Arbitration Agreements and Class Actions

Supreme Court Enforces Arbitration Agreement with Class Action Waiver, Narrowing the Scope of Ability to Avoid Such Agreements

SUMMARY
The United States Supreme Court yesterday continued its rigorous enforcement of arbitration agreements, including those containing waivers of class arbitration. The Court in American Express Co. v. Italian Colors Restaurant held that a contractual waiver of class arbitration is enforceable under the Federal Arbitration Act despite the plaintiffs’ claims that the cost of individually arbitrating a federal statutory claim would exceed the potential recovery.¹

BACKGROUND
The case arose out of a contract between American Express and merchants who accept American Express cards. The contract contained an arbitration clause that waived the merchants’ right to bring claims by class action.² The plaintiff merchants brought a claim against American Express alleging violations of the federal antitrust laws on the theory that American Express used monopoly power in the market for charge cards to force merchants to accept credit cards at higher rates than the fees for competing credit cards.³ This tying arrangement, the merchants alleged, violated the Sherman Act (the principal federal antitrust statute). The plaintiffs sought to proceed as a class, and sought treble damages for the class.⁴ American Express moved to compel individual arbitration under the Federal Arbitration Act (FAA).⁵ In resisting the motion, the merchants submitted evidence that the cost of litigating antitrust claims on an individual basis would be at least ten times the maximum potential damages for an individual plaintiff.⁶ The district court granted the motion and dismissed the lawsuits.

The Second Circuit Court of Appeals reversed, holding that the class action waiver was unenforceable because the prohibitive cost of individual arbitrations effectively precludes the merchants from enforcing their federal statutory rights.⁷ The Second Circuit twice reaffirmed this decision after the Supreme Court’s
decisions in Stolt-Nielsen S.A. v. Animalfeeds International Corp.,⁸ which held that a party may not be compelled to submit to class arbitration absent a contractual agreement to do so, and AT&T Mobility v. Concepcion,⁹ in which the Court invalidated a state-law rule barring enforcement of consumer contract arbitration agreements that contain class action waivers. The Second Circuit then en banc declined to rehear the case, with five judges dissenting.¹⁰

THE SUPREME COURT’S DECISION

In a 5-3 decision, with Justice Sotomayor recusing herself, the Supreme Court reversed. Writing for the majority, Justice Scalia, joined by Chief Justice Roberts and Justices Thomas, Kennedy and Alito, explained that the FAA requires that courts rigorously enforce arbitration agreements according to their terms, unless there is a “contrary congressional command.”¹¹ The Court found no such contrary congressional command in the antitrust law. The Court rejected plaintiffs’ claim that the class action device was an essential element of their ability to assert their antitrust claims, observing that class action procedures were first adopted in 1938, long after the Sherman Act was enacted. The Court recognized its previous holdings allowing courts to refuse enforcement of arbitration agreements if the claimant could not effectively vindicate its rights in arbitration, but held that the “effective vindication” exception applies to situations in which the claimant’s right to pursue a remedy is precluded. Here, the Court held, “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.”¹²

THE CONCURRING OPINION

In a brief concurring opinion, Justice Thomas joined the Court’s majority opinion in full, and wrote that the result is required by the plain meaning of the FAA. As he had in AT&T, he advocated a narrow reading of the circumstances under the FAA in which arbitration agreements may be overridden: “the FAA requires that an agreement to arbitrate be enforced unless a party successfully challenges the formation of the arbitration agreement, such as by proving fraud or duress.”¹³ He concluded that plaintiffs had not met that standard.¹⁴

THE DISSENTING OPINION

Justice Kagan, joined by Justices Ginsburg and Breyer, dissented. Justice Kagan would have held that the agreement in question had the practical effect of precluding the vindication of the plaintiffs’ federal statutory rights under the Sherman Act and thus was unenforceable under the “effective vindication” doctrine.¹⁵ She noted in particular that the agreement not only barred class actions, but also included various provisions that would have, in her view, reduced the costs of litigating the claims for an individual plaintiff.¹⁶ These provisions included prohibitions on joinder of multiple plaintiffs and on cost-shifting as well as confidentiality provisions that, in Justice Kagan’s view, prevented plaintiffs from using a common expert report.¹⁷
IMPLICATIONS

Use of class-action waivers is likely to increase
Together with AT&T Mobility and other recent Supreme Court decisions favorable to arbitration, the decision supports the enforceability in a broad variety of contexts, including the employment as well as business contexts, of arbitration agreements containing class action waivers.

Other procedural bars will not invalidate a class-action waiver
In AT&T, the arbitration agreement contained not only a class action waiver but also a variety of provisions designed to make it more practical for an individual to obtain realistic relief in arbitration (e.g., shifting all arbitration costs to the defendant for nonfrivolous claims, placing the seat of arbitration in the county of customer's billing, and providing a minimum amount of recovery for claimants who prevailed), leading some to conclude that it would be prudent to include such procedures in order to ensure the enforceability of class-action waivers in a consumer context. Today's decision makes clear that the Court's view on enforceability of arbitration agreements is more fundamental, namely, the Court considers the FAA as requiring enforcement of arbitration agreements unless Congress has said otherwise, so long as the agreement does not preclude the assertion of the claim.

The effective vindication exception is narrow
The Court curtailed the power of judges to invalidate an otherwise valid arbitration agreement based on the “effective vindication” doctrine. The Court’s standard sets a high bar, explaining that the exception “finds its origin in the desire to prevent ‘prospective waiver of a party’s right to pursue statutory remedies’” and finding that mere difficulties of “proof” do not eliminate the “right to pursue” antitrust claims. The Court left one narrow window for possible future litigation, noting that, beyond expressly forbidding the assertion of certain statutory rights, a contract might violate the “effective vindication” exception if “filing and administrative fees attached to arbitration [were] so high as to make access to the forum impracticable.” But this path is likely to prove narrow.

The decision may provoke a congressional reaction
Efforts over the last few years to restrict arbitration in various consumer settings have largely stalled in Congress. This decision may give new life to those endeavors.

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ENDNOTES


2 The agreement provided that “[t]here shall be no right or authority for any Claims to be arbitrated on a class action basis.” Slip op. at 1.

3 *Id.* at 2.

4 *Id.*

5 *Id.*

6 The economist stated that the cost of an expert economic analysis would be “at least several hundred thousand dollars, and might exceed $1 million,” while the maximum recovery for an individual plaintiff would be $38,549 when trebled. *Id.*


11 Slip op. at 3-4.

12 *Id.* at 5-9.


14 *Id.*


16 *Id.* at 7.

17 *Id.*

18 Slip op. at 6 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 637, n.19 (1985)).

19 Slip op. at 7.

20 *Id.* at 6.
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