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CLIENT ALERT

Do Not Delay, Arbitrate Today: Prejudice No Longer Necessary To Find Waiver of Arbitration Agreement

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Thanks to a new Supreme Court decision, the risk of implicitly waiving the right to arbitrate just became a lot greater. In a unanimous decision issued this week in *Morgan v. Sundance*, the Supreme Court of the United States held that participating in litigation may amount to waiver of a right to arbitrate regardless of whether the other side suffered prejudice. As the Court explained, waiver is simply "the intentional relinquishment or abandonment of a known right." In every other context, assessing waiver does not require an analysis of prejudice to another party. Yesterday's decision brings the analysis of whether a party waived its arbitration rights in line with ordinary waiver and contract analysis.

Plaintiff Robyn Morgan was an employee of Taco Bell. Her employment contract included an arbitration agreement. Disregarding that agreement, Morgan initiated a class action lawsuit against Sundance, the parent of Taco Bell, for violations of the Fair Labor Standards Act. Instead of immediately attempting to enforce the arbitration agreement, Sundance participated in the litigation. It filed a motion to dismiss, answered Morgan's complaint, and pursued settlement through mediation. Only after mediation failed—eight months after litigation began—did Sundance finally move to compel arbitration.

Eighth Circuit precedent had adopted a special waiver analysis for arbitration, finding waiver only when (1) a party knew of its right, (2) "acted inconsistently with that right," *and* (3) "prejudiced the other party." The district court found that Morgan had been prejudiced by Sundance's late switch from litigation to arbitration; on appeal, the Eighth Circuit disagreed. The Eighth Circuit assessed the stage of trial: discovery had not commenced, and the parties had not yet argued the merits of any issue. Finding that Morgan had not been "prejudiced" by Sundance's litigation conduct, the Eighth Circuit held that Sundance could still compel arbitration.

The Supreme Court granted certiorari to resolve a circuit split on this issue: eight other circuits had similar arbitration-specific rules requiring a showing of prejudice, while only the Seventh and D.C. Circuits did not.

In its unanimous decision, the Court recognized that the nine circuits' prejudice requirements grew from an interpretation of a congressional "policy favoring arbitration" enacted in the Federal Arbitration Act (FAA). According to the Court, however, that policy does *not* call for courts to favor arbitration through enactment of specialized rules. As the Court explained, "the policy is to make arbitration agreements as enforceable as other contracts, but not more so." Some courts historically had refused to enforce arbitration agreements; the FAA was enacted to reverse

that trend. The resulting policy gives arbitration agreements the same legal force as any other contract. At the same time, however, courts may not create "bespoke" procedural rules specifically for arbitration to promote that policy goal. Rather, courts must adhere to their ordinary procedural rules, treating arbitration clauses like any other contract provision, and a waiver of arbitration rights like any other waiver.

On remand, the Eighth Circuit will answer the question, "Did Sundance . . . knowingly relinquish the right to arbitrate by acting inconsistently with that right?" Or the Eighth Circuit "may determine that another procedural framework (such as forfeiture) is appropriate." But whatever framework it chooses, it must apply that framework just as it would to any other waiver issue.

This decision presents a departure from the usual pattern of Supreme Court arbitration decisions. Again and again, the Court has granted review to pull back a state rule or circuit precedent that treats arbitration clauses less favorably than other contacts. In this decision, the Court has made clear that the FAA's policy favoring arbitration is not unlimited. It requires recognizing arbitration rights to the same extent as—but no more than—any other contractual right.

The lesson for litigants is to make a decision *early* about whether to compel arbitration. Engaging in litigation rather than immediately compelling arbitration may amount to an implicit waiver; simple delay in asserting a right to arbitration may as well. While these may remain fact- (and jurisdiction-) specific questions, one point is now clear: a federal court will not look to the impact on the other party in analyzing whether the party waived arbitration.

Maxwell Johnson, a summer associate in Winston's Chicago office, assisted with this briefing.

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