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What 3rd Circ. Gets Wrong About Arbitration Enforcement

By **David Cinotti** (December 11, 2023, 2:40 PM EST)

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Assume that a plaintiff sues a defendant in the U.S. District Court for the District of New Jersey and the defendant contends that the claims are covered by an arbitration agreement between the parties.

Ordinarily, the defendant might respond to the suit with a motion to compel arbitration under Section 4 of the Federal Arbitration Act.

But does it make a difference if the arbitration agreement calls for arbitration in New York County, New York? The majority of courts to consider the issue, including the U.S. Court of Appeals for the Third Circuit, have held that Section 4 permits only the court in the district where the arbitration is to take place to compel arbitration.[1]

Those courts base that conclusion on the language of Section 4, which states both that if the court finds a dispute arbitrable, "the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement" and that "[t]he hearing and proceedings, under such [arbitration] agreement, shall be within the district in which the petition for an order directing such arbitration is filed."[2]

Accordingly, the reasoning proceeds, if the terms of the arbitration agreement call for arbitration in New York County, a motion to compel must be filed in the U.S. District Court for the Southern District of New York, in order to satisfy the requirements that the arbitration proceed "in accordance of the terms" of the parties' agreement and that arbitration take place "within the district in which the petition for an order directing such arbitration is filed."

That reasoning creates a procedural problem when claims filed in an action in one district are allegedly subject to arbitration outside that district. Some courts have held that the correct procedure in those circumstances is a motion to dismiss for improper venue under Federal Rule of Civil Procedure 12(b)(3).[3]

In June, the Third Circuit stated in a footnote in Henry v. Wilmington Trust NA that a Rule 12(b)(6) motion for failure to state a claim is the "appropriate procedural mechanism for enforcing" arbitration agreements that require arbitration in a different district. The decision was appealed to the U.S. Supreme Court, which denied certiorari on Oct. 16.[4]

As explained below, however, there are multiple problems with requiring a Rule 12(b)(3) or (6) motion

to enforce an agreement calling for out-of-district arbitration. The correct procedure is instead a motion to stay the litigation under Section 3 of the FAA.

FAA Section 3 contains no geographical limitations.

FAA Section 3 provides a means for a district court to stay an action before it when the claims are subject to arbitration, without regard to where the dispute should be arbitrated. It states:

> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.[5]

There is no indication in Section 3 that only some district courts can stay litigation before them. The statute broadly refers to a suit or proceeding pending in "any of the courts of the U.S.," and does not contain the language that courts have held limit the authority of district courts under Section 4.

In addition, the authority to stay under Section 3 does not depend on — and is a different sort of relief from — the authority to compel arbitration under Section 4.

According to the U.S. Court of Appeals for the D.C. Circuit, "Section 3 empowers a district court only to stay an action, leaving to the claimant the choice of arbitrating the claims or abandoning them. Section 4 allows the court to issue orders directing arbitration."[6]

Even if Section 4 channels motions to compel arbitration to the district court for the place of arbitration, Section 3 stays remain available in any district court where claims have been filed that belong in arbitration.

Requiring a Rule 12(b) motion to enforce an arbitration agreement unnecessarily complicates and undermines appellate jurisdiction under FAA Section 16.

FAA Section 16 contains specific rules on when arbitration decisions are appealable.

Section 16(a) provides that denials of a request to stay litigation under Section 3 and denials of a motion to compel arbitration under Section 4 are immediately appealable.[7] And under Section 16(b), "an appeal may not be taken from an interlocutory order" compelling arbitration or staying a case in favor of arbitration.[8]

Thus, appellate jurisdiction is ordinarily clear when a motion authorized by the FAA is decided: Under Section 16, "any order favoring litigation over arbitration is immediately appealable and any order favoring arbitration over litigation is not."[9]

But that is not so when Rule 12(b) motions are substituted for FAA motions. Although denial of an FAA-created motion favoring litigation over arbitration is immediately appealable, denials of Rule 12(b) motions are not normally appealable as of right because they are not final judgments disposing of the entire action.

The perplexing problem of whether the losing movant can appeal under FAA Section 16(a) the denial of a motion to dismiss, or for summary judgment, that raises arbitrability issues has led the Third Circuit to a complex analysis: "to determine whether an order constitutes an order that is appealable under § 16, we examine the label and the operative terms of the district court's order, as well as the caption and relief requested in the underlying motion."[10]

The Third Circuit might have to undertake that analysis when a party mistakenly moves under Rule 12(b) or Rule 56 for an order that the dispute should be arbitrated, but that complexity is unnecessary when the movant argues that the opposing party's claims must be arbitrated in a different district; that motion can and should be decided under FAA Section 3.

FAA Section 16's restrictions on the right to appeal are also undermined by requiring a Rule 12(b) motion instead of a motion to stay under the FAA. Granting a Rule 12(b) motion to dismiss a case in favor of arbitration would likely be appealable as a final order under Title 28 of the U.S. Code, Section 1291, because it disposes of the case before the district court.

As noted, however, Section 16(b) of the FAA precludes appeals from orders compelling arbitration or staying litigation in favor of arbitration.

Thus, the judicially created procedure of a Rule 12(b) motion to enforce an arbitration agreement calling for arbitration outside the district runs afoul of the FAA's pro-arbitration appellate rules because a party whose claims are dismissed in favor of arbitration will have a right to appeal that the U.S. Congress intended to foreclose in the FAA.

Neither Rule 12(b)(3) nor Rule 12(b)(6) is a proper fit to enforce an arbitration agreement.

Those courts that continue to require Rule 12(b)(3) motions need to reconsider that law under the Supreme Court's 2013 decision in Atlantic Marine Construction Co. v. U.S. District Court for the Western District of Texas.[11]

There, the court held that "Rule 12(b)(3) allow[s] dismissal only when venue is 'wrong' or 'improper.' Whether venue is 'wrong' or 'improper' depends exclusively on whether the court in which the case was brought satisfies the requirements of federal venue laws, and those provisions say nothing about a forum-selection clause."[12]

Instead, forum-selection clauses may be enforced by motions to transfer to a different district under Section 1404(a), which provides that for "the convenience of parties and witnesses, in the interest of justice, a district court may transfer any civil action to any other district or division where it might have been brought or to any district or division to which all parties have consented."[13]

Arbitration clauses are types of forum-selection clauses,[14] and thus Atlantic Marine holds that they cannot be enforced through Rule 12(b)(3). Courts have recognized that Atlantic Marine "shows that parties should not use Rule 12(b)(3) to raise an arbitration agreement — a type of forum-selection clause."[15]

Atlantic Marine does not foreclose the Third Circuit's Rule 12(b)(6) approach because the Supreme Court left open whether a forum-selection clause could be enforced through such a motion.[16] But Rule 12(b)(6) is less flexible and efficient than FAA Section 3.

On a motion to dismiss for failure to state a claim, a court cannot consider facts not alleged or incorporated by reference in a complaint.[17]

In many cases, the arbitration agreement or facts necessary to show a valid and enforceable agreement might not be alleged in the complaint or be subject to judicial notice.[18] On a stay motion, the court can consider whatever evidence about the existence or validity of an arbitration agreement that the parties produce, including after arbitration-specific discovery.[19]

Finally, requiring Rule 12(b) motions also conflicts with Federal Rule of Civil Procedure 81(a)(6), which states that the Federal Rules apply to proceedings under the FAA, among other laws, "except as these laws provide other procedures."

Under that rule, Rules 12(b)(3) and (6) do not govern applications to enforce arbitration agreements because the applicable procedures are found in FAA Section 3.

Notably, the U.S. Court of Appeals for the Seventh Circuit has recognized that "[n]o 'complaint' or 'motion to dismiss' or any other filing conceived by the Federal Rules of Civil Procedure need have been filed" where the relief sought is confirmation of an arbitration award because the procedures for confirmation are found in the FAA.[20]

Some district courts have correctly recognized that Section 3 is the proper procedure when a party seeks to compel arbitration in a different district.[21] Once stayed, the case may not be dismissed outright — which might result in an appealable order — under Third Circuit precedent.[22]

Conclusion

Atlantic Marine leaves open the possibility that the defendant in the example above could move to transfer venue to the Southern District of New York based on the convenience of the parties and witnesses under Section 1404(a), and then move to compel arbitration after venue was transferred.

It is not clear whether the transferring court must or should first decide whether the arbitration agreement is valid or enforceable, or leave that issue to the transferee court.[23]

In any event, a transfer motion might be the best procedure to enforce an ordinary forum-selection clause, but it is not necessary or efficient to enforce an arbitration agreement. Even if FAA Section 4 restricts district courts from compelling arbitration outside their district, FAA Section 3 allows them to stay litigation if the claims are subject to arbitration anywhere.

That approach is faithful to the language of FAA Section 3, as well as the intent of FAA Section 16 to prevent immediate appeals of decisions enforcing arbitration clauses and to permit appeals of decisions finding claims not arbitrable.

In addition, favoring Section 3 motions respects the Federal Rules' command that FAA procedures control when they apply.

The Third Circuit and other courts should correct their current law requiring a motion to dismiss based on an arbitration clause because it conflicts with the FAA, the Federal Rules of Civil Procedure, and — with regard to the improper-venue approach — Supreme Court precedent. It also creates unnecessary

confusion and complexity when the FAA "calls for a summary and speedy disposition of motions or petitions to enforce arbitration clauses."[24]

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[1] See, e.g., Ansari v. Qwest Commc'ns Corp., 414 F.3d 1214, 1219-20 (10th Cir. 2005); Inland Bulk Transfer Co. v. Cummins Engine Co., 332 F.3d 1007, 1018 (6th Cir. 2003); Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Lauer, 49 F.3d 323, 327-28 (7th Cir. 1995); Econo-Car Int'l, Inc. v. Antilles Car Rentals, Inc., 499 F.2d 1391, 1394 (3d Cir. 1974); Sea Spray Holdings, Ltd. v. Pali Fin. Group, Inc., 269 F. Supp. 2d 356, 363 (S.D.N.Y. 2003).

[2] 9 U.S.C. § 4.

[3] See, e.g., Faulkenberg v. CB Tax Franchise Sys., LP, 637 F.3d 801, 808 (7th Cir. 2011); Lim v. Offshore Specialty Fabricators, Inc., 404 F.3d 898, 902 (5th Cir. 2005); Pollara v. Radiant Logistics Inc., No. CV 12-0344 GAF (SPX), 2012 WL 12887094, at *6 (C.D. Cal. Mar. 20, 2012).

[4] Henry ex rel. BSC Ventures Holdings, Inc. Emp. Stock Ownership Plan v. Wilmington Tr. NA, 72 F.4th 499, 505 n.5 (3d Cir. 2023), cert. denied sub nom. Wilmington Tr., N.A. v. Marlow, No. 23-122, 2023 WL 6797729 (U.S. Oct. 16, 2023).

[5] 9 U.S.C. § 3.

[6] LaPrade v. Kidder Peabody & Co., 146 F.3d 899, 902-03 (D.C. Cir. 1998) (citations omitted).

[7] 9 U.S.C. § 16(a).

[8] Id. § 16(b).

[9] Ballay v. Legg Mason Wood Walker, Inc., 878 F.2d 729, 732 (3d Cir. 1989).

[10] Devon Robotics, LLC v. DeViedma, 798 F.3d 136, 146-47 (3d Cir. 2015) (footnotes omitted).

[11] Atlantic Marine Construction Co. v. U.S. District Court for Western District of Texas, 571 U.S. 49 (2013).

[12] Id. at 55.

[13] Atl. Marine, 571 U.S. at 59.

[14] See Scherk v. Alberto-Culver Co., 417 U.S. 506, 519 (1974) (stating that an arbitration clause is "a specialized forum selection clause that posits not only the situs of suit but also the procedure to be used in resolving the dispute").

[15] Boykin v. Fam. Dollar Stores of Michigan, LLC, 3 F.4th 832, 838 (6th Cir. 2021); see also City of Benkelman v. Baseline Eng'g Corp, 867 F.3d 875, 880 (8th Cir. 2017) (same).

[16] See Atl. Marine, 571 U.S. at 61.

[17] See Davis v. Wells Fargo, 824 F.3d 333, 351 (3d Cir. 2016) (holding that court on Rule 12(b)(6) motion "must accept the well-pleaded facts of the . . . complaint as true" and may also consider exhibits attached to the complaint[,] matters of public record, and documents integral to or explicitly relied upon in the complaint" (internal quotation marks omitted)).

[18] See, e.g., Boykin, 3 F.4th at 838 (holding that district court erred in granting Rule 12(b)(6) motion to enforce arbitration agreement because facts necessary to do so were not pleaded in complaint).

[19] See Guidotti v. Legal Helpers Debt Resolution, L.L.C., 716 F.3d 764, 776 (3d Cir. 2013) (holding that court should evaluate motion to compel arbitration under Rule 56 standard when arbitrability cannot be determined based on face of complaint and documents relied on the complaint).

[20] Webster v. A.T. Kearney, Inc., 507 F.3d 568, 571 (7th Cir. 2007).

[21] See, e.g., Robinson v. Ent. One US LP, No. 14-cv-1203 (AJN), 2015 WL 3486119, at *5 (S.D.N.Y. June 2, 2015) (construing motion to compel arbitration of pending claims as motion to stay under FAA Section 3); Duran v. J. Hass Grp. L.L.C., 10-cv-4538 (RRM) (SMG), 2012 WL 3233818, at *2-3 (E.D.N.Y. June 8, 2012) aff'd, 531 F. App'x 146 (2d Cir. 2013) (same).

[22] See Lloyd v. HOVENSA, LLC., 369 F.3d 263, 269 (3d Cir. 2004) ("The plain language of § 3 affords a district court no discretion to dismiss a case where one of the parties applies for a stay pending arbitration.").

[23] See, e.g. Mitchell v. Craftworks Rests. & Breweries, Inc., Civ. A. No. 18-879 (RC), 2018 WL 5297815, at *12 (D.D.C. Oct. 25, 2018) (resolving challenges to enforceability of arbitration clause calling for arbitration out of district before ordering transfer of case under Section 1404(a) because court lacked power to compel arbitration under FAA Section 4).

[24] Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 29 (1983).