Waiving or Forfeiting the Right to Arbitrate – Recent Cases Tackle Issue

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Increasingly, mandatory arbitration provisions are included in commercial agreements. After disputes arise, however, parties often claim that their adversary is no longer entitled to demand arbitration because of either forfeiture by reason of a failure to timely assert or waiver through intentional relinquishment or abandonment of this contractual right. In the arbitration context, the courts generally lump the two together under the rubric of "waiver."

Cases considering whether arbitration has been waived reflect how careful a party must be in seeking to preserve this right. Examples of this outcome are reflected in two recent federal cases.

Thus, the U.S. Court of Appeals for the Seventh Circuit decided that a debt collector had waived arbitration through "gratuitous delay" in *Smith v. GC Services Limited Partnership,* No. 18-1361, Oct. 22, 2018.

Smith involved a debt collection matter in which the debtor brought a class action against the collector alleging violations of the Fair Debt Collection Practices Act. The collector filed a motion to dismiss in August 2016 based, inter alia, upon the failure to state a claim. No mention was made of the arbitration agreement. Following the filing of an amended complaint, a second motion to dismiss was filed which again made no reference to the arbitration agreement. A discovery conference scheduled by a magistrate in February 2017 was held in March. After the conference, the collector for the first time demanded arbitration by letter which was refused by the debtor. In April 2017, the collector filed an answer and new matter to the amended complaint, but again did not mention the arbitration agreement.

In June 2017 the court denied the motion to dismiss. It was only in August 2017, 13 months after the commencement of the suit, that the collector formally moved to compel arbitration.

The Seventh Circuit noted that here there was no claim of an express waiver of the right to arbitrate; rather, the issue was whether there was a forfeiture of that right because "considering the totality of circumstances, a party acted inconsistently with the right to arbitrate."

The appellate court stated that there are many factors that "are relevant to this analysis, but diligence or lack thereof is particularly important" … "Did 'the party seeking arbitration … do all it could reasonably be expected to do to make the earliest feasible determination of whether to proceed judicially or by arbitration?'" To be included in this consideration is "whether the allegedly defaulting party participated in litigation, substantially delayed its request for arbitration or participated in discovery."

Here, the collector substantially delayed its request by not informally demanding arbitration until eight months after plaintiff had filed suit and "waited another five months before moving to compel." Moreover, "the company's actions were

manifestly inconsistent with an intention to arbitrate" in that it filed an answer and new matter to the amended complaint and supplemental briefs to the motions which contained no reference to arbitration. In addition, the appellate court appeared to be particularly disturbed by the failure of the collector to advise the district court of its letter demand for arbitration, unaccompanied by a motion to compel which, if granted, would have mooted the motions to dismiss.

Thus, the court states, waiver through delay alone can result even if prejudice has not been demonstrated.

Prejudice, however, is a relevant factor, even if there has not been significant delay. Thus, motions to dismiss based solely upon procedural or jurisdictional issues are generally not sufficiently prejudicial in that they do not seek a decision that resolves the dispute.

But prejudice is demonstrated when, as here, two motions to dismiss were based upon a failure to state a claim referencing a specific legal dispositive issue, as success by the defendant "ends the case just as surely as a judgment entered after a trial." In effect, submitting that basic substantive issue to the court and then, if unsuccessful, seeking to have it resolved at arbitration is essentially a "heads I win tails you lose "tactic with potential prejudice for the plaintiff and warrants a finding of waiver.

One month later, the Fifth Circuit was also confronted with the issue of arbitration waiver and reversed the district court which had found delay insufficient prejudice to warrant a finding of waiver in *Forby v. One Technologies (OT)* (17-10883, Nov. 28, 2018.

This class action, involving claims of deceptive practices and unjust enrichment in violation of Illinois law, was commenced in April 2015 in an Illinois state court. The matter was removed to the federal court in Illinois by *OT* without reference to arbitration. Thereafter, *OT* filed a motion to dismiss for failure to state a claim, and alternatively, to transfer to Texas on the grounds of forum non conveniens

as the agreement required arbitration in Texas. The case was transferred to Texas in March 2016.

In Texas, new counsel again filed a motion to dismiss for failure to state a claim and a reply brief, neither of which made mention of arbitration. On March 30, 2017, the Texas district court denied the motion to dismiss the Illinois claim as a matter of law but granted the motion to dismiss the unjust enrichment claim. Finally, on April 17, 2017, and only after a discovery conference and the filing by *Forby* of requests for production, did *OT* file a motion to compel arbitration. Eventually, on July 7, 2017, the district court granted *OT*'s motion and ordered arbitration, finding that *Forby* had suffered no prejudice notwithstanding the delay.

In reversing the district court, the appellate court noted two requirements for waiver in the Fifth Circuit: a party "substantially invokes the judicial process" and, causes detriment or prejudice to the adversary.

The appellate court agreed with the district court that *OT*'s "action of moving to dismiss *Forby's* claims with no mention of compelling arbitration demonstrated a desire to resolve the dispute in litigation rather than in arbitration." It had, in fact, invoked the judicial process notwithstanding that it was fully aware of the right to compel arbitration as reflected in its earlier motion in Illinois to transfer the matter to Texas.

But the appellate court disagreed with the district court's finding of insufficient evidence of prejudice, because the only prejudice was that of delay, "and delay alone is insufficient …".

While agreeing that delay alone will generally not result in a waiver, it may "along with other considerations, require a court to conclude that waiver has occurred." In this case, after the transfer to Texas, *OT* waited 13 months before moving to compel arbitration while attempting to obtain a dismissal with

prejudice from the district court. Indeed, it had obtained a partial dismissal with prejudice of *Forby's* claims relating to unjust enrichment.

The court recognized that not all motions to dismiss, such as those dealing with procedural or narrow ancillary issues, will result in such prejudice as to warrant a waiver because they do not reflect an attempt to seek a ruling on the merits. Sufficient prejudice will be found, however, when a party holds its right to demand arbitration in reserve while pursuing a court decision on the merits, and then, after not obtaining the desired ruling, attempts to relitigate the same issue by invoking arbitration. In effect, *Forby's* legal position was "damaged by *OT*'s delay in moving to compel arbitration."

These cases, and those from other circuits, reflect how courts at both the appellate and trial level have different perspectives on the issues of delay and prejudice as they relate to the waiver of arbitration. What does appear clear, however, is that a motion that invokes the judicial process by seeking a ruling that goes to the merits of the case (or, presumably, responds to it without also asserting the right to arbitrate), will usually result in a party's forfeiture of its right to insist on arbitration. Or, as a poet might say: "Neither wait nor litigate, if you wish to arbitrate." •

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