Class Arbitration Decisions in 2013 Confirmed the Importance of Class Action Waivers

By Lea Haber Kuck and Gregory A. Litt

The U.S. Supreme Court has taken an active interest in the difficult issues raised by the intersection of class actions and arbitration, issuing four class arbitration decisions in the last four years. In June 2013, it rendered two of those decisions, answering questions left open by the Court's earlier pivotal decisions in *Stolt-Nielsen S.A. v. AnimalFeeds International Corp.*[1] and *AT&T Mobility LLC v. Concepcion*.[2] These decisions—*Oxford Health Plans LLC v. Sutter*[3] and *American Express Co. v. Italian Colors Restaurant*[4]—had an immediate impact on pending class arbitration cases around the country, and together they confirm the importance of including class action waivers in arbitration clauses where the parties do not intend to permit class action proceedings.

Oxford Health Plans LLC v. Sutter: Interpreting the Sounds of Silence

In *Stolt-Nielsen*, the Supreme Court held that "a party may not be compelled under the FAA [Federal Arbitration Act] to submit to class arbitration unless there is a contractual basis for concluding that the party *agreed* to do so."[5] After the decision was rendered in 2010, parties continued to file class arbitrations,[6] but the federal courts split over how to proceed when an arbitrator infers a contractual basis for class arbitration even though the arbitration clause is silent on the subject.

The Second Circuit in *Jock v. Sterling Jewelers Inc.*[7] and the Third Circuit in *Oxford Health Plans*[8] each upheld an arbitrator's decision permitting class arbitration despite the lack of any specific reference to class actions in the arbitration clause. Both courts observed that the arbitrators made their decisions by interpreting the parties' arbitration clauses and finding a contractual basis for class arbitration, as required by *Stolt-Nielsen*.[9] After noting the narrow scope of review of arbitration awards permitted by the Federal Arbitration Act ("FAA"), both the Second and Third Circuits held that once the arbitrator has interpreted the parties' agreement, courts are not empowered to second-guess the decision.[10]

The Fifth Circuit, however, in *Reed v. Florida Metropolitan University, Inc.*, expressly rejected the Second and Third Circuit decisions explaining: "We read *Stolt-Nielsen* as requiring courts to ensure that an arbitrator has a legal basis for his class arbitration determination, even while applying the appropriately deferential standard of review. Such an analysis necessarily requires some consideration of the arbitrator's award and rationale."[11] After performing this analysis, the Fifth Circuit reversed the district court's decision, which had confirmed an arbitrator's clause construction award permitting class arbitration, and directed that the arbitration proceed bilaterally.[12]

To address this circuit split, the Supreme Court granted certiorari to review the Third Circuit's decision in *Oxford Health Plans*.[13] Oxford sought to rely on Section 10(a)(4) of the FAA, the same provision applied by the Supreme Court to vacate the award in *Stolt-Nielsen*, which allows a court to vacate an arbitral award "'where the arbitrator[] exceeded [his] powers.'"[14] Invoking *Stolt-Nielsen* and other precedents that set forth the extremely limited scope of permissible review under Section 10(a)(4), Justice Kagan, writing for the majority, explained that "the sole question" the courts may consider is "whether the arbitrator (even arguably) interpreted the parties' contract, not whether he got its meaning right or wrong."[15] In the case before it, the Court found that the arbitrator "considered [the parties'] contract and decided whether it reflected an agreement to permit class proceedings. That suffices to show that the arbitrator did not 'exceed[ ] [his] powers.'"[16] Accordingly, the Court affirmed the Third Circuit's decision and the arbitrator's award survived. The June 2013 decision has already been applied in several cases to ratify arbitrators' decisions permitting class arbitration despite facially silent clauses.[17]

Significant issues remain, however. In a footnote in the *Oxford Health Plans* decision, the Supreme Court noted that it would have faced "a different issue if Oxford had argued below that the availability of class arbitration is a so-called 'question of arbitrability,'" which would be "presumptively for courts to decide," and would thus allow the courts to review the arbitrator's decision *de novo*.[18] The Court noted that "*Stolt-Nielsen* made clear that this Court has not yet decided whether the availability of class arbitration is a question of arbitrability," but explained that the case did not provide it with the opportunity to do so because Oxford had agreed to submit the determination to the arbitrator.[19] In a concurring opinion, Justice Alito (joined by Justice Thomas) argued that the availability of class arbitration was a determination that should be made by the courts, but he recognized that Oxford's agreement to submit the question to the arbitrator removed the decision from the courts' consideration, and thus he joined the majority opinion.[20]

Only five months later, in November 2013, the Sixth Circuit held in *Reed Elsevier, Inc. ex rel. LexisNexis Division v. Crockett* that "the question whether an arbitration agreement permits classwide arbitration is a gateway matter, which is reserved 'for judicial determination unless the parties clearly and unmistakably provide otherwise.'"[21]

The court reasoned that "[g]ateway questions are fundamental to the manner in which the parties will resolve their dispute—whereas subsidiary questions," which should be left to the arbitrator, "concern details," and "whether the parties arbitrate one claim or 1,000 in a single proceeding is no mere detail."[22] The Sixth Circuit went on to determine that the parties had not "clearly and unmistakably" committed the class arbitration decision to the arbitrator, so it was left for the courts to decide, and the court decided that the clause, silent as to class proceedings, did not provide for class arbitration.[23]

The cases will continue to develop, and during the next year or two, they may provide more clarity on whether the availability of class arbitration is a decision for the courts or the arbitrator. But the unmistakable lesson to be learned from all of these cases is that if an arbitration clause is silent regarding class arbitration, the parties cannot be entirely certain what a court or arbitrator will do. To obtain certainty as to whether class arbitration will be permitted, arbitration clause drafters should either expressly assent to class arbitration or expressly waive it.

American Express Co. v. Italian Colors Restaurant: Waive It Goodbye

If parties expressly waive class arbitration, the Supreme Court has made clear that the waiver will be honored—even if the waiver is considered unconscionable under state law and even if it effectively forecloses the vindication of certain federal statutory rights.

In *Stolt-Nielsen*, the Supreme Court made clear that in the ordinary case, arbitrations cannot be brought on behalf of a class absent the agreement of the parties to this procedure,[24] and therefore certainly not when the parties expressly agreed to exclude arbitrations of class claims. But what about the case where waiver of the right to bring claims on behalf of a class conflicts with another legal principle or mandate?

In 2011, the Supreme Court ruled in *AT&T Mobility v. Concepcion* that California's state-law "*Discover Bank* Rule"—which applied California's unconcionability doctrine to bar class action waivers as unconscionable in some arbitration agreements—was preempted by the FAA, which requires courts to enforce arbitration clauses as written, with their class action waivers intact.[25] But state law unconscionability doctrines were not the only legal rules that courts used to strike down class action waivers, and in 2013, the Court took the opportunity to address the question in the context of federal statutory rights.

In 2009, the Second Circuit issued its first decision in a dispute between American Express Co. and Italian Colors Restaurant, a restaurant that accepted American Express cards.[26] Italian Colors brought claims on behalf of a class of merchants against American Express for alleged violations of federal antitrust law. In response, American Express sought to enforce the arbitration clause in its agreement with Italian Colors, which included a class action waiver. The Second Circuit struck down the class action waiver, finding that "the size of the recovery [potentially] received by *any* individual plaintiff will be too small to justify the expenditure of bringing an individual action."[27] The court cited a statement by the Supreme Court, almost 25 years earlier, that if the terms of an arbitration agreement operated as "'a prospective waiver of a party's right to pursue statutory remedies for antitrust violations, [the Court] would have little hesitation in condemning the agreement as against public policy.'"[28]

Six days after it decided *Stolt-Nielsen*, the Supreme Court granted certiorari in *Italian Colors* in order to vacate and remand the case to the Second Circuit for reconsideration in light of the *Stolt-Nielsen* decision.[29] On remand, the Second Circuit reaffirmed its power to strike down the class action waiver in the American Express agreement. It concluded that because its prior decision had not ordered class-wide arbitration—a decision which would have been at odds with *Stolt-Nielsen*—but had instead remanded to the district court to allow the defendant the opportunity to withdraw its motion to compel arbitration, its prior ruling was valid and could be reinstated.[30]

The Supreme Court granted certiorari again, resulting in the June 2013 decision. Reversing the Second Circuit, the Court held that a contractual waiver of class arbitration is enforceable under the FAA even when the plaintiff's cost of individually arbitrating a federal statutory claim—such as a claim for violation of the federal antitrust laws—vastly exceeds the individual's potential recovery.[31] The Court ruled that the "effective vindication doctrine" cited by the Second Circuit might be applicable if the arbitration clause actually barred a party from raising a federal statutory claim, but it could not be applied simply because the expense of proving a claim outweighed an individual's potential recovery.[32] Justice Kagan (joined by Justices Ginsburg and Breyer) filed a vigorous dissent, contending that the result of enforcing the class action waiver was that "[t]he monopolist gets to use its monopoly power to insist on a contract effectively depriving its victims of all legal recourse" against its allegedly anti-competitive practices.[33]

Since the Supreme Court issued its decision, the Second Circuit has applied it twice to cases brought under the Fair Labor Standards Act of 1938 ("FLSA").[34] In the first of those cases, *Sutherland v. Ernst & Young LLP*,[35] the plaintiff, on behalf of herself and others similarly situated, sought to recover overtime wages pursuant to the FLSA and New York state wage regulations.[36] The district court denied the defendant's motion to compel arbitration because it found that the class-action waiver provision in the arbitration agreement was unenforceable.[37] During the pendency of the appeal of the decision to the Second Circuit, the Supreme Court decided *Italian Colors*.

On appeal, the Second Circuit reversed, ruling that "in light of the Supreme Court's holding that the 'effective vindication doctrine' cannot be used to invalidate class-action waiver provisions in circumstances where the recovery sought is exceeded by the costs of individual arbitration, we are bound to conclude that Sutherland's arguments are insufficient to invalidate the class-action waiver provision at issue here."[38]

Three days later, the Second Circuit issued a similar decision in *Raniere v. Citigroup Inc.*,[39] in which employees of Citigroup raised claims that the court characterized as "virtually identical to those raised" in *Sutherland*.[40]

The message of *Italian Colors* and its Second Circuit progeny is clear: class action waivers are likely to be enforced even if it is economically unreasonable for an individual plaintiff to proceed alone, and even if the effective result is that plaintiffs have no practical means of enforcing their federal statutory rights.[41]

Conclusion

The Supreme Court's recent decisions demonstrate the importance of clearly drafting arbitration clauses with respect to class arbitration. Parties may explicitly provide for class arbitration in their agreements, or they can explicitly exclude it, but if parties fail to address the issue, they may end up in an unsettled procedural morass.

Endnotes

1. 559 U.S. 662 (2010).
2. 131 S. Ct. 1740 (2011).
3. 133 S. Ct. 2064 (2013).
4. 133 S. Ct. 2304 (2013).
5. 559 U.S. at 664.
6. There were 27 class arbitration filings with the AAA in 2010 and 36 such filings in 2011. *See* Gregory A. Litt & Tina Praprotnik, *After* Stolt-Nielsen, *Circuits Split, But AAA Filings Continue*, 27-7 Mealey's Int'l Arb. Rep., 22 (2012).
7. 646 F.3d 113 (2d Cir. 2011), *cert. denied*, 132 S. Ct. 1742 (2012).
8. 675 F.3d 215 (3d Cir. 2012), *aff'd*, 133 S. Ct. 2064 (2013).
9. 646 F.3d at 124; 675 F.3d at 222-24.
10. 646 F.3d at 125 (referencing decades-old principle of granting arbitrator's decision "substantial deference" (citation omitted)); 675 F.3d at 219 (noting application of "more deferential standard of review" in support of federal policy favoring arbitration).
11. 681 F.3d 630, 645 & n.13 (5th Cir. 2012) (citation omitted) abrogated by *Oxford Health Plans LLC v. Sutter*, 133 S. Ct. 2064 (2013).
12. *Id.* at 646.
13. 133 S. Ct. at 2068.
14. *Id.* (alteration in original) (citation omitted).
15. *Id.* (alteration in original) (citation omitted).
16. *Id.* at 2069.
17. *See, e.g., DIRECTV, LLC v. John Arndt*, No. 13-10033, 2013 WL 5718384 (11th Cir. Oct. 22, 2013) (per curiam); *Southern Comm. Serv., Inc. v. Thomas*, 720 F.3d 1352 (11th Cir. Jul. 12, 2013), *cert. denied*, 2014 WL 210671 (U.S. Jan. 21, 2014).
18. 133 S. Ct. at 2068 n.2.
19. *Id.*
20. *Id.* at 2071-72. Justice Alito noted that in the absence of a "concession" such as Oxford's, courts should "pause before concluding that the availability of class arbitration is a question the arbitrator should decide." *Id.* at 2072.
21. 734 F.3d 594, 599 (6th Cir. 2013) (internal citations omitted). At least one district court has disagreed with and declined to follow the Sixth Circuit's decision. *See Lee v. JPMorgan Chase & Co.*, ___ F. Supp. 2d ___, 2013 WL 6068601 (C.D. Cal. Nov. 14, 2013) at *4.
22. 734 F.3d at 598.
23. *Id.* at 599-600.
24. 559 U.S. at 664-65.
25. 131 S. Ct. at 1747 ("When state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA.").
26. *In re Am. Express Merchants' Litig.*, 554 F.3d 300 (2d Cir. 2009), *vacated*, 130 S. Ct. 2401 (2010).
27. *Id.* at 320.
28. *Id.* at 319 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 637 n.19 (1985)).
29. *See Am. Express Co. v. Italian Colors Rest.*, 130 S. Ct. 2401, 2401 (2010).
30. *In re Am. Express Merchants' Litig.*, 634 F.3d 187, 200 (2d Cir. 2011).
31. 133 S. Ct. at 2310.
32. *Id.* at 2011 (noting "the fact that it is not worth the expense involved in proving a statutory remedy does not constitute the elimination of the *right to pursue* that remedy").
33. *Id.* at 2313.
34. 29 U.S.C. §§ 201-204, 206-207, 209-219.
35. 726 F.3d 290 (2d Cir. 2013).
36. *Id.* at 293-94.
37. *Id.* at 295.
38. *Id.* at 298-99.
39. 533 Fed. App'x 11 (2d Cir. 2013).
40. *Id.* at 14 (finding the lower court erred in holding that a waiver is unenforceable as to the class or any individual "'if any one potential class member meets the burden of proving that his costs preclude him from effectively vindicating his statutory rights in arbitration'" (citation omitted)).
41. Without reference to *Italian Colors* and with only a passing reference to *Sutherland*, the Fifth Circuit issued a decision on December 3, 2013, overturning a decision by the National Labor Relations Board that an employer violated the National Labor Relations Act when it required its employees to sign a class action waiver. *See D.R. Horton, Inc. v. NLRB*, 737 F.3d 344, 362 (5th Cir. 2013).

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