosen to delegate the arbitrability issue to the arbitral tribunal, still remain issues for the courts' initial review and determination.

The Supreme Court also emphasized that it was ***not*** deciding whether there was a proper delegation by the parties in this case, instead remanding that issue back to the lower courts. Slip Op. at 8. By limiting its holding, the Court left unanswered certain other threshold questions regarding the broader arbitrability doctrine. Most notably, the Court expressed no opinion as to whether the incorporation of institutional rules into an arbitration agreement (here, the parties' agreement incorporated the AAA arbitration rules but did not otherwise specifically address to whom the question of arbitrability was to be delegated) is sufficient to demonstrate the parties' contractual intent to delegate the gateway issue of arbitrability to the arbitral tribunal. Slip Op. at 8. Consistent with longstanding Supreme Court precedent, that determination hinges on whether there is "'clear and unmistakable evidence'" that the parties agreed to do so. Slip Op. at 8 (quoting *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 944 (1995)). This issue will almost certainly be litigated on remand before the Fifth Circuit and receive renewed attention in other circuits and district courts.

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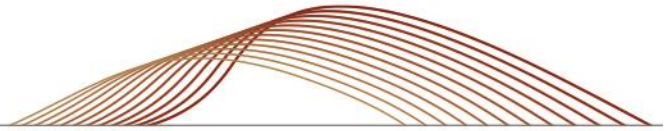

The *Schein* decision should remind parties that, when they are negotiating and drafting their arbitration agreements, they should carefully consider whether they wish an arbitral tribunal or a court to decide the gateway issue of arbitrability. Now that the Supreme Court has, at least in part, settled an important "who decides" question, going forward, parties and counsel should be mindful that arbitration agreements that "clearly and unmistakably" delegate the question of arbitrability to the arbitral tribunal will be enforced as written. And if there is any legitimate question whether the parties have "clearly and unmistakably" delegated the question of arbitrability to the arbitral tribunal, then a court will make that determination.

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