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Supreme Court Says FAA Preempts Ky. Arbitration Rule

By **Y. Peter Kang and Abraham Moussako**

Law360, Los Angeles (May 15, 2017, 10:35 AM EDT) -- The U.S. Supreme Court ruled Monday that the Kentucky high court's refusal to send to arbitration a wrongful death suit filed against a nursing home ran afoul of the Federal Arbitration Act, saying the state justices' ruling was tailored to "black swan" contracts and arbitrations.

By a 7-1 vote, the federal justices sided with Kindred Nursing Centers LP in a wrongful death case in which Kentucky's arbitration-averse high court had said a state-law contract rule required individuals with powers of attorney to explicitly authorize such arbitration agreements.

The U.S. Supreme Court ruled 7-1 on Monday that Kentucky's highest court was wrong to deny arbitration in a wrongful death case. (Law360)

The justices heard oral arguments in February over whether the Kentucky Supreme Court correctly ruled that Kindred could not enforce two arbitration agreements entered into by attorneys-in-fact who had been given express authority to enter into contracts on behalf of their principals. Kindred claimed that the Kentucky justices contradicted the U.S. Supreme Court's clear, repeated holdings that the FAA preempts state-law rules that discriminate against arbitration agreements.

The Kentucky Supreme Court had held that a general authority by someone with power of attorney to enter into contracts did not pertain to arbitration agreements, according to Kindred's petition. The state justices found that an explicit reference to arbitration is needed in a power-of-attorney document to authorize an attorney to enter into an arbitration agreement, because that agreement waives the principal's "'sacred,' 'inviolate' and 'God-given' right to a jury trial," Kindred said.

But on Monday the U.S. high court disagreed, pointing to its 2011 decision in AT&T Mobility LLC v. Concepcion that the FAA can preempt state laws prohibiting class action arbitration waivers. The federal justices also noted that even a state law that does not explicitly ban arbitrations but is clearly intended to limit them can be overturned.

"The Kentucky Supreme Court's clear-statement rule ... fails to put arbitration agreements on an equal plane with other contracts," according to Monday's opinion, authored by Justice Elena Kagan. "The court did exactly what Concepcion barred: adopt a legal rule hinging on the primary characteristic of an arbitration agreement — namely, a waiver of the right to go to court and receive a jury trial."

The U.S. justices said that the clear-statement requirement seemed to not apply to anything but arbitration contracts, and that the Kentucky decision justified its nonspecific language by citing "patently objectionable and utterly fanciful contracts," such as those prohibiting freedom of worship or forcing someone into servitude.

"Placing arbitration agreements within that class reveals the kind of 'hostility to arbitration' that led Congress to enact the FAA. ... And doing so only makes clear the arbitration-specific character of the rule, much as if it were made applicable to arbitration agreements and black swans," Monday's opinion said.

According to the suit, two residents of Kindred-operated Winchester Centre for Health and Rehabilitation, Olive Clark and Joe Wellner, had executed powers of attorney designating Janis Clark and Beverly Wellner as their respective attorney-in-fact before being admitted to Winchester. The designees later signed the admittance paperwork on their principals' behalf, the suit said.

The designees also signed a separate agreement that stipulated that any disputes arising out of a resident's stay would be resolved in arbitration, according to court papers.

After the patients died due to allegedly negligent care, Janis Clark and Beverly Wellner brought wrongful death and injury suits against Kindred.

The state trial court initially dismissed the suits in favor of arbitration, but the cases were revived after the Kentucky high court ruled that a power of attorney expressly authorizing the attorney-in-fact to manage the principal's financial affairs and health care decisions was limited to those categories, and did not include the authority to bind the principal to an optional arbitration agreement.

On appeal to the U.S. Supreme Court, Clark and Wellner argued that the Kentucky high court decision was valid because the rule was focused on contract formation, rather than contract enforcement, which the FAA purportedly did not cover. The federal justices rejected this interpretation Monday.

"Adopting the respondents' view would make it trivially easy for States to undermine the Act ... their reasoning would allow States to pronounce any attorney-in-fact incapable of signing an arbitration agreement — even if a power of attorney specifically authorized her to do so. (After all, such a rule would speak to only the contract's formation.)," Monday's opinion said. "If the respondents were right, States could just as easily declare everyone incompetent to sign arbitration agreements. (That rule too would address only formation.)"

While ruling that the Clark arbitration agreement had to be enforced, the U.S. high court remanded the Wellner agreement, saying it was unclear whether the Wellner power of attorney had the ability to sign an arbitration contract in spite of the Kentucky court's overturned interpretation

In a brief dissent, Justice Clarence Thomas said that he would have upheld the Kentucky decision as the FAA does not apply to state courts.

“In state-court proceedings ... FAA does not displace a rule that requires express authorization from a principal before an agent may waive the principal’s right to a jury trial,” Justice Thomas said.

Mayer Brown LLP's Andrew J. Pincus, counsel for Kindred, said Monday that he was “gratified” by the decision. He also said that the U.S. high court rightfully disagreed with the formation-versus-enforcement distinction the families had argued.

“It is particularly significant that the Court made clear that state laws governing contract formation may not discriminate against arbitration, because arbitration opponents have tried to argue that the FAA applies only to contract interpretation and enforcement,” Pincus told Law360 in a statement emailed Monday. “The Court’s clear rejection of that attempt to carve a loophole in the FAA’s protection of arbitration agreements eliminates a potential obstacle to arbitration contract enforcement in the lower courts.”

Wilkes & McHugh PA's Robert Salyer, who represented Clark and Wellner, noted that Monday's decision did recognize some space for state courts to maintain sovereignty in interpreting powers of attorney.

“While the Supreme Court reiterated that arbitration agreements must be as easy to form as any other contract, and that no State may add explicit 'hurdles' to formation, it also established precedent that the meaning and authority encompassed in State law-governed powers of attorney are matters solely within the jurisprudence of State law courts,” Salyer said.

Speaking of the Wellner power of attorney, Salyer said, “the U.S. Supreme Court made clear for the first time that, where a State court interprets the meaning of a document (creating agency) as not encompassing arbitral authority, that this interpretation will be left undisturbed. The U.S. Supreme Court invited the Kentucky Supreme Court to confirm that this is what the latter court was doing (interpreting), with the Wellner power of attorney.”

Imre Szalai, a professor at Loyola University New Orleans’ College of Law and an amicus in the case who supported the families, said he was disappointed but unsurprised with Monday's decision.

“Since the 1980s, the Supreme Court has become more hostile to litigation, and this is not just in the arbitration context,” Szalai told Law360 on Monday.

Kindred is represented by Andrew J. Pincus, Archis A. Parasharami, Daniel E. Jones and Matthew A. Waring of Mayer Brown LLP.

Clark and Wellner are represented by Robert E. Salyer of Wilkes & McHugh PA.

The case is Kindred Nursing Centers LP v. Clark et al., case number 16-32, in the Supreme Court of the United States.

--Editing by Edrienne Su. Photo by Jonathan Hayter.

Update: This article has been updated with comments and with further details on the case and Monday's ruling.
