ALTERNATIVE DISPUTE RESOLUTION – ARBITRATION: WAIVER OF FEDERAL ARBITRATION RIGHT NO LONGER REQUIRES SHOWING OF PREJUDICE

Morgan v. Sundance, 142 S. Ct. 1708 (2022).

ABSTRACT

In *Morgan v. Sundance, Inc.* the United States Supreme Court addressed a circuit split concerning whether a showing of prejudice is a prerequisite for finding a party waived the right to arbitrate a dispute. The Eighth Circuit, among the majority of circuits prior to *Morgan*, determined the Federal Arbitration Act's "policy favoring arbitration" permitted the waiver of arbitration to require a showing of prejudice, despite waiver of other contract rights lacking a requirement of prejudice. The U.S. Supreme Court *held* the Eighth Circuit erred in conditioning waiver of the right to arbitrate on a showing of prejudice.

The Federal Arbitration Act has broad application, including applicability in any contract with an arbitration clause that involves interstate commerce or maritime law. The Federal Arbitration Act preempts state law when state law and the Act conflict. However, parties may agree to the application of state arbitration law in an express contractual statement. Thus, the U.S. Supreme Court's holding in *Morgan v. Sundance, Inc.* causes a potential incentive for practitioners to contract around the Federal Arbitration Act and require state arbitration law where the state law requires a showing of prejudice for waiver of arbitration. This is because a showing of prejudice may better safeguard parties from unintentionally waiving the right to arbitrate by commencement of litigation or otherwise failing to promptly seek arbitration for the resolution of a dispute.

The North Dakota Supreme Court previously followed Ninth Circuit precedent in requiring prejudice for waiver of arbitration. Additionally, the states of Minnesota, Montana, and South Dakota have required the showing of prejudice for waiver of arbitration. North Dakota practitioners should be cognizant of the differing requirements for waiver of arbitration between the Federal Arbitration Act and state law and be mindful of the prospect of waiving arbitration rights unintentionally by commencing litigation of a dispute involving an agreement with an arbitration clause.

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I. FACTS

Robyn Morgan ("Morgan") was employed at a Taco Bell franchise in Osceola, Iowa, owned by Sundance, Inc. ("Sundance").[1] Sundance owned and operated over 150 Taco Bell franchises around the country.[2] As part of Morgan's application for her position at Taco Bell, she signed an agreement requiring use of confidential and binding arbitration, as opposed to litigation, to resolve employment disputes.[3]

Despite the parties' arbitration agreement, Morgan commenced litigation against Sundance for alleged violations of the Fair Labor Standards Act.[4] Morgan asserted Sundance frequently violated the Fair Labor Standards

1. Morgan v. Sundance, Inc., No. 4:18-cv-00316, 2019 WL 5089205, at *1 (S.D. Iowa June 28, 2019).
2. *Id.*
3. Morgan v. Sundance, Inc., 142 S. Ct. 1708, 1711 (2022).
4. *Id.*

Act by falsely recording hours so employees did not receive overtime pay.[5] Instead of asserting its right to arbitrate the employment dispute, Sundance defended against Morgan's suit by moving to dismiss.[6] After Sundance's motion to dismiss was denied, Sundance answered Morgan's complaint by asserting fourteen affirmative defenses, none of which mentioned the arbitration agreement.[7] The parties participated in mediation, but the suit failed to settle.[8]

Almost eight months after Morgan filed suit, Sundance moved to stay the litigation and compel arbitration under sections 3[9] and 4[10] of the Federal Arbitration Act ("FAA").[11] Morgan argued Sundance had waived its right to arbitrate by litigating for such a significant length of time before asserting its right to arbitrate the employment dispute.[12] The district court denied Sundance's motion to compel arbitration and dismiss the complaint, finding Sundance knew of the existence of the arbitration agreement, acted inconsistently with its right to arbitrate, and prejudiced Morgan by its inconsistent acts.[13] The district court found Sundance prejudiced Morgan by causing delay and wasting Morgan's effort.[14]

Sundance appealed the district court's order denying its motion to compel arbitration and dismiss the complaint.[15] The Eighth Circuit Court of Appeals applied the same three element test as the district court, but found there was no showing that Morgan was prejudiced by Sundance's acts because discovery was not conducted, four months of the eight month delay were spent awaiting the disposition of Sundance's motion to dismiss, and there was no evidence in the record that Morgan would have to "duplicate

5. *Id.*
6. *Id.*
7. *Id.*
8. *Id.*
9. 9 U.S.C. § 3 ("If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.").
10. 9 U.S.C. § 4 ("A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement.").
11. *Morgan*, 142 S. Ct. at 1711.
12. *Id.*
13. Morgan v. Sundance, Inc., No. 4:18-cv-00316, 2019 WL 5089205, at *5-8 (S.D. Iowa June 28, 2019).
14. *Id.* at *8.
15. Morgan v. Sundance, Inc., 992 F.3d 711, 713 (8th Cir. 2021).

her efforts."[16] Thus, the Eighth Circuit reversed and remanded the case to the district court.[17]

The U.S. Supreme Court granted certiorari to resolve the split among circuits as to the requirement of prejudice for waiver of arbitration rights.[18] The Court vacated the judgment of the Eighth Circuit and *held* prejudice is not required to find a party waived its right to stay litigation or compel arbitration under the FAA.[19]

II. LEGAL BACKGROUND

A. ARBITRATION IN GENERAL

Arbitration is a form of alternative dispute resolution which employs a neutral third party as decision maker as opposed to a judiciary.[20] Parties may agree to use arbitration to resolve disputes by including an arbitration clause in their contract; thus, parties cannot be forced to arbitrate a dispute they did not previously agree to arbitrate.[21] Parties may agree to specific arbitration terms "to allow for efficient, streamlined procedures tailored to the type of dispute. It can be specified, for example, that the decisionmaker be a specialist in the relevant field, or that proceedings be kept confidential to protect trade secrets."[22] Additionally, parties may agree to arbitration to reduce costs and delay in resolutions of disputes.[23]

B. THE FEDERAL ARBITRATION ACT'S PURPOSE AND SCOPE

The FAA was enacted by Congress in 1925[24] as "a response to hostility of American courts to the enforcement of arbitration agreements."[25] In enacting the FAA, Congress "intended courts to 'enforce [arbitration]

16. *Id.* at 715.

17. *Id.*

18. Morgan v. Sundance, Inc., 142 S. Ct. 1708, 1711 (2022).

19. *Id.* at 1714.

20. Thomas H. Oehmke, *Alternative Dispute Resolution: Commercial Arbitration*, 44 AM. JUR. TRIALS 507, § 1 (1992).

21. *See* Granite Rock Co. v. International Brotherhood of Teamsters, 561 U.S. 287, 297 (2010) ("[A] court may order arbitration of a particular dispute only where the court is satisfied that the parties agreed to arbitrate *that dispute*.").

22. AT&T Mobility LLC v. Concepcion, 563 U.S. 333, 344-45 (2011).

23. *Id.; see also* Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 628 (1985) ("[In agreeing to arbitration, a party] trades the procedures and opportunity for review of the courtroom for the simplicity, informality, and expedition of arbitration.").

24. Federal Arbitration Act, ch. 212, 43 Stat. 883 (1925) (codified at 9 U.S.C. §§ 1-16).

25. Cir. City Stores, Inc. v. Adams, 532 U.S. 105, 111 (2001); *see also* Karon A. Sasser, *Freedom to Contract for Expanded Judicial Review in Arbitration Agreements*, 31 CUMB. L. REV. 337, 340-46 (2001) (explaining the legal history of arbitration and the judicial interpretation of the FAA and its purpose).

agreements into which parties had entered,' and to 'place such agreements upon the same footing as other contracts.'"[26]

The FAA applies to contracts involving "any maritime transaction or a contract evidencing a transaction involving commerce."[27] The U.S. Supreme Court has interpreted the FAA's applicability to transactions involving commerce as broader than transactions "in commerce" and more analogous to transactions "affecting commerce," which is the broadest exercise of Congress' Commerce Clause Powers.[28] This broad interpretation of the FAA's applicability has led the U.S. Supreme Court to apply the FAA to transactions "involv[ing] interstate commerce, even if the parties did not contemplate an interstate commerce connection."[29] For instance, the Court determined that loans used to engage in business outside of the state of Alabama and to purchase inventory constructed outside the state of Alabama supported a finding that the agreements involved interstate commerce even though the agreements were executed in Alabama by Alabama residents.[30] Further, a ramp supervisor who trained, managed, and occasionally assisted agents in loading and unloading cargo from airplanes was found to belong to a class of workers engaged in interstate commerce.[31] Ultimately, the FAA is broad in scope and may apply even when an agreement's connection to interstate commerce is not substantial.[32]

C. SUBJECT MATTER JURISDICTION FOR FEDERAL ARBITRATION ACT CLAIMS

While the FAA is considered a body of federal substantive law which gives parties rights to seek to compel, confirm, vacate, or modify arbitral awards, the FAA itself "does not create any independent federal-question jurisdiction under 28 U.S.C. § 1331 or otherwise."[33] Thus, diversity

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26. Allied-Bruce Terminix Co. v. Dobson, 513 U.S. 265, 271 (1995) (quoting Volt Info. Sci., Inc., v. Bd. of Tr. Of Leland Stanford Junior Univ., 489 U.S. 468, 474 (1989)); *see also* Jodi Wilson, *How the Supreme Court Thwarted the Purpose of the Federal Arbitration Act,* 63 CASE W. RES. L. REV. 91, 98-102 (2012) (discussing the history of judicial hostility towards arbitration agreements); Charles Newton Hulvey, *Arbitration of Commercial Disputes*, 15 VA. L. REV. 238, 333-37 (1929) (detailing the history of non-binding arbitration in the United States); 7 PHILIP L. BRUNER & PATRICK J. O'CONNOR, JR., HISTORICAL DEVELOPMENT OF ARBITRATION—FROM PARIAH TO PRINCE § 21:2 (2022) (tracing the development of arbitration from before biblical times to the twentieth century).

27. 9 U.S.C. § 2.

28. *See* Citizens Bank v. Alafabco, Inc., 539 U.S. 52, 56 (2003) (citing *Allied-Bruce Terminix Co*., 513 U.S. at 273-74).

29. *Allied-Bruce Terminix Co*., 513 U.S. at 281.

30. *Citizens Bank*, 539 U.S. at 57.

31. Sw. Airlines Co. v. Saxon, 142 S. Ct. 1783, 1793 (2022).

32. Terry L. Trantina, *What Law Applies to an Agreement to Arbitrate?*, DISP. RESOL. MAG., Oct. 1, 2015, at 29, 30.

33. Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 25 n.32 (1983); *see* Badgerow v. Walters, 142 S. Ct. 1310, 1316 (2022).

jurisdiction or some other basis for independent jurisdiction must exist for a federal court to have subject matter jurisdiction of an FAA claim.[34] Generally, this means a party must show federal subject matter jurisdiction exists outside of the substantive rights granted by the FAA in order to bring a claim under the FAA in federal court.[35] Otherwise, the claim must be brought in state court.[36]

Addressing the constitutionality of diversity jurisdiction being used to bring FAA claims in federal court, the U.S. Supreme Court decided the FAA applies in diversity cases because Congress so intended.[37] This rule applies despite certain provisions of the FAA frequently amounting to substantive matters of law, even though the Court's holding in *Erie R.R. Co. v. Tompkins*[38] requires federal courts in diversity jurisdiction cases to apply state law to substantive matters.[39] Since "Congress may prescribe how federal courts are to conduct themselves with respect to subject matter over which Congress plainly has power to legislate," and the FAA "is based upon and confined to the incontestable federal foundations of 'control over interstate commerce and over admiralty,'" the U.S. Supreme Court has decided the FAA applies in federal diversity jurisdiction cases.[40]

Further, the U.S. Supreme Court has determined, with respect to an action seeking to compel arbitration under section 4 of the FAA, a federal court has subject matter jurisdiction if the underlying dispute between the parties presents a federal question.[41] However, this "look-through" approach

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34. *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 25 n.32.

35. *Badgerow*, 142 S. Ct. at 1316.

36. *Id.*

37. *See* Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395, 404-05 (1967); *see also* Allied-Bruce Terminix Co. v. Dobson, 513 U.S. 265, 271 (1995).

38. 304 U.S. 64, 71–80 (1938).

39. *Erie,* 304 U.S. at 71–80; *Prima Paint*, 388 U.S. at 404-05; *see also Allied-Bruce Terminix Co.*, 513 U.S. at 271.

40. *Allied-Bruce Terminix Co.*, 513 U.S. at 271 (quoting *Prima Paint*, 388 U.S. at 405).

41. Vaden v. Discover Bank, 556 U.S. 49, 53 (2009) ("A federal court may 'look through' a § 4 petition and order arbitration if, "save for [the arbitration] agreement," the court would have jurisdiction over 'the [substantive] controversy between the parties.'") (alteration in original).

does not apply when a party seeks to confirm or vacate an arbitral award under sections 9[42] or 10[43] of the FAA.[44]

Thus, while the FAA itself does not confer subject matter jurisdiction upon federal courts, claims arising under the rights afforded by the FAA may be brought in federal court if federal diversity jurisdiction is present, or, in actions seeking to compel arbitration under section 4 of the FAA, if the underlying dispute gives rise to federal question jurisdiction. FAA claims that do not satisfy federal subject matter jurisdiction must be brought in state court.[45]

D. The Prejudice Requirement

Section 2 of the FAA provides that "[a] written provision in any maritime transaction or a contract evidencing a transaction involving commerce . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."[46] The U.S. Supreme Court interpreted section 2 of the FAA as "a congressional declaration of a liberal federal policy favoring arbitration agreements."[47] This "policy favoring arbitration" eventually led nine federal circuits to adopt a requirement that prejudice be shown in the context of waiver of arbitration, despite no requirement of showing prejudice for waiver of other contractual rights.[48]

The Eighth Circuit, part of the previous majority of circuits, has, for decades, applied a three-part test[49] to determine whether a party waived its right to arbitration.[50] This test includes whether a party knew of its right to arbitrate, whether that party acted inconsistently with its right to arbitrate, and whether that inconsistency caused prejudice to the other party.[51] The

42. 9 U.S.C. § 9 ("If the parties in their agreement have agreed that a judgment of the court shall be entered upon the award made pursuant to the arbitration, and shall specify the court, then at any time within one year after the award is made any party to the arbitration may apply to the court so specified for an order confirming the award, and thereupon the court must grant such an order unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title. If no court is specified in the agreement of the parties, then such application may be made to the United States court in and for the district within which such award was made.").

43. 9 U.S.C. § 10(a) (allowing the federal district court in the district where the arbitral award was made to, upon application by one of the parties, vacate the award in the case of fraud, corruption, prejudicial misconduct, or the arbitrator exceeding its powers); 9 U.S.C. § 10(b) ("If an award is vacated and the time within which the agreement required the award to be made has not expired, the court may, in its discretion, direct a rehearing by the arbitrators.").

44. Badgerow v. Walters, 142 S. Ct. 1310, 1314 (2022).

45. *See id.*

46. 9 U.S.C. § 2.

47. Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983).

48. Morgan v. Sundance, Inc., 142 S. Ct. 1708, 1712 (2022).

49. *E.g.,* Fisher v. A.G. Becker Paribas Inc., 791 F.2d 691, 694 (9th Cir. 1986).

50. Stifel, Nicolaus & Co. v. Freeman, 924 F.2d 157, 158 (8th Cir. 1991).

51. *Id.*

element of prejudice was determined on a case-by-case basis, but could be shown by "lost evidence, duplication of efforts, use of discovery methods unavailable in arbitration, or litigation of substantial issues going to the merits[;] [a]dditionally, a party's failure to assert a prelitigation demand for arbitration may [also] contribute to a finding of prejudice because the other party has no notice of intent to arbitrate."[52] Nevertheless, "[d]elay in seeking to compel arbitration does not itself constitute prejudice."[53]

While the majority of circuits adopted a requirement of showing prejudice for waiver of arbitration, two circuits never did. The Seventh Circuit instead found prejudice to be "but one relevant circumstance to consider in determining whether a party has waived its right to arbitrate."[54] The District of Columbia Circuit Court also declined to adopt a requirement of prejudice for waiver of arbitration rights.[55] The D.C. District Court found a party did not waive arbitration rights when the defendant answered a complaint requesting arbitration as well as asserting defenses and counterclaims.[56] Further, that court also found a party did not waive the right to arbitrate even after litigation had been initiated.[57] Thus, the Seventh Circuit and the D.C. Circuit never went so far as to require a showing of prejudice to support the finding that a party waived its right to arbitration.

E. STATE ARBITRATION LAW

The Uniform Arbitration Act ("UAA") was promulgated in 1955 and last revised in 2000 by the Uniform Law Commission.[58] Thirty-five states have adopted either the UAA or the revised UAA ("RUAA").[59] The UAA "allows parties to agree to arbitrate a dispute before an actual dispute arises, which reverses the common law rule; and [] provides some basic procedures for the conduct of an arbitration."[60] The main goal of the RUAA "is to

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52. *Id.* at 159 (citations omitted).

53. *Id.* (citing Rush v. Oppenheimer & Co., 779 F.2d 885, 887 (2d. Cir. 1985)).

54. St. Mary's Med. Ctr. v. Disco Aluminum Prod. Co., 969 F.2d 585, 590 (7th Cir. 1992).

55. Nat'l Found. for Cancer Rsch. v. A.G. Edwards & Sons, Inc., 821 F.2d 772, 777 (D.C. Cir. 1987).

56. *See* Partridge v. Am. Hosp. Mgmt. Co., 289 F. Supp. 3d 1, 17 (D.D.C. 2017); Gordon–Maizel Constr. Co. v. Leroy Prods., Inc., 658 F.Supp. 528, 531 (D.D.C. 1987).

57. *See* Davis Corp. v. Interior Steel Equip. Co., 669 F.Supp. 32, 33–34 (D.D.C. 1987).

58. UNIF. ARB. ACT (amended 2000), prefatory note (UNIF. L. COMM'N 1955).

59. *Id.*

60. *Act Summary Tab*, UNIF. LAW COMM'N, https://www.uniformlaws.org/committees/community-home?communitykey=a0ad71d6-085f-4648-857a-e9e893ae2736 (last visited Nov. 14, 2022).

advance arbitration as a desirable alternative to litigation, but not to make arbitration simply another form of litigation."[61]

1. Arbitration Law in North Dakota

In 1987, the North Dakota Legislature adopted the Uniform Arbitration Act ("the Act").[62] The North Dakota Legislature amended and recodified the Act in 2003.[63] The Act provides that "[a]n agreement contained in a record to submit to arbitration any existing or subsequent controversy arising between the parties to the agreement is valid, enforceable, and irrevocable except upon a ground that exists at law or in equity for the revocation of a contract."[64] The Act allows parties to waive certain requirements of the Act but does not establish what constitutes waiver of the right to arbitrate.[65]

The North Dakota Supreme Court previously followed Ninth Circuit precedent[66] and required a showing of prejudice for a waiver of arbitration in *David v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*[67] In *David*, the plaintiff asserted the defendant waived its right to arbitration since the defendant had already answered the complaint, counterclaimed, and participated in discovery.[68] The North Dakota Supreme Court disagreed with the plaintiff, noting "[m]ore is required than action inconsistent with the arbitration provision; prejudice to the party opposing arbitration must also be shown."[69] Finding no prejudice occurred, the North Dakota Supreme Court found the defendant had not waived its right to arbitrate.[70] Thus, the North Dakota Supreme Court has previously required a showing of prejudice for waiver of arbitration rights.

2. Arbitration Law in Other State Jurisdictions

States surrounding North Dakota have established case law regarding waiver of arbitration rights. Minnesota has clearly established "a finding of waiver . . . requires a showing of prejudice to the party opposing

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61. *Policy Statement Revised Uniform Arbitration Act (RUAA)*, UNIF. LAW COMM'N, https://www.uniformlaws.org/HigherLogic/System/Download DocumentFile.ashx?DocumentFileKey=19b56af2-0289-2569-dd71-0ffc92eafd6a& forceDialog=0 (last visited Nov. 15, 2022).

62. *See* Uniform Arbitration Act, 1987 N.D. Laws 998.

63. *See* Uniform Arbitration Act, 2003 N.D. Laws 7 (codified at N.D. CENT. CODE § 32-29.3).

64. N.D. CENT. CODE § 32-29.3-06 (2022).

65. *See* N.D. CENT. CODE § 32-29.3-04 (2022).

66. Lake Commc'ns., Inc. v. ICC Corp., 738 F.2d 1473 (9th Cir. 1984), *abrogated by* Nghiem v. NEC Elec., Inc., 25 F.3d 1437, 1442 (9th Cir. 1994).

67. David v. Merrill Lynch, Pierce, Fenner & Smith, Inc, 440 N.W.2d 269, 274 (N.D. 1989).

68. *Id.*

69. *Id.* (citing *Lake Commc'ns Inc.*, 738 F.2d at 1477).

70. *Id.* at 275.

arbitration."[71] South Dakota requires a finding of waiver to include "prejudice to the party claiming waiver."[72] Finally, Montana requires "prejudice to the party resisting arbitration."[73] Thus, the jurisdictions surrounding North Dakota overwhelmingly require a finding of prejudice for waiver of arbitration pursuant to state law.

F. INTERACTION BETWEEN THE FEDERAL ARBITRATION ACT AND STATE ARBITRATION LAW

The FAA has been interpreted broadly and preempts conflicting state arbitration law pursuant to the Supremacy Clause of the United States Constitution.[74] The FAA has also been interpreted to preempt state law where the state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."[75] Those purposes and objectives are "enforcement of private agreements and encouragement of efficient and speedy dispute resolution."[76] In 1984, the U.S. Supreme Court clarified that the FAA applies in state courts as well as in federal courts [77] and has invariably reaffirmed that holding.[78] In fact, the U.S. Supreme Court has consistently recognized enforcement of the FAA is often times the task of state courts.[79] As explained above, when a federal court lacks subject matter jurisdiction to hear a case involving an arbitration dispute, the dispute must be heard in state court.[80]

Despite the FAA's broad application and preemptive effect, there are circumstances where state arbitration law is not preempted by the FAA. First, state law applies when the arbitration agreement is not part of a contract "affecting commerce" or maritime law.[81] Second, state arbitration law may apply when there is no applicable federal law.[82] Third, parties may agree to

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71. Stern 1011 First St. S., LLC v. Gere, 937 N.W.2d 173, 179 (Minn. Ct. App. 2020).

72. Rossi Fine Jewelers, Inc. v. Gunderson, 2002 SD 82, ¶ 9, 648 N.W.2d 812.

73. Stewart v. Covill & Basham Constr., LLC, 2003 MT 220, ¶ 8, 317 Mont. 153, 156 P.3d 1276.

74. Southland Corp. v. Keating, 465 U.S. 1, 10 (1984); *see* U.S. CONST. art. VI, cl. 2.

75. AT&T Mobility LLC v. Concepcion, 563 U.S. 333, 352 (2011) (quoting Hines v. Davidowitz, 312 U.S. 52, 67 (1941)).

76. *Id.* at 345 (quoting Dean Witter Reynolds, Inc. v. Byrd, 470 U.S. 213, 221 (1985)).

77. *Southland Corp.*, 465 U.S. at 15.

78. *See, e.g.*, Badgerow v. Walters, 142 S. Ct. 1310, 1316 (2022).

79. *See* Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 25 n.32 (1983); *see also* Vaden v. Discover Bank, 556 U.S. 49, 59 (2009) ("Given the substantive supremacy of the FAA, but the Act's nonjurisdictional cast, state courts have a prominent role to play as enforcers of agreements to arbitrate."); *Southland Corp.,* 465 U.S. at 15.

80. *See supra* Section II.C, SUBJECT MATTER JURISDICTION FOR FEDERAL ARBITRATION ACT CLAIMS.

81. 9 U.S.C. § 2; Citizens Bank v. Alafabco, Inc., 539 U.S. 52, 56 (2003).

82. UNIF. ARB. ACT, *supra* note 58, at 1.

apply state arbitration law.[83] In fact, the FAA does not prevent the use of state arbitration law to enforce agreements, even where the FAA would typically apply.[84] Thus, "parties may add portions of a state's arbitration law to the FAA's provisions or opt out of the FAA's provisions entirely."[85] However, "the state law principles invoked by the choice-of-law provision [must] not conflict with the FAA's prime directive that agreements to arbitrate be enforced."[86] Additionally, the U.S. Supreme Court has held a general choice of law clause selecting state law to apply to the contract as a whole, standing alone, is not enough to apply state law to arbitration agreements where the FAA would otherwise apply.[87] Thus, parties to a contract must clearly indicate the intent to circumvent the FAA and apply state arbitration law if so desired.

In sum, the goal of the FAA is to enforce arbitration agreements as other contracts are enforced.[88] The FAA is applied broadly in both federal and state courts.[89] FAA claims may end up in state court due to intention of the parties and federal subject matter jurisdiction issues.[90] Nevertheless, federal circuit courts and state courts have overwhelmingly agreed that the "federal policy favoring arbitration" requires a showing of prejudice for waiver of arbitration rights.[91] Despite this, the U.S. Supreme Court determined prejudice is not a prerequisite for waiver of arbitration rights.[92]

III. ANALYSIS

In *Morgan*, the U.S. Supreme Court unanimously held federal courts are not authorized to create rules specific to arbitration based upon the FAA's "policy favoring arbitration."[93] The U.S. Supreme Court based its decision upon its interpretation of the true meaning of "policy favoring arbitration" and the language of section 6 of the FAA.[94]

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83. Volt Info. Scis., Inc. v. Bd. of Tr. of Leland Stanford Junior Univ., 489 U.S. 468, 470 (1989).
84. *Id.* at 479.
85. Trantina, *supra* note 32 at 30.
86. UNIF. ARB. ACT, *supra* note 58, at 3.
87. Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52, 59-60 (1995).
88. *See* Allied-Bruce Terminix Co. v. Dobson, 513 U.S. 265, 271 (1995).
89. *See* Southland Corp. v. Keating, 465 U.S. 1, 12-16 (1984).
90. *See* Volt Info. Scis., Inc. v. Bd. of Tr. of Leland Stanford Junior Univ., 489 U.S. 468, 470 (1989); *see also supra* Part II.C. SUBJECT MATTER JURISDICTION FOR FEDERAL ARBITRATION ACT CLAIMS.
91. *See supra* notes 48, 67, 71-73.
92. Morgan v. Sundance, Inc., 142 S. Ct. 1708, 1714 (2022).
93. *Id.* at 1711.
94. *Id.* at 1713-14.

A. THE "POLICY FAVORING ARBITRATION"

The Court compared the standard waiver of a contractual right with the Eighth Circuit's requirement for waiver of the right to arbitration, finding waiver of the right to arbitration to be the only circumstance which requires a showing of prejudice.[95] Generally, waiver of a contractual right requires the "intentional relinquishment or abandonment of a known right."[96] To determine if waiver of a contractual right has occurred, courts typically look to the actions of the party who held the right, not to the effect those actions had on the other party.[97] Thus, prejudice is not typically a requirement for waiver of a contractual right.

However, based upon a Second Circuit decision, and eventually incorporated into the policy of FAA itself, "[t]here is . . . an overriding federal policy favoring arbitration."[98] In *Morgan*, the Court reiterated the federal policy favoring arbitration "is merely an acknowledgment of the FAA's commitment to overrule the judiciary's longstanding refusal to enforce agreements to arbitrate and to place such agreements upon the same footing as other contracts."[99] Thus, the federal policy favoring arbitration is meant "to make 'arbitration agreements as enforceable as other contracts, but not more so.'"[100] Therefore, the meaning of federal policy favoring arbitration does not support the requirement of a showing of prejudice for waiver of arbitration rights, since prejudice is not required in other contractual waiver contexts.[101]

B. PLAIN MEANING OF SECTION 6 OF THE FAA

Section 6 of the FAA provides all applications under the statute "shall be made and heard in the manner provided by law for the making and hearing of motions, except as otherwise herein expressly provided."[102] The Court in *Morgan* construed section 6 of the FAA to require the "usual federal procedural rules," thus making clear that arbitration specific rules are improper.[103] Since the usual federal rule for waiver of a contractual right does not require a showing of prejudice, the Court determined section 6 of the FAA supports that prejudice is not a required element for waiver of

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95. *Id.* at 1713.
96. United States v. Olano, 507 U.S. 725, 733 (1993) (quoting Johnson v. Zerbst, 304 U.S. 458, 464 (1938)).
97. *Morgan*, 142 S. Ct. at 1713.
98. *Id.* (quoting Carcich v. Rederie A/B Nordie, 389 F.2d 692, 696 (2d Cir. 1968)).
99. *Id.* (quoting Granite Rock Co. v. International Brotherhood of Teamsters, 561 U.S. 287, 302 (2010)).
100. *Id.* (quoting Prima Paint Corp. v. Flood & Conklin Mfg., 388 U.S. 395, 404, n.12 (1967)).
101. *Id.* at 1713-14.
102. 9 U.S.C. § 6.
103. *Morgan*, 142 S. Ct. at 1714.

arbitration rights.[104] Accordingly, a court may not develop unique rules favoring arbitration over litigation.[105]

IV. IMPACT

Morgan "expanded the circumstances under which a party may waive its right to demand arbitration" under the FAA.[106] By rejecting the previous majority rule among federal circuit courts, which required a showing of prejudice to waive the right to arbitration, the right to arbitrate is now easier for parties to unintentionally waive.[107] When prejudice of the opposing party was an element required for waiver of arbitration rights, a party who participated in litigation of a dispute in which the party had the right to arbitrate may have had the option to later correct their inadvertence by seeking arbitration.[108] If the other party was not prejudiced by commencement of litigation or other acts taken inconsistently with the right to arbitrate, the right to seek arbitration was left intact.[109] Now, parties may risk waiving arbitration rights by failing to promptly assert the right to arbitration.[110]

While the concern for a higher likelihood of unintentional waiver of arbitration rights is legitimate, even before *Morgan* the Eighth Circuit did not find waiver of arbitration rights based strictly upon passage of time, and it approached the analysis of waiver of arbitration on a case-by-case basis.[111] Additionally, the federal circuit courts that never adopted a requirement of prejudice for wavier of arbitration rights have followed the same case-by-

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104. *Id.*

105. *Id.*

106. Ryan Lawrence, *Waiving the Right to Arbitrate Becomes Easier*, MINN. LAW., (June 27, 2022), https://anthonyostlund.com/wp-content/uploads/2022/07/Anthony-Ostlund_Ryan_Lawrence-1.pdf.

107. *Id.*

108. *See, e.g.*, United States v. Williams Bldg. Co., 137 F. Supp. 3d 6, 11-13 (D. Mass. 2015) (allowing arbitration, due to lack of prejudice, because the party seeking arbitration only filed pleadings on the timelines required by the Federal Rules of Civil Procedure); Brownstone Inv. Grp. v. Levey, 514 F. Supp. 2d 536, 540-46 (S.D.N.Y. 2007) (finding no waiver after ten months of litigation and extensive discovery where the party seeking arbitration only defended against motions); Creative Telecomms., Inc. v. Breeden, 120 F. Supp. 2d 1225, 1232-36 (D. Haw. 1999) (finding no prejudice when one party moved for a stay to arbitrate eight months after filing the complaint and six months before trial).

109. *See, e.g.*, Rush v. Oppenheimer & Co., 779 F.2d 885, 887-90 (2d Cir. 1985) (finding the right to arbitrate remained despite the defendants' participating in discovery, service of an answer to the complaint, and an eight-month delay in pretrial proceedings).

110. *See* Partridge v. Am. Hosp. Mgmt. Co., 289 F. Supp. 3d 1, 18 (D.D.C. 2017) (finding defendants waived the right to arbitration because of substantial resources expended by the court and parties, despite defendants' timely invoking the right to arbitrate).

111. *See, e.g.*, Stifel, Nicolaus & Co. v. Freeman, 924 F.2d 157, 159 (8th Cir. 1991).

case analysis, seeing prejudice as merely a factor to consider.[112] Thus, while an inadvertent waiver of the right of arbitration may be more likely to occur after *Morgan*, waiver is unlikely to be based upon passage of time alone, and more likely to continue to be based upon a party acting inconsistent with its right to arbitration.

The *Morgan* decision creates a potential incentive for parties to contract around the FAA by showing a clear intention for state law to apply to arbitration agreements. Dependent upon the state law of the jurisdiction, contracting around the FAA may provide parties with what they may consider to be better protection – requiring a showing of prejudice for waiver of arbitration rights. As discussed, the right to arbitration is more easily waived after *Morgan* by inadvertence, negligence, or the like. If parties desire to maintain more protection against waiver of arbitration rights, they may be incentivized to require state law to apply to arbitration agreements where state law affords the requirement of a showing of prejudice.

Whether North Dakota and other nearby states will follow the federal courts and reject the requirement of a showing of prejudice for waiver of arbitration remains unanswered. The North Dakota Supreme Court previously followed Ninth Circuit precedent in requiring a showing of prejudice for waiver of arbitration.[113] Thus, the question becomes whether North Dakota will continue to follow the federal courts and, in turn, the new standard set by *Morgan*, or if North Dakota will maintain a requirement of prejudice for waiver of arbitration rights in future state law arbitration cases. For North Dakota practitioners, this query is significant as it is arguably unclear what standard the state of North Dakota may apply. Thus, practitioners in the state of North Dakota can protect clients' rights to arbitration by erring on the side of caution and assuming prejudice is no longer a requirement for the waiver of arbitration. Practitioners should counsel clients on the significance of due diligence in ensuring no waiver of arbitration will occur by commencing litigation or otherwise acting inconsistently with the right to arbitrate.

Additionally, understanding the current arbitration waiver laws in other state jurisdictions is important for practitioners who are licensed in multiple states. For example, practitioners in North Dakota who maintain licensure in

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112. *See, e.g.*, St. Mary's Med. Ctr. v. Disco Aluminum Prods. Co., 969 F.2d 585, 590 (7th Cir. 1992); *Partridge*, 289 F. Supp. 3d at 17 ("Courts assess, among other things, whether a party timely sought arbitration; whether the party now moving for arbitration engaged in litigation activity that induced the other party and 'the district court to expend time and effort on disputes, the resolution of which would not' move the dispute toward arbitration; and whether the party opposing arbitration would suffer prejudice from the movant's delay in seeking arbitration.") (quoting Zuckerman Spaeder, LLP v. Auffenberg, 646 F.3d 919, 923 (D.C. Cir. 2011)).

113. *See* David v. Merrill Lynch, Pierce, Fenner and Smith, Inc., 440 N.W.2d 269, 274 (N.D. 1989).

Minnesota should consider the differences among the FAA, North Dakota law, and Minnesota law for arbitration waiver.[114] Other state court decisions may also give guidance as to whether there will be a continued divide between the requirements for waiver of arbitration in state court and federal court, or if state courts will overwhelmingly decide to follow *Morgan*.[115]

V. CONCLUSION

In *Morgan*, the U.S. Supreme Court struck down the decades old majority rule of federal circuit courts which required a showing of prejudice for the waiver of arbitration rights under the FAA.[116] The FAA has broad application to all contracts affecting interstate commerce or maritime law and preempts any conflicting state law.[117] However, state arbitration law remains applicable to arbitration agreements not covered by the FAA and to arbitration agreements where the parties specifically intend for state law to apply.[118] Thus, in rectifying the federal circuit split on the matter of the requirements for waiver of arbitration, *Morgan* created a split between federal and state arbitration law in several jurisdictions. Whether states will elect to follow the *Morgan* decision and drop requirements of prejudice in the arbitration waiver context remains undetermined. Until state courts have the opportunity to decide whether to maintain prejudice requirements, practitioners must be aware of the differences in waiver standards between state and federal arbitration law. To ensure arbitration rights are not waived inadvertently, North Dakota citizens, companies, employees, practitioners, and others entering contracts involving arbitration agreements must not hesitate to exercise their right to arbitrate.

*AnneMarie Studer**

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114. *Compare* Morgan v. Sundance, Inc., 142 S. Ct. 1708, 1710-14 (2022) (holding no prejudice is required in federal courts), *with* Stern 1011 First St. S., LLC v. Gere, 937 N.W.2d 173, 179 (Minn. Ct. App. 2020) (requiring prejudice under Minnesota law), *and David*, 440 N.W.2d at 274 (requiring prejudice under North Dakota law).

115. Notably, the state of Texas has already declined to follow *Morgan*, requiring a showing of prejudice for waiver of arbitration in a state law case. *See* F.T. James Constr., Inc. v. Hotel Sancho Panza, LLC, No. 08-20-00096-CV, 2022 WL 4538870 (Tex. App. Sept. 28, 2022).

116. *Morgan*, 142 S. Ct. at 1714.

117. *See, e.g.*, Southland Corp. v. Keating, 465 U.S. 1, 10, 15-16 (1984).

118. Volt Info. Scis., Inc. v. Bd. of Tr. of Leland Stanford Junior Univ., 489 U.S. 468, 479 (1989).

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