

Class Actions

Recent Developments In Class Arbitration

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**A commentary article
reprinted from the
September 17, 2009 issue of
Mealey's Litigation Report:
Class Actions**



Commentary

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There have been exciting recent developments in the area of the law governing class arbitration. As the percentage of commercial, consumer, and employment contracts incorporating mandatory arbitration clauses continues to increase, numerous questions concerning the enforceability and scope of these clauses are increasingly likely to confront the courts. This Article will briefly review and summarize the current state of the law (both state and federal) on the propriety of allowing an arbitration to proceed as a class, where the arbitration clause is either silent on the issue or expressly prohibits class arbitration.

With the United States Supreme Court's recent grant of *certiorari* in *Stolt-Nielsen S.A., et al. v. AnimalFeeds International*, No. 08-1198 ("*Stolt-Nielsen*"), the Supreme Court is likely soon to weigh-in on one or more of these issues, at least as they pertain to arbitrations covered by the Federal Arbitration Act, 9 U.S.C. §§ 1 et seq. ("FAA").

The Stolt-Nielsen Action

On June 15, 2009, the United States Supreme Court granted *certiorari* to consider the following question:

"Whether imposing class arbitration on parties whose arbitration clauses are silent on that issue is consistent with the Federal Arbitration Act, 9 U.S.C. §§ 1 et seq."¹

The *Stolt-Nielsen* action concerns allegations that petitioners engaged in a global conspiracy to restrain competition in the world market for parcel tanker shipping services in violation of federal antitrust laws.² The parties to this action entered into industry-standardized international maritime shipping contracts that contained mandatory arbitration clauses.³ The arbitration clauses at issue, while broadly worded to cover any and all disputes between the parties, are silent on whether the mandated arbitration can proceed on behalf of a class.⁴

In 2003, respondent and others filed several related class actions against petitioners in federal courts around the country that were ultimately consolidated in one judicial district. After the Second Circuit reversed the district court's denial of petitioners' motion to compel arbitration,⁵ the respondent commenced an arbitration and the parties entered into an agreement concerning their arbitration of this matter.⁶ The parties' agreement, adopting Rules 3 through 7 of the Supplementary Rules Governing Class Arbitration promulgated by the American Arbitration Association⁷, allowed the arbitration panel, as a threshold matter, to determine whether the relevant arbitration clauses permitted arbitration to proceed on a class-wide basis.⁸

In accordance with the parties' agreement, respondent filed a motion with the arbitration panel for a "Clause Construction Award," seeking to have the Panel interpret the arbitration clause to permit the arbitration to proceed on behalf of a class of all direct purchasers of parcel tanker transportation services.⁹

On December 20, 2005, the 3-member arbitration panel unanimously decided that the arbitration clauses at issue, which were silent on the issue of class arbitration, nonetheless permitted class arbitration.¹⁰ Petitioners immediately petitioned the district court to vacate the arbitrators' decision under the FAA.¹¹ The court granted the petition, concluding that, under the FAA, the Clause Construction Award was made in manifest disregard of the law.¹²

On November 4, 2008, the Second Circuit reversed the district court's decision on the grounds that, *inter alia*, it was a question for the arbitrators, and not the courts, to decide. The Panel's construction of the arbitration clause was not in manifest disregard of the law or outside of their authority, since the FAA does not prohibit class arbitration where the relevant arbitration clause is broadly worded in scope, but silent on the issue.¹³

The court held that under the United States Supreme Court's decision in *Green Tree Financial Corp. v. Bazzle* ("Bazzle"), 539 U.S. 444 (2003), the principle that the FAA prohibited class arbitration unless the relevant arbitration clause specifically provided for it had been abrogated.¹⁴ The arbitration panel's construction of the arbitration clause that respondent could seek to have a class certified in arbitration was entitled to deference and should not be set aside under the FAA.

The Impact Of Green Tree Financial Corp. V. Bazzle

A significant issue in the present appeal to the Supreme Court is the fact that *Bazzle* was a plurality decision and, according to petitioners, did not reach the merits of whether the FAA permits arbitrators to allow a class arbitration when the parties' agreement is silent regarding class arbitration.¹⁵ Instead, petitioners contend that the Court in *Bazzle* remanded the case for a threshold determination by the arbitrators on whether the relevant arbitration clause was in fact silent regarding class arbitration or if the clause

forbade class arbitration.¹⁶ The clause construction determination in *Bazzle* had not been made by the arbitrators prior to the series of appeals that eventually led to Supreme Court review.¹⁷

The *Bazzle* Court's inability to reach a majority decision on the merits is claimed by petitioners to be critical because, prior to *Bazzle*, state and federal courts had reached differing conclusions on whether the FAA permitted class arbitration where the relevant arbitration clause was silent on the issue. Most notably, three federal circuit court decisions found that class or consolidated arbitrations were strictly prohibited under the FAA, unless expressly provided for in the relevant arbitration clause.¹⁸ On the other hand, numerous state courts, including the South Carolina Supreme Court in *Bazzle*, had determined that the FAA does not prohibit class arbitration even where the relevant arbitration clause does not specifically address the issue.¹⁹

In post-*Bazzle* jurisprudence, petitioners contend that the courts still appear to be divided on the issue of whether the FAA prohibits class arbitration unless specifically provided for in the relevant arbitration clause.²⁰

Critical Questions

The critical question presented in the *Stolt-Nielsen* appeal is how to balance the parties' legitimate interests in pursuing cost-effective arbitration, versus being forced into class arbitration on the one-hand or impermissibly losing the right to effectively pursue one's legitimate statutory claims on the other.

The petitioners argue, *inter alia*, that class arbitration may only occur upon express consent, and that the primary purpose of the FAA is to ensure that private arbitration agreements are enforced strictly according to their specific terms.²¹ Moreover, given that class arbitration significantly alters the monetary stakes of a single arbitrator's (or arbitration panel's) decision, which necessarily comes with limited judicial review, a party should not be thrust into such arbitration unless expressly consented to in the relevant arbitration clause.²²

The respondent argues, *inter alia*, that petitioners, as sophisticated business entities, could easily have inserted an express prohibition against class arbitration

into the arbitration clause at issue.²³ Moreover, the parties' arbitrational intent is a matter of contract interpretation best left to arbitrators, particularly where the parties have agreed, by contract, to arbitrate any disputes arising under their agreement.²⁴ It is not for the courts to second-guess an arbitration panel's good faith effort to interpret the parties' intent in a broadly-worded arbitration clause.

An additional consideration weighing against a strict prohibition of class arbitration unless specifically provided for is the dire consequences such a prohibition would have on negative value claims, that is, claims which cost more to litigate than the amount in dispute. If such claims could not be brought in court, but must be arbitrated in accordance with a mandatory arbitration clause, a prohibition, whether express or implied, of class arbitration would frustrate the statutory purpose and public policy underlying the antitrust and other important laws.

Jurisdictional Hurdle

It is possible that the Supreme Court may fail to reach the merits in the present appeal. The respondent asserts, *inter alia*, that the arbitration panel's interlocutory clause construction decision concerning the propriety of seeking class arbitration is not ripe for judicial review.²⁵ This argument was not raised below because it appears that the only federal appellate court to specifically address the appealability of a clause construction award did so only after the date of the decision appealed from in this case.²⁶ In *Dealer Computer Servs., Inc. v. Dub Herring Ford* ("Dealer Computer Services"),²⁷ the Sixth Circuit held that a district court lacks jurisdiction to consider a party's motion to vacate an arbitrator's clause construction award, unless and until a class is certified.²⁸ Specifically, the Sixth Circuit concluded that based on traditional considerations of ripeness, such as (i) the likelihood that the harm will actually occur, and (ii) the hardship to the parties if judicial relief is denied at this stage of the proceedings, clause construction determinations are intermediate in nature and do not qualify for interlocutory judicial review.²⁹

The petitioners argue, *inter alia*, that *Dealer Computer Services* has little persuasive value because in that case, which was a breach-of-contract dispute and not an international antitrust action, the respondent failed to articulate any immediate harm to petitioner prior

to the certification of a class.³⁰ Here, the petitioners' contend, harm is imminent due to the nature of this particular action.³¹ Moreover, if the Supreme Court denies petitioners judicial review of the arbitration panel's clause construction determination, petitioners assert they will be forced immediately to engage in lengthy and costly class certification discovery.³²

Class Arbitration Waivers In Federal Court

As a result of multiple litigations surrounding class arbitration where the relevant arbitration clause is silent on the issue, not surprisingly, there has been a dramatic increase in commercial, consumer, and employment contracts that specifically prohibit class arbitration. The enforceability of such express class arbitration prohibitions raises significant legal issues concerning, *inter alia*, the frustration of state and federal statutory rights and whether such prohibitions run afoul of well established state law principles governing unconscionability and contracts of adhesion.

Until about 2006, most federal circuits held that arbitration clauses expressly prohibiting class arbitration did not violate public policy concerns.³³ Recently, however, federal courts have begun finding that such prohibitions, particularly with respect to negative value claims, frustrate the legislative intent underlying important statutory rights.³⁴

In *Kristian v. Comcast Corp.*, the First Circuit struck down a portion of an arbitration clause containing a class prohibition because the effect would be to frustrate the Congressional purpose of the federal antitrust laws.³⁵ The court found that the standardized arbitration clause inserted into Comcast's customers' billing statements was enforceable, but that the express prohibition against class arbitration would effectively prevent plaintiffs from pursuing important statutory negative value claims, such as the antitrust claims at issue there.³⁶

Similarly, in *In re American Express Merchants' Litigation*, the Second Circuit recently invalidated the portion of American Express's arbitration agreements with many of its retail merchants that prohibited class arbitration.³⁷ The court concluded that enforcement of the class arbitration prohibition would effectively immunize American Express from federal antitrust suits by its merchants because, to do so, would render each individual merchant's arbitration costs prohibitive.³⁸

The *Kristian* and *American Express* decisions are of particular importance because each was decided under the “federal substantive law of arbitrability” and not general state law concepts of consumer rights or unconscionability which can differ materially among the various jurisdictions.³⁹

Class Arbitration Waivers In State Court

In a trend similar to that of its federal counterparts, a majority of recent state court decisions have held that class arbitration prohibitions are against public policy.⁴⁰ Generally, the state courts that have voided no-class arbitration clauses have done so because, if those clauses had been upheld, they would have rendered the enforcement of legitimate, negative value claims economically prohibitive.⁴¹ In striking down such class arbitration prohibitions under state law, the courts have often invoked concepts of unfairness or unequal bargaining power.

In the line of state court cases that have refused to strike down contract clauses that prohibit class arbitration, the courts generally hold that without proof of a draconian purpose or effect, such prohibitions are not *per se* unconscionable.⁴²

Recognizing the recent trend among both federal and state courts concerning prohibitions on class proceedings, the Illinois Supreme Court explained as follows:

If there is a pattern in these cases it is this: a class action waiver will not be found unconscionable if the plaintiff had a meaningful opportunity to reject the contract term or if the agreement containing the waiver is not burdened by other features limiting the ability of plaintiff to obtain a remedy for the particular claim being asserted in a cost-effective manner.⁴³

Conclusion

It appears that, particularly where negative value statutory claims are at issue, both federal and state courts are likely to strike down the portion of any mandatory arbitration clause that forbids class adjudication in order to avoid the frustration of statutory rights or to temper the inherent unfairness in contracts of adhesion. With respect to arm's length transactions where potential individual damages far outpace litigation costs, the law is considerably less settled. ■

Endnotes

1. *Stolt-Nielsen*, No. 08-1198, Order Granting Petition for Certiorari.
2. *Stolt-Nielsen S.A. v. AnimalFeeds Intern. Corp.*, 548 F.3d 85, 87 (2d Cir. 2008).
3. *Id.*
4. *Id.*
5. *JLM Indus., Inc. v. Stolt-Nielsen S.A.*, 387 F.3d 163 (2d Cir.2004).
6. *Stolt-Nielsen.*, 548 F.3d at 87-88.
7. These rules were adopted by the AAA shortly after the Supreme Court's decision in *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444 (2003). Since that time, in nearly every instance, where a broadly worded silent arbitration clause was involved, the arbitrators have construed it to permit a class arbitration. See <http://adr.org/sp.asp?id=25562>
8. *Stolt-Nielsen.*, 548 F.3d at 87-88.
9. *Id.* at 87-88.
10. *Id.* at 89-90.
11. *Id.* at 90.
12. *Id.*; *Stolt-Nielsen SA v. Animalfeeds Int'l Corp.*, 435 F.Supp.2d 382, 387 (S.D.N.Y.2006).
13. *Stolt-Nielsen*, 548 F.3d at 99-101.
14. *Id.* at 100.
15. *Stolt-Nielsen*, No. 08-1198, Petition for Writ of Certiorari at 4 (“Petitioners Br.”).
16. *Id.*
17. *Id.*
18. See *Champ v. Siegel Trading Co.*, 55 F.3d 269 (7th Cir.1995); *United Kingdom v. Boeing Co.*, 998 F.2d

- 68 (2d Cir.1993); and *Glencore, Ltd. v. Schmitzer Steel Products*, 189 F.3d 264 (2d Cir.1999).
19. Petitioners Br. at 11-12.
 20. *See Stolt -Nielsen*, 548 F.3d 85; *Shroyer v. New Cingular Wireless Servs., Inc.*, 498 F.3d 976, 992 (9th Cir. 2007); and *Kinkel v. Cingular Wireless LLC*, 857 N.E. 250, 262 (Ill. 2006) (permitting class arbitration under the FAA notwithstanding the arbitration clauses' silence on the issue); *but see Employers Ins. Co. of Wausau v. Century Indem. Co.*, 443 F.3d 573, 580 (7th Cir. 2006) (rejecting *Bazzle's* precedential value in abrogating the federal circuits that found a prohibition, under the FAA, of class arbitration unless the relevant arbitration clause expressly provides for it).
 21. Petitioners Br. at 17.
 22. *Id.* at 19.
 23. *Stolt-Nielsen*, No. 08-1198, Respondent's Brief in Opposition at 4 ("Respondents Br.").
 24. Respondent's Br. at 4.
 25. Respondents Br. at 23.
 26. *Id.*
 27. 547 F.3d 558 (6th Cir. 2009).
 28. *Id.* at 560-65; Respondents Br. at 24.
 29. *Id.*
 30. Respondent's Br. at 10.
 31. *Id.*
 32. *Id.*
 33. *See, e.g., Jenkins v. First Am. Cash Advance of GA, LLC*, 400 F.3d 868 (11th Cir. 2005); *Caley v. Gulfstream Aerospace Corp.*, 428 F.3d 1359 (11th Cir. 2005); *Omstead v. Dell, Inc.*, 473 F. Supp. 2d 1018 (N.D. Cal. 2007); *Livingston v. Asters Pin, Inc.*, 339 F.3d 553, 558 (7th Cir. 2003); *Snowden v. CheckPoint Check Cashing*, 290 F.3d 631, 638 (4th Cir. 2002); *Randolph v. Green Tree Fin Corp-Ala.*, 244 F.3d 814, 818-19 (11th Cir. 2001); *Johnson v. W. Suburban Bank*, 225 F.3d 366, 377 (3rd Cir. 2000).
 34. *See, e.g., In re American Express Merchants' Litigation*, 554 F.3d 300 (2d Cir. 2008)(The Labaton firm is one of the counsel for plaintiffs in that action); *Lowden v. T-Mobile USA, Inc.*, 512 F.3d 1213 (9th Cir. 2008); *Dale v. Comcast Corp.*, 498 F.3d 1216 (11th Cir. 2007); *Shroyer v. New Cingular Wireless Servs., Inc.*, 498 F.3d 976 (9th Cir. 2007); *Kristian v. Comcast Corp.*, 446 F.3d 25 (1st Cir. 2006); *Booker v. Robert Half Int'l, Inc.*, 413 F.3d 77 (D.C. Cir. 2005).
 35. *Kristian*, 446 F.3d at 55.
 36. *Id.*
 37. *In re American Express Merchants' Litigation*, 554 F.3d at 312.
 38. *Id.* at 316.
 39. *Id.* at 312
 40. *See, e.g., Betts v. McKenzie Check Advance of Fla.*, Case No. CL 01-320 AI (Fla. Cir. Ct. 2008); *Tillman v. Commercial Credit Fla. Loans, Inc.*, 655 S.E.2d 362 (N.C. 2008); *Simpson v. MSA of Myrtle Beach, Inc.*, 644 S.E.2d 663 (S.C. 2007); *Gatton v. T-Mobile USA, Inc.*, 61 Cal. Rptr. 3d 344 (Cal. Ct. App. 2007); *Vasquez-Lopez v. Beneficial Or., Inc.*, 152 P.3d 940 (Or. Ct. App. 2007); *Thibodeau v. Comcast Corp.*, 912 A.2d 874 (Pa. Super. Ct. 2006); *Muhummad v. County Bank of Rehobeth Beach*, 912 A.2d 88 (N.J. 2006); *Kinkel v. Cingular Wireless, LLC*, 828 N.E.2d 812 (Ill. App. Ct. 2005); *Whitney v. Alltel Commc'ns, Inc.*, 173 S.W.3d 300 (Mo. Ct. App. 2005); *Eagle v. Fred Martin Motor Co.*, 809 N.E.2d 1161 (Ohio Ct. App. 2004); *Lytle v. Citifinancial Services, Inc.*, 810 A.2d 643 (Pa. Super. Ct. 2002); *Scott v. Cingular Wireless*, 161 P.3d 1000 (Wash. 2007); *W. Va. ex rel Dunlap v. Berger*, 567 S.E.2d 265 (W. Va. 2002); *Coady v. Cross Country Bank, Inc.*, 729 N.W.2d 732 (Wis. Ct. App. 2007); *Leonard v. Terminix Int'l Co., L.P.*, 854 So. 2d 529 (Ala. 2002).

- 41. *Id.*
- 42. *See, e.g., Ranieri v. Bell Atlantic Mobile*, 759 N.Y.S.2d 448 (N.Y. App. Div. 2003); *Edelist v. MBNA Bank*, 290 A.2d 1249 (Del. Super. Ct. 2001); *Gras v. Assocs. First Capital Corp.*, 786 A.2d 886 (App. Div. 2001);
- Pyburn v. Bill Heard Chevrolet*, 63 S.W.3d 351 (Tenn. Ct. App. 2001); *Raines v. Foundation Health System Life & Health*, 23 P.3d 1249 (Colo. Ct. App. 2001).
- 43. *Kinkel v. Cingular Wireless LLC*, 857 N.E.2d at 274. ■

MEALEY'S LITIGATION REPORT: CLASS ACTIONS

edited by David Eldreth

The Report is produced twice monthly by



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ISSN 1535-234X