

RECENT DEVELOPMENTS

*Jack Ehleiter v. Grapetree Shores, Inc.**

I. INTRODUCTION

Whether parties waive their right to arbitrate a matter by participating in litigation has been a pressing question presented to the United States Circuit Courts¹ and United States Supreme Court.² The U.S. Supreme Court weighed in on the debate regarding arbitration waiver in two landmark decisions: *Howsam v. Dean Witter Reynolds, Inc.*³ and *Green Tree Financial Corp. v. Bazzle*.⁴ In these cases, the U.S. Supreme Court held that courts, not arbitrators, are in the best position to decide gateway issues, such as whether a dispute is subject to arbitration. Moreover, the language of the various decisions has left confusion among the circuit courts.⁵ The language of the decisions state that many types of "gateway questions" should be left to the arbitrator to decide.⁶ In the wake of the U.S. Supreme Court's landmark decisions, a circuit split has developed between the First and Eighth Circuits. The Circuits interpret the division of labor between the courts and an arbitrator in deciding certain issues that arise during litigation.

In 2005, the First Circuit examined the division of labor between the court and the arbitrator in situations of waiver, and firmly held that parties who behave inconsistently with their contractual right to arbitrate a claim waive that right.⁷ Should a question arise over the inconsistent behavior, the First Circuit held that it is appropriate for a court, not an arbitrator, to decide if their right to arbitrate has been waived.⁸ However, the First Circuit's

* *Jack Ehleiter v. Grapetree Shores, Inc.*, 482 F.3d 207 (3d. Cir 2007).

¹ *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79 (2002); *see Marie v. Allied Home Mortgage Corp.*, 402 F.3d 1 (1st Cir. 2005).

² *Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444 (2003).

³ *Howsam*, 537 U.S. 79.

⁴ *Green Tree*, 539 U.S. 444.

⁵ *See Green Tree*, 539 U.S. 444; *Howsam*, 537 U.S. 79.

⁶ *Howsam*, 537 U.S. at 85.

⁷ *See Marie*, 402 F.3d at 1.

⁸ *Id.* at 14 (stating that "the Supreme Court in *Howsam* and *Green Tree* did not intend to disturb the traditional rule that waiver by conduct, at least where due to litigation-related activity, is presumptively an issue for the court").

reading of *Howsam* and *Green Tree* is in stark contrast to the reading employed by the Eighth Circuit in its 2003 arbitration waiver decision.⁹

In *National American Insurance Co. v. Transamerica Occidental Life Ins. Co.*,¹⁰ the Eighth Circuit held that procedural issues such as waiver were presumptively for arbitrators to decide.¹¹ In making its decision, the Eighth Circuit also relied on the U.S. Supreme Court's decision in *Howsam*.¹² However, the Eighth Circuit read this decision to hold that while courts decide gateway issues such as whether a dispute is subject to arbitration, the parties can clearly reserve that right to arbitration, thereby making waiver a question for arbitrators.¹³

In April 2007 the circuit split deepened when the Third Circuit decided *Jack Ehleiter v. Grapetree Shores, Inc.*, in which it agreed with the First Circuit decision in *Marie* and unwaveringly distinguished the Eighth Circuit's *Transamerica* decision.¹⁴ The Third Circuit held that some litigation action inconsistent with a contractual arbitration right acts as a waiver, resulting in a forfeit of any right to subsequently request arbitration.¹⁵ Moreover, the Third Circuit reasoned that a trial court is in the best position to decide such questions.¹⁶

II. FACTS AND PROCEDURAL HISTORY

Grapetree Shores, Inc. (GSI) leased a portion of its hotel property to Treasure Bay V.I. Corp. (TBVI), which in turn operated the Divi Carina Bay Casino (Casino).¹⁷ Jack Ehleiter slipped and fell while walking down an employee stairway of the Casino.¹⁸ As part of TBVI's operation, it employed Jack Ehleiter as a card dealer pursuant to an Hourly Employment Agreement (Employment Agreement).¹⁹ The Employment Agreement between TBVI and Jack Ehleiter contained an arbitration clause requiring all disputes arising

⁹ *Nat'l Am. Ins. Co. v. Transamerica Occidental Life Ins. Co.*, 328 F.3d 462 (8th Cir. 2003).

¹⁰ *Id.*

¹¹ *Id.* at 466.

¹² *Id.*

¹³ *Id.*

¹⁴ *See Jack Ehleiter*, 482 F.3d at 218–21.

¹⁵ *Id.* at 217–18.

¹⁶ *Id.* at 209–10.

¹⁷ *Grapetree Shores, Inc. v. Ehleiter*, 47 V.I. 648, 650 (D. V.I. 2006).

¹⁸ *Id.*

¹⁹ *Jack Ehleiter*, 482 F.3d at 210.

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from employment at the Casino to be arbitrated.²⁰ In April 2001, litigation emerged from Ehleiter's injuries resulting from his slip and fall.²¹

A. Procedural History

Following Ehleiter's claim of injury as a result of a slip and fall accident on Casino property in April of 2001, "Ehleiter filed an action for negligence in the Superior Court, naming GSI as defendant."²² GSI answered the complaint with affirmative defenses claiming "Ehleiter's own conduct had proximately caused his damages and, alternatively, raised the defense of contributory negligence."²³ GSI's answer to Ehleiter's complaint made no mention of the arbitration clause in the employment contract.²⁴

Over the subsequent four years, the parties engaged in extensive discovery, which included taking more than nineteen depositions between them.²⁵ Both parties submitted and responded to several sets of interrogatories and requests for productions of documents, and submitted several expert reports.²⁶ Then, "[o]n May 13, 2003, while discovery was still ongoing and in response to a court order, the parties submitted to a joint stipulation certifying their readiness for trial by December 1, 2004."²⁷ The

²⁰ *Grapetree Shores*, 47 V.I. at 650. The pertinent sections of the employment agreement as they apply to arbitration provided very broad language stating:

16. ARBITRATION. Any controversy or claim arising out of or relating in any way to this Agreement, to the breach of this Agreement . . . including claims against Employer[s], its owners or subsidiary or parent or affiliated companies, and its or their officers, directors, employees, and agents (including any person or company that manages any portion of the Facility) . . . shall be resolved by arbitration and not in a court or before any administrative agency.

17. MATTERS ARBITRABLE. All claims or matters arising out of or relating in any fashion to this Agreement, to the breach of this Agreement, or to Employee's dealings with Employer, Employee's employment or the suspension or termination of Employee's employment with Employer shall be considered arbitrable. Arbitrable matters include, but are not limited to . . . the issue of arbitrability of any claim or dispute.

Id. at 653.

²¹ *Id.* at 650.

²² *Id.*

²³ *Id.* at 650–51.

²⁴ *Id.* at 651.

²⁵ *Jack Ehleiter*, 482 F.3d at 210.

²⁶ *Grapetree Shores*, 47 V.I. at 651.

²⁷ *Jack Ehleiter*, 482 F.3d at 210.

parties failed to settle in mediation.²⁸ Upon the motion of Ehleiter, the Superior Court entered an order scheduling trial for January 10, 2005.²⁹ Following a continuance given to GSI, due to a scheduling conflict with their counsel, trial was reset for March 21, 2005.³⁰ During the six-week period following the December 2, 2004 continuance granted to GSI, GSI filed a motion for summary judgment, a motion to implead a third party defendant, and Ehleiter filed a motion to amend his complaint to include a claim for punitive damages against GSI.³¹

On February 17, 2005, the final day to file motions and one day before the parties' joint and final pretrial statement and proposed jury instructions were due, GSI filed a motion to stay the case pending arbitration pursuant to Section 3 of the Federal Arbitration Act.³² This was the first that GSI asserted that, as an affiliated company of TBVI, it was entitled to have the dispute arbitrated pursuant to the arbitration provisions in the Employment Agreement entered into by Ehleiter and TBVI.³³ Under the Employment Agreement, Ehleiter agreed to arbitrate all claims against "affiliated companies" of TBVI arising from employment.³⁴

Ehleiter argued that GSI was not entitled to invoke the arbitration provisions of the Employment Agreement because GSI was not an "affiliated company" of TBVI, and even if they were, GSI had waived whatever arbitration rights it had under the Employment Agreement by actively litigating the matter for nearly four years.³⁵

B. Lower Court Rulings and Basis for Appeal

GSI and Ehleiter litigated this case before the Superior Court of the Virgin Islands (trial court) for nearly four years. It was following those four years that GSI moved to stay court proceedings pending arbitration pursuant to Section 3 of the Federal Arbitration Act (FAA).³⁶ The trial court denied GSI's Section 3 motion, holding that GSI, through its participation in lengthy

²⁸ *Grapetree Shores*, 47 V.I. at 651.

²⁹ *Id.* at 651.

³⁰ *Id.*

³¹ *Jack Ehleiter*, 482 F.3d at 210.

³² *Grapetree Shores*, 47 V.I. at 651.

³³ *Jack Ehleiter*, 482 F.3d at 210–11.

³⁴ *Grapetree Shores*, 47 V.I. at 653.

³⁵ *Jack Ehleiter*, 482 F.3d at 211.

³⁶ *Grapetree Shores*, 47 V.I. at 660.

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litigation and extensive discovery, had waived its right to arbitrate.³⁷ GSI appealed the trial court's denial of their Section 3 motion to the Appellate Division of the District Court of the Virgin Islands (Appellate Division) and successfully moved to stay trial proceedings pending resolution of the appeal.³⁸

On appeal, GSI contended that the trial court improperly decided the issue of waiver, where the language of the arbitration agreement and relevant authorities expressly provided that issues of arbitrability are to be put to an arbitrator, not a court.³⁹ GSI argued the broad language of the Employment Agreement between Ehleiter and GSI required that the trial court defer the allegations of waiver to the arbitrator, in the first instance, and not decide the question of waiver itself.⁴⁰

The Appellate Division held that under the FAA a party may petition the court in which an action is pending for a stay of proceedings to enforce an arbitration clause,⁴¹ however, Section 3 "conditions the court's grant of a stay of proceedings on a finding that the party was not in default in pursuing that remedy."⁴² The Appellate Division held that "default," as used in the statute, was to "be construed to apply to delays in asserting the arbitration clause while litigating the issues in a judicial forum."⁴³ The Appellate Division reviewed relevant decisions from the U.S. Supreme Court, as well as the Third and First Circuits, before it determined that the issue of waiver was appropriately decided by the trial court.⁴⁴ They also affirmed the trial court's denial of GSI's motion to stay proceedings pending arbitration.⁴⁵

III. THIRD CIRCUIT'S HOLDING AND REASONING

After the Appellate Division upheld the trial court's denial of GSI's Section 3 motion to stay litigation pending arbitration, GSI appealed to the

³⁷ *Id.*

³⁸ *Id.* at 651.

³⁹ *Id.* at 652.

⁴⁰ *Id.*

⁴¹ *Id.* at 653; *see also* 9 U.S.C. § 3 (1997).

⁴² *Grapetree Shores*, 47 V.I. at 653.

⁴³ *Id.* (citing *Hoxworth v. Blinder, Robinson & Co., Inc.*, 980 F.2d 912, 925 (3d Cir. 1992); *Marie v. Allied Home Mortgage Corp.*, 402 F.3d 1 (1st Cir. 2005); *N & D Fashions, Inc. v. DHJ Industries, Inc.*, 548 F.2d 722, 728 (8th Cir. 1976); *In re Mercury Const. Corp.*, 656 F.2d 933, 939-41 (4th Cir. 1981)).

⁴⁴ *Grapetree Shores*, 47 V.I. at 654-56.

⁴⁵ *See id.*

United States Court of Appeals for the Third Circuit (Third Circuit).⁴⁶ On appeal, GSI presented three issues to the Third Circuit for review.⁴⁷ First, "whether the Appellate Division had jurisdiction over GSI's appeal from the Superior Court's denial of its Section 3 motion, and whether [the Third Circuit], in turn, [had] jurisdiction to review the Appellate Division's order affirming the Superior Court's ruling."⁴⁸ Second, GSI raised the issue of whether arbitration waiver is a question for the trial court or an arbitrator.⁴⁹ Third, GSI raised the issue of whether the trial court correctly found on the merits that GSI waived any right it had to arbitrate by actively litigating Ehleiter's claim in court.⁵⁰

A. *Jurisdictional Issues*

While the parties did not raise a question of jurisdiction, the Third Circuit reasoned that appellate courts have "both the inherent authority and a continuing obligation to assess whether [they have] jurisdiction over a case or controversy before rendering a decision on the merits."⁵¹ The Third Circuit concluded that a literal reading of the statutory language of the FAA and 9 U.S.C. §16(a)(1)(A) conferred jurisdiction on the Appellate Division and Third Circuit to review the trial court's denial of a stay.⁵²

B. *Who Decides Issues of Waiver: Trial Court or Arbitrator?*

Recent decisions by the United States Supreme Court in *Howsam v. Dean Witter Reynolds, Inc.* and *Green Tree Financial Corp. v. Bazzle* provided GSI with the basis for an appeal to the Third Circuit.⁵³ GSI argued that the merits of Ehleiter's waiver defense was within the exclusive province of an arbitrator, not a trial court, to decide.⁵⁴ Additionally, GSI asserted that the language of the arbitration clause in the Employment Agreement reserved

⁴⁶ *Jack Ehleiter*, 482 F.3d. at 211.

⁴⁷ *Id.* at 209–10.

⁴⁸ *Id.* at 209.

⁴⁹ *Id.* at 209–10.

⁵⁰ *Id.* at 210.

⁵¹ *Id.* at 211; *see also* *Lazy Oil Co. v. Witco Corp.*, 166 F.3d 581, 585 (3d Cir. 1999); *Shendock v. Director, Office of Workers' Compensation Programs*, 893 F.2d 1458, 1461 (3d Cir. 1990).

⁵² *Jack Ehleiter*, 482 F.3d at 211–12.

⁵³ *Id.* at 215.

⁵⁴ *Id.* at 215.

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the issue of waiver by way of participation in litigation activity for an arbitrator to decide, not a court,⁵⁵ relying on the Supreme Court's decisions in *Howsam v. Dean Witter Reynolds, Inc.* and *Green Tree Financial Corp v. Bazzle*. The Supreme Court, in *Howsam*, resolved a dispute among the circuit courts over whether the application of a National Association of Securities Dealers (NASD) rule imposing a time limit on the submission of disputes for arbitration was a matter presumptively for the court or for the NASD arbitrator.⁵⁶ The Supreme Court held that "[t]he question whether the parties have submitted a particular dispute to arbitration, *i.e.*, the 'question of arbitrability,' is 'an issue for judicial determination unless the parties clearly and unmistakably provide otherwise.'"⁵⁷ Specifically, GSI argued that the Employment Agreement unmistakably provided that any questions of arbitrability were exclusively reserved for an arbitrator, and not the court, to decide.⁵⁸

In *Green Tree*, the Supreme Court held that the question of whether the parties' agreement prohibited the use of class arbitration procedures was an issue for the arbitrator to decide because "[i]t concerns contract interpretation and arbitration procedures" rather than "judicial procedures."⁵⁹ Despite this conclusion, the Court also reaffirmed the general division of labor articulated in *Howsam*, noting that the issues which relate to what kind of arbitration proceeding the parties agreed to are presumptively for the arbitrator to decide, while issues related to "whether they agreed to arbitrate a matter,"⁶⁰ are presumptively entrusted to the court for resolution.⁶¹

In analyzing GSI's claims in light of the Supreme Court's holdings in *Howsam* and *Green Tree*, the Third Circuit looked to its own long and consistent history of deciding that questions of waiver based on litigation conduct should be decided by a court, rather than referring the issue to an arbitrator.⁶² Beyond considering its own precedent, the Third Circuit looked

⁵⁵ *Id.* at 211.

⁵⁶ *Howsam*, 537 U.S. at 82–83.

⁵⁷ *Id.* at 83 (emphasis in original) (internal citations omitted).

⁵⁸ See *Jack Ehleiter*, 482 F.3d at 221.

⁵⁹ *Green Tree*, 539 U.S. at 452–53.

⁶⁰ *Id.* at 452.

⁶¹ *Jack Ehleiter*, 482 F.3d at 217 (internal citations omitted).

⁶² See *Wood v. Prudential Ins. Co. of Am.*, 207 F.3d 674, 680 (3d Cir. 2000); *Great Western Mortgage Corp. v. Peacock*, 110 F.3d 222, 233 (3d Cir. 1997); *PaineWebber Inc. v. Faragalli*, 61 F.3d 1063, 1068–69 (3d Cir. 1995); *Hoxworth v. Blinder, Robinson & Co., Inc.*, 980 F.2d 912, 925–27 (3d Cir. 1992); *Gavlik Constr. Co. v. H.F. Campbell Co.*, 526 F.2d 777, 783–84 (3d Cir. 1975).

to the 2005 decision in *Marie v. Allied Home Mortgage* by the First Circuit,⁶³ one of the few decisions that followed the *Howsam* and *Green Tree* decisions regarding arbitration waiver issues.⁶⁴ The question before the First Circuit in *Marie* was whether "waiver of the right to arbitrate due to inconsistent activity in another litigation forum remains an issue for the court even after the *Howsam* and *Green Tree* holdings."⁶⁵ The First Circuit held that the trial judge, having been directly involved in the entire course of the legal proceedings, is in a far better position to determine whether the belated request for arbitration is a thinly veiled attempt to forum shop.⁶⁶ Moreover, the First Circuit believed that because the inquiry into whether a party has waived its right to arbitrate a claim by litigating the case in court "heavily implicates 'judicial procedures,'"⁶⁷ the court should remain free to "control the course of proceedings before it and to correct abuses of those proceedings,"⁶⁸ rather than being required to defer to the findings of an arbitrator with no previous involvement in the case.⁶⁹

GSI urged consideration of the Eighth Circuit's decision in *National American Insurance Co. v. Transamerica Occidental Life Insurance Co.* ("*Transamerica*").⁷⁰ However, after careful analysis, the Third Circuit distinguished *Transamerica* from the case at hand because it involved prior arbitration conduct, rather than prior litigation conduct,⁷¹ and therefore found the *Transamerica* holding did not support GSI's position.⁷²

Next, the Third Circuit analyzed GSI's argument that the Employment Agreement provides for resolution of the waiver defense by an arbitrator, not the courts.⁷³ The Court thought it was clear that the provision did provide for an arbitrator to determine gateway questions of whether the underlying substantive dispute between them is arbitrable, however, it held that there were no references to waiver of arbitration in any section of the Employment

⁶³ *Marie*, 402 F.3d at 3.

⁶⁴ *Jack Ehleiter*, 482 F.3d at 217–18.

⁶⁵ *Marie*, 402 F.3d at 3.

⁶⁶ *Id.* at 13.

⁶⁷ *Id.* (citing *Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444, 452–53 (2003)).

⁶⁸ *Id.*

⁶⁹ *Jack Ehleiter*, 482 F.3d at 218 (citing *Marie v. Allied Home Mortgage Corp.*, 402 F.3d 1, 13 (1st Cir. 2005)).

⁷⁰ *Id.* at 219.

⁷¹ *Id.* at 220–21.

⁷² *Id.* at 221.

⁷³ *Id.*

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Agreement.⁷⁴ Therefore, the Third Circuit felt it could not "interpret the Agreement's silence regarding who decides the waiver issue here as giving the arbitrators that power, for doing so would force an unwilling party to arbitrate a matter he reasonably would have thought a judge, not an arbitrator, would decide."⁷⁵ Given the traditional rule, litigants would expect the court, not an arbitrator to decide the question of waiver based on litigation conduct. But without an expressly manifested intent being shown in the Employment Agreement to the contrary, the Third Circuit was unwilling to read such meaning into the Employment Agreement.⁷⁶ Ultimately the Third Circuit held that waiver of a right to arbitrate based on litigation conduct is presumptively an issue for the court, not an arbitrator, to decide.⁷⁷

C. Did GSI Waive Its Rights?

The final argument raised by GSI was that even if the trial court had the authority to resolve the waiver issue, it erred in finding that GSI had waived any right it may have had to arbitrate Ehleiter's claim.⁷⁸ GSI felt that Ehleiter failed to demonstrate that his legal position had actually been prejudiced by GSI's delay in invoking its arbitration rights, nor had Ehleiter been prejudiced by the extensive discovery that took place prior to the filing of GSI's motion to stay.⁷⁹

The Third Circuit turned to its precedent in *Hoxworth* to help decide whether GSI waived its right to arbitration based on litigation conduct.⁸⁰ In *Hoxworth*, the Third Circuit reasoned that "prejudice is the touchstone for determining whether the right to arbitrate has been waived" by litigation conduct.⁸¹ In *Hoxworth*, prejudice was characterized by the plaintiffs first as defendant's failure to raise arbitration promptly, thereby causing the plaintiffs to devote substantial amounts of time, effort, and money in prosecuting the action, and second, the ability of the defendants to use the Federal Rules of Civil Procedure to conduct discovery which would otherwise not be available

⁷⁴ *Id.* at 222.

⁷⁵ *Jack Ehleiter*, 482 F.3d at 222 (internal citations omitted).

⁷⁶ *Id.*

⁷⁷ *Id.*

⁷⁸ *Id.*

⁷⁹ *Id.* at 223–24.

⁸⁰ *Id.* at 222–25.

⁸¹ *Hoxworth v. Blinder, Robinson & Co., Inc.*, 980 F.2d 912, 925 (3d Cir. 1992) (internal citation omitted).

to them in the arbitration forum.⁸² The Third Circuit held waiver occurred in *Hoxworth* based on several factors, including, but not limited to: (1) participating in numerous pretrial proceedings during the eleven months before moving to compel arbitration, (2) taking the deposition of each of the named plaintiffs, depositions that would not have been available in arbitration, (3) filing a motion to stay discovery, and (4) consenting to the district court's first pretrial order.⁸³

Using the *Hoxworth* factors to guide their reasoning in the case at hand, the Third Circuit examined the extent of unnecessary delay and expense incurred by Ehleiter as a result of the GSI's belated invocation of their right to arbitrate.⁸⁴ Looking to the discovery expense of litigating the case for nearly four years, the Third Circuit held that "[e]ven were we to assume that some of the same discovery would have taken place in the District Court litigation had GSI promptly invoked its right to arbitration in the Superior Court action, a finding of prejudice would still be warranted on the record before us."⁸⁵ Moreover, the Third Circuit felt that "all the other *Hoxworth* factors strongly support a finding of prejudice here."⁸⁶

Therefore, the Third Circuit held that Ehleiter was "prejudiced by the unnecessary delay or expense that results when an opponent delays invocation of its contractual right to arbitrate,"⁸⁷ and thus, the trial court was correct in finding that GSI had waived any right to arbitrate by actively litigating the dispute at hand for almost four years to Ehleiter's detriment.⁸⁸

IV. CONCLUSION: UNCERTAINTY AMONG CIRCUITS REMAINS THE NORM

Whether parties have waived their right to arbitrate by actively participating in litigation will continue to be a question presented to the circuit courts and U.S. Supreme Court due to the circuit split following *Howsam* and *Green Tree*. While the decision in *Ehleiter* answers the question of whether the "traditional rule" that courts, not arbitrators, should decide the question of waiver in favor of the courts, the circuit courts remain split, with the First and Third Circuit requiring the courts to decide waiver

⁸² *Id.* at 926.

⁸³ *Id.* at 925–26.

⁸⁴ *Jack Ehleiter*, 482 F.3d at 224.

⁸⁵ *Id.* at 225.

⁸⁶ *Id.*

⁸⁷ *Id.* (internal citation omitted).

⁸⁸ *Id.* at 222.

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issues, while the Eighth Circuit stands firmly behind its ruling in *Transamerica* that it is the arbitrator's role to decide questions of waiver. Only time will tell if the circuits will work out the inconsistencies regarding waiver. Questions still exist as to the extent of the litigation conduct required to waive rights to arbitration. However, it seems inevitable that the U.S. Supreme Court will have to clarify what is the proper division of labor, a question that was inadvertently muddled in the inconsistent language of the *Howsam* and *Green Tree* decisions.

Catherine Woltering

