

FEDERAL COURT OF APPEAL ANNOUNCES REVIEW STANDARD APPLICABLE TO RULINGS ON MOTIONS TO STAY LAWSUITS PENDING ARBITRATION

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In a case of first impression at the federal appellate level, the First Circuit, in *Powershare, Inc. v. Syntel, Inc.*, 597 F.3d 10 (1st Cir. Mar. 1, 2010), held that the appropriate standard of review to be utilized by a District Judge when reviewing a Magistrate Judge's disposition of a motion to stay litigation pending the completion of a parallel arbitration proceeding is the clearly erroneous standard. The Court found that this standard was functionally equivalent to the *de novo* standard because the issue presented by the motion was a pure question of law.

A Summary of the Rulings

The facts of this case sound like the fact pattern of numerous cases in the federal court system. Two parties signed a contract that contained an arbitration provision, a dispute arose as to the performance of the contract, and one party sued the other, following which the defendant submitted an arbitration demand and filed a motion to compel arbitration and stay the lawsuit. Here, the Plaintiff countered by filing a motion to stay any arbitration, so that the lawsuit could continue as the sole venue for resolving the dispute.

The motions were referred to a Magistrate Judge, who denied the motion to compel arbitration, interpreting the arbitration provision such that arbitration was "optional" rather than mandatory, not foreclosing the right of the parties to sue in court. The disappointed party appealed the decision to the District Judge, who agreed with the decision of the Magistrate

Judge, stating that the Magistrate Judge's decision was "not clearly erroneous or contrary to law."

The First Circuit disagreed and reversed, finding that the arbitration provision provides for mandatory arbitration. Although the discussion of the interpretation of the arbitration provision is interesting, perhaps of greater interest, since it is an issue of first impression at the federal appellate level, is the discussion of the standard of review to be applied by a District Judge when reviewing a Magistrate Judge's disposition of a motion to stay a lawsuit pending arbitration.

The Characterization of the Motion Was Dispositive with Respect to the Review Standard

The determination of the appropriate standard of review depended upon the characterization of the motion as either a dispositive or non-dispositive motion. Federal Rule of Civil Procedure 72 sets out two different standards of review to be used by District Judges in reviewing the decisions of Magistrate Judges. Since Article III of the United States Constitution requires that District Judges exercise final decision authority in matters pending before them, when ruling on a dispositive motion, a Magistrate Judge may issue only a recommended decision which, absent a timely objection, ripens into an order. With respect to a non-dispositive motion, a Magistrate Judge may issue an order, which is subject to appeal to the District Judge.

Consistent with the concern that District Judges must exercise final decision authority, Rule 72 provides that in reviewing a Magistrate Judge's recommendation on a dispositive motion, a District Judge should engage in *de novo* review if there is a proper objection to the recommendation. Fed.R.Civ.Pro. 72(b). On the other hand, a District Judge may set aside the

ruling of a Magistrate Judge on a non-dispositive motion only if the ruling “is clearly erroneous or is contrary to law.” Fed.R.Civ.Pro. 72(a).

The issue presented in *Powershare* for the first time to a federal appellate court was whether motions to stay a lawsuit pending arbitration are dispositive or non-dispositive motions. Dispositive motions include those enumerated in 28 U.S.C. §636(b)(1)(A), “but this list is not exhaustive; rather, it simply ‘informs the classification of other motions as dispositive or nondispositive.’” 597 F.3d at 13. Motions to stay pending arbitration are not included in those listed in section 636(b)(1)(A).

The Court cited opinions from five district courts holding that motions to stay pending arbitration are non-dispositive motions, and one opinion holding that such motions are dispositive motions, because a ruling granting such a motion “has the practical effect of allowing the case to proceed in a different forum.” Disagreeing with that decision, the Court decided that such motions are non-dispositive because they “do not have the same character” as the motions listed in section 636(b)(1)(A), as they are not dispositive of either the case or of any claim or defense pleaded in the case. The Court stated that granting a stay pending arbitration “is merely suspensory,” with the district court retaining jurisdiction to dissolve the stay or to make orders with respect to any arbitral award. *Id.* at 14. Acknowledging that the scope of the judicial review of arbitral awards is narrow, the Court noted that such review does exist, and that the stay of a lawsuit pending arbitration does not amount to the final exercise of Article III power at the time that the district court acts on the motion to stay the lawsuit pending arbitration.

The Applicable Review Standard for Non-Dispositive Motions

The Court concluded that the Magistrate Judge's ruling was an order, not a recommendation, and that the District Judge acted appropriately in reviewing that decision under the "clearly erroneous or contrary to law" standard set forth in Rule 72(a). The Court further held that when the review of a ruling on a non-dispositive motion by a Magistrate Judge turns on a pure question of law, Rule 72(a) requires that the District Judge review the ruling (assuming that a proper objection is filed) under the "contrary to law" standard in the Rule, i.e., a *de novo* standard of review.

The Court held that nothing in the parties' contract expressly provided that an arbitrator would decide questions of arbitrability, and that since in this case the question of arbitrability depended on interpreting a contractual term, the motion presented a question of law. Therefore, the District Judge was required to review the decision of the Magistrate Judge using a *de novo* standard of review, because "for questions of law, there is no practical difference between review under Rule 72(b)'s 'contrary to law' standard and review under Rule 72(b)'s *de novo* standard." *Id.* at 15.

Finally, the Court noted that since it was reviewing the district court's decision of a purely legal question, its standard for review of the district court's decision also was a *de novo* standard.

The Arbitration Provision

In reviewing the district court's decision, the Court first grappled with the question of whether the federal policy favoring the arbitration of disputes resulted in a presumption in favor of arbitrability. Similar to the recent decision of the Third Circuit in *Century Indemnity*

Company v. Certain Underwriters at Lloyd's, London, 584 F.3d 513 (3d Cir. 2009), the Court declined to decide this issue, finding it unnecessary to do so since the plain language of the contract at issue “compelled” the decision that arbitration was required.

The arbitration provision provided that the parties “shall” submit disputes to arbitration, but also stated that “[n]othing in this clause shall prejudice Syntel or PowerShare’s right to seek injunctive relief or any other equitable/legal relief or remedies available under law.” The Court rejected the contention that this statement amounted to the reservation of a right to litigate rather than arbitrate disputes, finding that the plain reading of the word “shall” did not permit such an interpretation. Rather, the Court held that the only reasonable interpretation of the arbitration provision as a whole was that it mandated arbitration, but provided the arbitrator “broad legal and equitable powers” in awarding relief, including injunctive relief if deemed appropriate by the arbitrator.

Conclusion

Granting motions to stay lawsuits pending arbitration do not fully dispose of the lawsuit, or even of any claim or defense in the lawsuit, and the court retains jurisdiction to consider post-arbitration filings by the parties to confirm, vacate or modify the eventual arbitral award. To characterize such motions as dispositive would be improper. Since motions to stay lawsuits pending arbitration usually turn upon an interpretation of the contract containing the arbitration provision, the review standard for such motions will be the contrary to law or *de novo* standard.

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