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JEFFERSON BAR ASSOCIATION
33RD ANNUAL CLE BY THE SEA

AVOIDING LITIGATION: AN OVERVIEW OF ARBITRATION

March 18, 2022
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OVERVIEW OF THE FEDERAL ARBITRATION ACT

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The Scope of the FAA, 9 U.S.C. § 1 *et seq.*

The FAA applies in both state and federal courts and governs any arbitration agreement that: (i) is in writing; (ii) relates to a maritime transaction or a transaction involving interstate or foreign commerce; and (iii) the agreement is to arbitrate a controversy arising from such a transaction

Core Principle of the FAA: Arbitration agreements involving interstate or foreign commerce must be considered "valid, irrevocable, and enforceable, save as upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2.

This principle is supported by the following provisions:

- **9 U.S.C. § § 3-4** – Provisions requiring courts to stay proceedings involving matters referrable to arbitration and to issue orders requiring arbitration of such matters.
- **9 U.S.C. § 9** – Provisions requiring courts to confirm arbitral awards.
- **9 U.S.C. § 10** – Limited statutory grounds for vacating an arbitration award.

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The Scope of the FAA, 9 U.S.C. § 1 *et seq.* (cont....)

The FAA cuts a broad swath. Virtually all disagreements that can be submitted to courts for resolution can, with the parties' consent, be resolved in arbitration, and the FAA will govern. For example, the FAA can apply to commercial, employment, consumer and tort disputes.

Disputes to which the FAA does not apply:

- The FAA does not "apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce." 9 U.S.C. § 1. Thus, employees "actually engaged in the movement of goods in interstate commerce" are not covered by the FAA.
- Labor arbitrations and collective bargaining agreements are not governed by the FAA but are instead governed by separate statutes such as the National Labor Relations Act, the Labor Management Relations Act of 1947, and the Norris-LaGuardia Act.

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The Policy and History of the FAA

The Supreme Court has described 9 U.S.C. § 2 as reflecting both a "liberal federal policy favoring arbitration" and the "fundamental principle that arbitration is a matter of contract." *AT&T Mobility LLC v. Concepcion,* 563 U.S. 333 (2011).

Thus, "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration." *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.,* 460 U.S. 1 (1983).

In line with these principles, courts must place arbitration agreements on an "equal footing" with other contracts and must enforce arbitration agreements according to their terms.

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The FAA's Preemption Power

Section 2 of the FAA sets forth the FAA's power to preempt state laws that single out or disfavor arbitration. *See Kindred Nursing Ctrs., L.P. v. Clark, 137 S. Ct. 1421 (2017).*

States cannot prohibit arbitration outright, make certain classes of claims non-arbitrable, "condition the enforceability of arbitration agreements on compliance with a special notice requirement not applicable to contracts generally," or generally frustrate the intent of parties in connection with their agreement to arbitrate.

The FAA prevents states from singling out arbitration provisions, requiring instead that they place such provisions on the "same footing" as any other contract term.

The FAA also preempts state laws that invalidate class action waivers in arbitration agreements.

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Staying Litigation and Compelling Arbitration

When there is a dispute among parties in which one party wants to resolve the dispute before an arbitrator and the other before a judge, § § 3 and 4 of the FAA come into play.

These sections function together, as a practical matter, when a court is called upon to decide whether a dispute is arbitrable. Section 3 allows a court to stay litigation, while § 4 permits a court to compel arbitration.

The § 3 inquiry is one of scope. Section 3 requires examining whether the proceeding is referable to arbitration. That is, does the parties' dispute fall within the ambit of the arbitration clause? If so, § 3 gives the court the power to stay the litigation in favor of arbitration.

The § 4 inquiry is one of enforceability. Did an agreement to arbitrate form, and has it otherwise been complied with? If formation and enforceability are not at issue, the court must order "the parties to proceed to arbitration in accordance with the terms of the agreement."

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Staying Litigation & Compelling Arbitration (cont...)

Courts called upon to stay litigation, compel arbitration, or both, must answer two questions:

1. Is there an enforceable arbitration agreement?
2. Does the dispute fall within the scope of the arbitration clause?

If both of these questions are answered affirmatively, the parties will be required to arbitrate rather than litigate.

-*Huckaba v. Ref-Chem., L.P.*, 892 F.3d 686, 688 (5th Cir. 2018)

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Federal Arbitration Act – Introduction to Threshold Arbitrability

Separate and apart from the question of whether a dispute will proceed in court or in arbitration is the question of who will answer that question, judge or arbitrator. This is a question of "threshold arbitrability". Threshold arbitrability issues go to whether the case will stay in court or proceed before an arbitrator for adjudication on the merits.

When a party wishes to stay in court and is opposed to arbitration, they can raise threshold arbitrability questions by arguing one or more of the following:

(1) that the arbitration agreement or arbitration clause is unenforceable – *i.e.,* to place the agreement's existence "in issue" for FAA purposes,

(2) that the dispute does not fall within the scope of the arbitration agreement or arbitration clause, or

(3) that the right to arbitrate has been waived.

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Threshold Arbitrability Issue: Delegation Provisions

Rent-A-Center West v. Jackson, 561 U.S. 63 (2010)

Reaffirmed and refined the holdings in *Prima Paint Corp. v. Flood & Conklin Mfg. Co.,* 388 U.S. 395 (1967), and *First Options of Chicago, Inc. v. Kaplan,* 514 U.S. 938 (1995).

The "delegation provision" of an arbitration agreement assigns to the arbitrator questions about the enforceability of the agreement, including whether it is unconscionable.

The *Rent-A-Center* plaintiff argued the arbitration agreement was unconscionable and thus unenforceable. He challenged the entire agreement, not the specific delegation provision.

Section 2 of the FAA applies to this provision and requires enforcement of the agreement according to its terms. Thus, Section 2 required the "delegation provision" be treated as valid and enforceable unless the plaintiff specifically challenged it. He did not.

The Supreme Court held that a challenge to the validity of an arbitration agreement that contains a provision delegating authority to an arbitrator to determine enforceability of the agreement (*i.e.,* delegation provision) must be decided by the arbitrator, not a court.

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State Arbitration Law – Which Arbitration Law Applies?

While the FAA applies in both federal and state courts and extends to Congress's full reach under the Commerce Clause, all 50 states and the District of Columbia also provide for their own state law arbitration regimes.

Parties can contractually agree to apply state or federal arbitration law to their arbitration agreement.

However, when interstate commerce is not implicated, the FAA cannot apply and state arbitration law must control.

When interstate commerce is implicated, the parties may agree that either the FAA or state arbitration law will govern their agreement.

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The Arbitration Agreement – Formation Under State Contract Law

"[A]rbitration is a matter of contract[, thus] a party cannot be required to submit to arbitration any dispute which he has not agreed to submit." *See United Steelworkers of Am. v. Warrior & Gulf Nav. Co.,* 363 U.S. 574 (1960); *see also First Options of Chicago, Inc. v. Kaplan,* 514 U.S. 938 (1995).

Thus, in order for an arbitration agreement to be enforceable, the usual requirements for contract formation under state law must be satisfied including offer, acceptance and consideration.

An arbitration agreement is subject to common law defenses to enforceability, including fraud, duress and unconscionability (procedural, substantive). *Epic Sys. Corp. v. Lewis,* 138 S. Ct. 1612 (2018).

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Benefits of Arbitration Versus Litigation

- **More Cost-Effective** – Discovery & motion practice can be more limited in scope.
- **Faster Resolution** – Finality may be reached sooner than litigation, especially due to limited right to challenge arbitral awards.
- **May Reduce Runaway Jury Risks** -- May reduce high emotional distress or punitive damages awards, especially if not capped by an applicable law.
- **More Private Forum** – Less public forum versus court proceedings.
- **Ability to Select Arbitrator with Subject Matter Expertise** – Input into arbitrator selection process, rather than random judge assignments in court.
- **More Procedural Flexibility** – Parties can customize discovery and hearing rules
- **More Scheduling Flexibility & Access to Arbitrator** – More convenient for lawyers and witnesses. Easier access to arbitrator for disputes between the parties.

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Potential Disadvantages of Arbitration

- **Arbitration Fees** – Company may bear full cost of arbitration, and/or face multiple arbitrations.
- **Potentially High Discovery Costs** – Arbitrator may be permissive on discovery issues/motions.
- **Lower Dispositive Motion Success** – Less likely to grant dispositive motions, increasing likelihood that claim will proceed to hearing.
- **Arbitrator Scheduling Issues** – Desirable arbitrators may have full calendars.
- **Agreeing on an Arbitrator** – Parties may have difficulty agreeing on acceptable arbitrator.
- **Difficulty Urging Procedural Defenses** – Arbitrator may be less likely to accept procedural defenses, such as laches, statutes of limitations or exhaustion of administrative remedies.
- **Permissibility on Objectionable Evidence** – May be more likely allow hearsay and irrelevant evidence. Not bound to follow Fed. R. Evid., unless agreement states otherwise.
- **Arbitrator Bias** – May be influenced by incentives (e.g. paid for each hearing day, reputation concerns about pattern of rulings, and belief plaintiffs should have hearing opportunity).
- **Arbitration Is Not Automatically Confidential** – Private but not necessarily confidential.
- **Courts Generally Do Not Disturb Arbitration Awards** – Limited challenge grounds available.

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RECENT ARBITRATION CASES FROM THE UNITED STATES FIFTH CIRCUIT COURT OF APPEALS

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ISSUE – Proof required to show arbitration agreement formation "in issue"?
***Gallagher v. Vokey,* 860 Fed.Appx. 354 (5th Cir. July 1, 2021)**

- The Fifth Circuit found the "quantum of evidence required to prove or disprove the existence of an agreement to arbitrate is not entirely clear in this Circuit."
- Party resisting arbitration bears the burden of showing he is entitled to a jury trial under Section 4 of the FAA.
- When competent evidence of formation of arbitration agreement is presented, Section 4 of the FAA requires a party resisting arbitration to produce *some* contrary evidence to put the making of an arbitration agreement "in issue."
- Texas contract law was applied to find plaintiff unconditionally assented to the arbitration agreement terms. No evidence agreement formation was "in issue."
- **Fifth Circuit found:** (i) valid agreement to arbitrate; (ii) dispute fell within the agreement scope; and (ii) no federal statute/policy rendered claim nonarbitrable.

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RELEVANT ISSUE -- Arbitration Agreement Unenforceable Without Signature?
Trujillo v. Volt Mgmt. Corp., 846 Fed.Appx. 233 (5th Cir. Feb. 25, 2021)

- Plaintiff argued could not be compelled to arbitrate, because she did not sign arbitration agreement.
- Fifth Circuit applied Texas contract law to assess existence of a binding contract.
- Fifth Circuit *Huckaba* opinion, 892 F.3d at 689, found a signature is not required to bind parties to a contract unless the parties intended to require a signature. Unlike *Huckaba,* arbitration agreement in *Trujillo* did not contain express language requiring a signature to be bound by agreement.
- District Court also found the FAA does not require a signature for an arbitration agreement to be enforceable. Thus, lack of signature did not preclude enforcement of arbitration agreement.
- Evidence showing enforceable arbitration agreement included: (i) job application contained arbitration agreement provision; (ii) accepted employment knowing arbitration was a condition of employment; (iii) continued to work for Volt after receiving ADR policy in employee handbook; and (iv) plaintiff's claims fell within scope of arbitration agreement.
- **FINDING** – Fifth Circuit affirmed district court holding of valid and enforceable arbitration agreement, even without signature.

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RELEVANT ISSUE – Waiver of Right to Arbitrate?
Butler v. Z&H Foods, Inc., 2021 WL 4073110 (5th Cir. Sept. 7, 2021)

- Plaintiffs challenged motion to compel arbitration on several grounds, including argument Z&H waived its right to arbitrate based on litigation conduct.
- "Waiver of arbitration is a disfavored finding. But we will find it when the party seeking arbitration **substantially invokes** the judicial process to the detriment of or prejudice of the other party." *Int'l Energy Ventures Mgmt., LLC v. United Energy Group, Ltd.,* 999 F.3d 257, 266 (5th Cir. 2021).
- "Substantially invoking" requires some overt act in court that evinces a desire to resolve arbitrable dispute through litigation rather than arbitration.
- "Merely participating in discovery – without showering the opposing party with interrogatories and discovery requests – does not amount to waiver." *Keytrade USA Inc. v. Ain Temouchent M/V,* 404 F.3d 891, 898 (5th Cir. 2005).
- Z&H filed answer and responded to plaintiffs' discovery requests but did not make discovery requests or motions of its own. Z&H waited nine months to file motion to dismiss and to compel arbitration.
- **FINDING – Under Fifth Circuit precedent, conduct did NOT constitute a waiver by Z&H Foods of right to arbitrate plaintiffs' claims.**

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ISSUE – Is manifest disregard of law a ground for setting aside arbitration award?
***Jones v. Michaels Stores, Inc.*, 991 F.3d 614 (5th Cir. 2021)**

- Plaintiff invoked arbitration agreement after fired, and arbitrator ruled against her. Plaintiff then sued Michaels in federal court on same termination under different legal theory. Second arbitrator ruled *res judicata* barred later Title VII claims. Plaintiff asked federal court to vacate second arbitrator *res judicata* ruling based on manifest disregard of law in finding her Title VII claims were precluded.
- Fifth Circuit noted this appeal "is an opportunity to emphasize at least one thing that we have directly resolved: manifest disregard of the law as an independent, nonstatutory ground for setting aside an award must be abandoned and rejected." *See also Hall St. Assocs., L.L.C. v. Mattel, Inc.*, 552 U.S. 576 (2008).
- **FINDING** – Arbitrator's purported manifest disregard of law was NOT an independent, nonstatutory ground for setting aside arbitration award. Arbitration awards may only be vacated under limited reasons provided in FAA 9 U.S.C. § 10.

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ISSUE –Is Order Denying Reconsideration of Motion to Compel Arbitration Interlocutory?
***Doe v. Tonti Mgmt. Co., LLC*, 2022 WL 293222 (5th Cir. Feb. 1, 2022)**

- Following grant of motion to compel arbitration, plaintiff moved for reconsideration of the order. District Court denied motion for reconsideration, and plaintiff filed interlocutory appeal.
- Section 16(a)(3) of the FAA provides "an appeal may be taken from … a final decision with respect to an arbitration that is subject to this title." 9 U.S.C. § 16(a)(3). However, an appeal may not be taken from an interlocutory order compelling arbitration. *Id. at* § 16(b)(3).
- Thus, orders compelling arbitration that stay and administratively close a civil action pending arbitration are interlocutory and unappealable.
- **FINDING** – Denial of a motion for reconsideration of an order compelling arbitration does not possess any more finality than an order compelling arbitration itself; both are interlocutory and unappealable under § 16(b)(3) of the FAA.

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RECENT ARBITRATION-RELATED EVENTS AND ISSUES

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NEW FAA AMENDMENT BANNING PRE-DISPUTE MANDATORY ARBITRATION OF SEXUAL HARASSMENT AND SEXUAL ASSAULT CLAIMS

- On February 10, 2022, Congress passed the *Ending Forced Arbitration of Sexual Assault and Sexual Harassment Act of 2021* (H.R. 4445). President Biden signed it into law on March 3, 2022.
- The new law is now in effect and applies to disputes that arise on or after March 3, 2022.
- The new law adds a new Chapter 4 to the FAA that renders invalid and unenforceable (i) pre-dispute arbitration agreements related to claims of sexual assault or sexual harassment; and (ii) joint-action waivers prohibiting joint, class or collective judicial, administrative, or arbitration proceedings related to claims of sexual assault or sexual harassment. *See* 9 U.S.C. § 402(a).
- The new law applies to disputes or claims arising or accruing on or after enactment date.
- The new law does not (i) apply retroactively; (ii) apply to agreements to arbitrate other claims, such as gender discrimination, or harassment based on other categories (e.g. race or religion); and (iii) apply to voluntary, post-dispute agreements to arbitrate after a claim arises.
- RECOMMENDATION – Review existing arbitration agreements in light of this new law.

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NLRB Reconsidering "Gag Orders" in Arbitration Agreements

- On January 18, 2022, the NLRB announced it is considering adopting a new legal standard on whether confidentiality requirements ("gag orders") in mandatory arbitration agreements violate the National Labor Relations Act (NLRA).
- In *Ralph's Grocery Co.,* the NLRB has invited briefs by March 21, 2022 on: (i) whether the arbitration policy in that case interferes with employees' right to file board charges or board processes; and (ii) if FAA does not prevent NLRB from reviewing arbitration gag-orders under the NLRA, what standard should the NLRB apply to determine if such orders are legal?
- Potential Impact – This case could allow the NLRB to make mandatory arbitration contracts more worker-friendly by prohibiting confidentiality requirements and increasing employee protections against losing access to administrative agencies. Could overturn 2020 NLRB decision *California Commerce Club.*

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SOURCES AND REFERENCES

- Federal Arbitration Act, 9 U.S.C. § § 1 *et seq.*
- Louisiana Binding Arbitration Law (BAL), 9 La. R.S. § § 4204-4271
- Mississippi Arbitration Act (MAA), Miss. Code Ann. § § 11-15-1 – 11-15-37
- Texas Arbitration Act (TAA), Tex. Civ. Prac. & Rem. Code § § 171.001 *et seq.*
- Federal Arbitration Act (FAA) Glossary, Westlaw, Practical Law
- Understanding the Federal Arbitration Act, Westlaw, Practical Law Arbitration
- Employment Arbitration Agreements (US), Westlaw, Practical Law Labor & Employment
- *Congress passes FAA Amendment Banning Mandatory Arbitration of Sexual Assault and Sexual Harassment Claims,* Westlaw, Practical Law Labor & Employment, Feb. 15, 2022
- *NLRB Invites Briefs on Mandatory Arbitration Clauses*, NLRB, Jan. 18, 2022, available at https://www.nlrb.gov/news-outreach/news-story/nlrb-invites-briefs-on-mandatory-arbitration-clauses

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QUESTIONS?

Thank you for attending.

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