

# Class Action Monitor

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## Class Action Honors



## Use It or Lose It: SCOTUS Weighs in on Circuit Split, Holding Prejudice Is Not Required to Show Waiver of Arbitration Right

By Susan Shin, Pravin Patel, and Nicole Comparato

The existence of a valid agreement to arbitrate a dispute does not necessarily prevent a plaintiff from filing a lawsuit, nor does it stop a defendant from testing the waters and attempting to defeat such claims on a motion to dismiss. Nonetheless, the Supreme Court's recent decision in *Morgan v. Sundance, Inc.*, 142 S. Ct. 1708 (2022), should prompt defendants to think twice about wading into litigation at the risk of losing their right to arbitrate altogether.

On May 23, 2022, the Court resolved a longstanding circuit split regarding the issue of waiving the right to arbitration. For years, nine circuits—including the Eighth Circuit in *Sundance*—invoked the “strong federal policy favoring arbitration,” ruling that a party only waives its arbitration right by litigating the dispute **if** its conduct prejudiced the other side—thereby creating an arbitration-specific waiver rule (as prejudice is not normally considered for other waivers). The Supreme Court has now disagreed, siding with the other two circuits that decided an arbitration-specific rule is untenable because—in any other context—a federal court deciding whether a litigant waived a right does not ask if its actions caused harm. The Court has remanded *Sundance* for further proceedings, holding prejudice is not a factor in the waiver analysis.

## The District Court and Eighth Circuit Holdings in *Morgan v. Sundance*

Robyn Morgan worked as an hourly employee at one of defendant Sundance's Taco Bell franchises. Even though she signed an agreement to "use confidential binding arbitration, instead of going to court" to resolve any employment disputes, she later filed a nationwide collective action against Sundance in the District Court for the Southern District of Iowa for violations of the Fair Labor Standards Act, alleging Sundance flouted the Act's requirements to pay overtime wages. Rather than moving to compel arbitration, Sundance defended itself "as if no arbitration agreement existed." Sundance moved to dismiss the suit as duplicative of another collective action suit, answered the complaint after the district court denied its motion, and engaged in a joint mediation with the named plaintiffs in both collective actions. The other collective action suit settled, but Morgan's did not.

Eight months after Morgan filed suit, Sundance moved to stay the litigation and compel arbitration under Sections 3 and 4 of the Federal Arbitration Act ("FAA"). Morgan argued that Sundance waived its right to arbitrate by litigating for so long. Applying Eighth Circuit precedent, the District Court held that a party waives its contractual right to arbitration if it "knew of the right," "acted inconsistently with that right," and—most pertinent here—"prejudiced the other party by its inconsistent actions." The District Court found that the prejudice requirement had been satisfied, denying the motion to compel arbitration. On appeal, the Eighth Circuit reversed and remanded. The Eighth Circuit applied the prejudice requirement, but found it had not been satisfied, sending the case to arbitration because the parties had "not yet begun formal discovery" or contested any matters related to the merits. The Supreme Court granted **certiorari**.

## The Supreme Court's Decision Rejects Arbitration-Specific Procedural Rules

**The Supreme Court rejected an arbitration-specific** waiver rule that would demand a showing of prejudice and focused its opinion on "arbitration-specific variants of federal procedural rules" based on the "FAA's policy favoring arbitration." For waiver, the Court noted that the focus is on "the actions of the person who held the right" but that it "seldom considers the effects of those actions on the opposing party." The Court emphasized that the FAA's policy favoring arbitration does not "authorize federal courts to invent special, arbitration-preferring procedural rules." The Court highlighted that the policy intends to make arbitration agreements **as enforceable** as other agreements, not **more**.

Indeed, the Court outright rejected the creation of "novel rules to favor arbitration over litigation." The Court found that this rejection is supported in the text of the FAA itself, because Section 6 provides that federal courts treat arbitration applications "in the manner provided by law," or in other words, using the "usual" procedural rules. In this context, the Court held "Section 6 instructs that prejudice is not a condition of finding that a party, by litigating too long, waived its right to stay litigation or compel arbitration under the FAA."

The Court declined to make a ruling as to whether Sundance knowingly relinquished its right to arbitrate by acting inconsistently with that right, but remanded the case to the Court of Appeals to resolve that question.

## Key Takeaways

Particularly where a claim appears meritless, it may be tempting for a defendant to file a motion to dismiss or otherwise engage in the litigation only to get rid of it. This may be even more enticing when a defendant is facing a class action complaint, particularly in light of the Supreme Court's recent *Lamps Plus, Inc. v. Varela* decision, 139 S. Ct. 1407 (2019), which largely forecloses class-wide arbitration unless it is specifically provided for in the operative agreement. Perhaps, for example, a defendant may want to attempt to first resolve the claims on a class-wide basis in court, rather than deal with numerous individual arbitrations.

Yet, the *Sundance* decision demonstrates that this risk may not be worth it. Without the need for a plaintiff to show prejudice, under *Sundance*'s precedent, the plaintiff need only show that the defendant acted inconsistently with the right to arbitrate. It is a much lower bar to show that a defendant simply engaged in litigation than it is to show that engaging in that litigation wasted the plaintiff's time or resources.

The Court's decision also has further-reaching implications: defendants should be careful not to rely on the general policy favoring arbitration as a guarantee that they will eventually make it to arbitration. This decision shows that the Court is concerned with "arbitration-specific variants of federal procedural rules," meaning that waiver, forfeiture, and any other procedural bars normally available under the federal rules will not be affected by the policy favoring arbitration. Heeding this decision, parties should carefully consider the risks of engaging in a lawsuit filed by a plaintiff subject to an arbitration agreement, as compared to immediately seeking to compel arbitration.

Weil's leading class action practice will continue to monitor the evolution of case law on this issue for developments that may be relevant to our clients.

# About Weil's Class Action Practice

Weil offers an integrated, cross-disciplinary class action defense group comprising lawyers with expertise across our top-rated practices and hailing from our eight offices across the U.S.

Whether our clients face a nationwide class action in one court or statewide class actions in courts across the country, we develop tailored litigation strategies based on our clients' near- and long-term business objectives, and guided by our ability to exert leverage at all phases of the case – especially at trial. Our principal focus is to navigate our clients to the earliest possible favorable resolution, saving them time and money, while minimizing risk and allowing them to focus on what truly matters—their businesses.

For more information on Weil's class action practice please visit our [website](#).

## Class Action Honors (cont.)

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