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Supreme Court Reaffirms the Federal Arbitration Act's National Policy Favoring Arbitration

By Marcie B. Cornfield

In its Monday, November 26, 2012, ruling in *Nitro-Lift Technologies, L.L.C. v. Howard*, 568 U.S. __ (2012), the U.S. Supreme Court reiterated the "national policy favoring arbitration" that was created with the passing of the Federal Arbitration Act ("FAA"), and in the process demonstrated again both the applicability of the FAA in state courts and the importance to employers of drafting enforceable arbitration clauses in the first place.

The key issue in *Nitro-Lift* was whether the Oklahoma Supreme Court had the authority to ignore a contract's arbitration provision and determine whether the noncompetition agreements in two employment contracts were null and void under state law, rather than leaving that determination to the arbitrator in the first instance. Eddie Lee Howard and Shane Schneider were former employees of Nitro-Lift Technologies, L.L.C., which "contracts with operators of oil and gas wells to provide services that enhance production." Both Howard and Schneider entered into a confidentiality and noncompetition agreement with Nitro-Lift that contained an arbitration clause requiring that "any dispute, difference or unresolved question between Nitro-Lift" and the employees be resolved via arbitration.

Howard and Schneider eventually resigned from Nitro-Lift and went to work for a competitor. Nitro-Lift then served the two former employees with an arbitration demand, asserting that they had breached their respective noncompetition agreements. Howard and Schneider, however, did not agree to arbitrate the matter. Rather, they filed suit in Oklahoma state court, asking the court to enjoin enforcement of the noncompetes

and declare them null and void under Oklahoma state law. The state trial court refused to do so, ruling that the employment contracts contained legitimate arbitration clauses that required an arbitrator, and not the court, to settle the parties' dispute.

However, the Oklahoma Supreme Court retained the former employees' appeal and ordered the parties to show cause why the matter should not be resolved by application of Oklahoma state law governing noncompetition agreements. Nitro-Lift argued that any dispute as to the contracts' enforceability was a question for the arbitrator, relying upon Supreme Court precedent, including the Supreme Court's decision in *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440 (2006), which noted that under previous Supreme Court case law, the FAA "applies in both state and federal court." The Oklahoma Supreme Court was not persuaded. It held that despite the "Supreme Court cases on which the employers rely," the "existence of an arbitration agreement in an employment contract does not prohibit judicial review of the underlying agreement." In support, the Oklahoma court relied upon one of its own previous cases, which in the state high court's opinion conducted an "exhaustive overview" of U.S. Supreme Court decisions on the subject.

The U.S. Supreme Court disagreed and vacated the Oklahoma Supreme Court's decision, noting in the process that the state court had "disregard[ed] [the U.S. Supreme Court's] precedents on the FAA." In its decision, the Supreme Court reaffirmed the application of the FAA in state court and stated that "when parties commit to arbitrate contractual disputes," it is a "mainstay" of the FAA that "attacks on the validity of the contract, as distinct from attacks on the validity of the arbitration clause itself" should be resolved by the arbitrator. Thus, although the arbitration clause is itself "severable" from the rest of the contract - meaning that the former employees could have challenged the validity of the arbitration clause in state court as opposed to the validity of the underlying agreement - a state court cannot skip the threshold determination of whether an arbitration clause is valid and go straight to looking at the underlying contract. That, however, is what the Oklahoma Supreme Court did here, and by doing so, the Supreme Court said the state court "ignored a basic tenant of the [FAA's] substantive arbitration law."

The ruling again bolsters the use of arbitration clauses in employment agreements and demonstrates the need for careful drafting in the first instance. The threshold question under the FAA will be whether the arbitration clause is itself valid. If it is, then the merits of the dispute are resolved by an arbitrator, not a court. This will not, of course, cure any deficiencies that may exist in the underlying agreement - an arbitrator may still hold that the non-competition agreements drafted by Nitro-Lift are not enforceable - but it will provide employers with some assurance that a properly drafted arbitration clause will achieve the desired goal of more efficient and cost-effective resolution of matters. Moreover, as we have previously written, drafting an enforceable arbitration clause is itself a task that requires consideration and a skilled hand. Nonetheless, the *Nitro-Lift*

decision is another encouraging decision by the Supreme Court for employers who use or seek to use arbitration agreements.

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