New Jersey Law Journal

VOL. 213 - NO 4 JULY 22, 2013 ESTABLISHED 1878

IN PRACTICE

ALTERNATIVE DISPUTE RESOLUTION

Class-Action Arbitration Wins the Day

U.S. Supreme Court case may signify the end of the road for consumers seeking to invalidate waivers

By Elliot D. Ostrove and Jonathan E. Gates

In *American Express Co. v. Italian Colors Restaurant* (2013), a 5-3 majority of the U.S. Supreme Court held that the Federal Arbitration Act (FAA) requires courts to "rigorously enforce" arbitration agreements containing class-action waivers, even where doing so would make proving an individual federal-law claim prohibitively expensive. The court's pro-bilateral arbitration decision is not only the latest in a line of cases in which it has rejected consumers' efforts to engage in class-action arbitration, but may also signify the end of the road for parties seeking judicial relief in this area.

In upholding the class waiver at issue, the court relied upon other recent pro-arbitration precedent, including *AT&T Mobility v. Concepcion*, (2011). There, a 5-4 majority of the court determined that the FAA pre-empted a California rule, which had previously been applied to invalidate class-action waivers in consumer arbitration agreements as "unconscionable." That decision made clear the court's distaste for class-action arbitration, with the majority concluding that arbitration is "poorly suited to the higher stakes of class litigation." Even though *AT&T Mobility* concerned federal pre-emption of a state statute, the decision figured prominently in *Italian Colors*, which pitted two federal statutory schemes against each other.

The *Italian Colors* court also briefly discussed another of its recent decisions barring class arbitration, *Stolt-Nielsen v. Animalfeeds Int'l Corp*. (2010). There, the court considered the question of whether imposing class arbitration on parties whose arbitration agreements are "silent" on that issue is consistent with the FAA. In an opinion penned by Justice Alito, a 5-3 majority of the court held that it was not. Like *Italian Colors*, *Stolt-Nielsen* involved antitrust law, with customers of several maritime shipping companies bringing antitrust claims for supra-competitive prices that the shipping companies had allegedly charged over several years. The court vacated the arbitration panel's decision that the customers could proceed by way of class arbitration, holding that the FAA imposes "the basic precept that arbitration 'is a matter of consent, not coercion,'" and that, consequently, "a party may not be compelled under the FAA to submit to class arbitration unless there is a contractual basis for concluding that the party agreed to do so." In so holding, the *Stolt-Nielsen* court enumerated the benefits of bilateral arbitration as including "lower costs, greater efficiency and speed, and the ability to choose expert adjudicators to resolve specialized disputes."

In many ways, and in light of the line of cases that has come before it, the decision in *Italian Colors* should come as no surprise given the court's clear antipathy toward class-action arbitration.

The *Italian Colors* decision arose out of a tying arrangement between several merchants and American Express. According to the merchants, American Express had leveraged its monopoly power in the market for charge cards to force merchants to also accept credit cards at rates approximately 30 percent higher than the fees for competing credit cards. The merchants brought a class action in the U.S. District Court for the Southern District of New York, alleging that this tying arrangement violated Section 1 of the Sherman Act, a federal statute passed in 1890 that prohibits direct or indirect interference with the freely competitive interstate production and distribution of goods. The merchants also sought treble damages for the class under Section 4 of the Clayton Act, another federal statute, which, enacted in 1914, amended the Sherman Act. Together, the Sherman Act and the Clayton

Ostrove is a partner, and Gates is an associate, with Day Pitney in Parsippany. Their practices focus on commercial litigation.

Reprinted with permission from the JULY 22, 2013 edition of *New Jersey Law Journal*. © 2013 ALM Media Properties, LLC. All rights reserved. Further duplication without permission is prohibited.

Act prohibit tying arrangements if their effect might be to substantially lessen competition or create a monopoly in any line of commerce. It was this federal antitrust law that collided with the federal policy favoring arbitration codified by the FAA.

American Express's agreement with the merchants provided for the arbitration of disputes, and the court devoted just two sentences to describing its terms, explaining that the agreement contained: 1) a clause that requires all disputes between the parties to be resolved by arbitration; and 2) a clause providing that there shall be no right to class action of any claims. The court's brief description of American Express's arbitration agreement stands in stark contrast to its description of AT&T's agreement in *AT&T Mobility v. Concepcion*. There, the majority had described AT&T's arbitration agreement in great detail, praising its substantive and procedural fairness to consumers, and holding it up as a model arbitration agreement.

When American Express moved to compel arbitration, the respondents opposed the motion and submitted a declaration from an economist who opined that the cost of the expert analysis necessary to prove the class's antitrust claims would run, at a minimum, several hundred thousand dollars, and potentially over $1 million, while the maximum recovery for each individual plaintiff would be just $38,549 when trebled under the Clayton Act. Notwithstanding the evidence presented and hardship on the individual plaintiffs discussed, the District Court granted American Express's motions and dismissed the lawsuits.

After two trips up and down from the Second Circuit to the Supreme Court, the court granted certiorari to hear American Express's appeal and to consider the question "[w]hether the Federal Arbitration Act permits courts … to invalidate arbitration agreements on the ground that they do not permit class arbitration of a federal-law claim."

In an opinion written by Justice Scalia, the majority began its analysis by reaffirming what *AT&T Mobility* had recently held, namely that the FAA "reflects the overarching principle that arbitration is a matter of contract," and that courts must "rigorously enforce" arbitration agreements according to their terms. The majority based its holding that American Express's agreement must be rigorously enforced on three independent grounds: 1) no "contrary congressional command" required the court to reject the waiver of class arbitration; 2) the so-called "effective vindication" exception did not apply; and 3) adoption of the respondents' argument would necessitate a "judicially created superstructure" amounting to an impermissible "preliminary litigating hurdle."

Justice Scalia wrote that rigorous enforcement remains the rule even where a claim alleges a violation of a federal statute, unless the FAA's mandate has been "overridden by a contrary congressional command." The court found that in the case before it "[n]o contrary congressional command requires us to reject the waiver of class arbitration here." The court rejected the respondents' argument that requiring them to litigate their cases individually, as opposed to as members of a class, would contravene the policies underlying antitrust laws, reasoning that the "antitrust laws do not guarantee an affordable procedural path to the vindication of every claim." In the words of the majority: "No legislation pursues its purposes at all costs."

Also critical to the court's conclusion was its observation that the antitrust laws do not "evince an intention to preclude a waiver" of class-action procedure. The court noted that "[t]he Sherman and Clayton Acts make no mention of class actions."

Next, the court disposed of the respondents' "effective vindication" argument, which had posited that class waiver would bar effective vindication of the respondents' federal statutory rights because they would have "no economic incentive to pursue their antitrust claims individually in arbitration." The court disparaged the "effective vindication" doctrine as a "judge-made exception to the FAA," which had "originated as dictum" in the Supreme Court's decision in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth* (1985). The court recounted the doctrine's track record of failure, noting that other cases "have similarly asserted the existence of an 'effective vindication' exception, but have similarly declined to apply it to invalidate the arbitration agreement at issue."

The court explained that the exception originated from the desire to prevent "prospective waiver of a party's right to pursue statutory remedies." The court reasoned that simply because "it is not worth the expense involved in *proving* a statutory remedy does not constitute elimination of the *right to pursue* that remedy." According to the court, the class-action waiver "merely limits arbitration to the two contracting parties." The court also reasoned that because the Sherman and Clayton Acts predated the adoption of class-action procedure, the class-action waiver in American Express's agreement no more eliminates the merchants' "right to pursue statutory remedy than did federal law before its adoption of the class action for legal relief in 1938."

The court next turned to *AT&T Mobility*, which stands out as one of the court's strongest declarations against class actions in the arbitration setting. There, the court invalidated a California law which had conditioned enforcement of arbitration on the availability of class procedure because that law "interfered with fundamental attributes of arbitration." Specifically, the court invalidated the California law because it interfered with the dual goals of the FAA: 1) the enforcement of private agreements according to their terms; and 2) the encouragement of efficient dispute resolution. The majority quoted from *AT&T Mobility* for the proposition that "the switch from bilateral to class arbitration sacrifices the principal advantage of arbitration — its informality — and makes the process slower, more costly and more likely to generate procedural morass than final judgment." The court explained that in *AT&T Mobility*, "We specifically rejected the argument that class arbitration was necessary to prosecute claims 'that might otherwise slip through the legal system.'"

Finally, the court rejected what it called a "judicially created superstructure" created by the Court of Appeals' decision. According to the court, the "regime" established by the Second Circuit would require federal courts to determine the cost of developing evidence necessary

to satisfy the elements of federal statutory claims and the damages that could potentially be recovered in the event of a successful suit. In the court's eyes, this type of "preliminary litigating hurdle" would "destroy" the speedy resolution of disputes that "bilateral arbitration … was meant to secure."

Italian Colors completes a trilogy of recent Supreme Court decisions rejecting class-action arbitration, and confirms what was already known after *AT&T Mobility* and *Stolt-Nielsen* — the FAA requires arbitration agreements to be strictly enforced according to their terms. Further, *Italian Colors* not only illustrates the breadth of the court's ruling in *AT&T Mobility*, it also constitutes an expansion of the court's pro-arbitration position, with the court strictly enforcing an arbitration agreement even in the face of substantive federal statutory rights.

Ultimately, and absent a Congressional response delineating the FAA's relationship to other federal laws, the broad language of *Italian Colors*, coupled with the court's other recent pro-bilateral arbitration decisions, means that class-action waivers contained in arbitration agreements will be strictly enforced, and that class arbitration will remain the exception, rather than the rule.■