

No. 10-514

In The
Supreme Court of the United States

STOK & ASSOCIATES, P.A.,

Petitioner,

v.

CITIBANK, N.A.,

Respondent.

**On Petition For A Writ Of Certiorari
To The United States Court Of Appeals
For The Eleventh Circuit**

**REPLY BRIEF FOR PETITIONER
STOK & ASSOCIATES, P.A.**

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ARGUMENT**A. There is an Undeniable Conflict Among the Circuits as to Whether a Party Must Demonstrate That it has Suffered Prejudice in Order to Establish That an Opposing Party Has Waived its Right to Arbitrate**

It is well-recognized that the United States Supreme Court is more likely to grant certiorari review when there is a split of authority among the circuits, as stated explicitly by Rule 10(a) of the Rules of the Supreme Court of the United States. See *Bingler v. Johnson*, 394 U.S. 741 (1969); *United States v. O'Malley*, 383 U.S. 627 (1966). The Respondent argues, in its Brief in Opposition to the Petitioner's Petition for Writ of Certiorari, that there is no split of authority amongst the circuits with respect to the requirement that a party must demonstrate that it has suffered prejudice when attempting to establish that the opposing party has waived its right to arbitrate. This assertion is blatantly incorrect.

The Circuit Courts of Appeals themselves have recognized that there is a cognizable and profound "circuit split" with respect to the prejudice requirement with three circuits (the Seventh Circuit, the Tenth Circuit, and the D.C. Circuit) which do not require a showing of prejudice while the remaining circuits do require a showing of prejudice to varying extents.

The Seventh Circuit is the primary proponent of the notion that prejudice need not be shown in a waiver analysis. "Where it is clear that a party has foregone its right to arbitrate, a court may find waiver even if that decision did not prejudice the non-defaulting party." *St. Mary's Medical Center of Evansville, Inc. v. Disco Aluminum Products Co., Inc.*, 969 F.2d 585, 590 (7th Cir. 1992). Judge Posner, after reiterating the Seventh Circuit's rule of decision in *Cabinetree of Wisconsin, Inc. v. Kraftmaid Cabinetry, Inc.*, 50 F.3d 388 (7th Cir. 1995), stated "*ours may be the minority position* but it is supported by the principal treatise on arbitration 2 Ian R. Macneil, Richard E. Speidel, & Thomas J. Stipanowich, *Federal Arbitration Law: Agreements, Awards, and Remedies under the Federal Arbitration Act* §21.3.3 (1994)."

Aligned with the Seventh Circuit, the District of Columbia Court of Appeal has announced that it holds an opinion on the issue of prejudice that differs markedly from the majority view. For example, in the case of *Khan v. Parsons Global Services, Ltd.*, 521 F.3d 421 (D.C. Cir. 2008), the Court stated that "[a] finding of prejudice is not necessary in order to conclude that a right to compel arbitration has been waived, although 'a court may consider prejudice to the objecting party as a relevant factor' in its waiver analysis." (emphasis added). Similarly, in the case of *National Foundation for Cancer Research v. A.G. Edwards & Sons, Inc.*, 821 F.2d 772 (D.C. Cir. 1987) the Court stated:

This circuit has never included prejudice as a separate and independent element of the showing necessary to demonstrate waiver of the right to arbitration. See Cornell, supra. We decline to adopt such a rule today. Of course, a court may consider prejudice to the objecting party as a relevant factor among the circumstances that the court examines in deciding whether the moving party has taken action inconsistent with the agreement to arbitrate. See, e.g., Dickinson v. Heinhold Securities, Inc., 661 F.2d 638, 641 & n. 5 (7th Cir. 1981); Reid Burton Construction, Inc. v. Carpenters District Council of Southern Colorado, 614 F.2d 698, 702 (10th Cir.), cert. denied, 449 U.S. 824, 101 S. Ct. 85, 66 L.Ed.2d 27 (1980). But waiver may be found absent a showing of prejudice.

(emphasis added).

The Respondent, in its Brief in Opposition, makes the argument that the distinction between the minority and majority views is more a distinction of degree rather than a "blackline" distinction. This is hardly the case. In the Circuit Courts of Appeals which hold the majority viewpoint, prejudice is absolutely required to demonstrate waiver. For example, the Fifth Circuit, perhaps the most "pro-prejudice" Circuit, has stated "[P]rejudice ... is the essence of waiver." *Joseph Chris Pers. Services Inc. v. Rossi*, 249 F. App'x. 988, 991 (5th Cir. 2007) (emphasis added) (quoting *Miller Brewing Co. v. Fort Worth Distrib. Co.*, 781 F.3d 494, 497 (5th Cir. 1986)); "The proper

test is whether participation in litigation *prejudiced the other party.*" *Cargill Ferrous Int'l v. Sea Phoenix MV*, 325 F.3d 695, 700 (5th Cir. 2003); "Waiver will be found when the party seeking arbitration substantially *invokes the judicial process to the detriment or prejudice of the other party.*" *Walker v. J.C. Bradford & Co.*, 938 F.2d 575, 577 (5th Cir. 1991).

Even though courts are duly bound to follow their own precedent on the prejudice issue, some have recognized the failings of such a position, and only do so with great reluctance. For instance in *Walker v. J.C. Bradford & Co.* (5th Cir. 1991) the court opined:

In general, we do not look kindly upon parties who use federal courts to advance their causes and then seek to finish their suits in the alternate fora that they could have proceeded to immediately. Such actions waste the time of both the courts and the opposing parties. The decision whether to arbitrate is one best made at the onset of the case, and not part way through as Bradford seeks today. The attempt of Bradford's attorney to switch judicial horses in midstream either shows poor judgment, if planned, or poor foresight, if not.

Even the Court's sharp rebuke in *Walker* presupposes a benign motive and not shrewd manipulation for strategic gains, an avenue which is rife for exploitation, where a party need show a special prejudice to avoid the disruption of its suit.

In the same vein as the Fifth Circuit, the Eleventh Circuit, the Circuit from which this instant petition arises holds to the jurisprudence that waiver of the right to arbitrate will never be found where a party is unable to demonstrate that it has been prejudiced by the opposing party's failure to timely demand arbitration. As a case on point, the court in *Morewitz v. W. of England Ship Owners Mut. Prot. & Indem. Ass'n (Luxembourg)*, 62 F.3d 1356, 1366 (11th Cir. 1995) stated:

Nevertheless, the doctrine of waiver is not an empty shell. Waiver occurs when a party seeking arbitration substantially participates in litigation to a point inconsistent with an intent to arbitrate *and this participation results in prejudice to the opposing party.* *Price v. Drexel Burnham Lambert, Inc.*, 791 F.2d 1156, 1158 (5th Cir. 1986).

(emphasis added).

In *Ivax Corp. v. B. Braun of Am., Inc.*, 286 F.3d 1309, 1315-16 (11th Cir. 2002), the court pronounced "[i]n determining whether a party has waived its right to arbitrate, we have established a two-part test. First, we decide if, 'under the totality of the circumstances,' the party 'has acted inconsistently with the arbitration right,' and, *second, we look to see whether, by doing so, that party 'has in some way prejudiced the other party.'* *S & H Contractors, Inc. v. A.J. Taft Coal Co.*, 906 F.2d 1507, 1514 (11th Cir. 1990)." (emphasis added).

A comparison litmus test demonstrates the above that the Respondent's position, that there is no real conflict between the circuits regarding the prejudice requirement, is simply not supported by the relevant authorities. The distinction between the circuits on this point is palpable, outcome determinative, and is not just a matter of semantics as Citibank argues in its Reply. There is no doubt that, had the litigation between the Petitioner and the Respondent taken place in the Seventh Circuit or the D.C. Circuit, where there is no required showing of special prejudice, Respondent's participation in the Florida state court litigation without raising its claimed right to arbitrate, clearly would have been construed as a waiver of that right and, therefore, the Petitioner would not be before this Court seeking relief.

B. There is a Conflict Between the Circuit Courts of Appeals and the Various States With Respect to the Prejudice Requirement

In addition to the ineluctable conflict between the various Circuit Courts of Appeals with respect to the prejudice requirement, there is a clear conflict of authority between the Circuit Courts of Appeals and the standards employed by the courts of the various states on the prejudice issue. For example, in the case at bar, the Petitioner instituted litigation in Florida state court. The Respondent answered the Petitioner's complaint, failing to raise the issue of arbitration. Under Florida state law, this alone, with no showing

of prejudice, was enough to constitute a waiver of the Respondent's right to demand arbitration. *Bared and Company, Inc. v. Specialty Maintenance and Construction, Inc.*, 610 So.2d 1, 3 (Fla. 2d DCA 1992); *Hansen v. Dean Witter Reynolds, Inc.*, 408 So.2d 658, 659 (Fla. 3d DCA 1981); *King v. Thompson & McKinnon Auchincloss Kohlneyer, Inc.*, 352 So.2d 1235, 1235 (Fla. 4th DCA 1977) (all holding that no prejudice is required to establish waiver of the right to arbitrate). A similar result would have arisen had the Petitioner instituted litigation in, for example, Arizona state court. *Bolo Corp. v. Homes & Son Const. Co.*, 464 P.2d 788, 790 (1970).

By comparison, had the same litigation been instituted by the Petitioner in other state court jurisdictions, the result would be very different. See *Saint Agnes Med. Ctr. v. PacificCare of California*, 82 P.3d 727, 738 (2003) (“[I]n California, whether or not litigation results in prejudice also is critical in waiver determinations”) (emphasis added); *Chandler v. Blue Cross Blue Shield of Utah*, 833 P.2d 356, 360 (Utah 1992) (“We therefore adopt the principle that waiver of a right of arbitration must be based on both a finding of participation in litigation to a point inconsistent with the intent to arbitrate *and a finding of prejudice.*”) (emphasis added). Thus, with respect to the prejudice requirement, there is both a disparity of authority among the various Circuit Courts of Appeals *and* between the highest courts of the various states. As discussed above, this disparity is not simply a difference without a distinction. The divergence

Citibank failed to address in their Reply because it is the very premise upon which they pursued litigation in the trial court to exploit the disparate treatment of the prejudice issue between the Florida State and the Federal Court of the Eleventh Circuit. Rather, the stance on the issues of waiver, arbitration, and prejudice that a particular jurisdiction may hold will, of course, govern the outcome of litigation instituted in that jurisdiction on that issue.

After this Court takes a stance on this matter, either for or against the special prejudice requirement, the state courts will be guided by this Court's rule of decision, eliminating not just the inconsistency between the various Circuit Courts of Appeals but between the state courts as well, resulting in a uniform application of the principle.

♦

C. The Position Taken by the Majority of the Circuit Courts of Appeals is Inconsistent with the Supreme Court's Own Precedent

Pursuant to Rule 10(c), Rules of the Supreme Court of the United States, the Supreme Court, when determining whether to grant a petition for writ of certiorari, is more likely to grant such a petition where the case in question involves a Circuit Court of Appeals which "has decided an important federal question in a way that conflicts with relevant decisions of this Court." To be sure the petition filed by the Petitioner involves such a case.

Originally, the Federal Arbitration Act (the "FAA") was passed by Congress to counteract the courts of the various states' longstanding judicial hostility toward enforcing contractual arbitration provisions. *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, (2001); *Harris v. Green Tree Fin. Corp.*, 183 F.3d 173, 178 (3d Cir. 1999). However, subsequently, this Court has taken pains to make its jurisprudence well defined. This Court has repeatedly held that the FAA was not intended to elevate agreements to arbitrate over other contractual agreements by ruling that the FAA was not intended to place the veritable "thumb" on the scale favoring arbitration. This Court, in the recent case of *Rent-A-Ctr., W., Inc. v. Jackson*, 130 S. Ct. 2772, 2776, (2010), has stated, with regard to the FAA, the following:

The FAA thereby places arbitration agreements on an equal footing with other contracts ... and requires courts to enforce them according to their terms. Like other contracts, however, they may be invalidated by "generally applicable contract defenses, such as fraud, duress, or unconscionability."

(internal citations omitted).

It is this Court's position that contracts to arbitrate should be treated in the same matter as other any contract. It stands to reason that, if any other contractual right can be waived by acting inconsistently with that right, so too can a contractual right to arbitrate be waived by acting inconsistently with that right. However, the judge-made requirement

that a party must show special prejudice beyond the prejudice of participating in an alternate forum, when asserting that a contractual counter-party has waived its right to arbitrate, exalts contracts to arbitrate outside of the contractual norm and thus places a thumb on the scale favoring contracts to arbitrate over other contractual rights. Hence, the special "prejudice requirement" of the majority position is squarely at odds with this Court's own precedent.

D. The Abolition of the Prejudice Requirement is Supported by the Principal Treatise on Arbitration

It is for good reason that the most authoritative treatise on the issue of arbitration, 2 Ian R. Macneil, Richard E. Speidel & Thomas J. Stipanowich, *Federal Arbitration Law: Agreements, Awards, and Remedies under the Federal Arbitration Act* §21.3.3 (1994), supports abolition of the special prejudice requirement. The fluidity of their logic is most persuasive:

As a matter of arbitration policy, the current judicial approach to waiver seems unsatisfactory. The requirement of prejudice, particularly in courts loathe to find prejudice, protects the federal contract right to arbitrate at considerable cost to efficiency. The current approach tends to encourage litigation of whether a waiver in fact occurred. It sometimes permits a party who has chosen to engage in litigation to stop, demand arbitration, and move to another forum. And it often permits a defending party to waste

much time and sometimes considerable effort by the other and even gain litigation advantage before demanding arbitration.

Present waiver doctrine thus allows a great deal of laxity in enforcing arbitration rights. All this appears to be the exact opposite of what parties desire when they agree to arbitrate – delay instead of speed, formality instead of informality, and complexity instead of simplicity. It is difficult to justify the present legal situation on the basis that it is implementing the much trumpeted pro-arbitration policy. On the contrary it seems to have the opposite effect.

In the short run, requiring diligence in enforcing arbitration rights rather than the present laxity would mean that some cases will have to be litigated to the end, rather than tossed to the arbitrators after the main benefits of arbitration may have been lost. In the long run it would have a beneficial effect on arbitration, because it would prevent parties from playing litigational games if they want to arbitrate.

After discussing the problems with which the current system is fraught, at least in the jurisdictions holding the majority viewpoint, Macneil, Speidel & Stipanowich suggest a solution based on the language of the FAA itself, which solution follows the viewpoint held by the minority of the Circuit Courts of Appeal:

A more sensible approach is provided by the language of FAA §§3 and 4. If, under either

section, a party is in "default" in proceeding to arbitration, the relief is denied. Default, in this context, should be defined to include both an unreasonable delay in demanding arbitration and the choice to initiate litigation or defend a lawsuit without insisting on a known right to arbitrate. In neither case would proof of prejudice be required. This approach would reduce the incentive to litigate over the content of prejudice and provide an incentive to make a timely decision to insist upon the right to arbitrate or not.

As Macneil, Speidel & Stipanowich note in this subsection of their treatise, the prejudice requirement has the practical effect of (i) elevating the contractual right to arbitrate over other contractual rights, (ii) encouraging litigation rather than discouraging litigation, (iii) wasting the resources of litigants and the judicial system as a whole, (iv) preventing the advantages of arbitration clauses from being realized, (v) thwarting any pro-arbitration policy which may exist, and (vi) encourages the employment of litigation "games" by those who seek tactical advantage over their opponents by exploiting the diverse positions on the subject as a litigation tactic. It only follows logically that the removal of the prejudice requirement will have the practical effect of ridding the judicial system of these ills and limiting the freedom of contract principles that this Court has repeatedly endorsed.

CONCLUSION

A few points should be obvious from the above discussion. Unlike the representation of the Respondent, there is an ineluctable and discernable conflict of authority between the Circuit Courts of Appeals with respect to the requirement that a litigant demonstrate special prejudice when seeking to establish that an opposing party has waived its right to arbitrate by, for example, participating in litigation in a non-arbitral forum. Not only is there such a conflict in the federal court system but this conflict extends to the state court system as well. Furthermore, the viewpoint of the majority of the Circuit Courts of Appeals, which circuits require a showing of prejudice, is in diametric conflict with the precedent of this Court because such a requirement raises contracts to arbitrate above all other agreements. Finally, the Petitioner's argument, that the prejudice requirement should be abolished, is supported by the leading academic treatise of the issue of arbitration. For all of these reasons, as well as those discussed at length in the

Petitioner's Petition, this Court should grant certiorari to the Petitioner.

Respectfully submitted,

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