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LEGAL ALERT

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Second Circuit Holds Class Action Waiver Unenforceable in American Express Arbitration Agreement Despite the Supreme Court's Recent Decision in *Stolt-Nielsen*

In May 2010, the Supreme Court directed the Second Circuit to reconsider its decision in *In re American Express Litigation* regarding the unenforceability of a class action waiver in light of the Supreme Court's decision in *Stolt-Nielsen, S.A. v. AnimalFeeds Int'l Corp.*, 130 S. Ct. 1758 (2010). *See American Express Company v. Italian Colors Restaurant*, 130 S. Ct. 2401 (Mem.) (May 3, 2010) (vacating 554 F.3d 300 (2d Cir. 2009)). On remand, the Second Circuit found its original analysis unaffected by *Stolt-Nielsen* and held that the class action waiver within the arbitration agreement was unenforceable because "the cost of plaintiffs' individually arbitrating their dispute with Amex would be prohibitive, effectively depriving plaintiffs of the statutory protections of the antitrust laws." *In re American Express*, No. 06-1871 at 3, 18 (2d Cir. March 8, 2011). (For a copy of the Second Circuit's opinion, click here.)

The *American Express* antitrust litigation began as a consolidated class action brought by merchants who contracted with American Express (Amex) to accept its corporate, charge, and credit cards. *See In re American Express Merchants' Litigation*, No. 03-CV-9592, 2006 WL 662341 (S.D.N.Y. March 16, 2006). Plaintiffs alleged that the merchant contract violated the Sherman Act. The merchant contract contained an arbitration provision that required all claims "arising from or relating to [the] Agreement" to be resolved by arbitration. The contract also contained a class action waiver that purported to preclude merchants from bringing or participating in class actions regarding issues subject to arbitration. Based on the arbitration provision, the U.S. District Court for the Southern District of New York granted Amex's motion to compel arbitration. *Id.* The district court did not resolve the issue of the enforceability of the class action waiver, holding that the issue was for the arbitrator to decide. On appeal, the United States Court of Appeals for the Second Circuit reversed. *See In re American Express Merchants' Litigation*, 554 F.3d 300 (2d Cir. 2009). First, the Second Circuit held that the issue of the class action waiver's enforceability was a matter for the court, not the arbitrator. Second, the Second Circuit held "that the class action waiver in the [agreement] cannot be enforced in this case because to do so would grant Amex de facto immunity from antitrust liability by removing the plaintiffs' only reasonably feasible means of recovery." *Id.* at 320.

American Express sought review by the Supreme Court. In a May 3, 2010, order vacating the judgment and remanding the case, the Supreme Court instructed the Second Circuit to reconsider the case in light of the Supreme Court's recent decision in *Stolt-Nielsen*. 130 S.Ct. 1758. In *Stolt-Nielsen*, the Supreme Court had held that imposing class arbitration on parties who have not agreed specifically to class arbitration is inconsistent with the Federal Arbitration Act, 9 U.S.C. § 1 et seq. The Court stated that "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." *Id.* at 1775. (emphasis in original).

On remand to the Second Circuit, Amex argued that *Stolt-Nielsen* compelled a different result and that the class action waiver should be enforced. The Second Circuit disagreed. The court stated that *Stolt-Nielsen* did not bar a court from using public policy to find contractual language void, and agreed with plaintiffs that *Stolt-Nielsen* did not overrule or drastically limit prior precedent regarding the enforceability of class action waivers. *In re American Express Merchants Litigation,* No. 06-1871 at 21 (2d Cir. March 8,

2011). The Second Circuit acknowledged the holding in *Stolt-Nielsen* that parties cannot be forced to engage in a class arbitration absent a contractual agreement to do so, but stated that it did not follow that a contractual clause barring class arbitration is *per se* enforceable. *Id.* at 11.

Instead, the Second Circuit reconfirmed its prior holding that the class action waiver within the arbitration provision was unenforceable.[1] The class action waiver was unenforceable, the court found, because "the cost of plaintiffs' individually arbitrating their dispute with Amex would be prohibitive, effectively depriving plaintiffs of the statutory protections of the antitrust laws." *Id.* 18. The court stated that plaintiffs, as the party seeking to invalidate the agreement, bore the burden of proof to establish that arbitration would be prohibitively expensive, and found that plaintiffs had met that burden with an expert affidavit estimating the costs of individual litigation when compared with the amount of a potential individual recovery.[2] *Id.* at 18-21. Based on the record, the court found that "the size of any potential recovery by an individual plaintiff will be too small to justify the expense of bringing an individual action," and the fee shifting provisions of the antitrust statutes were "inadequate" to alleviate these concerns. *Id.* at 20-21. The court also stated that it was relying on "a firm principle of antitrust law that an agreement which in practice acts as a waiver of future liability under the federal antitrust statutes is void as a matter of public policy." *Id.* at 17. Accordingly, the court held that the class action waiver was unenforceable because "enforcement of the class action waiver in the Card Acceptance Agreement 'flatly ensures that no small merchant may challenge American Express's tying arrangement under the federal antitrust laws.'" *Id.* at 20 (quoting 554 F.3d at 319).

The Second Circuit was careful to qualify its holding by expressly stating that "we do not conclude here that class action waivers in arbitration agreements are per se unenforceable" or that they are per se unenforceable in the context of antitrust actions. *Id.* at 21. It also stated that the decision was not based on the status of plaintiffs as "small" merchants. *Id.* Instead, "each case which presents a question of the enforceability of a class action waiver in an arbitration agreement must be considered on its own merits." *Id.*

Although the Second Circuit did not frame its decision in terms of unconscionability, the Supreme Court is currently considering a potentially significant case regarding the enforceability of class action waivers held to be unconscionable under state law. In *AT&T Mobility LLC v. Concepcion,* No. 09-893, the Court will address whether the Federal Arbitration Act preempts California state law under which class action waivers in consumer arbitration agreements have been held to be unconscionable. Because courts in many states have held that class action waivers may be found unconscionable under state contract law principles using a similar analysis that the Second Circuit employed, the Supreme Court's decision may have a significant impact on consumer arbitration, as well as arbitration in similar contexts such as employment. Oral argument was held on November 9, 2010, and a decision is expected soon. (For Sutherland's Legal Alert regarding *Concepcion*, click here.)

[1] The Second Circuit also reiterated its prior holding that the issue of the class action waiver's enforceability was a matter for the court, not the arbitrator. *Id.* at 7.

[2] The expert estimated that a median volume merchant might expect several thousand dollars in damages, but that an expert antitrust study for purposes of litigation might exceed $1 million.

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