US Supreme Court Orders Strict Enforcement of Class Arbitration Waivers in *American Express Co. v. Italian Colors Restaurant* – A Contract Is a Contract Is a Contract

In commanding that class action waivers be enforced according to their terms, even where the plaintiff is able to show that pursuing an individual action in arbitration would be "prohibitively costly," the United States Supreme Court's decision in *American Express Co. v. Italian Colors Restaurant*, No. 12-133 (June 20, 2013) will reverberate in finance, consumer, commercial and employment litigation, and virtually every potential legal landscape in which class actions would seem more attractive to plaintiffs' counsel. Businesses should be cautioned, however, that class action waivers must be carefully drafted to avoid arguments that they interfere with the right to pursue statutory remedies.

Background

In *American Express*, a group of merchants brought a class action charging that American Express unlawfully used its monopoly power in the market for charge cards to force the merchants to accept inflated credit card fees, in violation of the federal antitrust laws. American Express moved to compel individual arbitration under the Federal Arbitration Act (FAA), 9 U.S.C. §1 *et seq*., invoking provisions in the merchants' contracts requiring arbitration of all disputes and providing that "[t]here shall be no right or authority for any Claims to be arbitrated on a class action basis," or otherwise in a representative capacity. In opposing American Express, the merchants submitted a declaration from an economist who opined that an expert economic study, an important component of proving the antitrust violation, likely would cost "at least several hundred thousand dollars and might exceed $1 million." Each individual plaintiff would need such a study; yet the average individual plaintiff could only hope to recover "$12,850, or $38,549 when trebled."

The US District Court for the Southern District of New York granted American Express's motion, but the Second Circuit reversed, holding that the declaration of the merchants' expert compellingly demonstrated that arbitrating disputes individually would be prohibitively expensive and preclude vindication of rights under the antitrust laws. The Second Circuit therefore held that the class action waiver in the merchants' contracts was unenforceable, invoking the "federal substantive law of arbitrability," which it interpreted to hold that federal statutory rights only may be waived in favor of arbitration if "the prospective litigant effectively may vindicate its statutory cause of action in the arbitral forum." 554 F.3d 300, 319 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 637 (1985)).

In an unusual sequence, the Second Circuit's *American Express* decision was subject to two rounds of reconsideration before the Supreme Court's decision yesterday, twice following Supreme Court decisions enforcing bilateral arbitration where plaintiffs had sought class proceedings. *Stolt-Nielsen S.A. v AnimalFeeds International Corp.*, 559 U.S. 662 (2010); *AT&T Mobility v. Concepcion*, 131 S. Ct. 1740

(2011). On both occasions, the panel stood by its original ruling invalidating the class action waiver, and the Second Circuit declined *en banc* rehearing, over the dissent of five of its judges.

The Supreme Court's Decision, Reinforcing Class Arbitration Waivers

The US Supreme Court granted *certiorari* and reversed, in a 5-3 decision delivered by Justice Scalia, who had authored the Court's decision in *AT&T Mobility*. Justice Sotomayor, who had been a member of the original Second Circuit panel in *American Express*, did not participate. The Court found that Congress had not evinced an intention to preclude waiver of class action procedures in the antitrust laws because the Sherman and Clayton Acts were enacted prior to Federal Rule of Civil Procedure 23, which authorized class actions. The enactment of Rule 23 did not change anything, the Court held, because the Federal Rules of Civil Procedure were not intended to modify any substantive right (such as the right to enter into a private arbitration agreement), and the Court had held in a prior case that the high costs of complying with Rule 23's requirements were not grounds for dispensing with those requirements.

The Court also considered whether a court-made exception to the FAA was viable in the absence of any statement on the issue from Congress. The Court acknowledged that certain requirements in arbitration agreements might run afoul of the unwritten "federal substantive law arbitrability," such as "a provision ... forbidding the assertion of certain statutory rights," or assessing filing and administrative fees in arbitration that were "so high as to make access to the forum impracticable." But the Court held that the fact that plaintiffs might lack sufficient *incentive* to pursue their claims in individual arbitration was not a ground for invalidating the class action waiver: "The class-action waiver merely limits arbitration to the two contracting parties. It no more eliminates those parties' right to pursue their statutory remedy than did federal law before its adoption of the class action for legal relief in 1938 [in Rule 23]." The Court found that its rejection of the argument "that class arbitration was necessary to prosecute claims that might otherwise slip through the legal system" in *AT&T Mobility* "all but resolves this case."

Justice Kagan, joined by Justices Ginsburg and Breyer, dissented, arguing that the "rule" of the "federal substantive law of arbitrability" – that an arbitration agreement may not thwart "vindication of federal rights" – "fits this case hand in glove."

Business Implications of *American Express*

Despite the broad sweep of the Court's decision in rejecting "judge-made" arguments based on the plaintiff's "insufficient incentive" to bring a claim on an individual basis, class action waivers may still present pitfalls for businesses if they constrain a party's right to pursue a statutory remedy. Arbitration agreements that interfere with statutory rights (such as by shortening a federal statutory limitations period, or by banning a statutory right to attorney's fees or statutory right to punitive damages) may be vulnerable. And the "federal substantive law of arbitrability" may still provide a ground for challenging the agreement to arbitrate where, for example, the arbitration filing fees are excessive. Thus, the arbitration agreement should specify, among other things, that the parties knowingly and voluntarily agree that the amount in dispute, whether large or small, should not be a basis for challenging the class action waiver, and the party initiating arbitration should be required to pay no more than the equivalent filing fee in court, any remainder being paid by the company. In other words, while *American Express* would enforce the class arbitration waiver as written, the company that favors bilateral arbitration must not create barriers to the individual's pursuit of statutory remedies in a bilateral arbitration.

In the final analysis, the Supreme Court's *American Express* decision should resolve a number of cases still pending in the Second Circuit and elsewhere in which, because the individual's considerable expense in proceeding alone, the "vindication of federal rights" has been argued in an effort to invalidate otherwise enforceable class arbitration waivers.

For more information or inquiries regarding class action waivers and bilateral arbitration agreements, please contact Litigation Partner and Chair of Kaye Scholer's Alternative Dispute Resolution Practice, Jay W. Waks, or Litigation Associate Noah B. Peters, who assisted in preparing this alert.

For analysis of the US Supreme Court's prior decision in Oxford Health Plans v. Sutter (June 10, 2013) on court deference to arbitrator awards that refuse to enforce class arbitration waivers, please see Kaye Scholer's Class Action Litigation Alert, "Oxford Health Plans v. Sutter – In Reaffirming the Deference to Be Given Arbitration Decisions, the US Supreme Court Has Paved the Way to Enforce Clear and Unambiguous Class Action Waivers and Bilateral Arbitration Contracts" (June 11, 2013).

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