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Supreme Court Rejects "Wholly Groundless" Exception to Contractual Delegation of Arbitrability Decisions to Arbitrators

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On January 8, 2019, the U.S. Supreme Court (the "Court") released its decision in *Henry Schein, Inc. v. Archer & White Sales, Inc.*, No. 17-1272. In a unanimous decision, the Court held that a court may not override a contractual agreement that delegates arbitrability questions to an arbitrator, even if the court finds that the claim of arbitrability for a particular dispute is "wholly groundless." The Court declined to address the question of whether the parties in fact contractually agreed to allocate the question of arbitrability to the arbitral tribunal, leaving that issue to be decided by the Fifth Circuit on remand.

The Court consistently has ruled that an arbitrator may only decide gateway issues of arbitrability if there is "clear and unmistakable evidence" of the parties' intent for such issues to be resolved in arbitration. It remains unclear, though, what constitutes "clear and unmistakable evidence" of party intent, including whether a contractual incorporation of arbitration rules that allocate gateway jurisdictional issues to the arbitral tribunal constitutes sufficient evidence of intent.

In the meantime, some federal courts have tried to short-circuit the process of having arbitrability issues decided in arbitration by deciding arbitrability questions themselves if the claim of arbitrability is "wholly groundless." Some courts, including the First, Fifth, Sixth and Federal Circuits, have ruled that even if the court finds "clear and unmistakable" intent to delegate threshold questions of arbitrability to the arbitral tribunal, the court may then conduct a further inquiry into whether the claim of arbitrability is "wholly groundless."

After *Schein*, it will be difficult for a party resisting arbitration to do so on any ground that is not explicitly recognized in the FAA.

This “wholly groundless” exception was developed to prevent waste of time and resources by giving courts the ability to adjudicate claims that clearly were not arbitrable even when the parties agreed to arbitrate their disputes. In *Schein*, the Court rejected the “wholly groundless” exception, holding that courts must allow the arbitral tribunal to decide gateway issues of arbitrability where the parties have so agreed, regardless of the court’s view as to the merits of the arbitrability question.

Case Summary

Schein relates to an antitrust dispute between dental products distributor Archer & White Sales (“Archer & White”), Henry Schein Incorporated (“Schein”) and dental equipment manufacturers (together, the "Defendants"). Archer & White sued the Defendants, who moved to compel arbitration based on the distribution contract, under which any dispute was to be resolved through arbitration “except for actions seeking injunctive relief.” Archer & White objected to arbitration because it partially sought injunctive relief, which, it argued, triggered the carve-out from arbitration.

The Defendants argued that the distribution contract delegated questions of arbitrability to the arbitrator because the contract expressly incorporated the arbitration rules of the American Arbitration Association (“AAA”), which provide that only arbitrators may resolve questions of arbitrability. Archer & White invoked the “wholly groundless” exception, arguing that where a party’s claim of arbitrability is frivolous or “wholly groundless,” a district court, rather than an arbitrator, may resolve the threshold question of arbitrability regardless of whether the parties agreed to have such questions decided by an arbitrator.

Relying on Fifth Circuit precedent, the District Court found that a “wholly groundless” exception existed, ruled that Defendants' argument for arbitration was wholly groundless, and denied their motion to compel arbitration. The Fifth Circuit affirmed the District Court’s decision, which Defendants appealed to the Court.

In *Schein*, the Court, in a *per curiam* opinion authored by Justice Kavanaugh, rejected the "wholly groundless" exception on the ground that it is inconsistent with the FAA, which provides that courts must enforce arbitration agreements according to their terms, including agreements that an arbitrator, rather than a court, will resolve threshold arbitrability questions. The Court remanded the case to the Fifth Circuit to address whether the contract at issue contained clear and unmistakable evidence to delegate the arbitrability question to an arbitrator.

Since it remains uncertain what constitutes clear and unmistakable evidence of party intent to have arbitrability issues decided by an arbitral tribunal, parties drafting arbitration agreements should consider expressly specifying who has authority to decide threshold arbitrability questions rather than relying on references to arbitration rules to express that intent.

Implications of *Schein*

Schein only decided the narrow question of whether the "wholly groundless" exception is permissible under the FAA. While previously utilized in the Fifth, Sixth and Federal Circuits, it was rarely invoked in practice. However, *Schein* is significant in a number of respects.

1. *Schein* affirms *First Options* and its progeny

Schein reaffirms the Court's decisions in *First Options of Chicago, Inc.* and *Rent-A-Center* holding that parties may delegate threshold arbitrability questions to the arbitrator if there is "clear and unmistakable" evidence of their intent to do so.

2. *Schein* forecloses other implied exceptions to the FAA

Schein advocates a strict textual reading of the FAA and arbitration agreements. After *Schein*, it will be difficult for a party resisting arbitration to do so on any ground that is not explicitly recognized in the FAA. This should give comfort to parties to arbitration agreements that courts will enforce such agreements according to their terms.

3. *Schein* leaves open the question of what constitutes "clear and unmistakable" evidence of intent to decide jurisdictional questions in arbitration

Schein expresses no view on whether the contract at issue actually delegated threshold arbitrability questions to the arbitrator (because the issue was not decided by the court of appeals). Thus, it remains an open question whether a contract's incorporation of arbitration rules — such as the AAA or ICC rules — that grant arbitrators the power to resolve threshold arbitrability questions is sufficient to constitute clear and unmistakable evidence to delegate threshold arbitrability questions to the arbitrator. Courts and academics are divided on how to address this important question.

Since it remains uncertain what constitutes clear and unmistakable evidence of party intent to have arbitrability issues decided by an arbitral tribunal, parties drafting arbitration agreements should consider expressly specifying who has authority to decide threshold arbitrability questions rather than relying on references to arbitration rules to express that intent.

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