AMERICAN BANKRUPTCY INSTITUTE

2019 Alexander L. Paskay Memorial Bankruptcy Seminar

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Lynn Welter Sherman
Adams and Reese LLP; Tampa

Student Researcher
Patrick Seidensticker
pseidensticker@law.stetson.edu

2019

43rd Annual Alexander L. Paskay Memorial Bankruptcy Seminar

ENFORCEMENT OF ARBITRATION CLAUSES FOR BANKRUPTCY DISPUTES

By: Courtney McCormick and Anna Haugen
McGuireWoods LLP

I. LIBERAL POLICY FAVORING ARBITRATION

A. In response to a widespread judicial hostility to arbitration agreements, Congress enacted the Federal Arbitration Act ("FAA") in 1925.

B. For decades, the Supreme Court has emphasized the strong federal policy favoring arbitration under the FAA. *See Epic Systems Corp. v. Lewis*, --- U.S. --- 138 S.Ct. 1612, 1621 (2018); *CompuCredit Corp. v. Greenwood*, 565 U.S. 95, 98, 132 S.Ct. 665, 669, 181 L.Ed.2d 586 (2012); *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 345–46, 352, 131 S.Ct. 1740, 1749–50, 1753, 179 L.Ed.2d 742 (2011); *Rent-A-Center, West, Inc. v. Jackson*, 561 U.S. 63, 67–73, 130 S.Ct. 2772, 2776–2880, 177 L.Ed.2d 403 (2010); *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26, 111 S.Ct. 1647, 1652, 114 L.Ed.2d 26 (1991); *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24, 103 S.Ct. 927, 941, 74 L.Ed.2d 765 (1983)

i) "[A]ny doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration," *Moses*, 460 U.S. at 24–25.

II. ENFORCEMENT OF ARBITRATION AGREEMENTS IN BANKRUPTCY

A. **Non-Core Proceedings**

i) "In general, bankruptcy courts do not have the discretion to decline to enforce an arbitration agreement relating to a non-core proceeding." *Whiting-Turner Contracting Co. v. Elec. Mach. Enter.'s Inc*., 479 F.3d 791, 796 (11th Cir. 2007); *see also In re Mintze*, 434 F.3d 222, 230 (3rd Cir. 2006); *In re Bateman*, 585 B.R. 618, 629 (Bankr. M.D. Fla. 2018).

a) *See also Meininger v. Discover Products, Inc., (In re Paulk)*, Adv. P. No. 8:18-00366-RCT (Bankr. M.D. Fla.) (Judge Colton recently compelled arbitration of FCCPA and TCPA claims, noting she lacked discretion on determining whether to compel arbitration.).

B. **Core Proceedings**

i) With respect to "core" bankruptcy matters, the Eleventh Circuit has "left the door open" and gives courts discretion on whether to compel arbitration. *In re Bateman*, 585 B.R. at 629 (citing *Whiting–Turner*, 479 F.3d at 796).

ii) The "Contrary Congressional Command"/*Shearson* Standard.

a) The FAA's mandate for arbitration may be overridden only by a "contrary congressional command." *Whiting-Turner*, 479 F.3d at 796 (citing *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 226, 107 S.Ct. 2332, 2337, 96 L.Ed.2d 185 (1987)).

1. To determine congressional intent, the Supreme Court in *Shearson* directed courts to look to three factors: (1) the text of the statute; (2) its legislative history; and (3) whether "an inherent conflict between arbitration and the underlying purposes [of the statute]" exists. *Shearson*, 482 U.S. at 227.

2. As for the Bankruptcy Code, the Eleventh Circuit already has found "no evidence within the text or in the legislative history that Congress intended to create an exception to the FAA in the Bankruptcy Code." *Whiting-Turner*, 479 F.3d at 796.

b) **The Third *Shearson* Factor: Whether an Inherent Conflict Exists between the FAA and the Bankruptcy Code**?

1. Compelling arbitration of contract disputes in bankruptcy, even those that are "core," typically do not inherently conflict with the Bankruptcy Code. *See In re Shores of Panama, Inc.*, 387 B.R. 864 (Bankr. N.D. Fla. 2008) (Killian, J.); *Whiting-Turner*, 479 F.3d at 796-97; *Carn v. Wall & Associates* (*In re Tomberlin),* Adv. P. No. 16-01115, 2017 WL 410337, at *4 (Bankr. M.D. Ala. Jan. 30, 2017); *In re Cardali*, No. 10–11185 SHL, 2010 WL 4791801, at *7 (Bankr. S.D.N.Y. Nov. 18, 2010).

2. In cases involving substantive rights created by the Bankruptcy Code, getting around the inherent conflict inquiry is more difficult.

a. For discharge violation claims, Judge Kimball found that no inherent conflict existed between compelling arbitration of those claims and the Bankruptcy Code. *See In re Williams*, 564 B.R. 770 , 775 (Bankr. S.D. Fla 2017) (finding that arbitration of the dispute was aligned with the federal policy favoring arbitration, and would not interfere with or affect the distribution of the estate).

1. Addressing the same issue (discharge violation claims), Judge Colton disagreed with Judge Kimball, finding an inherent conflict did exist as it undermines the bankruptcy court's authority to enforce its orders and exercise its contempt power. *In re Bateman*, 585 B.R. at 629-30. [1]

2. Judge Kimball did address that issue in *Williams*, noting that the bankruptcy court was not asked "to interpret the provisions of the discharge order itself, but instead to interpret a federal statute incorporated into that order. Other federal and state courts routinely interpret federal statutes. Arbitration panels do as well." 564 B.R. at 783.

b. In compelling arbitration of claims involving automatic stay violations, the Second Circuit found no inherent conflict existed as: (i) the debtor's estate had been fully administered and resolution would have no effect on the estate; (ii) the class action nature of plaintiff's claims lacked a direct connection to the bankruptcy case; and (iii) determination of stay violations require interpretation of a statute, not an order of the bankruptcy court. *MBNA v. Hill*, 436 F.3d 104, 109-10 (2d Cir. 2006).

1. However, the Second Circuit recently found that an inherent conflict exists between compelling arbitration of discharge violation claims and the Bankruptcy Code, reasoning that the bankruptcy court alone possesses the power and unique expertise to enforce the discharge injunction. *In re Anderson*, 884 F.3d 382, 390 (2d Cir. 2018)

3. Other Circuit Cases

a. *Moses v. CashCall, Inc.*, 781 F.3d 63 (4th Cir. 2015) (declining to compel arbitration of a declaratory judgment claim which would adjudicate a proof of claim finding an inherent conflict with the

[1] Judge Colton's decision in *Bateman* is currently up on appeal. *See Verizon Wireless Pers. Commc'ns, LP v. Bateman*, No. 8:18-cv-01394-SDM (M.D. Fla.).

Bankruptcy Code as the dispute would directly impact claims against the estate and the plan for financial reorganization but no inerent conflict as to the state law damages claim, in which resolution would merely augment debtor's estate).

b. *Ackerman v. Eber (In re Eber)*, 687 F.3d 1123, 1132 (9th Cir. 2012) (declining to compel arbitration of issues closely intertwined with dischargeability).

c. *In re National Gypsum Co*., 118 F.3d 1056, 1070 (5th Cir. 1997) (declining to compel arbitration of, *inter alia*, discharge violation claims finding inherent conflict existed where complaint raised issues central to the confirmed Chapter 11 plan).

iii) Is the Inherent Conflict Inquiry Still Valid?

a) Three recent Supreme Court decisions, *Epic Systems*, *Italian Colors*, and *CompuCredit* all appear to indicate that the Supreme Court has moved away from the inherent conflict test. In all three cases, the Court only looked at the plain text and legislative history in determining if a contrary congressional command exists to exempt a statute from the FAA's mandate. *See Epic Systems*, 138 S. Ct. at 1624-26; *Am. Express Co.* v. *Italian Colors Rest*, 133 S. Ct. 2304, 2309–10 (2013); *CompuCredi*t, 565 U.S. at 104.

1. In *Blackburn v. Capital Transaction Group, Inc.*, No. 2:13-cv-98, 2014 U.S. Dist. LEXIS 30310, at *9-11 (E.D. Tenn. Mar. 10, 2014) the court rejected pre-*CompuCredit* decisions that had endorsed the inherent conflict inquiry, holding that "because the Bankruptcy Code is silent" on arbitration, the FAA "requires the arbitration agreement to be enforced according to its terms, and there is no need to apply an 'inherent conflict' test." 2014 U.S. Dist. LEXIS 30310, at *9-11.

2. In *Walthour v. Chipio Windshield Repair, LLC*, 745 F.3d 1326 (11th Cir. 2014), the Eleventh Circuit observed that "in every case the Supreme Court has considered involving a statutory right that does not explicitly preclude arbitration, it has upheld the application of the FAA." 745 F.3d at 1331.

b) In *Bateman*, Judge Colton, relying in part on the Second Circuit's decision in *Anderson*, rejected arguments that the inherent conflict inquiry is no longer valid. 585 B.R. at 629 However, *Anderson* did

not consider whether the inherent conflict inquiry remains valid as the defendant, Credit One, failed to raise the argument below and only raised it for the first time on appeal. 884 F.3d at 388.

C. Whether Bankruptcy Proceedings Fall Within Scope of Arbitration Provisions

i) In *Bateman*, in addition to finding an inherent conflict, Judge Colton found that the broad arbitration clause did not encompass discharge violation claims under Florida law. 584 B.R. at 626-27.

ii) The *Bateman* decision reflects a recent trend of courts relying on state law to find claims outside of the scope of arbitration agreements. *See Anderson v. Deere & Co.*, 393 Mont. 157, 161-63 (Mont. 2018); *Perez v. DirecTV*, 740 Fed.Appx. 560, 561 (9th Cir. 2018); *Pictet Overseas Inc. v. Helvetia Trust*, 905 F.3d 1183, 1190 (11th Cir. 2018); *Grand Summit Hotel Condo. United Owners' Assoc. v. L.B.O. Holding, Inc.*, 195 A.3d 514, 520 (N.H. 2018).

iii) However, the Third Circuit recently found that the question of scope is a federal question, not controlled by state law. *Century Indem. Co. v. Certain Underwriters at Lloyd's, London*, 584 F.3d 513, 524 (3rd Cir. 2018).