Respondent not paying arbitration fees? Refusal may constitute waiver of right to arbitrate

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Arbitration can be very expensive. All major arbitration organizations charge fees for adjudicating a dispute, including initial filing fees, arbitrator fees and other variable fees that increase with the complexity and value of the dispute.

Arbitration proceedings that adjudicate disputes over multimillion-dollar agreements easily can incur seven-figure fees. Out of fairness, nearly all arbitration organizations' rules require both parties to share in those fees, absent language to the contrary in the parties' agreement. (*See, e.g.*, ICC Article 37 — Costs ("The advance on costs fixed by the Court pursuant to this Article 37(2) shall be payable in equal shares by the claimant and the respondent.")). But what happens when the respondent simply refuses to pay its share of fees after claimant has paid its share?

The Supreme Court of the United States recently weighed in on this issue, in part, in *Morgan v. Sundance, Inc*. (2022). The Supreme Court unanimously ruled that the Federal Arbitration Act (FAA) does not allow federal courts to invent special arbitration-preferring requirements, such as the need for a claimant to show it is prejudiced by a respondent's refusal to pay its fair share of arbitration fees before a court may find that a respondent has waived its contractual right to arbitration.

In the context of arbitration provisions, as with other contractual provisions, waiver is "the intentional relinquishment or abandonment of a known right."

Under the FAA, when a party to a contract containing an arbitration provision files a complaint in court, the court will normally stay or dismiss the proceedings and order the parties to arbitrate pursuant to their agreement. (*See* 9 U.S.C.A. § 3-4). When a respondent refuses to pay its share of arbitration fees, however, courts have held that there are two ways for the case to proceed in court: (1) the court may deny the defendant's motion to compel arbitration upon a finding that the defendant has *waived* its contractual right to arbitrate, or (2) the court may *lift the stay* on proceeding in court pursuant to Section 3 of the FAA. (*See* 9 U.S.C.A. § 3).

In the context of arbitration provisions, as with other contractual provisions, waiver is "the intentional relinquishment or abandonment of a known right." (*Morgan v. Sundance, Inc.* (2022)). Historically, to determine whether a party had waived its contractual right to arbitrate, courts applied a unique two-part test: "First, [they] decided if, under the totality of the circumstances, the party ha[d] acted inconsistently with the arbitration right, and, second, [they] look[ed] to see whether, by doing so, that party [had] in some way prejudiced the other party." (*Freeman v. SmartPay Leasing, LLC*, (11th Cir. 2019)).

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In *Morgan v. Sundance*, the Supreme Court partially abrogated this rule, declaring that a showing of prejudice was unnecessary for a finding of waiver of a contractual arbitration right, thereby directing courts to treat waiver of arbitration rights on the same footing as waiver of other contractual rights.

Nonetheless, even under the old test, numerous district courts have found that a defendant's refusal to pay requisite fees constitutes an act inconsistent with arbitration rights and amounts to a waiver. (*See Figueredo-Chavez v. RCI Hosp. Holdings, Inc.*, (S.D. Fla. Nov. 22, 2021) (citing *Freeman v. SmartPay Leasing, LLC*, (11th Cir. 2019)); *Mason v. Coastal Credit, LLC*, (M.D. Fla. Nov. 16, 2018); *Garcia v. Mason Cont. Prod., LLC*, (S.D. Fla. Aug. 18, 2010)).

Other district courts have found that a party's refusal to pay its share of arbitration fees constitutes a "default" under FAA Section 3. For example, in *Garcia v. Mason Contract Products* (S.D. Fla. Aug. 18, 2010), two parties contracted to have any contractual dispute arbitrated by AAA pursuant to the rules set by the same. After the defendant intentionally refused to pay its share of the arbitration fees — -which it was required to do pursuant to AAA rules — AAA permanently terminated the proceedings.

On a motion to lift the stay of federal court proceedings, the court found that defendant's refusal to pay constituted a default under

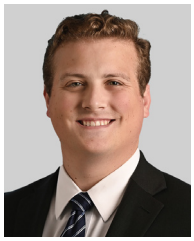
the FAA: "Plaintiff did not agree or assent to a AAA-like procedure; he agreed to a AAA-enforced procedure. Defendant's failure to comply with the contractual rules agreed to by the parties clearly constitutes a 'default' as that term is used in § 3 of the FAA."

In some cases, courts conclude that arbitration "has been had in accordance with the terms of the agreement" once an arbitration organization terminates proceedings after the respondent refuses to pay its requisite fees, and thereby nullifies the FAA's requirement for district courts to stay litigation. For example, the 10th U.S. Circuit Court of Appeals, in *Pre-Paid Legal Services v. Cahill* (10th Cir. 2015), found that lifting a stay of proceedings after dissolution of arbitration due to a defendant's refusal to pay "had gone as far as it could due to [defendant's] refusal to pay the fees" and, therefore, "arbitration had been had in accordance with the terms of the agreement."

Interestingly, the 10th Circuit found that the District Court's decision to lift the stay was *alternatively permissible* because the defendant's refusal to pay also constituted "default" under FAA Section 3.

These holdings are consistent with the trend of Supreme Court precedent that has curbed the undue deference afforded to arbitration over litigation. As the Supreme Court explained in *Morgan v. Sundance Inc.*: "If an ordinary procedural rule — whether of waiver or forfeiture or what-have-you — would counsel against enforcement of an arbitration contract, then so be it. The federal policy is about treating arbitration contracts like all others, not about fostering arbitration."

About the authors



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